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Introduction

45% reduction in carbon emissions by 2030; ‘net-zero’ by 2050. That’s the assessment of the Intergovernmental Panel on Climate Change (IPCC) of what’s needed for us to have a chance of limiting global warming to 1.5°C – the aim of the 2015 Paris Agreement.\footnote{1} And so ‘net-zero’ - a pledge to balance any further emissions with removal of equivalent carbon from the atmosphere - has become a key buzzword in the global fight to limit climate change.

This has led to a flood of net-zero promises across all levels of the economy. The UK has set a legally binding commitment to reduce emissions to net-zero by 2050. Globally, national net-zero targets now cover 85% of the world’s population and 88% of emissions, with 683 of the 2,000 largest publicly traded companies following suit.\footnote{2} In the finance sector, the prominent Glasgow Financial Alliance for Net Zero (GFANZ) initiative now includes over 450 financial institutions controlling over USD $130 trillion of assets across 45 countries.\footnote{3}

But promises are not enough; they need to be matched with clear, measurable, and effective emission reduction targets and action plans to ensure that net-zero commitments will be met in practice. \textit{And in this, many companies – and investors – are falling short.}

Implemented successfully, net-zero commitments by financial institutions have the potential to be a key tool to drive decarbonisation throughout the wider economy through stewardship and reallocating capital in line with the global transition. But implement them badly and the financial sector may continue to play a key role in financing - and thus enabling – the biggest carbon emitters.

Asset owners have a role to play here. As providers of capital, asset owners are in a position to monitor net-zero commitments by asset managers and banks - and hold them to account where those commitments are falling short. Against this backdrop, this briefing provides a non-technical overview of the net-zero landscape for asset owners to empower them to hold their financial service providers to account on their net-zero commitments.

Section 2 provides an overview of the net-zero landscape and key initiatives, with a focus on the prominent Net Zero Asset Manager Initiative (NZAM) and Net Zero Banking Alliance (NZBA). Section 3 provides a summary of key considerations in setting effective net-zero promises. Finally, section 4 provides some tips on how asset owners can engage with their financial service providers to increase net-zero ambitions.
The net-zero landscape
The net-zero landscape

Understanding the carbon impact of a company goes beyond insulating buildings and offsetting staff travel; it means understanding the full extent of emissions generated by an organisation’s upstream and downstream activities throughout the value chain. For banks and insurers, this means taking account of the impact of lending and underwriting activities. For allocators of equity and corporate debt, this means understanding the emissions and environmental impact of portfolio companies. For asset owners, this means recognising what their capital is ultimately financing. This can be a complex undertaking.

Various emission measurement and target-setting initiatives have been launched to help financial institutions navigate this space. However, the sheer number of initiatives – and in some cases, overlapping remits - can be confusing for those new to the space. Below, we highlight some of the different types of initiatives relevant to the financial sector, although many initiatives involve activity across multiple spheres of activity.¹

Some initiatives focus on setting a target, by providing a methodology or verification process to assess the extent and speed of necessary emissions reductions.¹ The most prominent of these is the Science-Based Targets Initiative (SBTi), which provides verification of company net-zero commitments to assess whether they are in line with the Paris Agreement. Some organisations have developed their own methodology (for example, Barclays has created its own in-house methodology to measure and track emissions) or use combinations of open-source methodologies based on perceived strengths and gaps.

Some initiatives provide methods for measuring emissions, which underpin a target. This includes the Partnership for Carbon Accounting Financials (PCAF), a standard for financial institutions to measure emissions across key asset classes, including equities, loans, corporate bonds, real estate, and project finance; and the Paris Agreement Capital Transition Assessment (PACTA), an open-source tool developed by the 2º Investing Initiative (2DII) for asset managers to use to measure the alignment of financial portfolios against various scenarios.

Some initiatives focus on public reporting. These may focus purely on emissions, such as the Carbon Disclosure Project (CDP), a platform for reporting on environmental impact; or have a wider focus to encompass public target-setting and reporting on progress. The most prominent among these are the GFANZ alliances, which require signatories to set a net-zero target and report on progress. At present this includes distinct alliances for asset managers; banks; asset owners; insurance; financial service providers (including ratings agencies and auditors); and investment consultants.

In addition, some initiatives set out to **align an institutions’ wider activities** with an emission reduction goal. These include, for example, Climate Action 100+ (CA100+), a group of investors which aim to undertake coordinated engagement with specific target companies on emission reductions.

Throughout this brief, we focus on two GFANZ initiatives, as key platforms for net-zero commitments by asset owners’ financial service providers:

**Net Zero Asset Manager Initiative (NZAM)**

The Net Zero Asset Manager Initiative (NZAM) was launched in December 2020 to provide a framework for asset managers’ net-zero commitments. It has quickly risen to become one of the most prominent climate signatory initiatives, with 236 signatories representing over USD 57.5 trillion in AUM between them as of February 2022. The pledge requires signatories to set a target for all assets under management (AUM) to be net-zero by 2050 at the latest, with interim targets set and reviewed every five years.

Importantly, the initiative has also demonstrated willingness to adapt – for example, by introducing post-signature expectations in relation to fossil fuels – which makes it a potentially useful tool for increasing the ambition of signatories.

**Net Zero Banking Alliance (NZBA)**

The Net Zero Banking Alliance (NZBA) was launched in April 2021 as part of the GFANZ initiative. It covers over 100 banks in 40 countries as of February 2022.

Signatories pledge to align operational and attributable GHG emissions from lending and investment portfolios with net-zero by 2050, with interim targets set for 2030 and every subsequent 5 years.

The scale of NZBA – covering 43% of global banking assets at the time of writing – makes this an important platform from which to encourage net-zero ambition. Like the NZAM, the NZBA also has a built-in mechanism for targets to evolve, with the first revision expected by April 2024 (albeit subject to approval by two-thirds of signatories) – providing an opportunity to increase ambition for existing signatories, albeit significantly late.
What does a credible net-zero commitment look like?
What does a credible net-zero commitment look like?

Time is short. Net-zero commitments need to be more than just vague promises – they need to be credible, realistic, and aligned with up-to-date climate science. However, understanding the technical aspects of a target – and so assessing the strength or ambition of a financial institution’s commitment – can be difficult.

Below, we set out some of the key considerations when thinking about the strength of a financial institution’s net-zero commitment.

Scope: what does the net-zero commitment actually cover?

Understanding the scope of a net-zero commitment – what is covered, or not covered by a target – is critical for understanding how ambitious a net-zero commitment truly is.

A key part of assessing the scope is identifying which assets or activities are covered by the commitment. For asset managers, this means understanding whether any assets under management or asset types are excluded from a target, and if so, the reasoning for the omission and whether high-emitting sectors may consequently be excluded. For banks, this means ensuring that targets don’t just cover loans, but also all relevant financial services for the bank in question, including capital markets activities.

It is also important to understand what emissions from those assets are actually being counted. The Greenhouse Gas (GHG) protocol\(^a\) – the foremost accounting standard used to measure emissions – categorises emissions into three different ‘scopes’:

- **Scope 1** emissions include emissions directly generated by the organization, for example from running vehicles or directly generated heating.
- **Scope 2** emissions includes indirect emissions purchased by the company, such as electricity purchased to power buildings.
- **Scope 3** emissions include all upstream and downstream emissions that a company is responsible for through its activity. For example, scope 3 emissions for a car manufacturing firm will include upstream emissions generated by mining and smelting the metal used for the bodywork, but also the downstream emissions generated by the end-user driving the car. Scope 1 emissions for a fossil fuel company will cover the emissions related to the extraction, while scope 3 will cover the burning of those fuels.

For financial institutions, a meaningful net-zero pledge means calculating not only emissions from direct operations (scope 1 and 2), but also the emissions of their portfolio companies and/or the emissions embedded in their financing – their ‘financed emissions’ (scope 3).
Additionally, it also matters which emissions are counted within those scope 3 financed emissions: whether a commitment by a financial institution to reduce its own financed (scope 3) emissions to net-zero includes the scope 3 emissions of portfolio companies and/or clients, or only those companies’ scope 1 and 2 emissions. For example, if an asset manager defines their own scope 3 emissions as just the scope 1 and 2 emissions of their investee companies, then some of the most GHG-intensive activities of some investee companies – such as driving petrol cars and burning fossil fuels – could be excluded from the target.

Data on scope 3 emissions remains at present variable across different sectors and companies. However, methodologies for calculating financed emissions from key asset classes (including equity, loans, real estate and project finance) have been developed, and efforts are under way to improve the availability of data on scope 3 emissions and integrate these into reporting and target-setting frameworks. For example, the Paris Carbon Accounting Framework (PCAF), a framework for financial institutions to report emissions, requires the reporting of scope 3 (financed) emissions of financial sector portfolio companies in the oil and gas sector from 2021; transportation, construction, buildings, materials and industrial activities from 2024; and all other sectors from 2026. However PCAF does not yet have guidelines on all relevant financial services.

Ask your asset manager:

- Does your target cover all your assets under management? If not, what assets or asset classes are excluded? Does this include any carbon-intensive sectors?
- What scopes of emissions are covered by your target? If you are not currently including scope 3 emissions, when do you plan to include these in target coverage? Do you plan to track and report on these emissions on an estimation basis on the meantime?
- Do your targets cover carbon only, or also other GHGs such as methane?

Ask your bank:

- What scope of emissions are covered by your short- and long-term targets? Do your targets cover all relevant financial services, such as capital markets activities?
- If you are not currently including scope 3 emissions, when do you plan to include these in target coverage? Do you plan to track and report on these emissions on an estimation basis in the meantime?
- Do your targets cover carbon dioxide only, or also other GHGs such as methane?
NZAM states that signatories should reduce emissions ‘consistent with an ambition’ of 100% AUM to reach net-zero target by 2050. Within a year of joining, signatories are also expected to set out an interim target for 2030. Targets should be reviewed every five years, with the proportion of AUM covered expected to grow to 100% by 2050 (but with the leeway to reduce should the AUM itself decline or fundamentally change in profile).

But while 2030 interim targets are required, there is no mandate for a minimum proportion of assets under management to be committed to the target – meaning ultimately signatories need not commit their total AUM until 2050. While 13 of the 44 asset managers who have published targets in the November 2021 NZAM progress report committed 100% of their AUM to be covered by 2030 targets, 17 committed less than 50% of their AUM, with the lowest committing just 0.55%.

By enabling asset managers to exclude a large portion of their assets under management from interim targets, there is a risk many of the highest-emitting sectors can be excluded from targets. In some cases, asset managers have set targets to cover only existing ‘green’ or ‘socially responsible’ funds – raising questions about whether managers may cherry-pick the funds covered by their targets to avoid including the highest-emitting sectors.\textsuperscript{xi} An analysis by Universal Owner of targets published in the 2021 NZAM progress report found that for some asset managers this ability to pick and choose AUM to be covered by a target could effectively exclude the vast majority of emissions; for example, for five large NZAM signatories, 10% of equity holdings were estimated to comprise 85% of emissions – meaning even committing 90% of AUM to a target could exclude 85% of portfolio emissions.\textsuperscript{xii} This could enable signatories to exclude the majority of emissions from their net-zero targets for decades to come.

Furthermore, the overall emission reduction will also depend on the actual emission reduction target: to what extent emissions from those AUM covered by a target will actually be reduced. The analysis by Universal Owner found that when analysing the target coverage (% AUM covered) against the target emission reduction, the effective 2030 decarbonisation target across published signatory targets was just 20%.\textsuperscript{xiii}

In terms of scope, NZAM requires signatories to take account of portfolio companies’ scope 1 and 2 emissions, and ‘to the extent possible’ scope 3 emissions. However, unlike NZBA, which sets out an expectation for fossil fuels to be included in accounting of clients’ emissions from 2021 and other high-emitting sectors from 2024, NZAM does not offer guidance on which sectors should be included or even treated as a priority for scope 3 emissions. As a result, whereas some signatories have already committed their scope 3 portfolio emissions to a target (either in totality, or where those emissions comprise a significant proportion of total emissions) or set a timeline for doing so, other signatories indicate they will do so only ‘when data is available’ – with no clear timeline for implementation.\textsuperscript{xiv}
The target-setting guidance states that targets should cover a ‘significant majority of a bank’s Scope 3 emissions’, including a phase-in of targets for scope 3 emissions from key high-emitting sectors such as oil and transport. In addition, targets should cover clients ‘with more than 5% of their revenues coming directly from thermal coal mining, and electricity generation activities’\textsuperscript{xviii} Annual reporting should include both absolute and intensity metrics, and signatories are expected to ‘[scale] up the financing of credible, safe, and high-quality climate solutions’.

However, signatory targets can exclude off-balance sheet activities such as underwriting, which are included only as ‘optional’ targets. This excludes a large stream of financing to potentially high-emitting sectors; 65% of bank financing for fossil fuels in 2020 was through the underwriting of bond and equity issuances.\textsuperscript{xx} By excluding these activities, the NZBA risks allowing banks to claim ‘net-zero’ alignment while continuing to provide direct and/or indirect financing for the continuation and expansion of fossil fuel projects.

The NZBA says that ‘off-balance sheet activities’ will be ‘reviewed for inclusion’ in the next version of the guidelines, expected in April 2024. However, given the lengthy timelines afforded for target-setting, the implementation date for these targets in practice are likely to be some time in the future – undermining the urgent need for a 6% decline in fossil fuel production each year between 2020 and 2030 according to the UN Environment Programme (UNEP).\textsuperscript{xx}

\textsuperscript{*} In June 2022, Race to Zero – the UN-backed campaign for net zero to which NZAM and NZBA are accredited – released new guidelines for member organisations. These include an expectation that targets should explicitly cover scopes 1, 2 and 3, and all portfolio/financed/facilitated/insured emissions. Partner organisations including NZAM and NZBA will have until June 2023 to reflect these updated criteria in their guidelines and articulate updated expectations for members.
Alignment with 1.5°C: does the commitment require urgent action on emissions?

2050 is the headline – but the IPCC have stated that emissions must also drop by 45% by 2030 to have a 50% chance of staying on track for 1.5°C by 2050. This requires immediate concerted action to reduce emissions in the near term. For example, as the UN Environment Programme (UNEP) note, an entity which continues business-as-usual emissions until 2049 and then reduces emissions by 2050 will not be considered aligned with a 1.5°C pathway.

Clear and ambitious interim targets are critical components of a 1.5°C -aligned long-term approach.

However, to calculate how fast and how deep to cut, investors first need to set out assumptions about how factors such as energy demand, living conditions and political action will develop over the coming years. These assumptions will have an impact on the ambition of a commitment by establishing the remaining carbon ‘budget’ in the wider economy. This will determine the rate of emission reductions needed within this timeframe by the economy at large – and thus the ‘fair share’ cuts for individual organisations.

In practice, many organisations use scenarios developed by international bodies to provide the context for their net-zero targets. These include for example the four illustrative ‘pathway archetypes’ to 1.5°C set out by the IPCC (P1 – P4), which set out visions of how 1.5°C might be reached – and the scale of societal changes needed in the meantime to achieve these goals. However, these pathways still differ significantly as to the climate implications.

For example, archetypes P1 and P2 assume lower carbon demand in the economy and limited use of carbon capture technologies to achieve a small temperature overshoot before returning to 1.5°C. P3 and P4, however, assume the continuation of emission-heavy consumption patterns, with a wider use of carbon capture technologies – currently untested at scale – to make 1.5°C possible, and a higher temperature overshoot (and associated social and ecological impact) in the meantime. An organisation relying on scenarios P3 or P4 to calculate the scale of emission reductions needed is therefore relying on widespread use of untested technologies to make 1.5°C feasible.

It is important to note, however, that the climate is a complex system and even the best climate models cannot predict outcomes with full certainty. This is especially important in relation to climate ‘tipping points’ - climate thresholds that, if reached, could result in abrupt and irreversible shifts. For example, the collapse of a key ice sheet could destabilize other sheets in its locality, resulting in a ‘domino effect’ and an irreversible sea level rise. For this reason, including an additional ‘buffer’ by reducing emissions by more than the minimum amount required by the chosen scenario can increase the chance of alignment with 1.5°C and decrease the risk of crossing these thresholds.
In addition, 45% reduction by 2030 is a global average. It does not take into account the responsibility of richer countries for historic emissions or different countries’ present ability to cut emissions without impairing their ability to meet basic human needs. This means that for richer countries, 45% may be an underestimation of their ‘fair share’.

Ask your asset manager/ask your bank:

- Have you published 2025 and 2030 targets? How have you assessed your ‘fair share’ of the 45% emission reduction by 2030 recommended by the IPCC? Do your targets consider responsibility for historic emissions?
- Is your net-zero target explicitly aligned with a 1.5°C scenario, involving low or no overshoot?
- Do your targets include an additional buffer to account for uncertainty in climate and portfolio modelling and around climate “tipping points”?

NZAM explicitly commits to 1.5°C as the guiding target and notes that interim 2030 targets should be ‘consistent with a fair share of the 50% global reduction in CO2 identified as a requirement in the IPCC special report on global warming of 1.5°C’.

However, it does not mandate that signatories assess carbon emissions against a ‘low or no overshoot’ scenario which relies only on limited untested carbon removal technologies to reach net-zero. This leaves the door open for future signatories to rely on scenarios assuming heavy use of untested carbon removal technologies.

In addition, NZAM does not set out any specific criteria for delisting a signatory, other than for non-compliance with the initial publication of targets and annual reporting cycle; no guidelines are set in relation to the ambition of the target. Without clear criteria for delisting signatories that are falling short of concrete action on climate, the initiative is at risk of enabling greenwash by enabling asset managers to claim to be making meaningful action – while dragging their heels up to 2050.
Unlike NZAM, NZBA explicitly mandates that banks use no-overshoot or low-overshoot scenarios and rely only conservatively on negative emission technologies.

However, the guidelines do list scenarios such as the IEA Sustainable Development scenario, consistent with net-zero by 2070 and heavily reliant on carbon capture and storage (CCS), as a possible scenario that banks can use. Furthermore, unlike NZAM it does not refer explicitly to the need to reduce emissions by half by 2030, as advised by the IPCC.

Additionally, upon joining NZBA, banks are given 18 months to set 2030 and 2050 targets for carbon-intensive sectors ‘where data and methodologies allow’ and a further 18 months for remaining carbon-intensive sectors ‘notwithstanding methodological limitations’. The banks must then report within one year on financed emissions and progress.

This in effect gives banks 4 years from signing to set targets and publish plans to meet them; a generous timeline in light of the need for urgent emissions reductions. While setting effective, science-based targets can be a time-consuming process, the fact that a number of European banks have already set targets indicates that this is possible.

Like NZAM, the NZBA does not list any public criteria for the delisting of signatories who fail to take meaningful action. Without a baseline standard for meaningful action towards a net-zero goal, there is a risk of some signatories taking the path of least resistance – and using their membership to greenwash their activities.\textsuperscript{xxvii}

\textsuperscript{xxvii} In June 2022, Race to Zero – the UN-backed campaign for net zero to which NZAM and NZBA are accredited – released new guidelines for member organisations. These include an expectation that the 1.5 target should be targeted ‘with no or limited overshoot’. Partner organisations including NZAM and NZBA will have until June 2023 to reflect these updated criteria in their guidelines and articulate updated expectations for members.
Offsets: how big is the ‘net’ in net-zero?

There are two main ways that organisations aim to reach net-zero: by reducing emissions outright; or by matching any further emissions with the equivalent removal of GHGs from the air – ‘offsetting’.

Offsetting schemes may focus on ‘avoided’ emissions – for example, protecting an area of forest to avoid it being cut down, funding renewable energy projects or replacing fuel cooking stoves with low-carbon alternatives – or on directly removing carbon from the air, for example by planting trees or through direct carbon capture technologies.

Offsetting emissions has become a key strategy for companies aiming to meet net-zero goals; a 2021 study of corporate net-zero commitments found that 19 of the 25 major multinational companies assessed planned to rely on offsetting to meet commitments, with only one company explicitly planning to meet goals without use of offsets.xxvii

However, relying on offsets to meet zero targets is a risky strategy and may lead to greenwashing. For example, it is difficult to assess whether such offsets are truly additional – that the renewable energy project would not have been implemented anyway, or that the forest was never at risk of being cut down.xxix

Relying on offsets to meet zero targets is a risky strategy and may lead to greenwashing.

Offsets may also have issues with long-term viability. A stove may break, or a protected forest may burn down – releasing the carbon anyway. Planting the wrong type of forest in the wrong place may harm ecosystems or soil integrity, or even increase local warming by absorbing – rather than reflecting – more of the sun’s heat.xxx There’s also a time delay - trees planted today may take years to remove equivalent carbon from the atmosphere. And even if schemes are viable and additional, using them to balance further emissions, rather than reduce existing carbon circulating in the system, does little to stop the global heating already ‘locked into’ the system from historic emissions – even though we are already close to crossing ‘tipping points’ which could result in irreversible carbon feedback loops.xxxi

Critically, there are also concerns about the social impact of such schemes: a 2021 Oxfam report estimated that land five times the size of India would be needed for planned carbon removal – raising fears of land grabs, transgressions of indigenous and community rights and risks to food security.xxxii Meanwhile, technological forms of emission capture remain untested at scale – and are unlikely to come online in time for the urgent reductions needed by 2030.
Ask your asset manager/ask your bank:

• Do you expect to make use of offsets to meet your net-zero targets? If so, what limits have you set on the use of offsets?

• How will you ensure your chosen scheme(s) enable long-term, additional carbon removal? Have you set any targets for this? Over what time frame?

• Have you assessed the social and human rights impact of your chosen scheme(s)? How will you monitor this going forward?

While the pledge allows for offsets, it notes that these should be used only where there are no ‘viable alternatives’ to eliminating emissions, focused on long-term carbon removal and signatories should ‘prioritise the achievement of real economy emissions reductions within the sectors and companies in which we invest’. However, this is not mandated and the initiative does not require asset managers to set caps on the use of offsets; mandate offsets to be additional or certified; consider the social impact of schemes; or set standards on the quality of offset schemes that signatories can use to claim emission reductions.

While the pledge allows for offsets, it recommends that these should not be used where ‘there are limited technologically or financially viable alternatives to [eliminating] emissions’ and should be ‘always be additional and certified’ with ‘appropriate due diligence on client offset claims’. However, the initiative does not require caps on the use of offsets or set standards in relation to the social impact of offset projects – leaving this for signatories to interpret.

Metrics: does the commitment involve intensity or absolute targets?

Absolute emission reduction targets are pledges to decrease emissions in real terms. Intensity based targets set a target reduction of emissions relative to a set unit – for example, a reduction in emissions per manufactured unit, number of employees or unit of revenue. For financial institutions, this may involve for example a reduction in emissions relative to the size of an economic portfolio or per dollar provided in financing.

Different targets may be used for different sectors. For example, an organisation may use an absolute target overall, or for specific sectors, but an intensity-based target in a sector where
emissions are expected to increase as a result of a transition to a low-carbon society (such as the production of renewable energy infrastructure).

However, the use of intensity emission metrics may mean that emissions themselves need not decrease in order to meet the target, or may even increase in real terms – so long as the unit of measurement grows at a faster rate (thus decreasing the ratio of emissions to unit of measurement). For example, an oil and gas company could increase their extraction of oil, while also increasing investments in renewable energy sources – and report an overall decrease in emissions intensity, while absolute emissions continue to increase. Moreover, because there is no standard metric of production across the whole economy, revenues have become a common denominator for unitising intensity – and this can be distorted by price rises. While these targets may be favoured by institutions which expect their AUM – and thus overall emissions – to grow in line with business expansion, using intensity-based targets alone raises the risk that the necessary reduction in absolute emissions will not be made at the scale that is needed. They are also inappropriate for sectors such as the fossil fuel sector – where the objective should be to encourage a reduction in oil and gas production, not more efficient extraction of oil and gas.

Ask your asset manager/ask your bank:

• Have you set absolute or intensity-based targets?
• If using intensity targets, have you also set an absolute emissions reduction target at portfolio level, or for specific sectors including fossil fuels?
• Will you report annually on absolute emissions regardless of the overall metric used?

| NZAM | NZAM allows signatories to choose to set either absolute or intensity-based targets, with no requirement for absolute emissions reductions. Of 44 asset managers who have published targets in the November 2021 progress report, an analysis by Universal Owner found that only 14 had set absolute emission reduction targets, with the other 30 setting intensity-based targets.

| NZBA | Like NZAM, NZBA allows signatories to choose to set either absolute or intensity-based targets, with no requirement for absolute emissions reductions. However, a positive step is that NZBA does mandate annual reporting of both absolute and intensity metrics regardless of target. |
Transparency: are net-zero targets transparent and public?

For a net-zero target to be credible, it must be open to independent scrutiny and monitoring. This includes publishing the target itself, along with the underlying target-setting methodology and key assumptions; using recognised and standardised carbon accounting methods where possible to ensure comparability with peers; and publicly disclosing progress on a regular basis, including reporting on emissions themselves.

**Ask your asset manager/ask your bank:**

- What methodology did you use to set the target? Has your target been independently assessed and verified?
- Will you report annually on progress towards the target and actual emissions, using both absolute and intensity metrics?

| NZAM | The pledge will involve an annual disclosure and reporting process, set to begin in 2022. Signatories disclose methodologies used in setting the net-zero target.\textsuperscript{xxxvii} |
| NZBA | While reporting has not yet begun, signatories will be required to disclose progress against targets on an annual basis, and report on progress against a transition strategy. |

Fossil fuels: do targets allow for the continued financing of coal, oil, or gas?

No new coal mines or mine extensions; no new oil and gas fields. That was the assessment of the International Energy Agency in May 2021 in their 1.5°C roadmap for the energy sector.\textsuperscript{xxxviii} However, a 2021 study found that the world’s 60 largest commercial and investment banks committed a total of USD $3.8 trillion to fossil fuels from 2016–2020.\textsuperscript{xxxix} Similarly, a 2020 study found that of 75 top asset managers, only 12 excluded coal from all portfolios.
under management – although a number of leading asset managers are putting in place comprehensive exclusion policies. A net-zero pledge which allows for financing new fossil fuel development is not a credible pledge.

A net-zero pledge which allows for financing new fossil fuel development is not a credible pledge.

Ask your asset manager:

• Have you set a commitment for a total exit of coal by 2030 in OECD countries and 2040 worldwide at the latest and published an implementation strategy to support it?

• Do you set explicit transition expectations for fossil fuel companies to which you have significant exposure?

• If you plan to engage with fossil fuel companies rather than divest, what escalation steps will you take, and on what timeline? Will divestment be considered if the company does not show progress? What will trigger these steps?

Ask your bank:

• Are you continuing to provide financing or underwriting services for new fossil fuel projects or related infrastructure?

• Do you have a strategy for a full phase-out of exposure to fossil fuels? Does this cover off-balance sheet activities?

• Have you requested that your fossil fuel clients publish transition plans in alignment with 1.5°C pathways?
The December 2021 NZAM Fossil Fuel Position set out that signatories are expected to have a ‘a robust and science-based policy for the organisation in relation to fossil fuel phase out’, covering ‘at a minimum’ the assets committed to be managed in line with net-zero, and meet the requirements set forth by at least one of five NZAM affiliated organisations.

However, by allowing asset managers to choose the standard with which they align their coal policy – rather than providing clear guidance – the door is left open for asset managers to simply choose – and claim compliance with – the minimum standard.

For example, one possible standard offered by the Fossil Fuel Position is that of the Net-zero Asset Owner Alliance (NZOA), part of the GFANZ umbrella, which sets out a clear expectation that no further thermal coal power plants should be financed, insured, built, developed or planned by signatories, and projects in a pre-construction phase should be immediately cancelled. However, another – the Powering Past Coal Alliance – requires only that signatories ‘support clean power generation’ and ‘restrict financing for unabated coal power generation, i.e. without carbon capture and storage’ – with no set timeline for compliance. This leaves the door open for signatories to continue support for coal mining, related infrastructure, and even continued coal power generation under the promise of carbon capture and storage – technologies which currently face barriers to widespread deployment.

No standard offered requires any restrictions on oil or gas financing.

In addition, as detailed above, fossil fuels may be effectively excluded from AUM targets until 2050. This leaves open the door for the continued support of fossil fuels for decades to come.

While NZBA expects signatories to ‘prioritise efforts’ in relation to the most GHG-intensive sectors, it does not require signatories to make specific commitments relating to halting financing for fossil fuels.

A recent study found that 24 signatories of the NZBA have provided $33 billion to companies expanding the extraction and production of oil & gas since joining the alliance in 2021, with over half of that amount ($19bn) coming from four of the founding signatories – HSBC, Barclays, BNP Paribas and Deutsche Bank.
released new guidelines for member organisations. These include an expectation that organisations should ‘recognise’ that ‘this requires phasing down and out all unabated fossil fuels as part of a global, just transition’ in order to meet net-zero goals in line with the scientific consensus. Partner organisations including NZAM and NZBA will have until June 2023 to reflect these updated criteria in their guidelines and articulate updated expectations for members.

Effectiveness: does the commitment aim to reduce real-world emissions?

Urgent, real-world emissions reductions are required to stay on track for 1.5°C. However, there is a risk that financial institutions will aim to simply reduce their own exposure to emissions by focusing their investments in typically low-emitting sectors (such as tech) and in high-income countries, rather than taking action to drive real-world and economy-wide decarbonisation among their portfolio companies.

A net-zero commitment, therefore, should be accompanied by a clear strategy on how to drive decarbonisation throughout a portfolio by supporting portfolio companies to align their own operations with a 1.5°C target.

For asset managers, this means engaging with companies in their portfolio to push for Paris alignment and drive decarbonisation. For banks, this may mean ceasing financing for activities that are misaligned with the Paris agreement and creating financing products which specifically aim to finance the global net-zero transition.

However, it is important that decarbonisation should not be used as an excuse by banks and asset managers to avoid divesting from companies and sectors which are not compatible with a 1.5°C world – such as fossil fuels.

Ask your asset manager:

- How do you plan to reach your net-zero goal? Will this focus on reducing real-world emissions among investee companies? If you plan to divest from, refuse to purchase debt for or deprioritise certain sectors, which are these and why have you chosen to do so rather than to engage on decarbonisation?
- Is your stewardship policy aligned with your net-zero commitment? Does it contain escalation policies in relation to companies who are not Paris-aligned? Does it cover all asset classes?
- Does your stewardship policy have a presumption to vote in favour of climate resolutions, with a ‘comply or explain’ approach? Do you make your voting decisions and rationales for
votes publicly available?

- Will you publish metrics on how much of your reported emissions reductions are the result of decarbonisation among portfolio companies, and how much are the result of changes to the underlying portfolio composition?

Ask your bank:

- How do you plan to reach your net-zero goal?
- Do you complement your targets with robust sectoral policies and clear financing conditions for companies to ensure that you do not finance Paris misaligned activities and instead contribute to the transition?
- Do you have a strategy in place to provide financing for the net-zero transition, such as investing in renewable energy and green infrastructure?

The pledge includes an expectation that asset managers should ‘prioritise the achievement of real economy emissions reductions’ and ‘implement a stewardship and engagement strategy, with a clear escalation and voting policy’.

While it is positive that engagement has been included, there is no presumption to vote in favour of climate resolutions at investee companies using a ‘comply or explain’ approach.

A 2021 study of voting practices for key environmental and social resolutions found that CA100+ and NZAM initiative members voted against almost a third of sampled environmental resolutions. In addition, NZAM signatories who are not also members of CA100+ did not outperform those who are members of neither coalition – raising questions over the extent to which the NZAM initiative is driving ambition and best practice on engagement.
The NZBA pledge states that signatories will meet net-zero commitments through ‘facilitating the necessary transition in the real economy through prioritising client engagement, and offering products and services to support clients’ transition’, as well as supporting industry action and support innovation and financing for climate solutions ‘that are compatible with the other Sustainable Development Goals’.

However, in practice these requirements are left open to the interpretation of signatories, with no minimum standards relating to providing transition financing – giving wide latitude for banks to claim they are acting in accordance with minimal action. Furthermore, they fail to recognise that ceasing financing to specific activities and clients needs to be part of the solution.

Fairness: Does it consider the need for a just transition?

The term ‘just transition’ refers to a fair and inclusive process that prioritises the social needs of people and communities impacted by the transition to a net-zero economy. In practice, this means understanding where people and communities stand to lose out from the global transition – such as through the loss of jobs and income among workers of coal-related industries – and ensuring that these individuals and communities reap the benefits of the global transition, for example by up-skilling workers to work in new low-carbon industries.

A just transition also means taking account of human rights within the emerging transition economy: including human rights in direct supply chains, but also the wider impact on land rights and rights to food, shelter and water arising which might be impacted by projects such as lithium mining, new renewable energy infrastructure, and offsets (as discussed above).

Ensuring a just transition will be a complex undertaking, and government will have a central role in ensuring that investments in communities and education are being directed where they are needed for benefits of the transition to be shared equitably. However, financial service providers will have a key role to play in directing flows of capital to the new economy – and using influence with investee companies to ensure that that no-one is left behind.

Financial service providers will have a key role to play in directing flows of capital to the new economy – and using influence with investee companies to ensure that that no-one is left behind.

Further information can be found in ShareAction’s briefing on Laying the Track: The Race to Zero The role of investors in addressing the just transition. Available at: https://api.shareaction.org/resources/reports/COP26-briefing-Just-Transition.pdf
Ask your asset manager:

- When engaging with investee companies on their plans for their emission reductions, do you require them to include consideration of a just transition for the company’s workforce and communities where the company operates and throughout the supply chain?
- Do you require investee companies to implement fair processes of negotiation and consultation with all affected stakeholders?

Ask your bank:

- Do you have a strategy in place to provide financing for individuals and communities affected by the transition? Does this include specific financing activities such as ‘green’ mortgages and loans for SMEs?
- Do you include social considerations when making decisions on providing financing for large-scale ‘green’ projects?
- Are you participating in any sector-wide groups or activities relating to a just transition?

| NZAM | The NZAM pledge calls for ‘asset managers to play our part to help deliver the goals of the Paris Agreement and ensure a just transition’, although does not set any expectations of specific action for signatories. |
| NZBA | The NZBA pledge refers to ‘giving consideration to associated social impacts’ and supporting solutions that ‘are compatible with other Sustainable Development Goals’, although does not set any expectations of specific action or financing activities. |

*In June 2022, Race to Zero – the UN-backed campaign for net zero to which NZAM and NZBA are accredited – released new guidelines for member organisations. These include an expectation that organisations should ‘phase down and out fossil fuels ‘as part of a global, just transition’. Partner organisations including NZAM and NZBA will have until June 2023 to reflect these updated criteria in their guidelines and articulate updated expectations for members.*
Accountability: how does the target align with other activities?

Even the most technically ambitious net-zero commitment may struggle to be successfully implemented if it comes into conflict with other incentives within an institution. A solid net-zero commitment should therefore be embedded at all levels of a financial institution, with the requisite tools and training provided and a clear framework to resolve any conflicts to ensure that net-zero commitments are not siloed within stewardship teams or sidelined in light of other priorities.

Ask your asset manager/ask your bank:

- Have you made a public commitment to aligning all your lobbying strategies and political activities with the goal of restricting temperature change to 1.5°C?
- Are climate strategies integrated into financial reporting? Do your financial statements and risk analyses consider key material financial risks relating to a 1.5°C transition?
- Are executive objectives and incentives aligned with the implementation of the climate strategy? If yes, to what extent?
How asset owners can engage their financial service providers
How asset owners can engage their financial service providers

Asset owners can help to drive higher net-zero standards by engaging with their financial service providers. Below, we outline three ways of doing so.

**Ask your bank or asset manager to publish their target if they have not already done so**

Asking your service providers to commit to regular public disclosure of targets can be a positive first step in pushing for greater transparency about their net-zero commitments. This should ideally involve an annual report on progress against the target, including disclosure of emissions using both absolute and intensity metrics, and accompanying sectoral policies.

**Engage with your service providers on the specifics of their commitment**

Asset owners are in a powerful position to engage directly with their service providers on the specifics their commitments to encourage greater ambition – and to challenge them where these commitments are falling short.

Asset owners can raise these kinds of questions during regular meetings or performance reviews. Net-zero approaches and commitments should be a factor in the procurement, review, and potential exit of service provider relationships, and can inform mandates for asset managers.

Annex A provides a full list of indicative questions you can use to engage your asset manager or bank on their net-zero commitments.

**Engage collaboratively with other asset owners**

Engaging your financial institutions alongside other asset owners who share your bank / asset manager can amplify the request and let institutions see the importance of this topic among their client base.

This could be through joint meetings, or larger asset owner joint initiatives. For example, the COP26 Declaration of Asset Owners – signed by a series of mission-driven asset owners - sets out basic criteria for a positive net-zero commitment: [https://www.cop26declaration.uk/](https://www.cop26declaration.uk/)

The Charities Responsible Investment Network (CRIN) and Responsible Investment Network Universities (RINU) are also able to provide support and guidance to non-profit asset owners on engaging with their financial institutions. For more information, email rin@shareaction.org.
References


xi See: https://ghgprotocol.org/


Intergovernmental Panel on Climate Change (IPCC) (2018) op. cit.


Ibid.


xlii Ibid.


xlviii Climate Action 100+ (n.d.). ‘Investor signatories’. Available online at: https://www.climateaction100.org/whos-involved/investors/ (accessed 18 March 2022)

Appendix
## Appendix A: Questions for financial service providers

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<th>Topic</th>
<th>Asset managers</th>
<th>Banks</th>
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| **Scope** | - Does your target cover all your assets under management? If not, what assets are excluded? Does this include any carbon-intensive sectors? How often will you review this coverage? When do you expect to reach 100%?  
- What scope of emissions are covered by your pledge? Does your scope 3 emissions include scope 3 financed emissions from portfolio companies where material?  
- If you are not currently including scope 3 portfolio emissions, when do you plan to include these? Are you tracking and reporting on these emissions on an estimation basis in the meantime?  
- Do your targets cover carbon only, or also other GHGs such as methane?  
- Are you regularly conducting scenario analysis across your portfolio and including this in your risk management strategy? | - What scope of emissions are covered by your short- and long-term targets? Do your targets cover all relevant financial services, such as capital markets activities?  
- If you are not currently including scope 3 emissions, when do you plan to include these in target coverage? Do you plan to track and report on these emissions on an estimation basis in the meantime?  
- Do your targets cover carbon dioxide only, or also other GHGs such as methane? |
| **Alignment with 1.5°C** | - Have you published 2025 and 2030 targets? How have you assessed your ‘fair share’ of the 45% emission reduction by 2030 recommended by the IPCC?  
- Is your net-zero target explicitly aligned with a 1.5°C scenario, involving low or no overshoot?  
- Does your net-zero commitment implicitly rely on the use of carbon removal technologies? If yes, have you assessed your commitments against other scenarios in which these technologies do not become widely available?  
- Does your target incorporate a buffer, given inherent uncertainties about tipping points and other climate phenomena, and low probabilities of success of key scenarios? | - Have you published 2025 and 2030 targets? How have you assessed your ‘fair share’ of the 45% emission reduction by 2030 recommended by the IPCC?  
- Is your net-zero target explicitly aligned with a 1.5°C scenario, involving low or no overshoot?  
- Does your net-zero commitment implicitly rely on the use of carbon removal technologies? If yes, have you assessed your commitments against other scenarios in which these technologies do not become widely available?  
- Does your target incorporate a buffer, given inherent uncertainties about tipping points and other climate phenomena, and low probabilities of success of key scenarios? |
| **Offsets** | - Do you expect to make use of offsets to meet your net-zero targets? If so, what limits have you set on the use of offsets? Do you / will you disclose details about the scale of offset use to meet your targets?  
- If you plan to make use of offsets, what scheme(s) are you using? Have these been certified by an independent body? How will you ensure that these offsets are truly additional, and will ensure long-term carbon removal?  
- Do you / will you publish details about the offset schemes you are using?  
- Have you assessed the social and human rights impact of your chosen scheme(s)? How will you monitor this going forward?  
- Do you plan any due diligence about whether and how portfolio companies are using offsets to reduce their own emissions? Do you plan to engage with them to ensure any offsets are additional and certified? | - Do you expect to make use of offsets to meet your net-zero targets? If so, what limits have you set on the use of offsets? Do you / will you disclose details about the scale of offset use to meet your targets?  
- If you plan to make use of offsets, what scheme(s) are you using? Have these been certified by an independent body? How will you ensure that these offsets are truly additional, and will ensure long-term carbon removal?  
- Do you / will you publish details about the offset schemes you are using?  
- Have you assessed the social and human rights impact of your chosen scheme(s)? How will you monitor this going forward?  
- Do you plan any due diligence about whether and how loan and financing beneficiaries are using offsets to reduce their own emissions? |
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| **Metrics** | - Have you set absolute or intensity-based targets?  
- If using intensity targets, have you also set an absolute emissions reduction target at portfolio level, or for specific sectors including fossil fuels?  
- Will you report regularly on absolute emissions regardless of the overall metric used? | - Have you set absolute or intensity-based targets?  
- If using intensity targets, have you also set an absolute emissions reduction target at portfolio level, or for specific sectors including fossil fuels?  
- Will you report regularly on absolute emissions regardless of the overall metric used? |
| **Transparency** | - What methodology did you use to set the target? Has your target been independently assessed?  
- Will you report on progress towards the target and actual emissions regularly using both absolute and intensity metrics?  
- Do you disclose emissions annually in line with recognised metrics? Does this include a breakdown of emission sources? Does it include a breakdown of fossil fuel exposure?  
- If you categorise specific products or funds as ‘carbon-neutral’ or ‘sustainable’, do you publish the underlying methods and metrics used to classify them as such? | - What methodology did you use to set the target? Has your target been independently assessed?  
- Will you report publicly on your success in meeting your targets?  
- Do you disclose emissions annually in line with recognised metrics? Does this include a breakdown of emission sources? Does it include a breakdown of fossil fuel exposure? Does this include all relevant financing/investment activities, including capital market underwriting?  
- If you categorise specific products or funds as ‘carbon-neutral’ or ‘sustainable’, do you publish the underlying methods and metrics used to classify them as such? |
| **Fossil fuels** | - Have you set a commitment for a total exit of coal by 2030 in OECD countries and 2040 worldwide at the latest and published an implementation strategy to support it?  
- Do you set explicit transition expectations for fossil fuel companies to which you have significant exposure?  
- If you plan to engage with fossil fuel companies rather than divest, what escalation steps will you take, and on what timeline? Will divestment be considered if the company does not show progress? What will trigger these steps? | - Are you continuing to provide financing or underwriting services for new fossil fuel projects or related infrastructure?  
- Have you set any restrictions relating to the financing of existing fossil fuel projects? Does this apply to both on-balance and off-balance sheet activities? Does it apply at both asset and corporate level?  
- Does the bank consider the climate and financial impact of existing fields under development or expansion of already producing fields?  
- Do you have a strategy for a full phase-out of exposure to fossil fuels? Does this cover off-balance sheet activities?  
- Have you requested that your fossil fuel clients publish transition plans in alignment with 1.5°C pathways? Will you exclude clients from your client base if they do not publish plans by a specific date? Do these plans include a commitment not to invest in further expansion of fossil fuels?  
- Has the bank adopted a definition of the Arctic region aligned with the area considered by the Arctic Monitoring and Assessment Programme (AMAP)? |
### Appendix A (continued)

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<td>• How do you plan to reach your net-zero goal? • Do you complement your targets with robust sectoral policies and clear financing conditions for companies to ensure that you do not finance Paris misaligned activities and instead contribute to the transition? • Do you have a strategy in place to provide financing for the net-zero transition, such as investing in renewable energy and green infrastructure?</td>
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<td>• Have you made a public commitment to aligning all your lobbying strategies and political activities with the goal of restricting temperature change to 1.5°C? Does this cover all subsidiaries and operational jurisdictions? Have you taken steps to ensure that any industry associations and alliances you are involved with do likewise? • Are climate strategies integrated into financial reporting? Do your financial statements and risk analyses consider key material financial risks relating to a 1.5 transition? • Are executive objectives and incentives aligned with the implementation of the climate strategy? If yes, to what extent?</td>
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