

CARBON DISCLOSURE PROJECT



CDP & CDSB Response to Defra Consultation

Measuring and reporting of greenhouse gas emissions by UK companies

July 2011

An introduction to CDP & CDSB

“The first step towards managing carbon emissions is to measure them because in business what gets measured gets managed. The Carbon Disclosure Project has played a crucial role in encouraging companies to take the first steps in that measurement and management path.”

Lord Adair Turner, Chairman, UK Financial Services Authority

“Climate Change is one of the greatest challenges of the 21st century... It is extremely important for investors to take account of climate change in their decision making. I wish the Carbon Disclosure Project success with its further efforts both in Germany and worldwide.”

Dr Angela Merkel, German Chancellor

“The Carbon Disclosure Project is vital and we've got to get everybody to participate in it. Climate change is a problem of prosperity and of unexamined processes and making investment decisions which may have made sense yesterday, but don't make sense for tomorrow.”

Former US President Bill Clinton

Carbon Disclosure Project (CDP)

The Carbon Disclosure Project (CDP) is an independent not-for-profit organisation, which operates the only global reporting system through which corporations, suppliers and cities report their greenhouse gas (GHG) emissions, climate change governance, risks and opportunities. CDP holds the world's largest registry of primary corporate climate change information. In 2010, over 3000 organisations in some 60 countries around the world measured and disclosed their greenhouse gas emissions and climate change strategies through CDP. For more information see www.cdproject.net. CDP now operates various major programmes:

Investor CDP is the largest collaboration of investors in the world and generates essential climate change information that helps drive capital flows to a low carbon economy. In 2011, over 551 institutional investors with assets of US\$71 trillion were signatories to Investor CDP, including Allianz, Axa, Goldman Sachs and HSBC.

CDP Supply Chain helps global corporations to understand the impacts of climate change across the supply chain, harnessing their collective purchasing power to encourage suppliers to disclose climate change information, targets and progress. Over 50 corporations including Ford and Unilever are members of CDP Supply Chain.

CDP Public Procurement provides a way for national and local governments to better understand the climate change related risk they face through the supply chain and work towards building a resilient, low carbon government supply chain. CDP Public Procurement works with a number of government departments and agencies.

CDP Water Disclosure provides critical water-related data from the world's largest corporations to inform the global market place on investment risk and commercial opportunity. In 2011, over 354 institutional investors representing US\$43 trillion in assets were signatories to CDP Water Disclosure.

CDP Cities provides a global platform that allows city governments to publicly disclose their GHG emissions data, analysis of climate change risks / opportunities and adaptation plans. CDP Cities allows city governments to demonstrate their commitment to transparency and facilitate the sharing of emissions data.

Climate Disclosure Standards Board (CDSB)

The Climate Disclosure Standards Board (CDSB) was formed at the 2007 annual meeting of the World Economic Forum. CDSB is an international organisation committed to the integration of climate change-related information into mainstream corporate reporting. CDSB works with leading professionals in accountancy, business, standard-setting and regulation to develop and advocate a generally-accepted global framework for use by corporations in disclosing climate change-related information in mainstream corporate reporting.

In support of its objectives, CDSB has developed a Climate Change Reporting Framework by drawing on the work of its Board members, on international developments in climate change regulation and on the work of the International Accounting Standards Board. Technical Working Group members include representatives of the major accounting firms, as well as national and international accounting bodies.

By drawing on these sources, as well as on ten years of good practice in climate change-related disclosure to CDP by thousands of companies worldwide, CDSB's Framework prescribes reporting requirements that are as consistent as possible with the most common features of voluntary and mandatory climate change disclosure and with the established financial reporting model.

CDSB's work programme is managed by CDP, which acts as Secretariat to CDSB. It is responsible for advancing the CDSB Framework in association with members of the CDSB Board, Advisory Committee and Technical Working Group. For more information see www.cdsb-global.org.

Consultation Response

Introduction

The Carbon Disclosure Project (CDP) and the Climate Disclosure Standards Board (CDSB) welcome Defra's invitation to comment on the options for complying with the requirements of section 85 of the Climate Act 2008.

CDP holds the largest database of corporate climate change information in the world and has been operating for over a decade. In the UK, CDP requests information from the largest 600 listed companies on behalf of 551 investors with £71 trillion in assets under management. Whilst the response rate to CDP for the FTSE100 (94%) is encouraging, the response rate drops to 69% for the largest 350 listed UK companies and 51% for the FTSE600.

CDP and CDSB therefore support mandatory carbon reporting (in principle) by British business on the basis that it is likely to:

- Provide transparency and vital information for shareholders;
- Encourage behavioural change and carbon reduction amongst business, as measurement leads to management;
- Inform investors and markets of the likely financial impacts of climate change on business; and
- Support government objectives to manage and mitigate climate change.

CDP and CDSB believe that, whether voluntary or mandatory, reporting provisions should be practical and effective in achieving policy objectives and therefore reporting requirements must be:

- Practical for companies to implement and supported by appropriate tools and guidance, so as not to add unduly to administrative burdens;
- Developed and prepared through a process of consultation and collaboration between all relevant parties, including corporations, investors, governments, NGOs and scientists;
- Designed to meet the needs of investors (as the primary user group of information provided in annual reports) by eliciting business relevant information;
- Supported by a proportionate infrastructure in terms of compliance, assurance, verification and enforcement, to make sure companies are reporting adequately and accurately;
- Compatible with international developments in climate disclosure and reporting (such as the GHG Protocol, ISO suite, CDM methodological framework, regulatory developments and CDSB's Climate Change Reporting Framework), in order to prevent overburdening companies that operate across national borders.

In order to maximise the effect of any regulation, it should be designed specifically to satisfy clearly defined policy objectives. Once the objectives of the regulation are clear, decisions on the scope, design and details of the regulation should follow automatically. The consultation document suggests that the objectives of the regulation would be to:

1. Help reduce emissions and achieve energy and resource efficiencies;
2. Elicit clear, focused and business relevant information;
3. Reduce/minimise regulatory burdens;
4. Align with, or at least take account of, the overall government framework on corporate reporting, climate and energy.

CDP and CDSB suggest that this should include both BIS' and the Financial Reporting Council's consultations on narrative reporting, DECC's Guidance on Carbon Neutrality and DEFRA's Green Claims Guidance.

CDP and CDSB strongly support these objectives and suggest that in addition, regulations should seek to satisfy the needs of the USERS of information produced. This in turn involves identifying the user populations and their needs from the information concerned. We suggest that further work needs to be done to ascertain who will use the information produced under new provisions and for what purpose(s). Information that is intended for the business review should be business relevant to investors rather than simply serving policy objectives in order to avoid immaterial clutter appearing in annual reports. Provision could be made for other, solely policy driven information, to be reported elsewhere. This in turn requires decisions about how any regulation will deal with the definition of what represents relevant and material information.

CDP and CDSB also encourage the UK Government to consider how provisions on GHG reporting can be extended over time to include the measurement and disclosure of carbon assets, such as carbon sinks, wind farms, etc. Any new regulation should also take account of international policy arrangements on climate change-related reporting as many large companies in the UK have multinational operations.

Having established the objectives of regulation and the needs of users, a checklist of tests can then be applied to each option for compliance with the Climate Change Act section 85 in order to compare their relative merits. Based on the above objectives, the list would include the following points:

Does the option under consideration:

1. Help to reduce emissions and achieve energy and resource efficiencies;
2. Elicit clear and focused information that is practical for reporting organizations to provide;
3. Minimise regulatory burdens and costs for reporting organisations;
4. Align with the overall government framework for reporting and climate and energy policy;
5. Satisfy the needs of users of information; and
6. Align as far as possible with the relevant international policy context?

For each positive answer, a supplementary question should be asked about whether the option is likely to achieve the objectives more effectively than other options under consideration.

General Comments on the Options

The four options are presented as if they are mutually exclusive. However, CDP and CDSB think that there might be merit in considering hybrid arrangements. For example, imposing mandatory provisions on listed companies, many of which are already making relevant disclosures in their business reviews, but endorsing enhanced voluntary reporting for others in preparation for the extension of mandatory provisions to all companies within a defined period. In other words, we believe that mandatory reporting should be phased in starting with listed companies first and then bringing more companies into the scope of the regulations over time.

Through CDP's experience of developing climate change-related disclosure practices for a decade, we are conscious of the complexities involved, but also the rapid progress that is being made to deal with those complexities. We would recommend that legislation is not so over-prescriptive as to impede the solutions that emerge as companies build their capacity to provide high quality climate change-related information. Elements of the French Government's Grenelle II Law are being phased in following periods of experimentation. CDP and CDSB think that a similar model is worth considering for some companies or some aspects of reporting in the UK and that mandatory reporting should be phased in over a pre-determined timeframe. We acknowledge that organizations are anxious for certainty about reporting requirements, but we think that a clearly defined plan and timescales will provide the certainty that companies seek.

CDP and CDSB believe that there are certain technical and practical issues that need to be addressed before mandatory carbon reporting can be made to work well. We encourage Defra to review a list of these issues in CDSB's Development Plan and soon to be published report on the state of international climate change-related reporting. Please consult CDSB's website at www.cdsb-global.org.

Responses to Consultation Questions

1. Do you support Option 1 (Enhanced Voluntary Reporting)

Only as an interim measure – as part of a phased approach described in this consultation response. CDP and CDSB support the continuation of voluntary reporting with enhanced features for some UK companies for a defined period designed to support a smooth transition to mandatory reporting. Not all UK companies have the resource, infrastructure, staff or expertise to prepare carbon reports to the level of detail and accuracy likely to be required by legislation. We suggest that enhanced voluntary reporting for companies other than listed companies should continue for a defined period of three to five years to build capacity and test various methodologies and approaches against policy objectives and for practicability. CDP's annual process should not simply be regarded as a voluntary reporting mechanism. It is also capable of being used for compliance with regulatory requirements as the underlying system is adaptable to cater for various levels of rigour and detail. We would welcome a discussion on how CDP's annual process could be used to support the transition from voluntary to mandatory reporting using an approach that is already familiar to and used by many companies.

2. Which ideas (outlined in option 1) for increasing the number of companies reporting on a non-regulatory basis would you prefer?

We support options b and c for enhancing voluntary reporting. Support for CDP and other non-governmental organizations has various merits, including:

- Many reporting organizations and users of information are already familiar with the CDP and GRI processes;
- CDP and GRI have an established procedure for aligning reporting indicators;
- We expect that, in terms of content, the information requirements in regulations would not differ significantly from those specified by CDP and GRI;
- CDP's electronic reporting system can be used to track and compare results and performance and to feed data into other data systems.

We also refer you to CDSB's Climate Change Reporting Framework Edition 1.0, which has been developed with a range of stakeholders to define an approach to climate change-related reporting that takes into account many relevant principles from existing regulatory and non-regulatory reporting practices.

We agree that, with support from UK Government, certain enhancements could be made to CDP, GRI and similar processes to improve further the quantity and quality of information. Enhancements could include the following and should inform the transition to mandatory reporting to a wider population over time:

- Support for the development of interactive data standards for the efficient disclosure, analysis and exchange of information;
- Pending consensus on standard, consistent approaches to climate change disclosure, methods of eliciting greater transparency about policy choices made by reporting organizations could assist the users of information. We suggest an approach along the lines of paragraph 2.24 of CDSB's Climate Change Reporting Framework Edition 1.0.
- Guidance on what type of information is useful along the lines of paragraph 2.38 of CDSB's Climate Change Reporting Framework Edition 1.0. and similar guidance by CDP and the GRI.

3. Should corporate reporting of GHG emissions be made mandatory for some companies? If so, please explain.

Yes. CDP and CDSB believe that in the first instance, reporting should be mandatory for listed companies on the basis that they are already required to include environmental information in their business review and should be broadly familiar with what is involved. We suggest then phasing in mandatory requirements for large private companies, carbon intensive companies and high energy users over a pre-determined timeframe using voluntary reporting mechanisms to build capacity during the phasing period.

We acknowledge that organizations are anxious for certainty about reporting requirements, but we think that a clearly defined plan and timescales will provide the certainty that companies seek.

4. If mandatory reporting is introduced, which would be your preferred option? 2, 3 or 4?

We support all options 2, 3 and 4 being phased in over a pre-determined timeframe. This should apply to listed companies in the first instance, then large private companies and then high energy users.

6. Do you agree that a company should specify which approach it is using to set its organizational boundary?

Yes, we consider this to be vital contextual information. The way in which a reporting organization determines the boundaries of its organization for GHG emissions reporting purposes is important for numerous reasons including transparency, comparability and

benchmarking. A theme that runs throughout research on effective GHG reporting relates to the way in which financial accounting and GHG accounting respectively distinguish between results over which a reporting organization has control (whether financial or operational) and results over which it has influence. Further research into and definition of the terms “control” and “influence”, taking into account developments in international financial reporting should be undertaken before decisions are made.

In their report for the European Union on GHG emissions reporting schemes, ERM notes that “*current guidance on setting of reporting boundaries...is typically open to a wide degree of interpretation by the user...*” For this reason, we believe that a single approach to organizational boundary setting should eventually be specified for all reporting organizations. However, in the meantime we contend that the organizational boundary used for reporting should be disclosed.

7. Do you agree that a company should (where possible), report on all their emissions within the chosen organizational boundary, including those that occur in their operations overseas? If you don't agree, can you explain which emissions you think a company should report?

CDP and CDSB agree that a company should report on all their emissions within the chosen organizational boundary IF the objective of regulations is to collect information about the GHG emissions of organizations rather than information about the GHG emissions that arise from facilities and activities conducted within a particular geography. In order to answer this question, decisions need to be made about the purpose of regulation/enhanced voluntary provisions and the needs of the users of information. If the purpose is to provide information for markets and investors, we believe that the footprint of the whole organization is relevant, including UK and overseas operations, because investors and markets view companies as a single entity, rather than one divided by national borders. However, we also think that the presentation of information needs to be sufficiently segmented to aid understanding so that users can discern geographical and other trends. Even if the purpose of regulation is to gather information about emissions specifically attributable to UK activities in order to track progress against UK targets, we think that it is equally relevant to include GHG emissions from overseas sources where they arise because of the purchasing, manufacturing, business or outsourcing decisions of UK businesses and their partners. Climate change is a global problem that transcends national borders. Naturally, companies will have varying degrees of access to information from overseas operations, which might make full compliance with some requirements difficult. CDP and CDSB therefore recommend that Defra contemplates the relative merits of a “comply or explain” approach for information about GHG emissions from non-UK sources.

8. Do you agree that, if it isn't possible for a company to report on all emissions within their organizational boundary (because of data problems, etc), then a company should clearly state the extent to which it has been able to report?

Yes. CDP and CDSB would suggest an approach similar to paragraphs 2.22, 2.23 and 3.17 – 3.19 of CDSB's Climate Change Reporting Framework Edition 1.0. We also refer Defra to GRI's G3 Guidelines which recognize that different relationships involve differing degrees of access to information and ability to affect outcomes. As we understand it, GRI distinguishes between entities over which the organization exercises control and those over which it has influence. We suggest that accurate, quantitative, verifiable information should be required from the former but that narrative disclosures and supporting statements (along the lines of the requirements from CDSB's Climate Change Reporting Framework – see above) might suffice in the latter case.

9. Do you agree that companies should be required to measure and calculate emissions from the six GHGs covered by the Kyoto Protocol?

Yes, in principle, BUT provided that they are relevant and material for the organization concerned. Where it would be unduly costly or impractical for a company to report on certain gases, we suggest that Defra considers publishing proxy data that allows companies to make estimates based on a standard approach that can be developed and refined over time.

10. Do you agree that companies should be required to measure or calculate and report on all their scope 1 and 2 emissions? If not, which emissions do you think a company should measure, calculate and report and why?

In principle, yes. All scope 1 and 2 emissions should be measured or calculated and reported as a minimum requirement under regulations. However, as noted above, we believe that any mandatory requirements should be accompanied by guidance, tools and materials that make it possible for companies to comply without imposing unreasonable costs or administrative burdens.

11. Do you think that companies should be required to measure and report on any of their scope 3 emissions?

Yes, but only under enhanced voluntary reporting in the first instance pending publication, testing and refinement of the WRI's Scope 3 GHG Protocol. However, in line with paragraph 4.27 of CDSB's Climate Change Reporting Framework Edition 1.0, we recommend that information (narrative or quantitative) should be disclosed in the directors' report where the emissions expose the company to risks, opportunities or financial impacts.

12. Do you agree that companies should specify in their directors' reports the company's total annual amount of GHG emissions in CO₂-e broken down by direct emissions and indirect energy?

Yes, but subject to all of the comments above about phasing in, boundary setting, provision of tools to minimize burdens and costs, etc.

13. Do you agree that companies should specify an intensity ratio?

Eventually yes in order to advance comparability. However, we believe that further research, including user engagement, needs to be conducted to establish which are the most appropriate intensity ratios to be used by different sectors.

14. Should companies specify a base year when they report their annual emissions?

Yes. However, Defra will need to publish guidelines or regulations on the circumstances in which the base year may be amended for the purposes of tracking performance.

15. Is there any other information which you think a company should report?

Yes. Some contextual narrative will be essential to help users of information understand GHG emissions results. CDP and CDSB recommend that Defra reviews the GRI climate indicators, the CDP information request and CDSB's Climate Change Reporting Framework to determine which other information is necessary to satisfy Defra's objectives and the needs of information users. We suggest at the very least that companies should report the type of contextual information listed in paragraphs 4.31 – 4.33 of CDSB's Climate Change Reporting Framework Edition 1.0. but that Defra should also consider the inclusion of the other requirements set out in Chapter 4.

16. If reporting is made mandatory, should companies be obliged to seek some kind of assurance or verification on their emission report? If not, could you explain your thinking?

CDP and CDSB agree that ideally independent third party assurance or verification should be obtained by companies as part of the mandatory reporting process. However, again, we believe that such requirements should be phased in and that Defra should consult with other regulators, such as those overseeing GHG reporting rules specified by the EPA in the USA, the NGER rules in Australia and the Greenhouse Gas Reporting Scheme in Alberta to ensure consistency to the extent possible and that any lessons those regulators have learned through experience is taken advantage of in the UK.

We encourage Defra to reconsider the views expressed in the CBI's report "All Together Now", which warn against mandatory verification or assurance pending further research into the costs and other implications. Furthermore, we cannot foresee how mandatory assurance or verification could be made to work in the absence of equivalence in standards (including standards related to engagement performance, quality control, competence and ethics) that are applicable to a wide range of providers conducting assurance activities. We encourage Defra to liaise with the IAASB in their development of ISAE 3410 before making a decision on verification/assurance.

Comments on regulatory impact assessment

CDP and CDSB encourage Defra to examine regulatory impact statements made by Government Departments in Australia and the USA responsible for the introduction of the National Greenhouse and Energy Reporting Act and the GHG Mandatory Reporting Rule respectively.

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