Practitioners' FAQ

Transition finance and the four financing strategies

1. What is transition finance and what are the four key financing strategies?
    - GFANZ defines transition finance as investment, financing, insurance, and related products and services that are necessary to support an orderly real-economy transition to net zero.
    - GFANZ has defined four key financing strategies that finance or enable the following:
        - Climate solutions – Entities and activities that develop and scale climate solutions
        - Aligned – Entities that are already aligned to a 1.5 degrees C pathway
        - Aligning – Entities committed to transitioning in line with 1.5 degrees C-aligned pathways
        - Managed phaseout – The accelerated managed phaseout of high-emitting physical assets
    - The strategies highlight that financial institutions should consider that the greatest emissions reduction may be achieved by directing financing and related services to — rather than divesting from — firms and assets that need to transition. In other words, financial institutions should focus not only on reducing their financed emissions, but also on financing emissions reduction.
    - As the global community progresses toward net zero, GFANZ expects that opportunities for transition finance will grow and the allocation to transition finance in portfolios will increase correspondingly.
    - For more information and illustrative case studies of the four key financing strategies, please refer to our Workshop in a Box on the subject.

2. How are the strategies consistent with emissions reduction targets of financial institutions?
    - GFANZ recommends that financial institutions use a range of metrics and targets to monitor and describe progress toward real-economy emission reductions; using only backward-looking portfolio footprint metrics could be misleading.
    - This reflects the reality that:
        - some activities may result in emissions reductions today and some in the medium and long term;

  - some activities may result in real-economy emissions reductions in other financial institutions' portfolios, but not necessarily in that of the original financial institution (e.g., with climate solutions); and

  - prioritization of the four key financing strategies could temporarily increase client and portfolio emissions in the short term, and using only portfolio emissions footprint metrics may not reflect the extent of transition activities the financial institution may be supporting.

- GFANZ believes that all four key financing strategies are necessary for the real-economy transition.

- One metric that financial institutions could consider using is an umbrella metric, transition finance, to represent the proportion of their total business related to the four key financing strategies collectively.

3. What is the relationship between the four strategies and existing taxonomies?
   - The financing strategies are not intended to serve as a formal or prescriptive taxonomy, disclosure framework, or reporting classification system.

   - Instead, they are voluntary and provide a lens for understanding whether and how particular assets, activities, or clients may be aligned to the transition.

   - The GFANZ four key financing strategies provide an overarching approach to transition finance; taxonomies could be a tool to apply the strategies to a particular sector or region.

4. Can an entity fall into multiple strategies?
   - The financing strategies are not mutually exclusive. For example, firms developing climate solutions may be already aligned to net zero or in the process of transitioning their own emissions.

   - The criteria for each strategy will be complex to define and require more work to develop into a set of requirements that could be adopted across the front and middle offices of different financial institutions and used for accounting purposes.

   - For now, if financial institutions decide to adopt the four key financing strategies for any reporting purposes, they should be transparent in the criteria they've used in setting the respective boundaries and the data used to inform these decisions.

About the GFANZ Net-zero Transition Plan (NZTP) framework

5. What is a Net-zero Transition Plan (NZTP)?
    - GFANZ defines a net-zero transition plan as a set of goals, actions, and accountability mechanisms to align an organization's business activities with a pathway to net-zero greenhouse gas (GHG) emissions that delivers real-economy emissions reduction in line with achieving global net zero. For alliance members, a transition plan should be consistent with achieving net zero by 2050 at the latest, and in line with commitments and global efforts to limit warming to 1.5 degrees C above pre-industrial levels with low or no overshoot.
    - Transition plans are the first step for the implementation of net-zero commitments — the road map for how a business will transition to net zero and deliver against their interim targets — a strategic planning tool, and a practical action plan.
    - The GFANZ NZTP framework is a principles-based, globally applicable, pan-sector set of voluntary recommendations and guidance that supports organizations in developing transition plans.

6. What is the difference between an emissions footprint and a net-zero transition commitment?
    - An emissions footprint is a backward-looking metric that captures the level of current greenhouse gas emissions across Scopes 1, 2, and 3. Performed over time, emissions footprinting can help track changes in emissions.
    - A net-zero transition commitment is a pledge to reach net-zero greenhouse gas emissions by a given time. It constitutes the starting point for transition planning since it lays out the overarching climate aim. Past and forecast emissions footprints can be helpful to inform the net-zero transition commitment.
    - A sole focus on backward-looking metrics such as emissions footprints may not reflect the extent of transition activities carried out and their potential future impacts. They may, therefore, disincentivize actions that finance or support real-economy emissions reduction efforts. GFANZ recommends using both forward- and backward-looking metrics to more accurately capture transition activities and their impact (for more information, please refer to the *Measuring Portfolio Alignment* report).

7. Why are transition plans important?
    - Net-zero transition plans will be a key mechanism to accelerate investment across every sector of the economy to unlock climate action.

    - GFANZ emphasizes that a high level of rigor and accountability must be applied to net-zero commitments and when using the four key financing strategies. This ensures financial institutions are supporting a whole-economy transition while achieving emissions reduction in the needed timeframes.

    - Net-zero transition plans provide the details on how financial institutions will fulfill commitments and the GFANZ transition plan framework provides a common framework across the finance sector and between finance and the real economy. This is supported by other GFANZ publications on transition plans for real-economy firms, sectoral pathways, managed phaseout, and portfolio alignment measurement; advocating for more ambitious climate policy from governments; and increasing the accessibility of climate transition data.

    - Specifically, transition plans:
        - translate commitments into meaningful action, embedding them throughout an organization's strategy, operations, and reporting functions;
        - build consensus and transparency across the financial sector by creating a level playing field to facilitate cross-sector comparability and measurement for net-zero commitments;
        - provide assurance that net-zero transition commitments have integrity and can be held to account;
        - ensure investment in the real economy facilitates decarbonization and does not shun engagement with the industries that require investment to fulfill a credible transition plan;
        - accelerate the deployment and rapid scaling of green investment while being responsible stewards of carbon-intensive assets. Divestment does not equate to decarbonization; and
        - create consensus to build trust, transparency, and accountability within the financial sector as it works to meet its 2030 targets and commitments.

    - For companies in the real economy, transition plans are the most effective way to provide financial institutions with information regarding their transition and level of ambition, which will inform the allocation of capital and services to support companies in the transition.

8. What does this framework recommend?
    - The GFANZ framework outlines four approaches for financial institutions to support the real-economy transition to net-zero emissions. See FAQ 1 for more information.

- GFANZ recommends that a financial institution's net-zero transition plan should address five themes comprising ten components:
    - Foundations (component: Objectives and priorities)
    - Implementation Strategy (components: Products and services; Actions and decision-making; Policies and conditions)
    - Engagement Strategy (components: Clients and portfolio companies; Industry; Government and public sector)
    - Metrics and Targets (component: Metrics and targets)
    - Governance (components: Roles, responsibilities, and remuneration; Skills and culture)

- The same framework can be applied to real-economy companies, as outlined in the report *Expectations for Real-economy Transition Plans*. Note that for real-economy companies, the Engagement Strategy component on "Clients and portfolio companies" would relate to the value chain instead. This acknowledges that for financial institutions, the majority of emissions is found in their financing activities rather than in their operations, while for real-economy companies, it is the whole value chain, particularly the supply chain, that houses the majority of emissions.

- While GFANZ encourages transparent disclosure of transition plans, the reports do not intend to provide detailed guidance on disclosure. Each financial institution should determine specific content, location, and frequency for disclosing the components of its transition plan, consistent with the requirements of their respective sector-specific alliances, business confidentiality, and jurisdictional requirements, if any. When preparing disclosure, institutions should consider the TCFD's Principles for Effective Disclosures.

9. How does the NZTP framework relate to risk management, and what is the relationship between the NZTP and the Task Force on Climate-related Financial Disclosures (TCFD)?
    - While there is significant overlap between climate-related risk management and transition planning, each activity has different objectives. Climate-related risk management focuses on the integration of climate-related financial risks into risk governance, processes, and strategies – often at individual decision levels. The net-zero transition plan represents the strategic alignment of a financial institution's core business and should include, but look beyond, an institution's own risk profile to support the net-zero transition in the real economy at the organizational level.

    - The TCFD published additional guidance on disclosing transition plans, and the GFANZ NZTP complements that guidance.

    - Recognizing that the TCFD framework is regarded as an industry best practice, GFANZ guidance articulates how a financial institution can disclose their net-zero transition plan within the four TCFD pillars, and recommends that institutions should:

- disclose their net-zero transition plans to stakeholders with their climate disclosures at least annually and
- consider the TCFD's Principles of Effective Disclosures in doing so.

Applicability of the GFANZ NZTP

10. Who can use the NZTP?

- The NZTP framework is designed to be applicable across the global finance sector. It includes a set of voluntary recommendations and guidance for any financial institution working toward net zero.
- Recommendation and guidance for the use of this framework is available for both financial institutions and real-economy companies. Both are equally encouraged to use and establish transparent communications based on the framework.
- The principles-based approach allows for flexibility to account for regional regulatory requirements, varying opportunities for engaging with the four financing strategies, and different net-zero timelines.
- Transition plans should reflect these unique circumstances and consider how the four key financing strategies can be best prioritized best given these external influences.

11. What is the importance of transition plans for real-economy companies?

- Reaching the collective aim of net zero by 2050 requires a direct reduction of greenhouse gas emissions in the real economy, which in turn necessitates the targeted flow of funds toward climate-positive actions.
- Transparent communication between financial institutions and their clients and portfolio companies is crucial to allow this targeted flow of funds. A common framework for transition planning helps to establish such transparent communication.
- The GFANZ NZTP constitutes a framework approach that is nearly identical for financial institutions and real-economy companies, and can help real-economy companies understand and navigate the growing expectations from financial institutions that are aligning their investment and finance strategies with net zero.
- Developing net-zero transition plans that use a common framework is an effective way for real-economy companies to provide financial

institutions with the information required to guide transition finance in line with their own net-zero strategy.

Implementation of the GFANZ NZTP

Elements of the NZTP

12. What are the elements of the NZTP and what are their purpose?
    - The GFANZ NZTP framework comprises ten components grouped into five themes. Together, these components constitute the full set of activities an organization should consider in developing and executing a credible transition plan.
    - Each institution is different, and the NZTP recommendations and guidance were written to be flexible for many different types of institutions: High-level net-zero commitments must be translated to be fit for purpose for each institution/company based on their structures, business plans, etc.
    - Transition planning will take time to fully develop. GFANZ recommends that every theme and component be addressed to constitute a full, credible net-zero transition plan over time.
    - The five themes are:
        - Foundations – The Foundations theme covers the principles, assumptions, and context that a financial institution should articulate once it has committed to achieving net-zero GHG emissions by 2050 or sooner. It has one component with recommendations and guidance: *Objectives and priorities*. Overarching considerations such as just transition, integration of nature, and use of carbon credits are discussed here.
        - Implementation Strategy – The Implementation Strategy theme covers how the financial institution can integrate transition strategies into its core business activities and decision-making processes as part of its strategy to align with the net-zero transition. There are three components to this theme: *Products and services*, which looks at how business interactions can be adapted to support the net-zero transition; *Activities and decision-making*, which looks at how internal functions can be adapted to integrate net-zero transition information; and *Policies and conditions*, which outlines considerations for managing highly significant climate challenges.

- Engagement Strategy – The Engagement Strategy theme recognizes that a net-zero transition will require action from across the financial sector, real-economy companies, and government, and that financial institutions play a significant role in supporting and advising clients and engaging with portfolio companies. The three components cover the different stakeholders: *Clients and portfolio companies*; peers in *Industry*; and those in *Government and public sector*. These components provide resources for financial institutions as they support and advise clients and engage with others to encourage development of net-zero transition plans and to build a supporting environment for the transition.

- Metrics and Targets – The Metrics and Targets theme and *Metrics and targets* component discusses how financial institutions can monitor progress toward net zero-aligned targets. GFANZ recognizes that emphasizing portfolio emissions reduction targets over others could have unintended consequences of reducing financing support to real-economy emissions reduction efforts as described in the four key financing strategies. Therefore, this component provides resources for financial institutions on various metrics and targets that cover real-economy emissions reduction, net-zero transition plan execution, and financed emissions.

- Governance – The Governance theme covers internal corporate governance mechanisms. The *Roles, responsibilities, and remuneration* component includes guidance on internal structures to ensure appropriate strategic and operational oversight with proportional compensation. The *Skills and culture* component recognizes that execution of a significant strategy to realize a net-zero transition commitment will require specialized skills and expertise as well as an organization-wide culture change.

13. Why do we need a dedicated theme on foundations?

- Foundations, in the form of objectives and priorities, are the basis for the approach an institution takes to realizing its net-zero commitment.
- Each institution is different, and the NZTP recommendations and guidance were written to be flexible for many different types of institutions: High-level net-zero commitments must be translated to be fit for purpose for each institution/company.
- Clear foundations are an articulation of the purpose and direction to a plan of action that will shape the individual components or tactics of the net-zero transition plan.

Developing an NZTP

14. Where should I start?

- The NZTP is not linear, but the themes reinforce one another and, taken together, form a cohesive strategy.
- Two considerations for determining a starting place are the approach your organization will take to transitioning and identifying the areas where transition planning could lead to the most notable results or where the need is greatest.
- For a first overview of the available guidance on transition planning by theme, refer to the GFANZ [Workshop in a Box series](#).
- Ultimate responsibility for internal cohesion of the plan lies with the Board and/or strategy oversight body; their support will be crucial.

15. What is expected of me if I choose to develop an NZTP now? Is the focus on transition planning for 2030 or 2050?

- GFANZ recognizes that transition planning is a new concept and that developing and implementing a plan will be a multiyear process.
- Very few organizations will have a complete net-zero plan at the beginning of the journey, and at the time of writing, there are areas of planning that are still being developed. The adoption of NZTPs is expected to increase progressively as data and methodologies for net-zero transition plans mature.
- It is crucial that organizations do not delay the process of transition planning due to information scarcity; instead, they should focus on starting early and improving their transition plan over time.
- While the overall aim of sector-specific alliance members should be to achieve net zero by no later than 2050, a transition plan enables organizations to lay out a gradual progress for their transition, including interim targets.

16. How do I choose which metrics to use?

- The choice of metrics is not trivial; GFANZ recommends using multiple metrics to track progress toward interim and final net-zero targets. Appropriate metrics will differ and must fit each organization.
- The GFANZ guidance outlines three broad categories of metrics and targets to monitor progress within. Use of all three categories allows to

capture progress made across multiple layers of the transition plan. The three categories are:
  - real-economy transition metrics and targets
  - plan execution metrics and targets
  - portfolio emissions metrics and targets

- Note that in some cases, the prioritization of the four key financing strategies could temporarily increase client and portfolio emissions in the short term. Therefore, using only portfolio emissions footprint metrics may not reflect the extent of transition activities the financial institution may be supporting. Forward-looking portfolio alignment metrics may help to more accurately represent the impacts of actions being taken.

17. How do I start with forward-looking metrics?
    - Unlike backward-looking metrics that concentrate on data from the past (e.g., past emissions), forward-looking metrics aim to capture how planned changes in activities following a transition plan might align with the goal of net zero or change risk and opportunity profiles. In this way, forward-looking metrics can help direct finance toward companies that are most actively advancing the transition to a net-zero economy, independent of their current emissions rates.
    - When determining which portfolio alignment metrics (both backward- and forward-looking) to work with, some suggested evaluation criteria include ease of use, transparency, scientific robustness, aggregability, and suitability for directing capital.
    - Please refer to the GFANZ *Measuring Portfolio Alignment* report for more detailed considerations.

18. Much of my organization's business involves working closely with clients/portfolio companies. How can transition planning help?
    - The NZTP framework recognizes the importance of a close collaboration between financial institutions and companies in the real economy. Its Engagement Strategy component on clients and portfolio companies focuses on this particular intersection and can help financial institutions navigate their engagement with clients and portfolio companies throughout the transition. To complement engagement, the GFANZ report *Expectations for Real-economy Transition Plans* outlines what financial institutions can expect from real-economy transition plans.
    - In addition, the development of a transition plan is the most effective way for clients and portfolio companies to provide financial institutions with information to inform their own transition strategy.

- Companies with credible transition plans and objectives may increasingly be able to access products and services tailored to low-carbon business models, while the range of services available to others may differ depending on their alignment with net-zero priorities.

Executing an NZTP

19. The actual transition plan won't be linear emissions reductions year over year unless I divest — how do transition plans help with this?
    - GFANZ recognizes that some essential transition actions, such as supporting firms in the early stages of transition or funding the managed phaseout of high-emitting physical assets, may result in increased financed emissions in the near term but contribute to meaningful decreases in the medium or long term.
    - Outlining detailed transition plans that are anchored in science-based scenarios and pathways, including specific policies and conditions in priority sectors and tracking using multiple metrics and targets, allows continued involvement with such activities without compromising credibility and responsible stewardship.

20. How can I show that my transition plan may need to change in the future?
    - Transparently highlighting sensitivities, assumptions, and dependencies within the plan and pointing to limitations and gaps in data, methodologies, and policies are helpful for clients, peers, and public policy to address such gaps over time.
    - Current limitations should not lead to delays in developing and executing transition plans. GFANZ encourages financial institutions and real-economy corporates to "start early and learn by doing." Cooperation across the whole economy is critical to accelerate widespread development and implementation of NZTPs in support of achieving net zero.

21. What if the guidance is incompatible with regulatory considerations?
    - Financial institutions are encouraged to use the recommendations within the voluntary framework wherever possible. However, this should not supersede jurisdictional requirements on transition planning or climate-related financial disclosure, where such requirements exist, or contractual requirements, including mandates with clients.

- Some types of financial institutions may also have unique legal or regulatory constraints that may differ by jurisdiction and may impact the extent to which individual elements of the guidance should be considered.