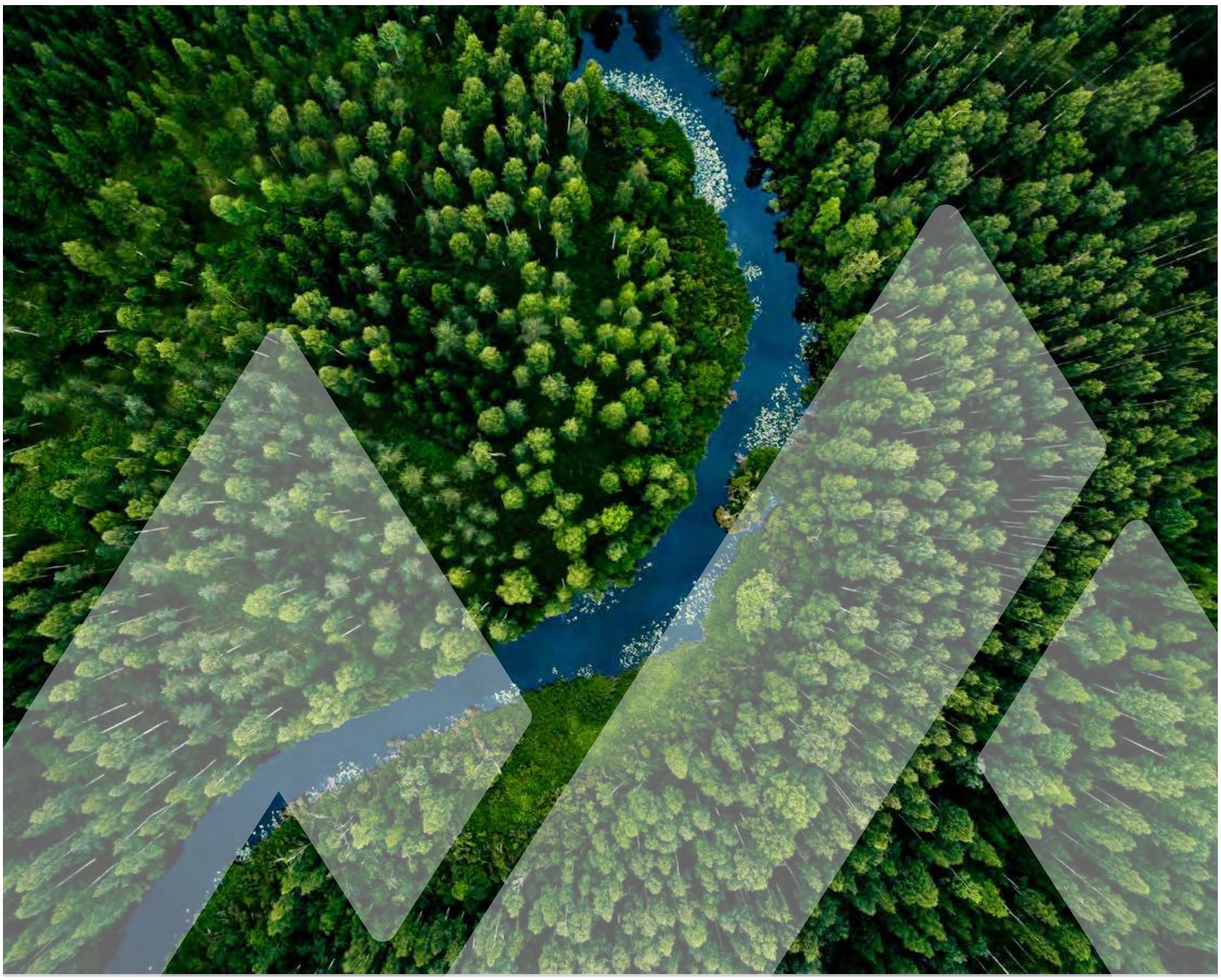
IMPACT+ Principles for Climate-Aligned Finance



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Executive Summary

IMPACT+ Principles for Climate-Aligned Finance

The world is united behind a 1.5°C target to avoid the worst impacts of climate change. Achieving this will require a fundamental shift in how financial institutions approach their business. Financial institutions seeking to pursue credible climate alignment must therefore become **impact-oriented**, focusing both financial and nonfinancial decision-making on facilitating rapid, real-economy decarbonization.

RMI's Center for Climate-Aligned Finance has developed the **IMPACT+ Principles for Climate-Aligned Finance** to help private financial institutions identify what matters most when developing climate alignment strategies:

Influence real economy decarbonization through financial and nonfinancial activities.
Every financial institution will need to identify and quickly mobilize the unique levers of influence available to them to proactively support economy-wide decarbonization.

Measure, steer, and report against transition targets on a sector-by-sector basis.
Understanding a financial institution's potential for impact starts by understanding its relationship to the real economy through different sectors, each of which will require different approaches, timelines, and investments to transition to a net-zero future.

Prioritize actions to expedite progress and maximize impact across key sectors, asset classes, and geographies.
Prioritizing actions where there is the greatest potential for impact in the real economy will allow financial institutions to effectively deploy limited resources where they are needed most, first. This should include consideration of a financial institution's unique influence, expertise, and exposure.

Adopt transition-relevant data and metrics to guide decision-making, without using a lack of data as an excuse for inaction.
Intentionally steering portfolios in line with climate goals will require data and metrics that are granular and forward-looking, and that address the most significant drivers of emissions. Financial institutions should not let a lack of perfect data delay action.

Collaborate to accelerate system-wide alignment.
Financial institutions should work collaboratively to enhance the likelihood of real-economy impact through harmonized engagement efforts, by developing solutions to common barriers, and by disseminating best practices. By working with all relevant stakeholders, financial institutions can more efficiently accelerate the transition to a net-zero future.

Transparently communicate alignment approaches and progress to all relevant stakeholders.
Financial institutions should measure, evaluate, and disclose both financial and nonfinancial alignment activities and progress against targets in public-facing, annual reporting.

+ Develop holistic oversight to minimize negative impacts.
Financial institutions should adopt holistic strategies and governance structures that implement the above principles to maximize positive impact while minimizing negative impact. Actions that lock in a misaligned future will disrupt progress, making the transition harder and more costly.

IMPACT+ Principles for Climate-Aligned Finance

Experts are united behind a 1.5°C target to avoid the worst impacts of climate change. Given financial institutions' crucial role in facilitating world economic activity, achieving a safe temperature target will require rapid action from private financial institutions working in tandem with other key stakeholders. Through climate alignment targets, financial institutions have demonstrated an increasing recognition of their role in the net-zero transition.

However, there is still a risk that aligning individual financial portfolios on paper will not sufficiently support the unprecedented, systemic emissions reductions needed across the real economy to achieve those goals.[i] Financial institutions seeking to pursue credible climate alignment must therefore become **impact-oriented**. Impact-oriented climate-aligned finance appropriate for the decarbonization of the global economy will require a fundamental shift in how financial institutions approach decision-making.

To provide clarity amid an evolving landscape, RMI's Center for Climate-Aligned Finance (the Center) has developed the **IMPACT+ Principles for Climate-Aligned Finance**. These clearly articulate our core vision of climate alignment and help private financial institutions identify what matters most when developing climate alignment strategies.

What are the IMPACT+ Principles

In this document, we define impact-oriented climate alignment and clarify the role of private financial institutions in achieving climate alignment. We then provide seven principles to help private-sector financial institutions create the strategies and conditions through which they can achieve impact while pursuing their climate targets.

This document is not designed to provide linear steps that financial institutions must take to set or meet their climate commitments, but rather to provide the boundaries within which financial institutions can develop effective alignment strategies based on their own unique strengths and mandates. Future work at the Center will develop targeted insights to support the implementation of these principles across the private finance sector.

i For example, portfolio alignment could be achieved by divesting from high-emitting firms without any change in overall emissions, as these emissions could be reallocated to other parts of the financial system, causing "emissions leakage." All actors should consider, and be transparent about, absolute emissions reductions resulting from activities. Divestment should not be seen as the primary driver of alignment, as high-emitting sectors need financial support to transition to low-emissions pathways if we are to maintain economic and social stability while decarbonizing.

Defining Impact-Oriented Climate Alignment

Climate alignment is the process of bringing the global economy's emissions in line with 1.5°C temperature targets. Alignment is imperative, as limiting global temperature rise to 1.5°C above preindustrial levels will greatly reduce the risks from catastrophic climate change. **Urgent action across every sector is required to meet this goal,** which will require halving global carbon emissions by 2030 and achieving net-zero emissions by 2050.

Impact-oriented climate alignment in the financial sector is an indispensable ingredient in achieving a 1.5°C future. We define this **as the process of focusing both financial and nonfinancial decision-making on facilitating rapid, real-economy decarbonization in line with 1.5°C pathways.** This entails setting climate targets that cover financial portfolios (Scope 3, category 15 of the Greenhouse Gas Protocol) and putting resources and incentives in place to enable action.

The term "impact" in this document is defined, in line with academic literature, as the change that a financial institution causes in the activities of real-economy actors that directly or indirectly reduces greenhouse gas emissions.[ii] Both the short- and long-term emissions outcomes associated with the capital and services provided by financial institutions must be considered, given the limited carbon budget left in the global economy to limit warming to 1.5°C.

This is a different approach from "impact investing," although the two are compatible. Traditional impact investing is a more general strategy, often pursued at the portfolio level, that seeks to create a positive social or environmental outcome while also generating financial returns. Impact-oriented climate alignment is concerned with how financial institutions can maximize their contribution to facilitating counterparties' decarbonization with the aim of achieving specific alignment goals while acting as prudent fiduciaries. Impact-oriented climate alignment does not assume or require concessionality, and these principles are designed to be adopted within the context of a for-profit financial institution.

Not all climate-aligned futures are equal. Facilitating a just and inclusive transition is an important goal when considering the type of alignment a firm is seeking to promote. This will require active consideration of gender justice, racial justice, and economic justice at both a local and global scale as they relate to decarbonization plans and projects. A just transition can remove barriers to sustainable economic growth and inclusively deliver the plurality of benefits that arise from alignment opportunities, including among historically excluded populations and geographies that stand to suffer the most from the impacts of climate change.

ii This change caused in counterparties' activities can also be intermediated by a third party, e.g., a financial institution can pressure policymakers to adopt a carbon tax that will in turn affect companies' activities.

Defining the Role of Finance in Climate Alignment

Meeting international climate goals will require an unprecedented acceleration and shift in how money flows globally within and across all sectors. Transforming the practices and priorities of the finance sector, the enabler of nearly all real-economy activity,[iii] is essential to deliver a rapid, just, and inclusive transition. This requires every financial actor to take a proactive role in the transition rather than maintaining a status quo in the global economy, which is currently aligned with a minimum of 2.4°C of warming.[iv]

The urgency and scale of the financing gap, estimated to be $2 trillion to $4 trillion per year by 2030 for the energy transition alone,[v] necessitates change from every type of financial institution to create a groundswell of climate action. Transitioning the global economy requires capital to flow toward climate-aligned assets while actively supporting decarbonization in hard-to-abate sectors. Although public funds will play a pivotal role in national and international net-zero transitions, private-sector finance will have its own unique role based on its existing relationships and influence in the real economy.

To achieve the global net-zero transition required, private financial institutions will need to engage with their clients, portfolio counterparties, and customers to promote and implement decarbonization activities. This engagement should be accompanied by, and help identify opportunities for, direct actions that financial institutions can take to drive climate alignment, including:

1. **Accelerating lending and investment in low-carbon solutions** (i.e., capital to originate net-zero solutions, including complementary infrastructure, networks, and markets)

2. **Supporting carbon-intensive industries pursuing active, substantial decarbonization** (i.e., financing to facilitate credible transition plans, sustainability-linked loans)

3. **Directing finance away from activities that do not or will not support the 1.5°C ambition** (i.e., divestment from unaligned projects and assets after unsuccessful engagement efforts, exclusions of firms without sufficient transition plans)

Given the need for systemic change in the financial and real economy, private financial institutions should also support enabling policy and regulatory measures. This has the potential to unblock additional flows, encourage climate action by reluctant actors, foster harmonization and innovation, and drive system-wide progress toward alignment.

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iii The real economy concerns the production, purchase, and flow of goods and services. The financial economy concerns transactions of money and other financial assets that represent ownership or claims to ownership of real goods and services. Through financial and nonfinancial activities, financial institutions can shape counterparty operations and outputs in the real economy.

iv Projected temperature rise per https://climateactiontracker.org/global/temperatures/.

v Estimated financing gap per https://www.ipcc.ch/site/assets/uploads/sites/2/2019/06/SR15_Full_Report_High_Res.pdf and https://www.iea.org/reports/net-zero-by-2050.

IMPACT+ Principles for Climate Alignment

In order to achieve a 1.5°C future, meaningful action in the financial sector will need to be swift, focused, and transparent. It will need to put real-world transformation ahead of looking good on paper. It will need to collectively target high-emitting sectors that most urgently require investment to transition while minimizing negative impacts across all firm activities.

At the Center, we aim to help financial institutions move away from "ticking the box" and toward impact-oriented guidance and strategies. These IMPACT+ Principles outline our stance on how private financial institutions should implement an impact-oriented climate alignment commitment:

Influence real economy decarbonization through financial and nonfinancial activities.

Measure, steer, and report against **transition targets on a sector-by-sector basis.**

Prioritize actions to expedite progress and maximize impact across key sectors, asset classes, and geographies.

Adopt transition-relevant data and metrics to guide decision-making, without using a lack of data as an excuse for inaction.

Collaborate to accelerate system-wide alignment.

Transparently communicate alignment approaches and progress to all relevant stakeholders.

+ Develop holistic oversight to **minimize negative impacts.**

Below we provide further detail on the key elements of each principle and why each is important to achieving climate alignment. The principles are complementary and interlinked and should not be viewed as mutually exclusive or linear. They are not designed to be an exhaustive list of actions a financial institution must take to be climate aligned, but they can inform the development of impact-oriented climate alignment strategies.

Principle 1

Influence real-economy decarbonization through financial and nonfinancial activities.

01

What is it?

Financial institutions should identify and urgently deploy their levers of influence to proactively support rapid real-economy decarbonization to enable the global economy to halve emissions by 2030 and reach net zero by 2050.

Levers of influence vary by financial institution but generally fall into two categories:

1. **Financial levers**—using lending and investment, advisory services, and capital market activities to alter the cost and availability of capital in support of a 1.5°C future through:
    - Allocating capital to financial activities that are actively contributing to 1.5°C alignment goals and/or sectoral transition goals.
    - Pricing capital allocations to reflect the climate risks present within investment opportunities and to encourage transition-related activities to happen faster and at greater scale while disincentivizing non-aligned activities.
    - Managing portfolio emissions by advising and monitoring the performance of clients on achieving their transition plans and excluding or divesting from clients and investment opportunities that are persistently incompatible with alignment goals.
2. **Nonfinancial levers**—encouraging changes in stakeholders' behavior and actions through:
    - Engagement with clients, portfolio counterparties, consumers, and/or customers to encourage action and transparency on decarbonization and transition plans. This engagement can be bilateral and/or collaborative with other financial institutions.
    - Stewardship by putting forward and voting on shareholder resolutions to enhance climate governance, transparency, and action.
    - Advocacy (e.g., with policymakers and regulators) to create and maintain a climate-aligned operating environment and to facilitate the disclosure of transparent, decision-useful climate-related data.

These levers are not mutually exclusive and should be deployed to enable every company and sector to transition along an actionable, scientifically credible decarbonization pathway.

Why is it important?

Meeting 1.5°C requires a rapid, economy-wide transition: every company and sector must ultimately come into alignment. An impact-oriented approach therefore requires a fundamental shift in the way lenders and investors interpret and execute on their role vis-à-vis the real economy**. Every financial institution will need to identify and mobilize the unique levers of influence available to them, as there is no universal alignment playbook.** Doing so will allow focused, meaningful, and immediate action since deployment is not contingent on data or methodology development.

Principle 2

Measure, steer, and report against transition targets on a sector-by-sector basis.

02

What is it?

Financial institutions should seek to adopt a sectoral approach to climate alignment. Each sector will be affected by, and contribute to, the low-carbon transition in different ways. Therefore, financial institutions should facilitate these transitions and align sectoral portfolios using bottom-up strategies, i.e., strategies based on models that address the unique capital needs and technological solutions required for industry-specific decarbonization pathways.

Using sector-specific pathways, financial institutions can work directly with clients to tailor financial products and services to meet the unique transition needs of that sector and conduct more informed engagement to ensure progress is made and reported. **These actions should be focused on facilitating decarbonization strategies aimed at tackling the source of emissions as quickly as possible, and actions should be informed by quantitative emissions targets, benchmarks, and technological pathways for real-economy assets.** This should include near-term targets and escalation policies. Escalation policies should include divestment options where sufficient progress has not been made.

Targets should be clearly in line with no/low overshoot scenarios,[vi] derived from credible top-down models where possible (i.e., models that account for science-based progress needed at global and inter-sectoral scales to limit warming to 1.5°C). Financial institutions should be explicit in explaining what actions are needed and by whom (i.e., financial actors, policymakers, corporates, and customers).

Why is it important?

Sectoral strategies have emerged as a key tool of choice for many financial institutions looking to drive real-economy decarbonization and make progress toward climate goals.

Understanding a financial institution's potential for impact starts by understanding its relationship to the real economy through different sectors, companies, assets, and legal frameworks within its relevant operational geographies. This should also account for varied alignment pathways, with longer transition trajectories likely needed for hard-to-abate sectors and developing market regions.

A sectoral approach gives financial institutions and stakeholders transparent insight into the emissions implications of their activities within the sectors most critical to transition. For example, such an approach can maximize a financial institution's impact by focusing action where it has the most influence, expertise, and exposure to climate change. Proactive engagement between financial institutions and industry actors can enable targeted problem solving of specific technical or financial barriers and accelerate adoption of the most feasible solutions for a given sector. This approach can also highlight investment needs for long-term solutions that are essential to achieve net-zero emissions.

vi In climate transition scenarios, limiting warming to 1.5°C can be achieved in several ways. Low/no overshoot scenarios refer to those that stabilize at 1.5°C, compared to overshoot scenarios in which warming exceeds and is then brought back down to an average of 1.5°C above preindustrial levels. Scientists agree that climate risks are much higher in overshoot scenarios. For more detail on 1.5°C mitigation pathways, see IPCC (2018) report.

Center for Climate Aligned Finance

Principle 3

Prioritize actions to expedite progress and maximize impact across key sectors, asset classes, and geographies.

03

What is it?

Financial institutions should **design impact-oriented alignment strategies that prioritize financial and nonfinancial actions to accelerate progress and drive real-economy decarbonization.** To do this, firms must consider their role in the global economy (e.g., type of financial institution and size), their portfolio composition (e.g., sectoral exposure and financial vehicles), the emissions profiles of the sectors they finance (e.g., high-carbon, hard-to-abate sectors), and the operating environments they work and invest in (e.g., differences in policy and regulatory landscapes).

Financial institutions should focus on accelerating decarbonization efforts in key sectors, asset classes, and geographies where they have high exposure to greenhouse gas emissions and potential for impact. Firms should lean in to the challenge of decarbonizing their existing portfolios and business lines and avoid "tick the box" exercises that can result in greenwashing. This is likely to require firms to focus strategic, meaningful actions on the hardest-to-abate sectors first in pursuit of long-term transformation of the global economy.

Beyond areas of prioritization, firms should aim to be "fast followers" of those that exhibit leadership and play an outsize role in a given sector, asset class, and/or geography. Such an approach will allow them to be additive in moving the transition forward by building momentum and harmonization where significant and credible progress has been made on decarbonization strategies.

Why is it important?

A financial institution's responsibility to climate alignment is equal to the maximum influence it could wield. Ultimately, this means that climate-aligned financial institutions will need to use all available levers of influence and approaches to achieve alignment across their entire business. Yet, as noted in Principle 1, because each financial institution is unique, the relevance of actions they have at their disposal will differ, along with the relative impact of each action on cumulative emissions reductions.

Prioritizing actions where there is the greatest potential for impact in the real economy will allow financial institutions to effectively deploy limited resources where they are needed most, first. While prioritization of actions is essential to maximize impact, particularly in the short to medium term, financial institutions should ultimately aim for comprehensive, rapid climate alignment.

> **"What you do makes a difference, and you have to decide what kind of difference you want to make."**
>
> — Jane Goodall, scientist and activist

Center for Climate Aligned Finance

Principle 4

Adopt transition-relevant data and metrics to guide decision-making, without using a lack of data as an excuse for inaction.

04

What is it?

Intentionally steering portfolios in line with climate goals will require data and metrics that are granular and forward-looking, and that address the most significant drivers of emissions. Transition-relevant data should be based on asset-level, quantitative data and metrics where possible. When unavailable, corporate and/or sector-level data can be used as proxies. Above all, transition-relevant data should point a financial institution's alignment efforts and resources directly to the economic activities that are central to a transformed, net-zero economy.

Transition plans and transition-relevant data are an essential part of measuring the impact of a company's alignment activities, as financial institutions will need to understand at a granular level how companies and sectors intend to scale decarbonization and invest in climate-aligned solutions over time. Financial institutions should start requiring that clients and investee companies publish credible, 1.5°C-aligned transition plans and report progress. These plans and data should then be assessed and used to inform financial and engagement strategies.

However, a lack of data is not an excuse for inaction—financial institutions do not need perfect data to begin engaging with companies or taking actions that finance climate solutions, support transition plans, and mitigate stranded asset risk. Where data gaps persist, financial institutions should actively pursue that data directly with corporates and/or through collaborative partnerships with peers, data providers, and regulators to drive improved data accuracy and availability.

Financial institutions should continuously expand, iterate on, and improve alignment strategies based on the best available data, metrics, and methodologies as these evolve.

Why is it important?

The urgency of the climate crisis creates two imperatives: 1) financial institutions must act on commitments now, and 2) action must be focused on the most immediate needs first. While there is a clear need for better data and tools to measure climate alignment, impact, and risks, **there is no such thing as perfect climate data**. By adopting the best available data while engaging with portfolio companies, data providers, climate finance experts, and regulators, financial institutions can begin taking action while simultaneously improving the future data landscape.

Climate-related tools and data are proliferating rapidly, but not all climate-related data is the same. Given the urgency of the transition, financial institutions must be smart about the type of data they use and request from their clients, prioritizing data that can inform a firm's next steps on its alignment journey. For example, current and backward-looking data (such as financed emissions) can be useful in reporting existing alignment and creating a baseline. However, backward-looking data cannot provide insight into the transition-readiness or future alignment of a company or sector. Without granular, relevant, and forward-looking data, financial institutions will struggle to measure and report their own climate alignment, identify climate-aligned opportunities, and assess and assist on a client's alignment progress over time.

Center for Climate Aligned Finance

Principle 5

Collaborate to accelerate system-wide alignment.

05

What is it?

Financial institutions should work collaboratively, both domestically and internationally, to develop solutions to common barriers and leverage best practices toward achieving climate goals. Collaboration may include bilateral and multilateral engagements, and these engagements should involve shaping and sharing innovative practices, tools, and resources. Convergence and creativity among coalitions of committed, ambitious actors can streamline and accelerate collective progress. Due to the systemic nature of the challenge, financial institutions should actively collaborate with all relevant stakeholders, including counterparties, NGOs, customers, data providers, service providers, policymakers, and regulators.

Collaborative efforts should never come at the expense of individual ambition or timely action. Collaboration does not imply financial institutions should employ identical strategies or violate antitrust statutes and associated regulations, but rather that every financial institution should work with the most effective, up-to-date resources and strategies to efficiently tackle the transition and reduce barriers to action and progress.

For example, collaboration is needed in developing sectoral targets, emissions-intensity metrics, and disclosure practices to build shared expectations among portfolio companies and clients (which would enable Principle 2). These will require partnership with key industry stakeholders, such as sectoral leaders, peer financial institutions, and trade associations.

Why is it important?

Climate alignment represents disparate financial actors working toward a common goal of aligning the real economy to 1.5°C. Given the systemic and complex nature of the challenge, it is unlikely that financial institutions can achieve alignment by acting alone, and the resulting piecemeal transition would almost certainly be more disruptive and costly. Collaboration can often enhance the impact of individual actions and levers of influence, as it amplifies and leverages a larger portion of the sector.

Collaboration can help financial institutions on their climate alignment journey in several important ways:

- **Capacity-building**—learning from ongoing progress and best practices, including staying abreast of constantly improving tools and resources, can support alignment efforts.
- **Reducing costs**—removing barriers to alignment, converging on common asks and approaches, and sharing costs of innovation and engagement across the market can all reduce costs for both financial institutions and corporates.
- **Policy advocacy and regulatory engagement**—sharing knowledge with policymakers and regulators can empower them to foster an enabling environment for climate-aligned finance.
- **Creating a level playing field**—standardizing and sharing approaches and developing common definitions can help accelerate progress among laggards. This can also reduce complexity and friction in the global market.

- **Plugging carbon leaks**—as individual portfolios and sectors are brought into alignment, ensuring that emissions are mitigated and not just transferred to other parts of the global economy can drive real-world reductions.

- **Supporting improved data and disclosures**—amplifying and aligning calls for improved data and transparency from corporates and clients can minimize reporting and compliance burdens and facilitate comparable reporting.

- **Converging around standards and frameworks**—fostering widely accepted definitions of key concepts and terms helps ensure that climate alignment progress is monitored, measured, and reported in a way that is fair (giving credit where credit is due), effective (leading to real-economy outcomes), and comparable (enabling accountability across sectors, asset classes, and geographies).

- **Problem-solving**—identifying and developing solutions to shared barriers and areas of concern can spur action and implementation at the firm, sector, and systems level.

Collaboration has a role to play in accelerating implementation of every other IMPACT+ principle outlined in this document.

> **“Every barrier must be an indication to try a different way in radical collaboration with each other.”**
>
> — Christiana Figueres, former Executive Secretary of the UN Framework Convention on Climate Change

Principle 6

Transparently communicate alignment approaches and progress to all relevant stakeholders.

06

What is it?

Financial institutions should communicate their alignment journey to relevant stakeholders. At a minimum this means explaining on an annual basis the steps they're taking across all relevant business units to make progress toward their climate alignment targets.

Financial institutions should measure, evaluate, and disclose both financial and nonfinancial alignment activities and progress against targets. Where possible, this should adopt a science-based, top-down approach that can be supplemented with a more granular sectoral approach, in line with Principles 1 and 2. If a firm is unable to set specific targets, or certain kinds of targets, qualitative reporting and disclosures are still encouraged, as are interim climate goals—even if they are not aligned with 1.5°C pathways. Transparency regarding areas of inaction (or delayed action) is also necessary to illuminate barriers and gaps in alignment approaches. While the ultimate goal should be to convey progress relative to real-economy emissions reductions (connected to sectoral decarbonization pathways and a just transition), transparency today is preferable to waiting for perfection.

Financial institutions should report against all relevant scopes of emissions, and against their sectoral and firm-level strategies, to demonstrate accountable progress on decarbonization. As data, metrics, methodologies, and climate science improve over time, financial institutions should seek to improve reporting. While financial institutions should honestly caveat the impact of their alignment efforts, data insufficiencies may not justify opacity or inaction.

Transparent communication should be accessible and digestible for all stakeholders, including civil society. This means publicly available reporting that is easily located on the firm's website and presented in clear, direct language.

Why is it important?

With no time to waste, transparency is a necessary mechanism to measure progress, create accountability, level the playing field, monitor systemic risks, and reevaluate ongoing priorities and strategies. **Without transparency, the world will be left in the dark as to whether financial institutions are taking the necessary steps to support active, substantial decarbonization.**

Transparency as to *how* portfolio emissions reductions are achieved helps provide insight into real-economy impact and minimize emissions leakage.[vii] Financial institutions do not need to prove causality and additionality of impact but should explicitly account for the reason for reported emissions reductions, e.g., due to portfolio reallocation, absolute emissions reductions, or reporting changes.

For financial institutions, transparency can promote internal and external credibility. Internally, translating the firm's alignment strategy into disclosed activities and outcomes can help clarify expectations for employees and clients, institutionalize climate as a priority, and encourage bottom-up momentum toward stated goals. Externally, growing demand for climate-related information and action from a range of stakeholders—from regulators to civil society—means transparent communication will be required for a financial institution seeking to credibly pursue climate alignment.

vii Emissions leakage refers the shift of greenhouse gas emissions from one place to another, without being reduced. This can happen in several ways, including from one financial institution's portfolio to another's, or from country to country, for example.

Principle 7

+ Develop holistic oversight to minimize negative impacts.

07

What is it?

Financial institutions should have processes in place to ensure that progress in one area of the firm is not undercut by its other activities. Over time, this will require holistic strategies and governance structures that implement the above principles to maximize positive impact while minimizing negative impact across all relevant activities.

Prioritizing impact in areas of relative strength is important (Principle 3), since alignment cannot happen overnight, but positive impact should not be negated by harmful real-economy impacts from other financial and nonfinancial activities. Just as public support for ambitious climate regulation and policy support at the supranational, national, and regional levels can accelerate climate alignment, support for policymakers, policies, or third-party organizations that either seek to embed the carbon-dependent status quo or impede climate action are examples of clear misalignment.

Minimizing the negative impacts of all business activities is therefore just as critical as actively creating positive impact. This should include consideration of the potential negative social and environmental outcomes of climate-aligned opportunities. Including consideration of a company's transition plan in investment decision processes is important for assessing alignment, for example, but it does not mean that broader ESG concerns such as biodiversity loss, gender justice, racial justice, and economic justice should be ignored. Climate alignment is an opportunity for inclusivity, equity, and environmental protection, but it must be implemented intentionally for these benefits to be realized and distributed.

Why is it important?

Ultimately, the choices made today will impact the amount of climate change and the severity of disruption. Every ton of carbon avoided or abated helps limit cumulative emissions and delays the potential of reaching destabilizing tipping points. Actions that lock in a misaligned future will disrupt progress, making the transition harder and more costly for economies and communities around the world. Much like driving with one foot on the brake, financial institutions cannot travel a consequential distance on their alignment journey unless they are simultaneously minimizing negative impacts and maximizing positive impact.

While financial institutions should enact immediate climate action through near-term prioritization, they cannot afford to perpetrate interim harm or ignore deprioritized sectors, geographies, and asset classes over the long term. Stakeholders will increasingly expect climate alignment commitments and actions to constitute an institution's entire business. Such a holistic approach to alignment can minimize systemic risks, capture value from spillover benefits, and avoid contributing to outcomes that are counterproductive to climate alignment goals.

> **"Climate change is the single greatest threat to a sustainable future but, at the same time, addressing the climate challenge presents a golden opportunity to promote prosperity, security and a brighter future for all."**
>
> — Ban Ki-Moon, former U.N. secretary-general

About the Center
The Center for Climate-Aligned Finance was established by RMI to help the financial sector transition the global economy toward a zero-carbon, 1.5°C future. With deep partnerships in finance, industry, government, and civil society, the Center works to develop decarbonization agreements within high-emitting sectors, build global frameworks for climate alignment, and support financial institutions in decarbonizing their lending and investing portfolios. Launched in 2020, the Center builds on RMI's 40 years of experience developing market-based solutions to accelerate the energy transition.
You can find more information about us on our website, **www.climatealignment.org**.

All images used are from iStock.com unless otherwise noted.

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