The EIB Group PATH Framework

Version 1.1 October 2022

Supporting counterparties on their pathways to align with the Paris Agreement



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For further information on the EIB's activities, please consult our website, www.eib.org. You can also contact our info Desk, info@eib.org.

European Investment Bank 98-100, boulevard Konrad Adenauer L-2950 Luxembourg +352 4379-1 info@eib.org www.eib.org twitter.com/eib facebook.com/europeaninvestmentbank youtube.com/eibtheeubank

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1. Introduction

- 1.1. As the EU climate bank and a public institution, the EIB Group is committed to support its clients to transition towards a low-carbon and climate-resilient future: in other words, to align their operations over time with the goals and principles of the Paris Agreement.
- 1.2. As set out in the <u>Climate Bank Roadmap</u> (CBR), the principal way in which the EIB Group can advance this transition is through the provision of finance and advisory services to invest in **Paris-aligned projects** investments in physical, human and natural capital consistent with a pathway towards low-carbon and climate-resilient development. The CBR, approved in November 2020, provides a clear interpretation of alignment in the context of EIB Group projects and products.
- 1.3. EIB Group support does not end, however, with the project alone. It is important to situate the project within the context of **counterparties' wider corporate activities** and their impact on the environment. The Group wishes to support specific investments within the context of a clear understanding how the counterparty intends to transition to a low-carbon and climate-resilient future and be able to support a counterparty, where appropriate, in making this transition. The EIB Group also needs to be able to address legitimate concerns from stakeholders around the risk of "**greenwashing**" i.e. providing financial support to a company that continues to engage inactivities that are difficult to reconcile with the long-term goals of the Paris Agreement.
- 1.4. This document presents the EIB Group framework to support the Paris Alignment of counterparties or PATH framework. It responds to a commitment made under the CBR to come forward in 2021 with counterparty alignment guidelines. It supersedes the existing EIB practice, set out in the CBR, which is based solely on presenting the wider decarbonisation plans of high-emitting borrowers in the Board report.
- 1.5. The framework presented in this document refers solely to lending and equity operations. For treasury investments, which by their nature do not lend themselves to counterparty engagement, a dedicated methodology adapted to financial markets has been developed under the principles of the PATH framework.
- 1.6. The regulatory landscape is evolving rapidly and the framework will need to change over time, reflecting the changes in EU legislation, global climate policies, the progress of EIB's counterparties against the goals of the Paris Agreement and stakeholder expectations, as well as lessons learned during the application of the framework. This PATH framework is introduced within the wider context of the CBR 2021-2025 and, as such, will undergo a midterm review and assessment.

- 1.7. This document is organised as follows. This section provides background and context on corporate alignment commitments, in light of European and national climate targets, as well as a summary of the evolving regulatory framework. Section 2 sets out the key principles applied by the EIB Group in developing this framework. Section 3 sets out the scope of the framework distinguishing between different types of typical EIB Group counterparties. Sections 4 to 5 present in turn the approach for corporates and financial intermediaries.
- 1.8. In line with the general principle of introducing changes in EIB Group procedures adopted in the CBR and the EIB's Energy Lending Policy (ELP), the PATH framework will be applied to all new operations being considered for appraisal from 1st January 2022. It will not apply to operationsalready under appraisal if approved before the end of 2022.

Background

- 1.9. The 2020s are the critical decade in the fight against climate change. The impacts of climate change are becoming more pronounced and the world needs to transition quickly to maintain a reasonable chance to meet the temperature goals of the Paris Agreement and adapt to the unavoidable impacts of climate change. This is confirmed by the Sixth Assessment Report of the IPCC. Published in April 2021, the IEA Net Zero Flagship Report estimates that just over 40 countries have adopted a net zero pledge, corresponding to approximately 70% of global CO2 emissions and GDP. Within the EU, political agreement has been reached on the EU Climate Law, including a legally-binding target of climate neutrality at the EU level by 2050, together with an ambitious 2030 climate target of at least 55% reduction in net emissions of greenhouse gases compared to 1990.
- 1.10. Businesses are following suit. **Many large corporates and financial institutions** have either set or committed to set ambitious climate targets. Businesses are increasingly scrutinised on their climate performance in relation to managing transition and physical climate risks. For example, over 1,000 corporates have committed to set science-based targets on the Science-based Targets initiative (SBTi). The Net-Zero Banking Alliance brings together forty-three banks that have committed to set net zero 2050 targets. Fifty-five financial institutions are planning to use the SBTi Guidance on target setting for the financial sector. The Transition Pathway Initiative (TPI), for example, publicly assesses the Paris alignment of high-emitting companies. The Taskforce on Climate-related Financial Disclosures (TCFD) and initiatives like the Carbon Disclosure Project (CDP) provide platforms and guidance for businesses to report on their management of emission reductions as well as transition and physical climate risks. Moreover, investors have started picking up this data to steer their portfolios towards better-aligned companies.¹

¹ For example, FTSE Russell warning non-aligned companies to improve climate performance or be deleted from their FTSE4Good Index or the Climate Action 100+, an investor-led initiative working with the world's largest corporate greenhouse gas emitters take necessary action on climate change, covering 80% of global industrial emissions.

- 1.11. In parallel, the regulatory framework on sustainability reporting is evolving quickly. In response to perceived shortcomings of the existing reporting framework for corporate sustainability, the Commission has issued a proposal for a Corporate Sustainability Reporting Directive (CSRD). This addresses disclosures relating to both climate mitigation and adaptation. This proposal is intended to apply to all large and listed corporates² from 2024 (i.e. reporting on activities in 2023). Under the proposal, a considerable portion of EIB Group counterparties would be obliged to meet standardised sustainability reporting practices over the coming years. This includes describing their strategy on ensuring the compatibility of their plans with the transition to a sustainable economy, including the limiting of global warming to 1.5°C in line with the Paris Agreement, outlining any targets it has set, and describing its resilience to different climate scenarios. More details on the proposed CSRD, including its relationship with the EU Taxonomy, are provided in Annex 1 to this document.
- 1.12. There are several other regulatory initiatives relevant to EIB Group counterparties. For financial market participants, for example, including investment fund managers, the Sustainable Finance Disclosure Regulation (SFDR) has entered into force on 10 March 2021. For banks operating in the Eurozone, a key reference point is also the Guide on climate-related and environmental risks published by the European Central Bank (ECB).

This guide, designed to meet new supervisory expectations associated with transition and physical climate risk, is anchored in the EC's Guidelines on non-financial reporting which in turn integrates the recommendations of the TCFD. Finally, under its mandate set out in the Capital Requirements Regulation, the European Banking Authority (EBA) has published draft technical standards for ESG disclosures specifying uniform disclosure formats, building on the recommendations of the TCFD.

² Large companies not listed on regulated markets are defined as companies that exceed at least two of the following criteria: (i) a balance sheet total of €20m; (ii) a net revenue of €40m; and (iii) an average number of 250 employees during the financial year. The Commission estimates that this will result in around 50,000 companies reporting sustainability information, compared to the current 11,600 companies that are within the scope of the Non-Financial Reporting Directive.

2. General approach of the PATH framework

- 2.1. This section sets out the key principles applied by the EIB Group in designing this alignment framework.
- 2.2. The overarching aim of the framework is to engage with counterparties that are either aligning or willing to align with the goals of the Paris Agreement. It does not intend to restrict supportonly to those counterparties that are already aligned. This reflects the goal of the Paris Agreement itself to make finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.
- 2.3. In practice, the need to align is most acute for companies in high-emitting sectors and those operating in a context of high climate vulnerability. This framework therefore focuses on these counterparties. In this sense, the approach developed below is targeted and proportionate.
- 2.4. As already referred to in the Introduction, the regulatory environment towards corporate sustainability reporting and climate-related disclosures, as well as best practices on climate management, is evolving fast. The PATH framework aligns with these developments as much as possible. In particular, it builds closely on existing and anticipated disclosure requirements within the EU, as well as the growing importance of reporting practices based on the recommendations of the TCFD. More details on the EU regulatory framework can be found in Annex 1.
- 2.5. As the EU Climate Bank, the EIB Group encourages counterparties to be ambitious in determining their alignment plans. However, it is clear that each counterparty will develop its own strategy, target and processes on its pathway to align reflecting the specific set of regulatory, technical, financial and economic constraints facing a particular business. It is not for the EIB Group to prescribe a particular solution or target. The counterparty remains solely accountable for its climate-related ambitions and targets, strategy, policies and procedures.
- 2.6. Whilst it is for the counterparty to determine its strategy, a clear and well-motivated explanation of the strategy should be available in the public domain for all stakeholders. Building on anticipated regulatory requirements, and as set out in more detail in section 4, the PATH framework promotes this transparency, placing particular focus for corporates on mid-term targets (5 to 10 years into the future) and options to decarbonise thereafter as well as increase its capacity to manage physical climate risk.

- 2.7. As a public institution, the Group wishes to support actively counterparties who are setting out on their transition pathway. In particular, where counterparties have not yet developed plans, or wish to update existing plans, the EIB Group can provide technical assistance to support the development of alignment strategies over a relatively short period of time. This may be particularly relevant for counterparties operating in regions most exposed to future climate change, or smaller or regional operators engaged in sectors that are challenging to decarbonise. Such technical assistance will be available both within and outside the EU.
- 2.8. The PATH framework is suitable for counterparties based outside of the EU. Whilst building on the EU regulatory environment, the framework needs to be flexible to work with counterparties across the world. The principle of common but differentiated responsibilities and respective capacities is central to the Paris Agreement and the CBR. This principle is reflected in the PATH framework, notably in the focus on explaining a particular climate strategy within the relevant regulatory and operating environment. The framework recognises that the adoption and disclosure of climate plans and targets can be a more complicated and lengthy process for counterparties based outside of the EU and that technical assistance needs to be available.
- 2.9. Whilst the PATH framework is centred on encouraging the transition, there needs to be a bottomline. For instance, it is difficult for a counterparty to defend a plan to decarbonise progressively over time, if, at the same time, it continues to invest in new long-lived assets which significantly increase emissions (e.g. new coal-fired power plant). As explained in more detail in Section 4, the PATH framework therefore limits EIB support to corporates that continue to invest in such activities to very specific circumstances involving innovative low-carbon projects.

3. Scope

- 3.1. This section sets out the scope of the PATH framework i.e. the types of counterparties to which it applies. The EIB Group essentially deals with four types of counterparties: sovereigns and sub-sovereigns; financial intermediaries, corporates and special purpose vehicles (SPVs). Note the term corporates covers companies operating under private law or public law (PSEs).
- 3.2. This framework is designed to apply to corporates and financial intermediaries at appraisal stage. It does not apply to sub-sovereigns and sovereigns, which are direct signatories of the Paris Agreement. The EIB Climate Bank Roadmap sets out the Group's approach towards supporting countries and municipalities to align, in particular through National Energy and Climate Plans, Nationally Determined Contributions or National Adaptation Plans.
- 3.3. In line with the EU regulatory framework, the PATH framework applies to **medium-sized or large corporates** and significant financial intermediaries and does not apply directly to small companies. In the context of EIB Group support to SMEs, it is worth recalling that the EIB Group Climate Bank Roadmap already sets out a clear alignment framework.
- 3.4. The PATH framework focuses on the EIB borrower, rather than a guarantor or promoter. Where a borrower is a fully consolidated subsidiary, subject to section 3.5 below, the Head of Group (the parent) will be assessed. This approach reflects the fact that the Head of Group has control over the subsidiary, and therefore the Head of Group climate policies also apply to their governed entities. However, for engagement purposes set out in Section 4 below, EIB may work with the borrower, and not the Head of Group, where duly justified in emission or resilience terms. The PATH framework does not extend beyond the borrower to consider, for example, customers and suppliers.
- 3.5. While subsidiaries are in scope of the PATH framework through the consolidated group approach, the framework does not apply to entities of a ring-fenced nature with more than one shareholder. This is because such entities, including Special Purpose Vehicles (SPVs) established for the sole purpose of financing a single isolated project (e.g. project finance), and funds, are assessed under the alignment framework of the CBR. As referred to in the Introduction, the PATH framework is designed to reduce the risk of EIB Group funds which ultimately are fungible from being used to support the wider corporate activities of a counterparty that is not in the process of aligning its activities. In the case of non- or limited-recourse funding structures, the proceeds of EIB Group finance are legally ring fenced i.e. they are not fungible to support the balance sheet of equity sponsors or wider equity participants. In addition, as set out in the CBR, the EIB only supports aligned assets through such non- or limited-recourse structures. It is therefore appropriate to deem these types of operations out of scope. The PATH framework does not extend beyond the vehicle to consider, for example, shareholders, contractors, offtakers or suppliers.

4. Methodology for corporates³

- 4.1. This section sets out the key elements of the methodology for corporate borrowers. As presented above, the aim of the PATH framework is to focus on high-emitting corporates, as well as those exposed to a high degree of physical risk from climate change. The first part below defines "high emitting" and "high degree of physical risk". The section then turns to highlight some of the key features of a corporate climate strategy which have been used to shape EIB engagement.
- 4.2. As highlighted earlier, the PATH framework covers both low-carbon and climate resilience aspects of a corporate strategy. In the next paragraphs, the treatment of low carbon aspects is elaborated in more detail than resilience aspects. This reflects the comparatively lean and flexible approach towards resilience in the PATH framework, in turn recognizing the relatively early stages in the development of physical climate risk management systems of corporates and leaving room for consideration of diverse operational risk contexts. As stressed in section 2, the aim of the EIB is to engage on this issue and provide support, where appropriate, rather than exclude.

Identifying relevant corporates

- 4.3. The first step is to identify corporates that are in high emitting sectors and/or operate in a context of high climate vulnerability.
- 4.4. A corporate is defined as **high emitting** if it has more than 20% of annual turnover from one or more of the following high-emitting sectors:
 - Consumers of large amounts of fossil fuels, either to generate heat or as a feedstock, forexample energy-intensive industry such as steel, cement and chemicals.
 - Corporates that use fossil fuels to generate electricity or produce heat.
 - Producers of fossil fuels, including oil, gas and coal.
 - Industries that are associated with high emissions, either indirectly, such as car manufacturers or more directly (e.g. provision of transport services; airports).
- 4.5. Annex 2 provides a full list of these sectors. This is based on a detailed assessment of emissions data within the EU.
- 4.6. The second dimension concerns counterparties operating in a context of high vulnerability to physical climate risks. Vulnerability is determined on the basis of the split of revenues in combination with data on physical climate risk. This is used to determine a score with corporates above a certain threshold being deemed as vulnerable. Examples of activities that may be deemed as highly vulnerable might include an agricultural company or industrial facility that requires significant fresh water inputs, as well as potentially exacerbating water stress for the wider community. As set out below, this triggers a particular course of EIB engagement.

³ The term corporates is used to refer to corporates operating both under private law and public law (i.e. so called "public sector entities").

Key elements of corporate alignment plans

- 4.7. Having identified the relevant counterparties, this section turns to the key elements of the alignment plans which shape the PATH framework engagement strategy. In examining the low-carbon dimension, the clear starting point is the need to reduce global greenhouse gas emissions in line with the remaining carbon budget to maintain a reasonable chance to limit global temperatures to 1.5°C.
- 4.8. Figure 1 presents such a decarbonisation scenario for the EU, highlighting the differing pathways for key sectors. Organizations such as the International Energy Agency (IEA) have created similarglobal emission reduction scenarios that show how different sectors need to reduce emissions over time. These scenarios also contain projections for economic development and industrial activities, such as GDP growth, tonnes of steel produced and passenger kilometres flown. Emissions and activities can be used to create emission intensity pathways.

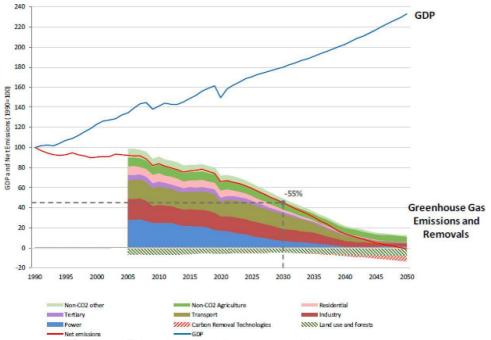


Figure 1: EU pathway to climate neutrality.

4.9. Emission reduction scenarios and sectoral emission intensity pathways can be used to benchmark the emission reduction ambitions of corporates. This is for example done by the Transition Pathway Initiative, which publicly assesses the climate ambitions of the world's largest emitters, and the Science Based Targets Initiative, which works with companies to set effective emission reduction targets. For the most carbon-intensive industrial sectors, such as steel and cement, specific emission-intensity decarbonisation pathways exist. For others, such as chemicals, these currently do not exist. If a company converges towards the 2050 carbon intensity of this pathway, TPI rates the company as having a Paris-aligned emission target. An illustration of the steel sector, reproduced from TPI, is shown in Figure 2.

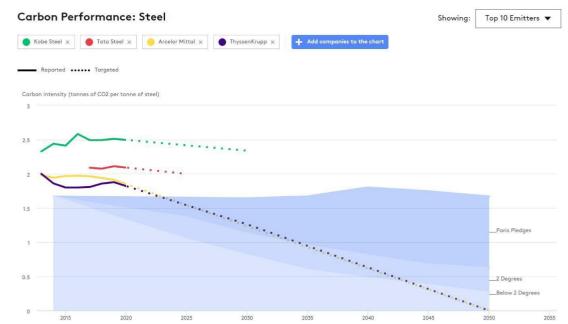


Figure 2: TPI carbon performance assessment of a selection of steel manufacturing companies.

- 4.10. As stressed in Section 2, it is for each corporate to define and explain its alignment strategy. With this in mind, and in light of the need to decarbonise rapidly in the critical decade and to achieve balance between emission sources and sinks by 2050, the PATH framework is developed around the public disclosure of two crucial elements to a decarbonisation plan:
 - A mid-term, rolling⁴, quantitative emission reduction target (e.g. 5 to 10 years into the future – i.e. aligned to the typical financial relationship through an EIB corporate loan);
 - 2. Options over a longer time horizon to achieve carbon neutrality towards mid-century.
- 4.11. The choice of a particular target should be motivated in the specific context of the corporate and the geography in which it operates. Analysis of emission reduction scenarios⁵ suggests global emissions need to fall by at least 4.2% on an annual linear basis from 2020 in order to limit the annual mean global temperature increase to 1.5°C. This value is considered as a **valid reference point** for the PATH framework to benchmark a corporate target. If a corporate is planning to decarbonise at that rate, or more quickly, this suggests the corporate is broadly ontrack to become aligned.

⁴ Rolling refers to the fact that over the lifetime of the EIB loan, civil society will expect corporates to update their targets periodically, for example recommended every 5 years, in line with best practice.

⁵ SBTi analysis based on scenarios from the Integrated Assessment Modelling Consortium (IAMC) and the International Energy Agency (IEA). The IAMC hosts an ensemble of more than 400 peer-reviewed emissions pathways, which have been compiled and assessed by the authors of the Intergovernmental Panel on Climate Change (IPCC).

- 4.12. This will not always be the case. There may be reasons why a corporate is not able to achieve such an absolute emission reduction rate in the medium term. It may already be relatively low carbon, compared to sector averages. It may belong to a "hard to abate" sector with no viable economic low-carbon alternative available in the short term. It may be operating in a region either without a national GHG emission target, or with one that does not imply steep absolute emission reductions. Corporates may face particular challenges to decarbonise rapidly given constraints around competitiveness and economic capability, as recognized in EU climate and energy legislation. In such cases, it is therefore important that the company motivates its existing targets in this context and makes reference to future actions or options to accelerate decarbonisation (e.g. replacing existing capital assets, once reaching life expiry, with zero-emission alternatives). This motivation, disclosed to the public, allows all stakeholders to come to a view on the corporate strategy.
- 4.13. The role of offsetting in the plan should be clearly presented, in particular where reliant on the **voluntary carbon market**. In line with good practice⁶, corporate plan should clarify whether offsets are used to supplement, rather than substitute for, reductions in emissions within the corporate value chain and the impact of offsetting on the proposed target. Plans should be clear about the criteria/approach to be used to source offsets.
- 4.14. Building on the proposed CSRD requirements, the plan should also indicate to the extent possible how the proposed alignment strategy takes into account of the interests of stakeholders, including in particular social partners. Disclosure on these issues can help inform and shape measures to ensure a just transition.
- 4.15. As set out above, a similar approach applies with respect to corporates operating in a context of high vulnerability to current or future **physical impacts of climate change**. In line with the evolving EU regulation and global reporting practices such as the TCFD recommendations, it is for each corporate to determine its management approach towards physical climate risks and disclose accordingly. A key issue is whether the corporate has identified and considered material physical climate risk in their business strategy, and this is translated into risk management procedures to inform operational decision-making.

⁶ For example, see SBTi Foundations for science-based net-zero target setting in the corporate sector

EIB engagement with corporates

- 4.16. The section turns to EIB engagement with corporates, based on the key elements of the corporate alignment strategy set out above. In short, and in the context of supporting an aligned project, the PATH framework groups corporates into one of two categories: those to whom the EIB requests certain actions to create or improve their alignment strategy over time; and those to whom it does not.
- 4.17. From a low-carbon perspective, the EIB will not request any further development of an alignment strategy from corporates whose current strategy either:
 - is rated as aligned by leading independent organizations (such as the SBTi or TPI) and has been publicly disclosed; or
 - meets the conditions in paragraph 4.10 and with a mid-term target that implies an annual linear emission reduction rate greater than or equal to the PATH framework reference rate referred to in paragraph 4.11; or
 - meets the conditions in paragraph 4.10 and with a mid-term target that implies an annual linear emission reduction rate less than the reference rate referred to in paragraph 4.11, but with a clear motivation as referred to in paragraph 4.12. This includes an explanation of the derivation of the target, as well as referencing it within the context of relevant national/international climate targets. Moreover, the options after the mid-term reflect theneed to accelerate decarbonisation.
- 4.18. In all other cases, corporates are contractually required to create and publish an alignment strategy, or revise their existing alignment strategy to address the points set out in paragraphs 4.10 to 4.12 and report to the EIB accordingly. This should occur within 12 months of the EIB finance contract signature. For corporates operating outside the EU, some flexibility can be considered in timing to reflect the wider operating environment of the corporate and/or the availability of technical assistance, as well as in the case of need for upstream engagement with public authorities for state-owned entities. Failure to comply with this contractual obligation would constitute a breach of contract. During the mid-term review of the PATH framework outlined in section 1.5 above, the EIB will look into further developing its rules of engagement. The application of financial incentives linked to the counterparties' performance against targets could be explored.
- 4.19. On the resilience side, the EIB will engage with high-vulnerability corporates that either do not have an alignment strategy at all, or where, as explained in paragraph 4.15, the strategy does not address the climate vulnerability context of their business model and the capacity to manage and reduce physical climate risk. If so, as with the low-carbon dimension, the corporate will be asked to publish a strategy, or revised strategy, within 12 months of the EIB finance contract signature, with the same potential flexibility in timing outside of the EU. The EIB recognises that some corporates will require support in order to identify material physical climate risks for their business models and to develop appropriate risk management systems, particularly in the case of highly vulnerable developing countries. It is important for EIB at this stage to engage and provide targeted support. The EIB Adaptation Plan will provide the wider overview as to how the EIB will strengthen upstream engagement with clients and wider market participants as well as advisory services to promote adaptation and resilience.

- 4.20. The EIB will report factually on the application of this framework in the Board report and will disclose accordingly as part of its wider commitment regarding environmental information within the ESDS (at approval stage) and ESCS (at completion stage).
- 4.21. In general, a corporate is considered to be aligning under this PATH framework i.e. engaged in the transition process if it meets the conditions set out in paragraphs 4.17 to 4.19. The exception to this general approach is considered next.

Activities incompatible with the Paris Agreement

- 4.22. It is difficult for a corporate to present a credible strategy around Paris alignment if, at the same time, it continues to invest for example in new high-carbon assets that are difficult to reconcile with the long-term goals of the Paris Agreement. In a recent report on <u>Net Zero by 2050</u> the IEA has drawn attention to the need, under a 1.5 degree scenario, to cease development of new coal-fired power plants or new oil and gas fields.
- 4.23. The PATH framework therefore introduces a list of activities which is incompatible with the goals of the Paris Agreement. These are:
 - **Oil and gas**: No new investment in high-carbon oil production techniques⁷ (e.g.tar sands, or oil shales), nor investment in new drilling for oil and gas in the Arctic region. In terms of existing assets, no increase in the level of oil production⁸, nor routine flaring of methane and best practice on methane loss reduction.
 - Coal: No investment in new thermal coal mines or new coal-fired⁹ power plants. In terms of existing assets, no production of thermal coal, except by integrated power utilities motivated by their own demand, which have, or agree to develop, a decarbonisation plan consistent with the PATH framework. This plan should cover all group activities, including coal mining.
 - Carbon sinks. Conversion of land, notably for agricultural and urban activities, that directly (e.g. through cropping or animal rearing activities) destroys high-value carbon sinks and ecosystem services which enhance resilience, such as rainforests and marshlands. ¹⁰

All corporates in scope - save for some limited exceptions set out in paragraph 4.26 below - will be required to undertake not to engage in these activities.

4.24. Under the PATH framework, the EIB will not in general support a project with a corporate that continues to engage in the incompatible activities set out in paragraph 4.23 with the sole exception of the conditions set out in paragraph 4.27. This is, in effect, the EIB bottom line. Although the positions of oil and gas producers are rapidly evolving, this framework will significantly restrict the capacity of the EIB Group to support such counterparties on balance sheet today.

⁷ Higher-carbon production techniques refer to the commonly-recognized industry classification of unconventional oil covering heavy oil, extra heavy oil, oil sand, tar sands, oil shale and bitumen

⁸ Increasing oil production will be measured as annual production compared to peak annual production over the period 2015 to 2020.

⁹ Defined as solid fossil fuel fired power stations (peat, soft brown coal and hard brown coal), in absence of CCS.

¹⁰ As per the EU Renewable Energy Directive, this is defined as expansion of agricultural activities in land that had a status of high carbon stock and high biodiversity areas on 1st January 2008. This includes primary and secondary forests, peatlands, wetlands and natural grasslands, as well as mangroves and coral reefs.

- 4.25. The EIB energy lending policy already restricts the types of carbon-intensive projects that the Bank can support. Since its adoption in 2019, the Bank no longer supports energy projects reliant on fossil fuels (e.g. production of oil or natural gas; power generation above 250 gCO₂ per kWh of electricity generated averaged over the lifetime for gas-fired power plants; large scale heat production basedon unabated oil, natural gas, coal or peat). The Climate Bank Roadmap further restricts support to research, development and innovation in products dedicated exclusively to the coal, oil and gas sectors. The PATH framework provides a consistent final layer, restricting EIB support further based on the wider activities of the counterparty set out in paragraph 4.23.
- 4.26. This said, the EIB Group recognises that oil and gas producers are in a strong position to invest in particular types of innovative low-carbon projects which are critical to the achievement of net zero emissions. One example is carbon capture, utilisation and storage (CCUS) which lends itself to extensive oil and gas industry experience with large-scale engineering, pipelines and sub-surface operations. Nearly three-quarters of CO₂ captured in large-scale facilities today is captured by oil and gas companies. A second example, based on long-term experience in liquid and gaseous fuel processing and refining, would be production of renewable hydrogen-based fuels. Other examples might include the production of advanced biofuels, in which many oil and gas companies have active R&D programmes, or experience in working in offshore locations relevant to installing and maintaining floating offshore wind farms.
- 4.27. The EIB could therefore present for approval to the Board demonstration projects and early commercial deployment of low-carbon technologies with excellent innovation content, as measured by the Bank's additionality framework (AIM). As mentioned, examples could include carbon capture, utilisation and storage (CCUS), renewable hydrogen, advanced biofuels, deep geothermal and floating offshore wind. Demonstrating the large-scale deployment of these low-carbon technologies will provide significant wider benefits central to driving deep decarbonisation.
- 4.28. In support of the REPowerEU Plan, the exception under paragraph 4.27 will also be applied to companies seeking EIB financing for renewable energy projects and electric vehicle charging infrastructure inside the EU as long as they do not plan new greenfield investments in coal power plants or mines. This change is effective as of the 26th of October 2022 and runs until 31 December 2027. This change and its implementation are subject to the Climate Bank Roadmap review and assessment expected in 2025 as per paragraph 1.6. The requirements set out in paragraphs 4.17 to 4.19 continue to apply to these counterparties. The Board will continue to be informed about whether any counterparty is involved in the incompatible activities presented in paragraph 4.23.

5. Methodology for financial intermediaries

- 5.1. Unlike corporates, financial intermediaries (FIs) are not direct emitters, nor are they directly responsible for reducing physical and transition climate change risks. Furthermore, assessing the greenhouse gas emissions and climate change risks within a lending or investment portfolio can be complex, not least because of the lack of reliable data.
- 5.2. However, the perception of the roles and responsibilities of FIs on climate change is changing. FIs are progressively expected to engage with their borrowers and investees and support them in their transition to a low-carbon and climate-resilient world. The European Central Bank (ECB) has communicated clear expectations to banks operating in the Eurozone. As discussed in section 1, and outlined in Annex 1, the proposed text for the Corporate Sustainability Disclosure Regulation (CSRD) significantly enhances the scope of the existing rules to cover all large undertakings including banks as well as all those listed on EU regulated markets and expands the scope of the existing reporting requirements under the Sustainable Finance Disclosure Regulation (SFDR) and the EU Taxonomy regulation.
- 5.3. Under its mandate set out in the Capital Requirements Regulation, the European Banking Authority (EBA) has published <u>draft technical standards</u> for ESG disclosures specifying uniform disclosure formats, building on the recommendations of the Financial Stability Board <u>Task Force on Climate-Related Financial Disclosures</u> (FSB-TCFD). The SFDR, which took effect from 10 March 2021, lays down sustainability disclosure obligations for manufacturers of financial products and financial advisers.
- 5.4. The EIB Group approach under this PATH framework needs to be placed in context. The <u>ClimateBank Roadmap</u> already sets out a clear alignment framework for multi-beneficiary investment loans (MBILs) and similar intermediated products, focusing on the core energy, transport and energy-intensive industry sectors. Moreover, only infrastructure funds whose investment strategies are fully aligned with the CBR are supported.
- 5.5. EIB Group is already adopting tighter standards with respect to the environmental performance of FIs. The proposed Standard 11 under the forthcoming updated EIB Environmental and Social Sustainability Framework (ESSF) has the intention to require EIB FIs to identify, manage and monitor the environmental and social impacts and risks arising from sub-projects, in line with applicable requirements and commensurate with the sub-project's size, nature, sector, sensitivity to environmental and social risks, socioeconomic context and location. In parallel, EIF is revising the ESG principles under the ESSF, taking into consideration relevant initiatives in the PA context, such as the ESG assessment of fund managers and banks, newly added restricted sectors and activities, climate risk portfolio assessment as well as institutional climate- and ESG-related reporting.

¹¹ Civil society organisations, such as Client Earth, are already pressuring Banks to clarify their engagement strategies (FT, 27 May 2021). Banks are also expected to do more on managing climate change risks, as illustrated by the ECB Guide on climate-related and environmental risks (ECB, November 2020), the EBA Report on management and supervision of ESG risks for credit institutions and investment firms (EBA, June 2021) and the BIS/BCBS reports on climate-related risks management and measurement methodologies.

- 5.6. The PATH framework for FIs will focus on large and significant counterparties, taking into account the wide diversity of FIs in terms of sizes and resources but also their portfolio's impact on CO2 emissions. Financial institutions with more than €30bn (or currency-equivalent) in total assets¹² or who are among the three largest in their country will be in scope, as well as fund managers with Assets under Management of more than €500m (or currency equivalent). Sovereigns, sub-sovereigns as well as microfinance, business angels, guarantee institutions are out of scope. In the case of National Promotional Institutions (NPIs), as partner institutions, the EIB Group will seek to share best practices on Paris alignment, including on disclosure.
- 5.7. Moreover, and in line with existing and forthcoming legislation, under the PATH framework the EIB Group will require all FI counterparties in scope to disclose in line with the TCFD recommendations, including in particular information in relation to transition and physical climate risk. If not currently the case, FI counterparties will have to disclose within 12 months after EIB Group contract signature. As per paragraph 4.18 with respect to corporates, flexibility in timing can be considered for FIs operating outside the EU.
- 5.8. In adopting this disclosure requirement, the EIB Group is cognizant of the ongoing work to develop uniform disclosure formats and technical standards to disclosure the transition and physical climate change risks embedded in banks' lending portfolios. The EIB Group will revisit this point as part of the mid-term review process outlined in section 1.5.
- 5.9. Where helpful, the EIB Group can assist FIs to meet these PATH framework requirements. Technical assistance can be provided to help develop a reporting framework. This may be particularly useful for smaller intermediaries, or those operating outside of the EU. More generally, the EIB Group will engage with interested counterparties in scope to encourage best practice in developing an alignment strategy, including providing guidelines building on leading financialsector initiatives.¹³

¹² For the avoidance of doubt, in line with Section 3.4 above, the reporting obligations of the Financial Institutions in scope will be done on a consolidated basis, i.e. covering also the activities of their subsidiaries with less than EUR 30bn assets.

^{13 13} This includes, but is not limited to the Net Zero Asset Owners Alliance and the Net-Zero Banking Alliance, the Paris Aligned Investment Initiative, IIGCC, the Collective Commitment to Climate Action (CCCA), Net Zero Investment Framework Implementation Guide, IIGCC, the Guidelines For Climate Target Setting For Banks, UNEP FI's Collective Commitment to Climate Action, the Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures: Supplemental guidance for Financial Sector, the CDP for FI, the Coalition for Climate Resilient Investment (CCRI), and the Transition Pathway Initiative — Science based targets for Financial Institutions and the Transition Pathway Initiative

Annex 1: Update on EU regulatory requirements for sustainability disclosure

In line with the goals of the Paris Agreement, there has been an increasing momentum at a global level to foster transparency about how social and environmental challenges are managed both at a national and at a corporate level. This information can help investors, civil society organisations, consumers, policy makers and other stakeholders to evaluate the non-financial performance of large companies and encourages these companies to develop a responsible approach to business.

The Task Force on Climate Related Financial Disclosure (TCFD) was established in 2015 by the Financial Stability Board to develop consistent climate-related financial risk disclosures for use by companies, banks, and investors in providing information to stakeholders. The TCFD recommendations were issued in 2017 and are a voluntary set of disclosures organisations could include in their financial filings or other reports centred around four pillars: governance, strategy, risk management and metrics and targets. Recently the G7 has expressed a willingness to make disclosures in line with the TCFD recommendations mandatory.

In parallel, at the EU level, EU law has been developing to encourage the disclosure by corporates of information on the way they operate and manage social and environmental challenges.

Pursuant to the Non-Financial Reporting Directive (NFRD), which came into force in December 2014, member states were required from December 2016 to require large (500+ employees) public interest entities (including credit institutions and insurance undertakings) to include a non-financial statement in their annual report, covering as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters. This Directive was accompanied by guidelines for companies to disclose environmental and social information and on reporting climate related information. Later, in January 2019, the Commission published new climate reporting guidelines which integrate the recommendations of the TCFD and take account of the forthcoming taxonomy on sustainable activities that is under development.

In April 2021, the Commission proposed a Corporate Sustainability Reporting Directive (CSRD) to replace the NFRD. It enhances the scope of the existing NFRD to cover all large undertakings (rather than just public interest entities) as well as all corporates listed on EU regulated markets and expands the scope of the reporting requirements in line with the Sustainable Finance Disclosure Regulation (SFDR)¹⁴ and the EU Taxonomy Regulation¹⁵. This proposal is intended to apply to all large and listed corporates from 2024. For non-listed SMEs, the EU Commission intends to develop voluntary proportionate standards.

Information provided under the CSRD will need to be audited and will have to cover inter alia: (i) their plans to ensure their business model and strategy are compatible with the aims of the Paris Agreement; and (ii) their targets related to sustainability matters and their progress vs these targets, (iii) the resilience of the undertaking's business model and strategy to risks related to sustainability matters. The European Financial Reporting Advisory Group (EFRAG) is developing reporting standards for the CSRD.

¹⁴ The Sustainable Finance Disclosure Regulation (SFDR) from March 2021 is designed to prevent green-washing in finance and provide a common set of rules on sustainability risks.

¹⁵ The Delegated Act supplementing Article 8 of the EU Taxonomy Regulation will specify disclosure requirements for companies concerning environmentally sustainable economic activities.

Sustainability disclosure is becoming increasingly mainstream for reputable entities, even where it is still voluntary. The CSRD is the latest step in an evolving regime of sustainability disclosure. It will apply to more companies and be more prescriptive about what should be disclosed and in which format. The CSRD will also apply to financial institutions. This is in addition to any voluntary disclosures which corporates are increasingly under pressure to make pursuant to the Task Force of Climate Related Financial Disclosure (TCFD) and to mandatory disclosures that banks are already expected to publish under the ECB's Guide on climate-related and environmental risks ¹⁶ and that will be further expanded following the adoption of the EBA technical standards on Pillar 3 disclosures of ESG risks.

In anticipation of this upcoming legislation on climate related disclosure and to help its counterparties prepare, the EIB's PATH framework focuses on requesting corporates to disclose their mid-term emission reduction targets and their long-term decarbonisation options as well as their resilience preparedness. For financial intermediaries, it requests disclosure according to the TCFD's requirements.

¹⁶ The ECB Banking Supervision's "Guide on climate-related and environmental risks" was published in November 2020. It includes a set of expectations on climate-related and environmental risk disclosures. These expectations correspond with the aforemental recommendations of the TCFD.

Outline of the proposed Corporate Sustainable Reporting Directive

Article 19a on page 42 of the Corporate Sustainable Reporting Directive proposal (CSRD) outlines the proposed requirements on corporate sustainability reporting found below. The EIB Group will refer to the final version of the CSRD as soon as it becomes available. Note that according to the proposal, reported sustainability information will be required to be audited (assurance). [From 1 January 2024], large undertakings and, as of 1 January 2026, small and medium-sized undertakings which are undertakings referred to in Article 2, point (1), point (a), shall include in the management report information necessary to understand the undertaking's impacts on sustainability matters, and information necessary to understand how sustainability matters affect the undertaking's development, performance and position.

- a) The information referred to [above] shall contain in particular:
 - a brief description of the undertaking's business model and strategy, including:
 - (1) the resilience of the undertaking's business model and strategy to risks related to sustainability matters;
 - (2) the opportunities for the undertaking related to sustainability matters;
 - (3) the plans of the undertaking to ensure that its business model and strategy are compatible with the transition to a sustainable economy and with the limiting of global warming to 1.5 °C in line with the Paris Agreement;
 - (4) how the undertaking's business model and strategy take account of the interests of the undertaking's stakeholders and of the impacts of the undertaking on sustainability matters;
 - (5) how the undertaking's strategy has been implemented with regard to sustainability matters;
 - ii) a description of the targets related to sustainability matters set by the undertaking and of the progress the undertaking has made towards achieving those targets;
 - iii) a description of the role of the administrative, management and supervisory bodies with regard to sustainability matters;
 - iv) a description of the undertaking's policies in relation to sustainability matters;
 - v) a description of:
 - (1) the due diligence process implemented with regard to sustainability matters;
 - (2) the principal actual or potential adverse impacts connected with the undertaking's value chain, including its own operations, its products and services, its business relationships and its supply chain;
 - (3) any actions taken, and the result of such actions, to prevent, mitigate or remediate actual or potential adverse impacts;
 - vi) a description of the principal risks to the undertaking related to sustainability matters, including the undertaking's principal dependencies on such matters, and how the undertaking manages those risks;
 - vii) indicators relevant to the disclosures referred to in points (a) to (f).

Annex 2: High-emitting sectors for corporate methodology

The table below shows the 17 sectors classified as high-emitting, adopting the standard naming convention under EIB's sector classification system, which are used in the methodology for corporates. These sectors have been selected based on whether they contribute more than 2% of direct emissions in the EU, as well as whether they exceed a particular threshold for carbon intensity score used as input in EIB Risk Management's Climate Risk Screening Tool. Finally, the segments *Airports, Heat supply, Gas production* and *Oil and gas distribution* have been added because they are part of carbon-intensive supply chain and likely to be impacted by the transition to a low carbon, resilient economy.

The following sectors are included:

- 1. Airports
- 2. Animal products
- 3. Aerospace
- 4. Automotive
- 5. Cement production
- 6. Chemicals
- 7. Coal mining
- 8. Fossil fuels
- 9. Glass production
- 10. Heat supply
- 11. Gas production
- 12. Oil and gas distribution
- 13. Production of metals other than steel
- 14. Power generation
- 15. Pulp and paper
- 16. Shipping
- 17. Steel production

The EIB Group PATH Framework

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Supporting counterparties on their pathways to align with the Paris Agreement



European Investment Bank 98-100, boulevard Konrad Adenauer L-2950 Luxembourg +352 4379-22000 www.eib.org – info@eib.org