Transition plans for a net-zero future

WWF

AVIVA

Acting on climate change to build a better tomorrow

Foreword

The world is in the middle of a climate emergency and millions of people are already living with the consequences. Storms, wildfires, floods, extreme temperatures and other climate-related natural disasters are more frequent and more violent. They are destroying homes, upending lives and costing billions of pounds a year. The global economy cannot carry on as if it's business as usual.

Aviva and WWF have joined forces now because we believe that despite the challenges, we can act to limit the scale and impact of climate change. The world knows what's needed to build a sustainable future. We can protect and restore natural habitats that absorb carbon. We can help communities deal with a more extreme climate. But all of us need to act, right now, to actually make that happen.

It takes partnership and collaboration. The choices we each take individually make a difference, but a sustainable future ultimately depends on the changes we all make together. The world's economy is underpinned by investors, insurers and banks. That means the financial sector has both the ability and the responsibility to work together with government and others to support and accelerate the shift of the global economy onto a sustainable path.

We must realign our financial system so that it delivers outcomes consistent with the Paris Agreement and achievement of 1.5°C and so that investment flows faster towards a low-carbon economy. We must do this in the timeframes outlined by the science. This paper sets out our joint call on the UK Government to accelerate the net-zero transition by harnessing the power of our financial services sector.

As the U.K.'s leading insurer and the world's leading global conservation organisation, Aviva and WWF aim to use our shared expertise and influence to help make this happen. Together, we can help more people unite to take action, and help lead the changes we all hope to see for people and the planet.

Amanda Blanc,
Aviva Group CEO

Tanya Steele,
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Executive Summary

To meet the Paris Agreement target of limiting global temperature rise to 1.5°C, global carbon emissions must be cut by ~45% by 2030. The world is currently on "a path to achieve only a 1% reduction by 2030".[1] Decisive action is urgently needed to put the world on the right track.

The financial services sector has a key role to play.

Since 2020, we have witnessed significant – though far from universal – climate risk disclosures and net-zero commitments from financial institutions (FIs). This is recognition of the fact that climate change represents a material financial risk to FIs.

However, many net-zero commitments to-date have been short on detail, narrow in scope, and lacking short term targets, making it difficult to assess their credibility or guard against greenwashing.

With significant global emission cuts needed this decade, government intervention is needed to ensure FIs move beyond climate risk disclosure and toward portfolio alignment with the net-zero and 1.5°C goal.

There is increasing consensus that transition plans are the critical next crucial step that FIs need to take. A net-zero 1.5°C aligned transition plan should outline the clear steps FIs will take to address their climate related risks and opportunities and ensure their business model, growth strategy and capital investments align with the net-zero and 1.5°C goal.

Detailed work to provide clarity on metrics and methodological approaches is also needed to ensure that such actions are consistently applied and accurately implemented by all market actors.

Government action is needed to both support transition plan development and enact public policies to achieve net-zero across the whole economy.

With its world leading financial services sector, and as host of COP26 and the G7 Presidency, the UK is uniquely placed to harness the finance sector to drive forward the net-zero transition both at home and abroad.

In doing so, the UK can deliver a stronger, more resilient economy, create high quality green jobs and establish the UK as the global hub for green finance.

To achieve this, Aviva and WWF recommend that:

1. **The UK government mandates UK regulated financial institutions to develop credible transition plans that align with net-zero and the 1.5°C goal of the Paris Agreement from 2023 onwards**. This requirement should be set in legislation as soon as possible and no later than the Treasury's Future Regulatory Framework (FRF)[2]. The ongoing oversight and supervision of the transition plans should be undertaken by the relevant regulatory and supervisory bodies.[1]

2. **As an interim measure, ahead of COP26 the Treasury should recommend to regulators that they require UK financial institutions to begin producing net-zero 1.5°C aligned transition plans by the end of 2022**. This can be done though supplementing the Treasury's March 2021 letters to the Bank of England's Prudential Regulation Committee and the Financial Conduct Authority.

3. **The UK Government should bring together regulators, industry and civil society to develop detailed guidance on the most appropriate metrics, methodologies and specifications for transition plans**.[2] They should have clear and timebound objectives linked to the transition plan policy goal and coordinate with existing initiatives and frameworks, notably the ongoing work of the Glasgow Financial Alliance for net–zero, TCFD and Science Based Targets for Financial Institutions.

4. **The UK Government should create a clear policy framework to drive net-zero across the real economy, signaling the steps and timescales by which they will be met.** The policies needed to achieve the Climate Change Committee's 6th Carbon Budget and the Government's upcoming Net-Zero Strategy provide opportunities for this.

5. **In parallel, the UK should use its role in the G7, G20 and other multilateral platforms to encourage other major economies to mandate transition plans globally**. As host of the G7 Presidency and COP26, the UK has a clear opportunity to progress this.

[1] To assist financial regulators, the government should also consider training or additional capacity to assist with technical evaluation and oversight processes of transition plans, for example with support of consulting firms and auditors to ensure that any new demands are met with corresponding expertise and resource

[2] The work should also consider wider business impacts beyond technical work, such as employee training, governance structures and measures that support cultural acceptance and smooth integration of proposed changes

Introduction

2021 is a pivotal year in the fight against climate change.

To meet the Paris Agreement target of limiting global temperature rise to 1.5°C, the world must cut carbon emissions by ~45% by 2030[3]. The world is currently on "a path to achieve only a 1% reduction by 2030"[4]. As Patricia Espinosa, former Executive Secretary of the UN Framework Convention on Climate Change rightly said, "decisions to accelerate and broaden climate action everywhere must be taken now".[5]

But just as the challenge is great, so is the prize. Mark Carney, former head of the Bank of England and now UN Special Advisor on Climate Action and Finance, described the net-zero transition as "the greatest commercial opportunity of our age."[6]

The UK is well placed to lead the way.

The UK has reduced its domestic greenhouse gas emissions by over 40% since 1990, whilst the economy has grown by almost 80%[7]. Low carbon industries already support almost 500,000 jobs across the UK, from electric car manufacturing in the Midlands to the offshore wind industry in the Humber. It is estimated that a further 240,000 green jobs could be created by 2030[8]. Globally, the benefits of shifting to a low-carbon pathway are estimated at $26 trillion by 2030[9].

UK businesses are also stepping up to the plate. There has been a rapid proliferation in UK firms committing to net-zero.[10] Investors and lenders are increasingly using their influence to drive net-zero across the real economy. Investment is rapidly scaling up into low carbon solutions.

However, it remains the case that the UK is off track to meet its net-zero targets and that further steps are needed to drive the transition at the pace and scale required to tackle the climate emergency.

The finance sector has a key role to play.

Recent research revealed that UK banks and asset managers were responsible for financing 805 million tonnes of CO2e in 2019 through their lending and investing.[11] Yet the finance sector can and must be part of the solution. It can support innovation in low-carbon technologies, such as better batteries for storing renewable energy. It can also engage with investee companies to press them to reduce their emissions. Its ability to influence corporate behavior, and the fact we simply cannot finance the transition from public funds alone, means that the role of private finance in driving the net-zero transition across the whole economy is crucial.

With its world leading financial services sector, and as host of COP26 and the G7 Presidency, the UK is uniquely placed to harness the finance sector to drive forward this transition both at home and abroad.

In doing so, the UK can deliver a stronger, more resilient economy, create high quality green jobs and establish the UK as the global hub for green finance.

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Mandatory TCFD disclosures: an important first step

The recommendations of the Taskforce for Climate-related Financial Disclosures (TCFD) represent a significant moment in corporate engagement with climate change.[12]

Since their introduction in 2017, both the number of entities disclosing TCFD-aligned information and the reporting quality has improved markedly.[13] Importantly, the TCFD framework has begun to shift the way organisations perceive and manage climate-related financial risks and opportunities.

In 2020 the UK government announced plans to make TCFD-aligned disclosures mandatory across the economy by 2025, with a significant portion disclosing by 2023. The G7 has since supported mandatory climate-related financial disclosures globally[14]. This is wholly welcome.

Beyond disclosure

While TCFD disclosures are hugely important, they should not be mistaken for actions to align with net- zero and the 1.5°C goal.

As has been pointed out by academics, “while TCFD can influence the nature of the information disclosed, it has no direct influence over the degree to which, and how appropriately, such information is used”.[15] TCFD in effect acts as a helpful thermometer – showing the level of risk in the system – but does not have the scope to turn the heat down.

Nor is a lack of information the sole barrier to the market addressing climate change. Climate change is fundamentally a failure of markets: those who damage others by emitting greenhouse gases generally do not pay.[16] This means that the biggest financial risks from climate change are not from losses to firms or industry sectors, rather from the macroeconomic systemic risks against which one cannot hedge. A study by the Economist Intelligence Unit estimated that left unchecked climate change risks a $43tn loss to the global economy.[17] This has potentially catastrophic impacts on the stability of the entire finance system and the wider society which it serves.[18]

Institutional investors are increasingly calling for measures that go beyond disclosure. The Institutional Investors Group on Climate Change brought together a group of investors representing $11tn in assets calling on banks to align their financing with the net-zero goal and to ensure that executive pay is linked to this target.[19]

As the timeframe for effective climate action shortens, with significant global emission cuts needed this decade, regulatory intervention must quickly move beyond risk disclosure as the primary tool to drive finance and corporate action on climate change.

Aviva's 2040 Net–Zero Commitment

In early 2021, Aviva announced plans to become a net-zero carbon emissions company by 2040. This is the most demanding target of any major insurance company in the world today.

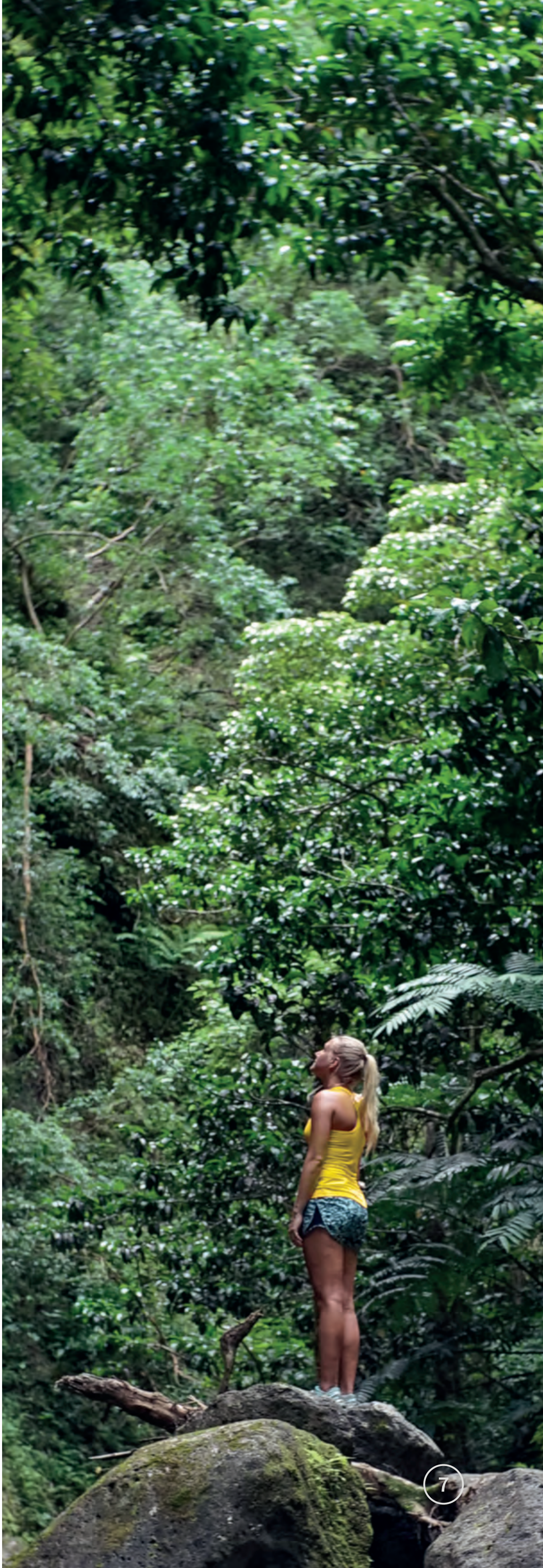
The goal will inform every aspect of Aviva's operations and investment decisions, and is a key part of its strategy to contribute to a sustainable economic recovery.

Aviva's 2040 net–zero plan means:

- ✔ **Net–zero carbon emissions from its investments by 2040;**
- ✔ **A 25% cut in the carbon intensity of its investments by 2025 and 60% by 2030.**
- ✔ **Net–zero carbon emissions from its own operations and supply chain by 2030.**
- ✔ **Stopping insuring or investing in companies that make more than 5% of their revenue from coal unless they have signed up to Science-Based Targets aligned to the Paris Agreement.**

The plan covers Aviva's scope 1, 2 and 3 emissions, the shareholder and policyholder assets where Aviva have control and data; and the main asset classes of Aviva's core markets (credit, equities, and direct real estate). Aviva will expand this further as new data and methodologies become available. More details can be found at **www.aviva.com/climate-goals**

Aviva plans to develop its own transition plan later this year detailing how it will meet its net-zero commitments and align its business to a 1.5°C pathway.



Aligning the finance sector with net–zero and the Paris Agreement

Since 2020, we have witnessed significant – though far from universal - net-zero commitments from financial institutions across the finance sector.

Leading banks, insurers and investors have been seen to embrace the net-zero goal and new industry initiatives have been established.

The UNFCCC's Race to Zero, and the new $70tn Glasgow Financial Alliance for Net Zero (GFANZ)[20], bringing together over 160 firms together responsible for assets in excess of $70 trillion from the leading net zero initiatives across the financial system, are helping accelerate the net-zero transition, in what has been described as a 'breakthrough' moment[21] for finance and a signal that the net-zero goal is now mainstream.

Voluntary net-zero targets are an important step towards portfolio alignment but challenges remain.

While there is growing consensus on what determines a credible and robust net-zero commitment (see WWF criteria[22]), to date, many net-zero announcements have been short on detail, narrow in scope, and lacking in short term targets, making it difficult to assess their credibility or guard against greenwashing.

Research has shown that while 31% of the FTSE 350 have a target to reduce emissions in line with net-zero or the Paris Agreement, meaningful detail about the assumptions, methodologies and strategies used are "often limited or missing"[23].

Further, while the underlying metrics, methodologies and frameworks are maturing - as a result of extensive work and growing voluntary commitments[24] - there is a growing risk of methodological divergence and fragmentation.

Further steps are needed to address such issues so that actions to meet net-zero are consistent, comparable and credible.

Transition plans: the next frontier in net–zero

Transition plans are crucial to ensure that high level net-zero targets translate into the absolute emission reductions that are required.

There is increasing consensus that transition plans are the next step that financial institutions need to take to meet the net-zero goal.

The UK's independent public advisory body, the Climate Change Committee, published an advisory report entitled The Road to Net-Zero Finance, which recommended "net-zero targets and plans be mandatory for financial institutions". This would "ensure that financial flows are consistent with the Paris Agreement and would show clear UK leadership".[25]

Mark Carney has frequently called on financial institutions and other firms to disclose their transition plans to net-zero to shareholders.[26]

The COP26 Presidency stated that "companies, banks, insurers and investors all have to adjust their business models and develop credible plans for the transition to a net-zero economy and implement them."[27]

The precise specifications of a transition plan should be a dynamic and evolving strategic process, that will vary depending on the sub-sector of finance (e.g. banks, asset managers/owners, insurance) and individual attributes of each institution (e.g. size, geographies, portfolio and loan composition).

Detailed work to provide clarity on metrics and methodological approaches is needed to ensure that actions are consistently applied and implemented by all market actors. There should also be transparency and mechanisms for stakeholders to hold firms to account.

A number of organisations have begun to develop guidance and principles. For example, the TCFD published proposed guidance stating that a firms' transition plans should help address its climate-related risks and opportunities, deliver on its climate targets, be anchored in quantitative metrics and be detailed and verifiable[28]. Such guidance, as long as it is in line with the latest climate science, lays the groundwork for further government action, as set out in our recommendations below.

The need for government intervention

Voluntarism is no longer enough to drive change at the pace or scale required. Public policy is needed.

In order to fully harness the finance sector to accelerate the net-zero transition, there needs to be commensurate public policy measures across the finance sector and the real economy both at home and abroad.

Internationally, reform of the global financial architecture is needed so that global institutions help support the net-zero transition[3], including through a new International Platform for Climate Finance.

As was recognised by G7 Finance Ministers in June 2021, action is also needed to address the macroeconomic impacts and market failures at the heart of climate change, such as by putting a price on carbon.

FI's alignment will ultimately be determined by the alignment of the real economy. It is important that government enacts policy changes to ensure that the real economy itself reaches net-zero. A clear and consistent roadmap for sectoral transition, including listed firms' own transition plans, will be needed The policy measures contained in the Climate Change Committee's 6th Carbon Budget report provide a blueprint for this and the Government's upcoming Net-Zero Strategy provides an opportunity to take them forward.

Public policy is also needed to drive forward net zero transition plans. Whilst there is growing recognition of the need to quickly transition business models towards a net-zero economy, the adoption of transition plans to-date remains low. Given the myriad of overlapping frameworks, initiatives and methodologies and relatively recent consensus around the net zero goal, this is in some respects understandable. However, if we are to get on track to meeting net zero, just as TCFD has become a mandated requirement across the sector, so too must transition plans.

[3] As set out in the report 'Harnessing the international financial architecture to deliver a smooth and just transition' supported by the Coalition for an International Platform for Climate Finance which Aviva convened and WWF are members

Recommendations for COP26

As host of COP26 and G7 presidency the UK has a unique opportunity to build on the progress made on TCFD reporting and establish new grounds for international leadership by introducing further measures to align the finance sector with the need to tackle climate change.

We recommend that:

1. **UK government mandates UK regulated financial institutions to develop credible transition plans that align with net-zero and the 1.5°C goal of the Paris Agreement from 2023 onwards**. This requirement should be set in legislation as soon as possible and no later than the Treasury's Future Regulatory Framework (FRF)[29]. The ongoing oversight and supervision of the transition plans should be undertaken by the relevant regulatory and supervisory bodies.[4]

2. **As an interim measure, ahead of COP26 the Treasury should recommend to regulators that they require UK financial institutions to begin producing net-zero 1.5°C aligned transition plans by the end of 2022**. This can be done though supplementing the Treasury's March 2021 letters to the Bank of England's Prudential Regulation Committee and the Financial Conduct Authority.

3. **The UK Government should bring together regulators, industry and civil society to develop detailed guidance on the most appropriate metrics, methodologies and specifications for transition plans**.[5] They should have clear and timebound objectives linked to the transition plan policy goal and coordinate with existing initiatives and frameworks, notably the ongoing work of the Glasgow Financial Alliance for net–zero,TCFD and Science Based Targets for Financial Institutions..

4. **The UK Government should create a clear policy framework to drive net-zero across the real economy, signaling the steps and timescales by which they will be met.** The policies needed to achieve the Climate Change Committee's 6th Carbon Budget target and the Government's upcoming Net-Zero Strategy provide opportunities for this.

5. **In parallel, the UK should use its role in the G7, G20 and other multilateral platforms to encourage other major economies to mandate transition plans globally**. As host of the G7 Presidency and COP26, the UK has a clear opportunity to progress this.

[4] To assist financial regulators, the government should also consider training or additional capacity to assist with technical evaluation and oversight processes of transition plans, for example with support of consulting firms and auditors to ensure that any new demands are met with corresponding expertise and resource

[5] The work should also consider wider business impacts beyond technical work, such as employee training, governance structures and measures that support cultural acceptance and smooth integration of proposed changes

Transition plans for a net–zero future: an opportunity for UK leadership

The UK's pre-existing leadership on climate action, allied with its pre-eminent financial services sector, represents a unique opportunity for the UK to harness the finance sector to drive forward the net-zero transition.

A net-zero finance sector is achievable. Indeed, it is essential and should be an overarching objective of the UK's Net-Zero Strategy. Mandating plans that align with net-zero and the 1.5°C goal of the Paris Agreement is the next step on that journey.

Endnotes

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Aviva and WWF are acting together on climate change to build a better tomorrow. Through our three-year partnership, we are advocating to realign the finance sector to a 1.5 degree pathway; working with communities in the UK and Canada to build healthier and more resilient ecosystems that help reduce the risk of climate-related natural disasters; and engaging millions of people to understand the power of their individual choices in contributing to a sustainable future.

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