



# A CLIMATE DISCLOSURE FRAMEWORK FOR SMALL AND MEDIUM-SIZED ENTERPRISES (SMEs)



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## **OVERVIEW**

A significant proportion of the world's businesses are small and mediumsized enterprises (SMEs). Globally, micro-enterprises (SMEs with fewer than ten employees) alone account for 70% to 90% of all firms<sup>1</sup>. As such, SMEs play an important role in reducing global emissions and bringing innovative climate solutions to the market. It is crucial that they are equipped with the tools and resources needed to measure their emissions, set greenhouse gas reduction targets grounded in science, take bold actions, report on their progress and ultimately reduce their emissions. This framework provides guidelines for SMEs on doing exactly that. It is open for anyone to use and can be used directly by SMEs to guide their reporting of climate impacts and strategies to multiple stakeholders. It can also be used by SME support organizations (such as consultancies) and data collectors to guide SMEs in climate disclosure.

The IPCC's Sixth Assessment Report is the latest reminder that dangerous climate thresholds are rapidly nearing and that impacts will continue to occur sooner rather than later. With  $1.1^{\circ}$ C of warming so far<sup>2</sup>, our climate has already changed, and some impacts are a reality. Immediate, rapid and large-scale reductions of greenhouse gas emissions are needed to limit global temperature rise to  $1.5^{\circ}$ C.

The framework is built up of a core section (consisting of three modules referred to as the "core modules") and four additional modules. Each module provides indicators that are considered important for SMEs to report on in their climate disclosures.

CORE MODULES						
MEASURE		СОММІТ		ACTION & IMPACT		
MODULE: ENERGY REPORTING	MODUL VALUE CH EMISSIC		LE: HAIN DNS	MODULE: MANAGEMENT & RESILIENCE		MODULE: CLIMATE SOLUTIONS
Module Name		Reasoning				
Core Module: Measure			Measuring emissions is a crucial first step that every company must take to understand its negative impact on the climate and take the right steps to reduce it.			
Core Module: Commit			Setting science-based targets that align with a 1.5°C future demonstrates a company's commitment to reduce its contribution to climate change and provides structure to its climate action.			

Core Module: Action & Impact	Reporting on key actions and initiatives a company is taking to reduce its emissions is important for understanding what the company is doing to meet its targets and the impact of its initiatives on the company's emissions.
Energy reporting	Energy-related activities represent, for many sectors, the most significant GHG emission sources. It is therefore important that companies disclose information about their energy generation and/or consumption. Energy disclosures incentivize companies to pull the right levers for reducing their emissions and impact on climate change.
Value chain emissions	A significant proportion of most companies' emissions lie outside their direct operations and are related to their supply chain and end-users. Companies should measure and report these emissions and work with their suppliers, customers, and other partners to truly reduce their impact on climate change.
Management and resilience	For a company to successfully and strategically change in line with the transition to a low carbon economy, it requires commitment and drive from its leadership. In addition to that, SMEs are often especially vulnerable to risks, including climate- related risks, as they often do not have robust risk assessment and management systems in place. Thus, demonstrating climate leadership and carrying out climate-risk assessments is key to ensuring competitiveness and climate resilience.
Climate solutions	SMEs are a force for innovation globally and have an opportunity for significant contribution in the growing market of low carbon products and services that enable third parties to reduce their emissions throughout their value chains. Disclosure on these products/services and their impacts would enable SMEs to attract investment, allow their business to grow, and increase their contribution to limiting climate change.

We recommend that SMEs adopt the core modules immediately and suggest that they report on the additional modules within three years. The modular approach is intended to make climate disclosure more manageable for SMEs, allowing them to prioritize the modules that are most important/relevant for them and their stakeholders. Having worked with SMEs over the last 12 years, CDP has observed that companies can take about three years to build the capacity to provide high-quality data from when they first get started. Although we recommend that SMEs report on all the modules in this framework within three years, we strongly encourage them to do it as quickly as possible within that timeframe.

## INTRODUCTION

The world is at a critical junction for global climate action. Amid growing attention and ambition, global greenhouse gas emissions still hit an all-time high in 2019. These need to halve by 2030 and reach net-zero by 2050 to decrease the risk of irreversible climate tipping points.

Businesses are demonstrating transformational ambition on climate action; corporate leaders have been working to reduce emissions within their operations and improve energy efficiency for years. Corporate commitments are growing, as evident in the exponential growth of companies joining the UN Race to Zero Campaign (more than 3,000 companies) and the Science-based Targets Initiative (SBTi), with over 1,000 companies having set targets aligned to a well-below 2°C or 1.5°C trajectory. Yet, much of this ambition and progress has been driven by high emitting, large, global corporations due to the public and investor pressure they face to reduce their emissions. As a result, much of the support and guidelines available for sustainability reporting do not cater to the needs of SMEs.

However, the transition is already underway, and if SMEs are not brought on board, they risk facing competitive disadvantages and losing out on low carbon opportunities. It is vital that SMEs are supported in making the most of the opportunities presented by transitioning to a low carbon economy. Their flexibility and capability to innovate makes them well placed and crucial for providing climate solutions that are key for limiting the global temperature rise to 1.5°C.

SMEs are increasingly being requested to commit to reduce their emissions and report progress against their commitments by their stakeholders and lenders. For example, as supply chain emissions are on average 11.4 times higher than operational emissions<sup>3</sup>, many large companies want their suppliers, often SMEs, to measure, report and cut down their own emissions - cascading climate action down the supply chain. SMEs that are unable to demonstrate their environmental action risk losing out on important opportunities. This has wider economic and societal impacts as SMEs are a backbone of most economies and significantly contribute to employment and social wellbeing. Being major engines of value creation, SMEs account for between 50% and 70% of value added in OECD economies. In emerging economies, SMEs contribute to, on average, 33% of GDP<sup>4</sup>. SMEs have a very significant role to play in both employment level and employment growth<sup>5</sup>. In high-income countries, SMEs with up to 250 employees have a 65% contribution to employment; the number rises to 78% for low-income countries<sup>6</sup>. When it comes to employment growth, in a majority of countries, SMEs between 5-99 employees alone account for more than 50% of total net employment creation<sup>7</sup>.

Furthermore, as financial institutions seek to reduce their portfolio emissions, they require environmental data from companies to feed into their investment and lending decisions. Many SMEs rely on financing from banks. According to trade credit insurer Euler Hermes, bank loans make up around 70% of external funding for European SMEs.

Therefore, it is important to provide SMEs with the framework, tools and resources needed to set commitments aligned with a  $1.5^{\circ}$ C future and disclose environmental performance.

To address this need, the SME Climate Hub was launched in 2020 in order to support SMEs on a large scale, providing them with resources to commit to reduce their emissions and report progress. This Framework will be available on the Hub for all SMEs to access.

#### **Defining SMEs**

For the purpose of this framework, SMEs are defined as non-subsidiary organizations with fewer than 500 employees, which is in line with the definition used by the SME Climate Hub and the Science-based Targets Initiative. These can be further categorized as micro (fewer than 10), small (10-50) and medium (50-500).

The definition of SMEs varies by country/region, however, employee numbers and revenue are the two most used indicators to define SMEs. The varying definitions of SMEs represent the different policy and structural contexts in which they operate as well as their vast heterogeneity<sup>8</sup>. At a firm and sector level, SMEs have meaningful variations based on other factors such as business model and technical and managerial capacities. While these variations demonstrate that size, defined by employee number, is not the only way to group SMEs, it is still relevant because organizations of similar sizes share significant commonalities regarding resources and expertise available for environmental action and disclosure.

<sup>3</sup>Transparency to Transformation: A Chain Reaction, CDP Global Supply Chain Report, 2020.

<sup>4</sup>Small, Medium, Strong, Trends in SME Performance and Business Conditions, OECD, 2017.

<sup>a</sup>Small and Medium-Sized Enterprises: Overview of Participation in U.S. Exports, United States International Trade Commission, 2010.

<sup>6</sup>Kok, J., C. Deijl and C. Veldhuis-Van Essen (2013). Is Small Still Beautiful? Literature Review of Recent Empirical Evidence on the, ILO: GIZ, www.ilo.org

<sup>7</sup>Inclusive growth for the green transition, OECD, 2018.

<sup>8</sup>SMEs: Key Drivers of Green and Inclusive Growth, OECD, 2018.

#### Note on micro and small SMEs

We acknowledge that reporting on all the modules in this framework may be too difficult for micro (fewer than 10 employees) and small (10-50 employees) SMEs, and that some of the indicators might not be relevant to them. Therefore, they may choose to focus on the core modules (Measure, Commit, Action & Impact). We have decided not to have a separate set of indicators for these smaller SMEs because as the organization grows, along with its knowledge and reporting capability, it should start reporting on all the modules in this framework. Having the same set of indicators for all SMEs will ensure that the data reported is consistent and comparable, facilitating its use in benchmarking and decision making by investors, purchasers, policymakers and other stakeholders.

#### Purpose

This framework is intended to stimulate SMEs' understanding and reporting of the most vital climate-related indicators and encourage immediate climate action.

It is recommended that SMEs use this framework to aid their sustainability reporting processes so that data on the SME's climate performance can be provided to investors, purchasers, policymakers and other stakeholders in a consistent and comparable manner. These stakeholders will then be able to reduce their climate risks at a portfolio level and make decisions aligned with a net-zero future, while SMEs will be able to meet future requests from these stakeholders and increase their competitiveness.

Ultimately, use of this framework will empower SMEs to measure, manage and track their progress against their climate commitments and provide a clear pathway to climate leadership. Users of the framework will be enabled to play an active role in the transition to a low carbon world and build resilience to climate change.

#### **Objectives**

In order to achieve the purpose of stimulating SMEs' understanding and reporting of the most vital climate-related indicators and encouraging immediate climate action, this framework aims to be:

- Modular, to enable flexibility to expand into other areas of environmental disclosure;
- Understandable, through use of straightforward language
- Open access and available for all;
- Streamlined and resource efficient to represent the minimum reporting requirements;
- Representative of best practice through alignment with other reporting frameworks.

#### Development

Based on experience from CDP's questionnaire and desktop research, this streamlined reporting framework is co-designed with the SME Climate Hub represented by the Exponential Roadmap Initiative (XRI), Normative and the We Mean Business Coalition. The development process includes researching the best practice available from other initiatives, standards, and frameworks such as the GHG Protocol, SBTi, TCFD, the 1.5 Business Playbook and the UN Race to Zero criteria. Based on the research results, alignment was implemented where deemed appropriate, bearing in mind the specific needs of SMEs and the objectives of this framework.

A public consultation was held, inviting feedback from SMEs, framework stakeholders and other intended users of this framework which informed the refining of the framework.

Throughout 2021 and 2022, CDP, in collaboration with the SME Climate Hub, will invite and consolidate feedback from SMEs and other intended users who trial the framework, informing the review and further developments in the framework in an iterative process. The framework will be updated on a regular basis in a version-controlled manner.

#### Intended users

The users of this framework can be divided into three groups: data providers, data users and organizations that link the two. Here, data providers are SMEs that will use the framework to disclose data on their climate impact and action. Data users are defined as organizations that use the disclosed information in decision-making processes involving the data providers. The two main types of organizations we envisage linking the data providers and users are SME support organizations and data collectors. Both may connect data providers with the framework, assist with reporting on the indicators defined in the framework, and supply the resulting information to the data users<sup>\*</sup>. Please see examples of these groups in the infographic below.



\*We envisage data collectors and SME support organizations linking data providers and data users, but going through these linking organizations is not necessary. Data providers are welcome to use this framework to provide data in a consistent manner directly to data users.

#### ALIGNMENT AND MAPPING WITH OTHER FRAMEWORKS

#### Approach to alignment

- Alignment with and influence from frameworks and standards such as the GHG Protocol, TCFD, CDSB, SBTi, SDGs and the 1.5 Business Playbook.
- Full alignment might not be appropriate as most reporting frameworks and standards are geared towards larger organizations. However, they can still inform SME reporting and as such, relevant elements have been identified and adapted for use in this framework.
- Standalone mapping documents may be produced at a later stage, showing overlap and alignment with other existing frameworks.

# **GUIDING PRINCIPLES**

## **Purpose of principles**

The seven principles below underpin this framework's disclosure recommendations/requirements and are designed to ensure that the data generated is of high quality and decision-useful for SME stakeholders, including financial institutions. Additionally, disclosures aligned with these principles will incentivize climate action among SMEs and improve understanding of their environmental impact.

These draw from the principles of the following key frameworks and standards: TCFD, CDSB and the GHG Protocol.

- **01** Disclosures shall be relevant to SMEs and their data users.
- **02** Disclosures shall be clear and understandable
- **03** Disclosures shall be objective and accurate.
- **04** Disclosures shall be complete and verifiable.
- **05** Disclosures shall be comparable to best practice corporate disclosures.
- **06** Disclosures shall drive impactful SME climate action.
- **07** Disclosures shall be annual and provided in a consistent format.

## **MODULES:** REPORTING REQUIREMENTS AND RECOMMENDATIONS

This section consists of the key areas of disclosure for SMEs. It is recommended that:

- SMEs report against metrics and indicators in the core component.
- Data users/stakeholders communicate to SMEs which modules they would like to see prioritized depending on the needs of the data user and factors unique to the SME, such as business type.
- SMEs look to expand their reporting to cover the four additional modules within three years



### How to use the Framework

This framework lays out the key climate-related indicators that SMEs should report on, and SMEs should use it to inform their disclosures. Companies may report this information in their mainstream reports or when using other data collection or reporting platforms.

This framework does not contain detailed guidance on how to report on the indicators, as there is a lot of guidance available that is suitable for SMEs to use. <u>The SME Climate Hub</u> has a dedicated "tools and resources" section that we encourage SMEs to utilize when reporting on the indicators in this framework.

We highly recommend reading each module's "Guidance and definitions" section to understand the indicators laid out in the framework better.

Each module recommends ("should") or requires ("shall") certain indicators and metrics from SMEs that are considered to be important, factoring in the requirements of data users and needs of the SMEs.

- Throughout the modules the term "shall" is used to indicate a requirement. Indicators denoted using "shall" are considered to be crucial reporting for SMEs regardless of the disclosers' reporting experience.
- Throughout the modules the term "should" is used to indicate a recommendation. Indicators denoted using "should" are considered to be optional, especially for small SMEs or those in their first year of reporting; however, reporting on these indicators is strongly advocated within three years.

## **MEASURE**

Every company should measure its emissions and determine its impact on the climate as a starting point. Only then can the company begin to manage and reduce its negative environmental impact effectively. This module lavs out the minimum level of disclosure required from SMEs regarding their emissions, aligned with existing standards and best practices such as the GHG Protocol, recognizing that emissions calculation can be challenging. There are several tools and resources available that can help SMEs get started with measuring their emissions; some of them are listed in the guidance section below.

## **Connections to other frameworks**

### TCFD

Metrics and targets recommended disclosure b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks

## SDG

Goal 13: Climate action

	Measure
What are your gross global operational emissions (Scope 1 and 2)?	<ul> <li>Companies shall provide:</li> <li>Reporting year</li> <li>Gross global emissions from combustion in owned or controlled boilers, furnaces, vehicles, etc. (Scope 1)</li> <li>Gross global emissions from electricity purchases (and purchased heat, steam and cooling) in the reporting year (Scope 2) *</li> <li>Calculation methodology</li> <li>Companies should provide a breakdown of their reported Scope 1 and Scope 2 figures.</li> <li>Companies shall ensure that there are mechanisms in place to confirm that the emissions data provided is sufficiently accurate and provide a comment on the accuracy.</li> <li>*For companies operating in areas where market instruments are available, both location-based and market-based Scope 2 figures should be provided. (See guidance below for more information)</li> </ul>
Are there any emissions that are in the reporting boundary but are excluded from the inventory?	Companies <b>shall</b> disclose any relevant sources of emissions excluded and provide the magnitude of significance.
Describe your emissions in the context of an appropriate business metric (Emissions intensity)	Companies should disclose their gross global combined Scope 1 and 2 emissions for the reporting year, in metric tons CO2e, per unit of physical activity or economic output (preferably per unit of total revenue).

## **Guidance and definitions**

The <u>GHG Protocol</u> sets standards to measure and manage emissions. The website provides calculation tools as well as PDFs of the Corporate Standard and Scope 2 Guidance. Please refer to the website if you would like explanations or examples of the disclosure requirements above. You may also find some tools suitable specifically for SMEs in the "Tools and Resources" section of the <u>SME Climate Hub</u>.

As specified in the table above, there are two methods of calculating Scope 2 emissions – *location and market based.* 

- **The location-based method** considers the average emission factors for the electricity grids that provide electricity to the reporting organization.
- The market-based method reflects emissions from the electricity that the reporting
  organizations have chosen or purchased in the market. It considers contractual
  arrangements under which the reporting organization procures power from specific
  suppliers or sources, such
  as renewable energy.

As summarized by the <u>World Resource Institute</u>, reporting both figures tells an important story about the company's carbon footprint and carbon reduction strategy. The location-based method reveals what the company is physically putting into the air, and the market-based method shows emissions that the company is responsible for through its purchasing decisions. For more information on this please refer to the <u>GHG Protocol Scope 2 Guidance</u>.

Reporting year: The most recent 12-month period for which data is provided.

**Gross global emissions:** This means total emissions before any deductions or other adjustments are made to take account of things such as offset credits or avoided emissions from the use of goods and services.

**Emissions intensity:** Emissions (metric tons CO2e) / Business metric (e.g., revenue). Intensity metrics describe an organization's CO2e emissions in the context of another business metric. In this way, the emissions are normalized to account for growth. Emissions intensity per unit of revenue is one the most common and easy means to calculate emissions intensity, which is why it is preferred that you provide this figure. However, this is not necessarily always the most appropriate to individual businesses and therefore you can also report an intensity or normalized metric that is most appropriate to your organization's own operations.

## COMMIT

It is essential for every company to commit to reduce their environmental impact. Target setting provides direction and structure to environmental strategy. SMEs setting targets aligned with science demonstrate initiative to their stakeholders and financial institutions.

The details of targets help data users understand how robust they are and whether they are consistent with a 1.5°C future.

Some initiatives allow SMEs to select from a set of pre-defined targets aligned with science, making the target-setting process simpler for SMEs. Two key examples are the <u>SBTi's SME</u> <u>initiative</u> and the <u>SME Climate</u> <u>Hub's Climate Commitment</u>. Companies are encouraged to sign up to such initiatives to align with the UN Race to Zero Campaign and aim to include the metrics highlighted in this framework when they report on their targets. **Connections to other frameworks** 

### TCFD

Metrics and targets recommended disclosure c) Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets

### SDG

Goal 13: Climate action

 Provide details of your targets and progress made against them
 All companies with a climate-related target shall state:

 • Target type (e.g., absolute emissions reduction, emissions intensity, net-zero)
 • Year target was set

 • Target year
 • Target year

 • Whether the target is aligned with a recognized target-setting standard/initiative

For emissions reduction targets, companies shall also provide:

- Scope(s) or Scope 3 categories covered
- Base year
- Covered base year emissions
- Covered base year emissions as a % of total base year emissions in selected Scope(s)
- % Targeted reduction from covered base year emissions
- Whether the target is science-based and/or Race to Zero aligned

For a net-zero target, companies shall also include:

- A near-term emissions reduction target aligned with science
- To what extent the net-zero target depends on neutralization (carbon removal) activities

If the organization does not have any climate-related targets, they **shall** state whether they intend to set one in the next two years or if setting a target was judged to be unimportant, they **shall** explain why.

### **Guidance and definitions**

**Covered base year emissions:** The base year emissions covered by your emissions reduction target. e.g., if your target relates to Scope 2 emissions of a particular business activity (e.g., office-based operations), the "covered base year emissions" would be the base year Scope 2 emissions relating to that business activity only.

Net-zero target: in line with the SBTi Corporate Net-Zero Standard, corporate net-zero is defined as:

- 1. Reducing scope 1, 2, and 3 emissions to zero or to a residual level that is consistent with reaching net-zero emissions at the global or sector level in eligible 1.5°C-aligned pathways
- 2. Neutralizing any residual emissions at the net-zero target year and any GHG emissions released into the atmosphere thereafter.

For further guidance on setting net-zero targets please refer to the SBTi Corporate Net-Zero Standard

**Neutralization of emissions:** neutralization of a company's residual GHG emissions (emissions that are unfeasible to reduce) with an equivalent amount of carbon removals. An effective neutralization strategy involves removing carbon from the atmosphere and storing it for a long-enough period to fully neutralize the impact of any GHG that continues to be released into the atmosphere (adapted from *Foundations for Science-based Net-Zero Target Setting in the Corporate Sector*)<sup>9</sup>.

Provide details of your targets and progress made against them

# **ACTION AND IMPACT**

Disclosure of emissions reduction initiatives demonstrates the steps the organization is taking to meet its climate-related targets and the impact those have on reducing the company's emissions. This module asks companies to disclose details of their initiatives to reduce emissions in Scopes 1, 2 and 3.

Connections to other frameworks

**SDG** Goal 13: Climate action

4	action and Impact
Have you, or do you plan to, take action to reduce your GHG emissions?	<ul> <li>Companies shall state whether they have any implemented or planned action(s)/initiative(s) to reduce their operational (Scopes 1 and 2) and value chain (Scope 3) emissions, providing the following details:</li> <li>Description of action/initiative type (e.g., operational efficiency, process efficiency, low carbon energy consumption, etc.)</li> <li>Initiative start date</li> <li>For each action/initiative, companies should also disclose:</li> <li>Estimated annual emissions savings as a result of action</li> </ul>
	<ul> <li>taken</li> <li>Scope(s) or Scope 3 category where the emissions</li> </ul>
	saving occurs Companies that do not have any emissions reduction initiatives <b>shall</b> explain why.
How have your emissions changed over time?	Organizations that have calculated their emissions in previous years should state how their emissions in the reporting year have changed compared to previous years, noting the reason(s) for change and explaining any deviation from set target(s).

## **Guidance and definitions**

Initiative type: To see examples of initiative types please refer to Appendix.

**Initiative start date:** The start date tells data users whether this initiative was implemented in the reporting year and if not, then when it is planned to be implemented.

**Estimated annual emissions savings:** Where savings occur on a non-annual basis, average the savings so that the annual figure can be provided.



Energy-related activities represent, for many sectors, the most significant GHG emission sources. This module provides transparency on the consumption and generation of energy by organizations. Awareness of this information incentivizes companies to make informed energy efficiency measures to reduce their emissions and impact on climate change.

## Connections to other frameworks

**SDG** Goal 7: Affordable and clean energy

Goal 13: Climate action

	Energy
Report your total energy consumption	Companies <b>shall</b> disclose their total energy consumption (purchased and/or self-generated).*
Disclose your renewable energy purchase and generation	Companies <b>shall</b> disclose whether they purchase and/or generate renewable energy and if so, the proportion of their total energy purchase or generation that this makes up. <i>Companies should provide details of their renewable energy</i> <i>consumption (i.e., is it self-generated, green tariff etc.).</i>

\* This should include all energy sources outlined in the scope 1 and 2 guidance of the GHG Protocol

## **Guidance and definitions**

**Renewable energy,** as defined in the GHG Protocol is "Energy taken from sources that are inexhaustible, e.g., wind, water, solar, geothermal energy and biofuels."

**Purchased energy** refers to the energy (electricity, heat, steam and/or cooling) an organization receives from a third party, i.e., outside the organizational boundary. Specific information on these energy carriers (electricity, steam, heat and/or cooling) can be found in section 5.3.1 and Appendix A of the GHG Protocol Scope 2 Guidance.

# **VALUE CHAIN EMISSIONS**

Most of a company's emissions lie in its value chain. It is important for companies to go beyond their direct operations to measure and influence their emissions across their value chains – from the goods they purchase to the disposal of the products they sell. This module requires/recommends disclosure on value chain emissions to determine the impact of companies' value chain on the environment.

## **Connections to other frameworks**

### TCFD

Metrics and targets recommended disclosure b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks

## SDG

Goal 13: Climate action



## **Guidance and definitions**

Value chain refers to the full lifecycle of a product or process, including material sourcing, production, consumption and disposal/recycling processes – as defined in a <u>WBCSD report</u>.

Pages 7-10 of the <u>Technical Guidance for Calculating Scope 3 Emissions</u> contain helpful descriptions of the categories listed above.

The GHG Protocol's <u>Scope 3 Evaluator</u> is a free tool that SMEs can use to start measuring their Scope 3 emissions.

There are also some tools suitable specifically for SMEs in the "Tools and Resources" section of the <u>SME Climate Hub</u>.

## **MANAGEMENT AND RESILIENCE**

For a company to successfully transition to low carbon, commitment and drive from its leadership is required. There is strong evidence that companies who integrate climate-related decisions and initiatives in the company-wide strategy are more likely to be able to take meaningful action and meet their climaterelated targets. Banks and lenders are increasingly requesting information on a company's climate risks. In addition to that, most SMEs do not have strong risk management processes, which makes them particularly vulnerable to global risks<sup>10</sup>. Building business resilience to climate change by identifying and managing risks has never been more important for SMEs. Robust risk assessment is key to climate resilience in the future.

## **Connections to other frameworks**

### TCFD

Strategy recommended disclosure a) Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term

Risk management recommended disclosure a) Describe the organization's processes for identifying and assessing climate-related risks

Risk management recommended disclosure b) Describe the organization's processes for managing climate-related risks

#### SDG

Goal 13: Climate action

<sup>10</sup>Small and Medium Enterprises and Global Risks: Evidence from Manufacturing SMEs in Turkey, International Journal of Disaster Risk Science, 2020.

Management and resilience		
Is there any member(s) of your organization responsible for overseeing climate change matters?	Companies <b>shall</b> disclose if there is an individual(s) responsible for overseeing climate change action and their seniority within the organization. If the company has a board, they should disclose whether there is board-level oversight of climate change matters.	
Is your company aligned with a net- zero future?	Companies <b>shall</b> state if their strategy and/or business model aligns with the latest and most ambitious science (i.e., halving emissions by 2030 and reaching net-zero by 2050 at the latest, thereby limiting global warming to 1.5°C).	
Do you assess your climate risks?	<ul> <li>Companies should state if they identify, assess, and manage climate risks.</li> <li>Companies should consider providing the following details of their risk management process:</li> <li>How frequently they carry out climate risk assessments</li> <li>Value chain stages covered (e.g., direct operations, downstream, upstream)</li> <li>Time horizon(s) covered</li> <li>Risk types considered</li> </ul>	
What are your major climate risks and how do you manage them?	<ul> <li>Companies should disclose:</li> <li>The risk type they have identified, e.g., transition risks (such as emerging climate regulation) or physical risks (such as flooding)</li> <li>The time horizon of the risk (e.g., short-term, long-term, or unknown)</li> <li>The likelihood of the risk occurring</li> <li>The impact of the risk materializing (how would this risk impact your business?)</li> <li>How the risk is being (or is planned to be) managed</li> </ul>	

## **Guidance and definitions**

A strategy and/or business model aligned with a net-zero future (by 2050 latest) is one that aligns with the latest and most ambitious climate science recommendations. i.e., halving emissions by 2030 and reaching net-zero by 2050 at the latest, thereby limiting global warming to 1.5°C.

**Climate-related risks** can be divided into two main categories: risks related to the transition to a low-carbon economy **(transition risks**) and risks related to the physical impacts of climate change (**physical risks**).

### **Risk types:**

Transition risks:

**Current and emerging regulation:** policy developments that attempt to constrain actions that contribute to the adverse effects of climate change or policy developments that seek to promote adaptation to climate change;

**Technology:** all risks associated with technological improvements or innovations that support the transition to a low-carbon, energy-efficient economic system;

Legal: all climate-related litigation claims;

Market: all shifts in supply and demand for certain commodities, products, and services;

**Reputation:** all risks tied to changing customer or community perceptions of an organization's contribution to or detraction from the transition to a low-carbon economy.

## Physical risks:

Acute: risks that are event-driven, including increased severity of extreme weather events, such as cyclones, hurricanes, or floods;

**Chronic:** longer-term shifts in climate patterns (e.g., sustained higher temperatures) that may cause sea level rise or chronic heat waves.

### Time horizons of climate-related risks:

There is a common perception that all climate-related risks are "long-term", arising in 10+ years; however, transitional risks such as policies, technology, and markets are emerging earlier than this, and physical risks including the frequency and intensity of storms, floods, and droughts are recognized risks today. Thus, it is important that companies consider short and medium term risks in their assessments as well.

# **CLIMATE SOLUTIONS**

SMEs are a force for innovation globally and play a significant role in bringing new low carbon or emissions-reducing products and services to market. Disclosure on these products/services and their impacts would allow SMEs to attract investment, allowing their business to grow and increasing their contribution to limiting climate change.

## Connections to other frameworks

**SDG** Goal 13: Climate action

## **Climate solutions**

Do you classify any of your existing goods and/or services as low carbon products or products that enable a third party to reduce GHG emissions in their value chain? If yes, companies shall disclose:

- % of total revenue from low-carbon products
- Product type or description/name of product(s) or service(s)
- Methodology/taxonomy used to classify product(s)/ service(s) as low-carbon or as product(s)/service(s) that enable third parties to reduce emissions (e.g., EU Taxonomy, Low Carbon Investment Registry Taxonomy)

Companies should also consider providing some additional information such as:

- Product category: low carbon product (has a low carbon footprint or embedded emissions) or enables avoided emissions (reduces customer emissions) or both
- For low carbon products:

Embedded emissions of low carbon products

For products that enable third parties to avoid emissions:

Estimated avoided emissions compared to the reference product

### **Guidance and definitions**

Low carbon products and products that enable avoided emissions: There is a distinction between products that are low carbon and products that enable avoided emissions. There remains a level of ambiguity over the definition of what constitutes a 'low carbon product'. While CDP does not want to constrict the definition of low-carbon products, they can be loosely defined as products with low embedded emissions, while products that enable avoided emissions refer to products that enable third parties such as customers to reduce their emissions.

## CONCLUSION AND AREAS FOR FUTURE WORK

## This framework lays out the indicators and metrics that SMEs should cover in their climate disclosure, attempting to strike a balance between comprehensive climate disclosure and reduced reporting burden.

It is acknowledged that the heterogeneity of SMEs – due to factors such as company size, experience with climate disclosure and nature of products/services offered by the business – means that not all indicators are relevant for all SMEs (although it is expected that the core section will be relevant for most SMEs). In addition, the priority of the four additional modules (energy reporting, value chain emissions, management and resilience, and climate solutions) varies depending on the SME and the needs of the stakeholder or authority that is requesting the SME to disclose.

The modular design of this framework and the recommended three-year time frame for building capacity should provide flexibility for different SMEs and data requesters to tailor the use of this framework to their disclosure needs and reporting capability. The framework is influenced by key frameworks and standards and will continue to evolve with developments in climate disclosure standards. Although this framework focuses on SME climate disclosure, there are other areas of SME disclosure that might be included in the future, such as:

- Carbon removals
- Measurable climate mitigation outcomes resulting from actions outside of a company's value chain, such as investing in nature protection or reforestation (also referred to as 'compensation')
- Broader environmental topics (e.g., water security, deforestation, biodiversity)

## **APPENDIX:** EXAMPLES OF CLIMATE-RELATED INITIATIVE TYPES

#### **Energy efficiency in buildings**

Insulation Maintenance program Draught proofing Solar shading Building Energy Management Sys-tems (BEMS) Heating, Ventilation and Air Condi-tioning (HVAC) Lighting Motors and drives Combined heat and power (cogen-eration)

#### Energy efficiency in production processes

Waste heat recovery Cooling technology Process optimization Fuel switch Compressed air Combined heat and power (cogen-eration) Wastewater treatment Reuse of water Reuse of steam Machine/equipment replacement Automation Electrification Smart control system Wind Tidal Wave Fossil fuel plant fitted with CCS Low-carbon electricity mix

#### Low-carbon energy generation

Solid biofuels Liquid biofuels Biogas Geothermal Hydropower Nuclear Solar heating and cooling Solar PV Solar CSP Wind Tidal Wave Fossil fuel plant fitted with CCS Motors and drives Product or service design

#### Waste reduction and material circularity

Waste reduction Product or service design Product/component/material reuse Product/component/material recy-cling Remanufacturing

### Fugitive emissions reductions

Agricultural methane capture Agricultural nitrous oxide reduction Landfill methane capture Oil/natural gas methane leak cap-ture/prevention Refrigerant leakage reduction Carbon capture and stor-age/utilization (CCS/U)

#### Low-carbon energy consumption

Solid biofuels Liquid biofuels Biogas Geothermal Hydropower Solar heating and cooling Solar PV Solar CSP Nuclear

## Non-energy industrial process

emissions reductions Process equipment replacement Process material substitution Process material efficiency Carbon capture and stor-age/utilization (CCS/U)

#### Company policy or behavioral change

Supplier engagement Customer engagement Site consolidation/closure Change in procurement practices Resource efficiency Waste management

#### Transportation

Business travel policy Teleworking Employee commuting Company fleet vehicle replacement Company fleet vehicle efficiency



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#### About CDP

CDP is a global non-profit that runs the world's environmental disclosure system for companies, cities, states and regions. Founded in 2000 and working with more than 590 investors with over \$110 trillion in assets, CDP pioneered using capital markets and corporate procurement to motivate companies to disclose their environmental impacts, and to reduce greenhouse gas emissions, safeguard water resources and protect forests. Over 14,000 organizations around the world disclosed data through CDP in 2021, including more than 13,000 companies worth over 64% of global market capitalization, and over 1,100 cities, states and regions. Fully TCFD aligned, CDP holds the largest environmental database in the world, and CDP scores are widely used to drive investment and procurement decisions towards a zero carbon, sustainable and resilient economy. CDP is a founding member of the Science Based Targets initiative, We Mean Business Coalition, The Investor Agenda and the Net Zero Asset Managers initiative.

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### EXPONENTIAL ROADMAP INITIATIVE

## Normative