Reporting Portfolio Emissions By Asset Managers

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Private fund sponsors frequently commit to collect and report data on the greenhouse gas ("GHG") emissions generated by companies in their portfolios, referred to as "portfolio" emissions and also known as "financed" emissions. In a 2020 report, the Carbon Disclosure Project estimated that financial institutions, including asset managers, on average reported financed emissions over 700 times larger than emissions from their own operations.

Asset managers collect data on portfolio emissions because investors in their funds and mandates request this information for their own ESG reporting and knowledge. Asset managers also collect the data as members of industry initiatives that require disclosure of GHG emissions data, such as the Task Force on Climate-related Financial Disclosures ("TCFD") and the Net Zero Asset Managers Initiative. Asset managers may also collect the data where they are required to do so, for example under the EU's Sustainable Finance Disclosure Regulation ("SFDR") or the International Sustainability Standards Board's ("ISSB") standards, which countries around the world are adopting into their national law – see our separate Debevoise In Depth on this topic. These standards require an asset manager to report information on its "Scope 3" emissions, which includes its portfolio emissions.

This note considers the frameworks under which an asset manager commonly collects and reports on its portfolio emissions. It also considers some of the practical issues which arise and possible solutions.

GHG Protocol

The original methodology to measure GHG emissions is the 2001 Greenhouse Gas Protocol ("GHG Protocol"). Under the GHG Protocol, there are three types (Scopes) of GHG emissions:

- Scope 1: Emissions from sources owned or controlled by the reporting company – direct emissions;

- Scope 2: Emissions generated from purchased energy – an example of indirect emissions; and

- Scope 3: All other indirect emissions throughout a company's upstream and downstream value chains – a further example of indirect emissions.

Under the GHG Protocol, Scope 3 GHG emissions are sub-divided into 15 categories. Of these, category 15 is for "Investments", which for an asset manager includes its portfolio emissions.

The GHG Protocol has published Technical Guidance for Calculating Scope 3 Emissions, which provides a detailed methodology for calculating and reporting each of the 15 categories of Scope 3 GHG emissions, including category 15 "Investments". The GHG Protocol's Guidance on reporting emissions associated with investments is primarily directed at companies that hold equity and debt investments as their own assets, with the company accounting for the relevant proportion of the emissions generated by such assets as part of its own Scope 1 and 2 emissions. The Guidance also states that, when Scope 3 emissions at the investee company are significant compared to other sources of emissions, the investor should account for its proportionate share of the Scope 3 emissions of the investee company. The Guidance further states that investors should prioritize for data collection those investments that are likely to contribute most significantly to total GHG emissions, and also describes methods for estimating emissions data from investee companies.

The GHG Protocol's Guidance notes that emissions associated with investments held on behalf of clients, including by fund managers, will be accounted for as Scope 3 emissions by the manager, but does not give further guidance on how emissions are accounted for in respect of particular asset classes.

PCAF

The Partnership for Carbon Accounting Financials ("PCAF") supplements the GHG Protocol by providing guidance for the financial services industry, including asset managers, on measuring the Scope 3 emissions from loans and investments. TCFD, which provides a framework for companies to disclose their climate-related risks and opportunities, recommends that banks, asset owners and asset managers measure and disclose financed emissions in line with the PCAF Standard. PCAF uses the term "financed emissions" to cover emissions generated by companies that receive loans from financial institutions and to cover emissions generated by investee companies in asset managers' portfolios.

PCAF has published the Global GHG Accounting and Reporting Standard for the Financial Industry. Part A of this Standard lays out a standard approach for calculating financed emissions for a variety of asset classes, including:

- Listed equity and corporate bonds;
- Business loans and unlisted equity;
- Project finance;
- Commercial real estate;
- Mortgages;
- Motor vehicle loans; and
- Sovereign debt.

PCAF has published separate guidance on measuring and reporting facilitated emissions (capital markets activities) and insurance-associated emissions. An asset manager which adopts Part A of the PCAF Standard will measure portfolio emissions as follows.

Firstly, it will report the absolute Scope 1 and 2 emissions arising from the companies it invests in or lends money to. As above, this encompasses emissions from sources owned or controlled by the underlying reporting company, such as exhaust emissions from company cars, as well as any emissions generated from purchased energy, for example to heat the reporting company's premises.

Secondly, for Scope 3 emissions arising from the underlying investee companies or borrowers, the asset manager will generally have regard to PCAF's phase-in approach, which envisages reporting Scope 3 emissions for oil, gas and mining sectors from 2021, for transportation, construction, buildings, materials and industrial activities sectors from 2023 and all other sectors from 2025. If the asset manager cannot report on required Scope 3 emissions because of data unavailability or uncertainty, it should explain this.

In each case, the asset manager will account for the relevant proportion of the underlying reporting company's emissions by reference to the proportion of equity or debt owned by the asset manager's mandate in the underlying company, relative to the total value of the company. The PCAF Standard provides the relevant methodology for the asset classes listed above. The PCAF Standard also provides guidance on sources of data and use of estimates, with estimates based either on data on "physical activities" provided by the borrower or investee company, such as tons of steel produced, or more broadly on data on the investee company's economic activities, such as the company's revenue, estimating its emissions based on average emissions in its sector.

Reporting Portfolio Emissions in Practice

Whilst asset managers may report to investors the emissions arising from a particular portfolio in line with the frameworks described above, some asset managers do not commit to report publicly their aggregate portfolio emissions across all their portfolios. Many asset managers for example opt out of reporting aggregate emissions under the SFDR principal adverse impacts regime. This is often because data on emissions at privately held portfolio companies can be difficult to collect, in particular Scope 3 emissions. In line with the PCAF Guidance above, asset managers may use estimated data, typically based on proxy companies in the same sector, but in practice asset managers are unwilling to publish aggregate emissions figures comprising large amounts of estimated data. Asset managers may also feel that reporting absolute emissions figures for the whole portfolio is misleading, as the bulk of an asset manager's portfolio emissions may arise from only a few portfolio companies with particularly high GHG emissions.

In addition, as an asset manager's portfolio emissions will likely rise during a fund's investment phase, when assets under management are growing, reporting on aggregate portfolio emissions can be misleading. This is regardless of whether the fund has committed to a particular sustainability objective, such as to reduce its investments' GHG intensity, for instance by converting a fossil fuel power station to a low carbon alternative. Arguably, using aggregate portfolio emissions as a sustainability indicator may encourage asset managers to divest from carbon intensive assets to reduce their emissions levels, although this does not reflect a 'real world' reduction in GHG emissions.

Many asset managers take alternative approaches, in particular the "portfolio coverage" approach, in which the asset manager assesses whether individual portfolio companies are adopting climate transition plans appropriate for their particular industry sector. The asset manager targets an increase in the proportion of investee companies which are themselves setting and delivering against transition plans. Asset managers may separately commit to engage with investee companies to help them develop capabilities to reduce their own GHG emissions.

Alternatively, an asset manager may adopt a "partial coverage" approach, committing to report on aggregate portfolio emissions from particular sectors or business groups within the portfolio, and excluding certain asset classes entirely where there is limited data availability or data quality is low. In addition, instead of reporting absolute GHG emissions with respect to its portfolio, an asset manager can choose to report relative figures, allowing better comparison with other asset managers, such as emissions per million EUR of asset under management, or emissions relative to the revenue of the investee company.

Conclusion

Asset managers should familiarize themselves with the methodologies for measuring GHG emissions under the PCAF standard when measuring and reporting on their portfolio emissions. Depending on their means and obligations to report this data, asset managers may choose to adopt a phased-in approach to reporting their portfolio emissions, prioritizing data collection and reporting for particular sectors where data is relatively easy to obtain or where emissions are relatively high. Asset managers should further be aware that the framework for calculating their portfolio emissions may change going forwards. For example, the Science Based Targets initiative ("SBTi") published in March 2025 a new proposed Net-Zero Standard. In recognition of the challenges in obtaining Scope 3 emissions data from value chain partners, the SBTi has placed greater emphasis on more qualitative, non-emission based metrics and targets, such as a company's proportion of suppliers that are themselves aligned to net zero, or the company's proportion of revenue derived from net zero aligned products and services. This may reduce the amount of Scope 3 emissions data which a fund's underlying investee companies may collect, in turn making it more challenging for asset managers to report portfolio emissions.

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