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THE FUTURE UK CORPORATE ENERGY AND CARBON REPORTING FRAMEWORK AND THE END OF THE CRC SCHEME

The Department for Business, Energy and Industrial Strategy (BEIS) has published its response to a consultation on proposals to streamline the UK corporate energy and carbon reporting framework and draft regulations to implement the changes. In a significant change to the current framework, new reporting requirements are to be placed on large unquoted companies and large LLPs. BEIS expects the number of reporting organisations to increase from 1,200 to 11,900.

Legislation has also been laid before Parliament to abolish the CRC Energy Efficiency Scheme as from April 2019.

The response follows BEIS' October 2017 consultation paper which sets out a number of options for reforming the framework which are considered in our client briefing: "The UK Clean Growth Strategy – New Energy and Carbon Reporting Rules". We set out below an overview of the revisions adopted by the Government.

Key Issues

- Quoted companies will have additional obligations to report on energy usage; but apparent reduction in scope of quoted company group reporting
- Large unquoted companies and large LLPs will have new more limited obligations to report on GHG emissions and energy usage
- Data will be required broadly on a group basis
- Reporting will be on a "comply or explain" approach
- CRC scheme is abolished from April 2019 but some obligations will endure

Legislation implementing the changes

The changes are to be implemented by the Companies (Directors' Report) and Limited Liability Partnerships (Energy and Carbon Report) Regulations 2018, published in draft (the 2018 Regulations). The 2018 Regulations provide for:

- Changes to obligations of *quoted companies* and the introduction of obligations for *large unquoted companies* through amendments to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (current obligations on quoted companies are contained in Schedule 7).
- The introduction of obligations for *limited liability partnerships (LLPs)* through amendments to the Limited Liability Partnerships (Accounts and Audit) (Application of Companies Act 2006) Regulations 2008.

SCOPE AND APPLICATION OF REPORTING PROPOSALS

The coverage of carbon and energy reporting remains largely as proposed in the consultation paper and distinguishes between UK quoted companies and UK unquoted companies / UK LLPs. Companies that are not registered in the UK would not be required to report, but any UK subsidiaries would need to do so.

(a) UK quoted companies

The current requirements for mandatory reporting of global greenhouse gases (GHG) will continue for quoted companies, subject to the changes referred to below. A quoted company will continue to report through the directors' report forming part of its annual report. The reporting requirements cover scope 1 direct emissions from combustion of fuel and operation of facilities, and scope 2 indirect emissions from consumption of purchased electricity, heat, steam and cooling. Reporting on scope 3 (supply chain impacts) would remain voluntary. In addition to GHG emissions, new reporting requirements will require affected companies to include the total energy use associated with their scope 1 and 2 emissions. In addition, for the first time, quoted companies will have to split out their figures for: (i) UK and UK offshore area; and (ii) non-UK.

For the purposes of these regulations, a quoted company is a company with its equity share capital included in the FCA's Official List, officially listed in an EEA State or admitted to dealing on either the New York Stock Exchange or the Nasdaq.

(b) UK large unquoted companies and UK large LLPs

In a significant change to the current regime, carbon and energy reporting will be extended to certain UK "large" unquoted companies as well as to UK large LLPs. A large unquoted company would report on emissions and energy use in the directors' report forming part of its annual report. A large LLP will report on emissions and energy use in a new 'energy and carbon report'.

These large unquoted companies / LLPs will report on UK scope 1 direct GHG emissions (but only for combustion of gas, and consumption of fuel for transport), and UK scope 2 emissions from consumption of purchased electricity (including for transport). They will also report on energy use represented by these scope 1 and 2 emissions. As for quoted companies, it will be voluntary for large unquoted companies / LLPs to report on their scope 3 carbon emissions. Reporting of UK offshore energy and emissions will be mandatory for organisations wholly or mainly involved in offshore activities (but otherwise will be voluntary).

The requirement to produce only UK figures is different from the position for quoted companies but reflects the position in the CRC Scheme and the Energy Savings Opportunity Scheme for energy auditing (ESOS).

Similarly to a quoted company, a large unquoted company or large LLP would need to include an intensity ratio tying the emissions to quantifiable factors (e.g. turnover or employees). It would also need to repeat information contained in the previous year's reports so that a rolling comparison can be made to identify changes year upon year.

Large unquoted companies

Of the various options floated in the consultation, BEIS has decided that the obligations would be placed on those unquoted companies regarded as

"large" companies - in basic terms those satisfying two or more of the following conditions (see below for large companies that are part of a group):

- More than 250 employees.
- Turnover of more than £36m.
- Balance sheet total of more than £18m.

Large LLPs

The test for being a large LLP tracks the test for being a large unquoted company (see below for large LLPs that are part of a group).

Many of the requirements for preparing and submitting an energy and carbon report (and consequences for failure to comply) mirror those in respect of a company's directors' report. For example, failure to comply with a duty to prepare an energy and carbon report would be a criminal offence if the member fails to take all reasonable steps for securing compliance with this duty. Civil penalties for late filing of the energy and carbon report would also apply.

Unregistered companies

BEIS has also decided to extend the reporting requirements to a small number of unregistered companies that are required to prepare a directors' report.

Increase in numbers of companies covered

BEIS states that this extended reporting requirement is likely to increase the total number of reporting companies from around 1,200 to 11,900. While this should provide a relatively straightforward method of determining qualifying companies, it would create divergence from the approach in the ESOS for which the qualifying criteria adopted the definition of "Large Undertakings" under EU law, which is slightly different (see our earlier briefing).

GROUP REPORTING

Where a parent UK parent company or LLP has to prepare group accounts, reporting is required on a group basis with the qualifications set out below.

An unquoted company or LLP that is a parent is only required to report if the group headed by the parent meets two or more of the following conditions:

- More than 250 employees in aggregate.
- Aggregate turnover of more than £36m net (or £43.2m gross).
- Aggregate balance sheet total of more than £18m net (or £21.6m gross).

No subsidiary (whether quoted, or unquoted, company or LLP) is required to report where it is included in the consolidated group directors' report or consolidated group energy and carbon report (as applicable) of the parent. As a result, the type of consolidated report required depends solely on the nature of the reporting parent entity (irrespective of the nature of the subsidiary entities contained in the group), as shown in the table below.

Reporting Parent	Type of Report Required
Quoted Company	Consolidated group directors' report
Large Unquoted Company	Consolidated group directors' report
Large LLP	Consolidated group energy and carbon report

A change in the scope of group reporting?

Under the 2018 Regulations, a group report can omit data about a subsidiary's operations that that subsidiary would not have to report if it was a standalone company (i.e. not part of a group). This would appear to have the potential to reduce significantly the current scope of reporting in circumstances where a quoted company prepares a consolidated group directors' report. For example, if a quoted company's directors' report covers a large unquoted company subsidiary, under the current framework it would generally have to report in relation to the combustion of all fuels at the subsidiary's facilities. Under the 2018 Regulations, however, it appears that it would only have to report in relation to combustion of gas at those facilities. It is not clear whether this is an intentional move by BEIS.

EXEMPTIONS AND 'COMPLY OR EXPLAIN' APPROACH

A company will be exempt from the requirements where its energy use does not exceed 40,000kWh during the relevant year. Where a directors' report or energy and carbon report is produced on a group basis, the threshold would be applied to aggregated energy use of all group entities covered by the report.

Similarly to the current mandatory GHG reporting obligations, all energy and carbon reporting obligations under the proposals would be on a "comply or explain" approach: Organisations would not have to report information where it would be impractical to do so.

In exceptional circumstances, an organisation would be able to withhold data where the directors (or, in the case of an LLP, the members) think this would be seriously prejudicial to the organisation's interests.

ADDITIONAL POINTS ON REPORTING SCOPE

All obligated organisations (whether quoted companies, unquoted companies or LLPs) will be required to provide a "narrative commentary" on all action they have taken on energy efficiency in the relevant financial year. However, BEIS has dropped the suggestion of requiring disclosure of ESOS recommendations and progress on implementing them due to concerns over commercial sensitivity of such information.

One of BEIS' most far-reaching announcements in the original proposals was its plan to consider whether the recommendations of the Taskforce on Climate related Financial Disclosures (TCFD) should be mandated within its streamlined reporting framework (See our briefing "Report urges Companies to Disclose Climate Change Impacts in Financial Filings"). Had it done so, key consequences for corporate reporting would have been the specific requirement for companies to include forward-looking analysis of climate impacts based on different climate change scenarios, and analysis of governance structures, strategy, and risk management approach for dealing

with climate change impacts. BEIS now states that it is too early to mandate the TCFD requirements but they will continue to examine this while considering the March 2018 report of the Green Finance Taskforce (which recommended implementing the TCFD in full).

ABOLITION OF THE CRC ENERGY EFFICIENCY SCHEME

Legislation has also been laid before Parliament to abolish the CRC Scheme after April 2019. Participants will need to buy their final allowances for the 2018/2019 compliance year by October 2019.

Beyond that date, various provisions of the 2013 and 2010 CRC Orders will remain operative in relation to compliance with previous periods. Participants should note the obligation to maintain certain records for 6 years after the relevant scheme year to which they relate (potentially up to April 2025). On the plus side, the possibility of refunds for surplus allowances remaining at the end of the last scheme year will remain in place.

FINAL COMMENTS

The reporting changes will take effect for all financial years of affected organisations beginning on or after 1 April 2019 and will apply throughout the UK.

While CRC will disappear, it appears that ESOS will remain in place as an overlapping mechanism with slightly divergent qualification criteria from the revised energy and carbon reporting framework. It is disappointing that BEIS has pushed back a decision on incorporating the TFCD into the revised framework at this stage. While it is important to bring changes into effect upon abolition of CRC reporting in April 2019, a constant drip-feed of reporting changes is unlikely to be welcome.

BEIS' response to consultation "Streamlined Energy & Carbon Reporting – Government Response – July 2018" can be viewed here.

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69697-5-2096