BEIS Consultation: Mandatory climate-related financial disclosures

ClientEarth Response

ClientEarth is a charity that uses the power of the law to protect people and the planet. We are international lawyers finding practical solutions for the world's biggest environmental challenges. From our offices in London, Brussels, Warsaw, Berlin, Madrid, Beijing, Luxembourg and Los Angeles, we work on laws throughout their lifetime, from the earliest stages to implementation and enforcement.

Top Lines

1. Despite clear investor demand, companies in the UK consistently fail to disclose material climate-related information to financial markets – likely breaching the law.
2. The Department of Business, Energy and Industrial Strategy's ("**BEIS**") proposals to enhance climate change-related disclosure obligations for publicly quoted companies, large private companies and LLPs are welcome, but inadequate. Unless the proposals are improved, they will not achieve the Government's objectives of mitigating climate change-related risks for companies and investors and smoothing the transition to net-zero. In particular, we are concerned that, although the consultation claims that its proposals introduce mandatory disclosures in line with the Task Force on Climate related Financial Disclosures' ("**TCFD**") recommendations, the content of the proposals do not make the disclosures mandatory in practice, and propose a standard of disclosure that differs from the TCFD's recommended disclosures.

3. To achieve its objectives, the Government must amend the proposed disclosure obligations to:
    a. require companies to disclose against each of the TCFD's 11 recommended disclosures in its July 2017 Final Report (the "**TCFD Recommended Disclosures**")[1];
    b. make the proposed disclosure obligations mandatory in practice, not just in name, and avoid a confusing 'comply or explain' approach;
    c. require companies to disclose a Paris-aligned strategy and financial accounts, with a credible plan for emissions reduction;
    d. provide financial regulators with effective accountability and enforcement powers;
    e. require auditors to provide assurance in relation to these disclosures; and
    f. expand the scope of the proposals to cover all companies that satisfy the criteria for large companies under the Companies Act 2006.

Background

4. It is now widely agreed that UK companies are failing to disclose material climate-related information.[2] This is despite clear and repeated assertions from investors, over many years, that consistent, comparable and high quality climate change-related information is highly material to their decision-making.[3] These continued disclosure failures undermine investors' ability to integrate climate-related information into their investment and stewardship decisions, increase financial stability risks and delay action to align the economy and financial system with the UK's commitment to achieve 'net-zero' greenhouse gas emissions by 2050,[4] as well as its emissions reduction targets in its nationally determined contribution under the Paris Agreement[5] and its sixth carbon budget.[6]
5. ClientEarth welcomes the proposals from BEIS to enhance climate change-related disclosure obligations for publicly quoted companies, large private companies and LLPs. However, in our view, in their current form, the proposals will fail to achieve their stated objectives. In order to provide investors, consumers and other stakeholders with the consistent, comparable and high quality climate-related information they need and expect, improvements must be made to the proposals in relation to content, application, accountability and enforcement.
6. This document sets out ClientEarth's response to the consultation questions.

[1] TCFD, 'Recommendations of the Task Force on Climate related Financial Disclosures: Final Report' (2017).
[2] For example, see ClientEarth, 'Accountability Emergency, A review of UK-listed companies' climate change-related reporting (2019-20)' (2021); FRC Reporting Lab, 'FRC Climate Thematic Review 2020' (2020).
[3] For example, see IIGCC, 'Institutional investors' expectations of corporate climate risk management' (2012).
[4] Section 1 Climate Change Act 2008.
[5] The Government's 'UK Nationally Determined Contribution' (2020) commits to reduce emissions by 68% (compared to 1990 levels) by 2030.
[6] The draft Carbon Budget Order 2021 (which is to be enacted pursuant to Part 1 of the Climate Change Act 2008) sets emission targets that imply a 78% reduction in emissions (compared to 1990 levels) by 2035.

Consultation Question Responses

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

7. We welcome that BEIS is proposing to expand the scope of companies that are required to make climate-related disclosures. However, we consider that the proposed scope for companies and LLPs is not sufficiently wide. As set out more fully below, we propose that the proposed scope should be expanded to also include UK registered companies and LLPs which meet the size criteria for large companies under the Companies Act[7] ("**CA Large Companies**"). In outline, this includes companies that satisfy two of the following three criteria: (1) turnover of more than £36 million; (2) balance sheet total of more than £18 million; and (3) more than 250 employees.

8. The consultation cites the Government's ambition for the UK to be a *"world-leader"* by making *"TCFD-aligned disclosures mandatory across the economy"*. However, BEIS' proposals lag behind current EU proposals for a Corporate Sustainability Reporting Directive ("**CSRD**")[8], which provide for detailed climate-related disclosures for all companies that meet the criteria for large companies under the Accounting Directive[9] (which are materially similar to the criteria for CA Large Companies), as well as listed small and medium sized companies (excluding micro-enterprises). The CSRD proposals recognise that companies meeting the thresholds for CA Large Companies can have a significant impact on the environment (regardless of whether they are listed) and that it is therefore appropriate for them to make climate-related disclosures.

9. BEIS' current proposals cover:

    a. UK companies with over 500 employees that are either: (1) traded on a regulated market; (2) banking companies; or (3) insurance companies.

    b. UK companies registered on AIM with over 500 employees.

    c. UK companies and LLPs that have over 500 employees and a turnover of more than £500 million.

10. We note that (c) above falls far short of the scope of the CSRD proposals, which would cover companies with only 250 employees and €40 million turnover. Despite BEIS' stated ambition to adopt a new regime that will apply *"across the economy"*, BEIS proposals are limited to companies with over 14 times the turnover compared to CSRD proposals. We consider that setting the thresholds at the levels currently proposed by BEIS would miss an opportunity to adopt a regime that effectively covers those companies across the economy that may have a material environmental impact.

11. We propose that the employee number threshold for (a) and (b) at paragraph 9 above is reduced from 500 to 250 (in line with the employee number threshold for CA Large Companies), and that (c) is replaced by companies and LLPs that meet the size thresholds for CA Large Companies (as defined at paragraph 7 above).

---

[7] Being companies that do not meet the size criteria for medium-sized companies set out at section 465 to 467 Companies Act 2006.

[8] See European Commission, Proposal for a Directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (2021).

[9] See Article 3 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, which provides that an undertaking is large is it satisfies two of the following three criteria: (a) turnover more than €40 million; (b) balance sheet total more than €20 million; and (c) more than 250 employees.

12. Imposing requirements to disclose in line with TCFD recommendations would not impose an undue burden on CA Large Companies, as the TCFD recommendations are a principles-based framework, which provide flexibility for issuers to disclose in a way that is proportionate to their size and circumstances. Furthermore, quoted companies and CA Large Companies are already required to disclose certain information on emissions and energy usage under the Streamlined Energy and Carbon Reporting regime ("**SECR**"), and will therefore already be collecting data on their climate impact in any event. In addition, our proposals would simplify the regime by bringing the scope of SECR and the TCFD disclosure regime into closer alignment. See also our response to question 9 in relation to SECR.

13. It is important that BEIS legislates to introduce requirements for CA Large Companies now, in order to incentivise such companies to develop their capabilities and data for reporting. BEIS proposals are intended to take effect for accounting periods starting on or after 6 April 2022. To the extent that BEIS considers that CA Large Companies may need additional time to plan and improve their capabilities for climate-related disclosures, it could introduce a phased introduction, with an expansion to include all CA Large Companies within scope for accounting periods starting in April 2023. This would match the EU's proposed timeline for introducing requirements for large companies under CSRD, which it anticipates will cover the financial year 2023. BEIS' consultation states that *"BEIS will review the case for expanding the scope of the regulations in 2023"*, which would likely mean that any further expansion would not take effect until accounting periods starting in 2025. However, the proposal to consult in 2023 does not provide sufficient certainty to companies as to whether they will be included in any future expansion of scope, and is too far in the future to incentivise companies to start improving their capabilities now. The next decade is crucial for climate action, so it is important that there is no unnecessary delay in companies improving their assessment and reporting of climate-related risks, opportunities and impact.

14. We agree that small and medium sized companies (as defined in the Companies Act 2006) can be excluded from the scope of the current legislative proposals, although it may be proportionate to extend the scope to such companies in future, when capabilities and industry best-practice for climate-related disclosures have further developed. However, we recognise that small and medium sized companies in certain sectors (such as energy or mining) can have a significant environmental impact, such that it may be appropriate for them to be required to make climate-related disclosures at this stage. We would therefore support BEIS exploring potential options to include any small and medium sized companies within sectors with a high potential environmental impact within the scope of these proposals.

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)?

15. See our response to question 1 on the scope of BEIS' proposals.

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

16. Consolidated group level climate-related financial disclosure could potentially lead to some companies or LLPs excluding information (such as climate-related risks or opportunities) from the consolidated disclosure which would be material to the resilience of subsidiaries, on the basis that they are not deemed material at the group level. This would deprive investors in such subsidiaries of relevant material information. Additionally, group level disclosures on climate strategies could potentially omit material information on the strategies for subsidiaries, where they differ from the group level strategy.

17. Accordingly, if climate-related financial disclosures for companies and LLPs are to be introduced at the group level, then the consolidated disclosure should include any information that would be deemed material to any subsidiaries which would themselves meet the scope criteria. See also our response to question 10 below on materiality. In addition, group level disclosures on climate transition strategies may in some cases need to set out specific strategies for individual subsidiaries or geographies, in order to reflect their different circumstances and account for their particular risks and opportunities. See also our response to question 7 below on disclosure of Paris-aligned strategies.

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

18. We agree that the strategic report is an appropriate place for the disclosure of climate-related financial information by companies. In addition, in order to assist investors in understanding the impact of climate-related risks and opportunities, the strategic report should identify and cross-refer to any line items or notes in the financial statements that directly relate to matters set out in the climate-related financial disclosures (such as relevant assumptions, asset impairments, provisions or contingent liabilities). See also our response to question 7 in relation to preparing Paris-aligned accounts.

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?

19. We do not agree. In the consultation document, BEIS asserts that it has aligned its proposals with the TCFD recommendations, by requiring disclosures under the four pillars proposed by the TCFD ('Governance', 'Strategy', 'Risk Management' and 'Metrics & Targets'). In its more detailed section on the proposed obligations, BEIS then suggests that companies will be required to disclose information under each of these headings, but proposes specific disclosure requirements which vary significantly from the 11 TFCD Recommended Disclosures set out in the TCFD's June 2017 Final Report. BEIS also specifically notes that one of the key TCFD Recommended Disclosures, relating to scenario analysis, will not be required. This approach would be a mistake. Companies must be required to disclose against the eleven TCFD Recommended Disclosures. This is because:

    a. The 11 TCFD Recommended Disclosures have become the base-line industry standard for disclosing material climate-related information, and are now widely used and understood (including by investors, for whom this information is vital).

    b. Replacing the 11 TCFD Recommended Disclosures with new and different disclosure obligations, while asserting that they are nonetheless aligned with the TCFD, will create significant confusion for preparers and users and undermine existing market practice, guidance and consistency with disclosures in other jurisdictions.

    c. BEIS' new disclosures appear to be intended to set a lower standard for disclosure than the 11 TCFD Recommended Disclosures. Signalling a move towards lower disclosure standards at this stage would be a regressive step. It is unclear from the consultation why BEIS considers that large companies would not be able to comply with the 11 Recommended Disclosures, as it does not identify any difficulties with providing those disclosures (save that it claims there is a *"skill and expertise gap"* in relation to scenario analysis).

    d. The TCFD Recommended Disclosure in relation to scenario analyses is not prescriptive about the level of detail of analyses that is required and allows for a proportionate approach to be taken that will not place an undue burden on companies. In addition, mandating that companies have to

undertake scenario analysis will incentivise companies to develop their capabilities for scenario analysis over time. Furthermore, conducting scenario analysis is a vital tool to enable companies properly to assess their climate-related risks and opportunities and set their climate strategy, and so removing the requirement for scenario analysis will lower the standard of other disclosures made by companies.

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?

20. We do not agree. As set out in our response to question 6, the new disclosure obligation should explicitly reference the 11 TCFD Recommended Disclosures. In addition, as set out below, the proposed disclosure obligation should be amended to require issuers to also disclose a Paris-aligned[10] strategy and financial accounts. Furthermore, we would support BEIS exploring proposals for investors to be provided with an annual advisory non-binding 'say-on-climate' vote to express approval or disapproval with a company's strategy.

21. We note that FCA Listing Rules 9.8.6(8) and 9.8.7 (which set obligations in respect of climate-related financial disclosures for all UK listed companies and for overseas premium listed companies) do not require companies to disclose Paris-aligned strategies or accounts. We would support the FCA adopting equivalent requirements to those proposed below, in its Listing Rules.

Disclosure of a Paris-aligned strategy

22. A mandatory requirement for companies to align their reporting with the TCFD Recommended Disclosures is a necessary starting point to ensuring better quality climate-related disclosures. However, on its own, this will not be sufficient to provide the material information that investors now assert is relevant to their decision-making. In order to adequately meet investors' current and emerging needs, BEIS must amend the proposal to additionally require companies to disclose a Paris-aligned strategy which sets out a credible plan to reduce emissions consistent with the best available science (which we refer to as "**TCFD+**"), as well as Paris-aligned financial accounts. This is because:

    a. The urgency of the climate emergency and escalating government action mean that investor information needs and company disclosures have evolved beyond the TCFD framework.[11]

    b. Investors are now demanding disclosures about companies' strategic alignment with the Paris Agreement objectives, including sector specific short term (i.e. up to 2025) and medium term (i.e. up to 2035) greenhouse gas emission reduction targets for scopes 1-3, and capital expenditure plans and accounts aligned with these targets.[12]

---

[10] I.e. consistent with the goals of the Paris Agreement under the United Nations Framework Convention on Climate Change. In particular, Article 2.1.a sets the goal of *"Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above preindustrial levels"*.

[11] For example, see Climate Action 100+, 'Net-Zero Company Benchmark' (2020); Transition Pathway Initiative, 'TPI State of Transition Report 2021' (2021); ISS, 'Climate & Voting – 2020 Review and Global Trends' (2021).

[12] For example, see UNFCCC, 'Race to Zero' (2020); UNEPFI, 'Net-Zero Asset Owner Alliance'; Sarasin & Partners, 'Paris-aligned accounting is vital to deliver climate promises' (2020); Carbon Tracker, 'When Capex met climate'. Climate Action 100+, 'Net-Zero Company Benchmark' (2020).

c. Unequivocal assertions by investors that such information is relevant to their investment and stewardship decision-making mean that it is material for all large companies and must be disclosed.[13]

d. Failure to reflect this reality in the new disclosure obligations will cause confusion for companies, undermine investor efforts to secure material information to guide their decision-making, and create costly inconsistency with new EU requirements which will require such disclosures.[14]

23. There is considerable support from companies and investors for Paris-alignment. By way of example:

a. Over 800 companies globally have publicly committed to pursuing scientifically informed emission reduction targets under the Science Based Targets Initiative.[15]

b. Investors with over $4.6 trillion assets under management have signed up to the Net-Zero Asset Owner Alliance and committed to transition their portfolios to net-zero GHG emissions by 2050.[16]

c. Over 130 of the world's biggest banks ($47 trillion) have committed to the Principles for Responsible Banking, to align their financing with the Paris Agreement goals.[17]

d. Institutional investors are increasingly bringing AGM resolutions, requiring companies to set and report against Paris-alignment targets, and have recently sent a letter to the largest corporate emitters calling for firms to commit to net-zero strategies.[18]

e. The Institutional Investors Group on Climate Change ("**IIGCC**", which has 250 members across 16 countries with over €33 trillion in assets under management) has indicated that it expects firms to prepare Paris-aligned financial accounts and has detailed the steps companies should take in doing so.[19]

f. Over 160 firms from across the financial sector (together responsible for assets in excess of $70 trillion) have signed up to the Glasgow Financial Alliance for Net-Zero, which supports the transition to net-zero emissions by 2050 at the latest.[20]

24. In addition, the Advisory Group on Finance for the UK's Climate Change Committee recommended in 2020 that the UK should commit to being a net-zero financial system and that it be mandatory for all financial institutions to adopt targets and plans for net-zero emissions by 2050.[21]

25. The above examples provide clear evidence that expectations regarding climate-related disclosures have now moved beyond the TCFD Recommendations. As investors increasingly attempt to mitigate systemic climate risks (i.e. risks that climate change poses to the stability of the financial sector as a whole), such disclosures are now widely being used in asset allocation and stewardship decisions, and

---

[13] For example, see Climate Action 100+; S&P Global, 'BlackRock voted against management at 53 companies over climate concerns' (2020); Nest, 'Nest going net-zero to support green recovery' (2020).
[14] See European Commission, Proposal for a Directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (2021).
[15] See https://sciencebasedtargets.org/.
[16] See https://www.unepfi.org/net-zero-alliance/.
[17] See https://www.unepfi.org/banking/bankingprinciples/.
[18] See https://climateaction100.wpcomstaging.com/news-and-events-2/ and 2 Degrees Investing Initiative, 'Passing the Baton'.
[19] IIGCC, 'Investor Expectations for Paris-aligned Accounts' (2020).
[20] See COP25 and COP26 Champions, Press Release (2021).
[21] Advisory Group on Finance for the UK's Climate Change Committee, 'The road to Net-Zero Finance' (2020).

are therefore material.[22] BEIS must therefore clarify and explicitly require that such information be disclosed as part of the proposed new disclosure obligations.

26. While currently there are a wide variety of frameworks and methodologies being used by companies in order to set Paris-alignment or net-zero targets, the lack of a single market standard should not be used as an excuse for inaction. Numerous initiatives are now underway to standardise and consolidate the different approaches being used, and Climate Action 100+ (representing $54 trillion investments) has issued a Net-Zero Company Benchmark[23] which provides a framework to assess companies' climate strategies. In the interim, some flexibility can be permitted to allow issuers to select the most appropriate approach for their business, as long as assumptions are reasonable, evidence-based and transparently disclosed. ClientEarth's 2020 Position Paper on Principles for Paris-alignment provides an example of a flexible and principles-based form of disclosure obligation which could be adopted, while standards and methodologies continue to develop.[24]

27. We propose that BEIS issues detailed guidance on the setting of Paris-aligned strategies, in order to assist companies in preparing credible strategies and to provide clarity as to the standard against which companies will be held by the FRC and PRA. At a minimum (and as set out in more detail in our Position Paper on Principles for Paris-alignment), we would expect any disclosed Paris-aligned transition strategy to be required to include:

    a. A credible strategy to align the company's business with global warming not exceeding 1.5°C with low or no overshoot,[25] consistent with the best available science. This must include reductions in the company's scope 1, 2 and 3 emissions (including emissions from investments and, for insurers, emissions from projects and companies that they underwrite – see our response to question 9 on scope 3 emissions). In addition, the strategy must not unreasonably rely on unproven or uncosted emissions reduction technology. BEIS should issue guidance for companies to assist them in setting credible strategies and in understanding the best available science. Currently, the best available science indicates that limiting warming to 1.5°C requires achieving global net-zero emissions by 2050 at the latest (although this will be earlier for certain sectors and countries).[26]

    b. Interim five yearly emission reduction targets.

    c. The company's underlying methodologies for setting targets and measuring progress (including detailing any material assumptions and uncertainties in those methodologies).

28. In addition, the disclosures on governance should allocate responsibility for implementing the transition strategy to specific individuals within the company, and set out a remuneration policy that incentivises senior managers to implement the company's transition strategy and to meet the targets.

29. We note that, if BEIS does not include a requirement to disclose Paris-aligned strategies within its proposals, it will fall behind the EU regime in this regard. The CSRD proposals will require in scope companies to disclose their plans to ensure that their business model and strategy are compatible with

---

[22] See for example, Climate Action 100+, Investor Signatories; S&P Global, 'BlackRock voted against management at 53 companies over climate concerns' (2020); Nest, 'Nest going net-zero to support green recovery' (2020).
[23] Climate Action 100+, 'Net-Zero Company Benchmark' (2020).
[24] ClientEarth, 'Principles for Paris-alignment' (2020).
[25] Falling within the IPCC's Pathway *"1.5°C-low-OS"* outlined at Chapter 2 of the IPCC 'Special Report: Global Warming of 1.5 ºC' (2018).
[26] *Ibid.* Note that Chapter 2 of the IPCC Special report finds that *"[Carbon dioxide reduction] deployed at scale is unproven, and reliance on such technology is a major risk in the ability to limit warming to 1.5°C"*.

the transition to a sustainable economy and with the limiting of global warming to 1.5°C, in line with the Paris Agreement. Given BEIS' stated intention to be a *"world-leader"* in this field, we urge BEIS to at least keep pace with CSRD proposals and mandate the disclosure of Paris-aligned strategies.

Paris-aligned accounts

30. It is vital that the requirement to disclose Paris-aligned strategies is supplemented by a requirement for companies to disclose Paris-aligned accounts (including the climate-related assumptions on which those Paris-aligned accounts have been prepared). Failure to reflect climate risks and opportunities in company accounts will result in inaccurate cost and return information (for example, failing to reflect asset impairments), meaning that both company directors and investors will make decisions based on inaccurate information. In addition, companies will be unable to set credible Paris-aligned strategies without such information. However, currently, companies are largely failing to align their accounts with the goals of the Paris Agreement, even where they disclose climate risks in line with the TCFD's recommendations.[27]

31. The IIGCC (which represents over €33 trillion in assets under management) has set out investor expectations on Paris-aligned accounts.[28] We propose that this could serve as a basis for BEIS or FRC to produce their own guidance on Paris-aligned accounts. In outline, the IIGCC expectations require: (1) an affirmation that the accounts are Paris-aligned; (2) adjustments to assumptions and estimates to ensure that they are Paris-aligned; (3) disclosure of the results of sensitivity analysis to variations in those assumptions and estimates; (4) disclosure of the implications of Paris-alignment to dividend paying capacity; and (5) confirmation of consistency between narrative reporting on climate risks and the accounting assumptions.

'Say on climate' vote

32. Many investors and NGOs have called for there to be an advisory vote at company AGMs on the adequacy of company climate change strategies and targets.[29] This approach has been advocated for by the UK Investor Forum, which represents members with over £20 trillion assets under management.[30]

33. As set out above, we consider that companies should be legally required to disclose Paris-aligned strategies and accounts. Under such a regime, companies that failed to disclose credible transition strategies would be subject to scrutiny and potential enforcement from regulators, and their directors could potentially be liable to claims by shareholders. However, we consider that it would be beneficial for this regime to be supplemented by a separate market-led accountability mechanism for investors to publicly signal their approval or disapproval of a company's climate change-related disclosures and emission reduction strategy. This could provide an effective mechanism for investors to hold companies to account that fail to adopt and disclose credible Paris-aligned strategies and could help to mitigate the risk of greenwashing (which is an increasing concern for investors and other stakeholders). Currently, shareholders must requisition resolutions at every company in order to hold such a vote at its AGM, which is highly inefficient and costly.

[27] IIGCC, 'Investor Expectations for Paris-aligned Accounts' (2020).
[28] *Ibid.*
[29] See CIFF, 'Say on Climate: Shareholder Voting on Climate Transition Action Plans'; Reuters, 'Show us the plan: Investors push companies to come clean on climate' (2021); Unilever 'Press release why we are putting our climate plans to a shareholder vote' (2021).
[30] Investor Forum, 'Say on Climate: An opportunity to deliver impact in the UK' (2020).

34. Accordingly, we would be supportive of BEIS exploring ways to introduce advisory 'say on climate' votes. However, we consider that there is a risk that companies may seek to rely on shareholder approval in such votes as evidence that their climate strategies are adequate, in circumstances where their transition strategies are in fact not credible or not consistent with the best available science, or otherwise fail to meet any legal or regulatory standards. This would undermine the purpose of introducing such votes. Accordingly, if advisory 'say on climate' votes were to be introduced, they would need to be subject to appropriate and effective safeguards to ensure that positive votes do not serve to absolve companies or directors of any legal or regulatory duties (including in respect of the new obligations to disclose Paris-aligned strategies and accounts), nor to ratify directors' actions under section 239 Companies Act 2006. Furthermore, regulators (including the FRC and PRA) must be obliged to take appropriate action against companies which disclose strategies that are inadequate, and should not rely on the fact that a company's strategy has been approved at a shareholder vote as a reason for adopting a lower standard of scrutiny.

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?

35. We do not agree. See our answer to question 6.

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?

36. We agree that large unquoted companies and LLPs (which are currently subject to lower requirements under SECR than quoted companies) should be subject to the requirements currently imposed on quoted companies under SECR, and propose that disclosure of scope 3 emissions should be mandatory under SECR.

37. Currently, the SECR disclosure requirements for large unquoted companies do not include the following (all of which are required for quoted companies): (1) emissions and energy usage from outside the UK; (2) any scope 1 emissions other than from combustion of fuel for the purposes of transport or from combustion of gas; and (3) scope 2 emissions from heat, steam and cooling. As a result, the SECR disclosures for large unquoted companies will omit significant elements of their emissions and energy usage.

38. The SECR requirements for quoted companies should be extended to apply to large unquoted companies, as:

    a. This would provide an incentive for such companies to reduce their emissions and energy usage, and would also provide investors in such companies with better quality climate-related information that is consistent and comparable with information for quoted companies (which may help to encourage investment in unquoted companies).

    b. This would provide comprehensive information on emissions that is vital in order for the UK Government to meet its commitment to achieve a net-zero emissions economy by 2050 in the Climate Change Act 2008 and the UK's carbon budgets set under that Act.

    c. Now is an appropriate time to expand the SECR disclosure requirements. The SECR regulations were issued in 2018 and came into force for financial years beginning from April 2019. Companies

have had time to develop their data and capabilities to comply with the existing requirements, and it is proportionate to increase the requirements at this stage.

39. For the same reasons, we propose that disclosure of scope 3 emissions should be made mandatory under SECR. This should include emissions of investments and financing activities, such as lending. For insurers, this should also include emissions from projects and companies that they underwrite.[31] Scope 3 emissions are the largest source of a company's emissions in most sectors,[32] so disclosing only scope 1 and 2 emissions provides only an incomplete picture of a company's climate impact. By way of example, it is estimated that the scope 3 emissions of oil and gas companies are six times their scope 1 and 2 emissions,[33] and that the portfolio emissions of global financial institutions are over 700 times greater than their operational emissions.[34]

40. The current system of voluntary scope 3 disclosures is not working, as companies are largely choosing not to disclose. Two thirds of FTSE 250 companies do not disclose their scope 3 emissions, and those that do are often not fully transparent about the methodology and exclusions they have applied in their calculations.[35] As a consequence, many companies' net-zero commitments do not include scope 3 emissions.[36] Not only does this render the commitments less effective, but it also risks giving a misleading impression to investors and the public as to companies' climate goals. Mandating disclosure of scope 3 emissions is necessary in light of the current failure of companies to do so voluntarily, and in order to ensure consistency and transparency in approach.

41. We recognise that collecting data on scope 3 emissions has some challenges, as they are sometimes outside of a company's ownership and control. However, given the significance of scope 3 emissions, this is not a good reason for inaction. Guidance is available for disclosing scope 3 emissions,[37] which could be supplemented by further guidance from BEIS. Any such guidance from BEIS could take a proportionate approach which recognises that companies will develop and improve their data over time. In addition, if the emissions disclosure requirements for large unquoted companies are enhanced (as proposed above), then this will provide more emissions data across supply chains and therefore make it easier for companies to assess their scope 3 emissions.

---

[31] See ClientEarth, 'Response to HM Treasury Call for Evidence on Review of Solvency II' (2021), which sets out why insurers should be required to align their businesses with the goals of the Paris Agreement (including scope 3 emissions from their underwriting portfolios).

[32] Science Based Target Initiative, 'Value Change in the Value Chain: Best Practices in Scope 3 Greenhouse Gas Management' (2018).

[33] MSCI, 'Scope 3 Carbon Emissions: Seeing the Full Picture' (2020).

[34] CDP, 'Financial Services Disclosure Report 2020: The Time to Green Finance' (2020). This report also identified that only 25% of financial institutions reporting to CDP disclosed their financed emissions, and only 27% of insurance companies are taking steps to align their underwriting portfolios with limiting warming to 2°C.

[35] ClientEarth, 'Accountability Emergency, A review of UK-listed companies' climate change-related reporting (2019-20)' (2021).

[36] The Climate Action 100+ Company Net-Zero Benchmark evaluated the climate disclosures of 159 of the world's largest emitters. It found that 52% of companies announced an ambition to achieve net-zero by 2050 or sooner, but only 53% of those companies (28% of the total companies in scope) included scope 3 emissions. See https://www.climateaction100.org/news/climate-action-100-issues-its-first-ever-net-zero-company-benchmark-of-the-worlds-largest-corporate-emitters/.

[37] For example, see Science Based Target Initiative, 'Value Change in the Value Chain: Best Practices in Scope 3 Greenhouse Gas Management' (2018); GHG Protocol, 'Technical Guidance for Calculating Scope 3 Emissions' (2013). In relation to investments, see IIGCC, 'Net-Zero Investment Framework' (2021); Net-Zero Asset Owners Alliance 'Inaugural 2025 Target Setting Protocol' (2021); COP26 Private Finance Hub Portfolio Alignment Team 'Measuring Portfolio Alignment' (2021).

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?

42. We do not agree with the proposal. The title and introductory explanation in the consultation appear to convey an intention to make the new requirements to report in line with TCFD recommendations 'mandatory'. However, the actual contents of the consultation propose a far weaker 'comply or explain' approach, whereby a company can decide not to provide the required disclosures, if it decides that *"climate change is not expected to materially affect the company's business model or strategy"*. This weak approach to the application of the new obligations would be a mistake. Investors have been clear that detailed climate change-related information is material for all companies. Adopting a weak 'comply or explain' approach provides an excuse for companies to delay compliance, will waste investors' time with arguments about materiality, and undermines effective accountability and enforcement by regulators. This would lead to slow implementation, lower quality disclosures with greater scope for 'greenwash', and increased uncertainty for companies, investors, and consumers.

43. The obligation to provide disclosure under each of the 11 TCFD Recommended Disclosures must be introduced on a clear mandatory basis (although the individual risks and opportunities that are disclosed under that framework would still be subject to a test of materiality). This is because:

    a. Investors expect issuers to use the TCFD recommendations to provide material climate-related information to satisfy existing disclosure requirements, and hundreds of companies now do so.[38]

    b. The UK government has committed to achieving a net-zero emissions economy by 2050 in the Climate Change Act 2008 and is legislating for a sixth carbon budget that equates to a 78% reduction in emissions (compared to 1990 levels) by 2035. In light of this, all companies will need to align with the required rapid reduction in emissions (both in the short term and the long term). This will only be possible if all large companies actively consider (and disclose) their climate transition strategies, governance arrangements, risk management systems and targets, and do not seek to rely on any exemption for supposed immateriality to avoid proper consideration of these issues.

    c. The TCFD recommendations are a principles-based framework, which provide flexibility for issuers to disclose in a proportionate way, so concerns about any undue burden are unfounded. In addition, although companies would be required to provide disclosure under each of the 11 TCFD Recommended Disclosures, the individual risks and opportunities that are disclosed would still be subject to a test of materiality.

    d. Existing laws protect companies and directors from frivolous or unfounded litigation in respect of good faith climate-related disclosures. Conversely, a confusing 'comply or explain' approach may lead to material omissions, increasing legal risk and uncertainty.[39]

44. In addition we propose that, when assessing whether a particular risk is material, companies must be required to consider not only whether the risk is material to the company's performance, but also whether it may have a material impact on people or the environment (referred to as the concept of *"double materiality"* in the CSRD proposals). Without such a rule, companies might focus only on risks that are material to their performance. However, risks that have a material impact on people or the

[38] For example, see BlackRock, 'Statement of engagement priorities for 2017-2018'; Bill McNabb, 'An open letter to directors of public companies worldwide'; LGIM, 'Time to act on climate change: engagement with consequences' (2016).
[39] See CCLI, 'Concerns misplaced: Will compliance with the TCFD expose directors to liability risk?' (2017).

environment will be of importance to investors that wish to invest in environmentally and socially responsible businesses, and companies will need to disclose and manage such risks if the UK is to meet its climate goals.

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

45. See the comments in our response to question 1 in relation to timing.

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

46. In ClientEarth's view, the biggest barrier to better climate change-related reporting in the UK is the current enforcement and accountability gap.[40] In recent years, ClientEarth has made numerous complaints to the FCA and FRC regarding companies' failures adequately to disclose material climate-related information under existing disclosure laws.[41] In all cases, the reported companies were in high-risk sectors but disclosed no meaningful information about climate change-related risks in their annual reports. Despite this evidence, the FRC and the FCA took no public enforcement action. We believe that failures by the FRC and FCA to enforce the law (and be seen publicly to enforce the law) severely undermines investor demands for market-wide, decision useful climate change-related information, and that their existing powers and resources are insufficient.

47. The consultation briefly notes some of the existing general accountability and enforcement mechanisms. In our experience, these are highly inadequate. Currently, the FRC has no meaningful powers to hold companies or their directors directly accountable for failures to disclose material information to shareholders, be that related to climate change, or otherwise. The power of the Secretary of State or the FRC to apply to the court for an order requiring the preparation of revised accounts or reports is weak, costly and procedurally difficult. To the best of our knowledge, it has never been used. We welcome that BEIS has acknowledged that the FRC lacks the necessary powers to hold auditors and directors sufficiently to account, and is currently consulting on replacing the FRC with a new Audit, Reporting and Governance Authority ("**ARGA**") which would have enhanced powers.[42] While the FCA has somewhat more effective enforcement powers at its disposal, so far, it has been very reluctant to use them, and they only apply to listed companies.

48. The UK's weak enforcement framework has been criticised directly by the European Securities and Markets Authority ("**ESMA**") in its Peer Review Report on Enforcement of Financial Information.[43] The lack of powers and resources is also highly anomalous compared to other jurisdictions. Corporate reporting regulators in the US, Australia, Canada and across Europe all have direct powers to require reporting restatements and hold companies and directors accountable for breaches.[44] In order to ensure that companies and their directors are appropriately incentivised to provide fair, balanced and material climate change-related information to investors and other stakeholders, and to minimise increasing risks of greenwashing, the FRC (or ARGA) and FCA must be provided with powers to

[40] See ClientEarth, 'Accountability Emergency, A review of UK-listed companies' climate change-related reporting (2019-20).
[41] For example, see ClientEarth, 'Insurance firms could face fines over climate reporting failure' (2018).
[42] BEIS, 'Restoring trust in audit and corporate governance: consultation on the government's proposals' (2021).
[43] ESMA, 'Peer Review on guidelines on Enforcement of Financial Information' (2017) at paragraph 74.
[44] See, in particular, new penalties and enforcement powers for EU regulators in the proposed CSRD: European Commission, Proposal for a Directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (2021)

require restatements and hold companies and their directors to account for providing inadequate or misleading disclosures, and given adequate resources to do so. We welcome that BEIS is proposing (in its separate consultation in relation to ARGA) that ARGA has a new power to direct changes to company reports and accounts without obtaining a court order and has increased powers to hold directors to account, and we would support enhanced powers in both those areas.

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

49. In ClientEarth's recent review of reporting by the 250 largest listed UK companies, we found that just 4% of audit reports clearly referred to whether or not the auditors had considered climate change-related factors in conducting their audit.[45] In light of clear demands from investors for companies to align their accounts with the Paris Agreement goals and for auditors to take this into account in their audits, this is a serious shortcoming that must be rectified.[46]

50. The consultation document notes the role of auditors in providing assurance in relation to company financial statements and the opinions that they are required to provide regarding 'other information' included within the annual report. It also notes that it is not intending to alter the role of auditors in relation to climate-related financial disclosures. Given clear failings by auditors under current requirements, this would be a mistake. In order to provide investors and other stakeholders with confidence they need in climate change-related disclosures, auditors must ultimately be required to provide an integrated audit over the entire annual report, including any new disclosure requirements arising as a result of this consultation. As an interim step, at the very least, auditors must be required to provide 'a limited assurance' opinion in relation climate-related disclosures included in the strategic report,[47] and to specifically test accounts against Paris-aligned assumptions and estimates and flag to shareholders where the assumptions fall short.[48]

[45] ClientEarth, 'Accountability Emergency, A review of UK-listed companies' climate change-related reporting (2019-20).
[46] IIGCC, 'Investor Expectations for Paris-aligned Accounts' (2020).
[47] As proposed at the EU level, see: European Commission, Proposal for a Directive amending Directive 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) No 537/2014, as regards corporate sustainability reporting (2021)
[48] As proposed by leading investors, see: IIGCC, 'Investor Expectations for Paris-aligned Accounts' (2020).

Joanne Etherton

Solicitor, Climate Finance Lead

jetherton@clientearth.org

www.clientearth.org

Dan Eziefula

Solicitor, Climate Finance team

deziefula@clientearth.org

www.clientearth.org

This document was written for general information and does not constitute legal, professional, financial or investment advice. Specialist advice should be taken in relation to specific circumstances. Action should not be taken on the basis of this document alone. ClientEarth endeavours to ensure that the information it provides is correct, but no warranty, express or implied, is given as to its accuracy and ClientEarth does not accept responsibility for any decisions made in reliance on this document.

Brussels **Beijing** **Berlin** **London** **Warsaw** **Madrid** **Los Angeles** **Luxembourg**

ClientEarth is an environmental law charity, a company limited by guarantee, registered in England and Wales, company number 02863827, registered charity number 1053988, registered office 10 Queen Street Place, London EC4R 1BE, a registered international non-profit organisation in Belgium, ClientEarth AISBL, enterprise number 0714.925.038, a registered company in Germany, ClientEarth gGmbH, HRB 202487 B, a registered non-profit organisation in Luxembourg, ClientEarth ASBL, registered number F11366, a registered foundation in Poland, Fundacja ClientEarth Poland, KRS 0000364218, NIP 701025 4208, a registered 501(c)(3) organisation in the US, ClientEarth US, EIN 81-0722756, a registered subsidiary in China, ClientEarth Beijing Representative Office, Registration No. G1110000MA0095H836. ClientEarth is registered on the EU Transparency register number: 96645517357-19. Our goal is to use the power of the law to develop legal strategies and tools to address environmental issues.