Call for inputs from Parties and stakeholders in the financial sector regarding ways to achieve Article 2, paragraph 1(c), of the Paris Agreement, including options for approaches and guidelines for implementation

CDP Europe Submission

Executive summary

CDP Europe is pleased to make its first input to the discussion on the alignment of financial flows to the Paris Agreement (2.1.c). CDP welcomes the establishment of the Sharm el-Sheikh Dialogue on 2.1.c as a space for Parties and observers to discuss this essential enabler for the achievement of Paris goals.

- CDP supports an inclusive, evidence-based, and purposeful discussion on 2.1.c, providing the latest insights and evidence-based recommendations with respect to non-Party stakeholders (NPS)' accountability and action. The inclusion of CDP in the Sharm el-Sheikh Dialogue on 2.1.c would allow evidence-based inputs and insights from 20 years of disclosure experience from private sector. The discussion should be linked with other workstreams, including the Global Stocktake and existing work like the finance pathway of the Marrakesh Partnership for Global Climate Action (MPGCA).
- Based on CDP's data analysis provided by disclosing entities in the last 20 years, transparent disclosure by companies, including financial services, cities, states and regions is key to shift the private financial flows and align them with the Paris Agreement.
- Concrete options for approaches for implementation by various stakeholders have been identified in CDP's flagship report on sustainable finance and build on data analysis of 332 financial institutions across the world disclosing voluntary through CDP's questionnaire and combining assets of over US $ 109 trillion. A more recent analysis conducted with the International Finance Corporation completes this work with identified best practices for regulators.
- National governments can leverage their authority to increase disclosure both in quantity and in quality by collaborating with and endorsing CDP, as well as supporting companies to prepare for reporting regulations.

CDP remains available to the Standing Committee on Finance (SCF) to provide further evidence and insights following this submission.

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1. Introduction

CDP's input to the SCF on 2.1.c is centered on existing analysis that are highly relevant to the discussion on finance alignment, ways for Parties to join forces with CDP in implementing article 2.1.c and suggestions for a purposeful process at the international level. In this submission we recall the insights already mapped in the addendum 4 of the latest SCF report at COP27 and complement this with the new publications on transition plans, including quantified data, as well as concrete actions to be taken by Parties at domestic and international levels to shift the trillions.

2. Way to achieve 2.1.c: shifting trillions requires transparent disclosure

CDP is a global non-profit that runs the world's environmental disclosure system for companies, cities, states and regions. Founded in 2000 and working with more than 740 financial institutions with over $130 trillion in assets, CDP pioneered using capital markets and corporate procurement to motivate companies to disclose their environmental impacts, and to reduce greenhouse gas emissions, safeguard water resources and protect forests. Nearly 20,000 organizations around the world disclosed data through CDP in 2022, including more than 18,700 companies worth half of global market capitalization, and over 1,100 cities, states and regions. Fully TCFD aligned, CDP holds the largest environmental database in the world, and CDP scores are widely used to drive investment and procurement decisions towards a zero carbon, sustainable and resilient economy.

For nearly two decades, CDP has been demanding environmental disclosure and action from companies, by bringing asset owners, asset managers, banks and insurers together to engage with companies on an industrial scale. Investors use our data on climate change, deforestation and water security to inform decision making, engage with companies, reduce risks and identify opportunities. CDP's work is essential, as multi-national enterprises are a significant actor in the climate crisis. A joint report[1] from CDP and The World Bank Group studies the effect of multi-national enterprises on carbon emissions and climate commitments. In 2021, just 157 large multi-national enterprises accounted for 10% of the world's industrial emissions and their supply chains accounted for another 50%. One in four of all multi-national enterprises have committed to net-zero GHG emissions by 2050, which demonstrates that progress has been made, however more action is needed to bring all actors in line with 1.5C. Investors are uniquely equipped to help mitigate environmental risks and push forward the low-carbon transition.

CDP's work embodies the logic that what is not measured cannot get managed. Through transparent disclosure on climate change, water security and forest, CDP accompanies and builds their capacity towards sustainability. As a result, companies, including financial services companies become aware of and act on their environmental and climate impacts, including climate risks in their financial strategy and rethinking their investment plan. On top of this investors are provided with reliable and comparable data on how companies they might invest in are managing climate and environmental issues (impacts, risks, dependencies, opportunities).

[1] Diversification and Cooperation in a Decarbonizing World (worldbank.org)

CDP is a founding member of the Science Based Targets initiative, We Mean Business Coalition, The Investor Agenda and the Net Zero Asset Managers initiative. A good mapping of CDP's contributions to pathways towards sustainable finance, is contained with 20 quotations in the last report of the SCF FCCC/PA/CMA/2022/7/Add.4 on "further work on mapping the available information relevant to Article 2, paragraph 1(c), of the Paris Agreement, including its reference to Article 9 thereof", is contained in addendum 4 to this report.

3. Quantified information on the state of alignment of private finance and transition plans

3.1 Approaches for implementation by national governments

CDP's last flagship report on sustainable finance analysed the environmental impact of financial institutions' portfolios and operations together, based on self-reported data from global asset managers, asset owners, insurers and banks. The report "Time to green finance"[2] is listed in the last SCF report to the COP and CMA[3] on the mapping of available information relevant to Article 2, paragraph 1(c), of the Paris Agreement, including its reference to Article 9 thereof (FCCC/PA/CMA/2022/7/Add.4) and finds that portfolio emissions are over 700 time larger than direct emissions. Financial institutions must urgently decarbonize their portfolios, by:

- **Closing the critical data gap through transparent disclosure of plans to align with Paris**. Despite the growing momentum of financial institutions announcing net zero targets, our data shows that in 2020 less than half of disclosing financial institutions and only 27% of insurers reported actions to align portfolios with limiting global warming to well-below 2 degrees Celsius.
- **Disclosing the impact and risks of their financing activities, instead of exclusively focusing on opportunities**. Financial institutions are increasingly focused on sustainable finance products – in 2020 76% identified opportunities in areas such as sustainability-linked loans, green and transition bonds, sustainable investment funds and insurance solutions, which are worth up to US$2.9 trillion. Most institutions did not report their credit risks (65%), such as borrowers' default on loan repayments and most (74%) did not report market risks, such as stranded assets and financial asset price devaluation. Yet, the reported risks associated with financing have a much higher potential financial impact than the reported operational risks (US$1 trillion combined versus just US$34 billion); and
- **Urgently engaging with companies and decarbonizing their portfolios**, through collective engagement initiatives such as CDP's Non-Disclosure Campaign and Science-Based Targets Campaign.

National governments have a key role to play in ensuring financial institutions measure their scope 3 financed emissions better, set a target to align their portfolio with a net-zero carbon world by 2050 and interim targets for their portfolio to reach that goal, engage with their portfolio

[2] https://cdn.cdp.net/cdp-production/cms/reports/documents/000/005/741/original/CDP-Financial-Services-Disclosure-Report-2020.pdf?1619537981
[3] https://unfccc.int/sites/default/files/resource/cp2022_08a04__cma2022_07_a04.pdf?download

on decarbonization and enhanced resilience, and validate how they intend to align with net-zero by giving shareholders an annual vote on their transition plan.

3.2 Recommendations for regulators

The analysis[4] of best practices in environmental disclosure policies, conducted jointly with the International Finance Corporation (IFC) in December 2022 identifies recommendations on the process of developing reporting policy, but also proposes guidance for regulators in six sets of actions:

- Broad consultation of global frameworks to better understand the overall trends in the environmental agenda, including the Kunming-Montreal Global Biodiversity Framework;
- Put double materiality as a central concept to many policies, to satisfy the appetite for information. The IFC and CDP are active in building the capacity of stock exchanges and market regulators, primarily by training them on how to formulate disclosure requirements suitable for decision-makers;
- Consider questions surrounding compliance, as they are more often on the agenda of decision-makers even when codes and requirements are voluntary;
- Ensure high-quality disclosure and get prepared for an increasingly active and granular approach in the nonfinancial and sustainability reporting policy space;
- Ensure the timely incorporation of developments in reporting frameworks, potentially at the level of metrics and targets; and
- Ground the need for mandatory disclosure requirements by introducing regulation requiring the disclosure of nonfinancial and sustainability information.

3.3. Approaches for closing the public-private environmental transparency gap

In May 2022, CDP collaborated with Bain & Company on a study[5] to understand the environmental transparency gap between public and private companies. The findings help quantify the scope of the challenge of 1.5° aligned pathway. Private companies trail public companies by a wide margin in reporting on environmental impacts. Even the most proactive private fund managers and companies are limited by the absence of standardized disclosure frameworks and meaningful comparisons with peers.

More than 13,000 companies, a third of which are public entities, reported to CDP on environmental and climate impacts in 2021. Yet while the 4,400 public companies in CDP's database cover 64% of global public market capitalization, the 8,700 private companies that report represent a tiny fraction of private market capitalization globally. Data from CDP's Climate Change 2021 Questionnaire, analyzed in conjunction with Bain & Company, shows that those private companies are far less likely than their public counterparts to report on greenhouse gas emissions, let alone take meaningful actions towards addressing the climate transition -

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[4] https://www.ifc.org/wps/wcm/connect/620c204f-bf44-41cb-83c8-fc298e94f6db/Analysis+of+Best+Practices+in+Environmental+Disclosure+Policies.pdf?MOD=AJPERES&CVID=omsKWrs

[5] https://www.bain.com/insights/closing-the-public-private-environmental-transparency-gap/

- Only 49% private companies report on Scope 1 and 2 emissions, compared with 88% of public companies;
- Only 29% report on any Scope 3 emissions vs. 70% of the public cohort;
- The effective coverage of Scope 3 emissions reporting is probably much lower, as many public and private companies are not yet reporting comprehensively on all 15 categories of Scope 3 emissions.

Private companies tracked by CDP cite resource constraints, capability gaps, and a lack of urgency from leadership as challenges to better reporting. To enable overcome this challenge, national governments should consider recommendations drawn from CDP's flagship report (see point 3.1).

4. Options for guidelines for Parties for achieving 2.1.c

4.1 Government Partnerships program

CDP's voluntary disclosure system is a unique mechanism for governments to accelerate the implementation of international and national climate and nature targets. CDP supports corporates, including financial services companies, and sub-national jurisdictions drive faster progress towards achieving climate neutrality and full recovery of nature by 2050. Companies reporting to CDP in 2022 represented about 74% of European market capitalization with over US$8 billion in annual revenue. The investor authority behind the CDP disclosure system – on a global level 680 investor signatories with US$130 trillion in assets under management and, in Europe alone, 200 investors with over US$100 trillion in assets – drive about 50% of the response rate by European companies. In addition, companies that also disclose environmental information throughout their supply chain – thereby taking responsibility for their value chain and purchasing decisions – number over 200 and represent US$5.5 trillion in value at a global level. From 2020 to 2022 alone, companies disclosing their environmental performance to CDP increased by 38% globally. In order to achieve the goals of the Paris Agreement and especially 2.1.c, and motivate all companies and sub-national jurisdictions to join in the transition, government support is needed. CDP has developed a government partnerships program[6] to frame collaboration in this regard.

National governments can support transparency, climate and environmental action through an endorsement. A government endorsement is a formal agreement of support by governmental bodies and other agencies for CDP's disclosure invitation. The government endorsement aims at including governments in CDP's annual disclosure cycle and provides them with insights into publicly reported data of corporates, cities and regions. Endorsing CDP's disclosure invitation also helps improve the climate change, water security and deforestation data reported by companies and local governments in the respective jurisdiction.

By endorsing the CDP disclosure system national governments can actively drive the increase in quantity and quality of climate and environmental data of corporates and local governments within their national jurisdiction, as well as trigger decisive action towards preventing dangerous

[6] see: https://www.cdp.net/en/policy/government-partnerships-program

climate change, water scarcity and deforestation. The information CDP obtains is vital because it underlies effective and efficient decision-making on policies and measures that advance the transition. CDP's data and insights – based on voluntarily disclosed primary information from companies and sub-national jurisdictions – and its resulting unique expertise can be utilized by governments to achieve the targets set forth in the Paris Agreement, the Kunming-Montreal Global Biodiversity Framework, the Sustainable Development Goals as well as the European Green Deal in the UE context.

For EU member states and EFTA countries, additional benefits exist by endorsing and partnering with CDP. These include automatically meeting several of the important climate-related obligations set forth by the EU and numerous international agreements because the commitments of governments partnering with CDP are closely aligned with EU and other international fora's policies, legislation and, consequently, member states' obligations.

4.2 Support the work of CDP on sustainable finance

Under an EU-funded project[7], CDP leverages EU LIFE funding to drive market uptake and scale EU ambition and best practice globally through the CDP system. To achieve these goals, CDP is engaging and enabling companies to disclose and act on their environmental impacts in line with the European regulatory requirements and a science-based transition to a net-zero and nature positive economy. Indeed, while the first reports made subject to the EU Corporate Sustainability Reporting Directive will be available from 2025, financial institutions need this information now to satisfy their own regulatory requirements. Supporting operational and aligned reporting frameworks like this project does, allows CDP to engage with companies to encourage disclosure on the specific data points investors need. Market readiness and implementation, technical alignment and provision of data and insights are parts of the activities running thanks to the project:

- Capacity-building activities for companies globally on EU disclosure regime;
- Connection with initiatives such as TCFD, ISSB, SEC, GRI, TNFD, SBTn, SBTI and GRI through CDP's global platform;
- Support of the evolution of CDP's disclosure system to integrate aspects of the EU's disclosure regime;
- Mapping of ISSB and SEC to ESRS and identifying best practice;
- Ensuring data can be used by capital market actors to drive corporate action; and
- Inform evolution of EU disclosure regime with 20 years of expertise on best practice reporting in line with science.

Similarly, CDP has been developing capacity building materials on taxonomies for practioners and decision makers. As tools like taxonomies are gaining more and more traction across the world, CDP's 20-year experience in ESG disclosure identified a set of common criteria for regional taxonomies that can, and should, be applied in order to ensure to drive capital allocation towards sustainable activities, reduce greenwashing and enable simpler comparison

[7] too read more about the project and access resources produced: https://www.cdp.net/ja/guidance/finaction-project

between investment opportunities. Over the first months of 2022, CDP ran an analysis of the taxonomies in development globally, in order to start designing an integration model to guide our future activities in this space. The study aimed to identify the different approaches for integrating sustainable finance taxonomies into the CDP disclosure system. Its findings are outlined in a policy brief “Seeking clarity amidst fragmentation”[8] (September 2022) and identified the following recommendations:

- Identify and adopt a **common baseline**, together with identifying linkages among taxonomies. CDP encourages this in order to avoid policy fragmentation and encourage interoperability;
- Ensure **alignment of taxonomies to the high-level policy goals**, in order to allow the capital allocation towards the policy agenda;
- Align sustainability taxonomies against disclosure requirements. Linkages should be made between the taxonomy criteria and economy-wide disclosure requirements. Where these requirements are put in place, they should include disclosure of taxonomy-aligned activities;
- **All ESG topics should be included**. If not, a plan should be in place to expand the scope of the taxonomy within time bound frames;
- Ensure **large scope of entities required to comply** with the taxonomy (ie issuers of green bonds, corporations, financial institutions, etc) should be as wide as possible, and a plan should be in place to extend compliance requirements to all capital markets actors;
- **Threshold and criteria** should be used to assess activities. In addition, these classifications and related tools should be science-based;
- **Transition activities and pathways should be timebound**. They should represent an improvement over the status quo. Moreover, particular attention should be given to those transition activities that require remedial efforts. CDP suggests ensuring the taxonomy does not conflate green and transition activities, and that there is a plan for transition requirements to become more stringent over time;
- **Sector coverage should extend as wide as possible**. If not all sectors, taxonomies should cover all high-emitting sectors and a plan should be put in place for the taxonomy to eventually cover all sectors.

All the criteria identified above can support the design of what this best practice should look like within sustainable finance taxonomies, which should cover a multitude of topics, interlinked by the “do no significant harm” principle and, as far as possible, be aligned to high level policy goals. The scope of the activities involved should not only consider activities that contribute to the environmental objectives set out in the taxonomy but also ones that may play a part in the transition to a more sustainable and resilient financial system: go beyond “green” to identify different “shades of brown"

[8] https://cdn.cdp.net/cdp-production/comfy/cms/files/files/000/006/829/original/Taxonomies_policy_brief_FINAL.pdf

5. Option for guidelines for a purposeful implementation of 2.1.c

As the world takes steps towards building a climate safe, deforestation free, water secure future, ambitious corporate action is more crucial than ever. Disclosure through CDP provides the bedrock for this. As the world's most comprehensive dataset, CDP's data both fuels and tracks global progress towards building a truly sustainable economy for people and planet.

For the Sharm el-Sheikh Dialogue on 2.1.c to deliver meaningful outcomes catalysing the shift of trillions, its process should be inclusive by ensuring that observers are transparently integrated in the discussions and by inviting them to provide evidence-based insights.

- Concretely, observers including CDP should be invited well in advance to the two workshops planed in 2023 and other activities falling under the Sharm el-Sheikh Dialogue on 2.1.c, ensuring affordability of attendance;
- The finance pathway[9] and the MPGCA work on greening finance should feed into the discussion.

[9] see https://unfccc.int/climate-action/marrakech-partnership/reporting-tracking/pathways/finance-climate-action-pathway#Climate-Action-Pathway-2021