

CRITERIA FOR EXCLUSION AND ENGAGEMENT WITH COAL AND PETROLEUM COMPANIES IN NORWAY'S GPFG

Recommendations of exclusion criteria and how they fit the current approach to divestments and natural adjustments of NBIM's investment portfolio:

NBIM has no exclusion criteria which address climate change risk. Following the Expert Group's mandate of considering GPFG's investment in companies with activities within coal, oil and gas, WWF proposes the introduction of new exclusion criteria for such companies.

The expert group should formulate clear and transparent criteria for exclusion. Companies which are not excluded should be subject to active ownership strategies to make their business models compatible with a 2-degrees scenario. This approach must be adapted to each relevant industry sector, i.e. utilities, basic materials and oil & gas.

Inputs to the development of industry-sector specific criteria for exclusion (further detailed in appendix 1 and appendix 2):

a) Coal mining companies: Exclusion criteria must be based on the share of revenue from thermal coal (used for power generation) relative to total revenue (implying that companies with more than X% of revenue from thermal coal should be excluded).

b) Electric utilities: Exclusion criteria based on the relation between the share of electricity generation from coal and renewables, and a qualitative assessment of the company's strategy for its future energy mix (i.e. companies with more than X% share of coal and with less than Y% of renewable energy would be subject for exclusion, taking also into consideration the company's strategy to change its energy mix on a medium and long-term horizon).

c) Oil & gas companies: Exclusion criteria based on (i) emission intensity calculated as metric tonnes of GHG emitted per barrel of oil equivalent (BOE) produced, and (ii) whether a company is searching for fields with a breakeven price deemed not in line with a 2-degree scenario (i.e. companies which has energy intensity above X would be subject to exclusion, taking also into considerations the company's investments in high-cost fields.)

WWF recommends the Expert Group proposes thresholds of acceptance in accordance with the above criteria. These thresholds should be re-evaluated continuously in order to ensure the effectiveness of the exclusion criteria.

Recommendations for an expectation document on climate, a strategy for active ownership with coal and oil & gas companies:

WWF would like to propose amendments to the existing "Climate change risk management" document in appendix 1. In this document we have (i) defined the concept of "climate change risk", encompassing not only the financial risk, but also the risk that a company's emissions profile is deemed not in line with UNFCCC parties and thus Norway's committed goal of limiting global warming to 2°, agreed at the Copenhagen Summit in 2009 (COP15). We also (ii) propose a new section presenting the exclusion criteria for the three sectors mentioned above. The aim is to clarify to the companies which are the expectations and the guidelines used by NBIM to choose between exclusion and active ownership (we refer to appendix 1 for further details). To verify that these expectations are implemented, the company should regularly follow up and report on its performance.

WWFs recommendations and what they will achieve:

WWF believes that excluding a company from the GPFG's investment universe and exercising ownership strategies should be two complementary strategies for the fund. WWF recommends that the Expert Group develops clear acceptance criteria to define which company profiles qualifies for exclusion, and which profiles qualifies for ownership strategies. These acceptance criteria must in WWF's view be consistent with a 2-degree emission trajectory. While such a consistency check is difficult to obtain in a reliable manner, i.e. it is difficult to determine the fair and relative contribution of single companies to the global atmospheric GHG concentrations, WWF underlines the necessity for the Expert Group to honour the political intention of its evaluation in such a climate political context. As such, the criteria should be evaluated and possibly amended continuously, while also likely increasing its level of stringency with time.

WWF recommends that strategic and operational guidelines are proposed by the Norwegian Government in the White Paper for the GPFG in 2015. Following the adoption of this White Paper, the climate risks strategy should be immediately implemented by the GPFG.

Appendix 1: NBIM's "Climate change risk expectations", with WWF suggested changes

Appendix 2: Illustrative examples of exclusion criteria applied to the sectors oil & gas and utilities in the GPFG portfolio.

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WWF arbeider for å stanse ødeleggelsen av verdens natur og økosystemer
- og for å skape en framtid der mennesker lever i harmoni med naturen.
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NBIM INVESTOR EXPECTATIONS

CLIMATE CHANGE RISK MANAGEMENT

Part 1: Original text of NBIM's "Climate Change risk management", with WWF's proposed amendments in red.

Part 2: New proposed section: "Exclusion criteria for coal, utilities and oil & gas companies".

Purpose

~~NBIM expects companies to manage risk associated with the causes and impacts of climate change resulting from greenhouse gas emissions and tropical deforestation. Our expectations are directed at companies with operations or value chains in sectors and regions materially exposed to such risk.~~

NBIM expects companies to manage climate change risk, here defined as having two components:

(i) financial risk, associated with the causes and impacts of climate change resulting from greenhouse gas emissions, emissions of short-lived climate forcers and tropical deforestation;

(ii) climate disruption risk, associated with a company's GHG emissions and energy efficiency's practices which are not deemed in line with the international political goal of limiting global warming to 2 degrees.

In the last section of this document, NBIM presents in details the current exclusion criteria adopted for three industry sectors, namely coal mining, electric utilities, oil & gas.

Establishing expectations and monitoring companies' responses to climate change risk is a priority for investors as there is overwhelming scientific evidence that climate change threatens long-term financial returns.

However, the complexity of environmental and financial systems presents a significant challenge. Economic activity that produces greenhouse gas emissions may lead to future financial, environmental and social impacts that are not reflected in current prices of goods and services. Coherent regulation can address this problem by placing a cost on emissions and so harness market forces to efficiently allocate resources to prevent or adapt to the impacts of climate change.

Tropical deforestation releases carbon stored in tropical forests into the atmosphere. A major cause of tropical deforestation is the growth in global demand for commodities that are produced through the clearing of tropical forest. Reversing tropical deforestation requires national and international standards and regulations that encourage the production and sale of such commodities in a sustainable way.

It is in this context that NBIM seeks to promote the conditions for well-functioning markets and to encourage the boards of our investee companies to integrate climate change into their wider risk management responsibilities.

Our expectations should serve as a reference point that companies may be measured against, either by their management or their owners. Our goal is to encourage constructive dialogue between companies' boards and investors.

Why climate change is an issue for investors

Most forms of current economic activity are carbon intensive. Progression toward a low-carbon economy to reduce the risk of dangerous climate change will require significant adjustments in a wide range of sectors.

Companies increasingly feel the financial impact of regulatory measures that set renewable energy targets and price greenhouse gas emissions through market-based mechanisms or taxes. Meanwhile, companies engaged in the production or sale of forest-related commodities, or related products, are increasingly operating in a market environment shaped by international standards for sustainable forestry. There is also a high general level of stakeholder concern on these issues, which makes the perception of how companies manage climate change risk important. In the medium and longer term there is increasing potential for climate change to directly and severely impact the activities of many companies. Change also gives rise to opportunity. Companies that mitigation and adaption at the lowest cost, develop profitable new low-carbon products and services and attract the best talent by building a reputation for responsible action on climate change will create the greatest long-term value.

Expectations

We expect companies to identify (i) **their impact on climate and continuous performance in terms of GHG emissions and energy efficiency** and (ii) material **[financial]** risks related to climate change, define an optimal mitigation strategy and take action to implement that strategy.

Companies should also have a well-functioning governance structure for risk and be transparent in their interaction with policy-makers and regulators. They should disclose sufficient information demonstrating an effective approach to:

- **Manage financial risk related to climate change**, including risk related to tropical deforestation.
- **Manage risk related to the need to reduce GHG emissions and improve the energy efficiency profile.**

NBIM expects that the companies which are not excluded from the GPFG's portfolio should provide a business plan, including a related investment strategy, which outlines the company's strategic direction to ensure alignment between its business model and a 2-degrees scenario.

A. Strategy for optimised investment in climate change risk mitigation

Companies should address climate change risk as an integral part of their business strategy and effectively and efficiently allocate resources to mitigate this risk.

The following questions should be considered in the strategic planning process:

- What are the material threats and opportunities to the company from:
 - the direct impacts of climate change?

- regulation and standards concerning climate change mitigation or adaptation?
- the need to reduce the company's GHG emissions with a trajectory deemed to be in line with a 2-degrees scenario.
- assess and report on the company's performance in GHG emissions and energy efficiency benchmarked against its own internal historical trend.
- Especially for company investment in major projects, assess the sensitivity to future scenarios for:
 - the sensitivity of their profitability related direct impacts (e.g. changes in water availability, extreme weather, etc)?
 - the sensitivity of their profitability related regulation (e.g. carbon prices, emission caps, renewable energy targets, mandatory technology requirements, restrictions on business operations in tropical forests, etc)?
 - the extent to which their GHG emissions from the project is deemed compatible to necessary emission profiles in a 2-degrees scenario.
- Are there specific environmental policies or guidelines that reflect the company's approach to climate change risk management and the management of risks related to tropical deforestation?
- What are the key implications of major risk factors for the business and what is the overall strategic response?
- What are the key implications of the need to reduce the company's GHG emissions, and what is the overall strategic response of the company?
- Are the risks and company response reassessed on a timely and regular basis?

B. Specific action to implement climate change strategy

Companies should take appropriate and timely action to implement their strategy to mitigate climate change risk. Implementation should encompass a company's direct operations and wider supply chain. Companies should also invest, where appropriate, in research to close gaps in the knowledge and technology needed to manage climate change risk.

NBIM does not expect companies to invest in research and development that is not central to their businesses or to diversify out of businesses where they have a competitive advantage. Investors have the responsibility to manage the risk associated with intrinsically carbon intensive products and services by adjusting the composition of their portfolios. Key questions for boards to consider include:

- What actions are being taken to mitigate climate risk in direct operations? For example, is the company pursuing:
 - energy and resource efficiency improvement programs?
 - increased use of less carbon-intensive raw materials?
 - optimisation of logistics and distribution?
 - compliance with international standards for sustainable forest management?
- What steps are being taken to address risk in the supply chain? For example, does the company:
 - have relevant procurement policies for products and services?
 - share best climate change practice with strategic suppliers?
 - require standards from suppliers and business partners which are in line with the company's overall climate change strategy as it relates to GHG emission mitigation?
 - integrate the cost-of-carbon into supply chain management systems?
 - monitor whether suppliers that deliver commodities, products, and materials produced in tropical forests comply with international standards for sustainable forest management?

- Does the company sponsor research and development in areas where there is a lack of knowledge or technology to assess and manage climate change risk?

C. Effective and efficient governance for risk management

To implement our expectations companies must have a corporate governance structure that facilitates realistic strategies to manage climate change risk. We expect boards to address the following questions:

- Does the board explicitly recognise the necessity of fully integrating climate change **risks** into its wider risk management responsibilities?
- Are there appropriate monitoring and reporting systems covering climate change risk?
- Is there a clearly defined line of responsibility and reporting in the organisation up to board level?

D. Transparency and disclosure

Companies should be transparent in how they manage climate change risk, and disclose information addressing the topics in this document. NBIM will use this information to identify the most important climate change issues affecting companies' economic performance and prospects, and to assess whether management is taking appropriate steps to address those issues.

The introduction of regulation that directly or indirectly places a price on carbon is a significant near-term risk factor for companies in many sectors and regions. As a result, NBIM emphasises the importance of (i) reporting on greenhouse gas emissions and (ii) **reporting on what actions the company undertakes to reduce its GHG emissions**, and considers the following questions when assessing a company's performance in this area:

- What are the company's current greenhouse gas emissions in tonnes of carbon dioxide equivalent (CO₂e) and in appropriate emission intensity units for the sector (e.g. revenue per tonne of CO₂e, production volume per tonne of CO₂e)?
- What is the breakdown of emissions arising from direct operations, use of purchased electricity and other supply chain inputs?
- Is the company's management signalling its quality by disclosing meaningful and quantitative emission intensity reduction targets with clear timelines **and the ability to benchmark company's performance relative to its own historical trend?** (Note that our focus is on continual improvement in emission intensity, as the use of this measure helps avoid confusion with the effects of increasing or decreasing demand and supply).
- Are emissions independently verified, with an estimate of uncertainty?
- Does the company set a uniform global standard for performance on carbon productivity/emission intensity, irrespective of where it has its operations? How does this compare with the expected development in regulatory standards?

When assessing companies that are exposed to risks related to tropical deforestation, NBIM considers the following questions:

- Does the company disclose information on its tropical forest footprint, how it monitors its impact on tropical forests over time, and its assessment of whether it poses a risk to its business operations?
- Has the company, or its suppliers, committed to achieve compliance with international standards for sustainable production of agricultural commodities, or sustainable forest management?
- Does the company report on the implementation of its commitments to reduce tropical deforestation?

Finally, we expect companies to provide information on their position on climate change legislation and regulation. Boards should address the following questions:

- What is the company's position on related legislation and regulation?
- What is the nature of the company's interaction with policy-makers and regulators?

- Does the company have policies or guidelines for engaging with policy makers and regulators? Do these provide guidance on funding and donations? Does the company report on this kind of expenditure?
- Has the company lobbied, or is the company lobbying relevant decision-makers in the context of securing existing production and use of fossil fuel? If yes, is the company publicly disclosing its activities and its position on the topic?

NBIM INVESTOR EXPECTATIONS

CLIMATE CHANGE RISK MANAGEMENT

As a large diversified investor with a long-term outlook, NBIM recognises ~~the potential for climate change to seriously impact the performance of its investments~~ **the emerging risks related to climate change**. We expect the companies we invest in to manage such risk and will present our expectations to their boards to ensure that the necessary policies and activities are implemented.

Our expectations cover four areas:

Strategy for optimised investment in climate change risk mitigation

Companies should plan for the effective and efficient allocation of resources to mitigate risk. Climate change should be integrated into a regular and comprehensive risk assessment process, particularly for investments in major projects. A clear strategy should be developed addressing significant threats and opportunities.

Specific action to implement climate change strategy

Companies should take concrete steps to minimise threats and capture opportunities. This includes considering initiatives in direct operations, supply chain management and research and development.

Effective and efficient governance for risk management

Companies should have a governance structure that facilitates an effective response to climate change risk. Boards need to fully integrate climate change into their wider risk management responsibilities. They should also ensure there is a clear delegation of responsibility in the management structure, appropriate monitoring and reporting, and incentives linked to key performance indicators.

Transparency and disclosure

Companies should disclose information on their climate change strategy, actions and governance, as well as report on greenhouse gas emissions, emission intensity reduction targets, and impact on tropical forests. They should also disclose their positions on climate change regulation and the nature of, and resources allocated to, interactions with policy makers.

NEW PROPOSED SECTION:

EXCLUSION CRITERIA FOR COAL, UTILITIES AND OIL & GAS COMPANIES.

NBIM consider exclusion and active ownership as complementary tools in the context of climate change risk management. Exclusion of companies from NBIM's investment universe is the most relevant tool for companies which currently – and likely in the near/medium term – are unlikely to enable a business model which is deemed consistent with a 2-degree scenario. For companies which either falls within or show a reliable potential to be consistent with a 2-degree scenario, active ownership strategies would be employed by NBIM.

In order to determine which companies would be excluded and which companies would be subjected to ownership strategies, NBIM refers to defined GHG emission performance thresholds to decide when exclusion or active ownership is the preferred option.

The exclusion criteria from NBIM's investment universe for the different industry sectors are as follow:

1) Coal mining sector: The exclusion criteria relates to an indicator measuring the share of revenue from coal mining (thermal coal for the production of electricity) relative to the total revenue of the company.

Given this indicator, NBIM sets a threshold for exclusion where:

- all companies with a share of revenue from thermal coal above X percentage are automatically excluded.
- all companies which are below this threshold remain in the portfolio and are subjected to further active ownership strategy.

2) Electric utilities: Exclusion criteria relates to an indicator which determines the relation between electricity production from respectively coal and renewable energy, measured in percent of total power production. This indicator will let identify companies which rely heavily on coal and companies which are relevant activity within the renewable energy sector. NBIM will also take into consideration the historical trends to analyse whether the company is increasing or decreasing its share of electricity produced from coal and renewable sources.

This analysis will identify companies that will be automatically excluded from the portfolio, and companies which will remain in the portfolio and are subjected to further active ownership strategy.

Thresholds are defined as following:

- companies with a share of coal >XY% and a share of renewables <XY% would be excluded.
- companies with a share of coal <XY% and a share of renewables <XY% would be further evaluated.
- Qualitative assessment of historical company based trends

3) Oil & gas companies: Exclusion criteria relates to an indicator measuring carbon intensity per barrel of oil and unit of gas produced (e.g. measured as CO₂eq. or GHG emissions per Barrel of oil equivalent)

Given this indicator, NBIM sets a threshold for exclusion where carbon intensity is X, and where:

- all companies with a carbon intensity value above this threshold are automatically excluded.
- all companies which are below this threshold remain in the portfolio and are subjected to further active ownership strategy.

In addition to this, NBIM will automatically exclude oil and gas companies which are actively searching for new production in inaccessible and expensive areas, if the production field has a breakeven oil price which is deemed not in line with the achievement of a 2-degree scenario.

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Illustrative examples of exclusion criteria for the sectors oil & gas and utilities in the GPFG portfolio

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Industry sector: Oil & gas

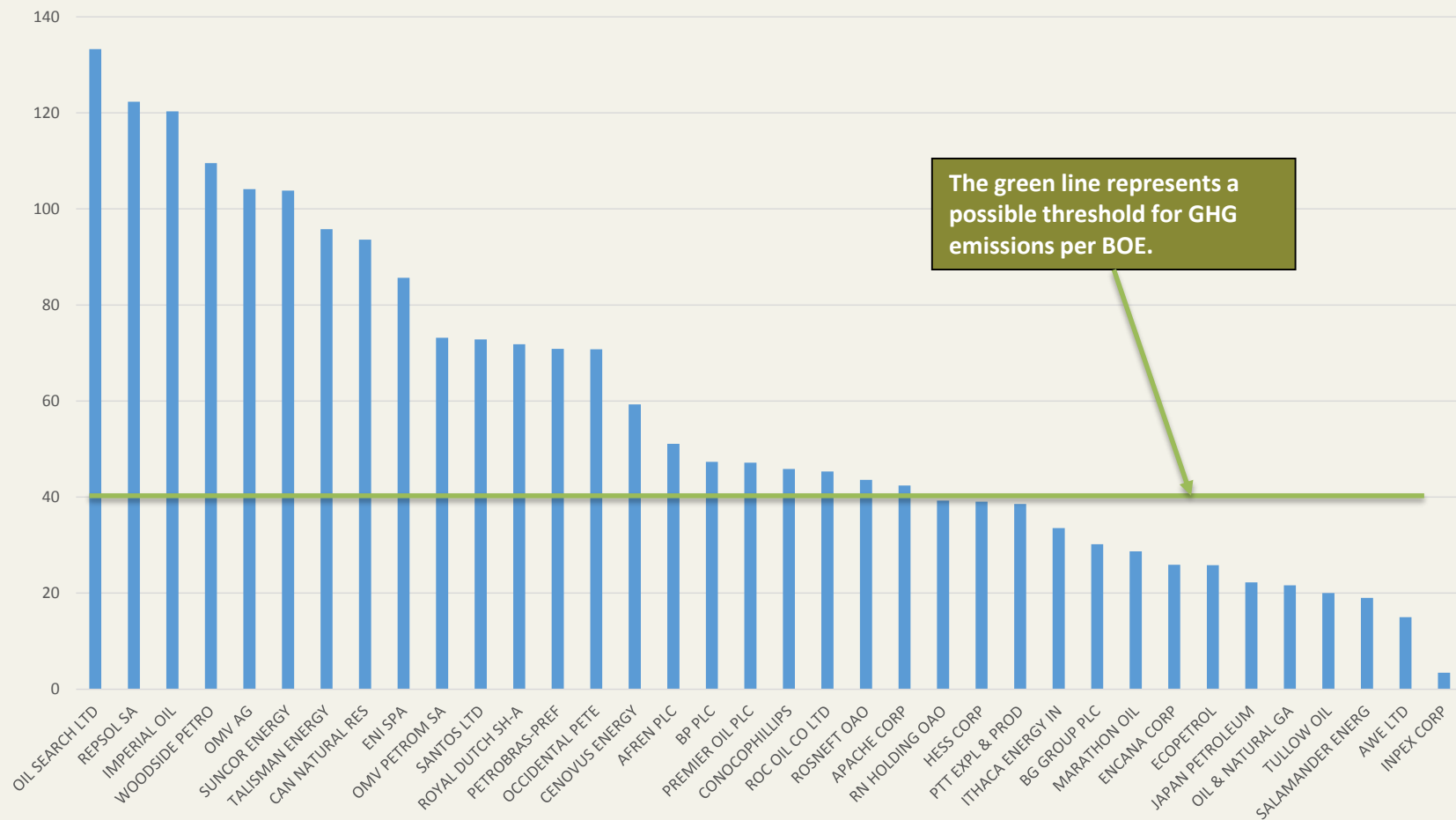
- Base sample: all companies (1000+) in the oil&gas sector according to ICB classification.
- Final sample: Bloomberg provides data on GHG emission intensity per BOE (metric tons CO₂/BOE) for 43 companies. 41 of those are present in the GPFG's portfolio (per 31.12.2013). Of the 41 oil&gas companies within GPFG's portfolio, 5 were excluded as outliers within our sample.
- These 36 companies represent 43% of the value of the whole GPFG's oil & gas portfolio.

Source: Bloomberg Professional® service.



Oil & gas companies: criteria for exclusion (no outliers)

GHG emission intensity per unit of BOE (barrel of oil equivalent) produced, in metric tons per BOE. Data for 36 companies in the oil & gas sector (5 companies excluded as outliers).
(Source: Bloomberg terminal, accessed may 2014).





Industry sector: Utilities (electric)

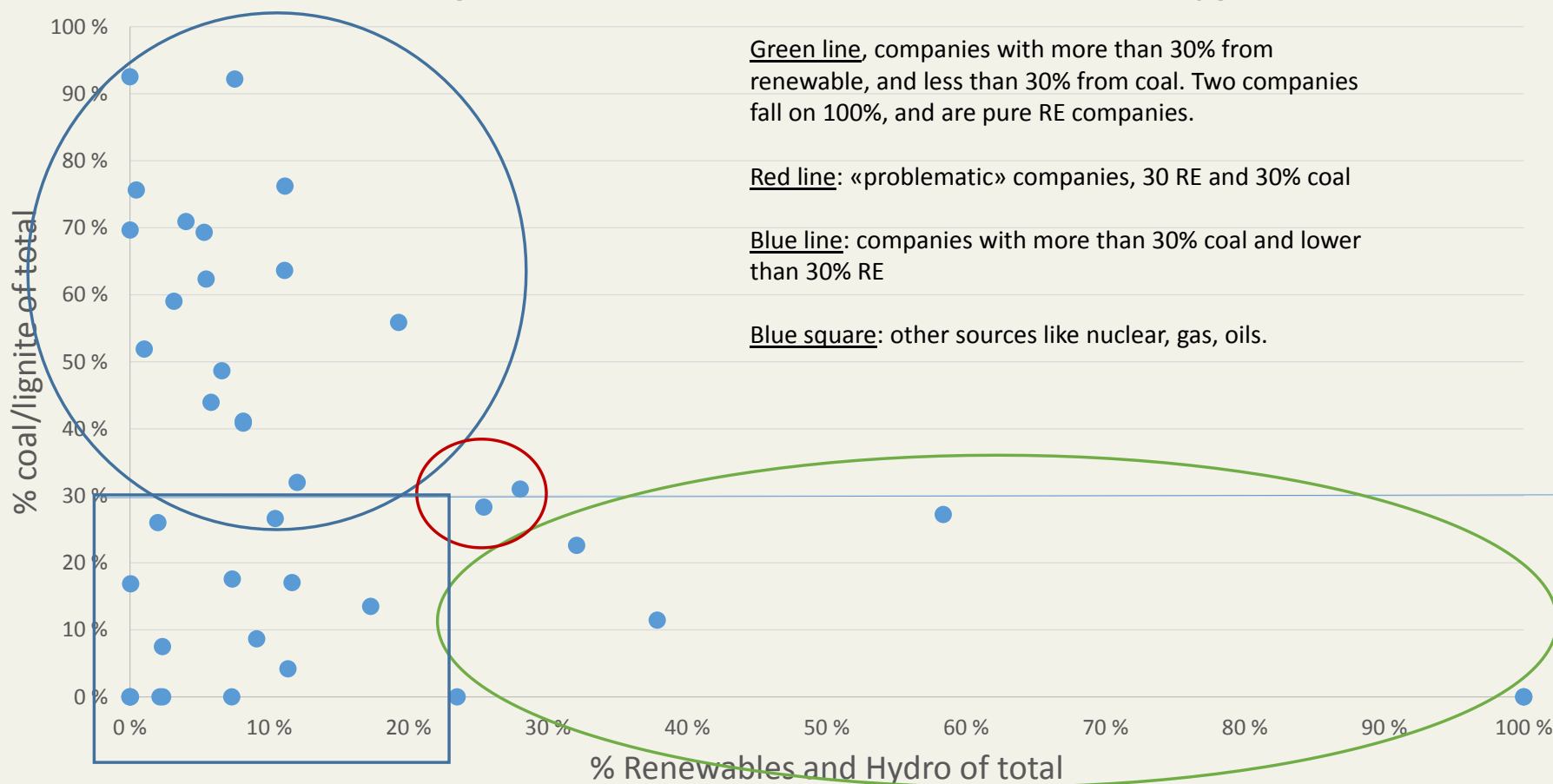
- Base sample: WWF has examined the 72 largest holdings (ranked by NAV base = net asset value) in the GPFG's equity portfolio (within the sector «Utilities» only). These companies represent 80% of the total NAV base in the GPFG's utilities portfolio.
- Final sample: 40 electric utilities. The remaining utilities companies were water, waste or other type, and have thus been excluded.
- The 40 companies covered constitute 60% of the value of the GPFG's utilities portfolio.

Source: Carbon Disclosure Project and companies' annual reports.



Electric utilities, share of RE vs coal

40 electrical utilities (among the top100 holdings in GPF's utilities list) representing ca. 60% of .
Distribution according to share of coal vs share of renewables (% of total electricity generation)





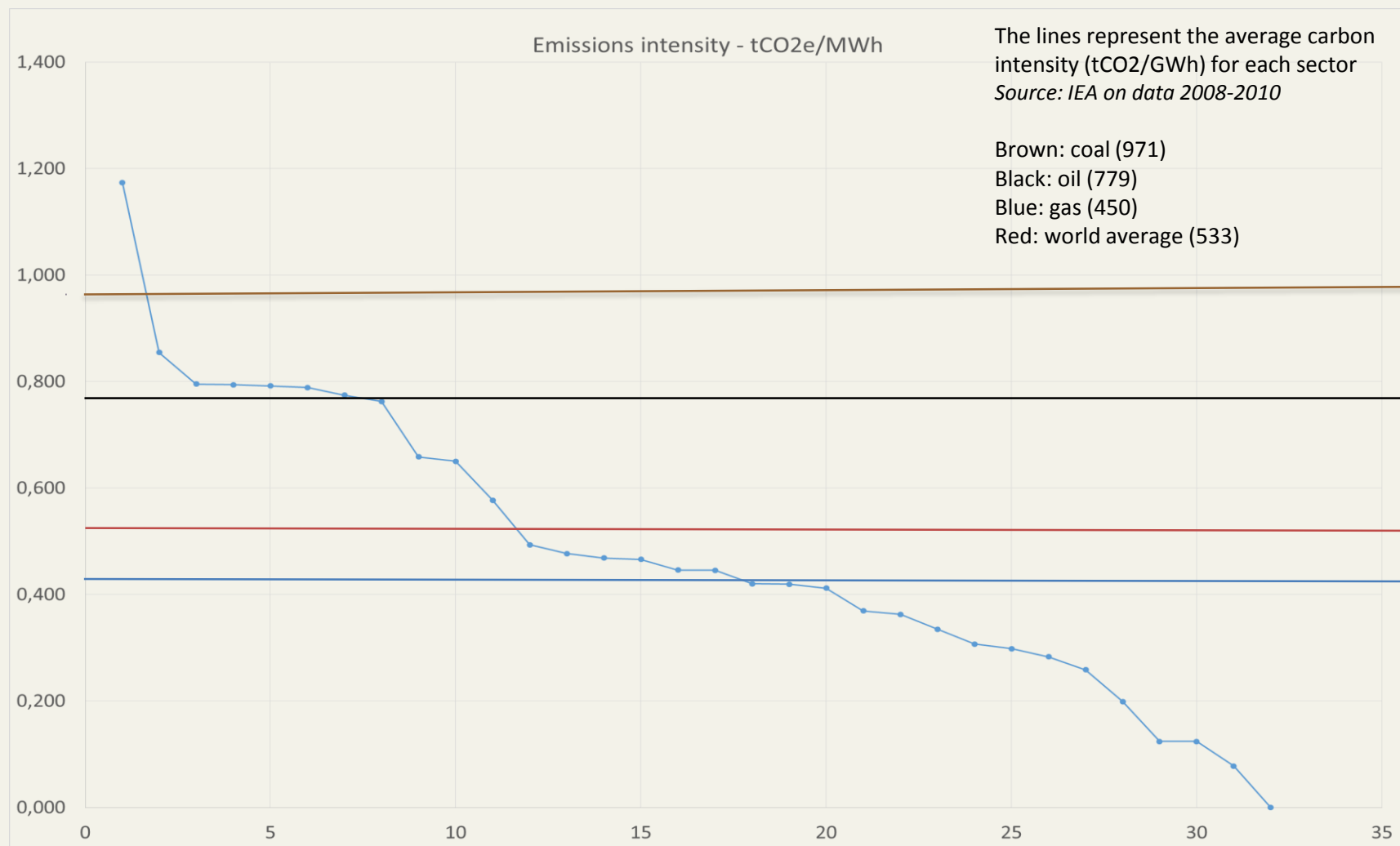
Electric utilities: carbon intensity (tCO₂/GWh)

The next graph shows the carbon intensity (metric tons CO₂/GWh) of 32 companies (where data is available), and the lines indicates the industry average for oil, gas and coal.

*Sources: Carbon Disclosure Project; Companies' annual reports.
Industry averages from IEA on data 2008-2010*



Electric utilities: carbon intensity (tCO₂/GWh)





Thank you

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