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REGENERATIVE CRISIS RESPONSE COMMITTEE

DEC 20 2021

Mr. Giel Linthorst, Executive Director
Partnership for Carbon Accounting Financials (PCAF)

Dr. Nate Aden, Sector Manager, Finance
Science Based Targets Initiative (SBTi)

RE: CONSULTATION ON PCAF AND SBTI NET-ZERO METHODOLOGIES

Dear Mr. Linthorst and Dr. Aden,

We appreciate the opportunity to participate in public consultations for both the Partnership for Carbon Accounting Financials (PCAF) draft new methods for public consultation[1] and the Science Based Targets Initiative (SBTi) Foundations for Science-Based Net-Zero Target Setting in the Financial Sector: Draft for Public Comment.[2] While we understand your efforts are managed separately, with PCAF focused on greenhouse gas accounting fundamentals and SBTi focused on standards for net-zero commitments, we thought it was important to share feedback on how these two critical pieces fit together.

For context, CarbonPlan is a nonprofit research organization dedicated to improving the transparency and scientific integrity of carbon removal and climate solutions through open data and tools. CarbonPlan has extensive experience with the design and operation of carbon markets, including research on the standards used in and the performance of voluntary markets. The Regenerative Crisis Response Committee (RCRC) is a nonpartisan group of 10 senior leaders from the banking, financial services, regulatory, and policy arenas who are committed to ensuring the United States' economic recovery is durable, equitable, and on a path toward lasting sustainability. Founded in late 2020, the RCRC works to identify, compare, and recommend changes in fiscal, monetary, and financial regulatory policies that are likely to enable the United States to achieve net carbon neutrality before 2050.

Our comments today focus on the use of carbon offsets in financial disclosures and net-zero accounting frameworks. In our view, net-zero climate targets require clear and consistent

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1 Partnership for Carbon Accounting Financials, PCAF's draft new methods for public consultation (Nov. 2021) (hereinafter "PCAF draft methods).

2 Science Based Targets Initiative, Foundations for Science-Based Net-Zero Target Setting in the Financial Sector: Draft for Public Comment (Nov. 2021) (hereinafter "SBTi white paper").

distinctions between emissions, credits for avoided emissions, and carbon removals.[3] As both of your organizations appreciate, there is a world of difference between a climate strategy that relies primarily on internal emissions reductions versus one that relies on external offsets. It is critical that reporting standards make these differences obvious, too.

We recognize the important efforts both PCAF and SBTi have made to incorporate these concepts into your respective frameworks, and believe your efforts will significantly improve private-sector net-zero governance. As detailed below, however, we also see some early signs that suggest the distinction between reducing internal emissions and using external offsets could end up muddied in practice. We urge both of your organizations to prioritize requirements that maintain clear distinctions between organizations that are cutting their own emissions and those that are relying on conventional offsets to claim carbon neutrality.

PCAF draft new methods for public consultation

In clearly separating portfolio companies' gross emissions from their emissions removals,[4] PCAF's draft standard lays the necessary accounting foundation for tracking net-zero targets. Reporting all gross emissions allows for objective validation of net calculations made by portfolio companies, while also enabling net values to be reported according to whatever standards or methods a company might choose. We commend PCAF for requiring the separate accounting of carbon credits, emissions removals, and direct emissions across scopes 1, 2, and 3.

We also appreciate that PCAF proposes to differentiate between credits for avoided emissions and carbon removal.[5] Accounting standards must distinguish between these types of credits because, as SBTi and others have noted, net-zero policies require carbon removal to compensate for unabated residual emissions. In contrast, the bulk of today's voluntary carbon offsets market does not distinguish between credits for avoided emissions and carbon removal. We encourage PCAF to make explicit the need for voluntary carbon markets to differentiate between avoided emissions and carbon removal in order for the reporting to illuminate more precisely a particular firm's climate strategy.

In order to further support a comprehensive baseline for net-zero accounting, we also suggest that PCAF consider two additional components in its reporting requirements. First, we suggest PCAF include a yes-or-no question to identify whether companies and assets are covered by a net-zero commitment. Second, PCAF could also require any affirmative answers to indicate the

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3 Sadie Frank and Danny Cullenward, Climate-related financial risk and corporate net-zero commitments, CarbonPlan (Nov. 1, 2021).

4 See PCAF draft methods at 33.

5 PCAF draft methods at 32 and 34.

applicable standard (for example, an SBTi standard or a corporate document articulating a bespoke approach).

Requiring this additional reporting would enable financial institutions to track the proportion of companies and assets aligned with net-zero goals, and would support transparency and validation across reporting locations. It would also impose negligible compliance burdens, as any asset or company subject to a net-zero standard should easily be able to identify the specific standard adopted. (Those without a commitment need only answer "no.")

SBTi Foundations for Science-Based Net-Zero Target Setting in the Financial Sector: Draft for Public Comment

We are also pleased to see SBTi exclude conventional offsets from use against net-zero targets in both the corporate standard[6] and the draft financial sector white paper.[7] From a technical perspective, SBTi's "neutralization" approach — which requires firms to prioritize steep near-term emissions reductions in line with the Paris Agreement without using offsets, and which also requires carbon removal for residual, hard-to-abate emissions — is consistent with science-based definitions of net zero. We applaud this position and encourage SBTi to maintain its "precautionary approach on the sequestration and storage of atmospheric carbon."[8]

Although we commend the technical rigor of SBTi's net-zero standard, we believe the success of this approach depends not just on the details, but also on sending a consistent message about the role of carbon offsets to the broader corporate and investment community. For this reason, we are also concerned that SBTi's "beyond the value chain mitigation" framework creates more confusion than clarity for practitioners. This prominent component of the SBTi corporate net-zero standard recommends that companies invest in additional activities to reduce emissions outside of their own supply chains, such as through the purchase of conventional carbon offsets in the forestry sector. These actions do not count toward companies' required emission reductions nor as a compensatory measure for unabated residual emissions, but SBTi repeatedly emphasizes this extra step.[9]

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[6] SBTi, Corporate Net-Zero Standard (Oct. 2021).

[7] SBTi white paper at 38.

[8] SBTi, SBTi-FI Foundation Paper for Net-Zero for Financial Institutions: Public Consultation Survey (Nov. 2021)

[9] SBTi white paper at 39 ("Beyond value chain mitigation cannot be used to meet net-zero target (i.e., cannot be used to claim net-zero), but is *strongly* encouraged as an optional and supplementary action in the transition to net-zero.") (emphasis in original).

Although we wholeheartedly support efforts to fund critical forest and ecosystem protections, we worry that this language conflates participation in the conventional offsets market (which primarily supports avoided emissions credits) with SBTi compliance efforts (which preclude the use of avoided emission credits while providing a limited role for carbon removal credits).

Unfortunately, it appears these concerns are manifesting in practice. For example, recent business reporting on the SBTi net-zero standard suggests it has given the "seal of approval to targets that rely on carbon offsets — paying for services such as tree-planting that remove carbon dioxide from the atmosphere."[10] Although that phrasing is technically accurate with respect to carbon removal's limited role in SBTi's net-zero standard, the take-away message regarding a "seal of approval" for offsets reflects the confusing semantics of what counts toward a net-zero target.[11] Meanwhile, offset industry commentary on the standard demonstrates a lack of clarity regarding the appropriateness of offsets for net-zero targets, emphasizing the centrality of conventional carbon offsets as a "beyond the value chain" mitigation strategy.[12]

While SBTi is not responsible for every article that is written about its standard, the mixed messages received in the business press and promoted by offset developers advertising their partnership[13] with SBTi demonstrates the need for greater clarity going forward. This is all the more important as SBTi expands its guidance to new sectors, particularly powerful actors in the financial sector, and potentially includes new terminology to describe offset-related concepts.[14]

We recognize that unintentional ambiguity or misunderstanding can result from the development of complex, novel standards — especially those that, like SBTi's, aim to raise the bar. Our intention in highlighting areas of potential confusion is not to nitpick SBTi's approach, but rather to call attention to how the standard is being described among the constituencies SBTi hopes to influence. We have no doubt SBTi means to do its job well, just as we have no

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[10] Ed Ballard and Dieter Holger, Rush of 'Science-Based' Climate Pledges Puts Pressure on Group That Checks Them, *The Wall Street Journal* (Nov. 11, 2021).

[11] *Id*. ("Some companies … as well as operators of carbon markets[] wanted offsets to play a bigger role, [SBTi co-founder and managing director Albert Carillo] Pineda said. 'All of these voices come through our process, and we have to manage all of that,' he said.")

[12] Denis Jorisch and Maria Carvalho, Why companies should care about the SBTi's new science-based net zero standard, South Pole (Nov. 3, 2021).

[13] Specifically, South Pole lists SBTi as a "partner" and uses SBTi's logo on its website. *Id*.

[14] We also understand that forthcoming SBTi guidance for companies in the forest and agricultural sectors could follow separate rules, which could potentially include changes to the allowed use of carbon offsets.

doubt that stakeholders with a financial interest in the status quo offsets model will look to exploit any ambiguities in their favor.

Finally, we encourage greater clarity around the limited use of carbon offsets not just to emphasize the need for ambitious pollution reductions as the core of any climate strategy, but also to properly support the development of permanent carbon removal in the decades ahead. As noted above, the voluntary offsets markets generally do not track the distinction between avoided emissions and carbon removal credits. Most of the credits they generate come from projects that primarily avoid emissions[15] — that is, those that are inconsistent with net-zero targets. Early movers in corporate carbon removal procurement have recognized that permanent carbon removal supply is "tiny" compared to what is needed for global net-zero compliance.[16] We urge SBTi to make sure that corporations and financial institutions following its standards recognize that today's offset markets do little to support the future need for permanent carbon removal, and avoid conflating efforts to grow these markets with the purchase of conventional offsets today.

We thank both PCAF and SBTi for the opportunity to comment on their consultations.

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15 Taskforce on Scaling Voluntary Carbon Markets, Taskforce on Scaling Voluntary Carbon Markets - final report (Jan. 2021) at 130.

16 Lucas Joppa et al. (2021), Microsoft's million-tonne CO2-removal purchase — lessons for net zero *Nature* 597: 629-632.