12 July 2022

LAPFF Response to Transition Plan Taskforce call for evidence

Background

- The response is required to be submitted online, each question response individually. Each response has a limit of 4,000 characters.
- LAPFF has taken the opportunity to provide our view on those issues which we consider relevant to our activities.

Detailed response

1. *Do you agree with the proposed definition of a transition plan? If not, why, and what alternative definition would you suggest?*

The definition states that the plan should set out how an organisation 'will adapt as the world transitions towards a low carbon economy'. In LAPFF's view, the terminology should be a 'decarbonised' economy or 'climate neutral' given that there are also non-carbon greenhouse gases. It would be preferable if the targets were to mitigate climate 'impact' rather than 'risk'. The term 'net zero' should be used with caution as it is not synonymous with greenhouse gas reduction targets, which are what should be provided. The emphasis should be on reducing emissions, not by using carbon offsetting initiatives. Further to LAPFF's view, the targets should, *de minimus*, be aligned with the Paris agreement.

2. *From your perspective, who are the key users of transition plans?*

It is evident from the call for evidence that the primary users of transition plans will be financial institutions and companies, as such plans will provide the framework for strategic decisions that company boards will need to be making now for the next five- and ten-year periods and for financial institutions over the same timeframe.

Other primary users will be politicians and policymakers who will be able to use transition plans to identify areas where strengthened regulation may be needed if the aggregate progress set out within transition plans is not indicating sufficient progress will be made. This will help ensure that the government is creating the right legislative framework for delivering change such as carbon tax.

Equally, transition plans will provide essential information for shareholders and other stakeholders including the public. For shareholders it will drive decision-making and help focus engagement; for employees and communities it will help their contributing to what needs to be a fair and just transition. In this way each stakeholder group will be able to understand respective roles and responsibilities as they plan for enabling a just transition to a decarbonised economy.

3. From your perspective, what are the key use cases for transition plans?

Key use cases will be for the sectors most likely to experience significant change. In ensuring a transition plan is set over an appropriate timeframe, investors will be able to set aside adequate resources to manage the risks and impacts on their portfolios which will include scrutinising investment managers on how they are managing the transition.

In engagement, a clear transition plan will help investors set clear expectations of companies, including how they are reporting their current impact and progress against targets. This will ensure that investors focus engagement to identify upcoming risks, and to identify strategies for mitigation.

A clearly set out transition plan will also be a core component in capital allocation decisions, giving confidence that key risks and opportunities have been identified and guiding investment decisions.

Another key use case from LAPFF's perspective is to ensure transition plans mitigate the financially material risks of an unjust transition. LAPFF supported the APPG for Local Authority Pension Funds inquiry into 'Responsible investment for a just transition'. Evidence to this inquiry showed that if the transition is viewed as unfair and unjust there is likely to be public resistance and a lack of co-operation, which may impede implementation of many of the practical measures necessary to reduce carbon emissions. The positive aspect of this is the potential for fostering skills and employee roles that are core to delivering decarbonised business growth.

4. *How should the TPT select which sectors to develop tailored transition plan templates for? Following that logic, what financial sub-sectors and real economy sectors should the TPT prioritise? In what order should these be addressed?*

In LAPFF's view, there should be a base principle-based transition plan template. Different sectors can then apply existing and developing guidance in identifying risks and opportunities, setting strategy and targets and timeframes aligned with remaining within the scientifically identified carbon budget.

The need for investors to ensure boards of companies in their portfolios are formulating appropriate strategies and applying associated transition plans was made more imperative by the Intergovernmental Panel on Climate Change's 2021 report. This sets out that, for an 83% chance of remaining within 1.5°C of warming, the global carbon budget will be used up by 2027 at the current emissions rate.[1]

5. *Given the mandate set out in the TPT's Terms of Reference, to what extent, and how, should the TPT consider issues beyond a firm's contribution to an economy-wide decarbonisation?*

The terms of reference set out that there is existing guidance from TCFD and from organisations such as Climate Action 100+ (CA100) and the Institutional Investors Group on Climate Change (IIGCC) in terms of a good quality transition plan. LAPFF has found the CA100+ benchmark particularly useful in identifying relevant metrics and targets for companies and appropriate timeframes that have an 'acceptability' for investors.

Of the 166 companies covered by the CA100+ initiative, which account for up to 80% of corporate industrial greenhouse gas emissions, only eight are listed in the UK. For the eight companies that are UK listed, it may not be the UK economy that is likely to be most relevant for them. In LAPFF's view, the primary consideration should be how a firm contributes to remaining within the available global carbon budget. Then for those that primarily only have operations in the UK, it would be more relevant to refer to the 'economy-wide decarbonisation'.

For particular sectors, such as oil and gas, consideration should be given to the International Energy Agency roadmap to net zero emissions by 2050 (IEA NZE) which sets out that 'no new oil and natural gas fields are needed in the net zero pathway'. For other sectors, such as the power sector, there are recognised pathways. For developed markets this would be a net zero emissions by 2035 target for electricity generation.

[1] https://www.ipcc.ch/report/ar6/wg1/

There are also initiatives such as the Science-Based Targets initiative which identifies appropriate targets for different sectors. Whilst LAPFF supports target setting, and identification of best practice within sectors, caution needs to be taken over targets aligned with net zero by 2050, as such targets only give a 50% chance of staying within 1.5°C warming.

For investors, as noted, the Glasgow Financial Alliance for Net Zero (GFANZ) is developing practice principles for financial sector transition strategies that are applicable across financial sub-sectors and jurisdictions.

An important dimension beyond the firm's contribution to economy-wide decarbonisation is how companies are considering and addressing the social implications of net zero. Not considering the social dimension could undermine support for net zero and slow the decarbonisation process. As such it is a material issue for both companies and investors. In addition, as the Greening Finance roadmap sets out, sustainability covers social issues. Leaving S out of transition plans would omit a large component of what responsible investors expect sustainability disclosures to include. Indeed, the value of transition plans would be considerably less if they omit how the transition will take place for stakeholders.

As such, LAPFF supports just transition plans, which it considers should also be integrated into reporting standards. The just transition is about the fair distribution of climate 'goods' (e.g., new jobs) and climate 'bads' (e.g., job losses) and covers workers, consumers, supply chains and communities, both at home and abroad. It is about both the outcome but also the process, engaging stakeholders and it being a planned and orderly transition. Plans should therefore cover company strategy on the issue, how the company intends to support and engage workers through the transition and promote good work, their approach to supply chains and ensuring human rights, engaging and addressing social risks facing communities, approach to supporting (vulnerable) consumers, and its approach to public policy.

6. *Which of these issues are a 'must-have' that need to be addressed in all transition plans, and which are 'desirable', which add depth or breadth but are not central to a transition plan?*

All the elements identified in the Terms of Reference 'including but not limited to: short, medium and long-term targets; specific actions for climate mitigation and adaptation; capex plans; specific sectoral considerations such as fossil fuel phase-out plans and plans for scaling up new investment areas' are considered as 'must have' to be addressed in all transition plans, even if this would take a 'comply or explain' approach.

LAPFF would commend the inclusion of a company's approach to a 'fair and just transition' to ensure funds, government, companies and communities all work together to decarbonise the economy with sustainable outcomes.

Additionally, LAPFF concurs with the expectation that companies should have 'Paris-aligned' accounts that properly reflect the impact of achieving real zero emissions for assets, liabilities, profits and losses.

Addressing both of these issues would be considered 'must haves' for the purposes of transition plan disclosure.

7. *Do you envisage any tensions between entity-level decarbonisation and economy-wide decarbonisation goals? If so, can you provide examples and any suggestions as to how the UK TPT may address these in its guidance.*

The sectors that consider themselves 'hard to abate' often have long lead-in times for zero-carbon capital projects. Certain companies will argue that they are unable to match the short-term economy-wide decarbonisation goals that are required. This is where the UK TPT might advise the regulatory regime addresses the needs of such sectors and that government focus attention on levers that would enable such projects.

8. *What other financial or non-financial, mandatory or voluntary frameworks and processes are you aware of that the TPT should consider as it proceeds?*

TPT should consider

- the voluntary framework on aligning corporate policy and practice with the temperature goals of the Paris Agreement as provided by the Global Standard on Responsible Climate Lobbying see www.climate-lobbying.com.
- IIGCC Investor Expectations for Paris-aligned Accounts, setting out evidence that companies are taking decarbonisation or the physical impacts from climate change into account in their financial statements, see https://www.iigcc.org/download/investor-expectations-for-paris-aligned-accounts/?wpdmdl=4001

Questions on Section 2: The Sector-Neutral Framework

9. *Where would you prefer for companies to disclose information on their transition plans? Please explain your reasoning, including on how the suggested location relates to the intended audience.*

LAPFF supports the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures report and considers all market participants should be encouraged to aim for the fullest relevant implementation. The Forum has long promoted mandatory climate risk reporting, the mechanism for which is already in place under the Companies Act requirements for companies to report financially material risks in the annual report. LAPFF also considers that in positioning themselves for the required decarbonised future, companies should disclose a transition plan.

Given the detail that may be required, it may be inappropriate to expect full plans to be set out in an annual report. Transition plans therefore should be produced as standalone documents on company websites. However, the main elements of plans should be set out in the annual report with a clear link to the full report. Providing the main elements will enable investors and other stakeholders to understand the material risks and the ways in which the company is decarbonising its business model. As set out above, financially material risks should also be set out to investors in the annual report as required under the Companies Act.

In addition, LAPFF also supports the Say on Climate initiative, which provides the opportunity for shareholders to endorse or not, the company's strategy, targets and progress. As such, mandatory requirements for transition plans should be accompanied by a mandatory vote on the transition plan. LAPFF considers this an important way to not only better understand a company's approach, but be able to consistently hold companies to account.

10. *How prescriptive should the Sector-Neutral Framework be, recognising the need to balance flexibility in how firms disclose transition plans with more prescriptive templates that seek to facilitate comparability of firms' transition plans?*

The sector-neutral framework should be prescriptive about the objectives and categories that should be covered.

The framework needs to be prescriptive about the objectives required to meet Paris goals and science-based targets. This is the objective set by governments and is the standard by which many investors and those in civil society already hold companies to account. Anything weaker would mean some companies do not disclose the scale of the challenge or the investment risks. It therefore increases the chance of greenwashing and poses market-wide risks.

The framework should be prescriptive not only about the overarching objective (set out above) but also what a transition plan needs to cover, including the main headings. This will enable shareholders and stakeholders to make comparisons between peer companies.

However, LAPFF considers within that framework that there should be scope for companies to set out their own approach tailored to the specifics of their company and sector.

11. *Should the TPT seek to standardise the data and metrics used to communicate ambition and measure progress in transition plans? If so, what are the standards for data and metrics that you would recommend including in the Sector-Neutral Framework and in supplementary sectoral guidance?*

As set out above, the framework needs to be prescriptive about the objectives. Anything weaker would mean some companies do not disclose the scale of the challenge or the investment risks. This applies to the data and metrics used and without prescription there is a greater chance of greenwashing. A transition plan that does not refer to these expectations on emissions reductions with timelines will be sub-optimal.

Setting clear targets and with specific metrics is a main ask that major investors make of companies. For example, CA100+ an investor group with $68 trillion of assets, expects companies to set targets aligned to 1.5°C.

The 2015 Paris Agreement set out a global framework to avoid dangerous climate change by limiting global warming to well below 2°C and pursuing efforts to limit it to 1.5°C. In 2021, the World Meteorological Association noted the world has already reached 1.2°C of warming. The Intergovernmental Panel on Climate Change has set out that, for an 83% chance of remaining within 1.5°C of warming, the global carbon budget will be used up by 2027 at the current emissions rate.

Given these risks, LAPFF expects the following of companies:

- Disclosure of a strategy addressing climate risk and carbon-emission reduction with clear timelines for action, which investors and others can therefore assess and hold the company to account over time.
- The company's targets are in line with limiting global warming to 1.5°C compared to pre-industrial levels, which is in line with LAPFF expectations and best practice.
- The company is committed to carbon neutrality by 2050 at the latest and targets are quantified for Scopes 1, 2 and 3, thus showing a full commitment to reaching net zero. As part of this commitment the company is focused on actual emission reductions and not heavily reliant on offsetting.

Given this, the transition plans should require companies to assess whether the plan and individual elements within it are aligned with a 1.5°C scenario.

12. *Question for small and medium-sized enterprises: what specific challenges do you foresee for SMEs seeking to prepare or use transition plans? How can the guidance and framework prepared by the TPT address these concerns?*

    LAPFF's focus is with larger, listed companies. However, LAPFF expects large companies to work with their supply chain to help suppliers decarbonise their business model.

    To decarbonise Scopes 1, 2 and 3, LAPFF expects larger companies to be working with suppliers (and customers) on reducing emissions. In some cases, companies are already setting dates for a proportion of contracts to be with suppliers with their own science-based targets in place.

    As part of just transition plans considering the social implications of climate action, LAPFF expects larger companies to set out how they are working with suppliers.

13. *Question for preparers only: if your firm does not already disclose information of the type outlined in this Call for Evidence, what are the reasons for that? For example, are there concerns about legal or possible market risks arising from disclosure? How could the work planned by the TPT address these concerns?*

    n/a

14. *Transition plans provide an opportunity to ensure the benefits of the climate transition are widely felt by UK households and consumers. How can the guidance developed by the TPT balance the need to minimise costs whilst encouraging companies to develop strategies to maximise benefits for all?*

    Transition plans should include the social implications of climate action. As already noted, not considering the social dimension could undermine support for net zero and slow the decarbonisation process. As such it is a material issue for both companies and investors. In addition, as the Greening Finance roadmap sets out, sustainability covers social issues. Leaving S out of transition plans would omit a large component of what responsible investors expect sustainability disclosures to include. Indeed, the value of transition plans would be considerably lower if they omit how the transition will take place for stakeholders.

As such, LAPFF supports just transition plans, which it considers should also be integrated into reporting standards.

The definition of 'all' set out in the question, should be widened. Ensuring wider benefits and a just transition, requires that transition plans consider not just consumers but also workers, supply chains and communities. LAPFF recently supported an inquiry by the All-Party Parliamentary Group for Local Authority Pension inquiry into a just transition. It found that:

- A just transition is about transitioning to a low carbon economy in a just way for society – and thus combines the environmental and social.
- It is about the fair distribution of climate 'goods' (such as new jobs and cleaner air) and climate 'bads' (such as higher costs associated with decarbonisation and job losses in certain sectors and places).
- It is about both maximising the opportunities of a green economy and mitigating the risks – locally, nationally and internationally.
- The social dimension is primarily about workers, consumers, supply chains and communities.
- It is about both the process and the outcome: engagement and involvement of stakeholders is critical.
- It involves a planned and orderly transition

This widening of approach would also be consistent with initiatives such as the government's Green Jobs Taskforce.

LAPFF considers that just transition plans should cover how the company intends to support and engage workers through the transition and promote good work, their approach to supply chains and ensuring human rights, engaging and addressing social risks facing communities, approach to supporting (vulnerable) consumers, and its approach to public policy.

15. *Do you agree with the principles proposed in the Call for Evidence? Why or why not?*

Taking the three principles in turn:

It is welcome that principle 1 references 1.5 °C scenario. However, the use of 'ideally' will considerably undermine the value of transition plans. The wording should be strengthened to ensure that all companies compare their plans with 1.5 °C. While it is not feasible to mandate alignment, companies should set out whether their plan is aligned with 1.5 °C. This is the expected standard of major investors, such as CA100+ and is aligned with the UK's international commitments as part of the Paris accord. Investors and stakeholders can then make judgements about the plan.

In regard to the plan covering 'the whole organisation' this should include upstream and downstream emissions (or Scopes 1, 2 and 3 emissions). As such, Principle 1 should be clearer about what this phrase means.

It is welcome that the plan focuses on short term actions and milestones. LAPFF would recommend there is a clear set of dates outlined. LAPFF considers that companies should set short-, medium- and long-term objectives with corresponding plans to reach them. This is aligned with expectations of other investors and investor coalitions such as CA100+. Alongside short-term targets, CA100+ expects companies to have medium term targets (2026-2035) and long-term (2036-2050) targets. These can then be used to assess whether companies are aligned with 1.5°C.

The principles should also make clear that the focus should be on actual emission reductions rather than offsetting and carbon capture and storage. Using voluntary offsets or carbon capture for avoidable emissions rather than taking the route of more substantial decarbonisation creates considerable investment and environmental risk.

Principle 3 could be strengthened regarding external verification of the emissions disclosures and the alignment of the target with 1.5°C. This verification should also include disclosure of the methodology. This will help investors trust the numbers and help guard against greenwashing.

16. *Are there any principles that you would add to the list outlined in the Call for Evidence? Why?*

As covered in previous submissions, the principles could be strengthened or added to by:

- Ensuring plans comparable to 1.5°C scenario, cover Scopes 1-3 emissions, and include short, medium and long-term targets (with definition of what time periods they cover).
- Focus on actual emission reductions (real zero) rather than offsetting and carbon capture (net zero).
- External verification of emission numbers and whether numbers aligned with 1.5°C.
- Include social dimension in transition plans – effectively ensuring transition plans are also 'just' transition plans.

17. *Which of the principles outlined in the Call for Evidence would you regard as 'must-haves' or as 'desirable'?*

All the principles are must haves but need to be strengthened or added to as per our response to questions 15 and 16.

18. *Principle 1 notes that a transition plan should cover the whole organisation. There may be challenges for internationally active firms in meeting Principle 1, given that different jurisdictions will have different economy-wide transition pathways.*

How can the TPT design its standard and guidance in a way that accommodates credible transition plans consistent with the broader strategy of a firm, but reflect differences between approaches taken in different jurisdictions?

Given that all jurisdictions are covered by the Paris Agreement which aims for to limit the temperature increase to 1.5°C above pre-industrial levels, the guidance can accommodate jurisdictions that may initially appear more challenging, by tailoring to such different approaches. For example, engagement through the Asia Transition Platform with Chinese financial companies has asked for emission reduction commitments 'in line with China's twin targets' but also for sector specific pathways for minimum standards for financing and capital market activities that include: for coal, policy to prohibit the financing of all new capacity addition and phase out by 2045 and for oil and gas, policy with clear restrictions on new exploration. Additionally, targets have been requested for 'sustainable finance'.

19. *Do you agree with the elements proposed in the Call for Evidence? Why or why not?*

The elements cover the main asks LAPFF makes of companies. These will help investors understand the ambition of companies and the targets and planned actions to meet that objective. It will help provide investors information on governance of climate change and companies' approaches to lobbying. It is welcome that the elements cover supply chain and products and services. It is also welcome that they also include approaches to metrics and monitoring.

As noted above, LAPFF considers it an oversight not to include an explicit element on a 'just' transition. This should include transition plans for workers, supply chains, communities and customers and cover likely impacts, engagement with stakeholders and overarching plans to ensure a just transition. More generally while the elements cover the main areas LAPFF expects, LAPFF is concerned the sub-elements in certain places are not specific enough. This may hinder comparability between companies and create issues with greenwashing.

For example, element A includes interim targets and dates but does not define what short- and medium-term means. This could be open to wide interpretation. Measures, targets and metrics should be more explicit regarding expectations on Scopes 1, 2 and 3 emissions. More detail would be welcome on expected disclosures on the alignment of capital expenditure with a 1.5°C scenario. On public policy engagement, LAPFF would expect to see disclosure of an annual monitoring and review process of climate lobbying policies and activities. The review should ensure all direct and indirect lobbying activities are captured. Examples are expenditure on lobbying activities and disclosure of membership of all industry associations. The review should also set out a clear framework for addressing misalignments between climate change lobbying positions adopted by the associations of which the company is a member and the goal of restricting global temperature rise to 1.5ºC.

20. *Are there any elements that you would add to the list proposed in the Call for Evidence? Why?*

As noted above, LAPFF considers it an oversight not to include an explicit element on a just transition. This should include transition plan for workers, supply chains, communities and customers and cover likely impacts, engagement with stakeholders and overarching plans ensure a just transition.

21. *Which of the elements outlined in the Call for Evidence would you regard as 'must-haves' or as 'desirable' for credible transition plans? In which instances should an entity assess materiality to determine whether an element is considered must-have and/or what level of disclosure detail is required?*

All the elements are required to make an assessment on the robustness of the transition plan. Having a complete picture of ambition and targets, actions internally and across the value chain, activity with policymakers, monitoring progress and having adequate oversight, are all essential components. What these must also include are standard expectations on how they are applied. Taking too flexible an approach will undermine investor confidence in the plans and their ability to assess the risks they and the market faces.

22. *Are there elements where you see substantial barriers to implementation? If so, which ones and why? Are you able to suggest alternatives which are both credible and practical?*

Companies are already reporting against these elements. As such, the taskforce should be confident about rolling transition plans out. Given the risks that climate change poses to investors and to the economy, there needs to be greater clarity about the degree to which plans are mandatory with fines for non-compliance. LAPFF has consistently raised concerns about the ‘comply or explain’ nature of some requirements of companies.

Further Feedback

23. Please share any other feedback or comments you may have on the work of the TPT and the Sector-Neutral Framework