

Response from members of the UK Extractive Industries Transparency Initiative Civil Society Network (UK EITI CSN)¹ to the “[Consultation on requiring mandatory climate-related disclosures by publicly quoted companies, large private companies and Limited Liability Partnerships \(LLPs\)](#)”

May 2021

Dear Sirs

Thank you for the opportunity to submit comments on the proposed mandatory climate-related financial disclosures (CRFD) by publicly quoted companies, large private companies and Limited Liability Partnerships (LLPs).

The following response is made on behalf of the UK Extractive Industries Transparency Initiative Civil Society Network (UK EITI CSN) by civil society members of the UK EITI Multi-Stakeholder Group (MSG).

We are pleased that the UK is adopting these important disclosures and believe that this reporting initiative has the potential to furnish investors, civil society advocates and others with the information they need to engage in meaningful discourse with industry and government around climate related concerns. We have identified a number of areas where the disclosures could be strengthened and hope that the regulations may be a catalyst for change in current business practices in the UK and globally. While the CRFD will rightly apply to all sectors, our focus is on the extractive industries (oil, gas and mining), including fossil fuels.

Executive Summary

We have provided answers, where possible, to your detailed questions below but wish to bring your attention to the following important points which we regard as pervasive:

- We note that whilst the CRFD provide financial information to users they are treated in company law as equivalent to ‘non-financial information’ in the annual accounts. Whilst we note that making these disclosures mandatory is a progressive step we believe they should be given legal equivalence with financial disclosures. Whilst it seems a narrow point of principle, as we will explain below the status of non-financial information means CRFD are regulated less stringently where errors and omissions are made and are subject to a lower level of external assurance.
- We are very glad that ‘other stakeholders’ are considered as potential users of the proposed disclosures however we note the initiative is primarily designed to meet the needs of investors. Whilst we recognise that historically, as providers of capital and bearers of financial risk, investors have been given primacy as users of financial information, climate related risk poses an existential threat to society at large and so we would like to see these disclosures specifically designed and governed for a wider range of stakeholders, to include

¹ <https://www.ukeiti.org/multi-stakeholder-group>

specifically but not exclusively: local communities affected by company operations, employees, customers and supply chain partners.

- The lack of an external audit requirement undermines the validity of the reporting initiative. Whilst we appreciate that the disclosures fall under the ambit of the annual financial audit, to the extent that they must be 'consistent' with the statutory financial statements we do not believe that this form of indirect audit provides sufficient assurance for users. We would like to see a mandatory audit requirement for these disclosures . Cognoscente of our point above we would draw your attention to studies in the academic literature which support the notion that investors are more likely to use these types of disclosures where they are subject to external assurance checks².
- For extractive companies (oil, gas and mining), disclosures should be on a project-by-project basis. For other sectors, disclosures should be broken down country-by-country. This level of disaggregation is essential to providing investors and civil society with relevant information to assess risk and would be in line with tax and payment transparency efforts which are currently in place.
- For fossil fuel companies (oil, gas and coal), a breakdown of reserves by type and project is necessary to provide data on potential future emissions associated with these reserves. This emissions information is important for investors and civil society to understand the risks underlying these reserves if they are burned and the risk of stranded assets if they remain in the ground.

Please see below our responses to your specific questions. We would be happy to discuss any of these points further.

Faithfully,

UK EITI MSG Civil Society Members

Martyn Gordon, Robert Gordon University

Joe Williams, Natural Resource Governance Institute

Miles Litvinoff, Publish What You Pay UK

Simon Clydesdale, Global Witness

² See for example Reimsbach, D.; Hahn, R.; Gurturk, A. 2018. Integrated Reporting and Assurance of Sustainability Information: An Experimental Study on Professional Investors' Information Processing. *European Accounting Review*. 27(3): 559-581

Answers to Consultation Questions

QUESTION 1: Do you agree with our proposed scope for companies and LLPs?

- We would eventually like to see CRFD become mandatory for most organisations however we recognise that the compliance costs associated with this may be burdensome for small organisations. We recommend that disclosures made by currently proposed in scope companies are monitored and refined with a view to rolling these disclosures out to more entities in future.
- The regulations apply to UK registered companies but not companies registered overseas with their securities listed on UK markets. We would like to see overseas entities listed on UK markets brought within the scope of this legislation and believe that this would be in line with the UK's ambitions to lead in this area. By way of precedent we direct you to the requirements of the Reports on Payments to Governments Regulations 2014 which apply to extractive companies both registered in the UK and listed on the LSE Main Market.

QUESTION 2: Our proposed scope includes UK registered companies with securities admitted to AIM with more than 500 employees. Do you have any views on expanding this to include other unregulated markets and Multilateral Trading Facilities (MTFs)?

- As above we wish to see these requirements adopted widely and would urge the government to keep the scope of the regulations under constant review with a view to expanding it where proportionate.

QUESTION 3: Do you agree with the proposal to require climate related financial disclosures for companies and LLPs at the group level?

- Our considerable experience with reporting in the extractives sector suggests that disclosures are most useful to civil society users where they are disaggregated at least to a country-by-country level and, for the extractive sector on a project-by-project level. We are concerned that wide group-based disclosures may be so high level as to be meaningless for a large number of users. It is our opinion that greater granularity in reporting allows better engagement with the information from a user's perspective and the increased transparency provided may also encourage more positive behaviour from companies. Where companies (especially the largest most internationalised firms) are able to report on a global level there is considerable scope for obfuscation of facts within the aggregation of data. Whilst there may be no malicious intent on the part of the companies involved, the sheer scale of the operations of some companies make it inevitable that clarity will be lost in the process of consolidation. For the extractive sector, civil society and investors require project-by-project disclosure, including reserves for fossil fuel companies, to assess the viability of one particular project versus another.

QUESTION 4: Do you agree that the Strategic Report is the best place for the disclosure of climate-related financial information by companies?

- Whilst it may be appropriate to include the CRFD in a separate section of the annual report and accounts from the financial statements (and the strategic report may be an appropriate

location) as highlighted in our Executive Summary we believe that CRFD should be given legal equivalence with the statutory financial statements required by the Companies Act.

- Whilst we agree that mandating these disclosures and including them as part of the annual report and accounts is a progressive step we believe that the secondary status currently afforded CRFD as ‘non-financial information’ detracts from their importance and may impact the value ascribed to the CRFD by both companies reporting and stakeholders using the information.
- As noted in our answers to Q12-16 this is a fundamental point with regards to the strength of enforcement and audit requirements to which CRFD will be subject.

QUESTION 5: Do you have views on whether LLPs should be required to disclose climate-related financial information in the Strategic Report (where applicable), or the Energy and Carbon Report?

- Please refer to our answer to Question 4.

QUESTION 6: Do you agree that requiring disclosure in line with the four pillars of the TCFD recommendations, rather than at the 11 recommendation level is suitable?

- We believe companies should report on all 11 areas set out under the TCFD guidance. Whilst the four pillars are a good start these are wide areas which leave open considerable scope for interpretation. We recognise that some tailoring and firm specific factors will have to be accounted for in each individual company’s CRFD (as with any corporate report) however we believe the comparability and usability of CRFD will be seriously impacted if the scope of reporting is left too wide.
- For extractive companies (oil, gas and mining), disclosures should be on a project-by-project basis. For other sectors, disclosures should be broken down country-by-country. This level of disaggregation is essential to providing investors and civil society with relevant information to assess risk and would be in line with tax and payment transparency efforts which are currently in place.
- For fossil fuel companies (oil, gas and coal), a breakdown of reserves by type and project is necessary to provide data on potential future emissions associated with these reserves. This emissions information is important for investors and civil society to understand the underlying risks of these reserves if they are burned and risks of stranded assets if they are left in the ground. Reserves disclosure on GHG emissions is identified as a reporting metric by the TCFD as an illustrative example for energy companies.³ However, there is no widespread reporting by fossil fuel companies of this metric, including at the project level.

QUESTION 7: Do you agree that information provided in line with the obligations set out above would provide investors, regulators and other stakeholders with sufficient information to assess the climate-related risks and opportunities facing a company or financial institution?

- We appreciate that other stakeholders are mentioned in the proposed regulations; we note however that the CRFD in their current form are intended primarily as a tool for investors to

³ See: Implementing the Recommendations of the Task Force on Climate-related Financial Disclosures. Pages 54-55. Energy Group Metrics – illustrative examples. <https://assets.bbhub.io/company/sites/60/2020/10/FINAL-TCFD-Annex-Amended-121517.pdf>

assess risk. Whilst this is a positive and progressive step we see the potential for much broader and more transformative usage of these disclosures.

- If companies are only required to report on CRFD to the extent that the information is material from the perspective of an equity investor assessing risk, there is considerable scope to omit information which may be vital to other stakeholders affected by companies' operations.
- We propose that companies should have to report under the four pillars based on an assessment of the impact that their activities will have on a broad range of stakeholders, identifying those materially affected. For example, a North Sea oil company reducing production may report on the risk to investors of reduced returns in the future as they transition their business; however we believe that the employees of the company and local communities that depend on the industry have an equal right to be considered 'material' and that risks of job losses and strategies to manage a skills transition should be within the scope of the CRFD.
- Whilst we believe there is a strong moral argument for recognising a wider stakeholder base in the CRFD we also believe that this may benefit companies as well. As mentioned in the consultation these disclosures may help businesses to communicate with consumers, whose attitudes are increasingly impacted by climate related factors. We believe that the climate will become an evermore pressing concern and predictor of consumer behaviour and therefore that companies must consider the impact their operations have on the climate as a central part of their business model if they wish to maintain their consumer base and more widely their social license to operate.

QUESTION 8: Do you agree with our proposal that scenario analysis will not be required within a company or LLP's annual report and accounts?

- We believe that scenario analysis may provide users with very useful information and should in no way be precluded. We would highlight however that in order to provide accountability any scenario analysis must be accompanied by a thorough explanation of assumptions. Where scenario analysis is used we would encourage transparency on the part of companies who should give account in future years of whether anticipated scenarios have been realised.

QUESTION 9: Would alignment of the scope for climate-related financial disclosures and SECR requirements, such that large unquoted companies and LLPs would be subject to the same reporting requirements under SECR as quoted companies, aid reporting of climate related financial disclosures and simplify reporting procedures? Do you have any views on the continuation of voluntary Scope 3 emissions reporting under SECR requirements?

- We do not currently have views on the above.

QUESTION 10: Do you have comments on the proposal to permit non-disclosure if the information is not material and the reasons why climate change is not material are properly explained?

- We strongly oppose this suggestion. See our response to Question 7 above which outlines our proposal for a scope based on material impact to a wider range of stakeholders than currently proposed.

- As outlined above we believe that these disclosures should be given legal parity with the statutory financial statements. In order for this to be achieved it is essential that CRFD are mandatory.
- There is already a high volume of voluntary climate related corporate reporting, some of which has received criticism for being a form of marketing or ‘greenwashing’ rather than a valued source of information and accountability. The strength of the CRFD proposed is that they are mandatory and consistent and therefore provide users with comparable and reliable information and may also encourage companies to address areas of their operations which may not be so favourable to report on.

QUESTION 11: Do you have comments on the proposed timing for these regulations coming into force?

- We agree that the timeline is reasonable.

QUESTION 12: Do you have any comments regarding the existing enforcement provisions for companies and the BEIS proposal not to impose further provisions?

- In line with our previous comments we would like to see the CRFD given equal legal standing with the statutory financial statements under Section 4 of the Companies Act 2006 (CA2006), with fixed automatic penalties for failure to deliver CRFD and potentially criminal sanctions where CRFD are wilfully misleading.
- We believe the powers conferred in the current draft under s4A CA2006 are unlikely to compel any companies who do not wish to make full disclosures to do so. These powers rely on either shareholders or the secretary of state for business pursuing civil action through a court; a recourse which, in our view, is highly unlikely except in the case of an extremely egregious breach or omission.
- We question whether this light touch approach to regulation signals the secondary importance of CRFD and may undermine compliance.

QUESTION 13: Do you have any comments regarding duties and enforcement provisions for LLPs?

- Please see 12 above

QUESTION 14: Do you have any comments on the responsibilities of auditors in relation to climate-related financial disclosures?

- We believe the lack of positive external assurance undermines the validity of the regulations.
- Whilst we recognise the requirement to produce disclosures which are consistent with the audited financial statements and that this consistency will be measured within the ambit of the statutory audit, we have some reservations. Firstly, this type of assurance gives users no certainty that companies have applied the TCFD framework appropriately. Secondly, there may be instances where inaccurate CRFD may not be inconsistent with the financial statements and therefore may not come to the attention of auditors.
- We would reiterate our point in the executive summary that these types of disclosures are more likely to influence investors’ decision making where they are subject to assurance.
- From our review of companies in the extractives sectors we also note that many companies voluntarily provide a form of assurance over their corporate social responsibility reports. This

best practice exhibited by more progressive companies demonstrates a willingness and ability to submit to assurance over these types of disclosures and we believe shows the feasibility of an audit requirement.

- We would also draw to your attention to the EU Corporate Social Responsibility Directive, proposals for which include an audit requirement. We applaud the UK's ambitions to lead on climate relate disclosures but believe that the lack of an audit requirement may leave the CRFD lagging behind other global initiatives.
- Whilst we recognise that there is a wider debate over the role of auditors and that multiple initiatives are underway to examine how this must change (not least your own consultation) we believe that these disclosures are important and require a form of assurance if they are to be taken seriously by companies reporting and stakeholders relying on the information.

QUESTION 15: Do you have any comments regarding the proposed enforcement of our disclosure requirements?

- See Question 12 above.

QUESTION 16: Do you have any comments regarding the impact of our proposals on protected groups and/or how any negative effects may be mitigated?

NA

QUESTION 17: Do you have any further comments about our proposals?

NA

[End]