Divest Oregon’s Critique of the Treasurer’s Net Zero Plan: A Significant Event with Significant Weaknesses

Why is Treasurer Read’s Net Zero Plan significant?

- It acknowledges that climate change risk is a financial risk to the Oregon Public Employee Retirement System (PERS) that threatens the benefits for retired state employees and commits to mitigating that risk.

- It brings the Oregon Treasury in line with all other State agencies that were mandated by executive order in 2020 “to take actions to reduce and regulate greenhouse gas emissions” (Governor’s Executive order 20-04).

- It commits to measurably reducing the “greenhouse gas footprint” of the PERS retirement fund and begins by partially quantifying that footprint with industry standard methodology.

- It includes private investment funds in the emissions analysis, which most other such plans omit.

- It takes several immediate steps to begin to address PERS financial climate risk:
  - It commits to no new investments in private funds that are “primarily” (undefined) fossil fuel focused.
  - It directs Treasury staff to review publicly traded investments that derive >20% of revenues from thermal coal, oil sands and fracked shale oil and gas by February 2025.
  - It calls for increased staffing at Treasury to be able to implement other longer-term strategies for mitigating climate risk.

- It sets specific targets for OPERF emissions reductions, although they are very long term (2035 and 2050).

While a significant event, the Net Zero Plan also contains significant weaknesses and raises many questions:

1. Will the Net Zero Plan actions occur soon enough to protect OPERF beneficiaries from climate risk?

To mitigate the financial risks of climate change, Treasury must act before the market devalues assets that are no longer wanted due to their negative climate impact, such as coal or other fossil fuels…or before they are damaged by climate change caused natural events such as flooding, hurricane, or fire.

The Treasury’s March 2022 decision to divest its Russian oil assets after Russia invaded Ukraine is a cautionary tale. Market prices by then had collapsed and there were no
buyers. Two years later there has been no overall reduction in Treasury’s Russian holdings, although they have lost most of their value.

The Net Zero Plan sets a goal of 60% reduction in emissions by 2035 and net zero by 2050, over 25 years from now. Current scientific evidence says these targets are not soon enough.

The latest Intergovernmental Panel on Climate Change (IPCC) Synthesis report CLIMATE CHANGE 2023 stresses the need for action this decade:

- “Climate change is a threat to human well-being and planetary health (very high confidence). There is a rapidly closing window of opportunity to secure a liveable and sustainable future for all (very high confidence). . . . The choices and actions implemented in this decade will have impacts now and for thousands of years (high confidence).” (P. 24) (emphasis added)

- “Delayed mitigation and adaptation action would lock in high-emissions infrastructure, raise risks of stranded assets and cost-escalation, reduce feasibility, and increase losses and damages (high confidence).” (P. 25)

- “For any given future warming level, many climate-related risks are higher than assessed in AR5 [IPCC’s 2014 report], and projected long-term impacts are up to multiple times higher than currently observed (high confidence). Risks and projected adverse impacts and related losses and damages from climate change escalate with every increment of global warming (very high confidence). Climatic and non-climatic risks will increasingly interact, creating compound and cascading risks that are more complex and difficult to manage (high confidence).” (P. 14)

This February, for the first time the world exceeded 1.5 degrees C for the past year. Scientists are increasingly concerned that exceeding 1.5 degrees C on a continuous basis will trigger multiple climate feedback loops with cascading effects:

- “Current global warming of ~1.1°C above pre-industrial already lies within the lower end of five tipping point uncertainty ranges. Six tipping points become likely (with a further four possible) within the Paris Agreement range of 1.5 to <2°C warming, including collapse of the Greenland and West Antarctic ice sheets, die-off of low-latitude coral reefs, and widespread abrupt permafrost thaw.” (summary page)

Scientific evidence indicates that many risky feedback loops amplify the need for climate action (Ripple et al. 2023):

- “[C]limate models may still be underestimating the acceleration in global temperature change that a large and interrelated set of amplifying feedback loops and tipping points could cause.” (P.86)

- “The remaining carbon budget is rapidly shrinking and waiting until 2050 to achieve net-zero carbon emissions might be far too late. The gap between projected emissions (assuming 2030 mitigation pledges are met) and emissions consistent with 1.5C is very large, and time is running out to avoid the worst effects of climate change. . . . Therefore, shortened timelines for carbon neutrality (before 2050), and more ambitious emissions drawdown with near-term requirements should be swiftly implemented as a response to this emissions gap.” (P.90) (emphasis added)
Economists and actuaries are now pointing out that traditional studies of climate-change economic impacts are wildly at odds with the findings of climate science summarized above. Consequently, many climate models are severely understating the economic impact of climate change. *The Emperor’s New Climate Scenarios* (P. 18).

The inconsistency has arisen largely because climate change economics papers have been chosen for publication only by economists without the input of climate scientists. *Loading the DICE against pension funds–Flawed economic thinking on climate has put your pension fund at risk* (P. 13)

- “For example, the investment consultant Mercer advised Australian super fund HESTA that a warming trajectory of 4°C in 2100 would result in a 17% portfolio impact. In contrast, research by climate scientists implies that the impact of a 3°C increase (or even lower) could be ‘catastrophic’, that climate tipping points could be triggered even at 1°C of warming, and that changes to our climate which could trigger tipping points are ‘too risky to bet against.’” (P. 12)

- “Pension funds have been poorly advised, inadvertently or not, on the dangers that climate change poses for their portfolios. The challenges that climate change poses to the retirement incomes of their members are not distant and small, but immediate and potentially wealth-destroying.” (P. 68)

**Bottom line:** Although the Net Zero Plan states that its 2035 60% emissions reduction and 2050 Net Zero targets are as aggressive as Treasury can be without major portfolio disruption, scientific evidence suggests major portfolio disruptions from climate change will occur well before those points. The Net Zero Plan timelines should be accelerated in line with updated science to protect OPERF beneficiaries.

2. Is the Net Zero Plan’s measurement of investment emissions comprehensive enough to identify all of OPERF’s significant climate financial risk?

*The plan ignores available data on critical Scope 3 emissions.*

The Net Zero Plan acknowledges that analyzing the exposure of a portfolio of OPERF’s size and complexity to direct and indirect greenhouse gas emissions is essential to assess our exposure to physical and transition risks (P. 10). Targeting investments generating CO2 and equivalent emissions, if done rigorously, will identify those investments that are most likely to be “stranded” as the world moves to reduce greenhouse gases.

But the current Net Zero Plan has a significant loophole: It excludes measurement of “indirect” Scope 3 emissions, which are estimated to be 75% of a company’s emissions. For example, it includes an oil company’s emissions from drilling, transporting and refining oil (Scope 1), and emission from the power they purchase (Scope 2) but not the majority of oil related emissions, those from burning the produced diesel or gas (Scope 3).

Omitting fossil fuel investments’ indirect Scope 3 emissions profoundly understates their risk to OPERF. Overall, the oil and gas industry produces 42 percent of global emissions, with 9% from Scopes 1 and 2 and 33% from Scope 3.
While the Net Zero Plan indicates that Scope 3 emissions will be included once they become generally reported, including what is available now will increase the chance of identifying high risk carbon intensive investments that need to be addressed sooner rather than later.

While Scope 3 emissions are not available for all companies, 37% of public companies worldwide currently report Scope 3 emissions. [July 2023 MSCI Net-Zero Tracker](https://www.msci.com/sg/en/sustainability/focus/climate-change/nzpro.php).

- California recently passed a law requiring corporations earning more than $1 billion to report their Scope 3 emissions beginning in 2025. [Harvard Law School Forum on Corporate Governance](https://harvardlawreview.org/2019/08/policy-and-law-enforcement-future battery companies for the planet/).
- ExxonMobil already reports Scope 3 emission estimates that, while flawed, begin to depict their vast quantities, reflecting their vast risk to OPERF. [Advancing Climate Solutions | 2023 Progress Report GHG Data Supplement](https://www.exxonmobil.com/responsibility/sustainability/).  

The plan ignores physical damage from climate change to OPERF investments

Targeting greenhouse gas emissions alone ignores the impact on investments due to physical damage from changes in the natural ecosystem caused by global warming, such as sea level rise or the increase in severe weather events.

The Treasury commissioned a Climate Scan Report by ORTEC in 2021 that called out managing such physical risks as a key strategy for mitigating climate risk. It provided a preliminary risk analysis for the OPERF portfolio based on the regional impacts of physical climate risk, evaluating risk drivers such as whether a country is closer to the equator and more greatly impacted by increased temperature, whether they are more or less at risk for decreasing land, labor and industrial productivity, or whether they have a lower economic capacity to buffer extreme weather losses.

In general, ORTEC projected that the longer it takes for globally coordinated action on climate, the more disruptive it will be for markets, with physical risks becoming the main contributor to climate financial risk. In their worst failed transition scenario, they projected significant impacts on OPERF’s portfolio returns by the 2030s and a 20% reduction of returns by 2060. More alarming, they state that “the physical risk impacts are likely understated.”

One of ORTEC’s key recommendations was to “embed climate change analysis at every level of risk analysis and decision-making along the investment process.”

To fully protect beneficiaries, the Net Zero Plan should include a broader approach such that all investment decisions include a climate change risk analysis both in terms of transition risk – or sudden repricing of assets as the market reacts to climate disruption – and in terms of the physical risks as we accelerate toward critical environmental tipping points.

**Bottom Line:** Omitting available fossil fuel investments’ Scope 3 emissions and physical damage from greenhouse-gas induced ecosystem changes profoundly understates the risk to OPERF.
3. Will engagement with fund managers and companies to ensure OPERF investments have “climate-or-transition aligned” or “credible net zero transition plans” – the Net Zero Plan’s core strategy – be effective?

There is increasing evidence that engagement with fossil fuel companies does not work.

2024: The Dutch Pension Fund, PZFW, the 10th largest pension fund in the world, announced that it had sold off its $3 Billion in fossil fuel holdings, including Shell, BP and Total Energies, after their engagement program failed. According to the Board Chair: “The intensive shareholder dialogue over the past two years with the oil and gas sector on climate has made it clear to us that most fossil fuel companies are not prepared to adapt their business models to ‘Paris’.”

2023: The Church of England announces it is divesting from the oil and gas sector after a similar failure of engagement.

2022: The U.S. House Committee on Oversight and Reform released a report and documents that show how the fossil fuel industry engages in “greenwashing” to obscure its massive long-term investments in fossil fuels and failure to meaningfully reduce emissions.

- “Even though Big Oil CEOs admitted to my Committee that their products are causing a climate emergency, today’s documents reveal that the industry has no real plans to clean up its act and is barreling ahead with plans to pump more dirty fuels for decades to come,” said Chairwoman Maloney.

There is no evidence anything has changed. Instead oil and gas companies are decreasing their commitment to alternative energy, “prioritizing dividends, share buybacks and continued fossil fuel production over increasing their clean energy investments,”

- While 75 of the world’s largest 112 fossil fuel companies now have net zero emissions targets, most lack credible Scope 3 emissions targets which makes them “largely meaningless” according to a recent review.

The UN Expert Group’s 2022 report on Net Zero commitments, “Integrity Matters,” recommends that “All net zero pledges should include specific targets aimed at ending the use of and/or support for fossil fuels” in order to limit global warming to 1.5 degrees C.

The Net Zero Plan leaves key engagement criteria undefined.

The Net Zero Plan does not define the criteria by which Treasury will assess “climate-or-transition alignment” nor the criteria or process for exclusion of investments not sufficiently aligned. That work is yet to be done by Treasury staff.

These definitions and criteria are critical to all the “Major Actions” of the Net Zero Plan, whether it be the initial review of carbon intensive investments, the increase of public and private “climate aligned” investments, or real asset and real estate investments with credible net zero transition plans.

**Bottom Line:** Given the current lack of evidence on the effectiveness of an engagement strategy, it will be up to the Treasury to demonstrate that it can satisfy its fiduciary duty to protect PERS beneficiaries by succeeding where others have consistently failed.
4. How will PERS beneficiaries and the public know this plan is working to protect pensions with the urgency called for by accelerating climate change?

Transparency is critical. As written, the Net Zero Plan lacks an annual robust reporting framework that would allow stakeholders to follow its implementation and ongoing results with interim targets so it can be adjusted as needed. Waiting until 2035 to know if it is “on target” is reckless.

How will Treasury assure us that their certification of “climate aligned” strategies are not just pledges without realistic implementation plans or demonstrable progress? The most recent overview of Net Zero plans — from company to national levels — indicates that so far the vast majority are just that: policy statements without robust adoption measures.

A Beneficiary Advisory Committee is proposed but no details are given as to how it will be “advisory” or what kind of beneficiary voices will be included.

5. How will the Net Zero Plan become a formal OIC policy?

Safeguarding OPERF from climate risk should not be the job of a sole treasurer or the Treasury staff alone; it must be OIC investment policy to be credible and long lasting. Only a policy can guide work, provide oversight, and create accountability.

The Net Zero Plan is inherently a policy shift. The Oregon Investment Council (OIC) is broadly mandated by statute (ORS 293.731) to formulate policies for the investment and reinvestment of OPERF contributions, and for the acquisition, retention, management and disposition of OPERF investments.

Systematically mitigating climate risk is a policy. It needs to be formalized, with the OIC taking an active role both in overseeing the implementation of any Net Zero Plan and how urgently the staff is acting to proactively protect beneficiaries.

6. Why is the Net Zero Plan limited to OPERF?

Treasury invests more than $40 billion in state funds in addition to OPERF. Why is the entire $140 billion in state investment funds not worthy of protection from urgent climate risk? The plan, and OIC policy, needs to extend to all such funds.