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Scope 3 Materiality: The Full Picture

Insight Briefing #5

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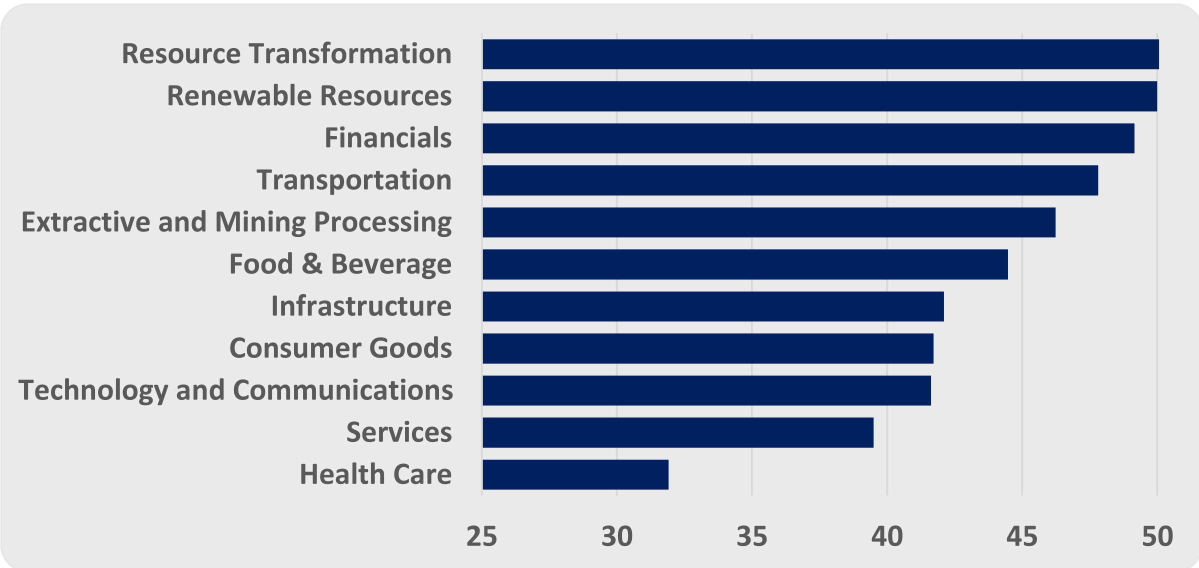
Scope 3 Materiality: The Full Picture

In our last Insight Briefing (*see Disclosure Delight – Insight Briefing, May 2022*), we highlighted positive progress on corporate emissions reporting globally. This improvement included increases in overall Scope 3 emissions disclosure rates. Indeed, we found that 44% of all companies we track in our global universe of major investable securities reported at least one category of Scope 3 emissions in the last reporting year. The average number of Scope 3 categories being reported by the companies we analysed is now 10 (out of the 15 categories).

Figure 1: Percentage of Companies Reporting Scope 3 Emissions by Sector



Source : Urgentem

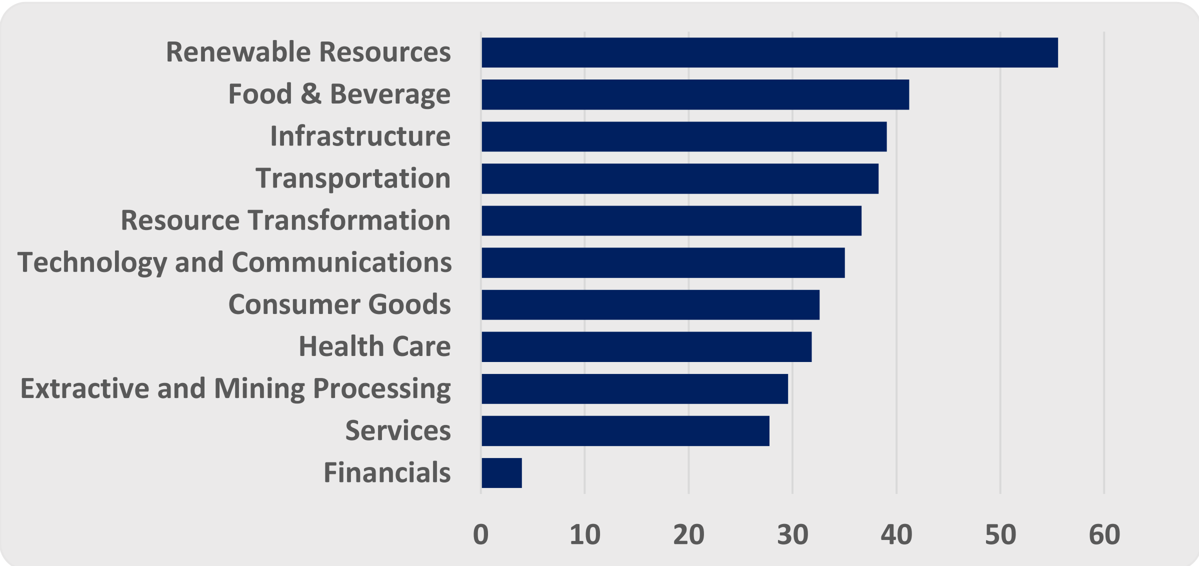
However, when it comes to Scope 3 emissions, understanding the details of the disclosure across the different categories is important. Just because a company has published some level of Scope 3 emissions does not necessarily mean that investors have the full and complete picture.

Materiality Matters

So, here we dig a little deeper in an attempt to gain a better understanding of the completeness of Scope 3 emissions being reported. We extend our analysis to examine if this improvement in Scope 3 disclosure has encapsulated the most important emissions for individual companies. Our more detailed analysis looks not just at the number of categories being reported, but also examines if emissions in the most relevant (material) categories for any given sector are also being disclosed.

In previous Insight Briefings we have discussed the importance of Scope 3 emissions, which can represent on average 85% of a company's total emissions, and in some cases significantly more! While we have noted an overall improvement in Scope 3 emissions reporting in terms of the number of companies reporting some level of Scope 3 and the number of categories being reported, it is crucial to check if companies have provided the details for the most important and relevant categories for their particular sector.

Figure 2: Percentage of Companies Reporting All 15 Categories of Scope 3 by Sector



Source : Urgentem

While Scope 3 covers a huge area of a company's emissions, encapsulating entire supply and value chains, our materiality analysis of Scope 3 emissions has found that in every sector a single, or just a couple of categories, are responsible for the overwhelming majority of Scope 3 emissions, and hence the majority of a company's overall emissions.

Sector Sensitive

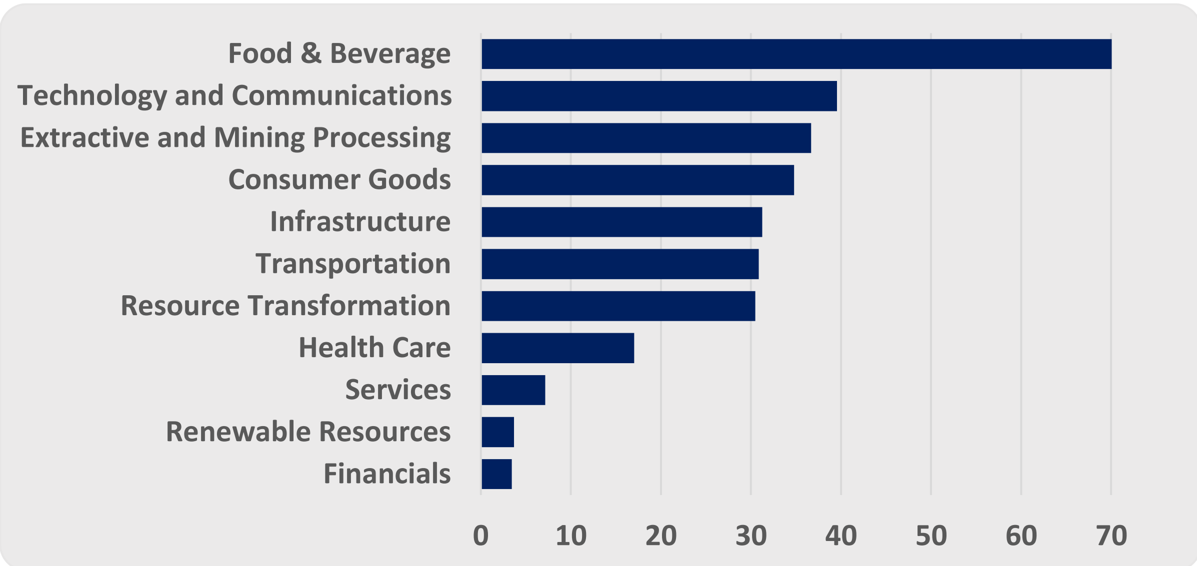
The specific categories of importance within Scope 3 are also highly dependent on the particular area of operations for any given company. These material Scope 3 categories are highly industry and sector sensitive.

For example, the Scope 3 emissions of the Extractives and Minerals Processing sector are highly concentrated within category 11, Use of Sold Product. This contrasts with the Financial sector, where the vast majority of Scope 3 emissions reside in category 15, the investments category.

Urgentem carries out detailed Scope 3 materiality analysis on a regular basis to identify the extent to which Scope 3 emissions are concentrated within individual categories for each sector and to assess the completeness of reporting and disclosure by sector and individual companies.

While we have noted great progress in overall emissions disclosure, sadly the number of companies reporting the most material category for their particular industry is still low at just 13% of all the companies we track in our global universe of major investable securities. When we carry out this analysis for those companies that have reported at least one category of Scope 3, we found that the average rate for companies disclosing their most important category of Scope 3 emissions was still only 28% across all sectors.

Figure 3: Percentage of Companies Reporting Material Category of Scope 3 by Sector



Source : Urgentem

Mixed Reporting

Again, there are significant and interesting sector variations when it comes to reporting of the important Scope 3 categories. While the Resource Transformation, Renewables and Financial sectors stand out as having the highest percentage of companies boasting at least one category of Scope 3 emissions disclosure, two of these sectors also rank among the bottom three when it comes to reporting the most important Scope 3 category for their industry. The two sectors in question are Renewable Resources and the Financials sectors.

Indeed, only 4% of the companies within the Renewable Resources sector which report at least one category of Scope 3, disclosed the emissions for the most material Scope 3 category, while for the Financials sector the material Scope 3 category disclosure rate stood at just 3.5%, according to our analysis.

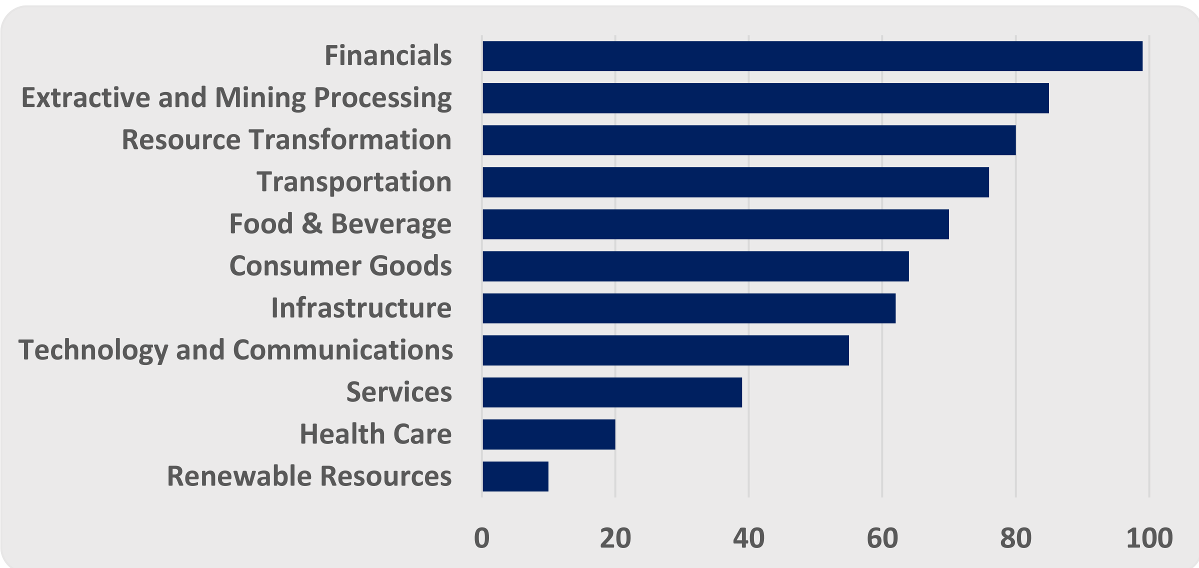
For the Renewable Resources sector this may not be too much of an issue as Scope 3 emissions are relatively more evenly distributed across the 15 categories compared to most sectors.

Financials Concentration

However, for the Financial sector this is extremely important. The Financial sector has the greatest concentration of Scope 3 emissions in a single category, namely category 15, Investments. Over 90% of a financial company's Scope 3 emissions can emanate from its investments, making category 15 disclosure extremely important. While we are seeing some improvement in this area of reporting, the Financial industry is still lagging many other sectors when it comes to disclosure of its most significant Scope 3 emissions.

At the positive end of the scale, the Food and Beverage sector stands out with 70% of the companies we analysed that report at least one category of Scope 3 emissions also disclosing the most important category. However, it must be pointed out that the category in question is one of the more widely reported generally. Following the Food and Beverage sector is the Technology and Communications sector with a 40% material category Scope 3 disclosure rate.

Figure 4: Percentage of Scope 3 Emissions in Material Category by Sector



Source : Urgentem

Extractives: Better Than Average

The Extractives and Minerals Processing sector, which is often the focus of our analysis given the sector's high emissions profile, actually comes out relatively better as far as Scope 3 disclosures are concerned and indeed emissions reporting overall. Within this sector, 78% of the companies we analysed provided at least some level of emissions disclosure. When it comes to Scope 3 reporting the Extractives and Minerals Processing sector is also above average (just) with 46% of companies reporting at least one category of Scope 3. For the most material category of Scope 3 (category 11, Use of Sold Product) again the Extractives and Mineral Processing sector is in the top 3 with 37% of companies providing data for this crucial category. We would, however, note that the higher levels of regulation within the Extractives and Mineral Processing sector may well be a contributing factor to these relatively higher emissions disclosure rates.

Conclusion

Overall, while emissions reporting is improving, even for Scope 3, we continue to emphasise the importance of careful and detailed analysis of individual companies' disclosures to gain a full understanding of a company's carbon footprint and alignment to various climate scenarios. Even the omission of a single category of Scope 3 can represent a major underestimate of a company's total climate impact.

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