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Working paper: Our view on climate transition plans

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MARCH 2023

Navigating a future-proof climate transition plan

Identifying an organization's risks, goals and actions related to its transition towards a lower carbon economy is typically captured in one key strategic element: a climate transition plan.

While both awareness of the issue and regulatory and stakeholder expectations are still evolving, this working paper represents our views on the key building blocks of a climate transition plan

What is a climate transition plan?

A climate transition plan is an action plan that clearly outlines how you will transform existing assets, operations, and business models to transition towards achieving net-zero by 2050.

Why do you need a transition plan?

Climate transition plans put climate change at the center of a company's strategy and operations. The process of developing, disclosing and implementing a credible transition plan helps to:

- Better understand the **transition risks** your organization will face
- Understand the **extent of transformation** that your business will inevitably need to undergo
- Understand the **financial consequences** of the transition and how strategically to future-proof against these
- Helps **articulate** to stakeholders the actions you intend to take and why

Out of 18,000+ organizations reporting to the Carbon Disclosure Project (CDP)[1] in 2022, only 0.4% had a credible transition plan.

A credible transition plan should help respond to certain basic questions, such as:

IMPACT: What is my organization's climate impact?

AMBITION: What targets am I setting to address the impact and why?

ACTION: How will these goals and targets be achieved?

Key barriers companies typically face in developing and executing a credible climate transition plan:

- Perception of climate change as a **long-term issue** rather than a short-term priority
- Lack of a clear **governance structure**, senior management buy-in and **accountability**
- Failure to involve the right internal stakeholders **across the organization**
- Failure to recognize the need for **operational transformation** and to drive it using the right **levers and incentives**
- Treating it as a **compliance exercise** rather than embedding it within the **business strategy**
- Insufficient **resources** and expertise
- Lack of **credibility and stakeholder support** for transition due to **insufficient clarity**

In this document we discuss the key drivers, risks and associated opportunities as well as our approach to developing a credible plan

[1] *Are companies developing credible transition plans? Carbon Disclosure Project (CDP), February 2023*

What is driving the adoption of climate transition plans?

A rapidly evolving landscape, enhanced stakeholder demand for and scrutiny on decarbonization targets and the credibility of meeting those, as well as a recognition of the risks and opportunities associated with climate change are gradually driving an increase (and improvement) in transition plan disclosures.

Inadequate transition planning comes with key risks

A strategic approach to developing and executing transition plans can help mitigate and manage key risks, as well as improve resilience.

Market risks

Customer preferences are changing, with 56% customers in a Carbon Trust survey [1] claiming to be more loyal to lower carbon brands. Companies failing to adapt to shifting market demands early enough risk losing competitive advantage.

Liability and reputational risks

Some businesses already face liability risks, linked to brand and reputational impacts, from their failure to adequately disclose their climate transition plans. Legal action on this issue is likely to increase in the next few years.

Technological and operational risks

A failure to appropriately account for technological changes, development and deployment required to achieve the transition can give rise to financial as well as business continuity risks.

Risks aside, a number of drivers are fostering the development of transition plans

Investors/Financial institutions

Financial institutions and groups such as and the UN PRI[2] and GFANZ[3] are demanding increasing disclosures around transition plans to understand how transition risks will financially impact their investments.

Society

People are demanding change, and companies are facing increasing pressure to demonstrate how they will transition to a low-carbon economy.

Politics

The Paris Agreement has spurred country level commitments, and new instruments such as carbon pricing and taxes are expected to follow. Companies are expected to demonstrate alignment with these.

Regulation

The ESRS[4] ,TCFD[5] and ISSB[6] include requirements for transition plan disclosures. Over time these disclosures will likely be subject to external auditor scrutiny, and companies are expected to have a robust plan in place.

Key outcomes typically associated with a credible transition plan

Brand and reputation	**Risk management**	**Business continuity**	**New revenue streams**
Resilience	**Credibility**	**Stakeholder satisfaction**	**Competitive advantage**

[1] https://www.carbontrust.com/news-and-insights/insights/consumer-demand-for-lower-carbon-lifestyles-is-putting-pressure-on [2] United Nations Principles for Responsible Investment (UN PRI); [3]Glasgow Financial Alliance for Net Zero (GFANZ); [4] European Sustainability Reporting Standards (ESRS);
[5] Task Force on Climate-related Financial Disclosures (TCFD); [6] International Sustainability Standards Board

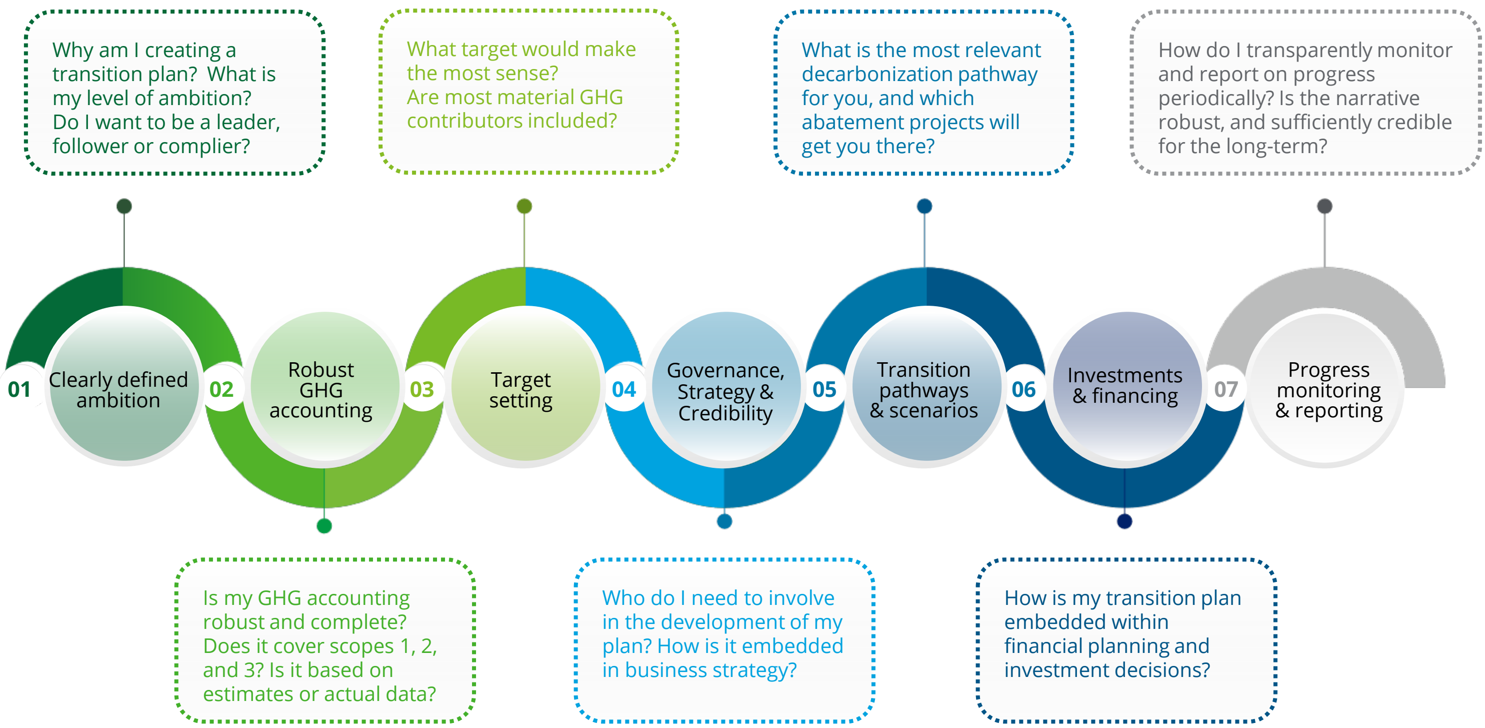
Deloitte's view on key elements of a climate transition plan

Creating an impactful, pragmatic, and action-oriented climate transition plan

We believe it is important for companies to work with a simple framework that meets regulatory requirements, but also drives the consideration of strategic implications of a climate transition plan.

Based on our experience and inputs from leading guidelines, standards and regulatory bodies[1], we believe there are certain key elements that a credible climate transition plan should include.

Our view on key elements of a climate transition plan to deliver value and protect against risks:



Some of the challenges we have seen and discussed with our clients, and which this framework will help resolve, are discussed in this document. Having an aligned vision on the purpose and ambition of the climate transition plan, as well as a credible narrative that supports and drives stakeholder endorsement will help ensure that it doesn't become a mere compliance exercise and is instead used as a driver for transformation internally and across the value chain.

We have zoomed in on selected elements on the following pages to help you get started on your transition planning process.

[1] *The European Sustainability Reporting Standard (ESRS), International Sustainability Standards Board (ISSB), Task Force on Climate-related Financial Disclosures (TCFD), and Carbon Disclosure Project (CDP).*

Climate transition plan

Zooming in on selected elements

1 Define ambition

- **Understanding your level of ambition**: Before committing to a target, we help you understand what the driver is behind the target. Do you want to be a leader, a follower, or are you setting a target merely to comply?
- **Benchmark against your peers:** We help you identify your peers' levels of ambition, which will help you understand your position relative to theirs.
- **Top management alignment:** We help you to ensure your senior management, including your board, is aligned on your level of ambition. Ultimately, they will be held accountable, not just for achieving your target, but also if your target is perceived to be insufficiently ambitious for your business model.

Deloitte Greenhouse lab
Understanding how and where to start is challenging. Through our **Deloitte Greenhouse Labs**, we work with you to understand your vision, ambition, as well as your unique challenges and constraints. The Deloitte Greenhouse Labs are rooted in powerful science and research from the fields of group dynamics, environmental psychology, design thinking, and innovation, bringing together the right stakeholders to brainstorm ideas, and presenting you with a path forward, both for your ambition and for your transition planning, based on consensus.

2 Robust GHG emissions accounting

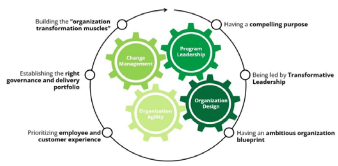
- **Data robustness:** Robustness, consistency and completeness of a baseline year as well as year-on-year metrics, boundaries and scopes and the extent of data processes, controls and systems will need to be assessed. We conduct a full review of your GHG emissions accounting process to identify levels of maturity.
- **Material emissions contributors**: We help assess the materiality of your emissions, particularly for scope 3 across each of the 15 scope 3 categories. We also assess Locked-in*, and non-GHG climate forcers** for materiality.

Value chain emissions

The approach to defining the material contributors to your value chain emissions should be tailored to the sector in which you operate.

For example, if you are a fossil fuel exploration company, you would need to report on indirect emissions from product use, as those emissions are inherently linked to your business model. As a financial services company, you would be expected to report on your financed emissions, which would be far more material than the emissions from your own operations.

Obtaining data from the supply chain requires significant change management and engagement processes which we help you establish



Only 42% of the world's largest emitters[1] have a comprehensive net zero target by 2050, or other commitments that cover all material GHG emissions, including material scope 3 emissions

[1] *https://www.climateaction100.org/, Review of 166 companies, accounting for up to 80% of global corporate industrial GHG emissions, 2022*

**Locked-in emissions are estimates of future GHG emissions that are likely to be caused by the undertaking's key assets or products sold within their operating lifetime. Source: ERSR E1 – Defined terms*

***Non-GHG climate forcers include the emission of gases and aerosols, and processes that contribute to global warming. Source: NewClimate Institute*

Climate transition plan

Zooming in on selected elements

3 Target setting

- **Decarbonization levers:** Each organization will have a unique set of decarbonization levers, based on its operating model and where its emissions hotspots are. We help you understand where you can make the most impact in reducing your emissions.
- **C-suite engagement:** Decarbonization targets often sit within the sustainability team's remit. Setting and monitoring a target requires top management to be involved, and we support you in enhancing C-suite awareness on the implications of the target and their associated responsibility.
- **Reporting versus strategic enabler:** We help you clearly define the objective of the target, as a compliance driven approach differs significantly from using the target as a strategic tool to identify risks and opportunities and to develop or reshape a company's climate transition strategy. Determining the objective upfront with key stakeholders is crucial to success.
- **Credible interim targets:** Whether you have a net zero goal or a science-based target (SBT), we help establish a defined pathway to achieve these targets, aligned with a 1.5°C scenario in line with the Paris Agreement.
- **Value chain alignment:** A target which does not include all material scopes 3 emissions lacks credibility and runs the risk of greenwashing. We help you identify priority hotspots in your value chain, and support in the engagement process, as enabling your value chain to set targets aligned to yours will be key to achieving your target.
- **Offsetting:** Disclosing the extent to which you will rely on offsets to achieve your target is key. We help you understand and navigate the risks associated with offsetting.

Although 69% of the world's largest emitters[1] have a net zero commitment, only 15% have a credible medium-term target and cover all material emissions.

Our view on absolute vs intensity targets

Climate targets can be absolute, or based on physical or economic intensity.

Absolute targets are straightforward and easy to track, but do not allow for easy comparisons of efficiency and intensity to that of peers. Physical intensity targets can encourage process improvements, but risk being viewed as less credible by stakeholders. Economic intensity targets provide flexibility for companies on a growth trajectory, but can show changes in emissions based on financial factors unrelated to climate action.

Each type of target has advantages and disadvantages but to be considered as a science based target, the target must result in an absolute reduction in line with climate science, making alignment with the 1.5°C scenario the most important aspect of any target.

[1] *https://www.climateaction100.org/, Review of 166 companies, accounting for up to 80% of global corporate industrial GHG emissions, 2022*

Climate transition plan

Zooming in on selected elements

4 Governance, business strategy & credibility

- **Alignment with business strategy:** We help you to ensure that activities and targets in the transition plan, including progress monitoring, are embedded in your business strategy and decision-making. Operational performance and decisions around current and future business models, including across the value chain, should align with the decarbonization target.

- **Accountability and responsibility**: We help establish a clear governance structure, including board level involvement and capacity building, with responsibilities and accountability and performance assessment against targets clearly defined. We also help establish incentives linked to progress against targets.

- **Cross-functional versus sustainability only:** We understand the key stakeholders that should typically be part of this process - multiple functions can bring clear benefits, such as providing a steering tool for management decisions, across the business. We facilitate the right level and type of engagement across your diverse range of internal stakeholders, including a consideration of just transition issues.

- **Integration with risk management:** By working with your risk management team, we help ensure that risks and opportunities associated with the transition are identified and managed in alignment with other business risks.

Our view on governance

Ensuring that your company has a credible climate transition plan in place and executes on it, is important to ensuring business resilience and continuity.
Not only for the short term, but to safeguard the long-term value creation of the business. Therefore it is key for the climate transition plan development and implementation process to not only be driven by the sustainability team. Engaging with and building up levels of awareness within other relevant internal departments, is essential. Moreover, a key success factor for implementation is to ensure CEO, Board and CFO-level involvement, buy-in and incentivization from the start.

Strategy Cascade™	Business choices (examples)	Climate transition choices (examples)
What is our winning aspiration?	• What is our purpose and ambition? • What are our financial goals?	• What measurable impact will we make on climate transition? • What is our emissions reduction target?
Where will we play?	• What services do we offer, in which stage of the value chain, to which customers in which geographies?	• What are our lower carbon offerings and toward which stakeholders?
How will we win in the chosen area(s)?	• What are our unique customer offerings? • What is our competitive advantage? Cost or differentiation?	• What makes our low carbon offering unique toward stakeholders? • What makes it better than others?
What capabilities must be in place?	• What assets, know-how and enablers like brands, partners and relations do we need?	• What GHG emissions-specific assets, know-how and enablers do we need? How will we mobilize our value chain?
What management systems are required?	• What structure, processes, decision rights, performance indicators and technologies are required?	• What GHG emissions reduction- specific processes, decision rights and performance indicators are required?

A recent Deloitte survey[1] of 353 audit committee members globally revealed that: 7

- **58% said that climate change is not discussed by the audit committee**
- **47% said they were not climate literate**

[1] *https://www.deloitte.com/content/dam/assets-shared/legacy/docs/perspectives/2022/gx-deloitte-chairs-guide-to-climate-action.pdf*

Climate transition plan

Zooming in on selected elements

4 Governance, business strategy & credibility (contd.)

- **Demonstrating company competence and intent:** The ability to design and successfully implement a robust climate transition plan is a powerful demonstration of the competencies and the intent of any organization and its leadership. Your climate transition plan allows you to demonstrate your ability to lead by example, secure the business foundation and amplify core values, which are all fundamental to trust-based relationships with stakeholders.
- **Credible and compelling narrative linked to strategy:** We help you to build a narrative that is not only based on a clearly defined ambition, target setting, insights and data from GHG accounting. We will also ensure this information is translated into an engaging and inspiring narrative, that aims to engage those stakeholders that are key to successfully implementing the climate transition plan. We ensure the narrative ties into the company strategy, its purpose and vision, to avoid it being perceived as a one-off project. It will allow you to build a clear picture of a resilient future horizon for the company.
- **Stakeholder centricity:** Stakeholders, both internal and external, are crucial in the design and implementation of the climate transition plan. Not only from an accountability perspective, but also for keeping them informed about objectives and progress. Having a general understanding of how different stakeholder groups view climate commitments can help companies to tailor and communicate climate actions effectively. We help you to gain and integrate these insights in the plan, to ensure solid engagement and acceptance among stakeholders.
- **Reliability, predictability and accountability:** We help you to articulate and explain the company's strategic objectives and considerations in the transition plan, creating clear expectations on goals, processes and timelines.

Elements of our approach

Reputational vulnerability assessment

Clear insights on existing and potential credibility vulnerabilities, including related company legacy issues.

Stakeholder analysis and issue maps

Deep and granular understanding of relevant (in)direct actors, levels of impact and influence in driving acceptance.

Issue communications strategies as contingencies

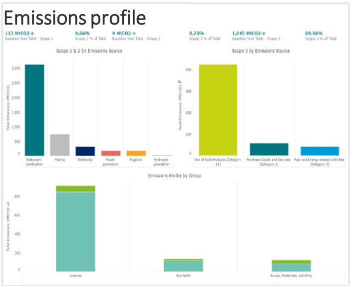
Availability of alternative stakeholder approaches and content in case of implementation issues.

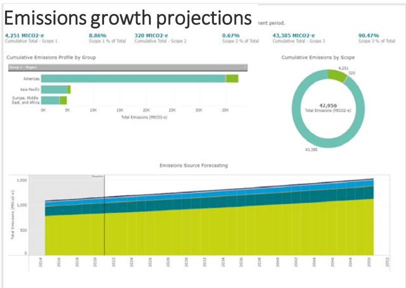
Climate transition plan

Zooming in on selected elements

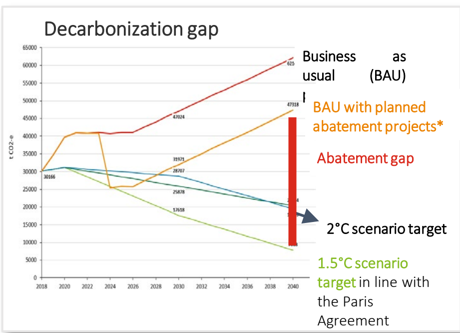
5 Transition pathways and scenarios

- **Understand your emissions projections:** Using our suite of Decarbonization tools[1], we help you identify and visualize where your emissions hotspots lie, within your operations, value chains, and regionally. Based on business growth projections and OpEx and CapEx plans, we estimate your emissions growth projections up to your chosen target year.





- **Identification of abatement projects:** By engaging with your operations teams and using our repository of abatement projects, we identify projects that will collectively contribute to your emissions reduction target, and their associated costs. We help optimize your project portfolio based on an analysis of costs vs abatement potential.
- **Identification of decarbonization gap:** Using the emissions projections data, and by inputting identified abatement projects, we enable you to identify the abatement gap, i.e. the emissions that will remain unabated once you implement all your planned projects, aligned with the transition pathway you have decided to select.
  This identifies the extent to which you will need to explore other decarbonization projects as well as carbon offsetting in the future, should other abatement options not be available. This provides relevant input for future financial planning, based on the projected cost of carbon in the future.



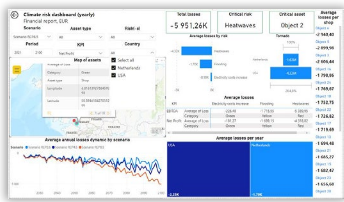
[1] *https://www.deloitte.com/global/en/about/press-room/deloitte-greenlight-solution.html*

Analyzing climate-related transition risks and opportunities in own operations and along the value chain

We help you to assess transition risks and their effect on a company's assets and operations based on various applicable climate scenarios, scaling down macroeconomic and social data to a sector- and region-specific level.

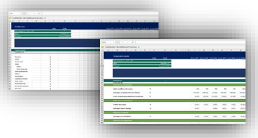
Climate risk modelling

Deloitte's Climate Risk Model conducts a scenario analysis of climate impacts on a company's assets and operations, and quantifies the financial impact of each scenario on business performance. The model gives you a clear picture of climate risks and opportunities.



Financial risk quantification

The Deloitte climate financial risk quantification module identifies the risk impact on financial KPIs (i.e. EBITDA), based on climate risks, climate scenarios, regions and time periods.



Climate transition plan

Zooming in on selected elements

6 Investment and financing

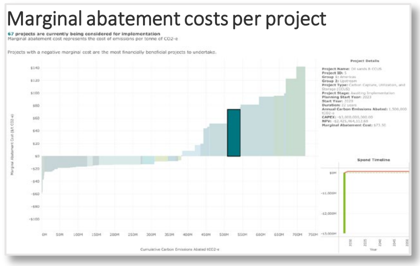
- **Embed in financial planning:** Many companies have a decarbonization target in place without an understanding of the financial implications of meeting it. We help engage operations, procurement, finance and strategy departments early on, and work with you to ensure current and future CapEx and OpEx projections include the cost of the transition and are aligned with EU Taxonomy and other regulatory requirements.
- Accounting for the impact of carbon pricing, grants and incentives, and regulations on the economic viability of the planned projects is part of our approach, and we can help put in place internal carbon pricing or shadow pricing as required.
- **Understand the tradeoffs:** We help you understand the marginal abatement costs for each of your decarbonization levers and abatement projects, which is key to prioritizing actions.

7 Progress monitoring and reporting

- **Transparency:** We help ensure that your reporting includes underlying details around the abatement projects, decarbonization levers, governance structures, strategic implications, and key risks and opportunities to ensure that your reporting provides your stakeholders with sufficient information to assess the robustness of your transition plan.
- **Auditability:** Ideally targets and progress against the transition plan should be subject to regular internal or external auditor review. We help you prepare for the audit and upskill your internal audit department to the requirements around transition plan disclosures and progress monitoring.
- **Frequency** of the reporting and review should be at least annual, to demonstrate progress.

Assessing the financial vs emissions reduction impact of various abatement options

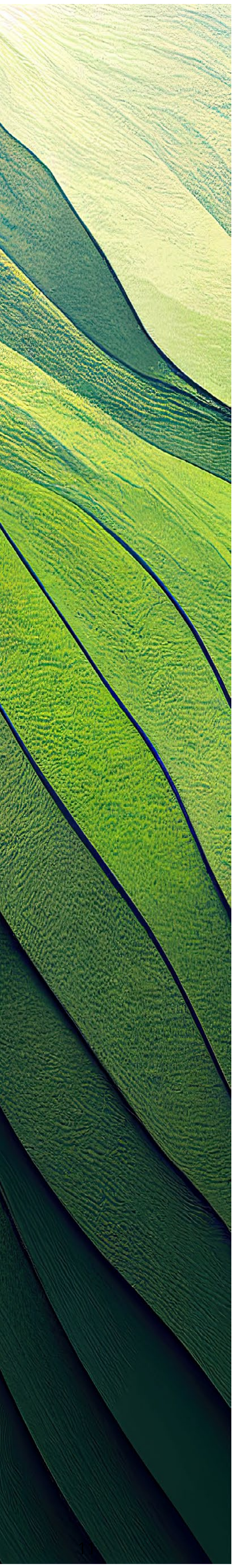
We use Marginal Abatement Cost Curves (MACC) to provide a simple and coherent way to compare the cost and emissions impact of different abatement projects or decarbonization measures, which can help decide on and prioritize decarbonization projects.



Only 5% of the world's largest emitters[1] explicitly commit to align their CapEx plans with their long-term GHG reduction target

[1] https://www.climateaction100.org/, *Review of 166 companies, accounting for up to 80% of global corporate industrial GHG emissions, 2022*

Common challenges & solutions



How do you integrate the transition plan into reporting, strategy and decision making?

It is essential for a company to assess the transition plan against its strategy and business model. Assessment results should be embedded into reporting and decision making. The methods on how to create awareness about the transition plan and integrate it into further decision-making remains an open question.

Solution

The growing demand for transparency and accountability, greater stakeholder interest and the developing regulatory frameworks encourage companies to be more open about their impacts. Disclosing the transition risks and impacts in annual reports and/or sustainability reports in accordance with ESRS, ISSB and/or TCFD requirements would enhance credibility, increase trust and help the organization to remain a step ahead of their competitors.

Moreover, a transition plan reveals transition-related blind spots, which is essential for companies to consider when shaping their business strategy. The more data management has on the transition plan, the more balanced their decisions are likely to be.
Also, if a company consists of several businesses, it is important to prepare individual plans for business clusters, which should ultimately be consolidated. Developing a climate transition plan that includes setting up governance and monitoring procedures helps companies organize themselves internally to meet future requirements. Given energy price trends and the expected introduction of regulatory levers such as carbon taxes, planning now will likely reduce future costs and risks, as well as enhance competitiveness. New business models offer the potential for innovative revenue streams.

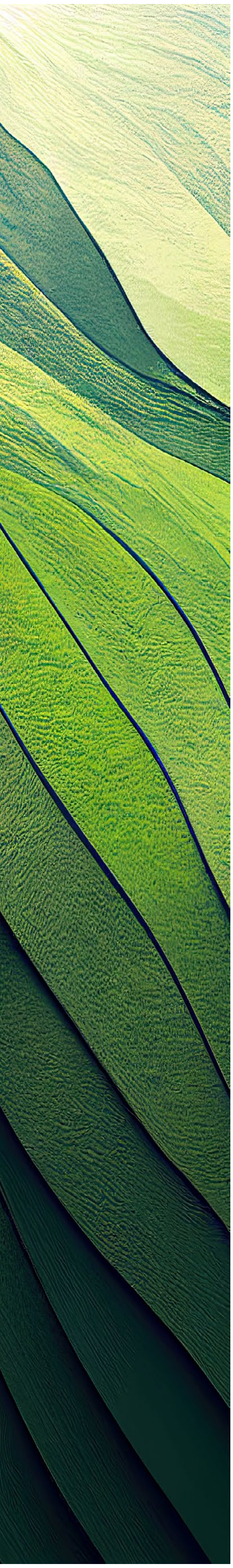
How can you ensure your underlying data is robust enough?

For many companies baseline emissions are often not clearly defined, IT systems and tools that facilitate climate data management are immature, inconsistencies are often observed in consolidation and in reporting across an organization, and value chain emissions are incomplete or unknown. This combination creates a flawed basis for a climate transition plan.

Solution

Data controls, systems, and management processes should be established that identify gaps and prioritize mitigation measures. Internal (through internal audit and internal controls) and external (through auditors) review of the data provides an additional level of confidence in data robustness. Without this foundational element, a climate transition plan risks being based on inaccuracies and could result in significant cost implications in the future.

Common challenges & solutions



How to gain buy-in and implement the plan across the organization?

Often a plan is developed at corporate level, without considering challenges across the organization and value chain, and without obtaining the necessary buy-in across the organization.

Solution

Embedding climate action into the core business strategy and governance arrangements is crucial, not just at corporate level, but also at operational and site level as well as across the value chain.
Unless a transition plan has an appropriate governance arrangement linked to it, that cascades down from board to CEO, CFO, to operational heads, across sites and operations, the plan is unlikely to succeed. Top management should be held accountable and involved throughout the process of developing the transition plan as well as the long-term execution stage.
A clear and detailed roadmap including tangible actions in the climate transition plan is fundamental to easily monitor progress. The requirements of the transition plan should be embedded within value chain operations through procurement and sales contracts. Appropriate incentives and KPIs related to the implementation of the transition plan can foster adoption and roll-out. The extent of change management that will be required to successfully embed the implementation of a transition plan within an organization should not be underestimated.

How can we appropriately account for business continuity risks in transition planning?

Business Continuity is “the capability of an organization to continue delivery of products and services at acceptable pre-defined levels following a disruptive incident / events” (ISO 22301). Undoubtedly, transition risks and transition planning affect your company’s business continuity management. To ensure resilience during the transition process, it is important to appropriately account for business continuity risks.

Solution

Collaboration is key. Connect your resilience strategy to your sustainability strategy and ensure there are regular touch points between the two teams. This enhances awareness, encourages knowledge exchange and fosters collaboration on these topics throughout the company, ensuring changes to the transition risk landscape and operational changes arising from your transition planning that affect your business continuity can be rapidly accounted for.

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