

Defining a Corporate Climate Finance Commitment

A Pillar of Corporate Climate Leadership

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Executive Summary

This guide presents opportunities for businesses to engage in climate finance in the era of the Paris Agreement. Under this new paradigm, carbon credits are placed within the broader context of climate finance to ensure adherence to the goals and emerging rules of the Paris Agreement, to increase relevance for a broad range of corporates and finally, to address the growing need for climate resilience and adaptation to climate change already underway. The guide also outlines options and practical recommendations for formulating and fulfilling a climate finance commitment within this new paradigm to help companies gain recognition for corporate climate leadership.

A Climate Finance Commitment: The Value for Business

Whether using markets to purchase carbon credits, commit to financing emission reductions within the value chain, or channel funds to other efforts to reduce carbon or increase resilience, businesses can benefit from:

- Recognition for climate leadership and contribution to Paris Agreement
- Quantified contributions to the Sustainable Development Goals (SDGs)
- Improved reporting to CDP
- Lower cost of reducing emissions in some cases
- Reduced exposure to carbon taxes or other compliance obligations and/or prepare for future compliance
- Shared value to stakeholders, especially when supporting projects within supply chains
- Reduced disruption to supply chain from climate change

Background

The ambition of the Paris Agreement provides the private sector with an opportunity to help not only close the ‘ambition gap’ to keep global warming well below 2 degrees, but also contribute to adaptation and climate finance—to be the engine accelerating the transition to a low-carbon, resilient world. In this new climate era, best practice corporate climate action calls for companies to take full accountability for their GHG footprints and to internalise the social and environmental costs of their emissions. Unless a company has reached zero emissions, this includes providing the financing for an equivalent of emission reductions somewhere else in the world and contributing to climate resilience and adaptation. Companies can use this commitment as an incentive to innovate, further drive down emissions, and gain recognition for climate leadership.

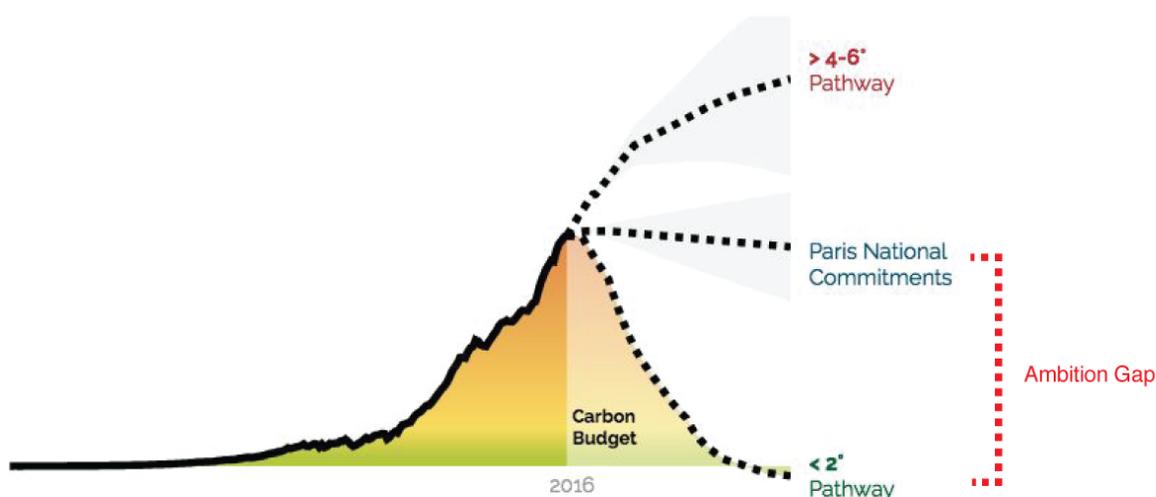


Figure 1. Closing the ambition gap to ensure a safe operating space for the planet.

Source: Science Based Targets

Historically, financing emission reductions outside corporate boundaries has primarily happened through carbon markets by trading carbon credits. Indeed, purchasing carbon credits is one of several ways to finance the low carbon transition. A key strength of using markets in this way is lower costs of abatement; that is, cutting more carbon for less money. In addition, by choosing carbon credits from standards that require contributions to sustainable development, each dollar invested does more than lower emissions – they also deliver great [social and environmental value](#).

Limitations of Carbon Offsetting + Solutions for a New Era

Perception as a Substitute for Internal Emission Reductions

A key challenge companies have historically faced when purchasing carbon credits is that they are perceived by some as a substitute for reducing an organisation's own footprint. While it has been documented that companies that purchase carbon credits are actually more likely to have internal reduction targets¹, it is clear that simply shifting the source of emission reductions is not sufficient to phase out net GHG emissions from all sources in the time scales required. Therefore, for credible climate stewardship, commitments to climate finance, which can include the purchase of carbon credits, must go alongside ambitious science-based internal reduction targets.

Broad 'One-Size-Fits-All' Solution

The concept of carbon neutrality to date has been positioned as a blunt solution that applies to any company, regardless of the details of their operations. To illustrate: if carbon neutrality is the uniform call to action, an IT company with a relatively small carbon footprint but tremendous influence and resources would be awarded the same recognition for going carbon-neutral as a major grocery chain, whose value chain emissions are not only exponentially higher, but far more difficult to measure and manage.

One solution has been to focus only on Scope 1 and 2 for carbon neutral claims. After all, one company's Scope 3 emissions are another's Scope 1 or 2. Said differently, it's someone else's problem. But following this to its logical conclusion, virtually all responsibility falls on just a few – fossil fuel extractors, energy companies, logistics and transport, and large manufacturers. And while these heavy emitters must step up, all businesses and indeed all individuals share a responsibility for owning their piece of the puzzle in driving demand to these heavy-emitting sectors. Going back to the example of the grocery retailer: Does its Scope 1 and 2 footprint represent the material part of its impact? Decidedly not. But should that company be solely responsible for its entire footprint, including all of Scope 3 emissions? Upstream suppliers and downstream customers should also play their part.

An approach based on shared accountability, climate stewardship rather than just carbon management, and collaboration can 'crowd in' new players and spur innovative approaches.

¹ Ecosystem Marketplace report, ["Buying in: Taking stock of the role of offsets in corporate carbon strategies,"](#) 2016.

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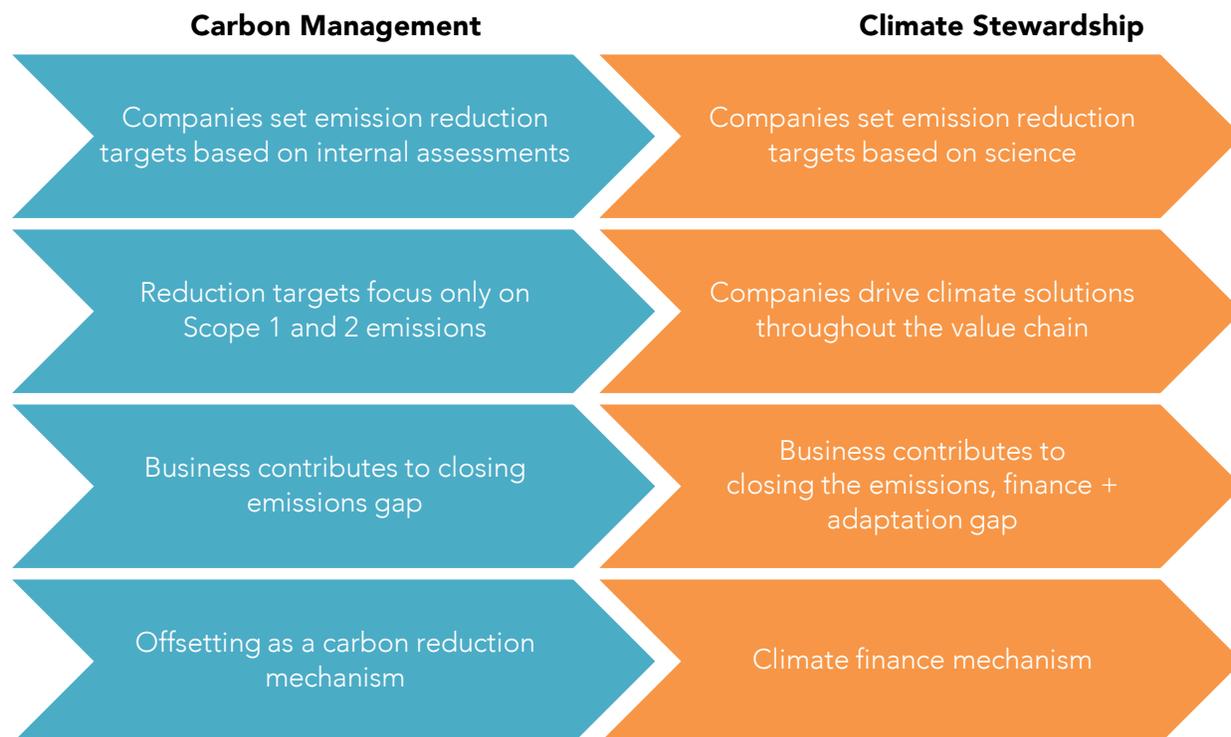


Figure 2: The evolution from carbon management to climate stewardship

Focus Only on Mitigation

Carbon credits have been used primarily as a tool for carbon mitigation. Yet it’s more important than ever to make our global economy and communities resilient to climate impacts already underway. These efforts are largely unfunded. What’s more, activities that have a climate mitigation impact should not be considered in isolation – they are part of the way people shelter their families, perform jobs, secure food, and move from place to place. Therefore, finance channeled to reducing carbon can and should also be structured in a way that maximises a broad range of positive SDG impacts, including climate adaptation and resilience.

Accordance with Paris Agreement

Under the Kyoto Protocol, only Annex 1 countries (primarily the developed world), made reduction commitments, which made it simple to trade carbon between companies in developed countries and projects in the developing world. However, in the Paris Agreement, every country has a target framed in its Nationally Determined Contribution (NDC). To further complicate, “the NDCs submitted under Article 4 are diverse in many aspects: target types, timeframes, metrics, sectoral scopes, and the distinctions between unconditional and conditional elements of NDCs.”¹ This wide variance makes it more difficult to ensure that a carbon credit comes from a project that both goes beyond ‘business as usual’ and is not ‘double counted’ – two key promises of carbon offsetting.

In a 2016 policy brief [“A New Paradigm for Voluntary Climate Action: ‘Reduce Within, Finance Beyond,’”](#) Gold Standard CEO Marion Verles proposed a new approach that solves this conundrum: rather than a company owning or retiring carbon credits, they can claim to have financed or provided the funding for emission reductions. These emission

1. Howard, Chagas, Hoogzaad, Hoch (2017). Features and implications of NDCs for carbon markets Available [here](#).

reductions would continue to be robustly quantified and verified by a third party, but would be documented in Certified Emission Reduction Statements, rather than traded in unitised carbon credits. This new mechanism is not only fit-for-purpose under the Paris Agreement, it also has practical applications in the context of corporate value chain activities.

Connection to Core Business

Some companies struggle with the fact that carbon credits come from projects outside their corporate boundaries, distant from the priorities of their core business. There are several ways to address this. A simple approach is to choose projects that take place in regions near facilities, suppliers, customers, or partners, or to select projects that contribute to the Sustainable Development Goals that align with corporate values and priorities. Beyond this, broadening the scope to include other dimensions of climate finance can make this more relevant for businesses in a wide variety of sectors and geographies, as discussed below.

New Channels for Climate Finance

Connecting climate finance commitments to corporate value chains is an emerging opportunity to address many of these challenges. Revisiting the earlier retailer example: When upstream Scope 3 emissions constitute a large percentage of a footprint, heavy supply chain emitters can develop ‘insetting’ projects within their own boundaries to issue carbon credits that they can then directly ‘retire,’ which means they would not be sold further. However, to make supply chain interventions even more pragmatic, new frameworks are in development to enable companies to quantify and certify the impact of emission reduction projects’ activity within their Scope 3 boundaries. This framework, being developed by Gold Standard, CDP, WWF and other partners, will provide guidance on making credible claims around the emission reductions, climate finance, and SDG impacts of the project without the need to issue or trade carbon credits.

Companies in the financial sector, on the other hand, can direct their finance commitment to financial products that drive the low-carbon transition, from climate bonds or green bonds to

new project financing. (Though the authors would like to highlight the need for credible quantification and verification of climate and development outcomes from these instruments.)

This represents an opportunity for different companies in different sectors to innovate and find new ways to contribute to climate mitigation and adaptation in ways that can ultimately benefit their stakeholders and even their own bottom line.

In Conclusion: Reduce Within, Finance Beyond

There is no doubt that further opportunities will continue to arise to help corporates play a role in driving the transition to a zero-carbon resilient economy. The core concept behind carbon credits – that is, a mechanism to channel finance from emitters to efforts that contribute to climate security – remains an essential ingredient to meeting the ambition of the Paris Agreement. We can't get there without it. In fact, the concept must be broadened to include not only carbon credits, but also certified emission reductions within value chains, investments in low-carbon solutions, and contributions to climate resilience.

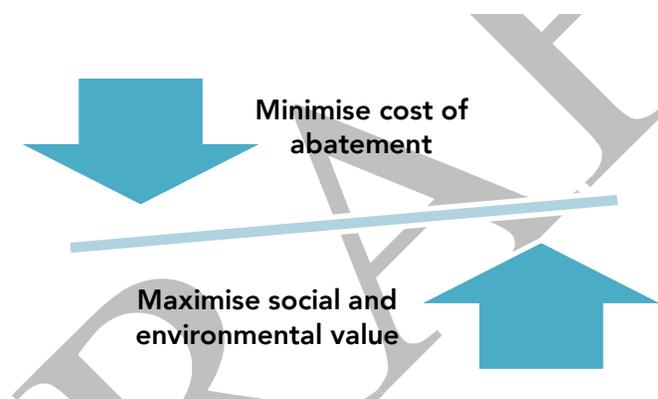


Figure 3: Smart use of climate finance mechanisms can optimise return on investment

Using market instruments like carbon credits to compensate for residual emissions remains an effective and practical tool to complement a corporate climate strategy, provided the company 1) has set an internal reduction target that's in line with what science tells us is needed to stay well below 2 degrees warming, and 2) plans long-term strategy and investments that do not go toward maintaining and expanding carbon polluting technologies. As part of a robust strategy for climate action, dedicating funds to emission reduction efforts outside corporate boundaries is the right thing to do.

Gold Standard, CDP and WWF encourage companies to use the Corporate Climate Leadership guidelines to inform their climate strategies, moving from carbon management to climate stewardship, and to refer to the following Practical Guide for defining and meeting a climate finance commitment.

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A Practical Guide for PILLAR 3 of Corporate Climate Leadership: Finance the Transition to a Zero-Carbon Resilient Economy

Corporates that wish to be recognised as climate leaders are advised to take accountability for their full carbon footprint. They can do so by making a commitment to finance the transition to a zero-carbon resilient economy and fulfilling that commitment by following one of these pathways or a combination of the two.

PATHWAY A: Support climate protection projects which are reducing emissions in an amount equivalent to unabated emissions.

1. **Use carbon markets to finance emission reductions**, that is, purchase carbon credits following the guidelines on page 8.
2. **Introduce value chain climate projects** both upstream and downstream that quantify and certify emission reductions and/or improve climate resilience to support suppliers, customers and other value chain stakeholders in their reduction and adaptation efforts.

PATHWAY B: Make a climate finance commitment based on the social cost of carbon to fund new efforts toward climate security

To determine a finance commitment, a company would calculate the remaining unabated emissions from the given year, and multiply that number by the social cost of carbon:

$$\text{Tons of GHG emissions} \times \text{Social cost of carbon} = \text{Finance commitment}$$

With that figure, that amount of funding would be channeled to efforts that contribute to climate mitigation, adaptation, or both. This would be done on an annual basis.

1. **Contribute to a new fund** that will allow collective action for climate security projects (fund to be developed).
2. **Purchase, fund or build renewable energy beyond your own operations**, actively contributing to changing the energy system.
3. **Develop or support new solutions** for climate mitigation and adaptation around the world.

Guidance for Selecting High Quality Carbon Credits as Part of a Climate Finance Commitment

Under the mantra of 'measure, reduce, and offset,' companies have included carbon offsets alongside their emission reduction efforts. By 2015, the voluntary carbon market had supported the reduction of nearly 330 million tonnes of CO₂.¹ Now, in a scenario in which all sources of anthropogenic GHG emissions need to be phased out, the voluntary carbon market stands 'at the ready' as a vehicle for climate finance. It allows for immediate action, with thousands of existing projects and the ability to scale quickly. The voluntary market can channel the funding needed to meet the finance needs of NDCs as well as adaptation efforts. In fact, the voluntary carbon market [has demonstrated its ability to deliver development benefits](#) that range from health and livelihoods to biodiversity conservation and gender equality. And it can do so at lower costs of abatement. The [World Bank State and Trends of Carbon Pricing](#) estimates that carbon markets can deliver emissions reductions at 35% lower cost by 2030. However, not all carbon credits are created equal. The following outlines what to look for in high quality carbon credits.

Best Practice Principles in selecting projects in the voluntary carbon market

- Select carbon credits that are:
 - Additional (from projects proven to have required the carbon finance to move forward)
 - Permanent (the emission reduction will not later be reversed)
 - Third party verified
- From projects that feature the following as mandatory requirements:
 - Inclusive of local stakeholders
 - Deliver and verify sustainable development impacts
 - Ensure best practice environmental and social safeguards
- Select sustainable development impacts relevant to your business objectives and stakeholder concerns
- Focus on countries relevant to your supply chain if applicable/desired, or consider projects in countries that are most vulnerable to climate change with the lowest means to combat it; for example, projects in serving populations living under the poverty line or projects in least developed countries (LDCs) or small island states