Nelson Design Services

31st October 2009

CDSB Secretariat
The Carbon Disclosure Project
40 Bowling Green Lane
London
EC1R 0NE
UK

**Ref: CDSB Reporting Framework – Exposure Draft**

Dear Sir/Madam

Please find attached some comments on the Exposure Draft that I hope will be of interest. This response has been developed from material originally posted to the web earlier this summer and which can be located here: http://petrolog.typepad.com/climate_change/2009/07/corporate-reporting-of-ghg-emissions.html.

I believe there is still a way to go before companies will be willing to present details of their carbon emissions in annual reports. I therefore applaud the CDSB's initiative to develop a reporting methodology and hope you will be arranging some follow-up meetings so that interested parties can learn more about the results of your current work and make future contributions.

Yours faithfully,

Robin Huttenbach, CEng, MIChemE
Director

robin.huttenbach@gmail.com

## Introductory questions

***1. Do you agree that a single global framework for climate change-related disclosure in mainstream reports is necessary and/or possible, notwithstanding the background of different national developments? If not, please explain why.***

This is a difficult question to answer. For now I would encourage groups to develop a range of methods and to then see which one(s) prove to be the most practical and reliable in use.

***2. Do you agree with CDSB's overall approach of aligning its Guiding Principles to existing relevant principles and objectives of financial reporting so as to elicit information of value primarily for investors? If not, please explain why and share with us your ideas for a new/different approach to climate change-related reporting.***

Alignment with existing principles is a desirable approach, but one that will inevitably restrict innovative thinking. See for example the IASB's position on Management Commentary http://www.iasb.org/Current+Projects/IASB+Projects/Management+Commentary/Management+Commentary.htm where some members of the drafting team considered commentary to be non-authoritative and not able to satisfy a requirement of neutrality. The IASB therefore does not propose to develop a standard, whereas the CDSB is working to produce some standard form of management commentary to help investors assess the risks climate change poses to the operation of a business. Please also see the entry on David Phillips corporate reporting blog http://pwc.blogs.com/corporatereporting/2009/08/management-commentary-reading-between-the-lines.html for alerting me to this point.

I believe the difficulty of aligning with existing principles arises from the fact that we have an accounting model (double entry, ledgers, balance sheet and profit and loss) that has served the developed and developing nations well over the last two hundred years, but in a World that did not need to account for the consumption of natural

resources. We are beginning to notice deficiencies in the model, but efforts by groups such as the CDSB and the GHG Protocol to address the reporting of emissions can only go so far without a change to the way financial performance is recorded. The difficulty of embarking on such a change is compounded by the fact that the accounting profession has just spent the last 15 years or so preparing a new set of international standards.

***3. At the current stage in its development, the CDSB Reporting Framework, including the Reporting Templates, are designed for general use by all companies within the stated scope of applicability. Do you agree that further work is required to develop the Reporting Framework, including the Reporting Templates, to take account of particular sector-specific issues related to climate change? If so, please provide your recommendations, referring to particular sector specific climate change-related initiatives if possible.***

I believe a fifth (and perhaps a sixth) template is required. These are outlined in my responses to Questions 4 and 6 and include:

- Return on Embodied Carbon Dioxide Employed (**ROCO2eE**), and
- A metric to quantify the degree of uncertainty associated with the amounts of carbon emissions an organization reports.

**Characterizing decision-useful information**

***4. Do you agree with the principles and characteristics of decision-useful information that CDSB recommends for making judgments on the information to be disclosed under CDSB's Reporting Framework? If not, what additional principles or characteristics are required, or which ones suggested in the Framework would you change?***

I think Sections 6.8 – 6.43 are too conceptual, long-winded and vague to be of much use. I would suggest that this part of the Exposure Guide be re-written to include some commentary on the need to risk assess reported emissions (particularly if any Scope 3 emissions are to be included) so that investors can understand the uncertainty / level of confidence a company has in the numbers it is reporting.

For example studies by Carnegie Mellon's Green Design Institute (GDI) on carbon footprinting: http://gdi.ce.cmu.edu/gd/Research/GDI-carbon-footprinting-onepager.pdf suggests that Tier 1 (direct) emissions from US industries constituted on average only 14% of total supply chain GHG emissions. Tier 1 + 2 (direct and indirect purchased power) emissions represented on average only 26% of the total.

Although details of which industries they studied have to be clarified, such values would serve to indicate just how large Tier 3 (other indirect) emissions may be and how much uncertainty could be associated with attempts to produce figures for management statements. This is not to say, that figures should not be published, but they should include a clear statement of confidence levels.

***5. Do you agree that the CDSB characteristics of decision-useful information are practical for companies to apply and sufficient to limit the amount of information disclosed to the most relevant content for users? If not, what additional guidance or information do you suggest CDSB include?***

No – see reply to Question 4.

**Content**

***6. Do you agree with the content that CDSB recommends for potential inclusion in disclosures under the CDSB Reporting Framework? If not, what additional areas would you recommend or which types of information in the Reporting Templates would you change?***

The four templates currently proposed cover operating emissions, but no estimate of the life cycle emissions / embodied energy content of the assets that a company would employ to run its business or how these might ultimately relate to their balance sheet and profitability.

It is therefore suggested that the CDSB develop a fifth template that would allow the magnitude of a company's profitability to be compared with its competitors or other market sectors in terms of the GHG emissions intensity of its operations (emissions + assets) with values typically expressed in terms of kilotonnes $CO_2e$ / $ output. Alternatively one could use the reciprocal performance metric: Return on Embodied

Carbon Employed (**ROCO2eE**) whose units could be expressed in $ / kilotonnes CO2e – this would be an equivalent to the more conventional return on capital employed (**ROCE**) and similar to the concept of Energy Return on Investment (**EROI**).

Estimating such values would not be a simple task in early years, particularly for businesses that are capital intensive and where the organizational boundaries of their Scope 3 emissions are open to interpretation.

***7. Does one or more of the jurisdictions in which you operate already have requirements for any of the content in the Reporting Templates to be disclosed according to local rules? If yes, are the requirements consistent with the proposed CDSB Framework including the Reporting Templates? If they are not consistent, what are the major areas of conflict or difference?***

No comments to make.

***8. CDSB's proposed Reporting Framework requires companies to define and explain the performance measures and indicators they use to track and demonstrate their progress in responding to climate change. CDSB considers performance measures and indicators to be crucial elements of decision-useful information as they aid understanding and comparability over time, provided that consistent metrics are used year on year. Do you foresee particular challenges in setting and explaining performance measures and indicators, and using those metric on a consistent basis over time? If so, please explain those challenges.***

The main challenge is to avoid turning the reporting of metrics into another box ticking exercise. I would say there is a high risk this will happen and that the only long term solution is to embed these reporting requirements into the financial reports themselves. This however (see also response to Question 2) would require a major review / rewrite of international financial reporting standards which is outside the scope of the CDSB's work.

## Practicalities

***9. How do you anticipate information for compliance with the CDSB Reporting Framework will be collected in your organization? If possible, please state whether in-house or proprietary software is likely to be used, which departments would be involved in the collection and review of information, and how long the annual information collection process is likely to take.***

European methods for collecting emissions data commonly rely on manual techniques and commonly are not to a fiscal standard. Auditing of figures from the previous year must be completed by April each year, so values accompanying annual accounts may be out of sync with financial reporting periods. This shortfall in available data can only be improved will if the EU imposes a requirement on companies to record emissions electronically and in real time.

The situation in the US should be better because the EPA's mandatory reporting system that begins in January 2010 requires electronic filing.

***10. What practical issues do you envisage when disclosing under the CDSB Reporting Framework? For example, constraints on the length of the mainstream report or particular requirements applicable in the jurisdiction in which you operate. What could CDSB do to limit any practical difficulties associated with reporting under the CDSB Reporting Framework?***

No comment.

***11. Is there anything else of relevance you would like to raise?***

**Clarifying the Reporting of Scope 3 emissions**

The Exposure Draft is unclear as to whether Scope 3 emissions should be reported, though the Appendix does include details of such emissions.

The Basis for Conclusions document explains the situation in respect to the reporting of Scope 3 emissions well – see in particular, Section 1.28. It is therefore suggested that some of this material be incorporated into the Exposure Draft.

## Reporting GHG emissions in Law

Further clarification should be sought as to whether there is a requirement in law for companies to provide details of GHG emissions with annual accounts. Financial accounts commonly only have to consider Scope 1 emissions, whereas cost accounting reports may be used to document Scope 1 and 2 emissions. Disclosure of Scope 3 emissions remains an issue that may have to wait resolution until the GHG Protocol issues new guidelines on product and supply chain accounting in 2010.

It is noted that reporting of GHG emissions may bring with it an increased likelihood of climate change litigation. This may substantially reduce the take up of a CDSB Reporting Framework.

## Section 6.5

The advocates of sustainability reporting would take exception to the suggestion that managing the impact of climate change related issues should help a company increase sales and lower its costs. More appropriately, companies should be seeking to reduce the carbon dioxide and equivalent GHG intensity of their operations.

## Minor Corrections

Title and descriptions of templates in Sections 2.2, 9.1 and 9.2 of draft should align with one another

Page 35 of draft: $N_20$ should be written $N_2O$ (O not zero)