Corrigendum: Clause 80 – Statutory Environmental Reporting
June 2008

Proposed Additions – to follow existing para 3.4.8

Issue 11 – Corporate Reporting of Greenhouse Gas Emissions

3.4.9 Clause 80 empowers the Secretary of State to issue, or cause to be issued, guidance on how companies should disclose information about their greenhouse gas emissions in their annual report and accounts. This guidance could be varied according to company sector, type, size etc. The new clause then requires that all companies which currently produce a business review (i.e. all companies other than qualifying small companies\(^1\)) must report on greenhouse gas emissions, having regard to any such guidance.

3.4.10 This would require:
- the UK Government to consider producing (or causing to be produced) guidance for companies on how to report their greenhouse gas emissions; and,
- all companies, other than small companies, to include emission information in their annual reports having regard to such guidance.

Benefits:

3.4.11 The benefits of Clause 80 are difficult to quantify, and there are none that can be monetised at present. Mandatory reporting requirements would force companies to measure their emissions, and it is argued that this may raise the level of consideration given to the issue of climate change. In addition, it is hoped that this may assist in the development of a usable standard. Common standards would then allow companies emissions to be compared against those of others.

3.4.12 However, the case that mandatory reporting helps companies reduce their emissions has not been proven. Although companies which voluntarily measure and monitor their greenhouse gas emissions may be more likely to manage them effectively, there is no settled evidence that shows that being required to report on emissions would drive effective emissions management. Whilst some analysis suggests that mandatory reporting might help lead to some uptake of energy efficiency opportunities, this correlation is not conclusive, particularly on how investors use this information in their decision making, and on

\(^1\) For the purposes of the Companies Act 2006, a small company is defined as one which meets two of three criteria - turnover not more than £6.5m; balance sheet total not more than £3.26m; and not more than 50 employees – and does not fall into one of the excluded categories (e.g. public, banking or insurance company).
the effectiveness of mandatory reporting without a direct financial incentive in driving emissions improvements in organisations.²

3.4.13 It should be said that many UK companies already disclose their emissions to schemes such as the EU Emissions Trading Scheme, in their Corporate Social Responsibility Reports and to voluntary initiatives such as the Carbon Disclosure Project.³ It is therefore difficult to ascertain what additional benefits a mandatory reporting requirement would deliver. However, the requirements, by providing guidance to companies, could help support the development of common standards.

3.4.14 There is also a requirement under section 417 of the Companies Act 2006 (the “business review”) for directors of quoted companies⁴ to report certain information, including on environmental issues, to the extent necessary for an understanding of the development, performance or position of the company’s business. The business review requirements in section 417 only came into force on 1 October 2007 for financial years beginning on or after that date, so the Government is not yet able to assess their impact in respect of environmental reporting. It may be that many quoted companies (currently around 1300 companies) will report their emissions in their business review. For those companies, the additional costs of complying with clause 80 would be lower than for those who are not already doing so. However, the scope of Clause 80 is much wider than just quoted companies – it would apply to all companies other than small companies.⁵ This would lead to significant new costs for medium and large-sized companies (there are at least 50,000 of them), many of which are being required to measure and report their emissions for the first time under these new mandatory requirements.

Costs:
3.4.15 As noted in paragraph 3.4.13, the reporting requirements set out in clause 80(4) would cover all UK companies (over 50,000) that are currently required to produce a business review under the Companies Act 2006. As a new obligation there would be fixed costs faced by all companies regardless of their size, as well as a variable cost element that would depend on the prescriptive nature of the relevant guidance. For example: the emissions that a company produces; how

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³ www.cdproject.net
⁴ A quoted company is defined in section 385 of the Companies Act 2006 as a company whose equity share capital is listed in the UK or in an EEA State, or admitted to trading on the New York Stock Exchange or NASDAQ.
⁵ For the purposes of the Companies Act 2006, a small company is defined as one which meets two of three criteria: turnover not more than £6.5m; balance sheet total not more than £3.26m; and not more than 50 employees – and does not fall into one of the excluded categories (e.g. public, banking or insurance company).
complicated they are to measure; whether direct or indirect emissions are included; \(^6\) if domestic and/or overseas emissions are to be included; and the extent to which existing reporting requirements such as the UK Emissions Trading Scheme, the Carbon Reduction Commitment or voluntary arrangements can also be used for any mandatory requirements. Costs may also vary if the guidance were to distinguish between different types of company, as is possible under Clause 80 (3).

3.4.16 Until decisions on the design of the reporting requirement have been made it is only possible to provide an indicative estimate for the possible cost of a reporting requirement. Based on analysis from the Carbon Reduction Commitment, it is possible to estimate a lower bound to the costs to business of the reporting requirement for the estimated 50,000 companies that the requirement could be applied to. This suggests that the costs of a mandatory reporting requirement would be in the order of £180 million per annum, as a minimum.\(^7\)

3.4.17 Currently, there is no evidence to support an estimate of what a more complex reporting requirement may cost. This would vary depending on the exact design of the mandatory reporting scheme, including decisions on the scope of emissions covered, the size and complexity of firm emissions, the level of precision in monitoring, whether emissions from overseas were included and if other countries introduced similar requirements for reporting emissions. Depending on the exact design, costs could be expected to be significantly greater than the minimum estimate of £180 million per annum. It is not possible at this time to provide a more robust cost estimate of a more comprehensive reporting requirement. Work to develop this guidance would require the production of a full Impact Assessment, setting out the costs and benefits of a range of options within a mandatory reporting regime, including the emissions coverage and scope which could drive the greatest emissions reduction.

3.4.18 The cost to the UK Government of producing the guidance is difficult to estimate and would depend on a number of factors: the scope of the guidance, the level of expert resource and stakeholder involvement necessary to develop workable guidance, and the level of agreement between parties. However, we would expect it to be in the region of £100,000 to well in excess of £200,000. The administrative costs for this would be incorporated within existing Departmental budgets.

\(^6\) There are various different emissions types defined under the GHG Protocol, for example emissions from sources that are owned or controlled by a company, such as combustion facilities, combustion of fuels in transportation and physical or chemical processes. These are known as scope 1, or direct emissions. In addition there are also various types of indirect emissions, for example, Scope 2 emissions which are generated by another party of electricity that is purchased and consumed by the company.

\(^7\) Based on extrapolating estimates by NERA for a mandatory reporting regime from approx 5,000 to 50,000 companies. See www.defra.gov.uk/environment/climatechange/uk/business/crc/pdf/nera-report.pdf (page iv)
3.4.19 It has been assumed that there would be no additional costs to Government or to the Financial Reporting Council (the regulatory body) of monitoring these additional reporting requirements, as the existing enforcement provisions of the Companies Act 2006 would apply (assuming the level of monitoring for the new requirements is the same as for the Director's Report as a whole). However, if the agreed standard required additional monitoring activity then the costs could increase substantially.

Section 4 (Small Firms Impact Test)

4.3 Following trading schemes
Reporting under Clause 80 would be applicable to companies currently required to produce a business review under section 417 of the Companies Act 2006), which means that companies falling under the Companies Act definition of a small company would be excluded. Depending on the scope of the emissions included, there could be an impact on small companies which were suppliers of companies required to report on the emissions in their supply chains, as might be possible under this clause.

Summary sheet changes

Addition: The Narrative reporting requirements in new clause 80 would all be administrative burdens.

Defra; 6 June 2008