For professional investors only

CASE STUDY:

December 2023

American Electric Power

Background

American Electric Power Co., Inc. (AEP) is a public utility holding company that engages in the business of generation, transmission and distribution of electricity. It operates through the following segments: Vertically Integrated Utilities, Transmission & Distribution Utilities, AEP Transmission Holdco and Generation & Marketing. The Vertically Integrated Utilities segment engages in the generation, transmission and distribution of electricity for sale to retail and wholesale customers through assets owned and operated by its subsidiaries.

Our engagement

We began engagement with the company in November 2019, asking why it had not yet provided Task Force on Climate-related Financial Disclosures (TCFD)-aligned reporting when other utilities in the US had done so. TCFD-aligned reports help demonstrate a company’s resilience to low-carbon scenarios and can indicate to investors that the company has appropriate risk mitigation responses in place.

The company acknowledged that it was yet to publish a scenario-based climate report. It cited regulatory considerations that can make it difficult to communicate certain kinds of decarbonisation pathways. However, the company said it was reviewing the position closely.

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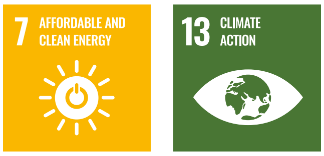
To keep the pressure on climate-related efforts, in 2020, we raised our concern that the company’s long-term strategy was not aligned with targets that would limit global warming to 1.5°C under the Paris Agreement. We wanted to encourage the company to align its strategy to a commitment to reach net-zero emissions by 2050.

Later that year at the Aspen winter energy roundtable, we conveyed the importance of TCFD reporting underpinned by rigorous scenario analysis including demand shifts that may happen more quickly than expected, and the need for more ambitious targets.

Engagement objectives:

Environmental:
TCFD-aligned disclosure with scenarios
Long-term ambition to achieve net-zero emissions

Sustainable Development Goals:



We welcomed the company’s consideration to increase the ambition of its 80% emissions reduction target by 2050 to a net-zero commitment if the scenarios, regulatory environment and customer rate case allowed during a Climate Action 100+ call in June 2020.

> **We enquired about the viability of setting a tougher target in line with the need for the utility sector to decarbonise by 2035**

Following the publication of its net-zero commitment by 2050 in early 2021, we enquired about the viability of setting a tougher target in line with the need for the utility sector to decarbonise by 2035 in order to limit global warming to 1.5°C. The company was wary of committing to net zero by 2035 due to technological, construction, customer price concerns and regulatory hurdles in some jurisdictions.

The company also said that it submitted a draft outline of its climate report, which will be aligned to the TCFD framework. It previewed the inclusion of three scenarios: business-as-usual, a mid-point; and 100% renewable energy and would include transition and physical risks/opportunities.

Following the report's publication in March 2021, we encouraged the company to consider pre-established scenarios in future analysis and were somewhat disappointed that policy-related transition risks had not been comprehensively covered. The company saw this as a federal issue rather than one to proactively model into its risk approach.

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In June 2022, the company acknowledged the need to accelerate the transition from coal and gas, however short-term capacity constraints might extend the company's reliance on coal.

Changes at the company

On its TCFD disclosures, in 2021, the CEO at the time said that its scenarios pointed to the last 5% of emissions being the most difficult to address. He reflected on the economic and social trade-offs of reaching net-zero versus capital spent elsewhere for the overall betterment of society.

We were pleased that the company recognised that any new investment in fossil fuels was risky from a stranded asset perspective. The company stated that it viewed natural gas as a placeholder for reliability until technology advances and not as a baseload as it prefers renewables.

In a call with the director of sustainability, we were pleased that the company would continue to consider revising its decarbonisation goals to reflect market factors.

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During an engagement in early 2022, the company said its sale of unregulated renewables segments to invest in transmission infrastructure enabled the company to de-risk and align capital allocation with its long-term strategy.

Following on from the company's June 2022 comments that short-term capacity constraints might extend the company's reliance on coal, the goals were improved in October 2022. In its new goals, the company published a goal of 80% reduction in emissions by 2030 (2005 baseline) and the ambition to be net zero by 2045.

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Next steps

We will continue to encourage the company to demonstrate that its medium-term target covers at least 95% of Scopes 1 and 2 emissions and the most relevant Scope 3 emissions, and are consistent with the Paris Agreement goals. We also will encourage it to evidence that its new material capital expenditure is consistent with the Paris Agreement goals with a published methodology.

This case study has been fact-checked by AEP to ensure a fair representation of EOS work carried out and changes made at the company.

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Engager
EOS

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