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Ms Carla Hopkins
DEFRA GHG Reporting Team
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Dear Ms Hopkins

Consultation on Greenhouse Gas Emissions reporting draft regulations for quoted companies

I am writing with the response of the United Kingdom Environmental Law Association ("UKELA") to the above consultation.

Who are UKELA?

UKELA is the UK's foremost membership organisation comprising both lawyers and non-lawyers. Our aim is to improve the understanding and awareness of environmental law, and to make the law work for a better environment. UKELA has a climate change and energy working party (**CCEWP**), which monitors and, where appropriate, comments on the development of climate change and energy related policy and legislation.

As many of UKELA's members work in private practice, they are well informed on how various environmental policy measures work and common issues that their clients face when complying with such measures.

In responding to consultations, UKELA's aim is to ensure that the proposed policy measure or law will work including within the policy and legislative landscape within which it is framed.

Purpose and scope of the regulations

As a result of the variety of its membership, the CCEWP is aware of the differing expectations of the various interest groups affected by the proposed regulations, such as company management and auditors, shareholders and environmental NGOs. We are also aware that the Department may have to reconcile competing policy objectives in terms of imposing pressures on commercial organisations to assist in meeting the UK's targets for reductions in carbon emissions, while also meeting the objectives of the Red Tape Challenge to reduce unnecessary regulatory burdens on business. In addition, given the current economic backdrop, the government is focused on encouraging the UK's economic growth ability to compete in international markets.

We think however that it would be helpful if, in its response to the Consultation (and where appropriate by amendments to the text of the draft statutory instrument), the Department set out more explicitly the objectives of the proposed reporting regulations, which are currently largely a matter of

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inference. We believe this would be helpful, both in terms of assisting company management and auditors in focussing on what needs to be achieved, and in terms of ensuring realistic expectations amongst stakeholders. We are conscious that this may be difficult to do given that the aims of GHG reporting are quite wide and the government may have concerns about making statements that people (such as NGOs) could rely on and challenge. However, we think on balance that the benefits of being more explicit about the aim of these regulations (that is actually getting reports that contain meaningful GHG data that leads organisations to manage their GHG emissions better) will outweigh such concerns.

We would endorse the proposal for the reporting requirements to attach to the directors' report. This will help make it more likely that the relevant information is read.

In the case of quoted companies which form part of a group, whether the GHG emissions reporting will be carried out on a group basis, or will only apply to the relevant activities of the quoted company itself will depend on whether the parent company chooses to prepare group accounts,. That would not necessarily be inappropriate. The parent company's decision in that respect may well reflect the extent to which companies in the group are part of a coherent organisation, or on the other hand more autonomous entities which form part of an investment portfolio. In many cases, the decision may also effectively be dictated by fiscal or other commercial considerations.

From another perspective, this aspect of GHG reporting, will make it more difficult for interested outsiders to compare like with like. This also follows from the fact that there is no single mandatory methodology which directors are required to follow in calculating emissions.

Plainly the statistics gathered will also only be of limited use to Government, given that quoted companies and groups of companies will vary considerably in the extent to which their activities are UK-based or more global in nature. We assume from the references to the activities of the company (or the group where this is relevant) that (in line with the Summary of Consultation Responses to "Measuring and reporting of greenhouse gas emissions by UK companies" published in June 2012) emissions from relevant activities are to be reported on whether or not the activities are in the UK. Notwithstanding the decision announced in the DEFRA response, if one of the purposes of the GHG reports is to assist the Government to meet UK targets for reductions in GHG emissions does it make sense for these reports to cover non-UK emissions?

It would seem to follow from this that the main benefit of the proposed regulations (a significant benefit, it is acknowledged) is that it will encourage those key shareholders who take an active interest in the environmental performance of their investments to take a more active role in influencing that performance.

We therefore think it would be helpful if the regulations set out more explicitly a requirement for reports to consider what scope there is for the company (or group as the case may be) to reduce relevant GHG emissions, the company or group's plans in that respect, and in reporting years after the first, progress or otherwise in implementing those plans. This would make it clear that the reporting is intended to be a dynamic process, to drive improvement, and not simply a statistical record.

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We would also suggest that the regulations need to set out more explicitly the "comply or explain" approach which, we understand from the Summary of Consultation Responses referred to above, the reports are intended to adopt in relation to the collection and reporting of emissions data.

Commencement

The Department expressly invited views on the commencement of the obligations under the regulations.

In our view, it is too ambitious to require annual reports published after 6 April 2013 to include the specified GHG information, as data will need to be collected in advance on a consistent basis.

From that point of view it is insufficient notice for companies to be aware of the policy intention as a result of Ministerial announcement. They will need to know the detailed requirements before the commencement of the relevant reporting year. These requirements should be set out in legislation and guidance.

We therefore think it would be more appropriate for the requirement to apply to reports for financial years ending after 6 April 2014.

It seems to us that the proposals in respect of narrative reporting are different in nature, so that there is no compelling reason for the introduction of GHG emissions reporting to be timed to coincide with it, although we note that for those affected by the regulations, it may be easier to deal with reporting changes that are required by both initiatives at the same time.

Fuel

Draft Regulation 3 requires the reporting of emissions that relate to the combustion of fuel in premises, or by machinery or equipment operated, owned or controlled by the company. It is assumed that all fuels of any type are covered. The CRC Energy Efficiency Scheme (CRC) currently requires organisations to report on 29 fuels. However there is an existing proposal to reduce this to just 4 main fuels (electricity, gas, kerosene and diesel) as a result of the administrative burden that reporting on all 29 fuel types causes. Other fuels are considered not to be used in quantities that are significant enough to justify the administrative burden to including them in the CRC. There may be some value in mirroring this proposal for GHG reporting, at least initially. It may indeed be appropriate to provide more generally, that where the majority of emissions from fuels are covered by a compliance scheme, and it would be disproportionate to report on emissions from the remaining fuels, companies shall not be required to do so.

GHG gasses

Given that nitrogen trifluoride (NF₃) has been added to the UNFCCC's inventory requirements, we believe that there is a case for adding it to the list of gasses to be reported on.

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Materiality Threshold

We appreciate that the Department has taken a policy decision that the scope of the requirements should extend to quoted companies, as opposed to unquoted companies, pending a review of their extension in 2016 to cover a wider range of larger companies.

However, we understand that it is possible in certain sectors for a company to be quoted, notwithstanding that it has relatively few staff. For these companies, the administrative burden of reporting will be heavy. In order to give those companies more time to prepare for reporting we suggest that at least initially there should also be a materiality threshold set in terms of annual expenditure on energy bills. Although in the case of companies or groups which fall below the threshold and in consequence did not report, directors should be under an obligation to state that relevant company or group expenditure fall below the threshold. Such a threshold could be reviewed at the same time that the Department reviews the extension of GHG reporting to unquoted companies.

Sectoral approach to methodology and changes to Methodology etc

Given the variety of methodologies that exist and are being used by companies reporting voluntarily on their GHG emission, we understand why the regulations are flexible as regards methodology. We think that in order to help investors compare companies within a sector, sectors ought to be encouraged to specify a single methodology that companies in that sector will use.

In keeping with the dynamic process which we think reporting should reflect (see above), and in order to encourage transparency, we believe that where from one reporting year to the next there is a change of methodology for calculating emissions or intensity ratios etc, the directors should be obliged to explain the reason for the change, and also to provide the appropriate recalculation for the baseline year information.

Baseline year

We understand that a number of organisations that have voluntarily been reporting their emissions would like to take as their baseline year the first year of voluntary reporting rather than the "first reporting year" as defined in Regulation 7 of the draft Regulations.

We can understand and sympathise with this, but suspect that the systems of reporting adopted voluntarily may well not coincide with the regime to be established under the Regulations.

It seems to us that the best solution is for such companies to provide both sets of baseline information, with a brief explanation of any material differences in methodology, group organisation etc which may be relevant.

We would also make the point that if there are significant changes in an organisation over the course of reporting years, the original baseline information may lose relevance.

We suggest that, subject to the requirement to explain, directors should be able to elect to substitute a new baseline year following a major change in organisation.

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Minimising the Regulatory Burden

We endorse the requirement in draft Regulation 5 to specify where relevant information was obtained as a result of compliance with pre-existing emissions reduction schemes. This is not only consistent with the requirement for transparency as to methodology, but is sensible in terms of encouraging companies to use this information in order to minimise the regulatory burden.

However, since the organisational basis used for these schemes will not necessarily be the same as that which will apply for the purposes of the draft regulations, we suspect that the practical benefit in using this data may be limited.

Verification

We consider that the Department should, as a long-term measure, consider the case for mandatory verification, as well as reporting of emissions, even if this may require further legislation. We would point out that this should not be unduly burdensome for quoted companies or their groups, particularly if, as we suggest above, there is also an energy-use threshold for the reporting requirement.

Apart from providing stakeholders with confidence in the reporting, verification also provides reassurance for the directors who have to sign off on the report. We think that there needs to be an acknowledgement that directors should be able to rely on the work of expert verifiers they have engaged for the purpose, and this should be reflected in the legislation or guidance.

Engagement of Stakeholders

In trying to ensure that any system of corporate reporting on GHG emissions is workable, it is important to speak to both the entities that will produce this data (in this case quoted companies) and also entities that will use the data – analysts and also environmental NGOs. If the Department have not already spoken to NGOs about how they plan to use this data and what information they think will be helpful to them and also to investors, we strongly recommend that the Department does speak to these organisations.

We note that as the regulations are to be made under the Companies Act, enforcement will be carried out by the Conduct Committee of the Financial Reporting Council. We would highlight the need for the regulator to be well prepared to engage proactively with NGOs and other interested bodies, who may well fall outside the circle of the Financial Reporting Council's normal stakeholders, on issues relating to the application and implementation of the regulations. This will help drive improvements in reporting by companies. A related issue, is that the Department may also need to assist analysts (who are probably more used to looking at financial rather than environmental data) to understand the data that results from the GHG reports. This will ensure that meaningful comparisons of competitors are made and that GHG reports do contribute to monitoring environmental claims and translate into reduced emissions.

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We would be happy to discuss the above points further if that would be helpful to the Department.

Yours sincerely

T C Hitchcock
Partner
DLA Piper UK LLP

On behalf of the Climate Change & Energy Working Party
United Kingdom Environmental Law Association

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