

UK GLOBAL LEADERSHIP ON NET ZERO FINANCE THE NEED FOR MANDATORY TRANSITION PLANS



E3G



Make My Money Matter



Summary

The time for net zero¹ finance is now.

We have less than ten years to halve global carbon emissions if we are to limit global temperature rise to 1.5°C, the target set out in the Paris Agreement on climate change. To meet this challenge, we must harness the power of the global financial system.

The UK has a unique opportunity to be a global leader on net zero finance, an essential industry for future prosperity. In realising this vision, the UK can build back better, making the UK finance sector, and the broader economy, stronger and more resilient as a result. The City of London should be at the forefront of that mission.

The Government has already laid solid foundations by announcing mandatory climate-related financial reporting (TCFD) for all large firms and getting G7 support for rolling out this requirement internationally – demonstrating the value of UK leadership in securing international

ambition. However, disclosing climate risk alone is not enough, and companies must take action now. The Government has already required net zero transition plans from companies bidding for government procurement contracts. The next step is to make the disclosure of net zero transition plans mandatory across the economy, including it as a part of TCFD requirements.² This should be supported by guidance to ensure firms set and implement net zero transition plans with integrity, aligned with the UK's climate commitments.

By taking this step, the Government can seize the opportunity for global leadership on green finance by COP26, helping create a resilient, sustainable, and prosperous UK financial sector, open for business to the growing global potential of green investment.

Who We Are

We are a group of Business and Civil Society Groups campaigning for the UK to build a world-leading net zero finance system.

Contact: heather.mckay@e3g.org

¹ Net zero emissions must be achieved through a trajectory that aligns with the Paris Agreement, e.g., limiting to 1.5°C warming.

² The TCFD is recommending the disclosure of transition plans as part of the recent consultation period.

What You Can Do

- > Write to the PM and the Chancellor expressing your support for an announcement by COP26 of the introduction of mandatory net zero transition plans, for aligning with 1.5°C, as part of required TCFD disclosures. This should be backed by clear guidance from regulators on formulating transition plans, to prevent greenwash.
- > Contact us for further information, and support on briefings, roundtables, or events.
- > Share this briefing.

Key Facts

- > The 2021 Global Investor Statement to Governments saw firms worth over \$41 Trillion call on G7 governments to implement mandatory TCFD.³
- > Firms responsible for over **\$70 Trillion** in assets are now committed to the Glasgow Financial Alliance for Net Zero.
- > A recent letter from leading UK financial institutions, responsible for over \$5 trillion in assets, called on the Prime Minister to develop a world-leading net zero financial system.
- > **76% of financial services firms** see opportunities in offering sustainable finance products and services, with a potential financial impact of up to US\$2.9 trillion.
- > Analysis of 25 large UK Banks and Asset Managers shows they are responsible for

about 1.8x the UK's domestic emissions – equivalent to the 9th largest emitting country globally.⁴

- > The full portfolio emissions of financial firms are estimated to be over 700 times greater than their direct emissions.⁵
- > One estimate of the FTSE 100's carbon footprint suggested that their total carbon footprint could be up to **15 times** the domestic carbon footprint of the UK.
- > SBTi's G7 Stock indexes analysis showed that the FTSE100 was aligned with 3.1 Degrees of warming, equal last place in a ranking of the G7 countries.⁶
- > Costs of continuing "business as usual" emissions will reach USD **\$5.4 trillion** a year by 2070.
- > Every \$1m in short run spending generates **2.8x** more full-time jobs in renewables infrastructure than fossil fuels.
- > Net Zero aligned investment, with no new investments in fossil fuels, would lower energy costs for the lowest income households and support the transition.



³ Over 450 investors managing \$41 trillion in assets tell governments to get climate policy right and massive investment will flow, IIGCC (2021)

⁴ This figure is an indicative measure, with the true impact of UK FIs estimated to be far greater.

⁵ Finance sector's funded emissions over 700 times greater than its own, CDP (2021)

⁶ No major G7 stock index aligned with Paris climate goals, UN Global Compact (2021)

Recent Policy Developments on Transition Plans

November 2020

The UK is making reporting **TCFD climate disclosures mandatory**, and leveraged its leadership on TCFD to result in the recent G7 Communique supporting moving towards mandatory TCFD disclosures.¹

November 2020

The Chancellor has called for large financial firms and companies to disclose transition plans for net zero, echoing comments by Mark Carney, the former Governor of the Bank of England and PM's advisor for COP26 and Finance.

June 2021

The Government now requires net zero commitments and transition plans from companies bidding for government procurement contracts.

June - July 2021

The TCFD carried out a consultation on the inclusion of transition plans as part of TCFD guidance.

July 2021

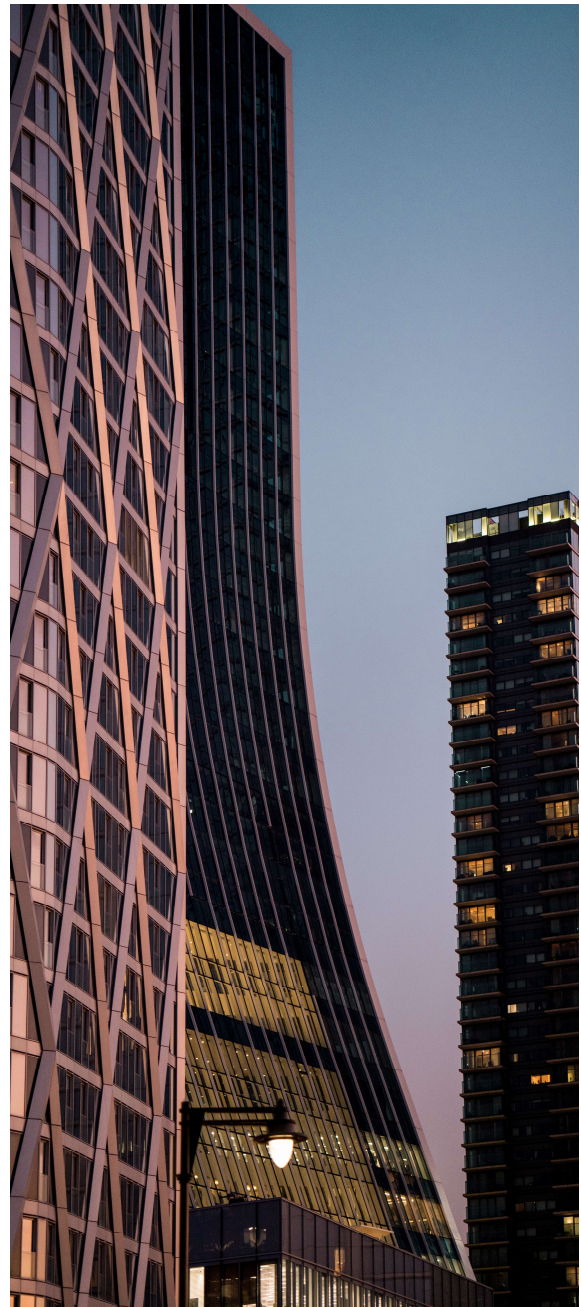
Competition to shape this space is growing, with the **EU Sustainable Finance Strategy** calling for financial institutions to disclose sustainability transition and decarbonisation plans, including intermediate and long-term targets and plans to reduce their environmental footprint.

July 2021

The Government's new report '**A new chapter for financial services**' stated that HMG will work closely with the regulators to encourage and support firms to publish transition plans, with further details provided before the end of 2021.

Opportunities of a Net Zero Finance Sector

- > Cementing the UK's position as a global hub of green finance. This will mean the UK can continue to attract business and investment to a robust, well-regulated, and sustainable UK finance market.
- > Increasing the economic resilience of the UK, as well as supporting the country in building back better through funding environmental and social resilience.
- > Realising the considerable financial, economic, and social co-benefits of a swift strategic UK shift in capital towards net zero aligned investments, including:
 - > Supporting sustainable industries
 - Lower energy costs for households
 - Funding future-fit infrastructure
 - The creation of good quality green jobs
 - Reducing the risk of sinking public and private capital into stranded assets.
 - Environmental co-benefits from sustainable supply chains
 - Natural Capital and Biodiversity protection and restoration



Background

This year the UK will host the COP26 climate summit. Following its postponement last year due to the COVID-19 pandemic, the summit is widely recognised as a critical moment to get the world on track to meet the goals of the Paris Agreement,⁷ including ensuring that the global temperature does not increase by more than 1.5°C. Achieving this will require the world to reduce its carbon dioxide emissions by 45% by 2030 and reach net zero by 2050.⁸

To achieve those targets, countries must commit to emission reduction targets and national net zero transition plans that are aligned with Paris this year. The IEA 'Net Zero by 2050' report clearly stated that a key milestone for these plans requires no new investment in new fossil fuel supply and redirecting flows to clean energy.⁹ Global clean energy investment must triple to \$4 trillion per year by 2030, maintained at that level through to 2050.

The world will only reduce emissions at the scale and speed required to meet net zero if the power of the private financial sector is harnessed. However, since the Paris Agreement was adopted in December 2015, over £2.7 trillion of new investment by Banks has been directed towards fossil fuels.¹⁰

As a global finance hub and as host of COP26, the UK is uniquely placed to take transformational action to align global financial flows with net zero.

⁷ COP26 is 5 years on from Paris, and there is an obligation for all countries to update their NDCs. It is therefore very important that it is a success.

⁸ [Special Report: global warming of 1.5C, IPCC \(2018\)](#)

⁹ [Net Zero by 2050: A Roadmap for the Global Energy Sector, IEA \(2021\)](#)

¹⁰ [\\$3.8 Trillion USD](#)



UK Finance Sector and Net Zero

The UK is leading the global trend for voluntary commitments from private finance to net zero.¹¹ Many financial firms are now making voluntary commitments to net zero, a cohort which to date includes Allianz, Barclays, Lloyds Bank, HSBC, Natwest, Aviva, Morgan Stanley and Santander. The UN-convened Net Zero Asset Owner Alliance has been joined by new initiatives such as the Net Zero Asset Manager Initiative and the Paris Aligned Investment Initiative. Some of the world's leading insurers and reinsurers, working together with the UN Environment Programme, have established a pioneering Net Zero Insurance Alliance (NZIA).¹² The Glasgow Financial Alliance for Net Zero (GFANZ) is also bringing together leading financial initiatives under the COP26 Race to Zero (R2Z).

However, relying on voluntary efforts is not sufficient given the urgency of climate change, and how far off we are in meeting our climate targets. In 2019, Mark Carney stated that the

¹¹ A [recent global survey](#) of over 500 pension funds and over 500 insurers indicated that 94% of insurers and 90% of pension funds either had committed to net zero or were planning to do so.

¹² [World's leading insurers and reinsurers and UN Environment Programme to establish pioneering Net Zero Insurance Alliance, UNEP \(2021\)](#)

UK's financial sector was aligned with 4°C or more of global heating.¹³ Today, private finance is still investing at scale in the fossil fuel economy, and the City of London is one of the biggest hubs globally for fossil investment and insurance. Recent analysis shows that 25 large financial firms are responsible for 1.8 times more CO₂e emissions¹⁴ than the territorial emissions of the UK itself.¹⁵ If scope 3 emissions were included, this figure would be far larger.¹⁶

Given the size and clout of the UK's financial sector, creating a net zero finance system will arguably be the most significant step the UK can take on tackling climate change. Moreover, according to a new report from the Grantham Institute, achieving a net zero and resilient economy is 'the best way of minimising the risks of climate change to the stability of the financial system and the macro-economy'.¹⁷ Therefore, it is imperative that the government puts in place the policies and regulation to get the UK finance sector on track to net zero.

In December 2020, the Advisory Group on Finance's report to the Climate Change Committee (CCC) recommended that the UK lead the world by committing to be the first net zero finance system – and, amongst other recommendations, require financial institutions to set targets and put in place transition plans to reach net zero emissions in line with the government's own objective and the goals of the Paris Agreement.¹⁸

In realising this, the UK can build back better – with the UK finance sector, and the broader economy, stronger and more resilient as a result. Voters¹⁹ and businesses are in support of a Green Industrial Revolution, which can, by investing in future-fit net zero infrastructure, create good quality green jobs and spread prosperity across the whole of the UK to the people and places in need.

However, by the government's own admission, the PM's 10-point plan will not get us to net zero by 2050²⁰ and is only a starting point. We must go further, faster to get on track to net zero. The opportunity for global green finance leadership is here for the taking, and the UK must seize it.

Government Actions Supporting a Net Zero Financial System

With the substantial momentum on net zero targets from private finance comes the growing importance of policy and regulation to support institutions in delivering their commitments, whilst ensuring these commitments are credible and consistent with the Paris Agreement temperature goal of 1.5°C.

The Government has already taken some important steps forward on its journey to a net zero finance system, including:

- > **The Prime Minister's 10-point plan for a green recovery** which stated an ambition to

¹³ [Bank of England boss says global finance is funding 4C temperature rise, The Guardian \(2019\)](#)

¹⁴ [Critics take aim at UK financial sector, the world's 9th largest carbon emitter, S&P Global \(2021\)](#)

¹⁵ [UK territorial emissions account for 1.1% of global emissions](#)

¹⁶ [The Time to Green Finance: CDP Financial Services Disclosure Report, CDP \(2020\)](#)

¹⁷ This report also calls for Transition Plans to support robust net zero [Central banks must play clear role in reaching goal of net](#)

[zero greenhouse gas emissions to tackle climate change, Grantham Research Institute on Climate Change and the Environment \(2021\)](#)

¹⁸ [The Road to Net Zero Finance, UK Climate Change Committee \(2020\)](#)

¹⁹ [Two-thirds of Brits support UK's green industrial revolution plans, Edie \(2021\)](#)

²⁰ [UK enshrines new target in law to slash emissions by 78% by 2035, UK Government \(2021\)](#)

'make the City of London the global centre of green finance'.²¹

- > The **UK COP26 strategy** has prioritised private green finance, echoing the Chancellor's recognition that 'financial services are a critical enabler in the drive for net zero'.²²
- > The **announcement by the G7 finance ministers** of their role in driving forward the transition of their economies and financial systems to net zero²³ and their support for TCFD in the recent G7 communique.²⁴

Promisingly, the Government is already installing some of the critical regulatory building blocks, including developing a UK green taxonomy and last year's announcement of mandatory climate risk disclosure by 2025 (TCFD).

The recent letter from the Chancellor to the Financial Conduct Authority and Prudential Regulation Committee updating their mandates to include supporting the net zero target,²⁵ and the Bank of England calling for mandatory disclosure of roadmaps to reduce firm emissions,²⁶ lays the groundwork for future regulatory action and is a clear signal to the market as to the direction of travel.

However, to support the scale and pace of the net zero transition required to align UK finance with the Paris Agreement, the Government must expedite the process and regulate to ensure that large UK companies and financial institutions

actively align their business strategies with the Paris Agreement.²⁷

The Government must set out clear guidance to level the playing field and ensure all companies are aligned with net zero. Failure to do so may risk inefficiency and confusion, non-compliance and even greenwash.



²¹ [PM outlines his Ten Point Plan for a Green Industrial Revolution for 250,000 jobs, UK Government \(2020\)](#)

²² [Chancellor sets out ambition for future of UK financial services, UK Government \(2020\)](#)

²³ [G7 Finance Ministers and Central Bank Governors meeting chaired by Chancellor agrees ambitious climate agenda in UK's COP Presidency year, UK Government \(2021\)](#)

²⁴ [G7 Communique \(2021\)](#)

²⁵ In its statement on prioritization in light of Covid-19, the Prudential Regulation Authority (PRA) outlined its commitment to the continued focus on embedding climate disclosure across the financial system and the UK.

²⁶ [Bailey doubles down on Bank of England's climate promises, Yahoo! Finance \(2021\)](#)

²⁷ [UK plc fails to report adequately on climate risks, Financial Times \(2021\)](#)



The Need for Mandatory Disclosure of Net Zero Transition Plans

The role of public policymaking and regulators in the transition is critical. With the Government placing its reputation on the line on UK Green Finance, it is **essential firms produce credible transition plans and that regulatory guidance protects against private sector greenwash.**

There is growing momentum towards transition plan disclosure, as reflected both by UK policy updates such as that to procurement rules,²⁸ and the EU Sustainable Finance strategy. However, the timescale for mandating transition plans must be accelerated.

The **UK Government should commit to mandating the disclosure of transition plans for net zero ahead of COP26.** These plans should include short and medium-term targets, long-term goals, and strategies with consistent and transparent regular reporting, supported by net zero aligned financial accounting. This mandate for disclosing transition plans should be included in the roll out of TCFD legislation within the UK.

²⁸ **Firms must commit to net zero to win major government contracts, UK Government (2021)**

²⁹ **New Financial Alliance for Net Zero Emissions Launches, UNFCCC (2021)**

³⁰ [UK plc fails to report adequately on climate risks, Financial Times \(2021\)](#)

Regulators could then be given the task of setting out the guidance and rules for these transition plans to ensure integrity and robustness. This standard setting could build on existing work by initiatives like the Glasgow Financial Alliance for Net Zero²⁹ and commitments under the Race to Zero.

The Government needs to provide direction and clarity to the market regarding 'what good looks like'.³⁰ Confusion in the finance sector regarding standards, methodologies, and timelines is already hindering private finance actors in developing credible net zero transition plans. Guidance could set out sector transition pathways which include information like key transition milestones and sectoral timetables.³¹

Clear guidance is also needed to ensure companies put in place plans which prioritise decarbonisation and actively influence business strategies to change.^{32,33} To ensure businesses deliver strategies aligned with a net zero pathway, companies should be required to produce independently audited Paris-aligned accounts³⁴.

³¹ **IIGCC report: Ambitious EU 2030 action essential for achieving net zero emissions, IIGCC (2020)**

³² **A new vision for sustainable finance: Plans to enhance the UK's global leadership, UKSIF (2021)**

³³ **Green groups raise concerns over Carney carbon credits plan, The Guardian (2021)**

³⁴ **Investor Expectations for Paris-aligned Accounts, IIGCC (2020)**

This is not about promoting divestment. It is about **ensuring constructive engagement between financial firms and real economy companies** to ensure alignment and accountability consistent with a smooth transition to net zero, in line with the Paris Agreement. It is also about creating plans for credible action when engagement fails to ensure long term financial stability.³⁵ Stewardship can play an important role in supporting this managed transition. Damaging and rapid divestment will be far more likely in the absence of credible transition plans.

Well placed policy and regulation can support and accelerate every large company and financial institution in implementing these plans to a high standard and can provide much needed clarity on what is expected from private finance to be aligned with the Paris Agreement.³⁶ If the world is to reach net zero, all major financial firms must act.

Additional Measures to support a Net Zero Financial System

Other measures which the Government should implement to create a Net Zero Finance System include:

- > **Expediting the roll out of mandatory TCFD, currently expected by 2025**, for all public interest companies (listed and unlisted) and

ensuring that the disclosures have integrity and include relevant net zero information.

- > **Fighting greenwash** by setting standards and guidance on ‘what good looks like’ to ensure that private finance implements high-quality transition plans which are credible, sufficiently ambitious, and consistent with the Paris Agreement 1.5°C temperature goal.³⁷
- > Introducing a requirement for **all listed companies to publish Paris-aligned financial statements**, with auditors required to provide an explicit opinion on their veracity. The need for Paris-aligned audited accounts already has significant investor support.^{38,39}
- > Establishing a **UK Green Taxonomy** which is a classification system for green which provides clear guidance to investors and business about which investments are compatible with the UK’s net zero and resilience target.
- > **Issuing Guidance to clarify director’s duties under section 172 of the UK Companies Act** to have regard for their impact on climate change, and thus duty to take preventative action.
- > Supporting **shareholder appraisal of credible net zero targets and transition plans**⁴⁰ as part of firms’ fiduciary duty to their shareholders. This could include establishing annual shareholder voting on transition plans. Through this, shareholders

³⁵ **Net Zero by 2050: A Roadmap for the Global Energy Sector, IEA (2021)**

³⁶ [More suggestions can be found in the COP26 Unit’s Private Finance Hub Strategy](#)

³⁷ Regulators should lean on resources from existing initiatives to provide clarity to the market on what good looks like for transition plans

³⁸ **Investor groups call on companies to reflect climate-related risks in financial reporting, UN Principles for Responsible Investment (2020).**

³⁹ Where directors choose not to use Paris-aligned assumptions in drawing up their accounts, they should be required to publish sensitivity analysis for a net zero pathway in the Notes to the Financial Statements. Details on what Paris-aligned accounting encompasses are provided by investors [here](#).

⁴⁰ [Shareholder Voting on Climate Transition Actions Plans, Say on Climate \(2021\)](#)



are empowered to take a more active role in evaluating company transition plans

- > Ensure that the Net Zero Strategy lays solid foundations for a strategic national approach to financing the UK's transition.
- > **Align with IEA recommendations on their roadmap to net zero by 2050**, including accelerating investment towards renewables and ceasing investment in new fossil fuel supply.
- > Creating space for meaningful stakeholder engagement between finance and real economy actors to support an inclusive net zero transition which is just and fair.
- > In line with the Government's 'nature positive' response⁴¹ to the Dasgupta review, set out a clear plan for the **implementation of the recommendations of the Review**, with clear deliverables in a timeframe compatible with the urgency of halting the loss of biodiversity and restoration of our natural capital.

Conclusion

Scaling net zero investment while aligning finance with net zero is imperative to green global recovery and meeting climate goals. Without this, the world will never meet the Paris Agreement targets.

Many of the UK's market actors and financial services industry want to play their part in supporting a sustainable net zero future for the UK. It is the Government's role to ensure they can implement net zero targets with integrity. To support them, a critical element is turbo-charging the growing norm for transition plans by announcing by COP26 a roadmap for the introduction of mandatory net zero transition plans within TCFD.

By doing so, the UK can cement its position as a global hub for the fast-expanding green finance sector, continue attracting business and investment, and cement its legacy post-COP26 as a global climate leader.

⁴¹ **Government commits to 'nature-positive' future in response to Dasgupta review, UK Government (2021)**