32. Climate change and fossil fuels: response to Memorial 32 (2017) and Conference reply

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1. Introduction

1.1 The Joint Advisory Committee on the Ethics of Investment (JACEI) was established by the Methodist Conference to advise the Central Finance Board of the Methodist Church (CFB) of ethical considerations relating to investment. This paper builds on the advice JACEI has given the CFB in the light of the Conference reply to Memorial 32 (2017) and Notice of Motion (2020) on climate change (Appendix 1).

1.2 In supporting the notice of motion from the Methodist Conference 2020, the Methodist Council asked JACEI to look again at the CFB holdings in fossil fuel companies. JACEI has undertaken a refresh of its analysis of the five companies which it deemed to have business plans aligned or closely aligned with the Paris Accord.

2. Assessing fossil fuel companies

2.1 In its paper to the 2020 Methodist Conference, JACEI noted that greater pressure has been placed on companies to commit to climate disclosure and targets, and that further change should be expected through 2020 and into 2021. Over the last twelve months, the world has seen huge disruption as Coronavirus has swept the globe. This has impacted companies worldwide, not least fossil fuel companies as travel ground to a halt, and energy demand reduced. The International Energy Agency (IEA) notes the worldwide reduction of emissions due the pandemic reversed as economic activity increased towards the end of the year, with December 2020 emissions 2% higher than December 2019[1].

2.2 In its refreshed and updated assessment, JACEI has focused upon:

- new information produced over this last year by the Intergovernmental Panel on Climate Change (IPCC), IEA and Transition Pathway Initiative (TPI) that has drawn attention to the scale of the challenge to meet the Paris goals and how far oil and gas companies are currently from doing so;
- a fresh reworking of its own methodology using its updated metrics and tighter criteria;
- and a revised and updated assessment of the performance of the five oil and gas companies.

1 https://www.iea.org/articles/global-energy-review-co2-emissions-in-2020

2.3 JACEI remained abreast of new developments through the year from companies within the Oil and Gas sector, including from those companies it excluded in 2020. JACEI reviewed the metrics used for assessment, removing some metrics, tightening others, and recognising limitations within the data from the impacts of COVID-19. JACEI also ratcheted up expectations where there is a credible case to do so, recognising that the Transition Pathway Initiative (TPI) in its 2021 State of Transition report notes that companies in most sectors are not reducing emissions fast enough to hit their 2030 targets.[2] The metrics used continue to be within the five pillars, which are:

- Asset mix
- Capital expenditure
- Climate strategy and governance
- Positive transition steps
- Decreasing emissions

2.4 JACEI recognises the pace of change needed within the industry, not least from the wider availability of company assessments through various tools including the Transition Pathway Initiative (TPI), and the Climate Action 100+ benchmark. These provide new and more detailed analysis about the preparedness of companies to transition to a low carbon economy, focusing on high emitting sectors. When JACEI started its assessment of the oil and gas sector back in 2017, there were limited resources to draw upon. Since then, scenarios based upon 1.5 degrees have been released from the Intergovernmental Panel on Climate Change (IPCC), as well as reports from the International Energy Agency (IEA) World Energy Outlook, with an anticipated report in May 2021 on Net Zero scenarios. The latest TPI research on 1.5 degrees concludes that there is no justification for adding new oil supply as there is sufficient production from existing wells to meet a 1.5 degree scenario, and that no European oil and gas company is currently aligned with 2 degrees, let alone 1.5 degrees[3].

3. The assessment outcomes

3.1 In its report to the 2020 Methodist Conference, JACEI noted certain expectations for the four companies that the CFB held, which it deemed acceptable for investment at the time: Royal Dutch Shell; Equinor; Repsol; and ENI. JACEI notes that the CFB currently holds Royal Dutch Shell in its equity funds (excluding the Epworth Climate Stewardship Fund), and Equinor in its Corporate Bond Fund. JACEI refreshed its company assessments, with new information from companies

2 https://www.transitionpathwayinitiative.org/publications/82.pdf?type=Publication
3 https://www.transitionpathwayinitiative.org/publications/48?type=NewsArticle

released during the last year, under its stricter metrics and tighter criteria, and considering new material from supporting sources. This has led to a different conclusion on the companies it assessed last year, namely that they are not aligned with the Paris Agreement.

3.2 Royal Dutch Shell held a strategy day in February 2021 which outlined its new strategy 'Powering Progress'. One of the four pillars of the plan is 'achieving net zero emissions' in which Shell underlines its support of limiting global warming to 1.5 degrees in step with society, through working with its customers. JACEI received a report covering details of the strategy, and whilst acknowledging the increased ambition of the company to limit warming to 1.5 degrees, was concerned regarding the onus placed on end users for the transition of the company. This gives the impression of the company as being a follower rather than a leader in the energy transition. This was also reflected in the capital expenditure plans, which showed a continued bias towards oil and gas, and a relatively small amount allocated to renewables and energy solutions.

3.3 Equinor released a specific update in November 2020 which outlined its ambitions to be a net zero company by 2050. Within its boundaries and assumptions, it also noted a reliance on society moving towards net zero in 2050, in a similar vein to Shell. JACEI noted its concern regarding this, as well as that in its 2020 report it was looking for absolute scope 3 emissions[4] targets from Equinor, which have not yet materialised. JACEI did however recognise that Equinor has been building its capacity in renewables.

3.4 ENI has released its 2021-2024 strategic plan which notes growing oil and gas production with a large proportion of its capital expenditure plans supporting this. ENI reports its sales from renewables and power business within a segment which also includes retail gas sales. From its advice in 2020, JACEI noted that ENI still retained its link within executive remuneration to production, although it has also increased its links to climate within its annual bonus and long term incentive plan.

3.5 Within its 2021-2024 strategic plan, Repsol continued to see oil and gas playing a key role in the energy mix going forward, with no commitment to reduce oil production. Repsol categorises its capital expenditure in renewables within Low Carbon Generation, which gives limited visibility into specific allocation decisions.

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4 As defined by the GHG protocol: Scope 1 emissions are direct emissions from owned or controlled sources; Scope 2 emissions are indirect emissions from the generation of purchased energy; Scope 3 emissions are all indirect emissions (not included in Scope 2) that occur in the value chain of the reporting company, including both upstream and downstream emissions.

It was also noted that Repsol will report its renewable/ electricity solutions within a combined division with other product offers, which again may limit visibility in future reporting.

3.6 JACEI has expressed its disappointment at meetings through the year that there has not been a faster transition or more commitments from within the oil and gas industry to align with the temperature goals of the Paris Agreement. At the time of writing, none of the companies covered under JACEI advice has emissions intensity plans to 2050 in line with well below 2 degrees using TPI data.

3.7 As well as the specific focus on the four companies mentioned above, in its 2020 report JACEI also included OMV in the list of companies that were not barred from investment by the CFB, even though the CFB did not hold it at the time. OMV is an Austrian producer and marketer of oil and gas, JACEI noted that emissions reductions targets for OMV were not as robust as they could be, noting a lack of absolute targets covering any scopes, and scope 3 emissions intensity targets that do not include fuel bought in trading. It was also noted that the emissions intensity targets covering scope 3 do not fall within the Paris Pledges band in the TPI analysis.

3.8 Although the focus of attention has been on oil and gas companies, JACEI has also been giving attention to extractive companies, recognising the wider view of the climate emergency. Regarding the mining companies covered in the JACEI advice, Anglo American has recently announced the demerger of its South African coal business, which, subject to shareholder approval, will be a standalone listed company as of the 7 June 2021. BHP Group is slightly different, as it has both oil and gas and coal operations. BHP Group has committed to exiting its coal business but, however, wants to retain its oil and gas business going forward. JACEI will continue to actively monitor this situation.

4. Further climate work

4.1 JACEI continues to encourage the work of the CFB in addressing the climate emergency, not just looking at the fossil fuel supply side, but discussing climate issues with companies across sectors to encourage transition to a low carbon economy. Both JACEI and the CFB remain committed to working proactively in dialogue with companies regarding these issues. Recognising the need for society to address the climate emergency, the CFB is considering how to support the goal of net zero greenhouse gas emissions by 2050 or sooner. JACEI has discussed some investor initiatives that the CFB could join that support this goal. The CFB has a voting policy with Church Investors Group (CIG) partners, where it votes against the board chair at companies viewed as climate laggards within specific sectors based on TPI analysis. For more information on the work of JACEI and the CFB as it relates to climate, please see the JACEI 2021 Annual Report.

4.2 Epworth Investment Management Ltd launched the Epworth Climate Stewardship Fund for Charities in late May 2020. The Fund applies all the CFB's existing ethical policies and also excludes companies that extract or refine fossil fuels or have a material involvement in supplying the fossil fuel industry and minimises exposure to companies that are responsible for high levels of greenhouse gas emissions. It also looks to invest in companies that positively contribute to the transition to a low carbon economy and is designed for those who want to disinvest from fossil fuels. More information on this fund is available on the Epworth website.

5. Conclusion

5.1 JACEI recognises that the pace of change needs to accelerate, as the world looks to limit warming to well below 2 degrees and aiming at 1.5 degrees in line with the Paris Agreement goals. Therefore, in the light of:

- new information produced over this last year showing how far oil and gas companies are currently from meeting the scale of the challenge;
- the updated metrics and tightened criteria of the JACEI methodology to reflect this urgency;
- and the revised and updated assessment of the performance of the five oil and gas companies;

JACEI concludes that these companies are not aligned with the Paris Agreement goals. This judgement corresponds with the experience of the CFB in engaging with these companies.

5.2 Whilst they have progressed in some areas that JACEI advised the CFB to look for, the past year has not provided enough evidence of further steps from these companies to consider them aligned or close to being aligned with the goals of the Paris Accord. JACEI has been disappointed by the limited steps taken over this past year in response to the climate crisis and recognises that it can no longer allow these companies the benefit of the doubt as to whether they are 'close to' being aligned.

5.3 Accordingly, and for these three reasons, namely the range of new material which has become available, the reworking of CFB's own metrics in response to this, and its revised and updated assessment, JACEI has advised the CFB to disinvest from and exclude Royal Dutch Shell and Equinor, and to exclude Repsol, OMV, and

ENI as JACEI believes they are not aligned with the Paris Agreement goals. JACEI has reiterated its previous advice to the CFB to continue to exclude the other ten companies on which it advised the CFB in 2020 and continues to keep these companies under review.

***RESOLUTION

32/1. The Conference receives the Report.

Appendix 1 – Conference Memorial 32 (2017) and Notice of Motion (2020)

1.1 Methodist Conference Memorial 32 (2017)

The Memorial and Reply drew attention to past considerations of fossil fuel investment by Conference, the extensive engagement on climate change undertaken by the Central Finance Board (CFB), overseen by the Joint Advisory Committee on the Ethics of Investment (JACEI), including working in collaboration with other institutional investors, including the Church Investors Group. It also outlined the three policies on investment and climate change applied by the CFB, with the first in operation since 2009, noting that almost twenty companies had been excluded from investment as a result.

The Reply to the Memorial also noted that excluding all fossil fuel companies from UK equity investment would lead to total CFB ethical exclusions forming 27% of the UK equity market.

It was noted that "Ethical choices need to be made in the context of the fiduciary responsibilities of the underlying Methodist investing organisations" and that "the removal of fossil fuel companies from a portfolio by a specific date raises questions of investment risk on which key stakeholders (such as pension fund trustees) would need to be consulted."

The 2017 Conference noted that it "affirms the ethical basis of this memorial, which is that if engagement with companies that are heavily dependent on the extraction of fossil fuels does not lead to business models compatible with the ambition of the Paris agreement, disinvestment will ultimately be the response."

The 2017 Conference rejected the specific request for divestment because there was further work to be undertaken with respect to relevant ethical and investment questions.

The 2017 Conference, via the Methodist Council, requested that JACEI:

a) examine the pace of change in the extractive industries sector;
b) in the light of the increasing urgency for more global action, continue actively to consider disinvestment criteria, timescales, and consultation processes required to disinvest from oil and gas companies that fail to comply with the ethical basis outlined above;
c) report to the Conference in 2018, with the expectation that any such company in which the Church invests has not aligned their business investment plans with the Paris Agreement target of a global temperature

rise well below 2 degrees, there would be a recommendation that the Church disinvest from such a company by Conference 2020.

1.2 Methodist Conference 2020

The Methodist Council met in October 2020 and voted to support the Conference Notice of Motion which amended the response to the JACEI report on the fossil fuel sector.

The full resolution passed is:

89/1. The Council supports the request that JACEI recommends that the Central Finance Board fully implements Notice of Motion 2017/109 and disinvests before the 2021 Conference from all oil and gas companies which are not currently aligned with the Paris Agreement target of a global temperature rise well below 2 degrees.