KPMG

The COP21 Paris Agreement:

A clear signal to business

Briefing on the outcome of COP21

The 2015 UN Climate Change Conference

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KPMG International

Introduction

A momentous agreement

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In an historic move, 195 countries met in Paris in December 2015 and committed to limit global warming to "well below" 2˚C above pre-industrial levels and to "pursue efforts" to keep it to 1.5°C.

This is an unprecedented international climate deal. For the first time ever, almost every country on earth has committed to cut its carbon emissions in order to achieve a collective goal.

The Paris Agreement, which officially comes into force in 2020, sends a clear and unequivocal signal to the private sector: a global political intention to shift to a low carbon, and ultimately zero carbon, future.

If the goal agreed in Paris is to be achieved it will require a transformation of global energy systems, transport and industrial processes over the next few decades. Businesses face both risks and opportunities in this transition since they must deliver the bulk of the necessary emissions reductions and investment.

Of course, the agreement is just the start and this is where the hard work begins. Governments face many political, policy and financial challenges in following through on the commitments they made in Paris. Yet we should not underestimate the significance of what has happened. International consensus on addressing climate change has finally been achieved after more than two decades of trying and failing.

This paper has been written for executives at KPMG member firm clients. It aims to explain what was agreed at COP21 and why it matters to the business community. It is not a detailed analysis of the text agreed in Paris, but rather a summary of the key points and their implications. I hope you find it useful in considering what a post-COP21 world means for your organization.

What was agreed at COP21?

Countries have committed to halting the rise in global temperature

The overall objective of the agreement is to keep the increase in global temperature to well below 2˚C above pre-industrial levels and to pursue efforts to limit it to only 1.5˚C. Temperatures have already increased by 1°C.

1.5°C - 2°C is the level at which science tells us that catastrophic and irreversible climate change impacts are likely.

The world will be carbon neutral

Countries agreed to peak greenhouse gas (GHG) emissions as soon as possible and to achieve carbon neutrality between 2050 and 2100. This means limiting emissions to the level that can be naturally absorbed by forests, oceans and soil.

All countries will set national targets to reduce carbon emissions and update them every 5 years

All countries must set national targets to reduce their carbon emissions and 188 have already done so. These targets are known as Intended Nationally Determined Contributions or INDCs.

The INDCs must be strengthened over time because the current targets are insufficient to limit warming to well below 2°C. (The existing targets will lead to warming between 2.7˚C and 3.5˚C above pre-industrial levels).

The Paris Agreement sets out a 5 year cycle of global stock takes to assess progress followed by the submission of updated INDCs. There will be an initial review in 2018 to inform the first submission of new or updated INDCs by 2020.

The first official stock take will take place in 2023 with new INDCs to be submitted by 2025. The cycle then continues in this way every 5 years.

Countries will report transparently on their carbon reduction progress

While the targets themselves are not legally binding, the agreement requires countries to report their progress transparently which in itself puts pressure on countries to deliver on their commitments.

Richer countries will provide financial assistance for poorer countries

Developed nations will provide US$100 billion per annum by the year 2020 to help finance green, low-carbon growth in developing nations and other nations are also encouraged to contribute on a voluntary basis. The agreement aims to increase this amount between 2020 and 2025.

Vulnerable countries will receive financial assistance for loss and damage from climate change

The agreement recognizes that poor countries that are most vulnerable to the effects of climate change, such as small island nations, need financial help to avert and minimize losses from events such as extreme weather. However, importantly for developed nations, there is no mention of liability and no legal mechanism for affected countries to receive financial compensation from richer nations whose fossil fuel-based economic development is responsible for the bulk of global carbon emissions to date.

What does it mean for business?

KPMG's predictions

The global economy will evolve to a low carbon model

The challenge of limiting temperature rises and achieving a carbon neutral world cannot be underestimated. It will require nothing short of a transformation of power production, transport and industrial processes within a few decades.

In order to achieve this goal and deliver on their national commitments to cut carbon, governments need to implement effective regulation, such as carbon taxes, emissions trading systems and energy efficiency standards that drive businesses to lower their emissions. They will also need to provide incentives for businesses to develop and deploy low carbon technologies such as renewable energy, electric transport systems and fossil fuel decarbonizing technology such as carbon capture and storage.

While the change will not be immediate, if the Paris Agreement is to succeed in its goal, then it must change the global economy over the medium to long term to one that discourages the consumption of fossil fuels and encourages low-carbon innovation.

Investors will look more closely at climate-related risk and opportunity

Now that governments have committed to creating a carbon neutral world, investors will take an increasing interest in how companies plan to build shareholder value in the changing global economy. They will expect companies to be more transparent about the financial, environmental and social risks and opportunities they face from the physical impacts of climate change, such as extreme weather, as well as from climate-related regulation, market dynamics and stakeholder pressure.

The Financial Stability Board's recently announced disclosure task force on climate-related risk is just one example of increasing investor scrutiny.[1] Other examples include the Portfolio Decarbonisation Coalition

1. http://www.financialstabilityboard.org/2015/12/fsb-to-establish-task-force-on-climate-related-financial-disclosures/ Retrieved 15 December 2015
2. http://unepfi.org/pdc/ Retrieved 15 December 2015
3. http://montrealpledge.org/ Retrieved 15 December 2015
4. http://www.bloomberg.com/news/articles/2014-05-11/power-decarbonization-cost-rises-22-to-44-trillion-iea-says Retrieved 15 December 2015
5. http://cleantechnica.com/2015/10/22/iea-13-5-trillion-climate-investment-needed-2030/ Retrieved 15 December 2015

(PDC)[2] of institutional investors that aims to decarbonize US$600 billion of assets under management and the Principles for Responsible Investment (PRIs) Montreal Carbon Pledge which commits investors to measure, disclose and reduce the carbon footprint of their portfolios.[3]

Investment in clean technology will grow dramatically

Some US$44 trillion is needed to decarbonize the global power supply, according to the International Energy Agency[4]; $13.5 trillion is required just to achieve the carbon cuts that were pledged by countries in the run-up to COP21.[5] The common global goal agreed in Paris sends a strong signal that is likely to significantly increase the flow of capital into the innovation and deployment of clean technologies.

Governments cannot afford to fund this transformation alone, and so together with multi-lateral institutions and other bodies, they will seek to leverage private sector investment. An example is the Mission Innovation initiative launched by Presidents Obama and Hollande that commits 20 countries to double their clean-tech research and development budgets over the next 5 years.[6] Other examples include the international solar alliance which brings together 120 countries in a push to mobilize US$1 trillion to scale up solar power production[7] and the African Renewable Energy Initiative which seeks to raise US$20 billion for large scale renewable projects in Africa.[8]

Pressure will grow for businesses to set 2˚C targets

The world has now agreed to limit global warming to well below 2°C. It is therefore likely that businesses, which account for the bulk of global emissions either directly or indirectly, will face increasing pressure to align their own carbon reduction strategies and targets with this global goal.

More than 100 of the world's leading companies have already committed to do so as part of the Science Based Targets Initiative[9]. It is likely that the approach taken by these pioneering companies will become standard practice for large companies worldwide over time. KPMG's Survey of Corporate Responsibility Reporting found that currently only one in ten of the world's largest companies that set carbon reduction targets do so in line with international carbon reduction goals.[10]

An international carbon market will emerge

The Paris Agreement allows countries to achieve their carbon targets through market mechanisms and emissions trading. The text refers to linkages between existing carbon markets and so could be the basis for a framework to link national systems to form an international system of carbon pricing. As more and more countries introduce their own carbon pricing systems, not least China whose system is due in 2017, increasing co-operation and linkage seems only a matter of time.

An expanding international carbon pricing system would offer clear benefits to business in terms of simplifying the very complex challenge of working within multiple national systems.

6. http://mission-innovation.net/ Retrieved 15 December 2015
7. http://www.theguardian.com/environment/2015/nov/30/india-set-to-unveil-global-solar-alliance-of-120-countries-at-paris-climate-summit Retrieved 15 December 2015
8. http://www.bloomberg.com/news/articles/2015-12-01/african-union-introduces-20-billion-renewable-energy-plan Retrieved 15 December 2015
9. http://sciencebasedtargets.org/ Retrieved 15 December 2015
10. KPMG International (2015) The KPMG Survey of Corporate Responsibility Reporting 2015, www.kpmg.com/crreporting Retrieved 15 December 2015

What should business focus on in a post COP21 world?

Operations

- Ensure that the business fully understands and is prepared for the potential financial, environmental and social impacts of climate change on the supply chain.
- Consider the effects of extreme weather such as storms and flooding on critical suppliers, possible disruption to the supply of key commodities and raw materials, and increasing water scarcity in many regions.
- Ensure that the right systems and processes are in place to deal with increasingly stringent carbon reporting requirements.
- Protect brand and reputation by developing and communicating a clear and consistent position on the issues of carbon and climate change, and showing what your business is doing to reduce emissions.
- Understand how the carbon reduction commitments made by the countries in which you operate are likely to affect your organization.

Strategy

- Engage with governments and industry to understand the direction of carbon reduction policy. Plan scenarios to explore how developing policy development is likely to affect your organization through regulation, penalties and incentives.
- Anticipate the impact of carbon pricing systems by building an internal carbon price into business planning and risk management (where there is no existing pricing system). Over 400 companies worldwide that report to the Carbon Disclosure Project (CDP) are already using carbon pricing internally to drive investments in emission reduction.[11]
- Understand the future risks and opportunities your business faces from carbon reduction regulation, changing market dynamics and stakeholder pressure, as well as the physical impacts of extreme weather, and be prepared to communicate your strategy clearly to investors.
- Align your company's carbon reduction strategy with the agreed global goal of keeping temperature rise to well below 2°C.
- Explore how your organization can benefit from increased investment flows into clean technology and low carbon solutions.
- Investigate opportunities to raise capital for investment in carbon reduction and low-carbon innovation, for example through green bonds or through clean technology incentives and subsidies.

11. https://www.cdp.net/CDPResults/carbon-pricing-in-the-corporate-world.pdf Retrieved December2015

How we can help

KPMG member firms offer climate change and sustainability services in around 60 countries. Our experts help organizations with the risks and opportunities of climate change and related legislation.

Ways in which we can support you include:

Strategy

Help you to understand and profit from disruptive change in the low carbon economy

— Identify and reduce climate-related risk in your supply chain

— Help you to minimize the costs of carbon taxes or carbon pricing systems worldwide

Compliance

— Help you understand and comply with carbon-reduction and carbon reporting legislation worldwide

Reporting

— Implement effective processes and IT solutions to gather, analyze and report carbon data across your organization

— Advise you on industry best practice for carbon reporting

— Provide independent third party assurance of your carbon data

Finance

— Advise you on issuing green bonds to raise capital for investments and innovations that reduce carbon emissions and/or increase energy efficiency

— Provide independent third party assurance for green bonds, e.g. use of proceeds

— Help you to identify and access tax incentives for carbon reduction and energy efficiency

KPMG thought leadership

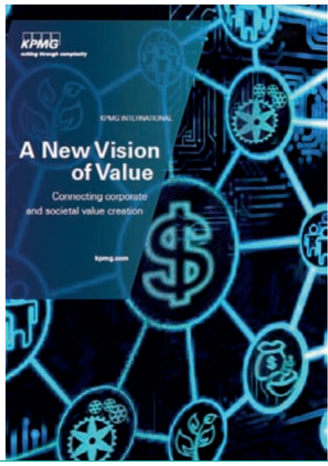
KPMG member firms have produced a range of publications on sustainability, including:

— The KPMG Survey of Corporate Responsibility Reporting 2015: Provides a snapshot of global CR reporting trends and a deep-dive into the quality of carbon reporting among the 250 largest companies in the world kpmg.com/crreporting

— Gearing up for Green Bonds: Provides practical advice on issuing a green bond kpmg.com/greenbonds

— A New Vision of Value: Explores how organizations can quantify and communicate the value they create for society kpmg.com/truevalue

— KPMG Green Tax Index: Analyzes the green tax policies of 21 countries worldwide kpmg.com/greentax



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