



Glasgow Financial Alliance for Net Zero (GFANZ) consultation

**Defining transition finance and considerations for
decarbonisation contribution methodologies.**

Note: Carbon Market Watch prepared this response with input from [Reclaim Finance](#).

SEPTEMBER 2023

First, which sector is your organization part of?

- Academic, education, or research institution
- Financial institution
- Government/Public Sector
- Industry or trade association
- Non-Profit Organization, Non-Governmental Organization, or advocacy group
- Private Sector, non-financial
- Other: Please specify

Please indicate your region:

- North America
- Middle East and Africa
- Latin America
- Europe
- Asia Pacific
- Africa
- Other: Please specify

Is your organization a member of a GFANZ sector-specific alliance?

- Yes
- No

If you are aware of examples of published transition plans or case studies/examples of transition finance and measuring impact of those transition finance activities in practice that are publicly available, please email mainstreaming@gfanzero.com. (Subject line "case studies" and providing the material or link to the material you are referring to. Submissions in all languages are encouraged.) Please click "Continue >>" below to continue to the main survey...



Part I: Transition Finance

Climate Solutions

Are the proposed attributes sufficient and flexible enough to help you identify assets to this segment?

- Sufficient
- Somewhat sufficient
- Not sufficient

What would be an appropriate revenue threshold for the purposes of identification?

- Below 50%
- 50%
- Greater than 50%

Would the feasibility of alignment to a science-based pathway over time be a key consideration when identifying Solutions and Enablers?

- Yes
- No

Are separate and/or additional attributes required for Enablers?

- Yes
- No

Are there any other considerations for Climate Solution attributes, especially relating to hurdles to implementation (e.g., additional KPIs to consider, data limitations, suggestions for specific attributes for Enablers)?

Aligned and Aligning

Are the proposed attributes sufficient to help you identify entities to this segment?

- Sufficient
- Somewhat sufficient
- Not sufficient



Is the proposed target timeframe for alignment, set at 2030 and articulated through net-zero interim targets, appropriate for the purposes of identification?

Yes

No

Is the proposed progress and two-year continuous performance threshold for Aligned and Aligning appropriate for the purposes of identification?

Yes

No

Are there any other considerations for Aligned/Aligning attributes, especially relating to hurdles to implementation (e.g., data limitation, lack of disclosure regarding capex, other KPIs for degree of alignment)?

Managed Phaseout

Are the proposed attributes sufficient to help you identify assets to this segment?

- Sufficient
- Somewhat sufficient
- Not sufficient

Are there any other considerations for Managed Phaseout attributes, especially relating to hurdles to implementation (e.g., data limitation, lack of disclosure regarding capex, other KPIs for tracking phaseout progress)?

Segmentation Method

Considering the proposed approaches, do you foresee any potential unintended consequences that may disincentivize financing in the four key financing strategies or motivate behavior that may not be supportive of the net-zero transition?

If you were to implement the proposed approaches today, what could be some challenges you might encounter?

Other



What sub-segments would you consider under the 'All Other' segment? Please identify and provide rationale and examples.

Any additional feedback regarding Part I of this consultation?

Overview and Current State

What is your organization's preferred approach for measuring the impact of transition finance activities, for example for capital allocation, monitoring, and disclosure purposes? What are the benefits and drawbacks of these approaches?

- Definitely not the EER approach, since it is highly inaccurate and sensible to heavy polluters that see their chance in hiding behind the "hard-to-abate" label.
- Monitoring the direct investments that are easily measurable, like the switching to renewable energy and energy savings. Or divestment, which is also traceable, if defined correctly. Anything beyond this should be reported on in a narrative style without the unhealthy urge to quantify impacts where there are high chances of correlation rather than causation.

Would best practice approaches for calculating EER add value to your current investment/financing/underwriting practices?

- Yes
- Somewhat
- No

What are key considerations for the development of a decarbonization contribution methodology? What challenges do you anticipate?

- The difference between 'Aligned' and 'Aligning' is not bulletproof. The consultation suggests that transition finance can go towards companies that are both aligning and aligned to 1.5°C pathways, yet are only the latter truthfully on the right pathway. A company that has committed to a 1.5°C pathway, but not yet acted upon it/ not yet proven to be able to be 1.5°C aligned, might not be worth investing in. Therefore, a clear definition of 'aligning' must be provided, and must certainly not lack the prerequisite of becoming aligned with the support of the transition money.
- The BAU scenario used in the consultation assumes that there are "no efforts to transition". This definition lacks conservativeness since efforts to transition should have been taken years ago, and, if any, are certainly not future-proof in the face of upcoming regulations and standards. Moreover, sector-specific pathways are also not specific enough for the forecasting of future emission levels of individual units, as aren't counterparty pathways, since they leave room for exaggeration. Not even a unit-specific BAU projection would be specific enough to fulfill the objective, since regulation and trends are evermore changing and emissions/transition trends very hardly ever predictable. (The shortcoming of the EER approach is that it is based on generating a supposedly

hard number from two controversial methods: a counterfactual baseline of supposed “business-as-usual” (BAU) emissions for a company or sector in which it fails to transition; and the emissions from a pathway where its transition plan is successfully implemented. EER would thus be an estimation rather than a measurement.

- It is also a unit that would be based on complex, opaque and therefore subjective assumptions. These assumptions would include factors such as energy demand, economic growth, corporate performance, and legal, regulatory and political changes, over many years, potentially decades. And because of this complexity, and because a counterfactual can never be proven right or wrong, companies and their financiers could use extremely favorable assumptions to boost the delta between the baseline and the target pathway.
- This approach of creating a unit based on the gap between an imaginary baseline pathway and a projected actual pathway closely parallels the conceptual foundation of the carbon offsets market. This is a key reason why the offsets market has recently been subject to heavy criticism in the media.¹ GFANZ should take note of the current legitimacy crisis in the offsets market if it wants to see where its EER proposal would likely lead if it were ever to be adopted.
- In addition to pushing EER for high-carbon companies, the paper recommends that an “avoided emissions” approach should be used for evaluating the climate impact of companies involved in developing climate solutions. This approach has been used in the past by companies developing renewables projects, and their financiers. But it has come under strong criticism and has mostly been dropped, including because of the problem of exaggerated baselines (for example assuming that electrical grids will only decarbonize very slowly), and the fact that a company does not reduce its real-world emissions by, for example, generating additional megawatts of clean power, or producing more EVs, but by phasing out its coal plants or internal combustion powered vehicles.²)
- Importantly GFANZ does not propose that baselines be determined by independent third parties, but by the relevant company and its financier (p.32).
- “Enablers” (technologies or services that accommodate Climate Solutions) are assumed to be “part of the Climate Solutions value chain”. In many cases, “Enablers” are already existing within units, which makes the accounting of “Enablers” as part of the Climate Solution unrealistic.

¹ See e.g. [Error Log: Exposing the methodological failures of REDD+ forestry projects](#), Carbon Market Watch, September 2023. This is just one of the most recent examples of the extensive literature on the repeated and ongoing failures of offsetting (see e.g. International Rivers, [Failed Mechanism: Hundreds of Hydros Expose Serious Flaws in the CDM](#), December 2007; B. Haya, [Measuring Emissions Against an Alternative Future: Fundamental Flaws in the Structure of the Kyoto Protocol’s Clean Development Mechanism](#), UC Berkeley School of Public Policy, December 2009; New York Times, [A Carbon Trading System Draws Environmental Skeptics](#), 12 October 2010; Öko-Institut, [How additional is the Clean Development Mechanism](#), March 2016; Financial Times, [Carbon offset gold rush is distracting us from climate change](#), 22 November 2019; West et al., [Overstated carbon emission reductions from voluntary REDD+ projects in the Brazilian Amazon](#), PNAS, 29 September 2020; Bloomberg, [How to Sell ‘Carbon Neutral’ Fossil Fuel that Doesn’t Exist](#), 10 August 2021; Carbon Direct, [Assessing the State of the Voluntary Carbon Market in 2022](#), 6 May 2022; Guardian, [Revealed: more than 90% of rainforest carbon offsets by biggest certifier are worthless, analysis shows](#), 18 January 2023; [Airlines want you to buy carbon offsets. Experts say they’re a ‘scam’](#), Washington Post, 17 April 2023; A Chapman and D. Masie, [Are carbon offsets all they’re cracked up to be? We tracked one from Kenya to England to find out](#), vox.com, 3 August 2023; J. Gabbatiss, [Analysis: How some of the world’s largest companies rely on carbon offsets to ‘reach net-zero’](#), Carbon Brief, 27 September, 2023; H. Blake, [The Great Cash-For-Carbon Hustle](#), New Yorker, 16 October, 2023)

² See e.g. Carbon Market Watch, [Corporate Climate Responsibility Monitor 2023](#), p.67, February 2023



What important references and research papers should we take into account with regard to further work on decarbonization contribution?

- GFANZ argues that current approaches based upon measuring and bringing down the emissions from the companies in financial institutions' portfolios disincentivize financial institutions "from going to where the emissions are and providing financing to bring them down over time" (p.26). Given that this assertion is core to the rationale for the new approach proposed in this paper, it is surprising that no case studies or modeling is presented to show that current approaches are actually disincentivizing financial institutions from accelerating the transition.
- The most important place "where the emissions are" is the fossil fuel sector, yet there is no discussion in the paper that addresses this sector specifically. When it comes to the oil and gas sector, any argument that the major companies are either a) serious about transitioning or b) lack the resources to pay for the transition at a time of high oil prices is not publicly and scientifically backed. Repeated studies show the tiny proportion of their budget that oil and gas companies are putting into sustainable alternatives. The IEA reports that the oil and gas industry's capital spending on low-emission alternatives (including supposedly "clean fuels" and carbon capture technology) was less than 5% of their upstream spending in 2022.³

Any additional feedback regarding the Overview and Current State section?

³ IEA, [Clean energy investment is extending its lead over fossil fuels, boosted by energy security strengths](#), 25 May 2023



Part II: Decarbonization Contribution Methodologies

Potential Approaches for Aligned and Aligning Transition Finance Strategies

What are considerations for choosing a BAU pathway for Aligned/Aligning transition finance strategies and what is the minimum required level of granularity (i.e., sectoral, regional)?

- Sectoral way too broad
- Regional way too generic
- If any, it should be based on individual historic emissions and future outlooks, taking into consideration upcoming rules, regulations, and the rise of normative (net-zero) standards.
- For some currently highly carbon-intensive industries, such as cement, steel and aluminum, their products cannot easily be substituted and will continue to be needed in high volumes. In these cases, a better case can be made for the need for transition finance, but no case studies are presented to show that the EER concept would be an effective tool to speed up these transitions. Nor is any convincing evidence presented to show that approaches based on well-designed sectoral policies including engagement/stewardship measures with financial consequences for not meeting agreed benchmarks would dissuade the provision of transition finance to companies with robust transition plans.

Concerning the timing of EER claims (see to Figure 9), do you concur with the general principles and considerations proposed?

- Agree
- Somewhat agree
- Don't agree

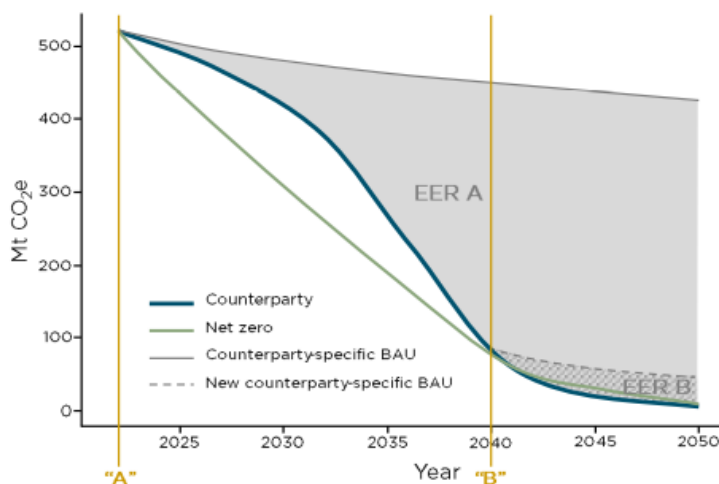
Are you supportive of Avoided Emissions reporting standards for corporates?

- Yes
- No

Any additional considerations/feedback for approaches for Aligned and Aligning transition finance strategies (e.g., regarding EER/ERP allocation to the portfolio; cumulative emissions vs. intensity-based methods etc.)?

- ECE (Expected Cumulative Emissions) only mentioned briefly, but unfortunately never picked up again: A useful concept introduced (yet unfortunately rather buried) in the paper is that of Expected Cumulative Emissions (ECE). ECE allows a financial institution to evaluate if the annual emission reductions targeted in an entity's transition plan are aligned with net zero, and it should be a required part of company and financial institution transition plans. ECE represents the cumulative total of expected remaining emissions of an entity or asset between the present and the time when it reaches net zero. As such it allows a financial institution to evaluate if the annual emission reductions targeted in an entity's transition plan are actually aligned with net zero, and to monitor its progress at aligning with net zero. It is a useful concept and ECE calculations should be a required part of company and financial institution transition plans.
- Figure 9: We do not concur with the principle of an FI being able to claim EER/EERB depending on the timing of the investment decision. If a company is able to decarbonise to the extent shown in the Figure without the transition money so desperately needed, the whole point of transition finance being urgent is weakened. We also do not agree with the proposition of FI's being able to account for EERs in general (see points made below).

Figure 9: Timing of financing decision impact on available EER



If the financing decision is made at point "A", the financial institution could report its share of EER based on the entire grey shaded area (EER A). If the financing decision is made at point "B", the available EER is reduced to the striped area (EER B). Note that in this illustration a counterparty-specific BAU emissions trajectory could have been derived from the counterparty's historical emissions performance.



Potential Approaches for Climate Solutions and Managed Phaseout Finance Strategies

Do you agree that avoided emissions approaches are well-suited to measuring the impact of Climate Solutions and Managed Phaseout?

- Agree
- Somewhat agree
- Don't agree

Rather than using LCA for determining emissions factors for the BAU and the low-carbon alternative, do you agree with the simpler approach of using end-use emissions for calculating avoided emissions?

- Agree
- Somewhat agree
- Don't agree

This consultation proposes that the full EER associated with Climate Solutions could be applied to related Enablers but disclosed separately from Solutions and Nature-based solutions. Do you support this approach?

- Support
- Somewhat support
- Don't support

Any additional considerations/feedback regarding impact methods for Climate Solutions, Enablers and Managed Phaseout (e.g., alternative approaches to avoided emissions; apportioning EER to Enablers, for example using a pro-rata approach)?

- The Science Based Targets initiative does not allow companies to count avoided emissions in meeting their targets.⁴ In 2021 Mark Carney, co-chair of GFANZ, was widely criticized for claiming that his infrastructure investment company Brookfield had reached net zero because of the avoided emissions of its renewables projects cancelled out the emissions from its gas infrastructure. Carney later rescinded this claim and stated that “I have always been – and will continue to be — a strong advocate for net zero science-based targets, and I also recognize that avoided emissions do not count towards them.”⁵

⁴ [SBTi Criteria and Recommendations Version 4.2](#), p.7, April 2021

⁵ Bloomberg, [Mark Carney walks back Brookfield Net-Zero Claim After Criticism](#), 25 February 2021

- The example of appointing EERs to lithium mining companies, since they are an “Enabler” for EVs is very alarming, since it would reward an unsustainable business model with great threats to natural ecosystems. It is true that electric vehicles have lower GHG emission levels as compared to fossil fuel powered vehicles. Yet, the EER awarding sends a signal that should not be sent to a technology/service that is not sustainable in itself. The battery industry should be seen as a sector with high needs for transition money to find alternatives for people and the planet.
- Obviously to be able to separate out coal phaseout emissions from other financed emissions, financial institutions would need to adopt policies halting finance for coal developers, and be able to show that the phaseouts they finance contain robust commitments that the phaseouts will happen on schedule, with social and environmental safeguards, and that lost power generation will be replaced with sustainable renewables and efficiency.

Allocation: Attribute the Expected Emission Reductions to the Financing Entity

Do you agree with leveraging the PCAF accounting method for EER allocation?

- Agree
- Somewhat agree
- Don't agree

Any additional considerations/feedback regarding impact attribution methods (e.g., alternatives to the PCAF accounting method; specific considerations for employing the proposed attribution method for EER; considerations about disclosure of EER; anticipated challenges when aggregating the EER at portfolio level)?



Other

Any additional feedback regarding Part II of this consultation?

- The proposed EER approach would encourage allocation of finance from low-carbon companies toward the highest polluters, while reducing any real incentives for these companies to make the rapid cuts in emissions needed for 1.5°C. And while GFANZ says the methodology would complement current approaches, in reality it would likely to be so favorable to financial institutions that there is a strong risk they would adopt it as their core “transition” metric.
- In particular, EER risks removing the still very inadequate, but growing, pressure from the finance sector for fossil fuel companies to move away from coal, oil and gas on 1.5°C aligned pathways. It would instead encourage approaches based on weak commitments to improve the emissions intensity of their operations. Fossil fuel companies are currently awash with cash and, as numerous studies have shown, are making at best a mostly performative effort to transition to clean energy.⁶ It is therefore not logical to claim that the key to pushing these companies to finally start to pull back on their production, transport and processing of oil, gas and coal — and their political promotion of high-carbon activities and anti-climate public policies — is to offer them even more capital.
- The paper is not clear over what timespan EER should be generated, but it presumably could be over the lifetime of a loan, or over the period between the financing decision and medium-term (say 2030) or long-term (say 2050) targets. The consultation paper is not clear on whether the projected EERs will be counterweighted at some point in the future when the distinction between reality and hypothesis could become clear. Nor does the paper highlight the need to adapt the BAU scenario as soon as lessons can be learned from the real-life outcomes of the fictional baseline projection. And even if such installations were made, the problem with this post facto correction is that it will only happen after the finance has been provided — potentially many years after depending on how often corrections are made — and the emissions have occurred. It is even implied that under the EER approach the consequence for a company that is failing to implement its transition plan would be for it to be rewarded with more financing to supposedly help get it back on track.⁷

CONTACT

Benja Faecks

Policy Expert

benja.faecks@carbonmarketwatch.org

⁶ See e.g. Reclaim Finance, [TotalEnergies, BP, Shell and ENI will blow up their carbon budget by up to 80%](#), 14 March 2022; Oil Change International, [Big Oil Reality Check: Updated Assessment of oil and gas company climate plans](#), May 2022

⁷ See text box on p.34 (“Use case for the EER metric to analyze an entity’s deviation from a net-zero pathway”)

