Net Zero Asset Owner Alliance response to the TCFD public consultation July 2021

The UN-convened Net-Zero Asset Owner Alliance (AOA), representing $6.6 trillion in assets from leading pension funds and insurance companies across the globe, warmly welcomes the proposed new guidance from the Financial Stability Board's Taskforce on Climate-related Financial Disclosures (TCFD). 2021 is set to be a landmark year for climate-related reporting. The proposed new guidance from the TCFD represents an important step forwards in the Taskforce's guidance to preparers. In particular, the AOA supports and welcomes the:

- Proposed cross-industry set of metrics that should be disclosed by all preparers, which would help investors who have diversified portfolios get a clearer overall view of risk and opportunities.
- Distinction between climate-related metrics and climate-related financial impact metrics.
- Emphasis on forward-looking metrics.
- Inclusion of transition plans and Paris Agreement alignment of financial portfolios, as well as updated guidance on target setting in line with key regulator developments and investor industry initiatives since 2017.
- Flexibility on how investors should measure and disclose portfolio alignment
- The framework in the Portfolio Alignment Technical Supplement on how a portfolio alignment methodology should be designed.

There are, also, areas where the Alliance believes the guidance could be made more effective. The points here draw from discussions with AOA members, key stakeholders, as well as the consultation responses from the PRI and UNEP-FI.

1. **Improving the comparability of disclosures**. The proposed new guidance would increase the quality and usefulness of disclosures, yet it is less clear how the Taskforce proposes to improve the comparability of TCFD reporting. From a users' perspective improving the comparability of climate metrics and targets is a high priority, as such the AOA recommends:

Metric / target	Non-financial companies	Financial companies
Disclosure of industry benchmarks for carbon intensity metrics	Company emission intensity disclosed alongside the average for its GICS industry group	The WACI or Implied Temperature Rise of a portfolio should be compared to a market performance benchmark (e.g., the MSCI World, FTSE 100, STOXX 500).
Adding a target setting template to the new TCFD guidance	Should include the scopes covered, reference scenario used, assumptions about negative emissions and offsets. See page 7 for a suggested template	Should include the scopes covered, methodology used, assumptions about negative emissions and offsets. See page 7 for a suggested template

The guidance calls for targets to "quantified and granular" yet without a common template for climate targets, it is unclear as to how this would be realised. A suggested template is provided on page 11.

2. **"2 degrees or lower" vs 1.5 degrees.** Since the Taskforce published its recommendations in 2017, it is not only market practice on climate-related disclosure that has evolved but also understanding of climate science, notably through the IPPC's Special Report on 1.5°C. Yet, the language in the TCFD on relevant scenarios remains unchanged since 2017 and refers to 2° and 1.5° interchangeably through the phrase – "2 degrees or lower".

   However, for preparers' use of scenario analysis or target setting and users' understanding of these disclosures, the difference is significant. The global carbon budget for 1.5° in the IPCC's 1.5°C report is approximately half that of commonly used 2°C scenarios like the IEA's SDS and NGFS' orderly and disorderly scenarios[1]. The difference with IEA's 2DS scenario is even larger still.

   The Alliance recommends revising the guidance on relevant climate scenarios from "including 2 degrees or lower scenario to "including a 1.5 degrees scenario".

3. **Internal carbon pricing.** The inclusion of internal carbon pricing in the cross-industry metrics is welcome. It will help provide users with information about assumptions companies and other preparers make on the pricing of carbon, as well as stimulating debate and regulatory preparedness within TCFD report issuers, especially in countries where carbon pricing has yet to be established, on what their disclosure should be**.**

[1] See table 4 on page 30 of this report a comparison of commonly used scenario's global carbon budgets.

Since experience and market understanding of carbon pricing varies considerably across regions, the Alliance recommends the guidance references in the annex on page 81 key publications where information on the levels of carbon pricing across different scenarios can be found. These include:

- Report of the high-level commission on carbon prices by J. Stiglitz and N. Stern (2017) https://www.carbonpricingleadership.org/report-of-the-highlevel-commission-on-carbon-prices
- Table 2.2 on CO^2 pricings for energy production, page 53 IEA Net Zero Roadmap https://www.iea.org/reports/net-zero-by-2050

Feedback on the Portfolio Alignment Technical (PAT) Supplement

The AOA welcomes the PAT paper as an important step forward in the development of design principles for portfolio alignment metrics. The AOA would welcome the opportunity to continue a dialogue on the development of portfolio alignment metrics with the PAT team. Key areas for clarification and development include:

- Absolute vs intensity-based measures. The guidance proposes the use of an intensity rather than absolute-based measure for the convergence benchmark. The Alliance would welcome further dialogue to clarify the adjustments made to move from an intensity-based measure to an absolute measure of the implied temperature of a portfolio.
- Single scenario selection. We would also welcome the opportunity to further discuss how to avoid bias through inappropriate selection of a single scenario benchmark.
- Use of language to describe each of the three alignment options. The headline recommendation is non-prescriptive with respect to the different alignment options and care should be taken to ensure the use of language in characterising each of the alignment options is objective and consistent with this – e.g. the statement that ITR models are "more sophisticated" than other alignment options (section B, page 5).
- Recommendation 13 suggests scenario developers build out benchmarks for methane. The CO2e of methane is captured in current models. This recommendation may shift the focus of developers away from improving methodologies and data quality and coverage to building out an improvement of a limited value for investors. We suggest changing to "in medium to long term".
- Recommendation 16 suggests that the credibility of company targets should be back-tested. This implies that financial institutions as users of the data and data providers would need to audit company targets. This could be avoided if companies themselves had their company targets audited by third parties.
- Recommendation 10/11 suggests including scope 3 emissions in the alignment benchmarks based on the position that they are "easily extracted from existing scenarios" (page 33). For the majority of sectors, the issues related to scope 3 emissions such as differences in data providers, comparability and double counting, remain unresolved. Further guidance from the TCFD to companies on disclosure of scope 3 emissions, would help mitigate these data challenges in the medium term.
- Recommendation 6 suggests using only convergence-based benchmarks. While, in principle, we welcome this recommendation, at present such benchmarks only exist for a limited number of

sectors. For financial institutions, a strict application of this recommendation would consequently result in lower coverage of assets under management, making the output from a portfolio alignment tool less decision useful. Allowing the use of convergence-based benchmarks along with rate-of-reduction benchmarks would significantly increase the coverage of assets under management, in particular for companies operating in heterogeneous sectors which make-up the majority of the world economy.

- Additionally, a further clarification could be made on the use of Enterprise Value Including Cash (EVIC) for deriving financed emissions vs Enterprise Value excluding cash, which is a standard corporate finance approach and advocated by the EU Technical Expert Group in their final report on EU Climate Benchmarks and ESG disclosures.

The AOA stands ready, and would welcome the opportunity, to support the PAT team via a technical exchange on the challenges above, in order to help find solutions to advance the development of forward-looking portfolio alignment metrics.

Annex 1: Target setting template[2]

GHG target disclosure template		
Target ID		
Overall number of active GHG emissions targets:		Include interim targets in the count
Target number:		
Target type:		Indicate whether this is aboslute or relative
Date the target was set:		
Target Information		
Scope(s) covered		For scope 2 emissions, indicate if calculations are location- or market-based. For scope 3 emissions, indicate the GHG protocol categories that are covered.
Organisational boundary		Describe the accounting boundary (e.g. operational/equity) on which the target is set. This should be consistent with its historical emissions and production/sales disclosures. Note additional exclusions if any (e.g. regional basis).
Percentage of in-scope emissions covered by the target :		
Base year:	Base year emissions:	For intensity targets, provide activity measure (e.g. tCO2e/Mwh or tCO2e/tonne of cementitious product)
Target year:	Target year projected emissions:	
Targeted reduction from base year (%)		
Targeted reduction from current year (%)	Current emissions:	Please indicate the most current year for which emissions data is available.
Target Methodology		
Verified by a independent third party?		If yes, please indicate the name of the independent third party that verified the target
Name of the reference scenario used		
Source describing how the percentage of in-scope emissions covered by the target has been calculated		Please indicate the title(s) of publicly available documents and relevant page numbers where information can be found.
Source describing transition plan outlining how this target will be met.		Please indicate the title(s) of publicly available documents and relevant page numbers where information can be found.
For Scope 3 targets, source describing the methodology used to calculate the Scope 3 emissions covered by the target.		
Indicate the % of the target to be achieved through offsets and provide a source specifying their type and the offset provider.		
For intensity targets, source describing the methodology used to calculate the carbon intensity.		

[2] The AOA is grateful to the London Stock Exchange Group for providing the basis for this template.