Guidance to assess transition plans

To reach global net zero by 2050, all industries and organisations must transition.

A transition plan is a **time-bound** and **trackable** strategy and roadmap presenting the milestones and actions for **reducing emissions** with a science-based pathway to **net zero**.

Climate Bonds INITIATIVE

Key takeaways

01

All transition plans must contain clear, measurable and ambitious targets for change.

02

Targets must cover the short, medium and long term with steep front loaded emission cuts in the near term.

03

Carbon credits and offsets cannot be used to deliver on these short to medium term targets.

04

Levers for change should be clearly identified and costed with a robust financial plan in place.

05

Supply chain and consumer engagement is key for industries with large scope 3 emissions.

Executive summary

Framework for assessing corporate transition plans

To reach global net zero by 2050, all industries and organisations must transition.

While progress has been made in growing renewable energy infrastructure, reducing reliance on fossil fuels in the energy generation and transport sectors, and propagating energy efficiency measures in buildings, much greater and faster action is needed across all sectors of the economy. Fossil fuel power needs to be rapidly phased out, hard-to-abate industrial sectors such as cement and steel need to be decarbonised, and agriculture and food systems need to be transformed.

Transition plans are key to this process, and every entity, particularly high emitters, should have or be developing a 1.5 degree Paris Agreement-aligned transition plan that is credible and realistic. Unfortunately, recent research from Sustainalytics highlights that very few companies have either developed or started to implement plans to align their operations with 1.5 degrees.[1]

A transition plan is a time-bound and trackable strategy and roadmap presenting the plans and actions for reducing emissions in line with a science-based pathway to net zero.

Accelerated action will depend on developing, implementing, monitoring and updating robust and ambitious transition plans. These plans will enable capital market actors to identify and direct finance to credible investments, driving forward the global transition to net zero. The creation of transition plans also aligns with the EU Corporate Sustainability Reporting Directive (CSRD)which includes requirements for disclosure on environmental improvements*.[2]

However, identifying credible transition plans is not always straightforward as these are complex and comprehensive strategies designed to transform the whole business to deliver on technical environmental performance targets. Therefore, Climate Bonds has expanded its Climate Bonds Standard & Certification Scheme to include the Certification of corporates based on the ambition and robustness of their transition plans. Further information is contained in Climate Bonds Standard Version 4.0 and the associated Checklist.

This paper is designed to provide a complementary and introductory guide to assist stakeholders understand the basic markers of a credible transition plan, however, it cannot replace independent in-depth verification and Certification. This short guidance paper and the requirements for Climate Bonds Certification are both based on the '5 Hallmarks of a credible transition' from our 2022 paper 'Transition for transforming companies: Tools to assess companies' transitions and their SLBs'.

These 5 Hallmarks are captured in the '**Triple A**' framework of *Ambition, Action and Accountability* illustrated below. Together these demonstrate the company is willing, able and transparent about moving toward a sustainable future.

* CSRD (2023) article 19a "*a description of the time-bound targets related to sustainability matters set by the undertaking, including, where appropriate, absolute greenhouse gas emission reduction targets at least for 2030 and 2050, a description of the progress the undertaking has made towards achieving those targets, and a statement of whether the undertaking's targets related to environmental factors are based on conclusive scientific evidence*".

Executive summary

Framework for assessing corporate transition plans

Figure 1: Triple A transition plan framework

AMBITION

- Performance targets

ACTION

- Robust plans
- Action

ACCOUNTABILITY

- Governance
- Verification and disclosure

Hallmarks for transition plans

For transition plans to be credible they need to include time-bound performance targets, implementation and finance plans, and be fully transparent. The 5 Hallmarks provide the framing guidance needed to determine whether a transition plan is sufficiently comprehensive (see Figure 2). The detailed content regarding target ambition and materiality of scopes can be found from additional sources – more information on these is provided below under Hallmark 1.

Information about a company's transition would ideally be contained within a comprehensive document that is publicly available and updated annually. However, often the information is fragmented and can be challenging to both identify and understand. Potential sources of information might include company-wide transition or climate strategy documents, annual corporate sustainability reports, and sustainable finance frameworks, among others.

Third party certification and/or verification of a transition plan, (currently provided by Climate Bonds and Assessing Corporate Transition (ACT) Initiative, among others) is a hugely valuable tool to support corporates in communicating their ambition to stakeholders as well as provide investors with have confidence in the credibility of the plan. Therefore Climate Bonds encourages third party certification for all plans. However, it is necessary for all stakeholders to understand what transition plans should contain and how to find additional related information.

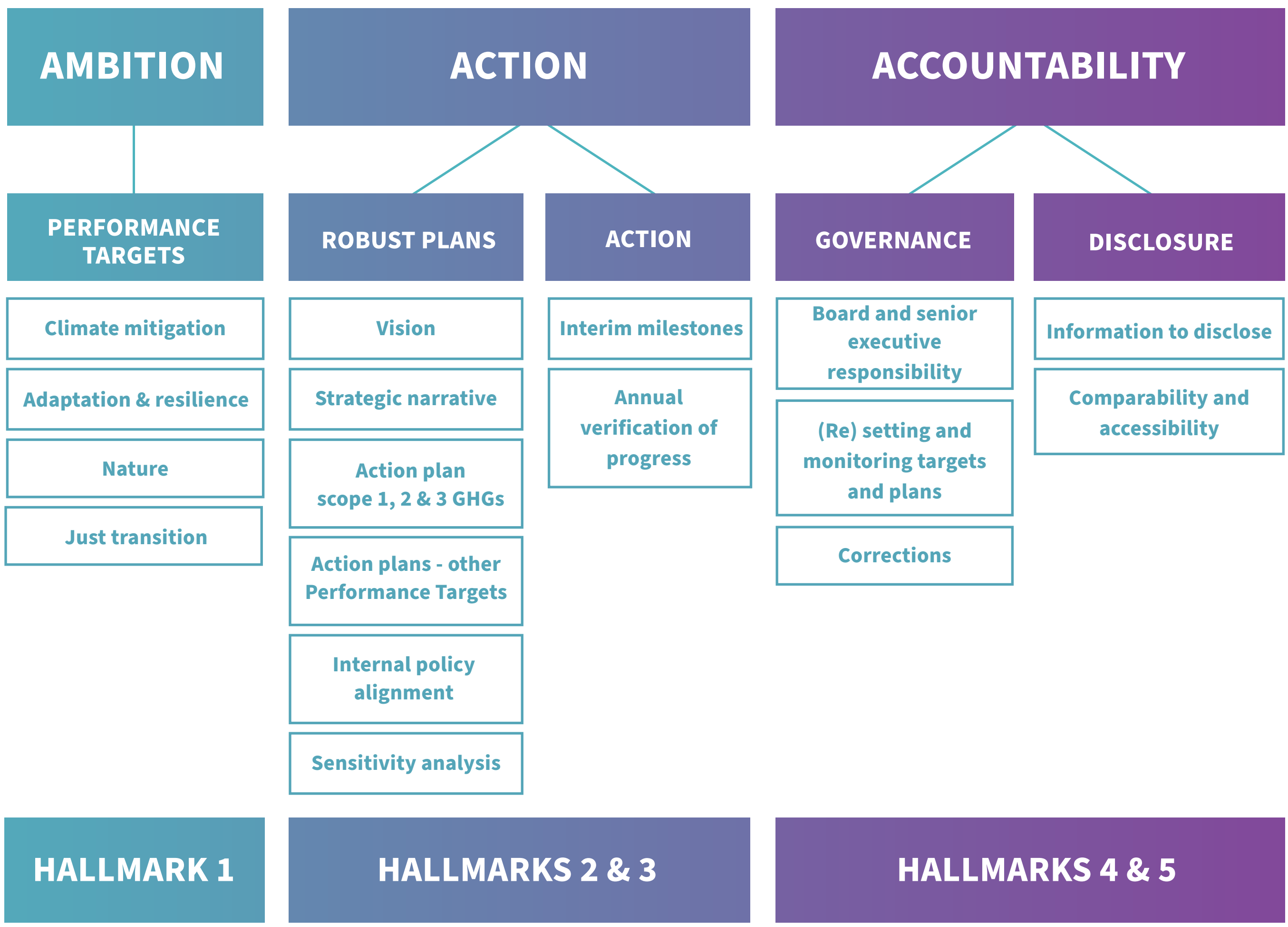
Hallmarks for Transition Plans

Triple A transition plan framework

To provide basic guidance to the market, Climate Bonds has prepared this short overview laying out the high-level requirements of transition plans as defined against the Climate Bonds 5 Hallmarks. These Hallmarks are fully aligned with and build on the thematic guidelines from ICMA as well as the disclosure requirements from the Task Force on Climate-Related Financial Disclosures (TCFD) among others. The key red and green flags for each Hallmark that indicate the credibility of transition plans have been identified. Green flags identify the main elements of a transition plan that should be present while red flags denote omissions or aspects that could be a cause for concern and require greater scrutiny. Each of the five Hallmarks for a credible transition should include information under the headings in Figure 2. Performance targets must include climate mitigation, and should also include other material environmental issues.

The European Sustainability Reporting Standards (ESRS) developed by EFRAG in 2022 to deliver on the Corporate Sustainability Reporting Directive (CSRD) provide a good overview of the types of performance targets that can be considered. The EU Taxonomy is a good additional source of guidance for sustainable activities across multiple sectors. [3,4]

Figure 2: Triple A transition plan framework and five hallmarks (Climate Bonds Initiative, 2021)



Hallmark 1:

Performance Targets

Performance Targets (PTs) set out the goals for positive change (such as the reduction in emissions over time) and should be measurable and material for the entity. These are important for defining credibility and need to cover all the relevant activities of a company as well as propose ambitious change in line with science-based guidance.

Ambitious targets vary by sector and what is considered ambitious can be found in the sector-specific decarbonisation pathway guidance from organisations such as Climate Bonds, Transition Pathway Initiative (TPI) and Science Based Targets initiative (SBTi).

Hallmark 1: Green Flags

1. The company has set performance targets that quantify their environmental goals for the short, medium and long term. In the case of climate mitigation, these performance targets relate to all (scope 1, 2 and 3) material GHG emissions from all of the company's operations that are under the company's control or influence*.[4,5]

Figure 3 below provides a high level overview of the emissions that should be considered for each sector. Any emissions not included in these targets, if they are not material or controllable, are explained and justified.

These targets cover the full time period until the company expects to reach net zero emissions, with interim performance targets specified that enable regular monitoring and reporting of progress.

2. These climate mitigation performance targets align with recognised, science-based sectoral decarbonisation pathways aligned with 1.5 degree global warming scenarios.**

These include criteria established by Climate Bonds, SBTi, TPI, RMI, IEA, ACT Initiative, IPCC, or UTS.[6]

Where sector specific pathways are not available, SBTi's Cross-Sectoral Approach (CSA) or best-in-class comparisons can be used.

However, national plans or Nationally Determined Contributions (NDCs) do not represent the scale of emissions reductions needed to deliver a net zero global economy by 2050 and should not be used.

3. Ideally, the company would have set performance targets addressing for, example biodiversity, adaptation and resilience, pollution prevention and control, and just transition, although guidance on these latter issues is less specific at the time of writing.

Hallmark 1: Red Flags

1. The company's Greenhouse Gas (GHG) performance targets are not front-loaded to the extent that alignment with the selected sectoral decarbonisation pathway(s) will not be achieved in the short- to medium-term. Climate Bonds insists that the company's mitigation performance targets are aligned with the sectoral pathway(s) by 2030 at the latest, in recognition of the need to nearly halve global emissions by 2030.

2. The company's mitigation performance targets are dependent on carbon offsets, which should only be used for 'last mile' or residual emissions that cannot be eliminated by the company and should not exceed 10% of emission reduction efforts.

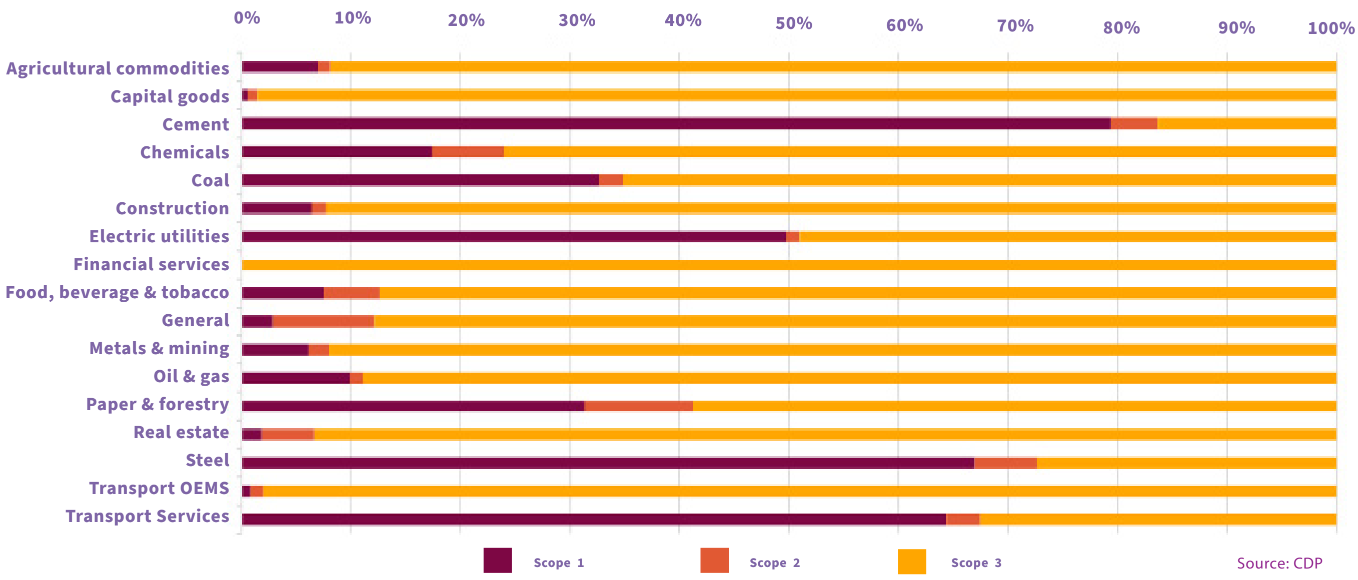
*For example, all scope 3 emissions should be included for Oil & Gas companies, as these can be avoided by the company changing their business operations away from fossil fuels. All material crop production emissions should be included for bread producers as these can be avoided by working with suppliers/changing suppliers to source emissions free inputs.

**These sectoral pathways should not simply reflect a sector average, or best-in-class, but be forward-looking pathways that are technologically feasible and ensure the sector will align with the overall goal of a net zero economy by 2050.

Emissions scope materiality by sector

Figure 3 demonstrates the materiality of emissions scopes by sector. This is high-level and provides an overview only, with further guidance available from CDP and the GHG protocol. Scope 3 is material for most sectors and should be included in transition plans where possible.[7]

Figure 3: Scope 1, 2, and 3 emissions by sector



Source: CDP

How to use transition pathways

Emissions reduction transition pathways chart the annual reductions in GHG emissions needed to align with global carbon budgets. The pathways have been developed by organisations such as Climate Bonds, ACT Initiative, SBTi, University of Technology Sydney, and Transition Pathway Initiative based on the latest available climate science.[8]

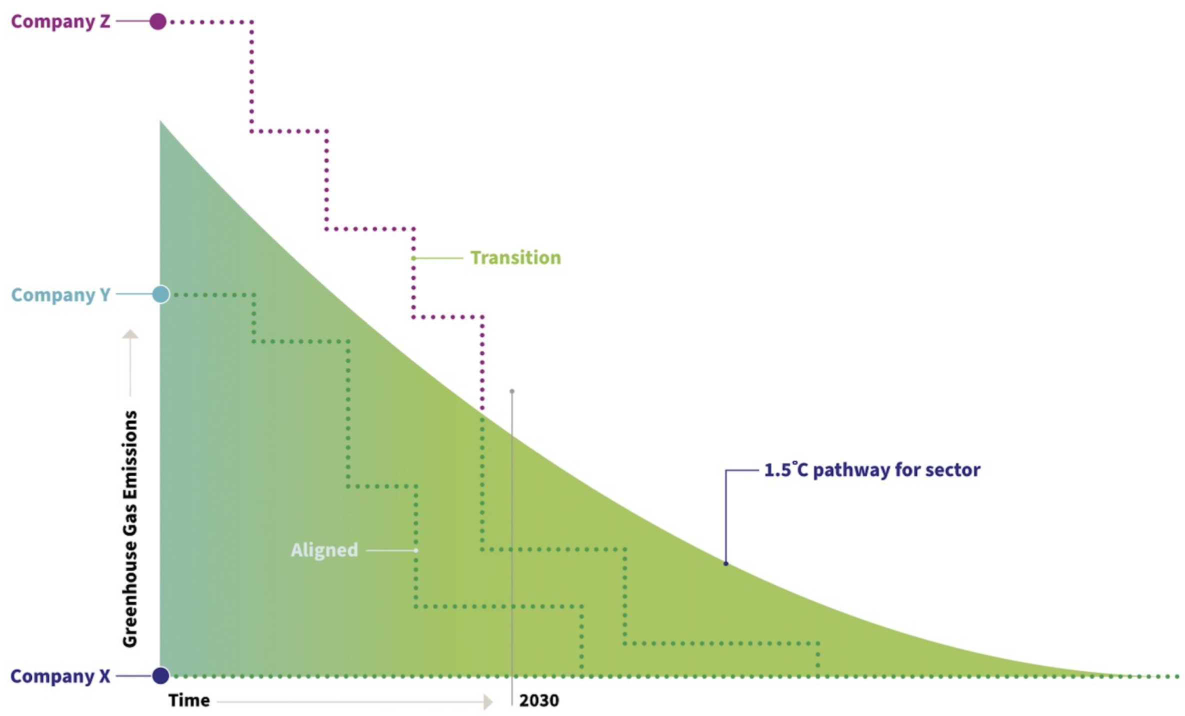
The Science Based Targets Network (SBTN) has also launched science-based targets for nature which can be used to inform transition plan targets on a broader set of metrics.[9]

A transition plan should indicate targets by year (for emissions these can be either absolute emissions or emissions intensity), for example, a reduction of X% from XXX kg/CO_2eq per tonne of product to 500kg/CO_2eq per tonne of product by 2030.

These targets can then be compared against the relevent sector pathway to determine whether the reductions are sufficiently ambitious.

Figure 4 gives an illustration of how a company's decarbonisation can be mapped against a science-based emissions reduction pathway, which must align with the 1.5-degree pathway by 2030 at the latest to be Certifiable by Climate Bonds. This is denoted by **Company Z** in the diagram below. **Company X** and **Company Y** already have emissions below the pathway and could be Certified as aligned.

Figure 4: Example emissions pathway and company alignment (Climate Bonds Initiative)



Hallmark 2:
Robust plans

A company's transition will only be credible if its transition strategy and associated action plans document achievable and trackable milestones detailing how the company will deliver on its selected performance targets.

This transition strategy needs to be fully integrated into the company's wider business model and plans.

Hallmark 2: Green Flags

1. The company has a vision that aligns future activities, assets and business model with the performance targets selected under Hallmark 1, and which identifies the main levers of change that will enable the transition to that vision from their current operations, assets and business model.

2. Any risks to other social and environmental areas such as biodiversity or just transition have been identified and mitigated, and the vision and levers of change are compatible with the company's broader environmental and social objectives, strategies and/or policies.

3. For each lever of change the company has a time-bound plan of the actions the company will take or is taking to implement it. This includes interim milestones and metrics that can be tracked and monitored.

For detailed examples of these please see the Entity Checklist here.

4. All the performance targets identified in Hallmark 1 should also be addressed in the action plan.

5. Any use of carbon credits or avoided emissions are restricted to addressing residual emissions only and are reported separately.

6. The company has a feasible financial plan detailing the financial implications of the transition, in terms of the costs and how it will be financed. The plan also identifies impacts on the overall financial position of the company, including, but not limited to impacts on revenues, costs and balance sheet. The financial plan includes interim milestones and metrics that can be tracked and monitored, using the Entity Certification Checklist for guidance.

7. The company has identified the key sources of uncertainty in any of the plans that are intended to deliver on the vision.

Hallmark 2

Robust plans (continued)

Hallmark 2: Red Flags

1. The vision or associated decarbonisation levers do not address all of the activities of the company. For example, stranded assets and activities that cannot be transitioned and need to be discontinued or phased out; scope 3 supply chain emissions in feedstocks, raw materials, and other inputs that the company has influence over via its supplier relationships; and procurement decisions.

2. Identified levers are not consistent with those of net zero pathways for the sector, claim much greater expected emissions reductions compared to similar measures adopted elsewhere or are not accompanied by strong supporting evidence for their relevance.

3. Identified actions are not concrete, and only vague descriptions are given, such as 'accelerate our transition to cleaner energy solutions', 'modernize our operations' or 'leverage green solutions'.

4. The timing and anticipated emissions reductions of the decarbonisation levers and associated action plans are not compatible with the (interim) performance targets per Hallmark 1.

5. The vision, levers, action plans or finance plan are not consistent with disclosures made in sustainability and wider TCFD reporting.

Supplemental questions:
(For sectors with large scope 3 emissions such as agriculture, food retail or oil and gas).

What supply chain engagement has the entity undertaken to help reduce its upstream/downstream emissions?

Hallmark 3

Action

This Hallmark is dedicated to ensuring that the vision and plans under Hallmarks 1 and 2 are being acted on. Hallmark 3 is a clear action plan that is already being implemented to support the delivery of interim performance targets, with identified metrics and indicators to assess delivery.

Hallmark 3: Green Flags

1. The company is already delivering the interim milestones and metrics identified in its action and financial plans.

2. Where those interim milestones or metrics are not met, the reasons are explained and corrective action is being taken.

3. The action plan is verified and reported on annually.

Hallmark 3: Red Flags

1. Any corrective action is not sufficient to ensure that interim performance targets will be met.

Hallmark 4
Governance

The transition plan and its implementation involve large scale, entity-wide changes. Robust internal governance structures need to be in place to ensure the changes are delivered. Hallmark 4: Governance covers the internal monitoring, accountability mechanisms, and leadership systems needed to drive the transition.

Hallmark 4: Green Flags

1. The Board is responsible for (re)setting and monitoring the delivery of the transition plan (including the performance targets, vision, action plans and finance plan). This includes any changes to the plan to correct for any under-performance or missed milestones, plus a regular reassessment at least every five years to reflect changing operating conditions and market developments such as new technologies coming online sooner than expected.

2. The company has developed the necessary internal governance systems and monitoring mechanisms to enable effective board level oversight.

3. The Board has signed off the performance targets and plans.

Hallmark 4: Red Flags

1. No public commitments to net zero have been made.

2. Any interim performance target or action plan milestone is unmet for a period longer than 12 months.

Hallmark 5

Disclosure

Transparency and external verification are critical for credibility. Disclosure also enables comparability across peers and allows global, national and sector progress to be assessed.

Disclosure should take place annually using recognised, comparable metrics such as absolute or intensity GHG emissions. This should follow the norms required for general purpose financial reporting which obliges disclosure of any information that, if omitted, misstated, or obscured, could impact the statement's reliability.

Hallmark 5: Green Flags

1. The company discloses key information about its performance targets and transition plans when established. Refer to the Climate Bonds Standard and the UK Transition Plan Taskforce recommendations for examples of good practice public disclosure requirements.

2. The company subsequently annually discloses progress against those targets and plans, and any recalibration or corrective action that has been taken in respect of them.

3. The company's transition plan is assessed and audited by an independent third party.

4. The company's GHG emissions are externally verified.

Hallmark 5: Red Flags

1. There is no commitment to annual reporting.

2. Information disclosed is not sufficient to assess progress against performance targets and action plans.

Take home messages

1 Transition plans are core tools to deliver a credible and robust transition to a Paris-aligned future. In order to ensure a transition has the targets, effective plans, financial resources and leadership needed, the transition plan must include the core elements outlined here.

2 Supporting this is the external transparency provided by standardised and regular disclosure of progress against targets. Assessing plans is highly challenging and information will often be unavailable or difficult to piece together from multiple fragmented sources.

3 Third party verification or certification should be used to avoid doubt and provide comfort to investors and other stakeholders that plans are credible.

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Endnotes

1 https://www.sustainalytics.com/esg-news/news-details/2023/04/13/morningstar-sustainalytics-launches-its-low-carbon-transition-ratings

2 https://finance.ec.europa.eu/capital-markets-union-and-financial-markets/company-reporting-and-auditing/company-reporting/corporate-sustainability-reporting_en

3 https://www.efrag.org/lab6

4 https://ghgprotocol.org/calculation-tools

5 https://ghgprotocol.org/calculation-tools

6 Climate Bonds Initiative, Transition Pathway Initiative, SBTi, UTS, ACT Initiative, International Energy Agency

7 https://cdn.cdp.net/cdp-production/cms/guidance_docs/pdfs/000/003/504/original/CDP-technical-note-scope-3-relevance-by-sector.pdf

8 Climate Bonds Initiative, Transition Pathway Initiative, SBTi, UTS, ACT Initiative

9 https://sciencebasedtargetsnetwork.org/how-it-works/the-first-science-based-targets-for-nature/

10 https://www.climatebonds.net/climate-bonds-standard-v4

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