Institute for Sustainable Finance

A4S ACCOUNTING FOR SUSTAINABILITY

The Transition Finance Playbook

A practical guide for financial institutions

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Contents

ABOUT THIS PLAYBOOK

The Moving Capital Markets (MCM) project was initiated by a group of financial institutions from the Canadian Chapter of the CFO Leadership Network, convened by Accounting for Sustainability (A4S). The aim of the project is to share learnings and create clear and specific actions to support the deployment of transition finance to influence real-world emissions reductions and help Canada meet its national targets.

This Playbook is an output from the MCM project. It captures top tips for action and practical examples, drawn from insights and feedback from MCM project group members as well as publicly available information.

Developed collaboratively by A4S and the Institute for Sustainable Finance (ISF),[1] the Playbook is intended to support other financial institutions, both in Canada and beyond, on the practical action they can take to scale up their transition finance activities. For a list of contributing individuals please see the Acknowledgements section.

Some of Canada's largest financial institutions have participated in developing the Playbook, including Caisse de dépôt et placement du Québec (CDPQ), Ontario Municipal Employees Retirement System (OMERS) and the Co-operators Group (Co-operators).[2]

The Playbook includes a range of practical examples, market realities, further information and additional resources. These can be identified using the symbols shown below.

	**Practical examples**	Peer examples that provide insight into what financial institutions are doing
	**Market realities**	Insights into the current conditions, trends and challenges
	**Further information**	Further details to dive deeper into the content
	**Additional resources**	Materials that provide further guidance

This Playbook was published in June 2025, and its guidance is current as of that date; however, users should bear in mind that transition finance is a rapidly evolving area and future developments in the field will need to be taken into account.

TERMINOLOGY

For the purposes of this report, we use the following definitions:

- 'Financial institution' can refer to banks, credit unions, and asset owners and asset managers, among other capital allocators
- 'Asset' can refer to physical assets, holdings in companies, and projects and, where relevant, fixed-income instruments

1 Further information on A4S and ISF can be found in the relevant sections at the end of this Playbook.
2 Addenda Capital provides investment management services for its majority shareholder, the Co-operators Group.

BACKGROUND: THE ROLE OF TRANSITION FINANCE

Climate change and biodiversity loss threaten our future in many ways, including posing risks to the smooth functioning of the global financial system. They could lead to reduced asset values and lower investment returns: for example, fixed assets in areas that are vulnerable to wildfires or flooding are attracting higher insurance premiums and are less appealing to buyers. We have only a limited time left to halve emissions by 2030 in order to keep global temperatures below 1.5°C of warming compared with pre-industrial levels. To do this, we need to plug a global transition financing gap of almost US$200 trillion between now and 2050.[3]

Some financial institutions are recognizing that addressing systemic sustainability-related factors aligns with their fiduciary duty to act in the interests of beneficiaries/clients. Technological advances, resource scarcity, policy changes, and shifts in consumer and corporate demand continuously alter the investing landscape. This is leading investors to develop transition finance strategies as part of their efforts to address the risks and capture the opportunities in the transition to net zero. Financial institutions can create long-term value by transitioning their asset holdings and expanding their investable universe to align with changing realities. These actions will help bridge the transition financing gap and accelerate the global transition to a net zero economy. As part of these strategies, financial institutions are engaging with their investee companies and clients on transition planning.[4] While the opportunities to finance the decarbonization of some economic activities and sectors have started to mature, others continue to lag. In particular, high-emitting sectors — those which contribute disproportionately to real-world emissions — continue to face major hurdles in getting financial support for decarbonization.

For instance, some financial institutions initially set targets on financed emissions and portfolio intensities as a way to encourage investments in low-carbon assets but are now realizing that this unintentionally deprioritized investment in high-emitting assets with credible transition plans. This underinvestment not only diverts capital away from areas where it could have the most significant real-world impact but also risks allowing high-emitting assets to be picked up by other market actors with less-than-transparent operations and limited interest in climate action.[5] Consequently, rather than simply divesting from high-emitting assets, financial institutions increasingly recognize the importance of actively supporting high-emitting sectors to develop and advance effective transition pathways.

CANADA

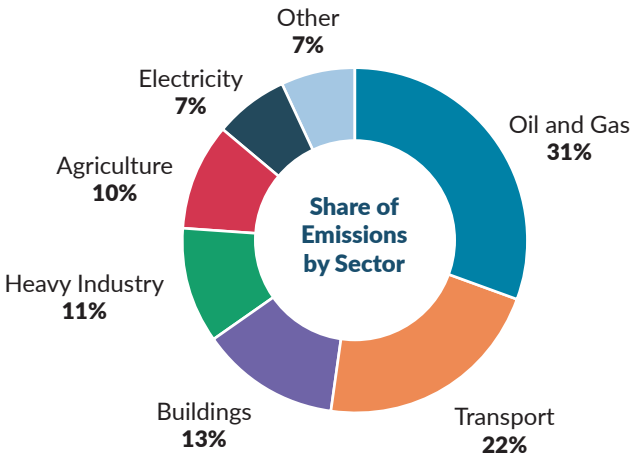
Around 30 Canadian financial institutions, including the 'Big Six' banks[6] and some of the largest Canadian pension funds, have adopted net zero targets and scaled up their efforts to align with the Paris Agreement. Despite this, the climate financing gap is currently acute for Canada, with an estimated annual investment gap of around CA$115 (US$82.5) billion.[7]

With oil and gas, transportation, buildings, and heavy industry representing more than three-quarters of Canada's total national emissions,[8] the country needs to make significant investment in decarbonizing these high-emitting sectors to achieve an orderly transition to net zero (see Figure 1).

3 Allen & Overy & Climate Policy Initiative (2023), How Big Is the Net Zero Financing Gap?
4 For further reading, see Network for Greening the Financial System (NGFS) (2024), Connecting Transition Plans: Financial and Non-Financial Firms.
5 For further reading, see Ringe, W-G and Gözlügöl, AA (2023), Net-zero transition: An inconvenient truth about carbon asset divestment (accessed: 23 May 2025); Gözlügöl, AA and Ringe, W-G (2023), Net-Zero Transition and Divestments of Carbon-Intensive Assets; Gayle (2024), Private equity firms ploughing billions into fossil fuels, analysis reveals.
6 As of January 2025, the Big Six — Royal Bank of Canada (RBC), Toronto-Dominion Bank (TD), Bank of Montreal (BMO), Bank of Nova Scotia (Scotiabank), Canadian Imperial Bank of Commerce (CIBC) and National Bank of Canada (NBC) — are all are listed by Net Zero Tracker as having a net zero target.
7 Sustainable Finance Action Council (SFAC) (2022), Taxonomy Roadmap Report. All CA$ amounts in this report are converted to US$ using the exchange rate of 0.0.7177 (16 April 2025).
8 Environment and Climate Change Canada (2024), Greenhouse Gas Emissions: Canadian Environmental Sustainability Indicators.

FIGURE 1

Share of Canadian emissions by sector



(source: Environment and Climate Change Canada [2024], Greenhouse Gas Emissions: Canadian Environmental Sustainability Indicators)

Currently, these sectors play a crucial role in economic stability and job creation but are struggling to develop scalable solutions and access financing to support decarbonization initiatives.

BARRIERS TO TRANSITION FINANCE

Financial institutions looking to scale up their transition finance are grappling with a number of challenges, including the market stigma of high-financed emissions, the absence of a single defined approach, a lack of high-quality data and consistent metrics, and an overall shortage in investable transition activities. These challenges are described in more detail below; many, if not all, are applicable globally. They are compounded by reputational risks when investing in high-emitting sectors, and by technological/market risks associated with investing in early-stage, enabler[9] technologies.

- **Stigma of high-financed emissions** – transition finance often requires accepting temporary increases in financed emissions in exchange for a promise of a greater overall emissions reduction in the long run. Yet financial institutions typically measure their progress on climate action via reductions in financed emissions and portfolio emissions intensity. In this context, they have found that internal and external stakeholders have limited understanding and acceptance of the temporary increases in financed emissions required to invest in high emitters. Until stakeholders can get comfortable with temporary increases to financed emissions as a part of long-term economy-wide decarbonization efforts, stakeholder pressure and the reputational risk of perceived greenwashing will continue to pose major barriers to such investment. These barriers can be further compounded by internal governance mechanisms, such as compensation and incentive plans being linked to emission targets, meaning that temporary increases in emissions may not be viewed favourably.

9 The Glasgow Financial Alliance for Net Zero (GFANZ) defines 'enablers' as "assets and entities that indirectly contribute to, but are necessary for, emissions reductions by facilitating the deployment and scaling of [climate] solutions or supporting the decarbonization of other actors' operations. Examples may include a battery maker that is a supplier to an electric vehicle manufacturer or the development of new or smart grid infrastructure."

- **No single defined approach** – the lack of a single, global definition for transition finance has contributed to challenges in scaling up investments and difficulty in measuring and comparing impact. Different definitions have been presented by financial institutions, coalitions and non-governmental organizations (NGOs), resulting in varying approaches across the economy, sometimes with conflicting interpretations around scope. In October 2024, the government of Canada announced a plan to deliver a "Canadian Taxonomy", with forthcoming guidance on priority sectors.[10] This is intended to guide financial institutions in defining and deploying finance to support Canada's net zero target, thereby helping to build comparability and credibility. It is also intended to be internationally interoperable. However, as this is yet to be developed, and until there is a global definition of what constitutes transition finance activity, financial institutions will continue to face challenges in scaling up transition finance.
- **Lack of high-quality data and consistent metrics** – the lack of available high-quality data and verifiable and consistent metrics[11] has meant that financial institutions struggle to access reliable information to assess transition plans and track progress. These issues arise from a variety of sources, including:
    - Many companies, especially small and medium-sized enterprises, lacking the resources to reliably measure, track and report data, especially for scope 3 emissions
    - Time lags in accessing decision-useful climate data
    - Data providers often using different methodologies and lacking transparency[12]
    - Only a small number of companies acquiring third-party assurance or verification
    - Limited use of forward-looking metrics and a lack of consensus on methodologies of calculation; forward-looking metrics are key for transition finance as they can capture the future decarbonization upside, or the increased decarbonization potential of transition investments

Additional resources: Overcoming data challenges and calculating an emissions baseline

In addressing the challenges associated with calculating an emissions baseline, A4S has developed a series of top tip guidance, tailored for finance teams of financial institutions. This series highlights key challenges and strategies for overcoming them, complete with case studies. More details can be found here:

- Financed Emissions – A4S Top Tips for Finance Teams of Financial Institutions.
- Facilitated Emissions – A4S Top Tips for Finance Teams of Financial Institutions
- Insurance-Associated Emissions – A4S Top Tips for Finance Teams of Insurers

10 Priority sectors include electricity, transportation, buildings, agriculture and forestry, and heavy industry. For further reading on the priority sectors, see Government of Canada (2024), Government advances made-in-Canada sustainable investment guidelines to accelerate progress to net-zero emissions by 2050. Accessed 23 May 2025.

11 Specific to Canada, the Canadian Sustainability Standards Board (CSSB) recently finalized its modification and adoption of the first two sustainability standards of the International Sustainability Standards Board (ISSB). While the new Canadian standards (CSDS 1 and CSDS 2) will alleviate many of the data challenges, their use remains voluntary. The Canadian Securities Administrator (CSA) has disclosed that it will engage its own process to review and potentially mandate the CSDS 1 and CSDS 2 standards. Meanwhile, the government of Canada has announced its intention to introduce mandatory climate disclosures for large, federally incorporated private companies. Despite these forthcoming measures, financial institutions will likely face continued data challenges in the short term.

12 International Organization of Securities Commissions (IOSCO) (2021), Environmental, Social and Governance (ESG) Ratings and Data Products Providers.

- **Shortage of suitable opportunities** – most high-emitting companies are either yet to develop or in the early stages of developing robust, Paris-aligned transition plans, meaning that the number of high-emitting companies suitable for transition finance investment is limited. In addition, enablers are often early-stage, speculative technologies and do not match the risk profiles required by some financial institutions. Investment in these early-stage technologies can be hampered by regulatory restrictions and duration mismatch concerns. For example, financial regulators in certain jurisdictions, including Canada, have implemented a stricter interpretation of global standards such as Basel III, which means that banks and insurers face even greater restrictions in allocating capital in high-risk, illiquid assets.

TOP TIPS

To invest credibly in transition activities, financial institutions need to demonstrate clearly their intent and ability to decarbonize and, in due course, tangible results. The following tips consolidate insights from the efforts of the Canadian financial institutions participating in the MCM project to scale up their own transition finance activities. They are divided into six key sections:

Secure executive support and strengthen governance	1. Get senior support for your transition finance approach 2. Evolve governance structures to oversee transition finance
Define the scope of your transition finance activities	3. Leverage third-party frameworks to define your transition finance activities 4. Understand different approaches to setting eligibility criteria
Build your capacity to invest in transition activities	5. Segment portfolios and set up transition vehicles 6. Align internal teams on the purpose, scope and features of transition deals
Factor transition planning and targets into due diligence and underwriting	7. Develop and publish clear assessment criteria drawing on external frameworks 8. Evaluate your engagement potential prior to investment 9. Embed decarbonization targets in underwriting strategies
Strengthen accountability through effective monitoring and engagement	10. Use a range of metrics to track the multiple facets of decarbonization progress 11. Develop dynamic engagement and escalation strategies 12. Empower investee companies and clients through education and capacity-building initiatives
Embrace your role as a steward of systemic change	13. Foster peer-to-peer collaborations 14. Collaborate with policymakers to drive economy-wide change

SECURE EXECUTIVE SUPPORT AND STRENGTHEN GOVERNANCE

Securing senior support and developing governance structures can facilitate the initiation and ongoing success of transition finance initiatives. Having senior-level buy-in can help you to progress your transition finance approach and demonstrate commitment at the highest level, which helps to build trust with internal and external stakeholders. Developing governance for transition finance helps to ensure successful execution.

Top Tip 1: Get senior support for your transition finance approach

Demonstrating how transition finance aligns with your institution's value creation and risk management, is key to securing senior buy-in. It will be much easier to get buy-in if it is clear how transition finance connects with your organization's wider strategy and goals.

The business case for transition finance could be built around showcasing how it enables your institution to capture new opportunities in the net zero transition and respond to market trends. Additionally, it could be viewed as a gateway to expanding the investable universe — for example, unlocking opportunities in emerging markets.

The development of a dedicated transition vehicle[13] can be used as a driver to raise awareness of transition finance and develop your definition and approach (see Top Tip 5: Segment portfolios and set up transition vehicles for more detail on transition vehicles).

You may have established knowledge and expertise in 'pure play' green investments which can be leveraged to develop your transition finance approach. It may be helpful to offer senior management and the board insight into how your transition finance approach compares with those of industry peers and to highlight your competitive edge.

Top Tip 2: Evolve governance structures to oversee transition finance

Evolving your governance structure can help to ensure that you execute your transition finance approach effectively. Clear board oversight, well-defined management roles, accountability and aligned incentives all have a role to play. Likewise, well-defined policies and guidelines can help enable and support decision making around transition financing activities.

The governance of transition finance is likely to evolve over time. There is no single universal model; some of the possible approaches are outlined in the box below.

Board level

A board-level investment committee reviews and oversees transition finance, ensuring alignment with broader investment objectives; or a board-level sustainability committee takes ownership and provides strategic oversight of transition finance.

Management level

A management-level sustainable investment committee and senior investment executives manage and monitor the process. Leadership accountabilities should be clearly defined, potentially with financial incentives linked to achieving specific outcomes.

Policy level

The purpose of internal policies and guidelines on transition finance is to provide a clear framework for decision making. This ensures consistency across your institution — including in investment, sustainability, governance and other key support functions that collaborate to execute transition finance effectively. This is discussed more in Top Tip 6: Align internal teams on the purpose, scope and features of transition deals.

13 'Transition vehicles' refers to investment sleeves/envelopes or funds. The different types of vehicles are explained further in Top Tip 5: Segment portfolios and set up transition vehicles.

Practical example: Co-operators – climate change factors embedded into the governance structure

"The governance of climate change cascades down from the Board and its committees to the executive management team, which is responsible for the execution of the corporate strategy. The executive management team allocates resources and ensures the organization has the capabilities to meet its climate-related targets, helps clients understand and manage their climate-related risks and steadily increases the proportion of the organization's investment portfolio in climate-related and resiliency-building investments. From the executive management team, mandates for climate action continue to cascade down to various business areas.

Sustainability metrics are included in the CEO and senior management's long-term incentive plan (LTIP). Senior management refers to vice president level and above. These metrics account for 15% of the LTIP with 10% relating directly to climate-related targets. 5% is related to our target on the percentage of invested assets in impact, transition and resilience investments and 5% is related to our operational emission reduction targets."

For further reading, see Co-operators (2023), 2023 Climate Report.

Practical example: OMERS – a transition sleeve approval process

OMERS recognizes that its governance structure is critical to ensuring the long-term execution and success of its sustainable investment strategy. Its Sustainable Investing (SI) Framework — which includes the SI Policy (approved by the Administration Corporation Board), related guidelines and procedures, and Climate Action Plan (CAP) — is governed and implemented across the OMERS enterprise.

An example of senior leadership support in action is OMERS's transition sleeve, announced in 2023. The sleeve is designed to finance new investments that contribute meaningfully to real-world decarbonization but whose emissions trajectory, at the point of investment, may not align with OMERS's interim climate goals. To ensure that OMERS's transition sleeve is aligned with long-term climate goals, the sleeve required review and approval across various levels of OMERS SI governance structure — including global investment heads, the management-level SI committee, the Administration Corporation Board Investment Committee and the Administration Corporation Board.

By securing buy-in at all levels of governance, OMERS has ensured that its approach to transition finance is well understood and embedded in decision making, strengthening its ability to support real-world decarbonization.

For further reading see, OMERS (2023), Climate Action Plan.

DEFINE THE SCOPE OF YOUR TRANSITION FINANCE ACTIVITIES

A clear definition of transition finance can help to drive internal work and allow internal and external stakeholders to understand your strategy and approach.

Top Tip 3: Leverage third-party frameworks to define your transition finance activities

You can use internationally recognized frameworks and government-endorsed taxonomies for your in-house definition of transition finance. For transparency, it is important to clearly communicate your definition and which frameworks and taxonomies you are drawing on.

Market realities: Third-party frameworks and taxonomies

Numerous third-party frameworks and taxonomies provide a definition of transition finance but there is limited consensus across them, so it is important to clearly communicate which frameworks and taxonomies you are drawing on. For a list of some commonly used definitions of transition finance, see Appendix 1: Definitions of transition finance.

Leveraging relevant local taxonomies, where available, can help to ensure that your transition financing activities are appropriate for the specific region. Government-endorsed taxonomies factor in domestic contexts, economic conditions and national climate ambitions to identify eligible transition activities.

Taxonomies and frameworks provide varying levels of details and can differ in their classifications. For example, while some frameworks and taxonomies label all financing activities that support the transition to net zero as transition finance, others include only activities that specifically target high-emitting sectors which are strategically important to the economy and likely to be overlooked in what is known as 'green finance'. Delineations are not absolute, and in many cases 'green', 'enabling' and 'transition' categories can overlap. For example, some frameworks might consider power transmission and distribution infrastructure, which are key enablers for the energy transition, as 'green', while others might consider them as 'transition'.

With this in mind, current third-party frameworks and taxonomies are helpful tools to guide users in defining transition finance, but one single framework or taxonomy may not offer a fully comprehensive solution. A flexible approach may be required, leveraging more than one framework or taxonomy at once and adapting their insights for practicality and ease of use.

Practical example: OMERS – developing a climate taxonomy

OMERS developed its in-house climate taxonomy by leveraging:

- External taxonomies and standards such as the ICMA Green Bond Principles, the Climate Bonds Initiative Taxonomy, the Independent Science Based Taxonomy (ISBT) and the Bank of Canada's climate-relevant sectors[14]
- Investor-developed taxonomies, notably those from Canadian pension peers
- Country or region-focused taxonomies such as those from the European Union, and emerging guidance from Canada and Australia

14 The Bank of Canada segments its climate transition scenario data into ten climate-relevant sectors: crops, forestry, livestock, coal, crude oil, gas, refined oil, electricity, energy-intensive industries and commercial transportation.

OMERS Climate Taxonomy

Category	De inition	Examples
Green	Investments that derive revenues from business activities that are in alignment with green taxonomies such as the ICMA Green Bond Principles.	Renewable Energy Green Buildings
Enabling	Investments whose business activities indirectly contribute to environmental objectives or can enable transition related activities.	Electricity Transmission and Distribution (T&D) Lithium and Copper Mining
Low Climate Impact	Investments whose business activities do not have a direct material climate impact as well as other financial instruments.	IT Consulting and Related Services Health Care Services
Grey	Investments whose activities have a direct material climate impact and where transition options are increasingly feasible.	Fossil Fuel Based Utilities Automobile Manufacturers
Hard to Abate	Investments whose business activities have a direct material climate impact and where transition options are not currently feasible.	Steel Manufacturing Oil and Gas Exploration and Production

For further reading, see OMERS (2024), OMERS Climate Taxonomy.

Market realities: Understanding interconnections when defining transition finance

A key challenge for market participants is adopting a systems-based approach that acknowledges the interconnections between 'green', 'enabling' and 'transition' assets. Evaluating each category in isolation risks overlooking critical synergies that drive systemic decarbonization. Recognizing the linkages can unlock further decarbonization across the economy, for example, by:

- Decarbonizing the value chain
- Defining transition pathways for high-emitting and hard-to-abate sectors
- Enabling interim progress while viable green alternatives mature (eg traditional automakers improving fuel efficiency while electric vehicles are developed as a viable green substitute)

OMERS has addressed part of this challenge by including a specific 'enabler' classification, which recognizes the role of enablers in unlocking further decarbonization. Its case study on transmission and distribution (T&D) systems illustrates this point.

"There is growing recognition of the critical role of T&D systems in enabling the energy transition. This has been recognized by institutions such as the International Energy Agency (IEA). Currently, industry classification systems, such as Global Industry Classification Standard (GICS), generally bundle T&D companies within the broader utilities sector, often defaulting them to Grey or a similar category when applying a climate lens. This makes it challenging to capture the unique value proposition of these key infrastructure assets. As part of OMERS Taxonomy, we have separated out T&D activities from the utilities sector to recognize their importance in enabling the transition to net zero by adding green electrons to the grid."

For further reading, see OMERS (2024), OMERS Climate Taxonomy.

Top Tip 4: Understand different approaches to setting eligibility criteria

In establishing the eligibility criteria for selecting your transition finance assets, different approaches may be relevant for different aspects, eg portfolio segmentation or setting up transition vehicles, (see Top Tip 5: Segment portfolios and set up transition vehicles for more information).

In addition, different approaches could be layered on top of each other. The first layer could involve the following:

1. **Sectoral approach** – this seeks to identify eligible sectors based on various factors, such as share of total national or global emissions, availability and feasibility of solutions, and relative importance in enabling future decarbonization. For example, a financial institution may include the oil and gas sector in its definition of transition finance due to its larger share of Canadian national emissions. The key challenge for this approach is justifying sector selection.
2. **Thematic approach** – investing thematically involves identifying assets that align with an overarching theme. For example, this might involve grouping assets around specific technologies or enablers.
3. **Sector-agnostic approach** – this approach avoids targeting any specific sector or theme, instead allowing all assets to be considered for inclusion.

You could then add a further layer to refine the selection of eligible assets. Approaches for the second layer of eligibility criteria include:

1. **Emissions-intensity-based approach** – financial institutions track the emissions intensity of their portfolios (see Top Tip 10: Use a range of metrics to track the multiple facets of decarbonization progress for more information on metrics). You can use a multiplier of emissions intensity to identify eligible assets that meet a minimum threshold. While using a quantitative criterion may be viewed more favourably by some stakeholders, there are two notable challenges with this approach:
    a. As portfolio emissions are expected to decline over time, the threshold set by these multipliers is also expected to decline. In other words, the number of assets that meet the eligibility criteria for being labelled as high-emitting grows naturally over time.
    b. Financial institutions may set a multiplier that is too high, eg some financial institutions apply a x10 multiplier to average portfolio emissions intensity but have found that there are few companies that both meet this threshold and are undertaking credible transition planning.

If you choose to use a multiplier to set an emissions-intensity-based threshold, you will have to consider active management of the multiplier (both at the outset and throughout its use) in order to ensure that it sets a high bar but is also attainable.

Practical example: OMERS – integration of intensity alignment and sector-agnostic approaches

OMERS developed a methodology for defining the eligibility criteria for its transition sleeve by integrating the frameworks of international organizations such as the Climate Bond Initiative (CBI) and GFANZ, while also drawing insights from peer practices.

Factors that make an asset eligible for this transition sleeve include:

- Being a high-carbon emitter
- Pursuing decarbonization
- Being aligned to a net zero 2050 pathway

For this purpose, OMERS defines high-carbon assets as "those meeting a predetermined emissions threshold. These assets are typically, but may not be restricted to, companies within the Energy, Utilities, Industrials, and Materials sectors."

For further reading see, OMERS (2023), Climate Action Plan.

2. **Principles-based approach** – this approach can help to refine the selection of eligible assets while maintaining a level of flexibility. For example, your selection approach could emphasize the concept of additionality — ie achieving outcomes that are better than the business-as-usual scenario — by demonstrating that your financial activity has improved the emissions profile of the investment, enabled increased renewable capacity or facilitated climate solutions. This would be particularly pertinent when potential investments do not meet a threshold criteria.

Practical example: Layering a thematic and principles-based approach

One financial institution used the themes of clean energy,[15] sustainable solutions[16] and business transformation[17] to guide its transition finance decision-making processes.

It also used a principles-based framework to consider impact throughout an investment's life cycle.

In order to satisfy the investment screening process, the asset must:

- Align with the goals of the Paris Agreement
- Provide additionality to what would otherwise occur
- Demonstrate accountability in impact and emissions reporting
- Be able to avoid or mitigate any material sustainability risks

15 Clean energy includes expanding low-carbon and renewable energy production and related technologies that support the addition of clean energy capacity to the energy mix and decarbonization of the power sector. This may include wind and solar development, distributed generation, electrical grid and distribution, and battery energy storage solutions.
16 This includes supporting proven technologies enabling the scaling and deployment of viable low-carbon solutions and services which accelerate decarbonization across sectors for a broad range of customers. This may include carbon capture and storage, green hydrogen, biofuels, electrical vehicle charging, and recycling, as well as other asset classes.
17 This entails providing capital and solutions to businesses across multiple sectors, enabling them to decarbonize their business and transition to a more sustainable business model. This may include investments in or partnerships with companies in sectors such as utilities that need to shift from fossil fuel to renewable generation, and industrial companies that need to deploy lower-emission technologies.

Market realities: Embedding flexibility into eligibility criteria

While strict threshold criteria such as minimum emissions intensity requirements and comprehensive, robust transition plans can help to add credibility, such requirements must be balanced with sufficient flexibility for use in today's markets.

Companies in high-emitting sectors often have uncertain and evolving pathways to net zero, shaped by changes in technology, policy and other region-specific factors. This means that the current number of companies which meet the high emission intensity thresholds and also have a credible transition plan is limited (see Top Tip 7: Develop and publish clear assessment criteria drawing on external frameworks for transition plan assessment).

Navigating transition deals therefore requires a flexible and agile approach that allows you to meet companies where they currently are while stewarding them towards net zero. Therefore, aligning your eligibility criteria with the maturity of currently available transition opportunities in the market, and constantly adapting these criteria as the market matures, are important steps to ensure that high-emitting sectors can transition.

BUILD YOUR CAPACITY TO INVEST IN TRANSITION ACTIVITIES

Building your institution's capacity to invest in transition activities through, for example, training and the development of transition vehicles, is an important step to deploying more transition finance.

Top Tip 5: Segment portfolios and set up transition vehicles

Since the majority of a financial institution's emissions typically sit in its portfolio, taking actions at the portfolio level can help to demonstrate a commitment to action. For a more targeted approach, you might also consider establishing specific investment vehicles for transition finance.

Portfolio-level activity – examples of action that a financial institution can take include the following:

- Setting sustainability screening criteria can help to ensure that all new investments and lending have a role to play in the transition.
- Segmenting the portfolio by transition maturity can be an effective mechanism for understanding your exposure to transition-related risks and opportunities, your portfolio's current alignment with net zero and where further decarbonization work is required. You can use this analysis to set financing targets for different segments according to their transition maturity.

Given that the decarbonization of the portfolio is typically monitored using financed emissions, you may find that your capacity to hold high-emitting assets in the portfolio is limited if you have an emissions intensity target. You could consider establishing or investing in separate transition investment vehicles: these could be funds or sleeves/envelopes. This can enhance your capacity for targeted financing and decarbonization of high-emitting assets. To address any doubt that the vehicle was created to allow continued investment in high-emitting sectors with no plans to decarbonize, investments made via the vehicle will need to credibly demonstrate a genuine intent to decarbonize, for example via a credible transition plan, and to be held accountable. Over the medium to long term, the relative success of the vehicle in reducing emissions will bolster credibility and can help to alleviate greenwashing concerns.

Transition investment funds – these allow capital to be pulled from various investors to be invested in line with a defined transition investment thesis. While pooling capital can increase scale, it may be difficult to unite investors under one investment thesis, as the scope of transition finance tends to vary from institution to institution.

Transition investment sleeves/envelopes – these allow the potential for emissions to be excluded from portfolio emissions and interim targets. This can boost a financial institution's capacity to invest in high-emitting assets, with a commitment to decarbonize, without jeopardizing interim portfolio targets. Using a dedicated transition investment sleeve can help to address the challenges associated with temporary increases in financed emissions.

Practical example: CDPQ – implementing portfolio segmentation and transition vehicles

CDPQ undertakes sustainability screening and portfolio segmentation and has a transition envelope. Its approach to identifying eligible assets at the portfolio level differs from its approach at the transition envelope level.

CDPQ's portfolio segmentation includes three levels of asset categories:

1. **Low-carbon assets** – assets identified as compliant with the CBI Taxonomy and inclusive of investments in renewable energy, sustainable transportation and low-carbon buildings, as well as in emerging sectors such as energy storage and efficiency and green hydrogen. As at December 31, 2024, CPDQ holds CA$58 billion in low-carbon assets, up CA$40 billion since 2017 and exceeding the target of CA$54 billion by 2025.
2. **SBTi-compliant assets** – assets that align with SBTi's standards. As of December 31, 2024, CDPQ holds CA$79 billion in SBTi-compliant assets.
3. **Nearly SBTi-compliant assets** – assets that are in the process of becoming compliant with SBTi's standards. As at 31 December 2024, CDPQ holds another CA$15 billion in assets in this category.

When they are added to their low-carbon assets (CA$58 billion), they have CA$152 billion aligned with the Paris Agreement or in the process of becoming aligned.

In addition, CDPQ uses a CA$10 billion **transition envelope** to decarbonize the highest-emitting sectors, enhancing its deployment of constructive capital in transition assets. This uses a sectoral approach, with target sectors identified as agriculture, electricity generation, transportation and materials. As of December 31, 2024, CDPQ holds CA$6.2 billion in transition assets.

CDPQ employs sustainability screening and has completed its exit from oil production and thermal coal mining by the end of 2023.

Having exceeded its original climate targets, CDPQ maintains its ambitious objective of seizing attractive investment opportunities in the context of the transition to a low-carbon economy while encouraging its portfolio companies to integrate climate-related risks and opportunities into their business practices and models.

For further reading, see CDPQ (2024), Sustainable Investing Report.

Top Tip 6: Align internal teams on the purpose, scope and features of transition deals

The key to a smooth and coordinated execution of transition transactions is to ensure that the investment team and all support teams are aligned on the scope and purpose of the transition deals, and on how these deals support the overall transition finance strategy.

Ways to upskill your internal teams include:

- **Introducing a transition finance playbook into your suite of training resources** – this could include an overview of transition finance approaches and principles, the organization's transition finance strategy, the methods to assess eligibility including the importance of credible transition plans, and case studies of current transition finance deals.

- **Conducting regular training sessions** – to build knowledge and capacity across all teams involved in transition finance transactions. A cross-departmental approach can ensure all teams are aware of key considerations, including the potential risks and opportunities of deploying capital in transition deals. It might also be useful to tailor training for specific cohorts, for example to equip underwriting committees with the knowledge to evaluate transition deals that have non-traditional risk-return profiles. Similarly, executives operating with incentives to reduce financed emissions might be averse to deals that would lead to a temporary increase in financed emissions, and specific engagement may be needed for them to understand how these transition deals align with the organization's wider climate strategy.
- **Leveraging external sources of information and training** – with much effort already being put into resources that can support capacity building across the ecosystem, organizations can benefit from tried and tested resources freely available online. For example, the Global Capacity Building Coalition is a global platform designed to help financial institutions access relevant resources including case studies and events.

Practical example: CDPQ – ensuring internal alignment for transition deals

CDPQ's investment in AES Indiana,[18] a company that provides retail electric service, demonstrates a successful transition deal, highlighting the critical role of internal education and alignment in executing such opportunities.

Challenge – AES Indiana is a US regulated utility company engaged in generating, transmitting and distributing electricity using coal, natural gas and renewables. At first glance, an investment that involves an electricity provider using coal looked like a step back with CDPQ's environmental ambition and plan. However, AES Indiana had a plan to decarbonize its assets.

Solution – Ensured that the support teams surrounding the investment teams understood the business plan, and especially regarding the decarbonization plan. Further, the involved teams were educated on how the deal aligned with CDPQ's long-term environmental goal. To do this, CDPQ had to first make sure that AES Indiana was serious about decarbonizing its assets and had a real plan aligned with SBTi or CBI criteria. An important part of the solution was the inclusion of the investment in CDPQ's Transition Envelope, a CA$10 billion envelope committed by CDPQ to decarbonize the highest-emitting sectors, which required the use of an external consultant to assess the alignment of the transition plan to CBI criteria. The external validation further confirmed that the AES Indiana investment program was robust and would result in a good sustainable investment.

Outcome – CDPQ provides support for AES Indiana's investment program, which includes increasing renewable energy capacity and the phase out[19] of existing coal capacity. Looking ahead, AES Indiana's energy mix will be comprised of renewable energy (wind, solar, energy storage) and natural gas. The alignment between internal teams facilitated the communication and trust building with AES Indiana and contributed to the success of the partnership.

Recommendation – CDPQ recommends establishing long-term partnerships with portfolio companies based on a shared vision and common objectives. CDPQ equally concludes that aligning internal teams is key to achieving long term vision and decarbonization deals. The use of tools such as envelopes in climate strategies, is equally recommended, although each institutional investor should create or use tools that are useful for their own targets.

For further reading, see GFANZ (2024), Case Studies on Transition Finance and Decarbonization Contribution Methodologies.

18 AES Corporation (2014), AES Announces Agreement to Sell Minority Interest in IPALCO Enterprises, Inc. to La Caisse de dépôt et placement du Québec. Accessed: 23 May 2025.

19 'Managed phase-out' refers to the early retirement of a significant amount of high-emitting assets. For further reading on managed phase-outs, see GFANZ (2022), The Managed Phaseout of High-Emitting Assets.

FACTOR TRANSITION PLANNING AND TARGETS INTO DUE DILIGENCE AND UNDERWRITING

Assessing the transition plans of potential investee companies and clients during due diligence and embedding targets during underwriting can help to translate transition ambitions into action. This is an additional layer to the due diligence and underwriting processes, complementing rather than replacing existing risk-return analysis.

Top Tip 7: Develop and publish clear assessment criteria drawing on external frameworks

Internationally recognized frameworks can be used to build robust and credible criteria for assessing investee companies and clients' approach to transition planning. This includes the various aspects of transition planning, ranging from strategic ambition and feasibility to implementation and engagement strategies. For a list of third-party resources, see Appendix 2: Further resources.

Publishing your criteria increases transparency for stakeholders and can help investee companies and clients to understand how to conform to your expectations.

Market realities: Embedding flexibility into assessment criteria

An OECD industry survey on transition finance, conducted in 2022, revealed that over 60% of investors were reluctant to provide transition finance, either broadly or for specific regions, due to a lack of clarity on how to assess credible corporate alignment with the Paris Agreement's goals.[20] This underscores the need for institutions to use reliable, third-party frameworks to guide their development of criteria for assessing transition planning of investee companies and clients.

Currently, companies operating in high-emitting sectors are unlikely to have robust transition plans in place. The Transition Finance Market Review (TFMR),[21] commissioned by the UK government, found that "a credible, [comprehensive, and full] transition plan cannot always be a pre-requisite for access to transition finance". It also concluded that the focus should not be solely "on transition plans but also on interim steps that can be taken now to empower a range of actors to participate in the market for transition finance". If companies are still maturing in their climate strategies, overly ambitious criteria may be counterproductive — so you will need to be pragmatic, taking into account the current state of transition finance. This may mean helping them to undertake transition planning rather than requiring a fully comprehensive transition plan from the start. Some approaches you could consider include the following:

- **Requiring investee companies and clients to align with a 2 °C pathway as a stepping-stone, with the ultimate goal of achieving 1.5 °C alignment.** Transition finance is an iterative and incremental process. By requiring investee companies and clients to align to a minimum of 2 °C, financial institutions can immediately allocate capital towards current decarbonization opportunities, while recognizing that further work is needed to align to 1.5 °C. As pathways to net zero become viable, financial institutions can tighten their requirements. This approach allows financial institutions to bypass the current lack of investable opportunities aligned to 1.5 °C, while continuing efforts to achieve the Paris Agreement's target of limiting global temperature rise to well below 2 °C above pre-industrial levels.

20 Organisation for Economic Co-operation and Development (OECD) (2022), OECD Guidance on Transition Finance.
21 TFMR (2024) Scaling Transition Finance: Findings of the Transition Finance Market Review.

- **Using transition-related metrics to determine the maturity of transition planning.** Financial institutions can support investee companies and clients in developing transition-related metrics that provide insight into the maturity and credibility of their transition-related activities. This could include emissions reporting, metrics which demonstrate progress against planned action, and financial indicators such as capex and opex allocation. For example, capex allocation can be an indicator of a company's commitment to net zero, but financial disclosure is still maturing. You may initially consider a high-level assessment of capex commitment and then gradually tighten your criteria to incentivize companies to progress on their decarbonization ambitions. As the market matures, your requirements will likely become stricter, possibly involving in-depth analysis of capex allocations and their alignment with specific emissions reduction targets. This gradual approach supports the development of transition finance practices while motivating companies to progressively improve their climate-related financial planning and disclosures. Other financial metrics which may be useful include allocation to transition-related research and development (including to new technologies). Details of how decision making supports transition action (such as the underlying mechanisms used to allocate capital, eg how you are using a shadow carbon price) can also be indicators of maturity.

  The key message is that it is important to meet companies where they are and help them to navigate the uncertain and dynamic path to net zero. Investing in decarbonization is a gradual, incremental process, with no expectation of perfection from the start. You might also consider how to adapt your approach to the realities of each asset class. Some asset classes have constrained time periods in which to make investment decisions. To effectively compete, you may need to develop tailored and agile assessment procedures. Examples include:

- Working with consultants to add agility to due diligence processes and speed up the investment decision-making process
- Using sector-based proxies to speed up analyses
- Tailoring assessment approaches by sector/asset class as well as region

As an example, OMERS states: "each of our business units faces distinct challenges and opportunities unique to its investment mandate. Our degree of direct influence is dependent on our level and type of ownership. To manage these differences, each business unit has developed an ESG assessment framework and corresponding asset management practices consistent with OMERS approach and tailored to their specific asset class characteristics."

For further detail, see OMERS (2023), Climate Action Plan.

Top Tip 8: Evaluate your engagement potential prior to investment

Understanding to what effect you can engage with potential investee companies and clients will help you assess how much you can influence their decarbonization activities. Assessing this potential involves evaluating both the decarbonization levers available to the potential investee company or client and whether you have enough influence to encourage action on those levers. For example, if you recognize that there is scope to electrify the fleet of an investee company, you must also assess whether you will have sufficient influence over executives to pursue that action. Influence can be in the form of a significant stake in the investee company, but it may also take other forms. For example, stakeholders may jointly agree to establish and oversee climate-aligned investment objectives, performance targets and accountability measures. This model emphasizes co-creating solutions, shared decision making and ongoing engagement even without having a significant stake.

Having engagement potential allows you to use your influence if there are deviations from the agreed-upon decarbonization strategy, whether caused by changes in the investee company or the client's approaches or by external factors. If a company has a comprehensive transition plan and delivers against it, limited engagement may be sufficient.

The level of engagement required will depend on the investee company or client's governance model, transition plans and how they deliver against them. In practice, this may look different for each asset class, which provides different mechanisms and channels to influence management. For example:

- **Private equity** – investors in this asset class generally pursue active ownership models, leveraging industry expertise, operational efficiency and performance incentives. Investors can assess and use available decarbonization levers to influence the asset's decarbonization trajectory.

Practical example: Strategic non-control influence

Financial institutions recognize the growing demand for non-control capital solutions in today's market. The following example illustrates how to maintain influence with a minority stake.

Challenge – a hypothetical company requires substantial capital to fund its growth initiatives but wants to maintain control. It is also reluctant to pursue traditional equity financing, which would dilute the influence of existing shareholders, whereas increasing debt through conventional markets risks over-leveraging the company's balance sheet.

Solution – the company seeks a strategic partner capable of supporting it with mergers and acquisitions and other growth prospects, while allowing it to retain control and maintain a healthy balance sheet. This leads to a non-control capital transaction with a sophisticated investor.

Outcome – upon executing a non-control capital transaction, the strategic partner works closely with the company to add meaningful value across several areas. These could include cost optimization initiatives, broad representation, resetting a capital allocation strategy, evaluating and restructuring an acquisition strategy, and assisting in enhancing operational efficiency.

Recommendation – a financial institution can consider non-control equity as a way to access alternative investment allocations. The lack of a control premium and the value add offered through strategic and operational expertise is offset by the attractive internal rates of return for investors.

Applying this approach to transition finance – drawing from this illustration, even with non-control influence, private equity investors can play a significant role in supporting high-emitting, carbon-intensive businesses in their decarbonization efforts. Through strategic partnerships, they can help to catalyse clean energy expansion, scale decarbonization efforts and attract additional capital, thereby actively contributing to the transformation of carbon-intensive industries.

- **Public equity** – this typically comes with less influence than private equity, and public equity investors may need to assess their level of influence before investing. Considerations might include whether the financial institution will have sufficient access to management and voting power to influence decarbonization outcomes. An important engagement tool for public equity investors is proxy voting (see Top Tip 11: Develop dynamic engagement and escalation strategies for further information).
- **Fixed Income** – fixed-income investors might have to rely on alternative levers of influence, such as contractual mechanisms, to drive decarbonization outcomes (see Top Tip 9: Embed decarbonization targets in underwriting strategies for further information). However, it is important to recognize that in the long run, fixed-income investors can also tilt the availability of new capital towards sectors with credible transition strategies, ultimately incentivizing broader corporate behaviour to align to transition strategies.

Top Tip 9: Embed decarbonization targets in underwriting strategies

Integrating decarbonization targets into underwriting strategies can promote accountability among investee companies and clients. This approach leverages interim targets and governance mechanisms to ensure that investee companies and clients uphold their climate commitments and make tangible progress towards decarbonization goals. Financial institutions can consider incorporating specific decarbonization targets and milestones into the underwriting process without needing to hold a significant stake in the company. Some illustrative examples of how underwriting committees can bind investee companies and clients by incorporating specific transition-related clauses include:

- Mandating use-of-proceeds disclosure, which provides financiers with details of how funds will be allocated
- Linking financing terms to the achievement of targets
- Defining the follow-on financing terms based on whether the company meets the initial targets
- Setting management incentives
- Mandating the verification of specific outcomes (eg third-party emissions verification)

Further information: Embedding decarbonization targets in fixed-income underwriting

To address the different levers of influence that fixed-income investors hold in comparison with equity investors, you could consider offering attractive financing terms to your clients in exchange for their commitment and progress towards a decarbonization target (ie this may translate to lower credit risk in certain scenarios). For example, you could consider transition-linked financing, incentivizing clients to meet climate commitments by tying borrowing costs to decarbonization targets. To strengthen risk assessment, you could also require ongoing annual disclosures on these targets.

Market realities: Engagement potential and underwriting

When a financial institution evaluates its engagement potential, it is strengthening its due diligence process by ensuring it has enough influence to impact the likelihood that decarbonization targets will be met. Embedding decarbonization targets in underwriting achieves a similar outcome to create ongoing accountability and incentives for investee companies and clients to achieve targets.

Combining the two approaches yields a robust framework in which climate alignment is embedded across the entire investment life cycle, from pre-investment vetting to post-investment monitoring. Depending on the financial institution, the investee company or client and the market, institutions may find success in using one or both options.

Practical example: From due diligence to underwriting

After assessing the alignment of a potential investment with a financial institution's transition strategy objectives, impact targets can be identified during the due diligence stage. Ideally, these will be quantitative, transparent, verifiable and informed by third-party guidance and scientific pathways, such as those developed by the Science Based Targets initiative (SBTi), where relevant.

The financial institution can then develop a high-level business plan, which incorporates the identified impact targets and any near-term actions, and which takes an informed view of longer-term activities and the resources needed to achieve them. This high-level plan is then included in the underwriting and reviewed by the investment team.

Post-acquisition, the investment team partners with the investee company's management team to execute the identified near-term actions and develop detailed business plans to deliver the impact targets. This includes developing an emissions baseline and identifying the levers to support decarbonization along with the estimated financial returns. This can be done for scope 1, 2 and material scope 3 emissions. Examples of levers can include the building out of clean energy solutions, the introduction or development of technologies to support energy efficiencies or decarbonization, carbon capture or storage, fuel switching, or decommissioning of carbon-intensive assets.

STRENGTHEN ACCOUNTABILITY THROUGH EFFECTIVE MONITORING AND ENGAGEMENT

Robust monitoring and active engagement are central to effective transition financing. Metrics can be leveraged to measure progress, improve engagement efforts and identify escalation triggers.

Top Tip 10: Use a range of metrics to track the multiple facets of decarbonization progress

No single metric is perfect on its own, and using a variety of metrics can help to provide a comprehensive and accurate picture of ongoing transition finance activities and their effectiveness. The need for multiple metrics should be balanced, to reduce the resource burden of tracking too many. Forward-looking metrics are particularly useful for understanding the value of transition deals. It may also be helpful to consider how to efficiently aggregate metrics to gauge overall portfolio alignment with decarbonization targets.

Backward-looking metrics

Backward-looking metrics use historical data to provide insights. Emissions intensity[22] metrics are among the most commonly used in the market. They are versatile, easily digestible and comparable. As a result, financial institutions have adapted them to form the basis for asset selection, target setting and emissions monitoring.

22 The use of emissions intensity is recommended by the Task Force on Climate-related Financial Disclosure (TCFD) (2017), Recommendations of the Task Force on Climate-related Financial Disclosures.

Type of emissions intensity metrics	Purpose	Description
Economic emission intensity	To understand how the emission intensities of different portfolios (or parts of portfolios) compare with each other per monetary unit	Absolute emissions divided by the loan or investment volume, expressed as tCO2e/$m
Physical emission intensity	To understand the efficiency of a portfolio (or parts of a portfolio) in terms of total greenhouse gas (GHG) emissions per unit of a common output	Absolute emissions divided by a value of physical activity or output, expressed as, eg, tCO2e/MWh or tCO2e/tonne product produced
Weighted average carbon intensity	To understand exposure to emissions-intensive companies	Portfolio's exposure to emission-intensive companies, expressed as tCO2e/$m

Source: based on PCAF (2022), Financed Emissions: The Global GHG Accounting and Reporting Standard, Part A.

Market realities: Emissions intensity metrics

As more financial institutions use emissions intensity metrics, it has become clear that there are a number of shortcomings with them:

- **Implied incentives** – when a financial institution sets a portfolio emissions intensity target, it may inadvertently disincentivize transition finance by limiting capacity for exposure to emissions-intensive assets. Evidently, the focus on emissions intensity has historically incentivized financial institutions to engage in short-term strategies and 'paper decarbonization'.
- **Obscuring the role of finance** – technological and policy changes generally lead to a reduction in emissions intensity over time. Other indicators are required to demonstrate that the financial institutions have generated additionality in emissions reduction. Focusing solely on emissions intensity can overestimate the impact of the finance.
- **Relation to overall emissions** – lower emissions intensity means lower emissions per output or monetary unit but does not necessarily mean lower overall emissions. For some companies, a reduction in emissions intensity might incentivize increased production, resulting in increases to absolute emissions.[23]
- **Consideration of future decarbonization** – emissions intensity metrics are backward-looking and do not consider the potential emissions reduction from ongoing plans. Due to the longer investment horizon, backward-looking metrics are likely to understate the value and effectiveness of transition finance. There is a shift towards prioritizing forward-looking metrics to capture the potential emissions reduction from investing in high-emitting assets.

Forward-looking metrics

Forward-looking metrics capture the increased decarbonization potential from investing in and decarbonizing high-emitting assets, which is essential for understanding the value of transition deals. When used with other metrics, forward-looking metrics can inform strategy, risk assessment and capital allocation decisions. Examples of forward-looking metrics include expected emission reduction (EER) metrics, committed emission reduction (CER) metrics and temperature scores.

- **EER metrics**[24] – these metrics, including avoided emissions and emissions reduction potential, measure the increased decarbonization potential from transition deals. The calculation of these metrics involves creating a baseline or business-as-usual scenario and comparing the projected emissions reduction from transition finance against that benchmark.

23 See Zhang, A (2023), Companies need to be "absolutely" clear about their emissions reduction (accessed: 23 May 2025) for discussion on how decreases in emissions intensity can lead to unabated growth in absolute emissions.
24 GFANZ (2023), Scaling Transition Finance and Real-Economy Decarbonization.

Additional resources: Using avoided emissions metrics

For further information on how to credibly and transparently use avoided emission metrics, see:

- World Business Council for Sustainable Development (2023) Guidance on Avoided Emissions
- PCAF (2024) New Guidance and Methods for Public Consultation

- **CER metrics**[25] – these aggregate the financial institution's share of an investee company or client's reduction commitments.
- **Temperature scores (also known as implied temperature rise)** – these are calculated by converting emission targets, which have varying scopes and time frames across companies, into an easily comparable temperature score that can be used to assess whether targets align with the Paris Agreement. "The scores should be interpreted as follows: This company's GHG reduction target implies an annual reduction rate that is consistent with an ambition heading towards X °C — under the assumption that all companies behave the same."[26] Temperature scores can also be aggregated to calculate the temperature alignment of the portfolio.

Market realities: Forward-looking metrics in practice

While forward-looking metrics are critical to capture and share the transition finance narrative, the subjective inputs in their calculation have led to some market concerns over the possibility of manipulation and overestimation. In addition, financial institutions often employ differing methodologies in their calculations, which currently limits their comparability. Nonetheless, when used in tandem with other metrics, forward-looking metrics help to inform the decarbonization strategies of financial institutions, offering insights into some of the nuances associated with transition deals.

Other metrics

There are a number of additional metrics that can assess and measure the ability of investee companies and clients to develop and follow through on their decarbonization plans. For example, this could include an assessment of governance or of existing budgets for decarbonization initiatives.

25 For further reading, see UN Environment Programme Finance Initiative (UNEPFI) (2023), Developing Metrics for Transition Finance.

26 WWF and CDP (2024), CDP–WWF Temperature Scoring Methodology.

Practical example: Addenda Capital – assessing climate transition maturity

Addenda Capital, a subsidiary of Co-operators, has developed 'climate transition maturity' criteria as part of its Climate Transition Framework in order to assess its current and future holdings against its climate transition expectations, helping the organization and its clients progress towards net zero targets. This assessment helps Addenda Capital's stewardship activities in leveraging the experience of those that are most mature and engaging with those that are the least mature.

The transition maturity criteria include the measurement of qualitative features such as board oversight, risk management, commitment to act and strategy incorporation. A summary of the criteria and levels can be seen below:

	LEVEL 1 AWARE	LEVEL 2 COMMITTED	LEVEL 3 ALIGNING
ENABLING ACTIVITIES + Board Oversight + Risk Management + Commitment to Act + Strategy Incorporation	2 of 4	3 of 4	4 of 4
GHG EMISSIONS DISCLOSURE* + Scope 1 & 2 - Operational GHG Emissions + Scope 3 - Value Chain GHG Emissions	1 of 2	1 of 2	2 of 2
NET-ZERO PATHWAY + Short Term Target + Long Term Target + Science-Based Target Alignment	0 of 3	1 of 3	2 of 3

Performance Against GHG Reductions Targets

Decarbonize trajectory — Is the company on track to meet its targets?

Climate Aligned or Catalytic

A company that is already fully aligned to net zero, under an internationally respected climate finance taxonomy, or involvement or development of catalytic solutions that contribute to reaching net-zero societal emissions by 2050.

**GHG performance will be monitored and considered in the eligibility assessment.*

Source: Addenda Capital (2023), Sustainable Investing Report.

As standards and methods for calculation continue to evolve, it is useful to consider both the limitations and the advantages of each metric. By weighing the costs and benefits of possible metrics, your institution can select a mix that provides a complete picture, while also balancing the resource intensity of developing and utilizing multiple metrics. Finding the right balance between simplicity and thoroughness is key to selecting your preferred metrics.

Top Tip 11: Develop dynamic engagement and escalation strategies

Effective engagement is a cornerstone of sustainable investing, enabling financial institutions to influence the corporate practices of investee companies and clients, catalyse positive change, and manage material sustainability-related risks across their portfolios. By developing a comprehensive engagement toolkit, with strategies tailored to different asset classes and investment scenarios, your institution can maximize impact and support the decarbonization path of investee companies and clients. This approach allows you to exert influence beyond conventional methods and drive long-term value creation across diverse investment holdings. It is also helpful to align your engagement strategy with your broader transition financing strategy to ensure coherence and maximize impact.

One potentially powerful engagement tool is proxy voting in public equity investments. Through shareholder engagement activity, it can enable investors to influence corporate behaviour, enhance sustainability outcomes, and arrive at reasonable resolutions regarding transition plans and targets. In private equity, institutions can opt to integrate decarbonization targets into the executive compensation structures of investee companies and clients, which can potentially align interests and motivate sustainable practices.

When engagement efforts do not produce desired outcomes, investors may consider escalation strategies such as dynamic divestment. This strategy can be implemented by financial institutions as a last resort when investees are unable to meet impact targets. It would need to include a defined timeline and evaluation criteria. For instance, if a company does not demonstrate significant progress or commitment within a stipulated period, it could be granted additional time to improve. If there is still no substantial improvement after this extended period, the institution may proceed to divest its investments in that company.

Additional resources: Understanding the key characteristics of an engagement strategy

There are several resources and case study examples on effective engagement strategies.

GFANZ's Financial Institution Net-Zero Transition Plans guidance highlights the importance of the following characteristics for an engagement strategy:

- **"Clear objectives:** the desired behaviours, requests, or results from clients or portfolio companies (including implementing a net-zero transition plan).
- **Timing of engagement:** length of engagement, deadlines, and milestones to indicate progress.
- **Coverage:** extent of engagement over client and company portfolios (e.g., as a percentage of the portfolio) and how to prioritize if 100% engagement has not been reached (e.g., by greatest potential influence or highest emissions).
- **Method of engagement:** including meetings, letters, conferences, educational material, and other forms of engagement selected based on engagement target and relationship (e.g., equity ownership, debt holder, client) and other considerations including levers available to the financial institution (e.g., side letters, insurance contracts) or length of time of the relationship or influence."

A4S resources include a suite of guidance and case studies for pension fund chairs and trustees on enhancing engagement with investee companies.

Practical example: Addenda Capital – a dynamic divestment strategy

Addenda Capital implements a dynamic divestment strategy as part of its climate transition strategies. The firm commits to establishing a divestment decision tree to determine investments that do not meet its clients' climate objectives.

In particular, its Climate Transition Equity Pooled Funds, which focus on holdings with a commitment on climate change and net zero, require companies within the funds to progress on climate transition commitments and remain actively engaged; upon failing to do so, they would be subjected to divestment.

By employing this approach, Addenda Capital aims to balance effectively its commitment to decarbonization with its fiduciary duty to clients, while showcasing the true potential of transition finance.

For further reading, see Addenda Capital's (2023) Sustainable Investing Report.

Top Tip 12: Empower investee companies and clients through education and capacity-building initiatives

Engagement is essential to the success of transition finance, serving as a critical tool to advance the climate commitments and actions of financial institutions. It can extend beyond your institution's specific targets to include broader empowerment of investee companies and clients to pursue and sustain initiatives independently. For instance, education and capacity building can empower investee companies and clients to better understand their own sustainability risks, build sustainable practices and develop decarbonization strategies by engaging with their own value chains.

To educate and build capacity within investee companies and clients, you can:

- **Leverage existing resources** – to produce playbooks and training materials that can support investee companies and clients.
- **Run capacity-building programmes** – such as workshops, seminars and webinars on specific challenging areas.
- **Organize engagement sessions** – to provide a space for knowledge sharing, collective learning and peer-to-peer discussions on practical action taken.
- **Facilitate online knowledge sharing** – creating platforms and communication channels to exchange experiences and solutions related to the transition strategies of investee companies and clients. These can foster a continuous and uninterrupted flow of efforts towards decarbonization, ensuring collective learning and promoting accelerated progress.

Areas to focus the above activity around could include:

- The business case for change
- Managing sustainability-related risks
- Calculating an emissions baseline
- Reducing scope 3 emissions
- Using decision-useful scenario models
- Identifying and assessing decarbonization levers
- Understanding transition finance principles
- Using transition-related metrics
- Assessing decarbonization pathways
- Setting and validating targets
- Developing a transition plan
- Aligning executive compensation with sustainability targets
- Understanding transition finance transactions
- Practical examples of companies delivering their transition plan

Education and capacity building at the investee company or client level can create a knock-on effect that helps to drive an economy-wide transition. Empowering investee companies and clients can catalyse systemic change within their sectors and value chain.

EMBRACE YOUR ROLE AS A STEWARD OF SYSTEMIC CHANGE

Financial institutions have a unique influence across the economy and can be key players in supporting an economy-wide transition. No single player can deliver the transition alone, but by actively engaging with others they can amplify positive impacts on the environment and the economy.

Top Tip 13: Foster peer-to-peer collaborations

Organizations with shared goals can work together to encourage change. Collaboration (while adhering to anti-trust laws) can help institutions to address systemic challenges more effectively and drive corporate transformation towards a net zero economy. This enables them to pool resources and share expertise, amplify best practices, and encourage sustained progress toward shared climate objectives.

Through collaborating with like-minded organizations, you may be able to:

- **Amplify impact** – while each collaboration is unique, pooling resources and influence may allow organizations with shared sustainability goals and commitments to drive more impactful change than individual efforts alone.
- **Share knowledge** – peers can facilitate knowledge sharing, enabling them to exchange learnings and resources effectively. Knowledge sharing can help institutions to improve their approaches in areas such as target setting, emissions accounting, climate disclosures and engagement.
- **De-risk investments** – individual exposure to financial and operational risks associated with investments may be reduced via co-investment. Co-investment could also be done alongside investors with different risk appetites, for example using blended finance structures. Enhancing the investment case for financial institutions can accelerate the scaling of new technologies critical for the transition and unlock key investment opportunities in emerging markets.

Practical example: Emerging Markets Transition Debt initiative – demonstrating critical partnership between financial institutions

CDPQ and OMERS, alongside other institutional investors, have committed to invest US$400 million in an Emerging Markets Transition Debt (EMTD) initiative. The EMTD, managed by Ninety One, aims to support the energy transition in emerging markets, with a focus on investments in three areas: clean infrastructure, clean technology and decarbonization. It will provide credit to high-emitting companies which have strong potential to reduce emissions to help bring about an energy transition, with the simultaneous goal of providing investors with an appropriate risk-adjusted return.

For further reading, see CDPQ (2024), Investor Leadership Network.

Top Tip 14: Collaborate with policymakers to drive economy-wide change

Support and regulation from policymakers can facilitate the scaling up of transition finance by providing an enabling and stable environment. However, policymakers need input from financial institutions and industry to build consensus and develop policy solutions, which in turn enables financial institutions to invest with confidence in transition activities.

Establishing two-way engagement with policymakers ensures that policy development does not occur in isolation and addresses key barriers preventing private sector adoption.

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27 All names listed in alphabetical order.

ABOUT A4S

A4S was established by HM King Charles III, when he was The Prince of Wales, in 2004 to make sustainable business, business as usual. We are part of the King Charles III Charitable Fund Group of Charities. We work with the global finance and accounting community to:

- Inspire finance leaders to adopt sustainable and resilient business models
- Transform financial decision making to respond to the opportunities and risks posed by the climate crisis and other environmental and social issues
- Scale up action to transition to a sustainable economy

A4S leverages its global networks, including the CFO Leadership Network, Circles of Practice, Accounting Bodies Network and Asset Owners Network, to enable the finance and accounting community to take a leadership role on sustainability. Through our outreach activities and A4S Academy learning and implementation programme, we empower and equip finance and accounting teams to embed sustainability in their organizations.

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ABOUT ISF

The Institute for Sustainable Finance is the first-ever cross-cutting and collaborative hub in Canada that fuses academia, the private sector and government with the singular focus of increasing Canada's sustainable finance capacity. The Institute's mission is to align mainstream financial markets with Canada's transition to a prosperous, sustainable economy.

By investing in education, professional training, research and partnerships, ISF helps to create the critical conditions for Canadian leadership on sustainable finance — at home and abroad.

Housed at the Smith School of Business at Queen's University, the Institute fills the gap in relevant data, expertise and business-oriented solutions for sustainable finance. By aligning financial knowledge and tools with climate change imperatives, ISF fosters Canada's leadership in the shift to a low-carbon global economy.

ISF's governance structure follows the Queen's University Senate Advisory Research Committee (SARC), which approves the Institute's mandate. ISF's Advisory Board is chaired by Chancellor Emeritus Jim Leech and consists of senior industry leaders and academics. ISF also has a Research Advisory Council (RAC), which informs the Institute's research agenda.

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APPENDIX 1: DEFINITIONS OF TRANSITION FINANCE

Definition		Reference
OECD	"Transition finance is generally understood as a means to decarbonize companies or economic activities that meet three specific criteria: (1) they are emissions-intensive, (2) they may not currently have economically viable or credible low or zero-emissions alternatives, and (3) they play a crucial role in future socio-economic development."	OECD (2022), OECD Guidance on Transition Finance
GFANZ	"Transition finance is defined as investment, financing, insurance, and related products and services that are necessary to support an orderly real economy transition to net zero. Transition finance is a means to support four key financing strategies essential for financing a comprehensive transition to a net zero economy (Climate Solutions; Aligned; Aligning; and Managed Phaseout)."	GFANZ Secretariat (2023), Scaling Transition Finance and Real-Economy Decarbonization
ICMA	"Transition finance focuses on hard-to-abate sectors for issuers of Green Bond Principles or Sustainability Bond Guidelines aligned instruments."	International Capital Market Association (ICMA) (2023), Climate Transition Finance Handbook
CBI	"Transition finance is defined as encompassing bond financing activities that do not fall into the category of low or zero-emissions (i.e., not green) but have a pivotal role, whether in the short or long term, in facilitating the decarbonization of an activity or supporting an issuer's transition toward alignment with the Paris Agreement. Transition finance is designed to expedite the decarbonization of hard-to-abate sectors, which is essential for transitioning the economy to a 1.5 °C pathway."	CBI (2021), Sustainable Debt Global State of the Market 2021 CBI (2023), The Climate Bonds Expanded Standard and Certification Scheme
METI (Japan)	"Transition finance refers to a financing means to promote long-term GHG emissions reduction initiatives that are taken by a company in emissions-intensive sectors considering to tackle climate change for the achievement of a decarbonized society."	Financial Services Agency, Ministry of Economy, Trade and Industry (METI) and Ministry of the Environment (2021), Basic Guidelines on Climate Transition Finance
EU Taxonomy	"Transition activities refer to activities for which no technologically and economically feasible low-carbon alternatives currently exist but [which] support the transition towards achieving net zero emissions."	EU (2023), Commission Recommendation (EU) 2023/1425 of 27 June 2023 on Facilitating Finance f or the Transition to a Sustainable Economy
(GFIT) (Singapore)	"Amber (Transition) label encompasses activities under the Traffic Light Classification System that are either in the process of transitioning to Green within a specific timeframe or facilitating significant short-term emissions reductions."	Green Finance Industry Taskforce (GFIT) (2023), Singapore-Asia Taxonomy for Sustainable Finance: 2023 Edition
RMI	Transition finance delivers "transition-enabling solutions for high-emitting counterparties and assets, which may otherwise not be eligible for green finance".	RMI (2023), Defining Transition Finance: Exploring Its Purpose, Scope, and Credibility

Source: based on Shirai, S (2023), An Overview of Approaches to Transition Finance for Hard-to-Abate Sectors.

APPENDIX 2: FURTHER RESOURCES

Organization	Resource
A4S	Transition planning (2025) An introduction to Aligning Transition Planning and Financial Planning: Key Questions for Finance Teams (2025) Accelerating the Transition: Assessing Progress and Driving Action (2024)
Assessing Transition Plan Collective (ATP-Col)	Assessing the Credibility of a Company's Transition Plan: Framework and Guidance (2024)
CDP (formerly Carbon Disclosure Project)	The State of Play: 2023 Climate Transition Plan Disclosure (2024)
GFANZ	Financial Institution Net-Zero Transition Plans: Fundamentals, Recommendations, and Guidance (2022) Expectations for Real-Economy Transition Plans (2022) Case Studies on Transition Finance and Decarbonization Contribution Methodologies (2024)
IFRS Foundation	Transition Plan Taskforce (TPT) Disclosure Framework (2023)
TransitionArc	Tool to assess corporate transitions (2024)