ecometrica

Technical Paper | Carbon Reporting in Directors' Reports

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Authors: Luke Harris[1] and Matthew Brander
Internal Reviewers: Gary Davis and Richard Tipper

Executive Summary

Carbon reporting is likely to become a standard feature of company annual Directors' Reports, either on a voluntary or mandatory basis. In the UK, the Climate Change Act (2008) tasks the government with introducing mandatory greenhouse reporting in Directors' Reports[2]. This paper sets out how greenhouse gas emissions can be included in company annual reporting, and how the financial liabilities associated with greenhouse gas emissions can be shown in a company's balance sheet. Ecometrica has used this reporting approach in its own 2010 Directors' Report, and has found this to be a simple undertaking which does not significantly add to the administrative burden of providing annual accounts. This paper is accompanied by a freely available template which can be used by other companies that wish to include their greenhouse gas emissions in their annual Directors' Reports.

Key terms: carbon accounting, carbon reporting.

[1] Contact Luke.Harris@ecometrica.co.uk
[2] Part 5, Section 85 of the UK Climate Change Act (2008). The government must introduce regulations under the Companies Act 2006 by 6th April 2012, or report to parliament on why the regulations have not been introduced.

Introduction

Carbon reporting involves quantifying the greenhouse gas emissions associated with a company's activities, and making a public statement of the result. There are a number of strong reasons for integrating carbon reporting with financial reporting, e.g. in annual Directors' Reports. Greenhouse gas emissions are increasingly associated with financial liabilities, for example through voluntary commitments to carbon offsetting, or through mandatory cap-and trade schemes or carbon taxes, and therefore carbon accounts need to be linked to financial accounts. In addition, investors, customers and other stakeholders are increasingly interested in companies' greenhouse gas emissions, in the same way that they require information on financial performance.

At present carbon reporting is predominantly a voluntary undertaking, however, it is likely to become mandatory in some jurisdictions in the near future. For example, the UK Climate Change Act (2008) requires the government to introduce regulations by 6 April 2012, which would make carbon reporting a mandatory component of annual Directors' Reports[3]. To help inform its decision on introducing the regulations the UK Government commissioned research by PricewaterhouseCoopers (2010) on the costs and benefits of carbon reporting. The research found that the majority of companies which currently report their emissions found the practice of quantifying greenhouse gas emissions beneficial and not financially burdensome[4].

Ecometrica has developed a format for reporting greenhouse gas emissions in Directors' Reports, including any related financial liabilities in the balance sheet. Ecometrica has used this approach in its own 2010 Directors' Report, and a freely available template is provided with this paper to aid other companies in reporting their emissions.

Carbon Reporting in a Directors' Report

The inclusion of greenhouse gas emissions in a Directors' Report can be broken down into two distinct components: the "Carbon Account" (which shows the balance of greenhouse gas emissions and removals or offsets, in units of tonnes of CO_2e) and the "Carbon Balance Sheet" (which shows any financial liabilities associated with the "Carbon Account"). It is possible that a company will not have any financial liabilities associated with its emissions, i.e. if it is not part of an emission trading scheme or has not committed to voluntarily offsetting its emissions. In this case the company will only need to complete the Carbon Account, and show that the Carbon Balance Sheet is not applicable or that there are no associated financial liabilities.

Table 1 shows the Carbon Account and the Carbon Balance Sheet for Ecometrica for the year ending 31 March 2010.

[3] The powers to introduce such regulations exist under the Companies Act 2006, and the Climate Change Act 2008 creates an obligation on the Government to implement these measures, or report to Parliament on why it has not done so.
[4] https://www.ukmediacentre.pwc.com/imagelibrary/detail.aspx?MediaDetailsID=1833

Table 1. Ecometrica's greenhouse gas emissions position for the year ending 31 March 2010.

Ecometrica Limited

BOX A

Carbon Account

	Year to 31 March 2010	**Year to 31 March 2009**
	tCO_2e	tCO_2e
Carbon offsets purchased	0	0
CO_2 released during year (Scopes 1-3)	(58)	0
Net carbon (release)/capture	(58)	0

BOX B

Carbon Balance Sheet

	As at 31 March 2010		**As at 31 March 2009**	
	tCO_2e	£	tCO_2e	£
Price of carbon	1	£11.55	1	£11.00
Carbon assets/(liability) bf	0	£0.00	0	£0.00
Carbon price change		£0.00	0	£0.00
Adjusted Carbon assets/(liability) bf	0	£0.00	0	£0.00
Carbon assets/(liability)	(58)	(£669.90)	0	£0.00
Intangible asset/(liability) cf	(58)	(£669.90)	0	£0.00

If the UK government introduces a requirement for greenhouse gas emission reporting in Directors' Reports, completing the Carbon Account may be the extent of the requirement.

Development of the Accounting Framework

When assessing how to report the financial effects of accounting for greenhouse gas emissions in monetary terms, we wanted to differentiate between emissions over a period and the position at the balance sheet date in the same way as financial accounts do. To this end we created a Carbon Account that takes into account all of the offsets purchased during the period as a positive figure and the total of equivalent tonnes of CO_2, the standard reporting unit for greenhouse gas accounting, released during the period as negative figures. The net figure between the two shows the company's "performance" in terms of CO_2e emissions for the period.

To turn a company's carbon performance into a financial figure, we wanted to consider what liability or asset may arise from emitting CO_2e in the books. If the company adopts the policy that it is liable to buy an offset for the CO_2e it emits, we can create a Carbon Balance Sheet showing the company's carbon position at the normal financial balance sheet date. By adding in the carbon price as at the balance sheet date we can determine that the company has either a liability (i.e. has not bought enough carbon offsets) or an asset (i.e. has bought carbon offsets that more than cover the company's CO_2e emissions from the first year it has accounted for carbon). A true and fair view of the carbon position of the company can therefore be reflected in the company's (financial) balance sheet.

At present there is no one single market price for carbon offsets. This is due to the varying nature of the offsets and trading schemes in existence. Unless the company concerned has chosen a specific policy stating the nature of the offsets it is going to purchase, or is within a trading scheme which has a market price for traded allowances, the lowest current market price would be used. At the time of writing some carbon offsets can be purchased for around £2.00. However, in the example used in this paper, the company has a policy of buying Plan Vivo certificates which are more typically between £9.00 and £12.00 for small purchase volumes, and the Carbon Balance Sheet therefore recognises a larger liability at the year end.

As a small company, Ecometrica includes the Carbon Account and the Carbon Balance Sheet in our Directors' Report. We believe that it would also fit in well in the Business Review section, which all companies not reporting as small companies are now required to include within their Directors' Reports, especially as the Companies Act 2006 specifically states that the review should give information on "environmental matters (including the impact of the company's business on the environment)".

The administrative costs of including carbon reporting within the Directors' Report were found to be minimal, adding less than 5% to the total cost of preparing the report. Approximately two days of administration support staff time were used to collate the data needed to quantify emissions (e.g.

travel records, waste data etc), half a day to enter data into a web-based carbon accounting tool[5], and half a day to present the information in the greenhouse gas account and carbon balance sheet.

Conclusions

Carbon reporting can be easily integrated with companies' financial reporting. This allows companies to provide greenhouse gas emissions information to investors and other stakeholders, and to show any financial liabilities associated with those emissions. Carbon reporting does not create any significant additional administrative burden in preparing annual Directors' Reports, and may create net benefits through helping to recognise and reduce financial liabilities, as well as greenhouse gas emissions.

References

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[5] Ecometrica used its own web-based carbon accounting software, *Our Impacts.* For more information on *Our Impacts* software visit http://www.ecometrica.co.uk/our-impacts.