Financed Emissions Initiative

Concept Note

Finance Sector Guidance on GHG Accounting and GHG Risk Management

Summary
Acting as market makers, capital providers, and advisers, Financial Institutions (FIs) and Portfolio Investors (PIs) are important actors in the shift to a low-carbon economy. Many FIs and PIs now report emissions from their operations (Scope 1 and 2). However, this says little about the full GHG exposure of their business and the resulting financial risks posed by them. The majority of emissions associated with FIs and PIs are created by the companies, technologies and projects they finance.

The transition to a low-carbon economy will create challenges for FIs and PIs. If governments are to limit climate change to 2^{0}C, Greenhouse Gas (GHG) emissions will become increasingly regulated and financially risky. These regulations and risks will not only impact direct emitters of GHGs, but also those who rely on them to do business, (including financial intermediaries[1]). Therefore, it is essential that FIs and PIs are able to measure and manage the GHG-intensity of their business and the financial risks that result from it.

The GHG Protocol Corporate Value Chain (Scope 3) Standard provides a framework for reporting value chain emissions, including emissions from financial products and services. Still, the guidance provided is 'high-level' and does not address potential carbon risks. Additional guidance is needed to enable FIs and PIs to accurately and consistently report their relevant emissions and enable them to identify, evaluate and manage carbon-related risks

Rationale for Financial Sector Guidance on GHG Accounting and GHG Risk Management
For more than ten years, companies have relied on the GHG Protocol *Corporate Standard* for guidance on accounting and reporting of GHG emissions. Many FIs and PIs now measure the GHG emissions of their own operations – over two thirds of FIs in the Fortune 500 reported their scope 1 and 2 emissions to the Carbon Disclosure Project (CDP) in 2011[2]. Nevertheless, reporting of financed emissions is not common.

In late 2011, the GHG Protocol released the Corporate Value Chain Accounting and Reporting Standard (the *Scope 3 Standard*). This standard provides a framework to account for emissions from an organization's entire value chain, including emissions from investments. That said, feedback from stakeholders suggested that more detailed guidance is needed to cater to the realities and needs of the finance sector. During a year-long scoping phase, and with input from an Advisory Committee, it was determined that the financial sector needs guidance on two distinct but interlinked challenges:

[1] 'Financial intermediaries' includes all organizations or institutional units involved in financial intermediation, including asset owners such as pension funds, their service providers in the asset management industry and banks.
[2] Global 500 Report, Carbon Disclosure Project, 2011

First, in order to facilitate harmonized and meaningful emissions disclosure, FIs and PIs need accounting guidance on how to measure and report GHG emissions from their financial products.

Second, FIs and PIs need guidance on how to identify, assess, and manage increasing GHG-related risks to portfolios and assets (particularly GHG intensive ones).

Establishing an internationally consistent method for calculating and disclosing financed emissions will enable FIs, PIs and their stakeholders to identify GHG emission 'hot-spots' in financial operations and provide a basis for them to reduce those emissions over time. In addition, policy-makers and regulators will be able to assess financial sector emissions in the context of a low-carbon economy and create rules to better align the sector to a low-carbon future.

Embedded GHG emissions in FI and PI debt and equity portfolios, whether they are current, ongoing or future (like fossil fuel reserves) emissions, can translate into financial risk. For example, as the effects of climate change become more prevalent, changing market and regulatory conditions may negatively affect the commercial viability, competitiveness and/or value of certain investments (particularly carbon-intensive ones). However, these risks will manifest in different ways and at varying intensities depending on the sector, asset class or type of financier. Therefore, providing FIs and PIs with a comprehensive and detailed framework to understand, assess and manage a range of 'carbon risks' will enable them to thrive in a future low-carbon economy.

The opportunity

To enable FIs and PIs to account for and report financed emissions and identify and manage subsequent risks, GHG Protocol and UNEP FI will facilitate development of two guidance documents.

The accounting methodology for financed emissions will be developed by an international group of cross-sector stakeholders including many financial institutions. This will help ensure that standardized and meaningful disclosure of financed emissions becomes common practice. Questions to be answered include: What is the business case for measuring and reporting financed emissions? How does the availability and quality of GHG data affect its usefulness to FIs and PIs? How should emissions from lending and investment activities be calculated? How should this information be reported to stakeholders?

Creating a practical, comprehensive and detailed framework to assess and manage carbon asset risks will help prepare FIs and PIs for the potential monetary threats posed by climate change. Questions to be answered include: Where are there carbon risks in lending and investment portfolios? What are effective and appropriate strategies to manage these risks? How can risk reduction and mitigation approaches be designed and implemented? What might be the catalysts that lead to government action on climate change that could strand carbon-intensive assets? What types of data need to be collected and analyzed to help determine when these actions may take place?

Current landscape

To-date, few FIs and PIs report emissions from their business activities, due in part to the lack of a standardized approach. Some FIs and PIs have developed their own methodologies, often in conjunction with consultants and/or NGOs. Methodologies currently exist for calculating emissions from numerous financial products/services, including: project finance; corporate and private loans; managed investment portfolios; investment banking services; savings; and capital grants. These methodologies were developed separately by multiple organizations and, as a result, lack consistency. Nonetheless, each has benefits that will inform the guidance development process.

Greenhouse Gas (GHG) Protocol

GHG Protocol is the most widely used international accounting tool for government and business leaders to understand, quantify, and manage GHG emissions. It provides the accounting framework for nearly every GHG standard and program in the world – from ISO 14064 to The Carbon Disclosure Project – as well as hundreds of GHG inventories prepared by individual companies world-wide. GHG Protocol has more than a decade of experience developing GHG accounting standards and guidance. GHG Protocol's highly successful multi-stakeholder standard development process, combined with the GHG Protocol's team of technical experts ensures high-quality publications and wide adoption.

UNEP Finance Initiative (UNEP FI)

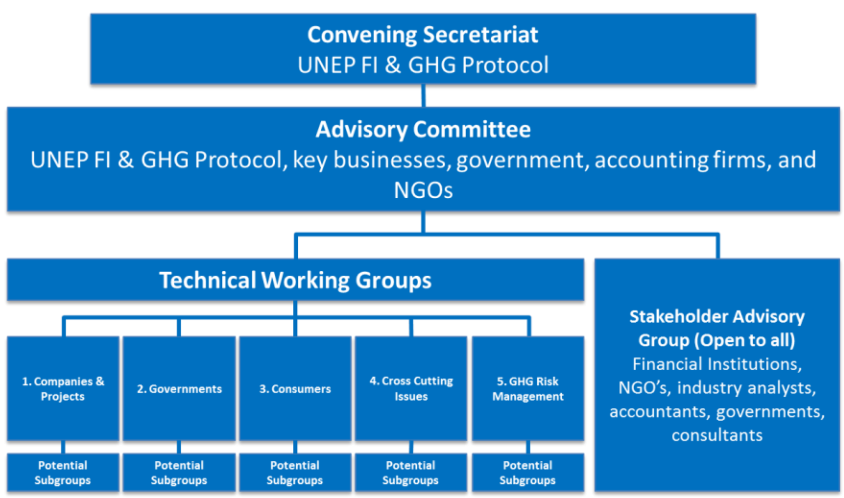
UNEP FI is a unique public-private partnership between the United Nations Environment Programme and more than 200 financial institutions – insurers, investors, lenders – working to better align the operations of financial markets with sustainable development. Within a wide range of activities that span normative frameworks, policy dialogue, training, and research, UNEP FI develops practitioner guidance on the integration of sustainability considerations into decision-making, including in the area of accounting and reporting. From 2003 to 2008, UNEP FI co-convened the process that developed the Reporting Guidelines and Financial Sector Supplement of the Global Reporting Initiative (GRI).

How the guidance will be developed

The Emissions Accounting Guidance and Carbon Asset Risk Guidance will be developed through an international, consensus-based, multi-stakeholder process with balanced representation from financial sector companies, governments, environmental groups, academics and consultants. Prior to launching the guidance development process, GHG Protocol and UNEP FI carried out a scoping phase including an online survey and in-person meetings with a wide range of stakeholders. Through this process, the need for guidance was confirmed and the scope of investment types to include was determined. Following the scoping phase, a governance structure, (see diagram) including an Advisory Committee were formed and Technical Working Group topics were established.

GHG Protocol and UNEP FI have assigned participants to each of the TWGs aiming for balanced representation by geographic location and organization type. The balanced representation of stakeholders, led by participation from FIs and PIs, will ensure that the guidance developed will be practical and accepted world-wide among financial practitioners.

Governance structure



Using the *Scope 3 Standard's* existing guidance for investments as a foundational framework, the Technical Working Groups will work with GHG Protocol and UNEP FI to draft the guidance. Road testers will use the draft guidance to carry out inventories of their investments. Concurrent to the road testing will be a public comment phase, where interested stakeholders provide feedback on the draft. All feedback will then be reviewed and revisions made to the guidance, followed by a second public comment period before final publication.

Proposed activities and timeline

Date	Project Phase	Activities
Sep 2012 – May 2013 (completed)	Scoping phase	Online survey to assess interest in project, gain initial understanding of potential scope, identify funders, advisory committee, and other key stakeholders. Roundtable discussions in London and New York focused on clarifying scope of guidance.
Jun 2013	Project Plan	Write project plan and finalize governance structure
		UNEP FI (including focal point UNEP FI members) and GHGP sign off on project plan and governance structure
Jul – Sep 2013	Form Advisory Committee	Agree on composition of Advisory Committee
		Recruit Advisory Committee members
		Advisory Committee meeting (including reaching agreement on the structure of TWGs)
Dec 2013 - Feb 2014	Launch TWG Process	Recruit Technical Working Group members
		Launch TWG through in-person meeting or webinars
Feb – Aug 2014	Drafting	TWGs conduct background research
		TWGs develop proposed scope of guidance for Advisory Committee review
		TWGs draft chapters and produce first draft of guidance (led by TWG leads)
Sept 2014 – Feb 2015	First public comment phase and road testing	Release draft for public comment and host stakeholder workshops
		Road testing
Feb – Jun 2015	First round of revisions based on feedback	Summarize feedback and GHG Protocol/UNEP FI propose revisions to TWGs and Advisory Committee
		Revise guidance based on comments (UNEP FI and WRI, with approval from TWGs and the Advisory Committee)
Jun - Jul 2015	Second public comment period	Release draft for public comment and host stakeholder workshops/webinars
Aug - Oct 2015	Second round of revisions based on feedback	Revise guidance based on comments (UNEP FI and WRI, with approval from TWGs and the Advisory Committee)
Sep – Oct 2015	Review and sign off	Internal review/sign off by Advisory Committee, UNEP FI, WRI and WBCSD
Nov - Dec 2015	Copy editing, design and publication	Copy editing (outsourced)
		Publication layout and Design (outsourced)
Jan 2016	Publication	Publish guidance and host launch event
Jan 2016 - onwards	Outreach	Various outreach activities, including speaking at conferences, print media, and training.