25.09.20

THE INVESTMENT ASSOCIATION

Investment Association Response to IIGCC Consultation on Net Zero Investment Framework

Setting Portfolio Targets, Objectives and Reporting

1. Do you agree with the combination of targets that are proposed to guide investor alignment with net zero global emissions by 2050?

Yes/ No/ Unsure

The IA welcomes a combination of targets (bottom up and top down; short-term and medium-term) to set the direction and ambition for a net zero investment strategy. We agree that a combination of aligned, transition and solutions objectives is sensible and more likely to achieve the outcome of emissions reduction in the real economy.

We note however that while asset owners may be free to adopt any and all targets, this would not necessarily be the case for investment managers. As you rightly point out in the consultation: Large multi-client asset managers, which operate a variety of mandates, may not be free to adopt alignment strategies or policies covering all of the assets under their management. The extent to which Paris aligned investment opportunities can be provided will depend on asset owner demand for segregated mandates or pooled funds that fit the Paris aligned model. We would echo this and say that in certain cases, for example, increasing the AUM invested in net zero or aligned assets, investment managers' ability to achieve targets is likely to be contingent on mandates from asset owners.

2. Do you agree that targets should incentivise an investor's contribution to emissions reduction in the real economy by including a main focus on the alignment of underlying assets?

Yes/ No/ Unsure

Targets that incentivise an investor's contribution in the real economy by including a main focus on the alignment of underlying assets is a core strategy to deliver on the net zero commitment.

However, there are still significant concerns around the availability of data for all underlying assets. This should be acknowledged and taken account of when setting targets.

3. What threshold for % of portfolio emissions in material sectors to be net zero aligned or subject of engagement do you consider to be feasible to achieve while achieving a sufficiently ambitious level of action?
____% (?)

It is our view that it would be more meaningful to differentiate between the threshold for % of portfolio emissions that are net zero aligned and those that are to be the subject of engagement. The former is predominantly contingent on the actions and commitments of companies whereas the latter is something an investment manager has within its control. Should these two numbers be used, we would further expect that the engagement target % should be higher - at least in the first instance - than the net zero aligned.

If just one number were to be used as the threshold for % of portfolio emissions, such a number would need to be reviewed on an annual basis as practices and methodologies evolve.

4a. Do you currently use a methodology for calculating avoided emissions or relative impact of investment in climate solutions?

Yes/ **No**

4b. Do you currently use a methodology for calculating aggregating emissions reduced by underlying assets at the portfolio level?

Yes/ **No**

Strategic Asset Allocation

5. For funds that do not use Strategic Asset Allocation, are the actions set out in the Framework transferable to your equivalent process (e.g. Total Portfolio Approach)?

Yes/ No/ **Unsure**

Our members would welcome detail around how the steps outlined in 2.4.1 would be transferable to a 'Total portfolio approach' and what this would entail. Specifically, they would welcome examples and case studies in the implementation guidance.

6. If not, what alternative approaches can be applied to support alignment through that process, that should be referenced in this framework?

[No response]

7. Do you agree that investors should aim to increase the contribution towards decarbonization and investment in climate solutions to the maximum extent possible even if that constitutes more than a 'fair' share distributed among investors?

Yes/ No/ **Unsure**

We support the increased allocation to climate solutions and indeed broadly agree that investors should aim to increase the contribution towards decarbonization and investment in climate solutions to the maximum extent possible.

The extent to which this will be possible however will differ for different actors. For investment managers, the extent to which we can increase this contribution will necessarily be constrained by our duties to act in the best interests of clients. At the heart of this responsibility is delivering on our clients' objectives and the generation of long-term sustainable returns. Any strategic asset allocation will therefore need to be aligned with the goals, risk tolerance, time horizon and investment objectives of our end client and therefore we agree with the statement 'to the maximum extent possible' in this context.

Listed Equity and Corporate Fixed Income

8. Given the large number of assets in a portfolio, and the need to provide a practicable approach for investors, are high impact NACE (and associated BICS/GICS) codes the best option to define the relevant scope for alignment for listed equity and corporate fixed income portfolios?

Yes/ No/ **Unsure**

We welcome efforts to alleviate the significant data and due diligence challenges that stem from asset owners' and investment managers' company-level assessments of the many thousands of individual assets that they may hold in listed equity and corporate fixed income portfolios. In the absence of a suitable alternative – we consider NACE codes to be a reasonable starting point. However, the IA is unsure as to whether high impact NACE codes are the best option from the perspective of proportionality or practicality, and whether their adoption may limit the scope for portfolio alignment. We understand from our member firms that not all firms use NACE classifications and to adopt these may involve additional cost.

If not, what alternatives could be used?
n/a

We do not have a suitable alternative to suggest at this time.

9. Do you agree that divestment should not be the standalone strategy for achieving the portfolio emissions reduction target, and increasing % of aligned assets?

Yes/ No/ Unsure

We wholeheartedly agree that divestment should not be the standalone strategy for achieving the portfolio emissions reduction target and that a broad range of strategies should be welcomed. Engagement as well as access to capital for companies developing new technology solutions are also key levers to drive change within portfolios.

10. Do you agree with the thresholds for a company to be considered net zero; aligned to a net zero pathway; transition potential?

Yes/ No/ **Unsure**

Challenges remain around determining the extent to which the emissions intensity of a company is in the line a net zero 2050 target as this relies heavily on obtaining requisite data from the company itself.

Given data concerns, in the first instance, signatories should not be required to 'tick every box'. Instead, they should use the list as a guide to assess whether information is available to make a determination that the company meets enough of the different thresholds to qualify.

11. Are there methodologies in the market, other than those specified in the Framework, that provide robust assessments of one or more of the criteria for assessing alignment and should be recommended for use by investors through this framework?

Yes/ **No**/ Unsure

None that we are aware of.

Application of the framework by Asset Managers

12. Does Box 4 sufficiently describe how asset managers can apply the Framework?

Yes/ No/ Unsure

The paper appropriately summarises investment managers' various business models and formats. We are broadly supportive of the notion that investment managers can adopt the long-term objective of aligning assets under management and investment strategies to the goal of achieving global net zero emissions by 2050, as proposed in Box 4.

Whilst we support the spirit of this broad objective, we would like to point out that the debate around what it really means for an investment manager to adopt a long-term objective to align its AUM and investment strategies to achieving this goal is very much a live one. It is not yet clear exactly what this means in practice, particularly given instances where multi-managers are serving many different clients with different needs and goals. We will be continuing to explore more closely what this means in practice and how investment managers of all business models could pursue such an objective in a meaningful and demonstrable way.

We also welcome the consultation's acknowledgment that certain aspects of the Framework could be applied across the whole business, for example, policy advocacy, whilst others will necessarily be fund- or mandate-specific. This reflects the differences in different clients' goals and objectives, for which it is important investment managers retain the flexibility to deliver on.

Our members continue to develop and bring to market new sustainable products and this Framework is a helpful tool to help deliver net zero alignment in such products. By contrast, whilst a helpful tool for new products, we would like to flag that there are likely to be significant difficulties in retrospectively applying this approach to existing products.

With respect to educating clients, a key part of industry's collective work this year has been to improve communication of sustainable and responsible investment characteristics of funds to investors – a key component of empowering clients to make informed choices.

13. What further detail or 'use cases' are needed to enable asset managers to utilise the Framework?
[Open ended]

In order to make the application of the framework by asset managers even more clear and pertinent, we would recommend further analysis, outreach and consideration of the following areas:

1. Outreach to the wholesale investment adviser market (discretionary and advisory) on non-pension and pension investments to consult their views and further the ultimate objective of aligning investment portfolios to the goals of the Paris Agreement.
2. Even more of a focus on empowering retail investors to make informed choices through the provision of further education.
3. Develop more explicit links to current and incoming disclosure regulations, in particular, reference to Article 8 and 9 funds under the EU Sustainable Finance Disclosure Regulation.
4. Utilize the IA Responsible Investment framework to explain how carbon/climate solutions strategies can be embedded at firm level and fund level.

In addition, we would urge caution on providing too much more implementation detail at this stage – but rather provide case studies on how firm are implementing elements of the framework already.

Emissions Accounting and Offsetting

14. Do you agree with the approach taken to emissions accounting described in Annex 1?

Yes/ no/ unsure

Yes, we agree. In particular, we are supportive of the stated objective that emissions accounting for the purposes of alignment does not have an objective of apportioning responsibility for emissions or assessing distribution among investors but rather that its purpose to "track the trajectory of emissions associated with a portfolio overall towards next zero".

Having made its intention plain, the approach to assess Scope 1 and 2 in the first phase and to move to Scope 3 in Phase II seems sensible and proportionate.

Furthermore, we agree that offsetting both externally or internally within portfolios should be discouraged and that offsets should not be used to meet emission reductions targets. We also agree that decarbonisation and avoided emissions should be addressed separately.

Emissions accounting is a key area and we believe that reporting on the targets and achievements in the different categories with the recommended metrics should encourage transparency. The PCAF initiative is a worth further consideration.

15. Should the Framework provide a specific recommendation(s) on accounting methodologies to be applied by investors e.g. for re-baselining emissions intensity targets?

Yes/ No/ Unsure

Yes, unless other initiatives, standard setters or protocols will be doing this.

General Feedback

In addition to the 15 questions set out in the consultation, we also welcome more general comments on the Framework. Please use the space below to provide your feedback.

The IA supports the IIGCC's Net Zero Investment Framework and acknowledges the significance that it holds for industry and wider society.

It would indeed be very useful for industry to coalesce around one framework that establishes the foundations for transitioning to net zero and we are particularly supportive of the IICGC's overarching goal to deliver on both real world emissions reductions and increase investment in climate solutions. We are particularly supportive of IIGCC's efforts to differentiate between the role of investment managers and asset owners, and the importance placed on each playing its specific role effectively.

We have encouraged our members to respond to the consultation directly, as their commercial and individual insights will be best placed to provide comprehensive feedback to the actions, metrics, targets and methodologies proposed.

From a collective investment management point of view, most notable are the challenges around:

- The extent to which firms would be able to adopt the framework across the whole house or a specific portfolio/asset class.
- The framework needs to acknowledge that the current data is imperfect and evolving. Very extensive data is required to make the proposed assessments. Firms with more limited resources may not be able to provide the level of detail required.
- Greater focus on the retail client is needed from the onset, including education.
- The framework needs to explicitly incorporate other established / adopted initiatives such as TCFD, the EU taxonomy and the FCA/ PRA's CFRF guidance.
- Finally, as the IIGCC moves into Phase II and expands the work to provide guidance and capture other asset classes, numerical based examples and case studies on what the targets and metrics would look like from a portfolio perspective should be developed.