PROPOSAL FOR DIFFERENTIATED ACCOUNTING PATHWAYS

Submitted via GHG Protocol's online folder

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Proposal and supporting information

1. **Which standard or guidance does the proposal relate to (Corporate Standard, Scope 2 Guidance, Scope 3 Standard, Scope 3 Calculation Guidance, general/cross-cutting, market-based accounting approaches, or other)? If other, please specify.**

General / cross-cutting

2. **What is the GHG accounting and reporting topic the proposal seeks to address?**

This proposal seeks to address the Corporate Standard's *Business Goals and Inventory Design* framing, with related changes across scope 2 and scope 3 documents.

3Degrees recommends creating new guidance that enables specified differentiated approaches to emissions inventories with follow-on implications for business goals, emission disclosures and claims. We call these specified approaches "differentiated accounting pathways."

3. What is the potential problem(s) or limitation(s) of the current standard or guidance which necessitates this proposal?

Today, the Corporate Standard and its companion documents are intended for organizations of virtually any size, business model, and emissions profile. As the Standard's popularity has grown, its one-size-fits-all approach has begun to have unintended consequences that undermine its purpose as a tool to enable and support company emission reduction ambitions and action. In some ways, compiling a compliant inventory has become the primary objective, rather than delivering an inventory that informs appropriate climate action. For example:

- Companies with smaller and/or highly geographically distributed footprints, spend disproportionate amounts of money and human resources on annual inventory work even though these efforts bear little resemblance to (and may be unnecessary to) the planning and execution of their critical emission reduction activities. This misdirects resources toward measurement that would be better oriented to action.
- Companies seeking to use data-rich measurement methods in support of large footprints and ambitious goals find no guidance in the Protocol, or worse, find that their emission reduction efforts are invisible when using the Protocol's prescribed measurement methods. This discourages innovative, ambitious action.
- Some companies attempting to make change in their supply chains find that a key Protocol assumption - that their purchasing power confers sufficient influence to compel both emissions reporting and emissions reductions activities from suppliers - does not hold true in their context. The Protocol's guidance leads such companies to expend considerable resources on supplier engagement programs that are largely ineffective in that emission reductions do not arise even after many years of effort. The absence of alternative scope 3 measurement approaches undermines the innovation needed to develop and undertake more effective action-paths.

We do believe that having a single dominant standard for greenhouse gas accounting is an important value that the GHGP provides. This proposal is intended to ensure that it can still stretch to meet the needs of so many different kinds of companies without resorting to a least-common-denominator approach.

4. Describe the proposed change(s) or additional guidance.

To enable companies to direct their resources in the most effective way possible, we seek Protocol guidance that enables companies to tune their inventory approach - the types of

sources they seek to quantify, the data sources and calculations they use, and the resulting focus created by their reports - to their circumstances as an emitter. In this Our objective is to create a simple, transparent way to focus company accounting activities, reports and claims so as to:

- reveal the emissions of most importance to society;
- support ambitious, effective emission reduction goals and tactics; and
- minimize resources required for accounting tasks that do not contribute to these aims.

To meet this objective, 3Degrees recommends creating new guidance that enables specified, differentiated approaches to emissions inventories with follow-on implications for business goals, emission disclosures and claims. We call these specified approaches "differentiated accounting pathways."

Differentiated accounting pathways would allow reporters to de-emphasize less-important emissions in their inventory work, while undertaking more detailed inventories for important emissions. Business goals and achievement claims would be differentiated as well, and appropriately so. Differentiated accounting pathways would focus the resources and goals of the reporting organization while also focusing the attention of stakeholders to those arenas of most importance in the business' context as an emitter. This idea is implemented to a limited extent with scope 3 category relevance criteria, but we propose more broadly applicable and directed guidance across the entire inventory.

We note that goal-setting initiatives and other supplemental guidance that relies in part on the GHGP do not serve the purpose of this proposal. The number of companies using the GHGP that do not report to CDP and do not have SBTi goals, is vast. Among 3Degrees' climate action customers, for example, far fewer than half are represented by these initiatives. These "silent" participants span a wide range of size, sophistication, and emissions. While there is certainly a place for ambitious initiatives to create additional guidance, the GHGP is now popular enough on its own to require differentiation in its guidance to encompass its wide range of users.

Differentiated accounting pathways could be constructed in any number of ways to meet the aims described above. Here, we present one example to illustrate our recommendation. Other constructs could also be explored.

Example: Accounting pathways differentiated by measurement system fidelity

This method differentiates greenhouse gas inventory approaches using "high fidelity" and "low fidelity" options. The "fidelity" rubric would separate more accurate, exacting approaches from more approximate, directional measurements. Accounting *pathways* would reflect reporters choosing high- or low-fidelity inventory approaches for each of scopes 1, 2, and 3.

The GHG Protocol's "Business Goals and Inventory Design" section would provide critical guidance to reporters choosing their accounting pathway. Generally speaking, companies with emissions of less importance to society within a given scope would be guided toward a

low-fidelity accounting pathway so as to minimize the resources and attention given to measuring those emissions.

In this "measurement system fidelity" example, the pathway choice would also influence the types of goals a company could set, because a low-fidelity inventory is not suited to quantitative inventory targets. This is by design: for unimportant (or unquantifiable) emissions, quantitative inventory targets are inappropriate.

Instead, through guidance or case studies, the GHG Protocol could encourage companies on low-fidelity pathways to undertake emission reduction activities directly – without quantifying a baseline – speeding the progress toward emission reductions vs. today's inventory approach. We note that many emission reduction activities are quantifiable in and of themselves, and hence could be used for goal-setting as appropriate even without a high-fidelity baseline inventory.

Measurement system fidelity choices would also affect a company's ability to make emission disclosures and claims; the specifics of necessary and appropriate disclosures and allowable claims would depend on their accounting pathway choices and could be incorporated into the claims guidance 3Degrees recommends in our supplemental *Claims Proposal*. Quantified emissions inventories and related claims are not possible with low-fidelity accounting approaches, for example, but other claims related to emission reduction activities pursued would be possible.

As such, the GHG Protocol would need to provide new, clear guidance that details:

- the need to choose an accounting pathway via inventory fidelity choices for each scope;
- criteria to make this choice;
- accounting instructions for the newly differentiated pathways (we note here that this example does not require new accounting approaches - reporters already use high- and low-fidelity inventory approaches, albeit variably and without labeling them as such);
- disclosure language, goals, and claims appropriate to the different pathways;
- action steps that can be taken to reduce emissions along each pathway.

To demonstrate at a more detailed level how this particular example might be implemented, sample pathway choices and implications are provided in a chart in answer to Question #8.

5. Please explain how the proposal aligns with the GHG Protocol decision-making criteria and hierarchy (A, B, C, D below), while providing justification/evidence where possible.

A. GHG Protocol accounting and reporting approaches shall meet the GHG Protocol accounting and reporting principles (see Annex for definitions):

- Accuracy, Completeness, Consistency, Relevance, Transparency
- Additional principles for land sector activities and CO_2 removals: Conservativeness, Permanence, and Comparability if relevant

Implementing this proposal for accounting pathways strengthens the principles by providing new guidance on "accuracy" and potentially "completeness" across differing contexts, and by expanding guidance on "relevance" - in all cases so as to enable companies to better match their inventory approach to their business circumstances (as already intended by the principles). Explanations are below.

- **Accuracy:** this principle is written so as to encourage reporters to apply judgment in their quest for an accurate inventory. It requires companies to "*achieve sufficient accuracy to enable users to make decisions with reasonable assurance as to the integrity of the reported information*" and to "*reduce uncertainty as far as practicable.*"

  In practice, though, we do not see reporters and stakeholders scaling their practices in line with this principle. The challenges are in both directions: striving for unnecessary accuracy for unimportant emission sources, and finding no path to increasing the accuracy of important emissions quantification.

  Striving for unnecessary accuracy

  Ever-increasing accuracy is considered a universal good rather than a potential misdirection of resources and stakeholder attention by most reporters. For example:

  - Companies spend a great deal of time seeking utility information from landlords even where their space is not separately metered, and/or when these emissions are trivial compared to others in their inventory;
  - Similarly, companies hunt down emission factors for each piece of HVAC equipment - in an office environment - so they can estimate fugitive emissions accurately, even when such equipment is not under consideration for refit or replacement for several years and the emissions are small;
  - Companies seek out emission factors for "hotel stays" when the only emissions from business travel that might be relevant to consider are from flights - and even then we question whether quantifying those flight emissions serves a decision-useful purpose vs. say, counting business trips.

  In these examples and so many others, the information dutifully sought is not decision-useful even when considering all stakeholders. Companies seek it out only because it is, in theory, available to them and as such the Protocol appears to require it. This interpretation is reinforced by GHG Protocol guidance across all documents and scopes. Case studies, calculation examples, tips, flow charts and guidance language emphasize obtaining the best data available, not as the principle states, the best data that is practical to obtain and which furthermore will provide useful information to decision-makers and stakeholders.

  Barriers to increased accuracy for important emissions

  The increasingly wide availability of large data streams alongside the advent of cost-effective data mining tools have together created numerous innovative ways to compile both company "activity data" and relevant greenhouse gas emission factors.

Scope 2 calculations. One example of this new capability is in scope 2 electricity emissions, where both location-based and market-based calculations can now be rooted in hourly usage and emissions data vs. the standard practice of using annual totals and averages, respectively, in many places around the world.

Despite the increasing availability of these data sources and the important insights they provide to grid emissions and strategies to reduce them, companies are not adopting these data sources in their standards-compliant reporting. This reluctance stymies innovative companies with emission reduction approaches aimed at (say) shifting the hours of electricity use to minimize emissions, or prioritizing energy efficiency efforts to those effective in critical time periods.

The Protocol does not prohibit or even overtly discourage the use of enhanced-accuracy data, but neither does it encourage or require it

Adopting new measurement systems can be costly and disruptive to a company's inventory process, and it can result in an increase in reported emissions. Therefore few companies choose to adopt new systems without a nudge or a firm push, for example guidance indicating that they should or must do so. Or, at a minimum guidance that modifies the types of inventory claims and goals they can make if they do not adopt appropriately-accurate measurement methods for their circumstance.

The recently-released FLAG guidance provides a helpful example of how a detailed set emission-measurement criteria can be created and standardized. However, we note that this guidance resulted from a lengthy process that still does not provide companies with clear directional indications as to the most appropriate measurement approach(es). The guidance is not prescriptive.

Clearer directional guidance and implications of adopting or not adopting new measurement methods, while still allowing choice of measurement approaches, would be possible using differentiated accounting pathways.

Accuracy: conclusion

This proposal's call for clear guidance which highlights companies' obligation and ability to make choices regarding the accuracy of their inventories would allow companies to implement the accuracy principle *as it is written*. Furthermore, highlighting these choices as distinct, codified pathways enables transparency about the choices made.

\+ **Completeness:** Creating differentiated accounting pathways need not exclude any emission sources, hence need not touch upon the completeness principle. As an aside, though, we do note that one way to create differentiated pathways would be to curtail measurement altogether for certain types of emissions within certain types of companies, aiming them instead toward goals related to common-sense action-steps. We believe creating pathways which allow companies to forego certain measurement tasks altogether provided they meet certain criteria, is worthy of consideration.

+ **Relevance:** The relevance principle emphasizes that an inventory should "*appropriately reflect the GHG emissions … of the company*" and serve *"the decision-making needs of users – both internal and external to the company*."

Similar to the Accuracy principle, the Protocol provides little direction as to the proper application of this principle in practice, with the notable exception of the scope 3 relevance criteria. Even there, though, the relevance criteria are used as a means to exclude certain scope 3 emission categories (which is good), but not as a means to decide an inventory approach for all scopes and sources - as one would expect from the Relevance principle.

In the Corporate Standard today, the Relevance principle is described only briefly and is focused on accounting boundaries. In the Scope 3 Guidance document, the focus as noted above, is once again on inclusion/exclusion of emission categories.

We propose and recommend that the language of the principle be embraced more fully, to encompass the accuracy principle as noted above, but also to embrace the larger objective of creating a decision-useful inventory. An inventory is not a climate action, and companies should be focusing on their actions moreso than their accounting.

B. GHG Protocol accounting and reporting approaches shall align with the latest climate science and global climate goals (i.e., keeping global warming below 1.5°C). To support this objective (non-exhaustive list):

- Direct emissions reported in a company's inventory should correspond to emissions to the atmosphere. Reductions in direct emissions reported in a company's inventory should correspond to reductions in emissions to the atmosphere.
- Indirect emissions reported in a company's inventory should in the aggregate correspond to emissions to the atmosphere. Reductions in indirect emissions reported in a company's inventory should in the aggregate correspond to reductions in emissions to the atmosphere.

This proposal is supportive of aligning with climate science in that its objective is to focus companies on taking action for important emissions, emphasizing the pre-eminence of that objective vs. assembling an inventory. As it sits today, the Protocol's use misdirects company resources toward measurement that should be used to take action, and inhibits company actions in cases where emissions are important and their finer measurement warranted.

C. GHG Protocol accounting frameworks should support ambitious climate goals and actions in the private and public sector.

- Would this proposal enable organizations to pursue more effective GHG mitigation/decarbonization efforts as compared to the existing standards and guidance? If so, how?
- Would this proposal better inform decision making by reporting organizations and their stakeholders (e.g. related to climate-related financial risks and other relevant information associated with GHG emissions reporting)?

As noted above in the "Principles" question, providing differentiated accounting pathways would better support ambitious goals for both large emissions of great importance to society, and for small emissions worthy of only limited attention from a measurement standpoint. Focusing companies toward appropriate action is a key objective of this proposal.

Also, our proposal will better inform stakeholders across the board in clear, simple language of an inventory approach taken by a company (in our example, "high-fidelity" or "low-fidelity").

This allows stakeholders both internal and external to decide whether the information provided is adequate for their decision purposes (reduction planning, goal setting, regulation, investment, product purchasing, etc.) whereas today such choices are hidden underneath positive verification opinions that do not elucidate the choices made in compiling the inventory. Providing named pathways with implications for goals and claims will create a short-hand but useful rubric in understanding inventory approaches.

D. GHG Protocol accounting frameworks which meet the above criteria should be feasible. (For aspects of accounting frameworks that meet the above criteria but are difficult to implement, GHG Protocol should provide additional guidance and tools to support implementation.)

- What specific information, data or calculation methods are required to implement this proposal (e.g., in the case of scope 2, data granularity, grid data, consumption data, emission information, etc.)? Would new data/methods be needed? Are current data/methods available? How would this be implemented in practice?
- Would this proposal accommodate and be accessible to all organizations globally who seek to account for and report their GHG emissions? Are there potential challenges which would need to be further addressed to implement this proposal globally? What would be the potential solutions?

No new data or calculation methods are required for this proposal. Rather, new judgment is required to differentiate/separate (say) measurement approaches, into pathways. The judgment (needed to create the guidance) need not be item-by-item specific to every possible (say) measurement system, but should be sufficiently clear to guide company inventory decisions onto appropriate pathways.

We believe this proposal would substantially enhance the accessibility of the GHG Protocol to all organizations globally as it would provide a built-in scaling system which simultaneously makes the Protocol more appropriate to large emitters while down-scaling it to smaller ones.

6. Consistent with the hierarchy provided above, are there potential drawbacks or challenges to adopting this proposal? If so, what are they?

Currently, the protocol leaves a great many judgments to reporters with the philosophy that as long as the judgments are reasonably transparent, these judgments should belong to the reporting companies. One effect of this proposal is to create clearer guidance to guide companies to specific measurement pathways, in effect leaning them toward certain judgments as opposed to others. This is intentional and appropriate given the broad audience of Protocol.

Nonetheless, it is not today's approach and would not necessarily be welcome; for example, large emitters may not wish to be "nudged" into a high-fidelity measurement pathway if they are not already using such measurement techniques.

Also, we expect there to be discontinuities in measurement values when companies make these choices, which may create challenges translating goals and achievements with new values. Still, if there are such discontinuities then bringing the new quantifications to light is all the more necessary since it means the emissions and actions being reported to date have been incorrect in some important fashion.

Finally, establishing pathways is meant to simplify the assemblage of inventories and transparent communication of the approaches taken. But it is a new taxonomy and may be viewed as a complication since the complexity today in inventory approaches is generally hidden from view.

7. Would the proposal improve alignment with other climate disclosure rules, programs and initiatives or lead to lack of alignment? Please describe.

We believe this proposal would improve alignment with other climate disclosure rules/ programs/initiatives in that it would allow such programs to decide and clearly communicate the expected or required accounting pathways for participating/affected companies.

For example, today CDP publishes an extensive technical guidance document to inform companies of expected scope 3 category relevance determinations, by sector. A pathways approach could encompass scope 3 category relevance as part of its makeup, such that declaring appropriate pathways for important sectors would communicate not only scope 3 category relevance, but also (for example) measurement system fidelity expectations for each scope.

8. Please attach or reference supporting evidence, research, analysis, or other information to support the proposal, including any active research or ongoing evaluations. If relevant, please also explain how the effectiveness of the proposal can be evaluated and tracked over time.

Please see the final page of this proposal.

9. If applicable, describe the process or stakeholders/groups consulted as part of developing this proposal.

This proposal resulted from detailed conversations across 3Degrees, including our climate consulting practice (which serves some of the largest companies in the world as well as many small/unlisted companies), but did not involve other stakeholders.

10. If applicable, provide any additional information not covered in the questions above.
N/A

Differentiated Accounting Pathways: Example

This graphic provides a brief illustration of differentiated accounting pathways using "measurement system fidelity."

In this example, a number of possible accounting pathways are available as reporters choose less-granular or more-granular measurement systems for each scope. Guidance would explain that low-fidelity approaches are preferred for smaller emitters generally, and for any emitter whose emissions in a given scope are unimportant to internal and external decision-making.

The choices made would affect the goals and achievement claims available, since low-fidelity approaches do not support quantitative goals; goals describing specific actions or quantified emission reduction efforts could be used instead.