→ Position paper — energy-use

PUBLIC SECTOR SUPERANNUATION SCHEME

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Superannuation funds are averse to unpredictable or unjustified risk and will seek to avoid major disruption and uncertainty that could impact on portfolio value.[1] Investors failing to take account of climate change and carbon finance issues in their asset allocation and equity valuation may be exposed to significant risks that, if left unattended, are likely to have serious investment repercussions over time.[2]

In the current environment, the financial risks to Australian companies of not managing their energy-use and greenhouse gas (GHG) emissions are increasing through a variety of related regulatory and reputation factors. These include:

→ Internationally, scientific consensus on climate change is strengthening and is being translated into action by governments. A number of European countries have introduced carbon taxes to control energy demand and GHG emissions,[3] and New Zealand and Japan have announced similar intentions.[4] UK Prime Minister, Tony Blair, has announced plans to cut CO2 emissions in Britain by 60% by 2050.[5]

→ The NSW state government introducing compulsory greenhouse benchmarks for electricity retailers, requiring them to reduce emissions by 5% on a per capita basis by 2007 compared with 1989–1990 levels.

Monash University has analysed the energy-use practices of the S&P/ASX 200 companies. Sectors with the highest levels of exposure include the manufacturing, mining, energy, building materials and transport sectors due to the energy intensive nature of their operations.[6] Given the level of risk, energy-use and GHG emissions data is under-reported by Australian companies,[7] which concurs with the worldwide findings of the Carbon Disclosure Project (CDP).

This Position Paper does not argue for or against the Kyoto Protocol. The Paper arises from the exercise of fiduciary duty to manage investment risk — on this occasion, in relation to energy use.

A background paper to this Position Paper outlines costs of energy-use practices including energy price risk, insurance costs and savings gained from improved efficiency and a higher return on investment from managing energy-use. It also outlines the business case for the management of GHG risk. Due to the increasing regulations and the direct cost benefits of minimising energy costs and risks, the management of energy-use and GHG emissions by Australian companies is necessary to mitigate financial risks and to reduce business costs.

1_Mansley, M. & Dlugolecki, A., 2001, Climate Change: A Risk Management Challenge for Institutional Investors, Discussion Paper No.1, Universities Superannuation Scheme Ltd: London p11.
2_Carbon Disclosure Project (CDP), 2003, Final Report, Innovest Strategic Value Advisors, p3
3_Reuters, 2002, 'World needs global green tax — EU agency head', Planet Ark News, 18 April, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=15532.
4_Ecogeneration, 2002, New Zealand proposes carbon tax, Ecogeneration Magazine, June/July, p15.
5_Times Online, 2003, 'Blair plans 60% cut in greenhouse gas output', 24 February, http://www.timesonline.co.uk.
6_The CDP has found that the financial impact of climate change will also affect financial services, transportation, agriculture, tours, and food sectors.
7_Further discussion of these risks and other environmental disclosure related issues can be found in the PSS/CSS Position Paper on Environmental Disclosure, August 2002, http://www.pss.gov.au/pss/news/environmental_non-disclosure.html.

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Results of the analyses suggest companies should:

- → Acquire or use appropriate expertise to ensure that informed energy-use and GHG emission-related decisions are made at all levels within the company;
- → Implement management initiatives to identify risk exposure and opportunities relating to energy-use and GHG emissions reduction — for example, by participating in voluntary government and/or industry based programs; and
- → Disclose energy-use and GHG emissions reduction strategies, targets and trends (consistent with the Greenhouse Protocol).[1]

Background to a position paper: The Business Case for Managing Energy Intensity Energy Price Risk

Rising energy prices in recent years have added to costs of production at all levels and are therefore reducing the profitability of firms.[2] Energy costs may also rise due to an increase in the Commonwealth legislated mandatory renewable energy target.[3] As energy costs and the costs associated with GHG emissions increase, companies not reducing energy-use and GHG emissions, risk losing control over operating expenses.

In a deregulated electricity market, reducing energy-use assists in managing electricity price risk. Modelling by Westpac Energy (part of Westpac's Financial Markets Group)[4] indicates that electricity price risk is often greater for Australian industrial companies than interest rate risk. In analysing the sensitivity of a number of industry sectors to both interest rate risk and electricity price risk, they found that for many companies the latter is greater. For example, a typical cement manufacturer could expect to have 11% of its after tax earnings at risk to interest rate movements (in the absence of hedging) and 16% at risk to fluctuations in wholesale electricity prices. In Europe, BASF, the German chemicals giant, estimates that every Euro 0.01 increase per kW hours results in additional costs of about Euro 58 million for some manufacturing sites.[5]

Australian companies can reduce exposure to energy price risk through better management of energy-use. For example, in 2001 Amcor invested $600,000 on an energy management program for its NSW operations. Projects with the capacity to deliver over $1.8 million in annual energy savings have been identified. A number of these have been implemented, saving $716,000 in the first year.

Efficiency

Energy costs can be the most closely controllable overhead after labour costs[6] and directly affect the bottom line.

Investment in energy efficiency competes with other capital investment. However, a growing number of cases reported by companies indicate that energy efficiency expenditure can also offer substantial returns compared to other investments. The cost savings and financial returns, and the potential to reduce GHG related risks through energy efficiency, provide additional weight to decisions regarding capital allocation.[7]

Monash research concluded as few as 14 S&P/ASX200 companies have integrated energy and GHG mitigation into corporate environmental management systems. This suggests that a significant majority of companies have not yet integrated continual improvement in energy efficiencies into day-to-day operations.

Return on investment (ROI)

Capital investments in energy efficiency, such as whole building upgrades, are sound financial investments.[8] A study conducted in the US assessed the financial risk and return from fourteen whole building energy efficiency upgrade projects.[9] The internal rate of return of the investment was calculated using a ten year project lifetime and the investment risk was measured as the variability in the expected investment return — the risk that it would produce more or less than the expected return on investment.

1_For example, CO2 emissions per tonne of output, $ energy expenditure/$ revenue, or $ fuel expenditure/$ revenue.
2_A survey of the members of the Australian Chamber of Commerce and Industry (ACCI) found that the cost of energy was the eighth of ten issues of most concern to Australian businesses. (ACCI, 2001, What business wants: ACCI's pre-election survey results, Australian Chamber of Commerce and Industry: Canberra, September.)
3_Australia's target is presently 2%, but is currently under review by the Federal Government. The UK Department of Trade and Industry estimates that power prices will increase by 5% to meet the UK's renewable obligation of 10% (presently 3%) of total energy production by 2010.
4_Bullock, G., 2002, 'Power to the people has a cost', The Australian, Business Survey Series no. 16, 20 November, p14.
5_CDP 2003 op. cit, p13.
6_In some industries, such as the aluminium industry, they can even be greater than labour costs.
7_For example, a recent study found that leaders in energy management in the US retail sector, taken as a group, outperformed laggards by nearly 70% over the past five years.
8_Romm, 1999, Cool Companies — How the Best Businesses Boost Profits and Productivity by Cutting Greenhouse Gas Emissions, Island Press: Washington, DC p55.
9_Rickard, S. et al, 1998, 'The Investment Risk in Whole Building Energy-efficiency Upgrade Projects', ACEEE 1998 Summer Study on Energy Efficiency in Buildings Proceedings, American Council for an Energy Efficient Economy, Washington, DC, pp4.307–4.318.

The average return was more than 20%, with a coefficient of variation (risk) less than one (this compares favourably against a range of investments such as the ASX 200, S&P 500, both government and commercial bonds).

For example:

→ US Aircraft manufacturer Boeing reduced the electricity used in lighting its buildings by up to 90% with a two year payback (ROI = 50%). The new higher quality lighting has cut down glare and helps workers reduce defects.[1]
→ Between 1992 and 2001 IBM's US operations invested in changes to manufacturing processes and facility infrastructure, including the use of high efficiency motors and lighting, and reducing reheat energy. These changes have saved an estimated 9.0 billion kw hours of electricity, avoided 5.5 million tonnes of CO2 emissions and reduced energy expenses by approximately US$508 million.[2]

Similar cases exist in Australia, for example:

→ Coles Supermarkets in Victoria has cut energy costs by $1 million and saved 17,000 tonnes of GHG emissions with a new lighting efficiency program. It expects to make more savings as it continues to develop high efficiency systems. More than 50 supermarkets across Victoria now reduce their lighting bills by more than $20,000 each year achieving combined savings exceeding $1,000,000 pa. Investment payback is less than 2 years (ROI > 50%).[3]

Cost savings

Australian case studies provide support that reducing energy-use can reduce oper-ating costs. Energy efficiency experts claim savings of at least 20% for factories, office buildings, hotels and shopping centres by following energy efficiency best practice.[4] Key areas typically identified for savings include lighting, heating, ventilation, air conditioning, motors, compressed air, and steam systems.

For example:

→ Coca-Cola Amatil has invested up to $130,000 in energy efficient lighting at all of its Australian sites. Its electricity consumption has dropped by 30 to 40% and the company is saving $30,000 to $50,000 pa at some sites.[5]
→ Telstra has identified a number of energy saving possibilities at two of its facilities in Sydney. The initiatives, including lighting controls, air conditioning audits, and power factor correction projects, will save $149,000 in annual energy costs and 2,500 tonnes in CO2 emissions per year with less than a two year payback (ROI > 50%).[6]

The CDP argues that early movers are better positioned to achieve cost effective risk management solutions, adapt to unforeseen future developments and exploit any upside opportunities. Both Federal and State Governments have recognised the benefits of energy efficiency. A range of subsidies and grants are available through the Australian Greenhouse Office (AGO) and state based authorities, such as SEDA, that provide cost savings to complying companies.

Insurance costs

Insurance costs may increase for those companies not reducing the energy and greenhouse intensity of their operations. Conversely, Insurance Australia Group has suggested that cheaper premiums may be offered to those undertaking energy-use and GHG emission reduction initiatives.[7]

The extent to which energy use and GHG emissions are prioritised by company directors and management is of potential concern to investors. Monash found only 18 S&P/ASX 200 companies have publicly disclosed commitments to reduce energy use or GHG emissions.

1_Romm, 1999, op. cit. p47.
2_IBM, 2002, Annual Environment Report, http://www.ibm.com/ibm/environment/annual2002/energy.shtml, access date: 18 November.
3_SEAV, 2002, Business Case Studies, http://www.seav.vic.gov.au/business/case_study/dnload/coles.pdf, access date: 11 November.
4_SEDA, 2002, http://www.seda.nsw.gov.au, access date: 19 December.
5_Australian Greenhouse Office, 2002, Greenhouse Challenge — Success Stories, http://www.greenhouse.gov.au/challenge/html/achievements/success_stories/coca_cola.html, access date: 11 November.
6_Source: Origin Energy Ltd.
7_Coleman, T., 2002, The Impact of Climate Change on Insurance against Catastrophes, Insurance Australia Group, p11.

Management of GHG Risk

Industrial companies operating in OECD countries will have some exposure to GHG emissions regulation.[1] Future regulatory trends, both internationally and in Australia, are likely to place constraints on the use of non-renewable energy and GHG emissions.

For example, the recently completed Government Business Climate Change Dialogue has urged Australian governments to develop a national energy efficiency program to help Australia overcome the effects of greater GHG emissions.[2] In the UK, the government has warned the airline industry that it will have to pay, through taxes and new regulation, for the estimated £1.4 billion that its GHG emissions cost Britain every year.[3]

Kyoto Protocol

Ratification of the Kyoto Protocol (Kyoto) internationally is a risk for Australian companies. Under Kyoto, most developed countries have agreed in principle to binding targets to reduce GHG emissions. Australia negotiated a target of 108% of 1990 levels to be achieved between 2008–2012. A target of 108% represents a significant reduction relative to the 'business as usual' case. The Australian government has decided not to ratify Kyoto stating that ratification would disadvantage some sectors of the economy, however it remains committed to meeting the 2008–2012 target.

While the Australian government remains opposed to ratification of the Kyoto Protocol,[4] there is widespread recognition by business and other stakeholders that regulation of energy-use and GHG emissions is likely to tighten in the short to medium term:

- → The Business Council of Australia (BCA) believes a global agreement including Australia and the US is inevitable and that reducing energy-use and GHG emissions to meet the Kyoto target now will make it easier and cheaper to meet future targets.[5]
- → Greater consensus is emerging among leading multinational companies that international action is necessary to reduce GHG emissions.[6]
- → Surveys of community attitudes in both the US[7] and Australia,[8] two countries that do not support the protocol, reveal support for both ratification and greater efforts to reduce energy-use and GHG emissions.
- → Strengthening of scientific opinion on reductions in energy-use and GHG emissions being necessary to minimise the risk of climate disruption[9] increases the potential of tighter regulation in future.[10]

Australian regulation and government initiatives

The Federal government has stated that it will rely chiefly upon voluntary measures to achieve its Kyoto target. However, trends toward mandatory regulation of energy efficiency and GHG reductions are emerging at the State level.

For example:

- → In Victoria, companies emitting more then 1,400 tonnes of energy related CO2 will be required to prepare an action plan for implementing measures which are consistent with world's best practice in energy efficiency. Under the scheme, all EPA licence holders must undertake an energy audit and report to the EPA on their progress.[11]
- → The NSW state government has introduced compulsory greenhouse benchmarks for electricity retailers, effective from 1 January 2003. Retailers must reduce emissions by 5% on a per capita basis by 2007 compared with 1989–1990 levels.[12]
- → The NSW Independent Pricing and Regulatory Tribunal recently recommended that greater energy efficiency be best achieved through additional mandatory codes and standards.[13]

1_CDP 2003, op. cit.
2_Wilson, N. 2003, 'Greenhouse action urged', The Australian, 14 April.
3_Ananova.com, March 2003.
4_The Australian Labor Party recently (May 2003) announced its intention to introduce a private members' bill to force ratification of the Kyoto Protocol.
5_Miller, 2002, op. cit.
6_A group representing some 160 multinational enterprises made a joint statement with the environmental group Greenpeace calling on world leaders for an international system for halting global warming. Pomeroy, R., 2002, 'Industry joins Greenpeace to demand climate action', Reuters News Service, 30 August, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=17509.
7_Reuters, 2002, 'US voters want strict greenhouse gas cuts — survey', Planet Ark News, 11 July, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=16805.
8_Greenpeace, 2002, Australians Support Kyoto, Media Release, http://www.greenpeace.org.au/media/pressdetails.php?siteid=8&newsid=724.
9_Scientific estimates indicate that reductions of 60% in developed countries are required to minimise the risk of climate disruption. IPCC, 2002, op. cit.
10_Recent technical analysis by the CSIRO suggests that despite present reduction efforts Australia's GHG emissions are likely to rise to between 170% and 230% of 1990 levels by 2050. (Foran, B., & Poldy, F., 2002, Future Dilemmas: Options to 2050 for Australia's population, technology, resources and environment', CSIRO Sustainable Ecosystems, Canberra: October, p157.)
11_EPA Victoria, 2002, Protocol for Environmental Management: Greenhouse Gas Emissions and Energy Efficiency in Industry, EPA Victoria, Jan.
12_Ecogeneration, 2002, Penalty set at $15 for NSW benchmarks, Ecogeneration Magazine, June/July, p15.
13_Environmental Manager, 2002a, op. cit: 6–7.

Market based mechanisms

Emissions trading

Emissions trading is favoured by key stakeholders because it encourages abatement at least cost and with high efficiencies. On balance, the prevailing view[1] is that a carbon trading scheme will be introduced in Australia in the short to medium term regardless of whether the federal government ratifies Kyoto.[2] The Third National Communication on Climate Change states that the decision against ratification 'does not rule out the subsequent introduction of such a scheme if further analysis demonstrates that this would be in the national interest.'[3]

Emissions trading schemes will be introduced in the EU and Japan in 2005, and while Australia has decided against ratification of Kyoto in the short term, recent events provide evidence of trends toward market-based solutions to reduce GHG emissions.[4]

For example:

- → The Council of Australian Governments (COAG) Energy Market Review has recommended that emissions trading be introduced in the electricity and gas sectors and that while intensive energy-users in the traded goods sector should be exempted (eg aluminium, steel), they should be required to achieve world's best practice in energy efficiency.[5]
- → The Australian Chamber of Commerce and Industry (ACCI) believes emissions trading, given the right conditions, should be considered as an option to provide substantial, least-cost abatement.[6]
- → The Shadow Federal Environment Minister has announced that a future ALP government would work with state governments to introduce emissions trading.[7] Companies, both internationally and in Australia, are beginning to trade CO2 to gain experience with emissions trading.[8,9] For example, in the US the Chicago Climate Exchange, which includes major US companies such as Ford, Dupont and American Electric Power, has been launched with companies agreeing to a voluntary but legally binding GHG emission cap and trade program.[10]

While uncertainty exists with respect to the final form trading schemes are likely to take, parties that meet their emissions obligations will be able to trade credits with companies unable to meet emission obligations.

This will expose less efficient companies to higher costs of compliance[11] and competitive advantage will shift toward those companies who are less emission reliant.[12] Experience indicates that some companies are not prepared for the potential CO2 liabilities that will likely arise should trading be introduced.[13]

Carbon taxes

Carbon taxes are also being introduced overseas to control energy demand and GHG emissions. Many of the European Union's 15 countries have introduced carbon taxes,[14] and New Zealand has announced similar intentions.[15] The Electricity Supply Association of Australia has assessed the effect on energy prices of such a scheme in Australia. It estimates that a carbon tax would increase retail electricity prices by between 7% and 25%, depending upon the price set, and that these increases will be significantly higher for industrial users.[16]

Research conducted by Monash found that only 20 ASX 200 companies provided information on energy use or GHG emissions in corporate disclosures.

1_For example, Richard Martin, CEO of NM Rothschild Australia has argued that 'With recent developments in international climate change policy, the question is no longer if, but when the global carbon trading market will emerge.'
2_Myer, R., and Hopkins P., 2002, 'How does Australia scrub up at the carbon sink?' The Age, 21 September, pB3.
3_The Australian Greenhouse Office, 2002, Australia's Third National Communication on Climate Change, Australian Greenhouse Office, Canberra, http://www.greenhouse.gov.au/international/third-comm/chapter4.html.
4_Bipartisan legislation has been introduced into the US Senate to cap emissions from electricity, industrial, commercial, and transport fuel sectors at 2010 levels. The bill provides for a mandatory emissions trading scheme: Anon., 2003,'Grass-roots greenery', The Economist, January 18, Issue 8307, Vol 366, p47.
5_Council of Australian Governments Energy Market Review, 2002, Towards a Truly National and Efficient Energy Market, Commonwealth of Australia, Canberra, December.
6_ACCI Chief Peter Hendy quoted from a speech delivered on his behalf at an Aust Emissions Trading Forum seminar in March, 2003.
7_Environmental Manager, 2003, Thompson to table ratification Bill, Environmental Manager, Issue 435, 6 May.
8_Saunders, C., 2003, 'Traders of nothing — How carbon emissions may save capitalism', Australian Financial Review, January 18–19, p45–46.
9_For example, twelve Australian companies recently paid $US100, 000 to participate in a carbon trading simulation run by NM Rothschild and the E3 group. Some 146 trades in 141 million tonnes of carbon dioxide valued at a turnover of $1.4billion ($10 per tonne) were made. One company failed to comply because it lacked the capital to buy enough permits to cover its emissions.
10_Greenbiz.com, 2003, 'More US Companies Launch Climate Change Initiatives', Greenbiz.com, April, http://www.greenbiz.com/news/news_third.cfm?NewsID=24336.
11_State Forests of NSW, 2002, Growing Trees for Carbon Credits — A Guide for Landholders, State Forests of NSW: Discussion paper, http://www.forest.nsw.gov.au/publication/forest_facts/growing_trees/default.asp.
12_Janissen, B., 2002, op. cit.
13_Trexler, M., 2002, 'Is $0 your best guess?' Environmental Finance, May, p23.
14_Reuters, 2002, 'World needs global green tax — EU agency head', Planet Ark News, 18 April, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=15532.
15_Ecogeneration, 2002, New Zealand proposes carbon tax, Ecogeneration Magazine, June/July, p15.
16_ESAA Generation Directorate, 2002, Impact of a carbon cost on Australia's electricity generation, Electricity Supply Association of Australia Limited, Melbourne.

Reputation Risk

Protection of corporate reputation is a key driver for a business to reduce energy consumption.[1] Some companies already involved in decreasing energy use are using their experiences for promotional purposes. For example, eight companies in the US have formed the Partnership for Climate Action, a vehicle that publishes positive results on emissions trading, emission credit generating projects, and emissions figures.[2] In the UK the government has launched an advertising campaign to publicise the performance of retailers and financial institutions that are energy efficient.[3]

Companies perceived by the general public as being major emitters of GHG, and who appear obstructive to mitigation efforts or 'anti Kyoto', may face boycott or other consumer protest actions (particularly in Europe). For example:

→ Green campaigners shut down all 28 of Esso's fuel stations in Luxembourg in protest at Greenpeace's claim that ExxonMobil contributed to the US decision not to ratify Kyoto.[4] Deutsche Bank has warned ExxonMobil that investors should be worried about the Greenpeace-backed StopEsso campaign because it is considered a brand risk.[5]

→ A US website has been launched to facilitate consumer boycott of the products of some companies not actively working toward decreasing energy usage. The website states: 'Brands and companies that don't respect the climate deserve to be pilloried'.[6]

Litigation Risk

While a very minor risk at present, as those affected by climate change seek redress in the courts from those seen as responsible, legal liability is a potential risk for energy and GHG intensive companies.[7]

The real costs to defendants of such actions would be reputational and legal rather than reparatory because they would be difficult to win (although NGOs like Greenpeace may run a case for a plaintiff as a cause celebre). However, flow-on effects may include 'licence to operate' concerns and the tightening of energy and GHG regulatory regimes in response to changes in public expectations and perceptions.[8] Companies may face lawsuits similar to those that have affected the tobacco industry.[9]

Market Responses to GHG Risk

Access to markets

A number of initiatives such as energy ratings schemes for buildings, vehicles, and household appliances are allowing for the integration of energy efficiency principles into procurement decisions across a range of sectors. Companies unable to offer products with adequate efficiency credentials may find it difficult to maintain market share. Federal Environment Minister, Dr David Kemp has stated that Australia is 'exporting in a world market which is less and less carbon tolerant, and which will become more reluctant to buy products which do not have better environmental qualities.'[10]

Energy and GHG intensive companies face the possibility of increased costs of capital. Major emitters may have to pay higher debt charges to climate conscious investors if emissions reduction steps, necessary to mitigate energy and GHG emissions risk, are not factored into project or business economics.

Financial Markets

GHG risk is embedded in every business and investment portfolio. Those not reducing the GHG risks discussed above may be susceptible to future losses of shareholder value.[11] Addressing issues of climate change risk is an essential part of good governance and fiduciary responsibility.[12]

1_ http://www.seav.vic.gov.au.
2_Freehills, 2002, Renewable Energy and Greenhouse Newsletter, 25 November, http://freehills.com.au.
3_CO2e.com, 2003, Government to publicise 'green' firms', 26 February, http://www.co2e.com/News/story.asp?StoryID=1030.
4_Reuters, 2002, 'Greenpeace shuts down ESS Luxembourg petrol pumps', Planet Ark News, 28 October, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=18344.
5_Macalister, T., 2002, 'Greenpeace hails Deutche warning', The Guardian, 11 October, http://www.guardian.co.uk./Print/0,3858,4521925,00.html.
6_FAB is a campaign to encourage commitment by the US to cap and cut its GHG emissions and rejoin global action to save the climate by highlighting the differences between different companies/brands in their approach to climate change mitigation — http://www.fabclimate.org.
7_See for example, Ward, H., 2001, Governing Multinationals: The role of Foreign Direct Liability, Royal Institute of International Affairs Briefing Paper, February.
8_Kerr, M. 2002, Tort Based Climate Change Litigation in Australia, Australian Conservation Foundation: Melbourne.
9_A recent report by former Chase Manhattan financial analyst Mark Mansley has concluded that, based on the litigation brought against the tobacco industry by sick smokers, the oil industry may incur damages in excess of US$100bn if found to be legally responsible for global warming. Mansley, M., 2002, Risking Shareholder Value? ExxonMobil and Climate Change, An Investigation of Unnecessary risks and Missed Opportunities, Claros Consulting, May.
10_Quoted in a speech to a climate change conference hosted by the Institute of Public Affairs, March 2003.
11_Modelling undertaken by Innovest in the US has found that the discounted present value of potential carbon liabilities within an energy-intensive manufacturing firm could represent up to 40% of its market capitalisation.
12_Innovest, 2002, Value at Risk: Climate Change and the Future of Governance, Innovest Strategic Value Advisors, Inc: New York, April.

Recently the Chairman of the ASX, Maurice Newman AC, stated that 'directors of emitters who don't take some precautionary measures soon, either by curbing emissions or by beginning a process of acquiring emission credits, could be putting themselves at risk for failing their duties as directors and be liable for damages from shareholders and customers some time in the future.'[1]

Consequently governments and long term investors, such as pension/ superannuation funds, are seeking ways in which to encourage companies to reduce risks to long term shareholder value and to disclose energy and GHG emissions to enable assessment of risk.[2]

For example:

→ Europe's largest pension fund, ABP, has recently begun addressing energy-use and climate risk in its stock selection process, beginning with two $100 million 'experimental' portfolios. On the basis of the portfolios' early outperformance, the fund is currently considering expanding the use of this 'environmental risk overlay' to a larger proportion of its $140 billion portfolio.

→ In 2002, representing a consortium of international institutional investors with $4 trillion in assets, the CDP sought GHG emissions disclosure from the global top 500 companies. The project arguably represents the most explicit acknowledgement yet that the financial community accepts the issue of climate change, and are addressing a need to protect their assets and avoid climate-related liability. A key finding was that while 80% of respondent companies acknowledge the importance of climate change as a financial risk, only 35–40% were actually taking action to address the risks and opportunities.[3]

Due to the possibility of regulatory and litigious constraints on energy companies emerging as a risk to shareholder value, the US Congress is presently investigating whether energy companies are adequately disclosing environmental risks, raising the possibility that disclosure of energy-use and GHG emissions may be mandated.[4]

Shareholder activism

Institutional shareholders in the US are using their voting rights to pressure companies to reduce energy and GHG-related risks to shareholder value.[5] These include mainstream pension funds like the California Public Employee Retirement System (CalPERS), and America Institutional Shareholder Services (ISS).[6]

For example:

→ In 2003, 140 environment and social issue-related proxy resolutions have been filed against 92 companies, 31 of which (up from 19 and 8 in the previous two years respectively) were energy and GHG related. These sought disclosure of GHG emissions and the adoption of energy-use reduction policies. The average support level for these resolutions has more than doubled since 2000, rising to an average of 18.8% in 2002.[7] One resolution against Canadian steel firm IPSCO recently drew 49.2% support.[8] In 2002 several were withdrawn after companies agreed to produce information on emissions and engage in dialogue with shareholders.[9]

→ Among those facing GHG related shareholder resolutions in 2003 are the five largest CO2 emitters among US electric power companies. A coalition of shareholders, including the State of Connecticut Plans and Trust Fund, filed the resolutions calling on companies to report the economic risks associated with GHG emissions and the economic benefits of committing to substantial GHG reductions,[10] with more than 26% supporting the resolution against American Electric Power.[11]

1_Quoted in AETF review, April/May 2003.
2_For comparative examples, see Calpers in the US and HERMES in the UK.
3_CDP 2003, op. cit. p1.
4_Reuters, 2003, 'GAO to meet regulators on corporate green liability', Reuters News Service, 10 January, http://www.planetark.org/avantgo/dailynewsstory.cfm?newsid=19352.
5_Bayon, 2002, op cit: 31.
6_Friedman, J., 2002, 'Survey: More investors are questioning corporate governance and backing resolutions that go against management's wishes', Los Angeles Times: Los Angeles, 30 May, pB1.
7_Greenbiz.com, 2003, 'Treasurers warn of risks to investments from Climate Change', 3 April, http://www.greenbiz.com/news/news_third.cfm?NewsID=24364.
8_Socialfunds.com, 2003, Canadian Greenhouse Gas and Toxic Emissions Resolution Garners Near Record Support, 7 May, http://www.socialfunds.com/news/article.cgi/article1115.html.
9_Knight, D., 2002, 'Environment: Shareholders Challenge Companies on Global Warming', Inter Press Service, 2 May.
10_Hastings Group, 2003, 'Top five CO2 emissions polluters among electric utilities face shareholder resolutions on global warming', Press Release, 16 January, http://www.hastingsgroup.com/release011603.pdf
11_Environment News Service, 2003, 'Shareholders Worried About Global Warming', 23 April, http://ens-news.com/ens/apr2003/2003-04-23-09.asp#anchor1.

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