CERB
Centre of
Excellence in
Responsible Business
THE PAKISTAN BUSINESS COUNCIL
(A Company set up under Section 42 of the Companies Ordinance 1984)

FINANCED EMISSIONS CALCULATIONS

Nazish Shekha
Head of Initiative
Centre of Excellence in Responsible Business

BACKGROUND

IFRS S2 requires an entity to disclose :

- Information about climate-related risks and opportunities that could reasonably be expected to affect the entity's cash flows

- Disclose its absolute gross greenhouse gas emissions generated during the reporting period, expressed as metric tonnes of CO2 equivalent, classified as scope 1, 2 and 3 greenhouse gas emissions (including financed emissions)

- Its access to finance or cost of capital over the short, medium or long term (collectively referred to as 'climate-related risks and opportunities that could reasonably be expected to affect the entity's prospects').

BACKGROUND

- **IFRS S2 requires an entity to disclose :**

- Measure its greenhouse gas emissions in accordance with the *Greenhouse Gas Protocol: A Corporate Accounting and Reporting Standard (2004)* unless required by a jurisdictional authority or an exchange on which the entity is listed to use a different method for measuring its greenhouse gas emissions

- In particular for Scope 3 greenhouse gas emissions, disclose:

1. The categories included within the entity's measure of Scope 3 greenhouse gas emissions, in accordance with the Scope 3 categories described in the *Greenhouse Gas Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard (2011)*;

2. Additional information about the entity's Category 15 greenhouse gas emissions or those associated with its investments (financed emissions), if the entity's activities include asset management, commercial banking or insurance;

SCOPE 1, 2 AND 3 EMISSIONS

Scope 1:

Direct GHG emissions that occur from sources owned or controlled by the reporting company:

i.e., emissions from combustion in owned or controlled boilers, furnaces, vehicles, etc.

Scope 2:

Indirect GHG emissions from the generation of purchased or acquired electricity, steam, heating, or cooling consumed by the reporting company.

Scope 2 emissions physically occur at the facility where the electricity, steam, heating, or cooling is generated.

Scope 3:

All other indirect GHG emissions (not included in Scope 2) that occur in the value chain of the reporting company.

Scope 3 can be broken down into:
1. **Upstream** emissions that occur in the supply chain (for example, from production or extraction of purchased materials)
2. **Downstream** emissions that occur as a consequence of using the organization’s products or services.

GHG PROTOCOL(SCOPE 3)

- The GHG Protocol Corporate Value Chain (Scope 3) Accounting and Reporting Standard categorizes scope 3 emissions into 15 categories:

Which are listed in Figure 2-1, the emissions resulting from a reporting company's loans and investments fall under Scope 3 downstream emissions, more precisely under Scope 3 category 15 (investments).

FINANCED EMISSIONS

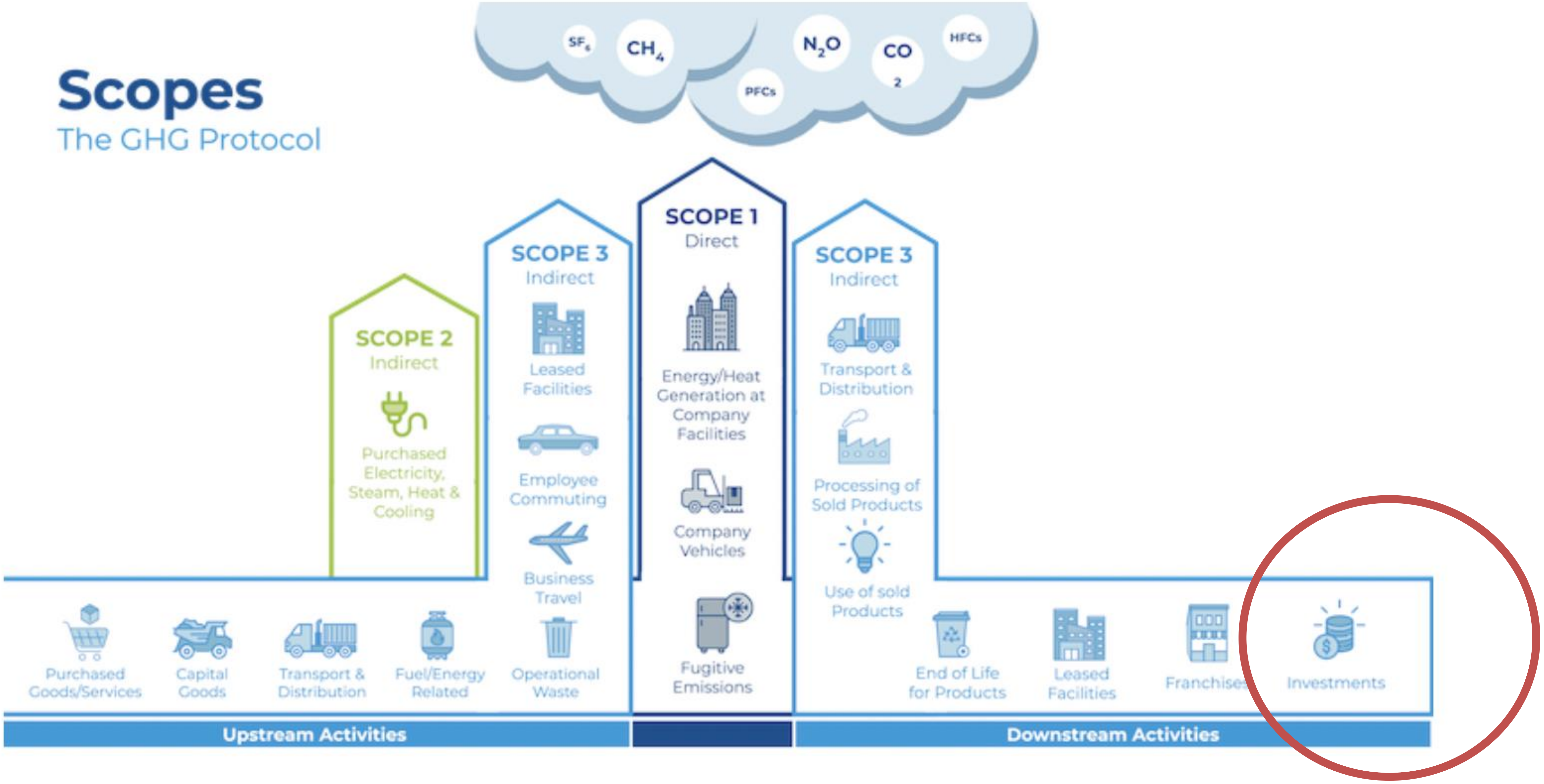
- In addition to managing greenhouse gas (GHG) emissions created from their day-to-day activities, financial institutions are also accountable for financed emissions. These are the emissions related to loans, underwriting, investments, and other financial services.

- Financed emissions are emissions generated as a result of financial services, investments, and lending by investors and companies that provide financial services. They fall under scope 3, category 15 from the Greenhouse Gas Protocol (GHGP).

A Paris Agreement aim is “making finance flows consistent with low GHG emissions and a climate-resilient pathway." Financial institutions and investors play a major role since they currently provide significant funding for fossil fuels and other high-emissions industries.

Scopes

The GHG Protocol



ACCOUNTABILITY

According to the Carbon Disclosure Project's (CDP) The Time to Green Finance report, financed emissions account for 700 times more than a financial institution's directly generated emissions.

PCAF'S SIX ASSET CLASSES

PCAF has developed a standard for six asset classes

GENERAL APPROACH TO FINANCED EMISSIONS CALCULATION

Understand and analyze scope

Identify and evaluate which of your asset classes will be included, as well as the industries and geographies your customers, or counterparties, operate in.

Develop a transparent set of assumptions

Main assumptions

- Operational approach
- Equity Share Approach
- Financial Approach

Source the available data.

Gathering the data you need to perform your calculations starts by engaging with clients. But you will also need to evaluate available third-party data consolidators and build proxy assumptions to fill data gaps.

Calculate emissions

Percentage share of the financing of the business or project and assume an equal-share responsibility for the resulting GHG emissions from the business or project.

Note: There is a standard equation for calculating financed emissions

BASIC PREMISE OF CALCULATING FINANCED EMISSIONS

$$\text{Financed emissions} = \sum_i \text{Attribution factor}_i \times \text{Emissions}_i$$

(with i = borrower or investee)

$$\text{Attribution factor}_i = \frac{\text{Outstanding amount}_i}{\text{Total equity + debt}_i}$$

Financed emissions = Attribution Factor X Scope 1 & 2 Emission Per Loan or Investment

Attribution Factor = % Share of Loan or Investment (e.g., Total Loan / Total Debt + Equity)

GENERAL APPROACH TO FINANCED EMISSIONS CALCULATION

Source: The Partnership for Carbon Accounting Financials (PCAF)

CHALLENGES

The World Resources Institute's (WRI) Banking Beyond Climate Commitments paper highlighted the following challenges:

- Lots of time, money, and resources are needed to assess and develop needed data
- Lack of standardized legislation, policies, methodologies, and tools when measuring impact
- Scrutiny over the additionality and fungibility of green bonds
- Limitations from governments and financial regulators that hinder the progress of Paris-aligned decision-making
- Firms' participation in greenwashing as a result of difficulty creating standards that apply to all sectors