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U.S. Treasury Unveils Principles to Guide Financial Institutions' Net-Zero Commitments

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On September 19, 2023, the U.S. Treasury Department introduced nine guiding principles for private sector financial institutions that have made net-zero commitments. The principles are intended to highlight and encourage the adoption of best practices and promote consistency and credibility in the approaches taken to set and achieve net-zero commitments. The **"Principles for Net-Zero Financing & Investment"** are also intended to help attract private sector capital to address the **economic and environmental impacts of climate change**.

The nine principles focus on Scope 3 greenhouse gas emissions, which generally comprise the majority of financial institutions' GHG emissions.

- **Principle 1.** A financial institution's net-zero commitment is a declaration of intent to work toward the reduction of greenhouse gas emissions. The Treasury Department recommends that commitments be in line with limiting the increase in the global average temperature to 1.5°C, consistent with Paris Agreement goals. To be credible, this declaration should be accompanied or followed by the development and execution of a net-zero transition plan.
- **Principle 2.** Financial institutions should consider transition finance, managed carbon emission phaseout, and climate solutions practices when deciding how to achieve their commitments.
- **Principle 3.** Financial institutions should establish credible metrics and targets and endeavor, over time, to assign metrics and targets for all relevant financing, investment, and advisory services.

- **Principle 4.** Financial institutions should assess client and portfolio company alignment to their (i.e., financial institutions') targets and to limiting the increase in the global average temperature to 1.5°C.
- **Principle 5.** Financial institutions should align engagement practices—with clients, portfolio companies, and other stakeholders—to their commitments.
- **Principle 6.** Financial institutions should develop and execute an implementation strategy that integrates the goals of their commitments into relevant aspects of their businesses and operating procedures.
- **Principle 7.** Financial institutions should establish robust governance processes to provide oversight of the implementation of their commitments.
- **Principle 8.** Financial institutions should, in the context of activities associated with their net-zero transition plans, account for environmental justice and environmental impacts, where applicable.
- **Principle 9.** Financial institutions should be transparent about their commitments and progress towards them.

More than 100 U.S. financial institutions have independently made voluntary net-zero commitments, according to the Department. Alongside publishing its principles, the Treasury Department also highlighted key announcements related to transition planning. This included the Glasgow Financial Alliance for Net Zero's (GFANZ) announcement that over 50 U.S. financial institutions – and more outside the U.S. – had committed to independently publish their net-zero transition plans over the coming year. The Treasury Department also **applauded a $340 million commitment** by philanthropic organizations, including the Bezos Earth Fund, Bloomberg Philanthropies, ClimateWorks Foundation, Hewlett Foundation and Sequoia Climate Foundation, to help financial institutions develop and execute their net-zero commitments.

Taking the Temperature: The Treasury Department's voluntary principles could encourage more U.S. financial institutions to make their own net-zero commitments. The principles build on existing guidance, including from the Science Based Targets Initiative, GFANZ, and the UK's Transition Plan Taskforce (TPT) Disclosure Framework. This promotes the global alignment of various standards and frameworks, the importance of which we often discuss. But the federal government-backed principles have also drawn criticism amid the increasing politicization of climate-related issues in the U.S. One critic, West Virginia Treasurer Riley Moore, called the principles a bid to convince financial institutions "to leverage their economic power to transition the country away from the coal, oil and natural gas industries." He added that "[t]his policy framework is a direct shot at West Virginia's economy."

We have written frequently about political criticisms of and challenges to climate and ESG-related initiatives, in particular in connection with the financial services sector, including federal efforts such as the launch of an ESG Working Group comprised of nine Republican members of the House of Representatives, led by Oversight and Investigations Subcommittee Chair Bill Huizenga, to "combat the threat to our capital markets posed by those on the far-left pushing environmental, social, and governance (ESG) proposals;" the introduction of a bill by two House Republicans to restrict

investment managers from taking into account ESG considerations in investing on behalf of retirement funds; Republican members of the House Committee on the Judiciary sending letters to the steering committee members of Climate Action 100+, Ceres and CalPERS, requesting documents and seeking information regarding antitrust compliance by virtue of their participation in climate-related industry initiatives; and the introduction of four bills by Republican members of the House Financial Services Committee targeting various business and market activities that implicate ESG issues. At the state level, several Republican-controlled state legislatures, including Oklahoma and West Virginia, have enacted laws mandating divestment of state funds from asset managers deemed to "boycott the energy industry" or restricting investment managers from casting proxy votes for the purpose of furthering "non-pecuniary interests."

However, as we commented in the context of the UK's TPT Disclosure Framework, developing and implementing transition plans will enable organizations to direct strategy, promote coordinated, purposeful actions, support organizational transformation and enhance the information available to investors, allowing them to price risk and make capital allocation decisions. Elsewhere, in Hong Kong, for example, the Monetary Authority's Executive Director urged banks to ramp up their net zero transition planning, providing them with high-level principles to guide such planning. As the U.S. Treasury principles emphasize, "appropriate transparency is part of a credible commitment and is necessary for external accountability."