STARTUP COALITION

CARBON MARKETS INNOVATION FORUM

www.startupcoalition.io www.cmif.co.uk

Department for Energy Security & Net Zero
Scope 3 Emissions in the UK Reporting Landscape Call for Evidence

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About the Startup Coalition:

The Startup Coalition (formerly Coadec) is the policy voice of tech startups and scaleups in the UK. Since 2010, Startup Coalition has worked to engage on behalf of tech startups in public policy debates in the UK across a range of priority issues for startups including access to finance, immigration and skills, and technology regulation.

About the Carbon Markets Innovation Forum:

The Carbon Markets Innovation Forum (CMIF) was founded in October 2023 to convene startups in the carbon markets and ensure they have a seat at the policy table. This includes actors in the compliance and voluntary carbon markets, and is aimed at startups involved across the carbon market supply chain, **carbon accounting** - supporting the quantification of greenhouse gas emissions: **carbon markets intermediaries** - supporting the integrity of the market through software, infrastructure and ratings; **carbon credit providers and project developers** - the folks doing the actual removal and emissions reductions downstream, and providing carbon credits to the market.

We operate an open-doors policy to celebrate, educate and empower startups in the carbon markets, with a specific focus of ensuring they have the chance to feed into the UK Government's policymaking process. Once a quarter we invite startups to join our CMIF summit, under the strategic direction of our steering committee and secretariat. We also aim to equip UK policymakers, regulators and officials with information about and access to the innovative carbon markets.

General Remarks

Startup Coalition interacts with hundreds of startups in the UK across all sectors of the economy. In October 2023, we launched the Carbon Markets Innovation Forum (CMIF), an initiative that convenes startups in the carbon markets to discuss policy issues that impact the sector. We define the carbon market sector as the end-to-end supply and demand of carbon credits. This includes both the compliance market, which exists as the UK Emissions Trading Scheme in the UK, and the Voluntary Carbon Market (VCM). Both of these markets are a fundamental part of the UK's transition to net zero, in supporting hard-to-abate sectors to offset their impact, and also to enable any firm to complement their own internal decarbonisation processes through additional action. The VCM is also one of the only sources of revenue for the carbon removal sector, which is a critical and underfunded part of the net zero transition.

General Impact on Startups

The startups and scaleups we work and interact with everyday would be impacted by a mandate for scope 3 emissions reporting to varying degrees, as a direct compliance activity, as part of supply chains to larger organisations facing new compliance obligations, and also as suppliers of services to support compliance.

Critically, we contend that if a scope 3 reporting mandate is executed well it could accelerate the net zero transition, particularly as Scope 3 emissions can account for 80% (and according to some partcicpants, of some firms they deal with it's often over 95%) of a firm's total emissions whilst also stimulating demand for carbon accounting services.[1] Reporting requirements can enable more informed investments by businesses and investors, and also more informed consumer choices.

The power of emissions reporting just being mandated for larger businesses mustn't be underestimated. The effect of this would have significant implications for up and down the supply chain as the multiplying effect would cause firms who aren't under any reporting requirements to still legally calculate and disclose their emissions or face losing business.

In contrast, mandating Scope 3 emissions reporting for firms of all sizes could create overly onerous requirements for firms that do not have the resources or know-how to comply, impacting growth and jobs. Furthermore, firms in the long tail of small businesses, including startups, already have relatively low emissions, meaning it's unclear that expanding mandatory Scope 3 emissions reporting to this cohort would achieve the objective of supporting the net zero transition.

Voluntary carbon market

Reporting emissions is one of the key gateways to participating in the carbon market, and consequently, efforts by the government to support and accelerate the accounting of emissions are to be applauded. However, as always, the introduction of new requirements

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[1] What are scope 1, 2 and 3 emissions? | Deloitte UKDeloittehttps://www2.deloitte.com › focus › climate-change › zer...

on firms comes with trade-offs. If scope 3 emissions reporting were to be mandated this would also likely lead to increased demand for the carbon markets to enable action off the back of emission quantification.

Collation of responses

To compile this detailed response, Startup Coalition convened an open meeting of the CMIF, inviting a range of startups involved in the carbon market to participate in a discussion, and/or to submit a written submission. All of the firms that we spoke to are in the ClimateTech sector and all of them already do or plan to report their scope 3 emissions.

<u>Response to Questions 1-4</u>

All firms we spoke to report their scope 3 emissions, except one who plans to report it for the first time at the end of this year. Startup Coalition does not currently report scope 3 emissions.

<u>Response to Questions 5-9</u>

Startups that participated in our CMIF evidence gathering process did not report material issues with the ISSB's assessment of the value of scope 3 information. Similarly, no participants had issues with scope 3 reporting contained in IFRS 2 or the use of the GHG protocol for scope 3 reporting. Firms believed that there was merit in the UK Government clearly directing travel in standards to avoid fragmentation. Participants advocated that any UK endorsed reporting standard should be aligned with industry and international best practice.

<u>Response to Questions 10-11</u>

Importantly, startups that participated in our CMIF evidence gathering process all already report their Scope 3 emissions, or plan to in the near future. The fact that they operate in the supply of products and services that support the quantification and reporting of emissions means they are well placed to do this themselves.

However, participants expressed reservations about the ability of their customers to adequately measure the true extent of scope 3 emissions in their supply chains today, as it is a difficult challenge to fully calculate due to the current poor reporting of other firms within those chains. The endeavour to report also requires significant time and resources, which small businesses are severely lacking. According to one firm that participated in our evidence gathering process, it takes an average of three months to prepare a business before they can start reporting scope 3 emissions and although there are logistical challenges for larger firms, smaller firms experience the most delays due to greater resource constraints.

Firms also noted how mandated reporting would highlight 'transition risks' for many firms, allowing them to navigate regulatory or legal changes with regards to net zero – giving them a 'data buffer' to understand risk in their supply chains which would help them to mitigate the most negative potential effects from minimum environmental standards. This knowledge would also better help them to absorb shocks in supply chains.

Startups also expressed their frustration at there being far too many frameworks that "consulting groups and strategy firms are using to measure scope 3". There is "not a consistent methodological approach". There was unanimous support for the UK Government to provide consistency.

> *"There is a direct clash between data availability and quality of data. To gain access or produce (high) quality data is very resource intensive and so you rely on small businesses for data, this then is a problem, if the government wants to compel reporting, then they need to lay out in advance exactly what they will do to allow firms to prepare, clarity is vital".*

Participants also expressed concern that firms have to make a lot of assumptions about the environmental impact in the downstream use of a product and in its end-of-life phases. The most accurate way of reporting these emissions would be to carry out a life cycle assessment on a product but this can cost tens of thousands of pounds per item and can take months to calculate. This is unrealistic to expect small businesses to execute.

Importantly, some firms that we spoke to were of the view that emissions reporting should be mandated for all firms across the economy but that smaller firms should also receive varying levels of government support based on their revenue and number of employees. This would prevent certain firms from slipping through the cracks whilst also helping smaller firms to shoulder the cost burden. They believed that if all firms were not mandated to maximise regulatory alignment with other nations then it could risk significant trade friction with foreign markets.

In the same vein, it was also pointed out by some, that a lack of 'across the board reporting' could act as another arbitrary limit to Britain's already sluggish growth; this does not necessarily mean that the UK needs to have every firm report scope 3 emissions, however, the more firms in regulatory misalignment the worse it will be for the economy. The government needs to strike a key balance as to not overburden firms whilst also preventing trade friction – otherwise, the UK risks advanced economies getting ahead, such as the EU and California, both of whom have already changed legislation which will eventually require general scope 3 emissions reporting, in 2025 and 2027 respectively.[2] (general is specified as to be clear, there are rare instances in which a small number of firms are currently required to report specific scope 3 emissions, but to be sure it is not nearly as expansive as the proposed reporting mandate in this call for evidence).

Response to Questions 12-17

We did not speak to investors directly as part of our information gathering process for this response, however feedback from startups that did participate suggested that they believed that reporting scope 3 emissions would incentivise investment into ClimateTechs in the carbon accounting supply chain. They also suggested that they would envisage scope 3

[2] https://www.thomsonreuters.com/en-us/posts/esg/california-climate-reporting-law/

emissions becoming part of investor decisions, as emissions become a proxy for regulatory risk.

There was concern from participants about the government having direct oversight of emissions reporting and participants generally agreed that oversight should be in the hands of an independent regulatory body. This would minimise exposure to political change, thus leading to more certainty and consistency for businesses.

Participants agreed that Scope 3 reporting is important for value chains, economies, and consumer awareness. There was general agreement that mandating Scope 3 emissions reporting would be beneficial for increasing demand for products and services that support emissions reporting. There was also feedback that reporting could galvanise those sectors that remain incredibly stubborn to change. For example, construction is an industry where data is unstructured, siloed and inaccessible. Mandated reporting could force the sector at large to change this: rapid digitalisation and data sharing could decarbonise the industry and decrease barriers for smaller startups trying to innovate and decarbonise the sector. It would also give incumbents a greater picture of their emissions and help them target specific parts of their supply chain, which in construction has extensive end-of-life and down and upstream emissions.

There was also support for mandating reporting as a way of accelerating the initial quantification of emissions that can otherwise be perceived to be too challenging and complex, meaning that time is not spent on the actual decarbonisation.

> *"I saw a post on LinkedIn the other day from a disheartened sustainability manager saying that they spend so much time, effort and energy on (emissions) reporting… but they should be putting resources into (emissions) reduction, direct reduction."*

Critically, the point above stresses the importance in not just focussing all energy on reporting. Fixating all time, effort and resources on measurement and reporting risks losing sight of the wood for the trees. The point of measurement and reporting emissions is to inform and drive emissions reduction. However, resources are limited. Greater direction from the Government would create more clarity and consistency for firms, meaning they can accurately assign resources and execute to deadlines.

Response to Questions 18-20

One of the largest barriers to producing consistent scope 3 data is the current variety of frameworks being used by hundreds of consulting and strategy firms. This variety has created a situation where firms feel the government should step in to endorse a single approach/methodology to promote clarity and consistency.

Response to Questions 21-24

It is estimated by a recently published report that just 7.7% of small and medium businesses are reporting scope 3 emissions, 73% are concerned about the upfront costs if they had to report scope 3 and 65% of them describe the reporting standards as “complex”.[3] However, over 80% say that sustainability is important to them. These are firms who want to report their emissions as part of a proactive effort to reduce their greenhouse gas footprint, yet they face significant barriers to do so – the two key barriers being a lack of clarity on what to report, the cost associated with quantification.

Response to Question 25

No response.

Response to Questions 26-32

Although SECR is broadly supported as being a reliable framework it does however primarily focus on the emissions and energy assessment part of reporting and pays little to no attention about risks to firms. Some of the participants in our evidence gathering process believed that SECR needs to be aligned with other guidelines such as the Energy Savings Opportunity Scheme (ESOS) for “a more unified criteria”.

The major concern coming from firms in the sector does not seem to be a potential inability of small businesses and startups ultimately being required to report scope 3 emissions using the GHG protocol. The issue is the quality of available data. It is not to the standard it should be, however, this is something that could eventually be smoothed out naturally as more firms adjusted to emissions reporting and firms in the supply chain also started reporting their emissions.

Response to Questions 33-37

Two schemes that overlap are SECR and ESOS. Whilst they are similar in that they both require businesses to report and understand their energy impact, ESOS assesses energy usage whereas SECR assesses a firm’s energy consumption and emissions. They also have slightly different requirements to qualify based on employee numbers and annual turnover/balance sheet, their reporting period also differs in that ESOS works in four year cycles and SECR is reported once a year, to be contained within a business’s annual accounts. The duplication here (for qualifying firms, which are large) is the reporting of energy usage. By cutting down energy reporting to just one for the reporting schemes, reporting would be made more efficient.

> *“We need sector specific calculation methods. Data quality scoring would improve this”.*

Response to Questions 38-39

No response.

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3 https://www.sage.com/en-gb/company/sustainability-and-society/planet/?utm_medium=socialnetwork&utm_source=linkedin&utm_content=HS_410be73b-b08e-4b7a-8904-daca2a16cb8e&utm_campaign=NPS_FY24_GSO_owned_EmployerBrand#cop28