

# Science Based Targets initiative for Financial Institutions

## Draft Methods Feedback Summary

December 16, 2019

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## Project Background

In 2018 the Science Based Targets initiative (SBTi) launched SBTi-Finance, a project to help financial institutions (FIs) align with the ambition of the Paris Agreement. The project is focused on developing methods, criteria, and guidance for FIs to set science-based targets (SBTs). It applies to universal banks, pensions funds, insurance companies, and public financial institutions.

World Resources Institute (WRI) is the managing SBTi partner for this project and works closely with WWF and CDP through a project core team. Navigant and the 2° Investing Initiative provided technical support on method development and road testing.

During 2019, SBTi-Finance developed a set of draft methods which use an asset-class-based approach to link FIs investment and lending portfolios with climate stabilization pathways. The methods are described in the table below.

<i>Asset Class</i>	<i>Method</i>	<i>Description</i>
Real Estate	Sector Decarbonization Approach (SDA)	Emissions-based physical intensity targets are set for non-residential buildings' intensity and total GHG emissions.
Mortgages	SDA	Emissions-based physical intensity targets are set for residential buildings' intensity and total GHG emissions.
Electricity Generation Project Finance	SDA	Emissions-based physical intensity targets are set for electricity generation projects' intensity and total GHG emissions.
Corporate Instruments (equity, bonds, loans)	SDA	Emissions-based physical intensity targets are set at sector level within the portfolio for sector where sectoral decarbonization approaches are available.
	Paris Agreement Capital Transition Assessment (PACTA)	Sectors are assessed at individual business activity level for select activities.
	SBT Portfolio Coverage	FIs engage a minimum of 30% of their investees (in monetary or GHG emissions terms) to have their own SBTs.

From April to September 2019, SBTi-Finance conducted an inclusive, multi-stakeholder consultation process to gather feedback from FIs and other stakeholders (including consultancies, academia, and NGOs) on the methods' practicality and credibility. This process included road-testing of the draft methods by FIs, distribution of an online survey to broad stakeholders, and an in-person workshop held in New York City.

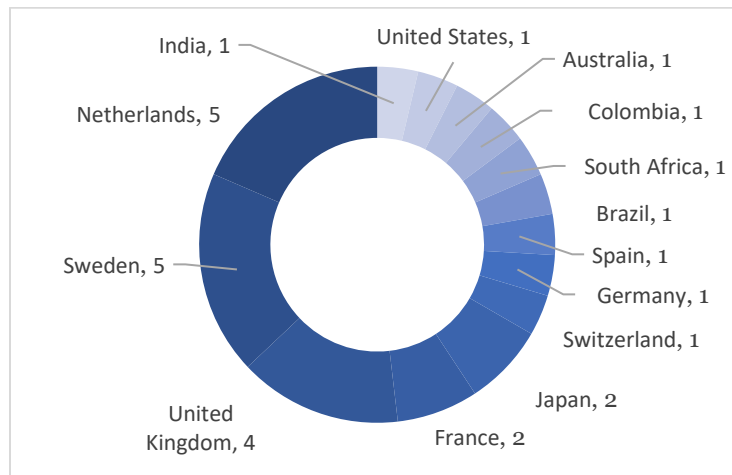
This document presents a summary of the feedback received from the consultation process. This feedback informs revisions to the methods and criteria. The final methods, criteria, and guidance are planned for launch in summer 2020.

## Road Tester Feedback

A total of 27 FIs from more than a dozen countries completed road testing of one or more of draft methods. Most road testers were commercial banks. The table below shows the distribution of FIs across methods and institution types.

<i>Institution Type</i>	<b>Method</b>					
	SDA Mortgage	SDA Real Estate	SDA Electricity generation finance	SDA Corporate Instruments	PACTA Corporate Instruments	Portfolio Coverage Corporate Instruments
<i>Asset Manager (6)</i>		2	1	1	2	1
<i>Commercial Bank (13)</i>	3	2	3	2	7	1
<i>Commercial Bank/Asset Manager (1)</i>		1				
<i>Cooperative Bank (1)</i>	1					
<i>Development Financial Institution (1)</i>			1			1
<i>Insurance Company (6)</i>	1	2		3	5	3
<i>Pension Fund (1)</i>	1				1	
<i>Total</i>	6	7	5	6	15	6

The figure below illustrates the locations of the road testers' headquarters in 14 countries.



## Methods Applicability or Coverage & Data Accessibility

Six financial institutions who applied to road test encountered method applicability and data accessibility issues that prevented them from completing the target-setting exercise. The SDA and PACTA methods were not applicable to some FI's portfolios because of their limited sector coverage. The tight timeline for road testing and limited internal capacity during summer were also cited by FIs as common reasons for not being able to complete the road test. Incomplete road testing responses are not included in this section.

### SDA for Real Estate

FIs can align their real estate portfolios with the Paris Agreement and set an emissions reduction target using the SDA.

*Potential target output:* Financial institution A commits to reduce its real estate portfolio GHG emissions \_\_\_% per m<sup>2</sup> by 2030 from a 2017 base year.

Eight responses were received for this method.

#### **Is the draft method practical to apply?**

Four road testers voted yes and four provided additional comments (without voting yes or no). In general, road testers found the method straightforward and that it provided a good, first indication of their portfolios' alignment with the Paris Agreement. The availability and quality of required input data were the biggest challenges for implementing the method. Due to reliance on proxy data, the results yielded by the method could be rough but could still be used as an initial indication.

#### **Is it useful for target setting and decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

Four road testers voted yes and four provided additional comments. Road testers found the method helpful because it could provide a good first indication of the portfolio's alignment with a global pathway. In one road tester's words, it provided "a very crude answer to a complex question." Incorporation of regional pathways (given different weather patterns) and more refined sector pathways (given varying emissions intensified by sectors) beyond residential versus commercial real estate (e.g. for shopping centers) would derive more meaningful SBTs and ensure higher buy-in from the organization. Alignment with a global pathway alone could generate equity issues for some regions.

#### **How many hours did it take you to apply the method?**

The average time spent by seven road testers was 30 hours. Time spent ranged from 5 to 75 hours.

#### **What challenges did you encounter while applying the method?**

In general, road testers found it challenging to retrieve energy consumption data for their global assets. It was also challenging to find complete datasets for activity data in square meters. In addition, there was a large variation in how "areas" were calculated in square meters for different property types. How

road testers calculated them internally did not always align with the guidance in the method. Several road testers also found it challenging to predict portfolio growth.

### **What data sources did you use for the method?**

Most road testers used a combination of internal data reported by portfolio companies or tenants and external databases, including the EU Building Database and the IEA's carbon emission factors. Some worked with external data service providers to compile the portfolio emissions inventory with custom built tools.

### **Do you think setting absolute emissions targets could be meaningful for this asset class?**

Five road testers voted yes and two voted no with further explanations. Road testers who found absolute targets valuable cited various reasons. One road tester responded that if the investor had control over these assets, the end target should be a zero emissions target in absolute terms. One road tester responded that intensity targets and absolute targets complement each other for tracking impacts of different activities in a portfolio. Road testers who said absolute targets are not suitable thought they could be difficult to implement on a global, diversified and growing portfolio. Those who said absolute targets are unrealistic thought that absolute emissions reductions are beyond their control.

### **In addition to the SBT for this asset class, would it be useful to have additional targets related to actions to achieve the SBTs?**

Four voted yes and three selected "other" with further comments. Most road testers saw value in additional actions to complement SBTs and cited examples such as engagement of tenants, fund managers and suppliers, renewable energy targets and energy efficiency targets.

### **What actions could be helpful to reduce your asset class level emissions?**

- A. Engage and support clients to improve buildings' emission data transparency (e.g. encourage energy or emission data disclosure, encourage clients to set a science-based target, etc.) - **2 votes**
- B. Engage and support clients to improve energy performance (e.g. provide financial instruments to support abatement measures, incentivize improvement through preferential assessment, etc.) - **4 votes**
- C. Divert new investment towards low-carbon buildings (e.g. set mandate for maximum carbon intensity for new investment) - **1 vote**
- D. Discontinue investment in buildings that are inconsistent with decarbonization pathway at the end of the investment maturity - **0 votes**
- E. Shift existing portfolio away from carbon-intensive buildings - **0 votes**

### **What target could you envision setting based on these target modeling results? Do you think these are targets that you can actually set and could be meaningful for your overall institutional strategy?**

While most road testers saw the potential to set targets based on the road testing results, they found that further analysis was needed to the initial top-down targets to yield more realistic and practical

targets to drive institutional strategies (e.g. targets by asset or departments, back testing of targets to gain internal buy-in). The initial targets could serve as foundations for discussions with asset managers and portfolio companies on cost and benefits of each strategies and options to drive emissions reductions.

Some road testers were reluctant to set actual targets based on these results due to limited quality of input data and lack of control over assets to reduce emissions.

**Can you suggest alternative methods for this asset class?**

Road testers found emission-based methods and the SDA useful, but suggested they could be complemented by additional targets/KPIs (e.g. energy performance certificates) and targets set using more granular pathways (regional and sectoral). Again, as compared to proxy data, use of FIs own portfolio data would derive more meaningful targets.



## SDA for Mortgage

An FI can align its mortgage portfolio with the Paris Agreement and set an emissions reduction target using the SDA.

*Potential target output:* Financial institution A commits to reduce its mortgage portfolio GHG emissions \_\_\_% per m<sup>2</sup> by 2030 from a 2017 base year.

Four responses were received for this method.

### **Is the draft method practical to apply?**

Two voted yes and two voted “other” with written responses. Similar to the real estate method, road testers found the method practical to apply, but estimating emissions of their mortgage portfolios was challenging due to reasons such as the fact that clients are not required to provide these data when signing the mortgages.

### **Is it useful for target setting and decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

Three voted yes and one voted other with written responses. Most road testers found the method useful for driving institutional alignment with Paris. One thought that it had the potential to serve this purpose in the future and was considering ways to improve their data collection system.

### **How many hours did it take you to apply the method?**

The average time spent by four road testers was 54 hours. Time spent ranged from 36 to 75 hours.

### **What challenges did you encounter while applying the method?**

Road testers cited the lack of access to energy performance, floor area data, and emission factors for energy labels as major challenges. Two road testers also found growth projections of their portfolios difficult to estimate.

### **What data sources did you use for the method?**

Road testers used a combination of internal and external data (the EU Building Database and national database) to come up with square meter and energy-related emissions for target setting.

### **Do you think setting absolute emissions targets could be meaningful for this asset class?**

Two voted yes and two voted no. Road testers had divided opinions on the value of absolute emissions targets for mortgages. Road testers who voted no cited that limited data granularity did not give meaningful emissions estimates, flux in portfolio could lead to misleading impressions that emissions were reduced when they were not, and absolute targets could constrain portfolio growth. Road testers who voted yes did not provide additional clarifications.



**In addition to the SBT for this asset class, would it be useful to have additional targets related to actions to achieve the SBTs?**

Three voted yes and one voted no, indicating that most road testers found it valuable to set additional action targets. No additional clarifications were provided.

**What actions could be helpful to reduce your asset-class-level emissions?**

- A. Engage and support clients to improve buildings' emission data transparency (e.g. encourage energy or emission data disclosure, encourage clients to set a science-based target, etc.) - **2 votes**
- B. Engage and support clients to improve energy performance (e.g. provide financial instruments to support abatement measures, incentivize improvement through preferential assessment, etc.) - **3 votes**
- C. Divert new investment towards low-carbon buildings (e.g. set mandate for maximum carbon intensity for new investment) - **1 vote**
- D. Discontinue investment in buildings that are inconsistent with decarbonization pathway at the end of the investment maturity - **0 votes**
- E. Shift existing portfolio away from carbon-intensive buildings - **0 votes**

**What target could you envision setting based on these target modeling results? Do you think these are targets that you can actually set and could be meaningful for your overall institutional strategy?**

Road testers had mixed view on this question. Two road testers thought that property-specific data was needed to derive more meaningful targets to inform organizational strategies, or that preliminary targets based on proxy data needed to be analyzed further. In addition, internal alignment was needed to set targets. Though not entirely ready to set targets, one road tester found it a useful exercise to go through for understanding the input data required for future target setting and for raising awareness internally.

Can you suggest alternative methods for this asset class? One commercial bank commented that for this method to work well, it would be useful to have guidance on where banks could and should influence and support with financial products and services, as compared to areas such as grid decarbonization, where governmental actions were needed more.





## SDA for Electricity Generation Project Finance

An FI can align its electricity generation project finance portfolio with the Paris Agreement and set an emissions reduction target using the SDA.

*Potential target output:* Financial institution A commits to reduce its electricity generation project finance portfolio GHG emissions \_\_\_% per kWh by 2030 from a 2017 base-year.

Five responses were received for this method.

### **Is the draft method practical to apply?**

Four voted yes and one voted “other.” In general road testers found this method useful for target setting. It helped them see the gap between their current efforts and the Paris Agreement. The method was also readily understandable by stakeholders. However, data availability and the use of proxy data still presented challenges for setting targets and deriving meaningful targets.

### **Is it useful for target setting and decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

Three voted yes and two voted “other.” In general, road testers found the method useful as it helped reveal the gap between their current portfolio emissions intensity the Paris Agreement. Some challenges cited include the lack of plant-specific data to derive meaningful targets and not being applicable to portfolios with dominantly renewable energy projects.

### **How many hours did it take you to apply the method?**

The average time spent by four road testers was 41.5 hours. Time spent ranged from 6 to 100 hours.

### **What challenges did you encounter while applying the method?**

The most common challenges were related to data, including misalignment of emissions factors and gaps in internal data collected to carry out the exercise. One bank discussed the difficulty of predicting portfolio growth.

### **What data sources did you use for the method?**

In general, road testers prioritized the use of internal energy portfolio data and data reported by portfolio companies. When these were not available, they used data from data providers and external databases.

### **Do you think setting absolute emissions targets could be meaningful for this asset class?**

Three voted yes and one voted no. Road testers voting yes cited reasons such as allowing direct comparability with other sectors or other asset classes (e.g. corporate loans). One reason given by a road tester as to why absolute targets were not useful was that they did not represent change in business and efficiency improvements or allow comparison among peers.



**In addition to the SBT for this asset class, would it be useful to have additional targets related to actions to achieve the SBTs?**

Three voted yes and one voted “other.” In general, road testers found action targets valuable for this asset class and cited reasons such as incentivizing investment in infrastructures that unlock more potential for renewable energy.

**What actions could be helpful to reduce your asset class level emissions?**

- A. Engage and support clients in pre-project phase (e.g. encourage adoption of low-carbon technologies in due diligence phase) - **2 votes**
- B. Engage and support clients to improve projects’ emission data transparency (e.g. encourage energy or emission data disclosure, encourage clients to set a science-based target, etc.) - **1 vote**
- C. Engage and support clients to improve performance (e.g. provide financial instruments to support abatement measures, incentivize improvement through preferential assessment, etc.) - **0 votes**
- D. Divert new investment towards low-carbon projects (e.g. set mandate for maximum carbon intensity for new investment) - **2 votes**
- E. Shift existing portfolio away from carbon-intensive projects - **1 vote**

**What target could you envision setting based on these target modeling results? Do you think these are targets that you can actually set and could be meaningful for your overall institutional strategy?**

Road testers had mixed answers for this question. One road tester found the modelling exercise valuable for them to set a target for a carbon neutral portfolio by 2030, and one road tester found that they were already on track to align with a below-2°C scenario. Others discussed how this method was not most applicable to a portfolio with dominantly renewable energy or proposed alternative approaches.

**Can you suggest alternative methods for this asset class?**

One development finance institution suggested using absolute emission baseline instead of expected power production, as it allowed easier comparison of electricity generation project finance with other asset classes (e.g. corporate loans). One bank suggested looking at intensity targets based on INR Crore revenue- tCO<sub>2</sub>e/INR Cr (as recommended by Task Force on Climate-related Financial Disclosures).



## SDA for Corporate Instruments

Physical emission intensity target (e.g. kgCO<sub>2</sub>e/tonne production) could be set at the portfolio level for sectors covered by the SDA: Power generation, Cement, Iron & Steel, Aluminum, Pulp & Paper, Transport, and Buildings.

*Potential target output:* Financial institution A commits to reduce GHG emissions from the steel sector within its corporate lending portfolio XX% per tonne of steel by 2030 from a 2017 base-year.

Six responses were received for this method.

### **Is the draft method practical to apply?**

Road testers found the method to have data challenges (activity and enterprise value data difficult to obtain, time lags in reported data) and require manual company-sector linkages that are time-intensive. A proposed solution was to provide additional default data (e.g., emissions factors) for initial screening purposes. One insurance company commented that the SDA implicitly requires investors to hold and engage with their investees to achieve their targets, which would be a positive way to drive emissions reductions in the real economy.

### **Is it useful for decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

Road testers found the method more useful for macro-assessment than decision making and target implementation due to data gaps at the company level. Data gaps are especially challenging for non-listed companies. One road testing bank found the method difficult to apply due to confusion around metrics, impact attribution and calculation rules, potentially leading to inconsistent results.

### **How many hours did it take you to apply the method?**

The average time spent by six road testers was 35 hours, with a range from 8 to 48 hours. The SDA for Corporate Instruments was on average more time-intensive than the PACTA or SBT Portfolio Coverage approaches.

### **What challenges did you encounter while applying the method?**

Road testers reported that the primary challenges for applying this method were data availability, unclear sector links, limited sector coverage, lack of attribution guidance, and insufficient company data disclosure. In the absence of SBTi guidance, there was also some confusion about the tradeoffs between ownership and portfolio weight allocation approaches. One suggestion was to make SDA sector taxonomies more consistent with standardized sector taxonomies.

### **What data sources did you use for the method?**

Road testers used a range of public, subscription and private data sources. Road testers identified lack of standardization as a challenge that could undermine the consistency of inventories and outputs. The most challenging data areas are related to non-listed companies and future business activity. One road tester indicated that “there’s no perfect data source except CDP.”

**Which of the two allocation approaches ("Portfolio weight approach" and "Balance sheet approach") did you use and why did you choose it over the other approach?**

Most road testers preferred the portfolio weight approach for SDA/corporate instruments as a basis for informed decision making. However, a couple of road testers indicated the balance sheet approach is better for emissions budget allocation and target setting. Road testers recommended that the SBTi advise on enterprise value versus market capitalization apportionment approaches within balance sheets. The SDA method doesn't provide guidance on allocation approaches, but road testers indicated that it should to maintain consistency and avoid creating loopholes for low-ambition targets.

**Which sectors are most usefully covered by the SDA method?**

Road testers reported that the electricity and building sectors were most usefully covered by this method. One road tester requested coverage of passenger and freight transport, but another road tester mentioned that companies often don't fully disclose transport information. Road testers indicated that the boundaries of analysis (i.e., allocation of tenant energy use to building owners) and user perspectives (e.g., real estate manager versus "asset itself" for buildings) could use more clarification and standardization. Regarding the sector basis of the SDA, one road tester indicated that differences between individual companies' intensities and sector average varied by a factor of at least ten. One road tester highlighted the need for harmonized metrics between financial/activity reports and GHG analysis.

**Could setting sectoral absolute emissions targets be meaningful for this asset class? For example, absolute emission reduction can be derived from the global or regional decarbonization pathway for sectors available in SDA. Companies' activity growth projection is assumed to be at the same level as the sectoral activity projection in the underlying scenarios.**

While several road testers indicated that absolute targets would be meaningful at the investee level for company target setting, several road testers indicated that absolute targets would not be meaningful for portfolio-level corporate instruments since they would incentivize divestment rather than investment in efficiency improvements and other mitigation activities. Feedback indicated that absolute targets would be more meaningful if linked with intensity targets.

**Would it be meaningful to set absolute emissions reduction targets to sectors that are not covered by SDA? With this method, absolute emissions are reduced by the same percentage to keep global temperature increase within well-below 2°C (min. 2.5% annual linear reduction) or a 1.5°C trajectory (min. 4.2 % annual linear reduction).**

Road testers agreed that absolute emissions reduction targets would be meaningful for investees beyond SDA subsectors. However, road testers had mixed opinions on the utility of absolute contraction targets for corporate instrument portfolios beyond SDA sectors. On the one hand, such targets could be meaningful for investees, though perhaps less informative than SDA-based targets, and on the other hand they would not be meaningful for investor portfolio target setting.

**In addition to the SBT for this asset class, would it be useful to have additional targets related to actions to achieve the SBTs?**

Road testers all agreed that action targets would be a useful addition for corporate instrument SBTs. Suggested actions include development and operationalization of related financial products (e.g., lower interest rates for companies that achieve their SBTs), engagement with top emitters, and SBT portfolio

coverage. This feedback links with the potential development of criteria on FIs' disclosure of target implementation strategies.

**What target could you envision setting based on these target modeling results? Do you think these are targets that you can actually set and could be meaningful for your overall institutional strategy?**

Road testers indicated that the method's data and boundary issues prevent meaningful targets to guide institutional strategy, with the exception of power sector targets. One road tester wrote that SDA-derived 2050 portfolio intensity targets were higher than current intensity levels—a broader problem for this method linked to its reliance on global average values. Independently of target setting, road testers indicated that the method can be useful for monitoring investee company emissions intensity.

**Can you suggest alternative methods for this asset class?**

Road testers indicated that the method should be integrated with net-zero approaches and alternative methods including PACTA and SBT portfolio coverage.

**Please add any additional comments here:**

Road testers indicated that the SDA is more in line with carbon budget logic than PACTA, but that the method is more useful for individual company-level target setting than FI-level target setting.

Recommendations included:

- Guidance on the use of allocation methods for the calculation of portfolio intensity
- Analysis guidelines for the perimeter to be used for the calculation of production and emissions data
- Guidelines on extrapolation to calculate future production values (2030) and base year IEA scenarios values.
- Guidelines for the integration of SDA, SBT coverage and PACTA outputs at the portfolio/institution level
- Provide market benchmarks (not only scenarios): portfolios/indices/funds for SDA covered sectors so that FIs can benchmark their current and targeted intensities with other portfolios
- Metrics, data sources and choice options could be more clearly defined:
  - What is a source of sectoral data (IEA B2DS scenario (ETP 2017))?
  - More indications could be provided on how to allocate/weigh emissions across portfolio/investees.
  - Balance sheet and capital market concepts are mixed up: enterprise value as well as market capitalization (capital market) have limited relation to a balance sheet, while book value and assets (balance sheet) have limited utility to be used for market priced instruments to calculate investors' prorate in a firm's financing. It could be considered to distinguish different approaches for different assets: listed securities of listed corporates, unlisted loans of listed companies, assets of unlisted firms as well as face and market values of equities and bonds.

- To consider more real economy and impact-linked metrics instead of capital market metrics (enterprise value and market capitalization):
  - Enterprise value and market capitalization (EV and mCap) are too sensitive to stock and debt price volatility. The use of such metrics is not supportive of climate performance ambition for some companies since they artificially win better climate performance at a portfolio level, thanks to bigger and growing mCap and not due to GHG reductions (capital market biases have a limited link to real economy and induced impact)
  - Another issue is a discrimination of undervalued stocks and unlisted companies that could have more ambitious real climate performance and progress while having limited success at capital markets (mCap and EV); at portfolio level this is unrecognizable if capital market-linked metrics are used
  - These biases are more important when it comes to long-term projections. They could nullify all SBT setting efforts at an asset class/portfolio level and mislead asset allocation decisions, favoring not climate actions but bigger mCap and EV.
  - Probably "real economy" metrics—book value, assets/liabilities, own capital, face value of debt—should be prioritized by both listed and unlisted issuers, since it will better link carbon impact, economic activity, financial instruments and associated performance, and risks and opportunities at a portfolio level. In this case the methods should assure the use of face/nominal value of investments (not market ones) to properly estimate investors prorate

## PACTA for Corporate Instruments

Whereas SDA is based on physical emissions intensity approaches, PACTA is focused on production capacity and technology type data (vehicles manufactured per year, GW electricity, etc.).

*Potential target output:* Financial institution A commits to increase installed capacity in renewable electricity by XX MW by [year] across the [asset class] portfolio companies that we are specifically targeting in the context of our climate actions.

Fifteen responses were received for this category.

### **Is the draft method practical to apply?**

Most road testers found the method practical to apply. Among the FIs that did not find it to be practical, reservations were expressed about its opacity, pdf output, sector mapping inconsistencies, insufficient technology granularity, and target-setting discrepancies. One road tester requested additional information on how this approach would apply to credit portfolios as opposed to equity and corporate bond portfolios.

### **Is it useful for decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

Most road testers found the PACTA-related spreadsheet at least partially useful for driving Paris alignment, especially with regard to bond and equity portfolio granularity, CapEx and production plans. Limited portfolio coverage and lack of raw output data were cited as challenges.

### **How many hours did it take you to apply the method?**

The average time spent by fifteen road testers was 11 hours, excluding one outlier that spent more than 4,000 hours. Generally, road testers found that using the method was easy and intuitive.

### **What challenges did you encounter while applying the method?**

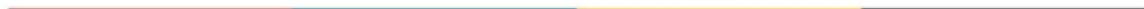
Challenges related to this method include limited portfolio coverage, lack of data transparency (outputs and assumptions) and difficulty translating results into actionable information.

### **What data sources did you use for the method?**

Most road testers used their own portfolio data, with some supplementing external sources such as MSCI, company reports or consultancies.

### **Which of the two allocation approaches ("Portfolio weight approach" and "Balance sheet approach") did you use and why did you choose it over the other approach?**

Most road testers used the portfolio weight approach; one road tester used the balance sheet approach because data were available from the bank in that format. A couple road testers that used both approaches remarked on the inconsistency of results across approaches and reported a need for additional guidance on allocation approaches.



**Which sectors are most usefully covered by the PACTA method?**

Road testers identified power, coal and oil and gas as the most useful sectors.

**In addition to the SBT for this asset class, would it be useful to have additional targets related to actions to achieve the SBTs?**

Almost all the road testers responded yes to this question. However, it is not clear how action targets would be expressed, assessed or tracked.

**How could PACTA-based targets be expressed and tracked?**

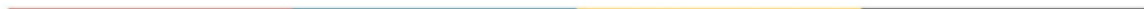
Road testers did not have consistent answers on how PACTA-based targets could be expressed and tracked. There is evidently a need for more information on how FIs could use PACTA for target expression and tracking.

**What target could you envision setting based on these target modeling results? Do you think these are targets that you can actually set and could be meaningful for your overall institutional strategy?**

Road testers provided mixed answers to this question, with four not answering or not finding the PACTA results sufficient to set a target. Among the remaining responses, most were oriented around energy capacity, e.g., “Companies in portfolio X should reduce total gas capacity to 410 MW in 2023 compared to 2018.” A few respondents requested additional data related to PACTA.

**Can you suggest alternative methods for this asset class?**

Respondents suggested absolute emissions reduction targets and the portfolio coverage approach as potential alternatives to PACTA.





## SBT Portfolio Coverage for Corporate Instruments

In this method FIs have a minimum percentage of their investees (in monetary or GHG emissions terms) set their own SBTs. The method is a financial sector analogue to supplier engagement targets for 'real economy' companies' scope 3 emissions.

*Potential SBT Portfolio Coverage target output:* Investment firm A commits that 30% of its equity portfolio by market capitalization will have SBTs by 2025.

Six responses were received for this method.

### **Is the draft method practical to apply?**

Most road testers indicated that the method is practical to apply, with suggestions to focus on sectors with SBT/SDA method coverage, develop alternate engagement target types (e.g., related to economic intensity), provide ISIN numbers for SBT companies, and clarify attribution among FIs and investees.

### **What data sources did you use for the method?**

Road testers used a range of data sources including the SBTi website, CDP database (question C4.1a), TruCost, FactSet and FIs' own primary data. The CDP self-reported data are a potential source of broader science-based alignment beyond the leading companies that have targets officially approved by SBTi.

### **Is it useful for decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway?**

With the exception of one development FI, road testers indicated that the SBT portfolio coverage method is useful for driving institutional Paris alignment. Road testers indicated that FIs' engagement is a key component of achieving real economy emissions reductions, though there's a need to specify portfolio coverage and other details.

### **How many hours did it take you to apply the method?**

The average time spent by six road testers was 8 hours, with responses ranging from 2 to 20 hours.

### **Is an emissions-based metric practical to apply?**

Road testers were divided on the practicality of an emissions-based metric for portfolio coverage, with notes on data limitations, accounting challenges related to intermediate financing and uncertain portfolio coverage. Several road testers felt that an emissions-based metric would be practical to apply with SBTi-related emissions data and additional emissions-reductions estimates.

### **Which economic metric should be used (asset under management, market capitalization, etc.)?**

AUM was the preferred metric among 4 of the road testers, with one suggesting value amount on the balance sheet as an alternative.

### **Please describe the target output from applying this method.**



Road testers indicated a preference for AUM-based targets for equity and bond portfolios, with one referencing CDP Question C4.1a as a potential data source for a broader pool of self-identified science-based goal adopting companies.

**What percentage of your portfolio are SBT companies?**

Road testers reported current SBT coverage ranging from 0.5% to 26% of AUM. One road tester noted that coverage levels can vary significantly depending on whether the metric is AUM, company valuations or company-reported GHG emissions.

**What SBT portfolio coverage threshold (30% is the currently proposed threshold) is most appropriate? Should we propose to focus on engagement of the top emitters?**

Road testers generally accepted the 30% AUM threshold as an appropriate starting point, noting that ambition will vary geographically, across sectors (including concentration levels), and between small and large cap portfolios. There was a fairly even split on whether coverage should be required of top emitters. Similarly, one road tester suggested that coverage requirements be linked to sectors with available SBTi sector methods (i.e., not including oil and gas as of 2019).

**Which equity and debt asset classes could be practically applied by this method?**

Road testers consistently indicated that listed equity would be appropriately and meaningfully covered. One road tester indicated the portfolio coverage method would also be applicable for fixed income.

**Should this method keep the maximum 5-year timeframe requirement?**

All road testers except one agreed that SBTi should keep a maximum 5-year timeframe requirement; the exception suggested that 5 years would be too short for their geographical and sector focus areas.

**What challenges did you encounter while applying the method?**

Top challenges identified by road testers included ambiguous wording, limited sector and company coverage of existing SBTs, data formatting (across FactSet/Trucost/CDP), data availability and attribution of investee mitigation actions to investors.

**Can you suggest alternative methods for this asset class?**

Suggested alternatives included SDA, other engagement targets such as “active discussion with most-emitting clients” and sector-specific approaches.

**Please add any additional comments here:**

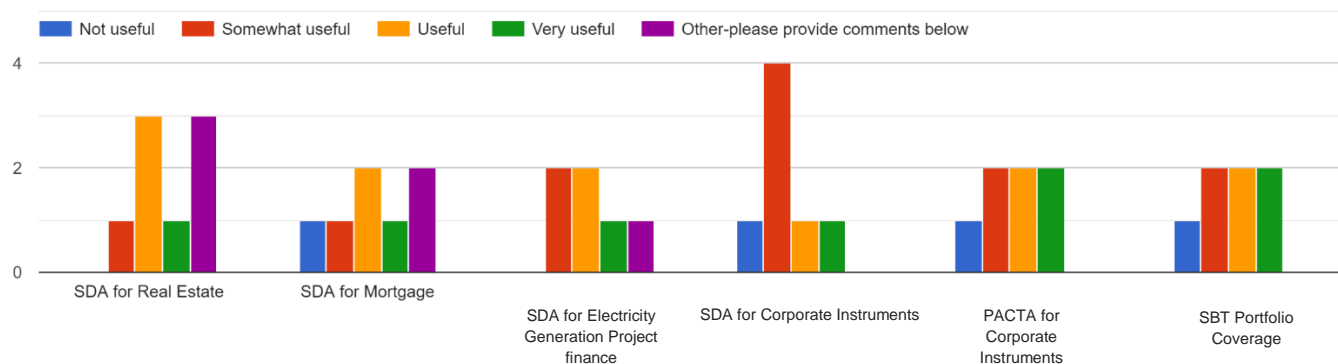
Road testers submitted extensive additional comments that covered data disclosure requirements, engagement methods, coverage requirements, increases to 2050 and the role of divestment, among other topics.



## Stakeholder Advisory Group Survey Responses

**Nine** stakeholders from financial institutions (who did not participate in the road test), nonprofit organizations, and consultancies submitted responses to an online survey.

**How useful are the following methods for target setting and decision making to drive institutional alignment with a Paris-aligned climate stabilization pathway? 8 responses total**



### Summary of additional comments to this question:

#### SDA for Real Estate

- Pathway is limited to residential and service (but logistics and industrial buildings present a significant part of investors' total assets)
- The method mentions that FIs should take regional pathways into consideration. Further clarification is needed on what this means

#### SDA for Mortgage

- Direct data disclosure is challenging for mortgage portfolios, which means the reliance on average data creates difficulty for target setting and monitoring

#### SDA for Electricity Generation Project Finance

- It would be useful to incorporate the tenor of the project finance instruments that are in a portfolio alongside the projected portfolio growth rate

#### SDA for Listed/Private Equity and Corporate Bonds and Loans

- Unintended consequences of a global pathway need to be considered: it will encourage finance flows into developed countries, instead of developing ones; suggestion to consider ETP regional pathways
- Need a hierarchy of recommended methods, as SDA/PACTA sector coverage is limited

#### PACTA for Listed/Private Equity and Corporate Bonds and Loans

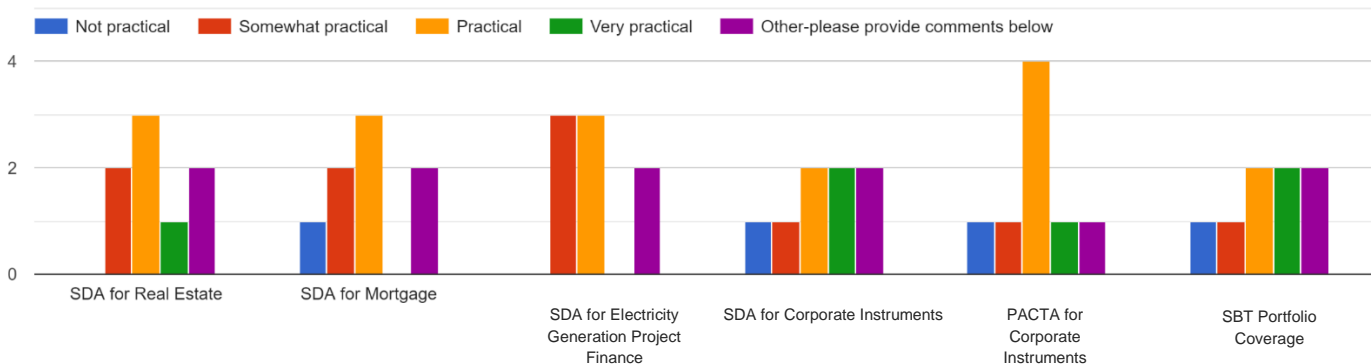
- Limitations of sector coverage and SME coverage

- Limited transparency of obtained results at corporate level
- User-friendly and good decision-making tool
- Difficult to grasp useful next steps only from visual content; more quantified and descriptive data needed
- Outputs are in absolute units instead of intensity unit, so it's difficult to integrate into the SBT setting work

#### SBT Portfolio Coverage for Listed/Private Equity and Corporate Bonds and Loans

- Interesting to see if this approach could be extended to relationships between FIs (though there is very little information on how financial companies can interpret their relationships with each other)
- General suggestions for SDA and PACTA: use two other methods for sectors or geographies that are not covered by SDA and PACTA

#### How practical is it for FIs to use the outputs from the following methods to set targets and drive institutional alignment with Paris-aligned climate stabilization pathway? 8 responses total



**In addition to the SBTs for these asset classes, how could actions be integrated? For example, for the real estate and mortgage asset classes, FIs could be required to install renewable energy equipment for building-scale use or make investment towards low-carbon buildings (e.g. set a mandate for maximum carbon intensity for new investment).**

- Eight stakeholders expressed support for integration of actions and provided different example actions that can be considered, including energy savings check and discount rate based on energy performance for mortgaged homes, targets for investment in energy efficiency and green buildings, and rules in investment policies to avoid the acquisition of high-carbon emitting assets for real estate.
- One stakeholder commented that at a minimum, FIs must commit to end financing for new fossil fuel projects to be in line with the Paris Agreement. Another stakeholder mentioned they are developing criteria for acceptable actions for a managed decline of fossil fuel extraction in line with the science of the IPCC 1.5°C report, which can be used by investors using a "voice" strategy and "exit" strategy.

- Two stakeholders mentioned the need for other indices (e.g. indicators for when certain investments become incompatible with the SBTi).

**Can you suggest alternative methods or target-setting approaches that enable alignment with the Paris Agreement? Please specify the relevant asset classes.**

Along with suggesting multiple alternative methods, stakeholders provided comments on current scope of methods:

- Need to focus on not only the emitted carbon by also *extracted* carbon on the supply side of the fossil fuel market
- Can apply the SDA transport methods to vehicle loans in a similar manner as SDA for mortgage
- For corporate instruments and electricity generation project finance in particular, calculating attribution using outstanding exposure (versus, for instance, initial capital allocated or other financial advice/services provided) ignores the other ways in which emissions are attributed to FIs, and around which SBTs must be set.



# Summary of Comments from Road Testing Feedback Workshop

On September 25th, 2019, SBTi-Finance hosted an in-person road testing feedback New York City to gather detailed additional feedback from road testers on draft science-based target-setting methods and collect inputs on options to address key technical issues. After a summary of feedback from road testers was presented, workshop participants were divided into four discussion groups. This section presents the summary of participants' feedback to the discussion questions provided:

## **Portfolio SBTs require substantial data inputs, and access to such data can be an issue. What resources could SBTi develop to address current financial institution data challenges?**

There was consensus among workshop participants that existing data is very fragmented and there is high variation in existing emissions factors. While they can get support from consultancies or other paid databases, a centralized, jointly founded, client- and sector-based data repository would be very helpful. Users should be able to upload data for sharing with others.

As FIs often share the same high-emitting clients it would be beneficial to have a combined balance sheet that ensures consistency in reporting requirements from various actors to reduce reporting fatigue.

## **In the SBTi framework, FIs may be required to set an emissions or capacity-based target. In addition to quantitative SBTs, should FIs also be required to disclose the implementation strategy (e.g. investment, divestment, engagement) to achieve these targets?**

Workshop participants have different views on this question. Some think that as FIs will be asked about their implementation anyway, it is not necessary for the SBTi to play that role and add to the reporting fatigue FIs are experiencing. If SBTi really wants to have a requirement, it needs to be very simple.

Some find disclosure of implementation strategies or theory of change with the SBTi crucial for FIs' targets to be credible, especially for FIs' portfolio targets. But the strategies should stay at macro level without getting into granular details.

## **Which types of target-setting methods (emissions-based, capacity-based, portfolio coverage, other) are most actionable for FIs?**

Stakeholders provided comments on each type of target. Participants think that absolute emissions reduction targets should be aimed for if the end goal is emissions reduction in the real economy, but it can be very difficult for banks. Intensity targets are more actionable and can be a middle ground, but they can also be criticized. PACTA capacity targets are helpful on the portfolio level and can be valuable for engagement, but lack transparency and do not let you dig deeper. The portfolio coverage approach is easier to implement and can complement sectors where the SDA and PACTA are not feasible. However, how the target should be formatted (e.g. with a minimum threshold or formatted as a % coverage increase) and the metric (e.g. economic or emissions-based) should be refined.

## **Are emissions-based (e.g., SDA), capacity-based (e.g., PACTA) and portfolio coverage-based targets meaningful to drive emissions reductions in the real economy?**

Workshop participants had varying levels of familiarity with the draft methods but identified several situations where these targets could meaningfully drive real emissions reductions.

**What proportion of an FI's balance sheet must be covered to achieve a credible portfolio target? If these methods cannot achieve this level, what alternative methods exist?**

This question was not discussed during the workshop but will be covered in the SBTi-Finance criteria.

**For asset class level emissions accounting, which of the two allocation approaches ("Portfolio weight approach" and "Balance sheet approach") did you use and why did you choose it over the other approach?**

This question was not discussed during the workshop but will be covered in the SBTi-Finance criteria.

