

# S&P Paris-Aligned Transition ESG Indices Consultation on Eligibility Requirements and Constraints

**AMSTERDAM, MAY 2, 2024:** S&P Dow Jones Indices (“S&P DJI”) is conducting a consultation with market participants on potential changes to the S&P Western Europe Plus LargeMidCap 100 Paris-Aligned Transition ESG Index and the S&P 500 Paris-Aligned Transition ESG 100 Index. To ensure the indices continue to meet objectives, and as a result of previously received feedback, S&P DJI is proposing to make changes to the indices’ eligibility requirements and constraints, as detailed below.

## Eligibility Factors

S&P DJI is proposing to extend the existing data coverage requirement in effect for all Sustainalytics and S&P Trucost Limited (Trucost) data sets to include all relevant Sustainable1 data sets.

Proposed Change	Methodology	
	Current	Proposed
Dataset Coverage	<ul style="list-style-type: none"> <li>Must be covered by all relevant Sustainalytics data sets.</li> <li>Must be covered by all relevant Trucost data sets.</li> </ul>	<ul style="list-style-type: none"> <li>Must be covered by all relevant Sustainalytics data sets.</li> <li>Must be covered by all relevant Trucost data sets.</li> <li><b>Must be covered by all relevant Sustainable1 data sets.</b></li> </ul>

## Exclusions Based on Business Activities

S&P DJI is proposing to introduce new exclusions for involvement in Oil & Gas activities, superseding the existing exclusions for Shale Energy, Oil Sands and Arctic Oil & Gas Exploration.

Proposed Change	Methodology	
	Current	Proposed
Shale Energy: Extraction	Level of Involvement Threshold: <b>≥5%</b> Significant Ownership Threshold: N/A	--
Oil Sands: Extraction	Level of Involvement Threshold: <b>≥5%</b> Significant Ownership Threshold: N/A	--
Arctic Oil & Gas Exploration: Extraction	Level of Involvement Threshold: <b>≥5%</b> Significant Ownership Threshold: N/A	--
Oil & Gas: Production	--	Level of Involvement Threshold: <b>&gt;0%</b> Significant Ownership Threshold: <b>≥10%</b>
Oil & Gas: Generation	--	Level of Involvement Threshold: <b>&gt;0%</b> Significant Ownership Threshold: <b>≥10%</b>

## Exclusions Based on Revenue Thresholds in Fossil Fuel Operations and Power Generation

S&P DJI is proposing to revise the existing exclusions for involvement in Oil Exploration or Processing and Natural Gas Exploration or Processing.

Methodology		
Proposed Change	Current	Proposed
Oil Exploration or Processing	Revenue Threshold: <b>≥10%</b>	Revenue Threshold: <b>&gt;0%</b>
Natural Gas Exploration or Processing	Revenue Threshold: <b>≥50%</b>	Revenue Threshold: <b>&gt;0%</b>

## Exclusions Based on New Thermal Coal Exploration, Extraction or Transportation Projects

S&P DJI is proposing to introduce additional exclusions for involvement in new Thermal Coal Expansion projects, utilizing data from Sustainable1's Business Involvement Screens.

Methodology		
Proposed Change	Current	Proposed
Coal Expansion: Mining	--	In-situ Reserves Value: <b>&gt;0%</b>
Coal Expansion: Power Plants	--	Power Generation Capacity: <b>&gt;0%</b>
Coal Expansion: Transport/Infrastructure	--	Capex: <b>&gt;0%</b>

## Exclusions based on Fossil Fuel Reserves

S&P DJI is proposing to introduce additional exclusions on companies with fossil fuel reserves, as measured by Trucost.

Methodology		
Proposed Change	Current	Proposed
Thermal Coal	--	2P Fossil Fuel Reserves <sup>1</sup> <b>&gt;0</b>
Other (Non-Metallurgical) Coal	--	2P Fossil Fuel Reserves <b>&gt;0</b>
Conventional and Unconventional Oil	--	2P Fossil Fuel Reserves <b>&gt;0</b>
Natural Gas	--	2P Fossil Fuel Reserves <b>&gt;0</b>
Shale Gas	--	2P Fossil Fuel Reserves <b>&gt;0</b>
'Other' Oil and Gas	--	2P Fossil Fuel Reserves <b>&gt;0</b>

<sup>1</sup> 2P, or 'proven and probable' reserves, are those with more than a 50% probability to be recovered.

## Exclusions Based on Greenhouse Gas Emissions Intensity of Power Generating Companies

S&P DJI is proposing to exclude companies identified as ‘Majority Power Generation Companies’<sup>2</sup> with electricity production carbon intensity exceeding a predefined threshold.

Proposed Change	Current	Methodology	
		Proposed	
Majority Power Generating Companies	--	$\frac{GHG1_i}{Total\ Power\ Generation_i} > 207^3\ gCO_2e/kWh$	Where: GHG1 <sub>i</sub> = Scope 1 GHG emissions in tCO <sub>2</sub> e for the company i Total Power Generation <sup>4</sup> <sub>i</sub> = The total power generated (GWh) by constituent i

## Exclusions Based on Sustainalytics ESG Risk Rating

S&P DJI is proposing to revise the exclusions based on Sustainalytics ESG Risk Rating.

Proposed Change	Current	Methodology	
		Proposed	
Exclusions Based on Sustainalytics ESG Risk Rating	As of each rebalancing reference date, rank eligible securities by Sustainalytics ESG Risk Rating and exclude, by count, the highest ranked 20% of the total number of securities in the index universe.	As of each rebalancing reference date, exclude companies with a Sustainalytics ESG Risk Rating > 30.	

## Exclusions Based on S&P Global ESG Score

S&P DJI is proposing to introduce an additional exclusion based on the S&P Global ESG Score.

Proposed Change	Current	Methodology	
		Proposed	
Exclusions based on S&P Global ESG Score	--	As of each rebalancing reference date, the index verifies that at least 30% of the total index weight is excluded by applying the ESG-related exclusions relative to the underlying index after applying the non-ESG listing criteria. If the 30% exclusion threshold is not met, the index identifies the sector with the least exclusions by weight and applies a single exclusion to remove the	

<sup>2</sup> Majority Power Generation Companies are defined as those companies whose combined revenues from relevant Trucost Sectors is greater than or equal to 50%. Relevant Sectors: Coal Power Generation, Natural Gas Power Generation, Petroleum Power Generation, Biomass Power Generation, Nuclear Electric Power Generation, Landfill Gas Power Generation, Geothermal Power Generation, Wind Power Generation, Solar Power Generation, Hydroelectric Power Generation, Wave & Tidal Power Generation, and Other Electric Power Generation.

<sup>3</sup> Label ISR soutenu par les pouvoirs publics (2023). Appendix 7: Exclusions.

FR: <https://www.lelabelisr.fr/wp-content/uploads/Referentiel-Label-ISR-dec23.pdf>

EN: [https://www.lelabelisr.fr/wp-content/uploads/EN\\_Referentiel-Label-ISR-mars24.pdf](https://www.lelabelisr.fr/wp-content/uploads/EN_Referentiel-Label-ISR-mars24.pdf)

<sup>4</sup> Total Power Generation is the combined total of the following data points: Coal Power Generation (GWh); Natural Gas Power Generation (GWh); LPG Power Generation (GWh); Petroleum Power Generation (GWh); LNG Power Generation (GWh); Wind Power Generation (GWh); Solar Power Generation (GWh); Biomass Power Generation (GWh); Geothermal Power Generation (GWh); Wave & Tidal Power Generation (GWh); Hydropower Power Generation (GWh); Nuclear Power Generation (GWh); Landfill Gas Power Generation (GWh); Other Power Generation (GWh).

		Methodology	
Proposed Change	Current	Proposed	
		constituent with the worst S&P Global ESG Score from that sector. The process continues iteratively until the 30% target exclusion target is reached.	
Exclusions based on S&P Global ESG Score and Sustainalytics ESG Risk Rating	-	<p>The index verifies if at least 10% of the total index weight is excluded by ESG Risk Rating or S&amp;P Global ESG Score.</p> <p>If the 10% exclusion threshold is not met, the index identifies the sector with the least exclusions by weight and applies a single exclusion to remove the constituent with the worst S&amp;P Global ESG Score. The process continues iteratively until the 10% target exclusion target is reached.</p>	

### Constituent Weighting

S&P DJI is proposing to revise the objective function by introducing an additional Capitalization Type requirement. The below tables outline the index-specific change.

S&P 500 Paris-Aligned Transition ESG 100 Index	
<b>Current</b>	<p><i>Objective Function</i></p> $= \frac{1}{N} \sum_{i=1}^N \left( \frac{(Parent\ Weight_i - Optimized\ Weight_i)^2}{Parent\ Weight_i} \right) + \frac{1}{K} \sum_{k=1}^K \left( \frac{(Parent\ Sector\ Weight_k - Optimized\ Sector\ Weight_k)^2}{Parent\ Sector\ Weight_k} \right)$
<b>Proposed</b>	<p><i>Objective Function</i></p> $= \frac{1}{N} \sum_{i=1}^N \left( \frac{(Parent\ Weight_i - Optimized\ Weight_i)^2}{Parent\ Weight_i} \right) + \frac{1}{K} \sum_{k=1}^K \left( \frac{(Parent\ Sector\ Weight_k - Optimized\ Sector\ Weight_k)^2}{Parent\ Sector\ Weight_k} \right) + \frac{1}{J} \sum_{j=1}^J \left( \frac{(Parent\ Capitalization\ Type\ Weight_j - Optimized\ Capitalization\ Type\ Weight_j)^2}{Parent\ Capitalization\ Type\ Weight_j} \right)$ <p><i>Note: The market capitalization type of the S&amp;P 500 constituents is defined based on the S&amp;P U.S. BMI.</i></p>

S&P Western Europe Plus LargeMidCap 100 Paris-Aligned Transition ESG Index	
<b>Current</b>	<p><i>Objective Function</i></p> $= \frac{1}{N} \sum_{i=1}^N \left( \frac{(Parent\ Weight_i - Optimized\ Weight_i)^2}{Parent\ Weight_i} \right) + \frac{1}{K} \sum_{k=1}^K \left( \frac{(Parent\ Sector\ Weight_k - Optimized\ Sector\ Weight_k)^2}{Parent\ Sector\ Weight_k} \right) + \frac{1}{M} \sum_{j=1}^M \left( \frac{(Parent\ Country\ Weight_j - Optimized\ Country\ Weight_j)^2}{Parent\ Country\ Weight_j} \right)$
<b>Proposed</b>	<p><i>Objective Function</i></p> $= \frac{1}{N} \sum_{i=1}^N \left( \frac{(Parent\ Weight_i - Optimized\ Weight_i)^2}{Parent\ Weight_i} \right) + \frac{1}{K} \sum_{k=1}^K \left( \frac{(Parent\ Sector\ Weight_k - Optimized\ Sector\ Weight_k)^2}{Parent\ Sector\ Weight_k} \right) + \frac{1}{M} \sum_{j=1}^M \left( \frac{(Parent\ Country\ Weight_j - Optimized\ Country\ Weight_j)^2}{Parent\ Country\ Weight_j} \right) + \frac{1}{J} \sum_{j=1}^J \left( \frac{(Parent\ Capitalization\ Type\ Weight_j - Optimized\ Capitalization\ Type\ Weight_j)^2}{Parent\ Capitalization\ Type\ Weight_j} \right)$

where:

- $N$  = Number of companies selected
- $K$  = Number of sectors in the universe
- $M$  = Number of countries in the universe
- $J$  = Number of capitalization types in the universe

### Optimization Constraints

S&P DJI is proposing to remove the existing Fossil Fuel Reserves constraint as the exclusion is superseded by the proposed addition of a Fossil Fuel Free exclusion, revision of the Diversification Absolute Max Company Weight constraint, removal of the Diversification Relative Company Weight constraint, and introduction of an additional constraint based on Near-Term Target Alignment.

Proposed Change	Methodology	
	Current	Proposed
Fossil Fuel Reserves (FFR) Constraint	$\leq 20\% \times$ FFR of underlying index	--
SBTi Near Term Target Alignment Constraint	--	$\geq 40\%$ of index weight must have an SBTi near-term target aligned with a 1.5°C scenario, and, $\geq 45\%$ of High Climate Impact Sectors <sup>5</sup> weight within the index must have an SBTi near-term target aligned with a 1.5° C scenario
Diversification Absolute Max Company Weight	$\leq \max(10\%,$ underlying company weight)	$\leq \max(18\%,$ underlying company weight)

<sup>5</sup> Underlying index constituents are assigned a status of either 'High' or 'Low Climate Impact' based on GICS Sub-Industry Group. For more information on high/low climate impact, please see [here](#).

Proposed Change	Methodology	
	Current	Proposed
Diversification Relative Company Weight	± 5% from underlying index company weight	--

### Constraint Relaxation Hierarchy

S&P DJI is proposing to revise the Constraint Relaxation Hierarchy.

Proposed Change	Methodology	
	Current	Proposed
Constraint Relaxation Hierarchy	<p>If the optimization does not achieve a solution, each constraint in the hierarchy is relaxed in the order listed below and repeated, if necessary, until a solution is found.</p> <ul style="list-style-type: none"> <li>Weighted-Average Sustainability ESG Risk Rating</li> <li>Diversification Absolute Max Stock Weight</li> <li>Diversification Relative Stock Weight</li> <li>Liquidity Max Stock Weight</li> <li>Fossil Fuel Reserves</li> <li>Green-to-Brown Revenue Share</li> <li>1.5°C Climate Scenario Transition Pathway Budget Index Alignment</li> </ul> <p>If the optimization is not solved after relaxing all the above constraints, the following constraint is relaxed:</p> <ul style="list-style-type: none"> <li>Number of Stocks Selected</li> </ul> <p>The following constraints are considered hard constraints and are not relaxed:</p> <ul style="list-style-type: none"> <li>Weighted-Average Carbon Intensity (WACI) Target</li> <li>7% Decarbonization Trajectory WACI Target</li> <li>High Climate Impact Sectors Revenue Proportion</li> <li>SBTi Near-Term Target Alignment</li> </ul>	<p>If the optimization does not achieve a solution, each constraint in the hierarchy is relaxed in the order listed below and repeated, if necessary, until a solution is found.</p> <ul style="list-style-type: none"> <li>Liquidity Max Stock Weight</li> <li>Number of Stocks Selected</li> <li>1.5°C Climate Scenario Transition Pathway Budget Index Alignment</li> </ul> <p>The following constraints are considered hard constraints and are not relaxed:</p> <ul style="list-style-type: none"> <li>Weighted-Average Carbon Intensity (WACI) Target</li> <li>7% Decarbonization Trajectory WACI Target</li> <li>High Climate Impact Sectors Revenue Proportion</li> <li>Diversification Absolute Max Stock Weight</li> <li>Near-Term Target Alignment</li> <li>Green-to-Brown Revenue Share</li> </ul>

### IMPACT ANALYSIS

For an analysis of the impact of the proposed changes, please refer to the file available [here](#).

### CONSULTATION

Additional data and analysis may be made available in the Client Resource Center [www.spglobal.com/spdji/en/client-services/](http://www.spglobal.com/spdji/en/client-services/), which may be updated from time to time throughout the consultation without notice. Additional data and analysis may also be made available upon request.

## **IMPLEMENTATION TIMING**

S&P DJI is proposing to implement the previously described methodology changes, if adopted, in conjunction with the upcoming rebalancing, which takes effect prior to the market open on **Monday, June 24, 2024**. If adopted, the changes will first be visible to clients beginning on **Friday June 14, 2024**.

## **QUESTIONS**

Please answer the following questions and provide S&P DJI with the reasoning behind your answers:

1. **Do you agree with the proposal to extend the existing data coverage requirement to include Sustainable1 data sets?**
2. **Do you agree with the proposal to introduce new exclusions for involvement in Oil & Gas activities, superseding the existing exclusions for Shale Energy, Oil Sands, and Arctic Oil & Gas Exploration?**
3. **Do you agree with the proposal to revise the existing exclusions for involvement in Oil Exploration or Processing and Natural Gas Exploration or Processing?**
4. **Do you agree with the proposal to introduce additional exclusions for involvement in new Thermal Coal Expansion projects, utilizing data from Sustainable1's Business Involvement Screens?**
5. **Do you agree with the proposal to introduce additional exclusions on companies with fossil fuel reserves, as measured by Trucost?**
6. **Do you agree with the proposal to revise the exclusions based on Sustainalytics ESG Risk Rating?**
7. **Do you agree with the proposal to introduce an additional exclusion based on the S&P Global ESG Score?**
8. **Do you agree with the proposed constituent weighting formula change for the S&P 500 Paris-Aligned Transition ESG 100 Index?**
9. **Do you agree with the proposed constituent weighting formula change for the S&P Western Europe Plus LargeMidCap 100 Paris-Aligned Transition ESG Index?**
10. **Do you agree with the proposal to remove the existing Fossil Fuel Reserves constraint as the exclusion is superseded by the proposed addition of a Fossil Fuel Free exclusion, revision of the Diversification Absolute Max Company Weight constraint, removal of the Diversification Relative Company Weight constraint, and introduction of an additional constraint based on Near-Term Target Alignment?**
11. **Do you agree with the proposed changes to the Constraint Relaxation Hierarchy?**
12. **If any of the proposed changes are adopted, do you agree with the proposed implementation date?**
13. **Do you have any other comments or feedback regarding the proposed changes outlined above?**

## **CONSULTATION**

Participation in this consultation is important as S&P DJI gathers information from various market participants to properly evaluate market participants' views and preferences. Please respond to this survey by **May 10, 2024**, as S&P DJI does not accept responses post the survey closure date. Prior to the Index Committee's final review, S&P DJI may request clarifications from respondents as part of that review.

To participate in this consultation, please visit the online survey available [here](#).

*Please be advised that S&P DJI reviews and considers all feedback before a final decision is made. However, S&P DJI makes no guarantees nor is under any obligation to comply with any of the responses. The consultation may result in no changes or outcome of any kind. If S&P DJI decides to change the index methodology, the change(s) will be announced to clients and posted to the S&P DJI website with prior notice ahead of the effective date.*

Thank you for taking the time to complete this survey.

For more information about S&P Dow Jones Indices, please visit [www.spglobal.com/spdji](http://www.spglobal.com/spdji).

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### FOR MORE INFORMATION:

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## CONSULTATION