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CONSULTATION RESPONSE DECEMBER 2023

SCOPE 3 EMISSIONS IN THE UK REPORTING LANDSCAPE

E3G RESPONSE TO CONSULTATION

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Delivering a credible sustainability reporting regulatory framework will be essential if the UK is to deliver on its ambition to become a world-leading Net Zero Aligned Financial Centre. Scope 3 emissions account for an estimated three-quarters[1] of company-level emissions and it is essential that they are reported.

Summary

> Scope 3 information has high value and widespread uses for market actors including the business itself, investors, and lenders[2]. Although many UK businesses have been conducting Scope 3 reporting for several decades[3], the UK still has a large disclosure gap that must be addressed[4].

> In setting out the role of Scope 3 disclosures within a broader Sustainability Disclosures Regime (SDR), regulators should prioritise interoperability with requirements in other jurisdictions. We recommend that the UK adopts the ISSB approach to Scope 3 disclosure when setting out disclosure requirements. This will unlock investment opportunities between jurisdictions and reduce the reporting burden for multinational companies.

[1] CDP, 2023, **CDP Technical Note: Relevance of Scope 3 Categories by Sector**

[2] TCFD, 2021, **Metrics, Targets, And Transition Plans Consultation**

[3] Greenhouse Gas Protocol, 2011, **Corporate Value Chain (Scope 3) Standard**

[4] Bloomberg Professional Services, 2023, **Closing the Scope 3 GHG emissions data gap**

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Key recommendations in E3G response

- The UK should as soon as possible provide forward clarity to the market on its plans to provide a single, overarching and coherent Sustainability Disclosures Regime for businesses on sustainability disclosures.
- The UK should not delay in implementing its commitment to adopt ISSB S1 and S2, which will ensure interoperability of UK requirements with those of other jurisdictions.
- The UK should:
  - Take steps to increase the accessibility and utility of Scope 3 information. This includes ensuring consistency of response format and developing clear, machine-readable data tags.
  - Ensure that both large listed and non-listed companies are required to disclose their Scope 3 emissions, in order to create a level playing field across the economy.
  - Embed Scope 3 disclosure requirements in a timely wider package of SDR reforms including disclosure of mandatory transition plans and against a science-based green taxonomy.

Chapter One: Streamlined Energy and Carbon Reporting (SECR)

General Questions

1 - What is your company number? If you work for an LLP, please state so here.

- 05158916

3 - What is your role in relation to company reporting? For example, are you a reporting entity, a company within the supply chain of a reporting entity, an investor and/or a user of accounts, contracted to report on behalf of a reporting entity, part of a consultancy firm, or part of a voluntary reporting scheme?

- E3G is a non-profit global climate think tank, creating cross-sectoral coalitions to solve climate policy challenges. We use sustainability disclosures to better understand the role played by firms in the UK and global net zero transition, and to inform our future work on the essential policy reforms required to deliver the UK's Net Zero Aligned Financial Centre.

4 - What role does Scope 3 emissions reporting currently play in your organisation? If your organisation does report its Scope 3 emissions, which Scope 3 emissions categories are you currently reporting on and why? Is this on a voluntary or mandatory basis? Please state whether you have done so in the past and, if you no longer report Scope 3 data, why.

- **Sustainability disclosures, including Scope 3, are an essential building block for the UK's Net Zero transition.** These disclosures can enable the identification of material business risk by a range of market actors, policymakers and CSOs, and can facilitate the mobilisation of investment at scale towards net zero opportunities. Sustainability disclosures are valued by leading UK investors and businesses who recognise both threats and opportunities from the net zero transition; 99% of the UK's 100 largest companies by revenue report on sustainability to some degree[5]. This is particularly the case for our organisation, a climate think tank, which uses Scope 3 disclosures as part of a broader package of disclosures to assess the progress made by the UK on the net zero transition, and effective risk management processes by the private sector.

- **Scope 3 disclosures are considered highly valuable to investors, due to the variety of use cases they have.** A TCFD consultation found that 95% of disclosure data users found disclosure of Scope 3 metric useful to inform decision making[6]. Key benefits included:

  - Promoting interoperability with other economies, unlocking investment and reducing reporting burdens.
  - Helping investors understand and apply Scope 3 information to minimise transition and physical risk in their value chain.
  - Allowing companies to understand where emissions hot spots are in their value chain, manage related risks and engage with their supply chain to reduce their overall emissions.
  - Ensuring that wider market actors such as ratings agencies, auditors, index providers and proxy advisors have the data they need to provide high quality services.

[5] KPMG, 2022, **Survey of Sustainability Reporting**

[6] TCFD, 2021, **Metrics, Targets, And Transition Plans Consultation**

> Tackling greenwashing and allowing businesses and consumers alike to verify the credibility of advertised claims.

Chapter Two: Scope 3 GHG reporting

General questions

5 - Do you agree or disagree with the ISSB's assessment of the value of Scope 3 information?

> **We agree with the ISSB's assessment of the value of Scope 3 information for businesses looking to address climate-related risks in their value chain. Scope 3 emissions are the largest proportion of most companies' GHG impact and exposure[7], meaning that analysis of this category of emissions is crucial to integrating climate risk in corporate decision making**. CDP recently pointed out that Scope 3 emissions account for, on average, three-quarters of a company's emissions. This can be much higher in some sectors such as Oil and Gas, where Scope 3 emissions represent almost nine tenths of the total emissions exposure of each company. This can be much higher for the financial sector[8].

> **ISSB S1 and S2 focus on providing material information to investors, lenders, and other creditors[9].** Scope 3 disclosure requirements have been included in IFRS S2 because they are considered material for primary users of general-purpose financial reports.

> **Scope 3 has a variety of use cases for non-businesses users. For example:**

- **Scope 3 emission information can help investors to measure and manage transition and physical risks and opportunities in their portfolio, to inform targeted stewardship activities and inform capital reallocation**. A 2020 CDP report showed that financial institutions' Scope 3 financed emissions are over 700 times greater than their operational emissions[10]. Scope 3 disclosure helps investors to understand where emissions risk is concentrated in the value chain of different companies. For example, a fertiliser company may have high emissions associated

[7] TCFD, 2021, **Metrics, Targets, And Transition Plans Consultation**

[8] CDP, 2023, **CDP Technical Note: Relevance of Scope 3 Categories by Sector**

[9] IFRS, 2023, **IFRS Sustainability Standards Navigator**

[10] CDP, 2020, **The Time To Green Finance**

with purchased goods, as well as high emissions related to the application of their fertiliser (GHG Protocol defines these as Scope 3 Category 1 and Category 11 emissions), but low emissions in other emissions categories.

- **Lenders can use Scope 3 information to manage climate-related risks, increasing the resilience of their lending portfolios**. A high emission footprint constitutes an economic risk to companies as decarbonisation pressures increase from consumers, policymakers and other stakeholders. In the UK, loan exposures to fossil fuel producers, energy utilities and emissions intensive sectors are equivalent to around 70% of the largest UK banks' regulatory capital[11], meaning UK banks have a high level of fragility when exposed to climate risks. When financing emission-intensive sectors, UK banks are increasingly setting Scope 3 targets as part of their approach to managing risk. Credible data on Scope 3 emissions enables lenders to better understand the impact of their investments. This supports action to incentivise decarbonisation throughout their own value chain through tools such as offering favourable rates to decarbonising companies, and stewardship.
- **Scope 3 emissions information is also useful to actors in the wider capital market ecosystem (e.g. data services, credit ratings**). Many financial service providers are committed to offering products and services that help manage climate risk and support the transition to net zero[12]. Scope 3 emissions data is an essential part of this. Examples include:
    - Rating agencies need Scope 3 data to identify companies' exposure to transition-related climate risks and assess how this affects credit ratings.
    - Auditors are increasingly being asked to ensure that reported Scope 3 emissions data has quality, integrity and independence. The UK is a global leader in audit excellence[13] making this a huge growth opportunity for the UK audit sector.

[11] Bank of England, 2019, **The 2021 biennial exploratory scenario on the financial risks from climate change**

[12] Net Zero Financial Service Providers Alliance, 2023, **Committed to Net Zero**

[13] BEIS, 2022, **Restoring trust in audit and corporate governance**

- Index providers increasingly offer net zero and transition indices. Reliable, comparable Scope 3 emissions data improves the accuracy and integrity of their ratings for company reporting in same category. This contributes to more coherence between different providers.

- Proxy advisors will need information on Scope 3 emissions to provide informed advice for investors on company progress on net zero.

  - **Emissions information is also valuable for the verification of environmental claims about products by companies and consumers.** Scope 3 emissions data is essential for companies seeking to avoid greenwashing, and for consumers to verify the credibility of advertised claims about products. Regulators, including the Advertising Standards Authority, Competition and Markets Authority and Financial Conduct Authority, are taking action to address misleading claims[14]. For example, Tesco withdrew adverts after the Advertising Standards Authority found it did not "hold any evidence in relation to the full lifecycle of any of the products in the Plant Chef range"[15]. Scope 3 emissions data will help businesses speak about their climate credentials with confidence and will benefit consumers by empowering them with reliable information to make more sustainable choices.

> **For a full explanation of the benefits of Scope 3 reporting to businesses, see our response to question 15.**

6 - In general, what is your view on the approach to Scope 3 reporting contained within IFRS S2? Please consider the ISSB's approach to materiality in your answer.

> **We support the IFRS Foundation's decision to require company Scope 3 GHG disclosures as required by the ISSB. IFRS S2 sets out a valuable framework for companies to disclose their Scope 3 emissions against**. This is because these disclosures benefit investors as set out our response to Chapter 2. The key benefit of their approach is that it creates consistency in reporting across a variety of businesses in the economy, increasing the comparability and use-value of emissions data

[14] ASA, 2023, **Greenspeaking with confidence**

[15] FT, 2022, **Tesco rebuked over greenwashing in adverts for plant-based food**

- **We therefore strongly encourage the timely adoption of the IFRS S1 and S2 by the UK, in line with its public statements of intention, as these are designed to provide the global baseline for sustainability standards**, endorsed by IOSCO and the Financial Stability Board, amongst others, and are designed to work coherently with IFRS standards which form the basis of UK financial reporting standards. Ensuring interoperability in the UK's climate reporting framework will help reduce preparer costs and provide investors with useful information (which they can compare over time for a company, and compare different companies at a point in time)
- **Post adoption of IFRS S1 and S2, the UK should consider further steps, e.g. creation of guidance, to drive interoperability with other international disclosure standards**. This is especially important to avoid those UK companies which will be requested to disclose sustainability information on a double materiality basis in the future, for example through the EU's CSRD extraterritorial effect, from needing to create parallel reports.

7 - What is your view on the use of the GHG Protocol for the purposes of Scope 3 reporting within IFRS S2? Will this lead to comparable and consistent reporting that is useful for investors and users of accounts?

- **The use of the GHG Protocol for the purposes of Scope 3 reporting within IFRS S2 is a positive development which will support more comparable and consistent reporting of climate-related emissions**. The GHG Protocol is by far the most widely used global standard for measuring and reporting greenhouse gas emissions[16]. The application of the GHG protocol methodology by IFRS S2 will help to ensure that entities are using a consistent and comparable methodology for reporting their Scope 3 emissions. This further supports interoperability across jurisdictions. At COP28 global support for ISSB was reaffirmed by close to 400 organisations from 64 jurisdictions[17].

- **Increased comparability of emissions information will be particularly beneficial for investors and users of accounts**, who will be able to compare the climate-related performance of different entities more easily. This will allow investors to make more informed investment decisions and to identify companies that are taking effective action to address climate change.

[16] Jia et al, 2023, **A Rapid Review of GHG Accounting Standards**

[17] IFRS, 2023, **ISSB at COP28**

> **The formal recognition of a standardised credible methodology which is already a de facto market standard, i.e. the GHG Protocol, will help to reduce the administrative burden on entities.** Standardisation of reporting guidance will reduce the risk of fragmentation, meaning that companies will not need to develop bespoke processes for measuring and reporting their Scope 3 emissions. This will enable companies to more easily report and compare Scope 3 data, and to focus on more strategic activities such as developing and implementing climate-related mitigation and adaptation strategies.

> **The use of the GHG Protocol for Scope 3 reporting within IFRS S2 supports interoperability with other jurisdictional approaches, such as California and the EU.** For example, the European Corporate Sustainability Reporting Directive and California's Climate Corporate Data Accountability Act[18] require companies to use the GHG Protocol Corporate Standard and Corporate Value Chain Accounting and Reporting Standard[19]. The GHG Protocol is also widely adopted through voluntary frameworks such as CDP, with companies representing 66% of global market capitalisation disclosing to CDP in 2023[20].

8 - Would using the ISSB's approach to Scope 3 reporting have knock-on consequences for your organisation that the Government should be aware of? For instance, you may wish to consider the interaction between IFRS S2 and any EU regulations, or other energy/emissions reporting requirements that your organisation may be impacted by.

> **Scope 3 reporting is likely to become the global expectation and a de-facto requirement for UK multi-national corporations as an increasing number of jurisdictions require Scope 3 reporting**. The number of UK companies that will need to disclose Scope 3 is likely to grow rapidly over the coming years due to proposed adoption of ISSB guidance both in the UK and in key international jurisdictions. Whilst many UK multinational companies already disclose their Scope 3 emissions on a voluntary basis, many companies who operate in the EU are likely to be required to report on Scope 3. From next year, 1,183 UK companies operating in the EU[21], as

[18] California, 2023, **SB-253 Climate Corporate Data Accountability Act**

[19] See California Senate Bill-253 Climate Corporate Data Accountability Act and the EU Corporate Sustainability Reporting Directive which adopts the European Sustainability Reporting Standards (ESRS). The ESRS allows companies to use the GHG Protocol or ISO 14064-1: 2018.

[20] CDP, 2023, **Record 23,000+ companies disclose environmental impact through CDP**

[21] Wall Street Journal, 2023, **At Least 10,000 Foreign Companies to be Hit by EU Sustainability Rules**

well as multinationals investing in both jurisdictions, will be required to disclose (where material) in line with the Corporate Sustainability Reporting Directive (CSRD). Given that the EU accounts for 42% of UK trade (equivalent to £340 billion in exports[22]), it is safe to assume that going forward an increasing number of UK companies will need to disclose Scope 3 emissions data to the EU either due to their business there or to attract EU finance.

> **Other jurisdictions bringing in Scope 3 reporting requirements in line with ISSB include the State of California.** Representing the world's fourth largest economy, the Assembly of California adopted SB 253, California's Climate Corporate Data Accountability Act[23]. The act requires U.S. companies doing business in California and with total annual revenues exceeding $1 billion to disclose their annual Scope 1, Scope 2, and Scope 3 GHG emissions to an emissions reporting organization that contracts with the California Air Resources Board (CARB).

> **Interoperability is the only way to ensure that UK non-financial reporting requirements aid UK businesses in accessing international investment and trade opportunities**. Adopting the ISSB framework will ensure that the UK remains a competitive place to do business and will reduce unnecessary reporting burdens.

> **The UK must provide forward clarity on its SDR plans, including the timeline for adopting ISSB, in order to provide a useful and coherent framework for businesses on sustainability disclosures**. This certainty is critical to minimising reporting costs and maximising benefits is solving the issue of fragmentation. This will ensure that UK businesses and investors can avoid being overburdened by varying disclosure requirements and can make full use of the advantages that Non-Financial Reporting brings. To do this, the UK must fully adopt ISSB S1 and S2 as soon as possible. ISSB is the emerging global sustainability standard, backed by the G7, the International Organisation of Securities Commissions, and with jurisdictions such as Australia, Brazil, Canada, Japan and South Korea setting up adoption processes on ISSB[24]. Crucially, the ISSB Scope 3 definition is significantly aligned with the EU's CSRD[25]. This means that interoperability between the UK's reporting

[22] House of Commons, 2023, **Statistics on EU-UK Trade**

[23] California, 2023, **SB-253 Climate Corporate Data Accountability Act**

[24] IFRS, 2023, **ISSB: Frequently Asked Questions**

[25] IFRS, 2023, **European Commission, EFRAG and ISSB confirm high degree of climate-disclosure alignment**

requirements and those of the EU can be achieved by incorporating ISSB S1 and S2 into UK requirements.

Chapter Three: costs and benefits of Scope 3 reporting

General questions

15 - What are your views on the overall costs and benefits of Scope 3 reporting? Please be as specific as possible.

16 - What benefits could Scope 3 reporting bring to your organisation? Please be as precise as possible when explaining the basis of any benefits you provide. If you currently produce Scope 3 data voluntarily under SECR, please explain the benefits you have received and how they have changed over time.

- **The benefits of Scope 3 disclosure far outweigh the costs for firms. Firms, and other users overwhelmingly find Scope 3 data useful for decision making.** A TCFD consultation found that 95% of disclosure data users found disclosure of Scope 3 metric useful to inform decision making[26].
- **To further unlock the benefits for all users, we must address the huge disclosure gap on Scope 3 emissions.** Bloomberg estimates that in 2020 just 20% of business reported on their Scope 3 emissions[27]. Businesses also tend to disclose on the emissions that are easiest to calculate (e.g. corporate travel and office utilities) rather than other areas which may have more related emissions. This gap makes it difficult for businesses to identify risk in their value chain and other users to use information for decision making. Mandatory requirements and clear guidance would help address this disclosure gap.
- **For businesses, reporting on Scope 3 brings benefits including:**
    - **Supporting sustainable business planning**. To account for climate related risks and identify opportunities to cut emissions, it is essential that companies are disclosing their Scope 3 emissions. As the risk and reality of climate related damages increase, it is essential that businesses are aware of where climate related risk lies in their value chain. In 2011, a Tsunami in Thailand lead to Japanese auto manufacturers having to curtail production due to the disruption this

[26] TCFD, 2021, **Metrics, Targets, And Transition Plans Consultation**

[27] Bloomberg Professional Services, 2023, **Closing the Scope 3 GHG emissions data gap**

disaster had on their supply chains[28]. Better understanding of Scope 3 emissions can inform businesses of where steps are needed to increase the resilience of their supply chains.

- **Increased understanding of emission risk across a businesses' value chain enables them to take action to decarbonise through tools such as procurement.** Scope 3 reporting requirements incentivise large companies to understand their exposure to climate risk through their value chain and drive economy wide decarbonisation. Large companies, by requesting Scope 1 and 2 data from their suppliers, can build information on Scope 3 and mitigate climate risk and drive significant decarbonisation. CDP's supply chain programme saw 200 large companies drive 231 million tCO_2e of emissions reduction initiatives in 2021[29]. Practical actions include updating purchasing and evaluation processes and supplier code-of-conducts to include emission reduction initiatives.

- **Unlocking investment by ensuring that UK businesses meet investors' needs.** Disclosing Scope 3 emissions data strengthens investor perceptions about the corporate governance of businesses, critical at a time when the UK is struggling to compete for global investment[30]. Investors based in jurisdictions where Scope 3 reporting is required will need UK firms to provide high quality and interoperable Scope 3 emissions data in order to qualify for investment. Addressing this challenge is crucial to sustaining FDI in the UK, with our largest affected investment partner being the EU. Once CSRD comes into effect in 2024, EU investors will require Scope 3 data from UK investments in order to maintain the £10.4bn a year in EU to UK investment[31].

> **For use cases for other Scope 3 information users – such as investors, lenders and wider market actors – see our response to question 5.**

> **Scope 3 reporting requirements must come as part of a larger package of reforms including Transition Plans and a science-based UK Green Taxonomy.** Together this regime will help drive business and sector level transitions and deliver on the UK's green goals. The gold standard for transition planning – as

[28] Reuters, 2011, **Thai floods batter global electronics, auto supply chains**

[29] CDP, 2021, **Engaging the Chain: Driving Speed and Scale**

[30] FT, 2023, **Why is the UK struggling to attract foreign direct investment?**

[31] CBRE, 2023, **UK Capital Flows In & Out**

set out by the Transition Plan Taskforce – is aligned with the ISSB framework so as to aid businesses once ISSB S1 and S2 are adopted in the UK[32].

17 - What costs could Scope 3 reporting bring to your organisation? Where possible, please give a breakdown of each element of cost. Please be as precise as possible when explaining the basis of any costings you provide. If you do currently produce Scope 3 data voluntarily under SECR, please explain the costs you have incurred and how they have changed over time.

> **Whilst reporting can be expensive, reporting costs are outweighed by benefits**. In a 2022 survey, ERM found that Scope 3 reporting rates were low, not due to cost concerns, but because companies in each of the investors' value chains were not conducting Scope 1 & 2 reporting and so the investors could not easily access data[33]. Investors and other data users consistently assert that the benefits outweigh the costs[34].

> **Reporting on Scope 3 emissions is nothing new and reporting costs are continuing to fall as it becomes more commonplace.** The first reporting and accounting standard - released by the Greenhouse Gas Protocol after extensive stakeholder and market input in 2011[35] - built on a decades long practice of identifying and engaging with value chains to increase business resilience. There are numerous tools and frameworks designed by designed by business bodies to interpret the GHG Protocol Standards on Scope 3 within their sector. Trade bodies like the recently launched Carbon Accounting Alliance[36] show the range of the Carbon Accounting options available to businesses. The Transition Plan Taskforce's 'gold standard' guidance for business disclosure also includes Scope 3 information in line with the ISSB reporting framework[37].

> **For many businesses, Scope 3 reporting is less intensive than expected.** PwC found that typically as much as 80% of an organisation's supply chain emissions come from as few as one-fifth of its purchases (at one public-sector agency, just 20 suppliers were responsible for 94% of the agency's

[32] TPT, 2023, **The Transition Plan Taskforce Disclosure Framework**

[33] ERM, 2022, **Costs and Benefits of Climate-Related Disclosure Activities by Corporate Issuers and Institutional Investors**

[34] TCFD, 2021, **Metrics, Targets, And Transition Plans Consultation**

[35] Greenhouse Gas Protocol, 2011, **Corporate Value Chain (Scope 3) Standard**

[36] BusinessGreen, 2023, **Carbon Accounting Alliance: Trade body formed to represent burgeoning sector**

[37] TPT, 2023, **The Transition Plan Taskforce Disclosure Framework**

Scope 3 emissions)[38]. Additionally, this means that engagement can be easier than expected once emissions hot spots have been identified.

Chapter Four: Post-Implementation Review

General questions

28 - Are the current SECR requirements targeted at the correct population of businesses (including LLPs)? If not, which types of businesses and of which size do you think the requirements should apply to? If you think that different requirements should apply to different populations of businesses, please specify.

> **Both large listed and non-listed companies should be required to disclose their Scope 3 emissions in order to create a level playing field across the economy for listed companies. This should accompany extending transition plan disclosure requirements to all large private companies in the UK to support transition and opportunity-catching** - As highlighted by Chris Skidmore MP's Independent Review of Net Zero, the transition to net zero is a whole economy transition[39]. Scope 3 disclosure requirements should be rolled out to large businesses across the economy regardless of whether they are listed or not to ensure an equitable playing field.

29 - SECR reporting is currently required within a company's annual report. Would it be more appropriate to report on SECR in another document or format?

> **Regardless of where the report is produced, there is a need to enhance data accessibility by ensuring consistency of response format and data tagging**. To enable accessibility, Scope 3 – and all - disclosure data should be accessible online. The use of consistent digital tags, formats and metrics will allow for more valuable aggregation and comparison and will support the training and reliability of AI tools which may in time be used to analyse aggregate corporate data. Digital tags should be aligned with ISSB guidance to ensure comparability. Putting data online and making it easy to access and use will be crucial to maximising its benefit. Beneficiaries of accessible online data will include market analysts, central banks and policymakers.

[38] PwC, 2022, **Tackling the Scope 3 challenge**

[39] HM Government, 2023, **Mission Zero: Independent Review of Net Zero**

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About E3G

E3G is an independent climate change think tank with a global outlook. We work on the frontier of the climate landscape, tackling the barriers and advancing the solutions to a safe climate. Our goal is to translate climate politics, economics and policies into action.

E3G builds broad-based coalitions to deliver a safe climate, working closely with like-minded partners in government, politics, civil society, science, the media, public interest foundations and elsewhere to leverage change.

More information is available at **www.e3g.org**