# 'Reforming the business energy efficiency tax landscape'

## A consultation response by CDP, the Institutional Investors Group on Climate Change (IIGCC) and the UK Sustainable Investment and Finance Association (UKSIF).

**About the respondents**

CDP (formerly known as the Carbon Disclosure Project) is a UK-based global NGO which operates an annual corporate environmental disclosure program on behalf of 822 institutional investors with assets of $95 trillion. More than 5,000 of the world's largest listed companies disclose climate information through CDP, including 232 of the FTSE350 in 2015. www.cdp.net

The Institutional Investors Group on Climate Change (IIGCC) represents more than 118 pension funds, insurance companies and fund managers, who collectively have €12 trillion of assets under management. IIGCC encourages public policies, investment practices, and corporate behaviour that address long-term investment risks and opportunities associated with climate change and support the move to a low carbon economy. www.iigcc.org

The UK Sustainable Investment and Finance Association (UKSIF) is the membership association for sustainable and responsible financial services. It promotes responsible investment and other forms of finance that support sustainable economic development, enhance quality of life and safeguard the environment. UKSIF has approximately 240 members and affiliates including pension funds, asset managers, research providers, financial advisers, banks and non-governmental organisations. www.uksif.org

**Overarching Points**

In this consultation response we have responded to the government's questions 1 to 5 in the way that they have been framed. The following three points summarise the key issues that we are seeking to communicate in our response.

1. As groups representing investors and their role in the fight against climate change we want companies to reduce emissions and investors to fund the transition to a low-carbon economy.

2. Mandatory carbon reporting is the only policy initiative out of the EU ETS, CRC, CCL, and ESOS that provides a lens through which investors can view the entire company and adjust their investment portfolios accordingly.

3. As a global financial centre, UK leadership on this issue is particularly important.

**Question 1. Do you agree with the principle of moving away from the current system of overlapping policies towards a system where a single business/organisation faces one tax and one reporting scheme? Please provide evidence on level and types of benefits of an approach like this.**

**Answer to Question 1**

Simplification

We fully agree that is sensible for the government to try to simplify the current system of overlapping policies which has developed over a number of years under successive governments, in order to send clear policy signals on the government’s expectations of companies.

Measurement and Reporting

We do not agree that there should be a single reporting scheme as proposed by the government. Although there are clear arguments that previously there may have been too many individual reporting requirements, and although it may well be possible to beneficially reduce the number of requirements, it does not necessarily follow that all user needs can be met by reducing the number of requirements from many to one. Companies report information to different stakeholders for a wide range of purposes and we feel that this diversity of function has not been fully recognised by the review, especially as regards investors. This is discussed further in our answer to Question 4 (and our answer to Question 2 also contains relevant material).

It is perhaps worth noting at this point that ESOS deals with the measurement and management of UK energy use and applies to a wide range of companies of all sizes, whereas the UK Mandatory GHG Reporting requirement deals with the reporting of global GHG emissions and applies to ‘quoted companies’ listed on the UK’s main markets. Both require the creation of data about a company’s use of energy, but they have different boundaries, purposes and users.

However, we are fully in agreement with what we believe is actually the underlying principle of the government’s idea of a single reporting scheme, which is that there should be a single methodology through which companies gather and aggregate consistent and comparable information about their energy use and purchases, and then a single set of emissions factors[1] for converting data about UK energy use into GHG emissions. We recommend that this methodology is based on the internationally accepted and widely use Greenhouse Gas Protocol[2]. It is this work of measurement and accounting, rather than the act of reporting, which requires the majority of the resource from companies in relation to regulatory requirements.

We would like to see a situation where this work can be done once in confidence by companies, with the resulting data fit for use by companies when reporting energy and emissions data in a variety of ways to different stakeholders as required. The analogy to this

[1] Variables used to estimate the GHG emissions when they are not directly measured.
[2] World Business Council for Sustainable Development, and World Resources Institute. 2004. ‘GHG Protocol Corporate Accounting and Reporting Standard - Revised Edition’: http://www.ghgprotocol.org/standards/corporate-standard.

in the world of financial reporting would be the consistency of data produced across a business under International Financial Reporting Standards.

As a result of this review the government now has an opportunity to review the guidance given to companies on how to measure energy use and calculate GHG emissions across different policy instruments (including all those mentioned in the consultation document) and to ensure that the methodologies are consistent so that companies can report against different requirements using the same underlying accounting framework. This could have a significant impact in reducing administrative and compliance costs – one of the objectives of the government review – as well as increasing the extent to which consistent and comparable data is available to investors and other data users. Some investors have stated a desire for this government guidance to take a sector-specific approach, given that emissions sources and profiles differ greatly across industrial sectors.

Pricing

One of the objectives of this review is “consistency with fiscal consolidation plans”, which we take to mean that the UK government’s income through taxation must not be reduced as a result of any reforms. This is a helpful practical steer, however it is not a complete guide as the review does not clearly set out what is to be taxed and why. Specifically it does not explain whether the government’s intent is to create an energy tax or a carbon tax and whether the desired outcome is to reduce energy use or to reduce GHG emissions – the review’s proposals appear to aim at both, but the details of policy design are important here and it cannot always be assumed that energy efficiency will lead to emissions reductions, or that carbon pricing will lead to reduced energy use.

It would be helpful if the government could acknowledge this tension and be clear as to whether the envisaged ‘single tax’ will be a carbon tax, which is something that we would strongly support. If, on the other hand, the tax is to be an energy tax it is important to ensure that it is ‘carbon smart’ and helps to achieve the UK’s climate policy objectives to the maximum extent possible.

The UK government has long held the position that the EU ETS should be the primary carbon pricing mechanism for the UK, and the current view does not propose any change to how the EU ETS operates in the UK. We do not propose any such change, however it is important to recognise that currently companies receive multiple carbon price signals through EU ETS, CRC and CCL which are complicated by exemptions such as those provided by CCAs. We believe that this situation requires rationalisation in order to create effective UK carbon pricing that will drive behaviour change.

Given the range of options available to the government based on the current policy landscape, making the CCL the UK’s main domestic carbon pricing mechanism (after EU ETS) seems a sensible suggestion and one which will offer a welcome simplicity to companies. We note however that explicitly framing CCL as a carbon tax will require an in-depth review of CCL tariffs which goes beyond Question 9 in this consultation about gas and electricity, and should include further consideration of CCL’s interaction with EU ETS to encourage overall carbon price convergence, and its applicability to renewable energy.

**Question 2. Do you agree that mandatory reporting should remain as an important element of the landscape in driving the uptake of low carbon and energy efficiency measures? If not, why not?**

**Answer to Question 2**

<u>The purpose of the existing mandatory reporting requirement: investor use of data</u>

The benefits of corporate GHG accounting for external audiences as well as for the audience within the company (which schemes like ESOS address) was reiterated in the run-up to the introduction to mandatory reporting:

- The call of investors for more companies to report and for those reports to be more comparable is laid out in (Department for Environment, Food and Rural Affairs 2010, sec. 4.2[3]). This document reviewed the outcomes of corporate GHG emissions reporting including investor use of the data.

- The investors’ role in transitioning to a sustainable economy is detailed in the regulatory impact assessment into options for increasing corporate carbon reporting (Department for Environment, Food and Rural Affairs 2011[4]). In section 6.11 investors explain how they would use the data.

Investor use of the data was a key message from the UK government when it announced mandatory reporting at Rio+20 Earth Summit. The media release said “The UK is the first country to make it compulsory for companies to include emissions data for their entire organisation in their annual reports. The introduction of the reports, following consultations with leading businesses, will enable investors to see which companies are effectively managing the hidden long-term costs of greenhouse gas emissions.” (Department for Environment, Food and Rural Affairs, UK 2012[5]).

Therefore while we support simplifying the overlapping regulations that may apply to companies, the unique feature of mandatory reporting – that it applies to the entity into which investment is made - must not be lost.

<u>The value of the existing mandatory reporting requirement</u>

We agree that mandatory reporting should remain as an important element on the landscape.

CDP and many other actors were supportive of the introduction of The Companies Act 2006 (Strategic Report and Directors’ Report) Regulations 2013, often described as ‘Mandatory GHG Reporting’. During the consultation period and evidence-gathering period that led up to

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[3] 2010. ‘The Contribution That Reporting of Greenhouse Gas Emissions Makes to the UK Meeting Its Climate Change Objectives - A Review of the Current Evidence’. Department for Environment, Food and Rural Affairs:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/69262/pb13449-corporate-reporting-101130.pdf
[4] 2011. ‘Impact Assessment of Options for Company GHG Reporting’. Regulatory Impact Assessment. Department for Environment, Food and Rural Affairs.
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/82354/20120620-ghg-consult-final-ia.pdf
[5] Department for Environment, Food and Rural Affairs, UK. 2012. ‘Leading Businesses to Disclose Greenhouse Gas Emissions’. Defra News. June 20. https://www.gov.uk/government/news/leading-businesses-to-disclose-greenhouse-gas-emissions

the regulation’s introduction a great deal of evidence was submitted by us and others which showed that mandatory reporting would act as a driver for the uptake of low carbon and energy efficiency measures. While space does not permit us to summarise all of that evidence here, we refer you to Defra’s extensive Evidence Summary published in 2010[6]. As a briefer point of reference we also refer you to the text of the UK government’s press release[7] on the announcement of UK Mandatory GHG Reporting in June 2012:

*“The decision follows the consideration of extensive evidence and the detailed analysis of consultation responses to gain the views of businesses and individuals, the majority of which opted for a mandatory reporting approach.*

*Businesses said a compulsory approach would:*

*•Provide the first step in enabling companies to manage and reduce emissions;*

*•Mean more transparency from companies;*

*•Provide a single consistent standard; and*

*•Provide information to the business that could save them money through reduced energy costs.”*

<u>The rationale for making reporting mandatory</u>

Voluntary GHG reporting is extremely widespread among large UK companies. Therefore we were asked in the run-up to introduction of the current UK requirement, and have again been asked during this consultation, whether it is necessary to have mandatory reporting at all.

Some of these arguments for mandatory reporting are already made in the quote from the government’s own press release cited above, in addition we feel it may be helpful to state our own key arguments on this point which are:

1. Corporate GHG reporting provides useful information and stimulates energy savings and emissions reduction activities through catalysing measurement and management. However not all companies choose to report voluntarily, meaning that potential benefits from this activity are not captured across the economy. Mandatory reporting captures these benefits universally and enables systematic use of emissions data in investment decisions.

2. Mandatory reporting provides a mechanism for setting and enforcing one consistent set of rules for how energy and emissions should be measured and accounted for. In a scenario where reporting is purely voluntary a wide variety of methodologies are used and the resulting data is not always comparable or useful. Mandatory reporting brings order and simplicity to this fragmented landscape.

3. Mandatory reporting requirements send a signal to the market that something is important. Removal of an existing requirement could send a signal to the marketplace that the matter in question is no longer considered to be important. This could be taken as a signal that the UK private sector is not seriously expected to transition to a low carbon economy.

[6] See footnote 2

[7] See footnote 4

4. The UK Mandatory GHG Requirement deals with the inclusion of global climate change information in annual reports. The regulation is differentiated from other UK policy measures that deal with energy and emissions in two important ways (the global scope of the emissions to be reported, and the inclusion of this data in the annual report) which relate to UK policy processes and goals that have to date been outside the scope of the Business Energy Efficiency Taxation review. We will discuss these issues further in our answer to Question 5, but we note here that these ‘out-of-scope’ policy considerations add further arguments for maintaining GHG reporting in annual reports.

<u>The key characteristics which we would like to see retained in Mandatory GHG Reporting</u>

We are strongly in favour of maintaining the key features of the existing UK GHG Mandatory Reporting requirement under the Companies Act. At this point we will set out what we consider those key features to be. They are:

1. Reporting is mandatory;
2. Reporting is annual;
3. Reports are made in annual filings to Companies House;
4. GHGs are reported, together with relevant contextual information including methodology, base year, the previous year’s emissions, a relevant intensity metric, etc;
5. Global activity (not only UK activity) is reported;
6. The reporting period should be the same as for financial reporting, or companies should explain why this has not been possible;
7. The reporting boundary should be stated;
8. Companies should state whether verification or assurance have been conducted on reported data.

We believe that some improvements could be made to the existing requirements for reporting GHG data in annual reports, based on what has been learned from implementation of the regulation so far together with the evolution of best practice and the requirements of new EU legislation. For example we believe it will important to further align GHG reporting with corporate reporting of risk and strategy as firms prepare themselves for the transition to a low carbon economy.

We will be providing further detail on this point in our response to the government’s forthcoming consultation on the UK’s transposition of the EU Non-Financial Reporting Directive. As regards the reporting of GHG emissions specifically we have provided some suggestions in the following section.

<u>Enhancing the effectiveness of mandatory corporate carbon reporting</u>

One of the benefits of regulation is the introduction of consistency and hence comparability. There is considerable convergence on the use of the GHG Protocol’s *Corporate Standard*[8] or one of many aligned methodologies such as ISO 14064-1 (International Organization for

[8] See footnote 1

Standardization 2013[9]) (World Resources Institute 2013[10]) within voluntary reporting. In climate disclosures made by FTSE 350 companies via CDP in 2015, the *Corporate Standard* was the most commonly cited methodology (37% of 232 disclosing companies[11]) followed by DEFRA's "*Guidance for businesses on measuring and reporting their greenhouse gas emissions*[12]" (31% of 232 disclosing companies) which directs UK companies towards the *Corporate Standard* or methodologies based upon it. However, these are accounting and reporting frameworks allowing considerable flexibility for the practice of carbon reporting to evolve.

Sources of incomparability are *inter alia* the use of different measurement techniques, estimation formulae and GHG emission factors. Although emissions factors are provided by the GHG Protocol, an organisation does not have to use them to legitimately state that the *Corporate Standard* methodology has been applied (GHG Protocol 2012[13]). As for Global Warming Potentials (GWPs)[14], it was not until 2012 that the GHG Protocol began to steer organisations towards a particular set of GWPs (Ecometrica 2012[15]) (GHG Protocol 2015[16]). Both the *Corporate Standard* and ISO 14064-1:2006 allow companies three options in drawing a boundary around the organisation whose emissions are going to be reported: emissions from entities over which the company has financial control; emissions from entities over which the company has operational control; and the third approach - equity share - proportional emissions from entities according to the percentage of economic interest that a company has in them. At the extreme end of the spectrum, this flexibility in boundary choice can result in emission figures that differ by as much as 73% (unpublished research by A. Smith 2015). Defra's 2010 Evidence Summary cites an OECD report published in 2010 *Transition to a low-carbon economy: public goals and corporate practices* that found that the lack of prescription in the GHG Protocol's *Corporate Standard* would not lead to fully comparable reporting.

In the initial stages of Parliamentary debate over UK mandatory reporting, one aim was to inject standardisation into what was already a common practice among the larger UK

[9] International Organization for Standardization. 2013. 'ISO 14064-1:2006 - Greenhouse Gases -- Part 1: Specification with Guidance at the Organization Level for Quantification and Reporting of Greenhouse Gas Emissions and Removals'. Accessed April 4. http://www.iso.org/iso/catalogue_detail?csnumber=38381.

[10] World Resources Institute. 2013. 'ISO, WRI, and WBCSD Announce Cooperation on Greenhouse Gas Accounting and Verification | World Resources Institute'. Accessed April 4. http://www.wri.org/press/2007/12/iso-wri-and-wbcsd-announce-cooperation-greenhouse-gas-accounting-and-verification.

[11] Source: 2015 disclosures via CDP by FTSE 350 companies, see cdp.net or contact CDP for more information

[12] https://www.gov.uk/guidance/measuring-and-reporting-environmental-impacts-guidance-for-businesses

[13] GHG Protocol. 2012. 'FAQ | Greenhouse Gas Protocol'. http://www.ghgprotocol.org/calculation-tools/faq#calculation

[14] As there are a number of GHGs, their radiative forcing effects are often expressed relative to the radiative forcing of one unit of carbon dioxide ($CO_2$ equivalent or $CO_2e$) using GWPs. GWPs have been amended over time and are expressed over different time frames.

[15] Ecometrica. 2012. 'Greenhouse Gas Protocol Update Would Provide Guidance on GWPs'. August 21. http://ecometrica.com/article/greenhouse-gas-protocol-update-would-provide-guidance-on-gwps.

[16] 2015. 'Global Warming Potential Values'. Accessed August 7. http://www.ghgprotocol.org/files/ghgp/tools/Global-Warming-Potential-Values.pdf.

companies[17]. Support for this outcome continued to be expressed as the government reviewed whether to regulate reporting or not [18] (Department for Environment, Food and Rural Affairs 2009, para. 8[19]), (Department for Environment, Food and Rural Affairs 2010, para. 84[20]). The regulatory impact assessment[21] emphasised the call for comparable information from the Confederation of British Industry and others (section 4.5).

In the event though the regulations are not prescriptive and in consequence the benefits of comparability are not being fully realised. This review of the mandatory reporting regulations is an opportunity to address this at least in part, particularly the boundary issue.

Another methodology question remains open that relates to accounting for emissions associated with electricity consumption. This is covered in Defra's voluntary reporting guidelines. There has been a major international review among GHG practitioners on how to do this (Sotos 2015[22]). Defra undertook a consultation on the same issue, but a conclusion is still outstanding[23]. We believe that this work is relevant to Question 9 of the current consultation; while we have not been able to provide a response to that question within the consultation timeframe we will be happy to follow up on this issue separately with HMT, DECC, BIS or DEFRA.

We will be making these and related points in our response to the forthcoming government consultation on the UK's plans for transposition of the EU Non-Financial Reporting Directive.

**Question 3. Should such reports require board level sign-off and should reported data be made publicly available? Please give your reasons.**

**Answer to Question 3**

<u>Response to question 3 in relation to the existing GHG reporting requirement</u>

We are strongly in favour of maintaining the key features of the existing UK GHG Mandatory Reporting requirement under the Companies Act. Given that in our view one of these key features is inclusion of entity-wide GHG information in annual reports our answer to this question is yes.

In the context of putting entity-wide GHG information into annual reports, the reasons for board level sign-off and public reporting are as follows:

- Annual reports should contain information that is material, relevant and useful for investors and other stakeholders. In the case of the vast majority of companies data

[17] 'Climate Change Bill House of Lords Debates, 30 January 2008, c732'. *TheyWorkForYou*. January 30. http://www.theyworkforyou.com/lords/?id=2008-01-30b.656.0#g732.3.
[18] Department for Environment, Food and Rural Affairs. 2009. 'Impact Assessment of Guidance on Measurement and Reporting on Greenhouse Gas Emissions'. Department for Environment, Food and Rural Affairs.
[19] Department for Environment, Food and Rural Affairs. 2009. 'Impact Assessment of Guidance on Measurement and Reporting on Greenhouse Gas Emissions'. Department for Environment, Food and Rural Affairs.
[20] See footnote 3
[21] See footnote 4
[22] Sotos, Mary. 2015. 'GHG Protocol Scope 2 Guidance Executive Summary - An Amendment to the GHG Protocol Corporate Standard'. World Resources Institute.
[23] https://consult.defra.gov.uk/climate-change/ac04ad33

fitting this description will encompass environmental matters, including GHG emissions.
- Under UK company law, annual reports must be made publicly available and must be signed off at Board level.

A typical institutional investor view on this question is: “*Climate change and a company’s response to it represents a risk to the business that Directors need to be able to demonstrate they are managing - it would also ensure better reporting if senior executives were responsible*.[24]”

<u>Our response in relation to other UK company reporting</u>

CDP’s experience of running a voluntary climate disclosure system for 15 years suggests that public reporting is an extremely powerful lever for behaviour change. Public reporting activates a reputational driver which for many companies can be translated into financial terms. The government can thus create a value proposition for corporate investment in energy efficiency without the need to spend any public money.

Public reporting also facilitates competition between similar companies as to who will report better performance, again without any cost to the public purse. This well-founded insight was behind the CRC’s ‘league table’ and we recommend that the government finds a way to take this idea forwards.

The government proposal suggests the development of a single reporting scheme based on ESOS (although ESOS is currently not strictly a reporting scheme). Currently ESOS compliance is demonstrated through an online registration portal run by the Environmental Agency.

We suggest that relatively small tweaks are made to this system so that companies are asked to report on the energy saving opportunities that have been made possible by their ESOS audit, and then annually on the progress made to implement these energy saving measures, and that the answers to these questions be made publicly available on the Environment Agency or DECC websites. This low-cost mechanism could provide a strong reputational and competition driver for companies although further consultation would be required by DECC to ensure that the requirement was framed appropriately and did not require companies to report commercially confidential information about energy efficiency investments (NB: company-level GHG emissions information is so widely reported that we do not anticipate this data to be considered as commercially confidential by companies.)

As regards the question about whether reporting should be signed off at Board level, we feel that it is always best practice for a Board to be aware of energy issues. We note that the PWC/CDP study commissioned by Defra to inform the decision to introduce the UK Mandatory GHG Requirement found that the main benefits cited by companies from their existing voluntary reporting practices were:

1. Providing transparency to the Board;
2. Brand building and public reputation;
3. Being able to set targets for reductions.

[24] Source: UKSIF internal consultation with investor members, October 2015

If this is the case for voluntary reporting then there seems no reason not to expect mandatory reporting also to go through a company’s Board. Furthermore if the government were to adopt our suggestion of making disclosures about ESOS-related investment public, it would be appropriate for Boards to be aware of these public disclosures.

**Question 4. Do you agree that government should develop a single reporting scheme requiring all ESOS participants (and potentially the public sector) to report regularly at board level? If so, what data should be included in such a report?**

**Answer to Question 4**

Our response to Question 3 has outlined a suggestion as to how to adapt the existing ESOS reporting process to incentivise investments in energy efficiency, and of what data should be included in this reporting. If public sector organisations were to undertake ESOS audits then they could also be included this reporting process. Given that this reporting would be public it seems likely that Boards would want to be aware of what is being disclosed, and to sign it off.

With regards to Question 4 we are unsure of exactly what is being proposed by the government and in particular what is meant by ‘to report regularly at board level’:

- As we said in our response to Question 1 we do not agree that a single reporting scheme can satisfy the needs of all stakeholders and data users.
- As we said in our response to Question 3 we are strongly in favour of maintaining the key features of the existing UK GHG Mandatory Reporting requirement under the Companies Act. Currently this applies only to ESOS participants which are quoted companies although we would be open to seeing this requirement applied also to unlisted companies.
- If – as we presume - by ‘report regularly at board level’ the government is proposing that data related to ESOS (e.g. UK energy use, or the potential for investment in projects) should henceforth be included in annual reports, our response is that for large companies with operations in more than one country, or are groups whose members have undergone multiple ESOS audits, it would be more appropriate to report energy/emissions at entity level as this is more likely to be relevant and material to investors.

At this point it may be useful again to step back and consider the purpose of the different types of policies and reporting that we are talking about.

<u>ESOS, CCL, CRC and CCAs</u> all deal with organisational activity, energy use and emissions in the United Kingdom and encourage or require UK organisations to look in detail at their practices in individual operations and facilities with a view to improving energy efficiency and reducing GHG emissions in the United Kingdom.

The most obvious audiences for any public reporting of this information will be UK regulators, UK customers, competitor companies and energy service providers. However for companies of a significant size this information is unlikely to be material enough to include in entity-level annual reports, other than in aggregated form.

The intended outcome of reporting this data would be the incentivisation of investment in energy efficiency and emissions reductions by UK-based facilities and sub-entities on a bottom-up basis. This is very much in line with the aims of this UK review of business energy efficiency taxation.

The UK Mandatory GHG Requirement has a rather different function and should not be treated as comparable to the policy measures listed above. It requires UK quoted companies to report their direct and indirect GHG emissions from operations, facilities and activities everywhere in the world and at group level. In common with the UK-based requirements it aims at incentivising energy efficiency and emissions reduction but it has an additional goal of facilitating engagement between investors and companies, enabling the management of climate risk, and thus supporting the transition to a low-carbon economy.

The most obvious audiences for information in annual reports are investors and regulators.

The intended outcome of this reporting is for an informed assessment to be made of the management and future prospects of a company. Information should therefore be presented at entity level, which may include aggregating data across different geographies and across different sub-entities.

The bigger picture – issues which have been 'out of scope' of this review to date

Hopefully the comparison above has helped to explain why we do not believe that a single UK-based reporting scheme can work to meet the needs of all companies and all users. It does seem sensible and realistic to consolidate a number of existing UK-based requirements and to use public reporting to incentivise investment in energy efficiency, but we recommend that the government excludes the UK GHG Reporting Requirement from this process.

As we mentioned in our answer to Question 1, the UK Mandatory GHG Reporting requirement was introduced in a wider context of issues which are apparently 'out of scope' for this review relating as they do to UK policies around financial reporting, foreign affairs, international development and climate change. However we would urge the government to take these matters into consideration and to consult with other departments before making any changes to the reporting requirement.

We have summarised the key issues below in turn. They comprise:

1. EU Non-Financial Reporting
2. Financial Stability
3. Integrated Reporting
4. International Development
5. Global Climate Change

1 – EU Non-Financial Reporting

The requirement to include GHG emissions in annual reports comes in a wider context of regulatory requirements to report material environmental matters. These requirements already exist in the Companies Act and will be further strengthened before the end of 2016 when the UK transposes the Directive 2014/95/EU on disclosure of non-financial and diversity information by certain large undertakings and groups[25] ("NFR Directive".) We anticipate that the government will transpose the NFR Directive by making a new amendment to the Companies Act in 2016, and that the government will include in that amendment process any changes to the Act that have been agreed as a result of this current consultation on Business Energy Efficiency Taxation which means that these two policy processes are inextricably linked.

[25] http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32014L0095

The intended outcome of the reporting of environmental matters such as GHG emissions alongside financial information in annual reports is to enable a holistic assessment of a company’s management and performance. To quote the preamble of the NFR Directive: “disclosure of non-financial information is vital for managing change towards a sustainable global economy by combining long-term profitability with social justice and environmental protection. In this context, disclosure of non-financial information helps the measuring, monitoring and managing of undertakings' performance and their impact on society.“

2 – Financial Stability

Enabling investors to make a holistic assessment of corporate management and performance is important not only at the level of an individual company but also at system level, as the Governor of the Bank of England recently pointed out in a speech to Lloyd’s[26] on 29th September 2015. This speech, entitled “Breaking the tragedy of the horizon – climate change and financial stability” pointed out that

> *“Any efficient market reaction to climate change risks as well as the technologies and policies to address them must be founded on transparency of information.*
>
> *A ‘market’ in the transition to a 2 degree world can be built. It has the potential to pull forward adjustment – but only if information is available and crucially if the policy responses of governments and the technological breakthroughs of the private sector are credible.*
>
> *That is why, following our discussions at the FSB last week, we are considering recommending to the G20 summit that more be done to develop consistent, comparable, reliable and clear disclosure around the carbon intensity of different assets.”*

3 – Integrated Reporting

Both the EU NFR Directive and Mark Carney’s speech are manifestations of a global movement in which the UK has to date been a leading participant by virtue of its role as a global hub for the financial sector. In the financial and voluntary sectors significant work has been done to promote the integrated reporting to investors of financial and non-financial information which is relevant and material. Notable initiatives include production of reporting frameworks by the International Integrated Reporting Council (IIRC) and the Climate Disclosure Standards Board (CDSB), both headquartered in London.

4 – International Development

The UK government has indicated support for the principle of integrating financial and non-financial reporting at international meetings in Rio (2012) and Addis Ababa (2015) as we can see reflected in the relevant outcome documents.

> *Text from ‘The Future We Want’[27], the outcome document from the UN Rio+20 Earth Summit*
>
> *47. We acknowledge the importance of corporate sustainability reporting and encourage companies, where appropriate, especially publicly listed and large companies, to consider integrating sustainability information into their reporting cycle. We encourage*

[26] http://www.bankofengland.co.uk/publications/Pages/speeches/2015/844.aspx
[27] https://sustainabledevelopment.un.org/index.php?menu=1298

*industry, interested governments and relevant stakeholders with the support of the United Nations system, as appropriate, to develop models for best practice and facilitate action for the integration of sustainability reporting, taking into account experiences from already existing frameworks and paying particular attention to the needs of developing countries, including for capacity building.*

*Text from Outcome Document[28] to UN Financing for Development conference, 2015*

*37 …We will promote sustainable corporate practices, including integrating environmental, social and governance factors into company reporting as appropriate, with countries deciding on the appropriate balance of voluntary and mandatory rules…*

5 – Global Climate Change

The UK's strategy of leadership in this area is reflected in the Foreign & Commonwealth Office's 2014-15 Priority Outcomes document, 'Our Purpose[29]', which states that under the 'Prosperity' theme and 'Energy and Climate' topic the UK's diplomatic goals include: *"UK/EU climate leadership advances global action at the UN Secretary General's Climate Summit."*

Given that at time of writing there are 30 days remaining until the start of the UN Summit in Paris, and given that other UK energy policy announcements have recently made the UK's claim to climate leadership more difficult to demonstrate, we suggest that it would be prudent for the government to take the opportunity as soon as possible to draw back from proposing any diminishment of the GHG Mandatory Reporting Requirement which was proudly announced by the UK on a global stage at the Rio+20 conference in 2012.

[28] http://www.un.org/esa/ffd/wp-content/uploads/2015/08/AAAA_Outcome.pdf

[29] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/305461/FCO_priorities_14-15.pdf

**Question 5. The government recognises the importance of ensuring market actors have access to transparent, reliable and comparable information to support financing and investment in energy efficiency and low carbon measures. How best can a streamlined report achieve this? To what extent does your response apply to other large companies (as defined in the Companies Act) that are not listed companies?**

**Answer to Question 5**

Ensuring market actor access to transparent, reliable and comparable information

We have answered this question to a very large extent in our response to Question 4.

In short, we believe that investors require useful information about listed companies to be reported in annual reports filed with Companies House. The information reported should cover the company's entire operations, and be global in scope. Having a mandatory reporting requirement provides an opportunity to maximise transparency, reliability and comparability of data as we noted in our response to Question 2.

However, we find it very hard to see how a streamlined reporting scheme relating to UK energy use could be sufficient for this purpose. We suggest that the government's consolidation of existing requirements does not include the GHG Reporting Requirement.

Our suggestion as outlined in our response to Question 3 is therefore that the government should:

1 – Retain the key characteristics of the existing UK Mandatory GHG Reporting requirement within the Companies Act;

2 – Consider adapting the existing ESOS compliance reporting process so that additional material is reported annually, and so that selected information about implementation of ESOS audit recommendations is made publicly available online by the Environment Agency.

Extending the GHG Reporting Requirement to non-listed companies

We note that although this is not explicitly stated in the consultation document, this question probably constitutes the review of this issue which the government promised to undertake after the first two years of the Mandatory GHG Reporting Requirement. Defra's 2012 Summary of Consultation Responses[30] in relation to the requirement says:

*Next Steps*

*Following the public consultation, the Government has agreed with the majority of respondents to introduce regulation to require some companies to report their GHG emissions in the directors' report of their annual report. The Government is committed to reducing the regulatory burden on companies and so has decided to introduce Option 2 (regulation for all quoted companies) which has the lowest regulatory cost of the regulatory options. Experience of this introduction will be used to update the cost and benefit information contained in the final impact assessment. In 2016, the Government will take a decision, based on this updated information, whether to extend the requirement to all large companies.*

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[30] 'Measuring and Reporting of Greenhouse Gas Emissions by UK Companies - Summary of Consultation Responses', June 2012, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/86569/20120620-ghg-consult-sumresp.pdf.

As groups representing investors our expertise relates to the interaction between investors and companies, in which annual reports play a crucial role. Clearly this investor lever is not present in the same way for non-listed companies.

However we note that the original decision to create the GHG Reporting Requirement was based strongly on the benefit to companies from this reporting, as well as the benefit to investors. Clearly therefore there are arguments for extending this benefit across the economy and for creating a level playing field from a regulatory perspective.

We also note that there are other market actors who may see benefit from this reporting – most obviously upstream supply chain counterparties. CDP's Supply Chain program has 75 members who are corporations with major purchasing power, working together to drive GHG and climate disclosure by their suppliers and then to develop procurement practices which incentivise and further drive the resulting efficiencies.

There is also a conceptual consideration that if the UK plans to implement carbon pricing across the economy through the reform of CCL (alongside the EU ETS) then this will apply to all market actors, and it would be consistent to also expect all actors above a certain size to measure, manage and report their impacts.

Extending other reporting to non-listed companies

A streamlined reporting requirement which applied to all ESOS participants (which we would consider should be separate from Mandatory GHG Reporting) would by definition apply to both listed and unlisted companies.

Given the conceptual argument around carbon pricing outlined above, and the opportunities for energy efficiency believed to be available in the public sector, we suggest that the government consider also extending such a scheme to publicly owned entities even though they are not bound by ESOS.

**We have not submitted responses to Questions 6 -20.**

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