

## Net-Zero Asset Owner Alliance

### A Call for Comment on carbon neutrality / “implied temperature rise” methodology convergence

April 2020

Calls for comments (and related evidence) allow interested parties including data and service providers, non-governmental organizations, academia, and the general public, to express their views, and support the Net Zero Asset Owner Alliance (Alliance) efforts to advance the state-of-play with respect to Net-Zero (Paris-aligned) Portfolio Target Setting by increasing methodology and data robustness, strength and transparency, and related efforts to measure members portfolio interactions with emissions.

The content received will be used to inform various efforts of the Alliance, such as target setting guidance, reporting, methodological uses, and public facing progress reports. Additional information to justify or support comments made is also welcomed. All input received will be kept confidential and internal, unless consent is given by the respondent.

We will share this call for comment directly with all data/service providers and NGOs we believe may be interested in commenting, it will also be posted publicly on the Alliance website [www.unepfi.org/net-zero-alliance](http://www.unepfi.org/net-zero-alliance). See Annex I for those who received a direct invite to comment, if your organization wishes to be included in future communication please submit your organization name, webpage link, and a contact email to [the contacts at the end of this document](#), we intend to give parties who otherwise might not have been identified and consulted a chance to submit information.

#### Request for Comment (not compensated)

This document outlines the requirements of a range of members in the Net Zero Asset Owner Alliance with regard to setting emission targets to achieve net-zero investment portfolios by

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2050. It is not an offer of commercial contract. This document outlines needs with the view to informing a wide variety of data and service providers, NGOs, and public, as to the needs and insights of the AO membership. We seek responses and insights from those who may be qualified.

Please provide responses through <https://forms.gle/QdUzkCYgBN7skd4j9>.

### Context – A collective carbon neutrality target

The [Net-Zero Asset Owner Alliance](#) is an international group of institutional investors with a commitment to “transitioning our investment portfolios to net-zero GHG emissions by 2050 consistent with a maximum temperature rise of 1.5°C above pre-industrial temperatures, taking into account the best available scientific knowledge including the findings of the IPCC, and regularly reporting on progress, including establishing intermediate targets every five years in line with Paris Agreement Article 4.9.

Members will seek to reach this commitment, especially through advocating for, and engaging on, corporate and industry action, as well as public policies, for a low-carbon transition of economic sectors in line with science and under consideration of associated social impacts.

This commitment is made in the expectation that governments will follow through on their own commitments to ensure the objectives of the Paris Agreement are met.”

### [Download the Collective Commitment Document](#)

The Task Force on Climate-related Financial Disclosures (TCFD) is considering how asset owners and managers could disclose information on the position of their portfolios relative to the transition to a net zero carbon economy. As a result of this and other climate related movements, major asset owners (within or independently of the NZAOA) have started to use metrics that describe where their investment portfolios are positioned relative to the goals of the Paris Agreement. The TCFD believes that such information is likely to be informative for investors as countries increasingly commit to furthering the goals of the Paris Agreement. To

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take this topic further, the TCFD has created an “Implied Temperature Rise Associated with Investments” working group, which coordinates closely with the NZAOA.

### Our need – a call for comment from climate data providers, NGOs, academia or public.

In order for us to monitor progress and report against this 1.5°C target and feed this ambition into the COP26 process in close coordination with the UN Special Envoy for Climate Action and Finance as well as the TCFD secretariat, we express a need to develop robust measurement methodologies. While various solutions providing an “implied temperature rise” metric already exist, more convergence is urgently needed. The NZAOA is not designed to develop such solutions. Instead, this “Call for Comment” defines the core methodology principles required and is launched in order to generate adequate methodology developments that will better suit our needs.

The methodologies we need to achieve this goal should be based on the following principles (underlined features are “must haves”):

### Core principles

#### 1. Impact.

- a) The methodology must provide investors / users with a quantified view of the impact of their investments on climate change. This is generally described as an “inside-out / impact” approach, which differs from more traditional “outside-in / VaR / risk” approaches. However, NZAOA members, as long-term institutional investors, act in the belief that ultimately those two approaches necessarily converge: investment strategies that degrade ecosystems will harm long-term investment returns.
- b) The quantification of the alignment of a company’s activities against the pathway commensurate with a 1.5°C temperature rise is key for asset owners’ beneficiaries and asset managers’ clients in understanding climate-related risks associated with individual funds, products, and investment strategies.

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## 2. Forward-looking.

- a) The methodology must provide investors / users with a forward-looking metric, at 5year intervals through to 2050.
- b) As a result, the nature of the metric is expected to require integrating forward-looking data such as sectorial and geographical GHG reduction requirements, Capex, green revenues, green share / brown share as well as public corporate commitments to “decarbonize” business mix in the “real economy”, for example in line with technology shifts derived from the EU Taxonomy, per sector.
- c) Methodologies that are unable to factor such strategic reorientation commitments, especially those with a shorter timeframe, will not be considered compatible with the methodological principles.

## 3. GHG footprinting.

- a) GHG emissions footprinting must form the basis of this methodology; GHG Protocol Scopes 1 and 2 must be included.
- b) Scope 3 emissions (eg “upstream” and “downstream” / product-related emissions) should be covered at least for sectors where these are material (>40% of total emissions).
- c) With respect to Scope 2 and 3 emissions, how potential double-counting of emissions is identified and treated should be clearly explained and justified.
- d) With respect to all GHG emissions data used, the sources of that data should be identified as well as how the completeness and accuracy of the underlying data is validated.
- e) The NZAOA expresses a preference for footprint intensity normalization rules based on Enterprise Value. This is also the approach pursued by the EU within taxonomy-related developments.
- f) Principles 2 and 3, in combination, require that forward-looking metrics are translated into future carbon footprint implications. Assumptions around this translation should be clearly explained.

## 4. Portfolio alignment / investment “temperature”.

- a) The methodology may produce several KPIs and qualitative insights, but it must deliver a “core” metric expressed in terms of a forward looking carbon KPIs (both relative to production and absolute) as well as temperature KPI, for users to assess considerations around “portfolio alignment” with the Paris Agreement.
- b) See also “Coverage” section below for asset class aggregation concerns.

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**5. Science-based decarbonization.**

- a) The methodology must be based on adequate IPCC scenarios and seek to promote “real world impact” by encouraging investment decisions that lead a decarbonization of the economy. While the sharing of emissions responsibilities and emissions reductions must be explicit and explained, it is however understood that “real world” impact requirements are currently challenging.

**6. Portfolio management.**

- a) The methodology must allow to compare single companies in a given sector and decide which company is better aligned towards net-zero by 2050 or an implied temperature rise of 1.5°C, as a basis of all investment decisions. This requirement effectively rules out methodologies which are based on estimations per sector alone.
- b) While initiatives such as SBTi are preferably expressed at sector or asset class level, this metric must be able to be expressed at individual issuer and portfolio levels (including multi-asset class portfolios) and may also be extended at an asset class level. The metric must make sense at both individual security and portfolio levels, to guide both investments and Asset and Liability Management (ALM) decisions.
- c) This metric must also be able to produce KPIs per sector, comparing these to a sector average or range, notably to guide engagement and ALM decisions, in coordination with the NZAOA’s Engagement Track, as well as other relevant organisations such as Climate Action 100+.

**Technical assumptions**

**7. Data sources.**

- a) Reported data must be favored over inferred (proxy-based) data, in particular where it is robust (eg audited, publicly reported), even though it is understood that a significant amount of GHG emissions measurement are estimates.
- b) Proxies may be used to cover lack of data provided these are transparent, and based on robust and dynamic (revised regularly) extrapolation rules.

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- c) Companies / emitters should be able to view their own data (GHG emissions, Capex, etc) and approve or correct it if necessary. When such corrections are made, they must be identifiable by data users.

#### 8. Sector biases.

- a) The methodology may look at companies based on sector specific analysis (using market-based sector classifications) or by comparing companies globally based on aggregate emission levels.
- b) Sector specific analysis could help investors select best-in-class companies while aggregate emissions analysis could inform wider investment strategies, promoting a deviation away from certain “high temperature” sectors altogether.
- c) The methodology may also offer a technology-agnostic/sector-agnostic transition pathway.
- d) Outright divestment assumptions *per se* are not favoured, but may be justified for “outdated” technologies, such as thermal coal, that present no clear value-add towards carbon neutrality.

#### 9. Climate scenarios.

- a) The use of specific climate scenarios (either individual scenarios or combinations of scenarios representing a given consensus), as well as deviations or exclusion of others, must be explicit regarding socio-economic and technological developments as well as climate policies, especially the underlying energy mix and sensitivity to specific technologies such as CCS.
- b) The approach should accommodate not only a single scenario but a set/corridor of scenarios to reduce dependency on individual providers’ and scenarios’ data, assumptions and narratives. In any case, if multiple scenarios are used, their coherence and consistency must be made explicit.
- c) A special attention is given to 1.5 °C IPCC scenarios with limited/no overshoot and no or limited use of CCS/BECCS: the methodology should notably align with IPCC P1 and P2 scenario carbon reduction suggestions.
- d) To improve comparability, scenarios can for example be based on and if possible connected to regulatory stress-testing initiatives, where appropriate.
- e) The underlying scenarios should be regularly reviewed and where new evidence becomes available should be updated to reflect this. Unrealistic or obsolete scenarios must be

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discarded. The approach should be sufficiently flexible to enable sensitivity analysis to be performed by users with respect to key assumptions and data choices. This flexibility should include accommodating not only a single scenario but a set of scenarios to take account of the uncertainty associated with future developments and to reduce dependency on individual models or data providers.

#### 10. Back-testing.

- a) The methodology should provide at least 5 years of back-testing capability, although it is understood that its forward-looking nature (Principle 1) can make back-testing challenging.
- b) The methodology should be “neutral” regarding corporate ownership structures (eg mergers) and consolidation across asset classes.

#### 11. Coverage.

- a) The asset classes covered must include at least corporate debt and equity.
- b) The security coverage must include at least the main listed equity indices.
- c) Covering other asset classes is valued and encouraged, in particular sovereign debt, Real Estate and Infrastructures. Sovereign debt “modules” must integrate both the 2015 COP21 NDCs and revised 2020 COP26 NDCs. Solutions for other asset classes are encouraged.
- d) In addition, it must set out clearly how the temperature KPI can be aggregated across investments in different asset classes, sectors and companies for users to assess the overall “portfolio alignment” with the Paris Agreement.
- e) Methodologies that cover only a small set of carbon intensive sectors will not be considered compatible with the methodological principles, although a variable methodology depth across sectors may be acceptable.

#### Usability & platform requirements

#### 12. Target-setting & reporting.

- a) Once finalized, the metric must be readily leverageable by investors (and link to sectoral pathways to net-zero by 2050) to monitor progress against their intermediate (TBC) and long term NZAOA targets (at a sectoral level or at least portfolio level) and support annual public reporting from NZAOA members.

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### 13. Transparency, replicability, stability.

- a) The methodology principles must be documented and transparent, meaning the results produced by calculations can be replicated by other investors using the same databases.
- b) In addition, changes over time to the methodology should be carried out in a controlled manner, should be documented and analysis of change conducted to ensure that period to period changes can be properly interpreted.
- c) The methodology and/or organization promoting it should make it possible for companies to validate and where appropriate or correct the data or results.

### 14. Open source.

- a) The NZAOA publicly favors open source platforms, but nonetheless encourages the development of methodologies that may be proposed by commercial enterprises, provided those commercial solutions are in line with the methodology principles described in this document and are documented, transparent and replicable.
- b) Whether the methodology has been developed by a public or private organization, it should disclose how the methodology, and where appropriate its implementation, is validated. Any potential conflicts of interest should be clearly disclosed.
- c) More generally it should leverage existing frameworks where applicable, such as the TCFD, SBTi, IIGCC PAII, TPI, PCAF, PACTA, INVECAT, CDP / Tropic, etc. The methodology should be regularly benchmarked against other methodologies.

### 15. Pluggability.

- a) The methodology should ideally use underlying databases and classification systems that make it “pluggable” into financial data terminals (notably by using standard financial market identifiers such as ISIN and CUSIP codes) to improve usability and enable as widespread users as possible, beyond NZAOA members in due course. NZAOA members do not expect, however, such “pluggability” from the outset.

### 16. Communications.

- a) The basic principles of this methodology must be simple to explain to non-specialist audiences, while the full underlying methodology may remain complex.

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### Next steps:

Some existing tools and methodologies satisfy several of the above requirements, and SBTi developments will be helpful, but no initiative currently fulfils enough requirements for NZAOA members to converge on an existing solution. Combinations or modifications of existing approaches, as well as entirely new solutions may equally suit the needs of NZAOA members, provided they cater to the needs expressed in this document. NZAOA members are aware the requirements listed above are demanding and not expect any provider to fill all gaps, but consider this a roadmap to highlight a trajectory over time. However, it is expected that deviations from requirements be identified and explained. Members are also fully open to extra suggestions and/or being challenged on certain requirements expressed above.

This work will be conducted in close coordination with the TCFD's "Implied Temperature Rise" working group and the COP26 Climate Finance Track. As highlighted above, neither the NZAOA nor the TCFD secretariat will advocate for a specific commercial solution, but members will be free to choose individual tools provided these fit the remits outlined in this document.

### Expected Response:

1. The Alliance encourages interested parties to respond "point by point".
2. Referencing the Criteria number they refer to the respondent, if a data or service provider, should clearly indicate if they are able to produce the required criteria or not.
3. Then respondent, whether data/service provider, NGO, academia or member of the general public should then express a view on the criteria under response.
4. To facilitate ease in your response the following survey is provided, you are encouraged to respond through the survey: <https://forms.gle/QdUzkCYgBN7skd4j9>

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**Timeline:**

**April 21** – Publication and circulation of Call for Comment

**May 01** – Deadline to submit Responses

Alliance will react to qualified responses only.

NZAOA members will review comments with an aim to screen proposed features against the key building blocks outlined in this document, understand key judgements and trade-offs for each features, weigh pros & cons and assess robustness in liaison with solutions providers.

**Note:**

This call for comment offers no compensation or contract. Rather it is an indication of the needs of the members of the Net Zero Asset Owner Alliance. Preparing this document will indicate needs from Alliance to a range of service providers who may be interested in tailoring their products to the standards contained herein. Any bilateral arrangements of compensation or contract are separate and distinct from the Alliance.

We issue this methodological criterion with the expectation that data/service providers will react beginning to transition in this direction of improved and more transparent data and outputs as described in the criteria above.

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PLEASE SUBMIT REACTIONS AND COMMENTS:

- By Survey <https://forms.gle/QdUzkCYgBN7skd4j9>
- By May 01 2020

We look forward to the ideas of providers in enhancing this version of the call for comment

**Main contacts:**

*With any question please contact:*

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## Annex I

The Alliance attempted to identify all known potentially interested partners. The Alliance will share this document with the following list. In an effort to be transparent this list is made available to the public. If you wish your organization to be included in future notifications of a similar nature please complete the survey and include your organizations contact details.

1. 2dii
2. 427
3. Acclimatise
4. Arabesque
5. Asset Owner Disclosure Project, ShareAction
6. Baringa
7. Beyond Ratings
8. Bloomberg ESG Data
9. Carbone 4
10. Carbon Delta (MSCI)
11. Carbon Tracker
12. CDP
13. Climetrics
14. EcoAct
15. Engaged Tracking
16. ERM
17. Investor Agenda Founding Partners
18. ISS
19. Oliver Wyman
20. Ortec Finance
21. OS-Climate
22. PWC
23. Quantis
24. Right.XDC
25. SBTi FI
26. SENSES
27. Southpole
28. Sustainalytics
29. TPI
30. Trucost (S&P)
31. Vigeo Eiris (Moody's)
32. Vivid Economics

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