Sustainability Reporting – Scope 3 (SR3) content package

.msg global

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msg global solutions has created a Sustainability Reporting – Scope 3 (SR3) Content Package to be used as an optional tool on the SAP Sustainability Control Tower (SAP SCT) platform with the aim of accelerating the Scope 3 calculation and reporting of an organization.

1. Introduction

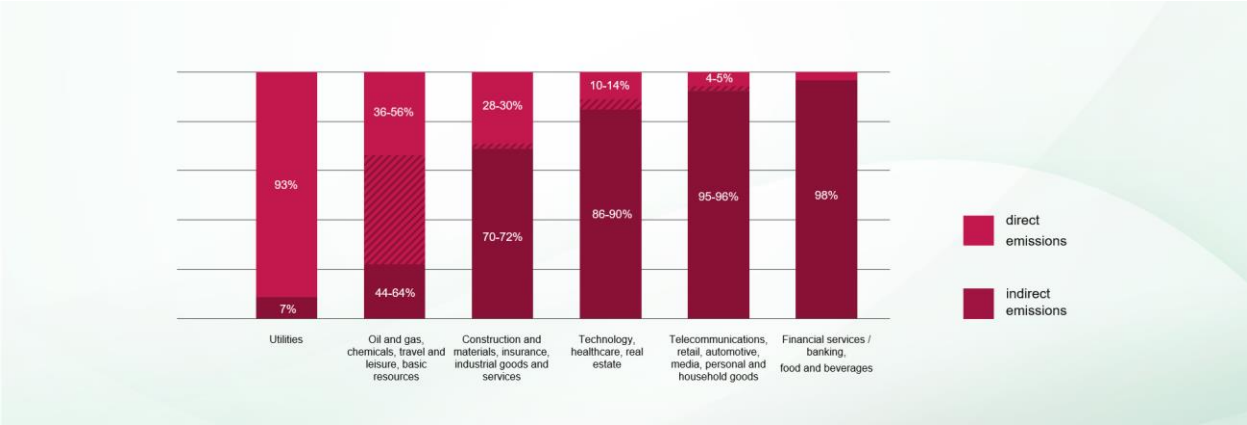
Companies must be aware and understand the full scope of impacts they create to get to a more sustainable economy today. The new emerging regulations also point in the same direction, demanding companies assess impacts beyond their operations, bringing more detailed and in-depth disclosures. **Such demand will urge companies to understand not only their own Environmental Social and Governance (ESG) strategy and position but also the ones of their suppliers and across their value chain**.

Having an ESG strategy is key to achieving social responsibility which is not only important for showing commitment but also to the general business of the company by attracting more consumers, investors, or employees. Apart from this, the business will benefit in terms of risk management by allowing the company to address the potential risks in a proactive way.

One of the main challenges companies face when setting targets and ambitions in their ESG strategy comes from their indirect impacts, mainly from those generated in their greenhouse gas (GHG) emissions.

The situation and scope of indirect impacts vary depending on the industries in which companies operate. It helps companies to ensure competitiveness and resilience. Differences among sectors **may differ in the high range - from counting approximately 7% of indirect emissions from operations connected with utilities to becoming the highest share of indirect emissions counting to 98% in overall GHG performance in the financial sector as well as for food and beverages production,** mainly due to diversified types of operations and long value chains.

Figure 1. ESG Reporting – demand for deeper insights into Carbon footprints.



Source: Principles for Responsible Investment. (n.d.) Managing ESG Risk in the Supply Chains of Private Companies and Assets, download (unpri.org), 2023.

Holistic analysis and overview across supply and value chains is an inevitable part of the sustainability management and reporting process, enabling companies to calculate and gain more accurate insights into their carbon footprints. This holistic analysis gives a broader view of a company's processes, allowing the identification of hotspots that are responsible for the main environmental impacts and being aligned with global sustainability goals.

The report of both the direct GHG emissions (Scope 1) and the indirect emissions from energy consumption (Scope 2) is the most common one for companies, however, **in recent years the report of indirect emissions, both upstream and downstream, (Scope 3) has become a critical aspect at the time of calculating the carbon footprint of a company and identifying its overall impact in GHG emissions.** Not only the Scope 3 emissions can represent the larger portion of a company's overall emissions, but also understanding and disclosing them shows the commitment that an organization has towards sustainability.

Scope 3 emissions calculation stands as an equal challenge for companies of all sizes - **for larger ones to obtain high-quality and relevant data from their suppliers to comply with regulatory requirements, and for smaller companies to start gathering data to be able to respond to data queries from larger companies and with this to maintain their reputation and competitiveness in line with the procurement policies.**

2. Challenges

With the high demand already in place to collect data reflecting the company's sustainability activities and commitments, and now with the inclusion of indirect impact on Scope 3 emissions to be assessed, **companies will face this extended challenge to collect data reflecting sustainability operations from its different stakeholders, especially more demanding to reach beyond its tier 1 suppliers.**

Collecting data from different parts of the value chain may be a time- and resources-demanding process. However, it also brings additional challenges in terms of data quality and comparability, and in some cases, dealing with data built upon different methodologies applies to some extent that such data is hard to be comparable at the level of overall company's suppliers.

The lack of data may generate an increasing challenge for companies to apply methodologies in calculating their Scope 3 emissions based on estimations rather than accurate calculations. **In cases when accurate data from suppliers is not entirely available, companies use spend-based methods to calculate indirect emissions that, in such cases, reflect industry-average results rather than actuals in emissions from suppliers.** With this given approach, data collected as input may not represent the most accurate and suitable approach.

Therefore, when defining indirect Scope 3 emissions methodologies, **the approach selection may raise additional obstacles for companies in delivering detailed insights as a starting point for further management decisions in reducing carbon emissions, or even developing needed procurement assessments and policies**. In addition, defining accurate methodology may be vital to further assessments if a company builds future ambitions to expand evaluation on more granular levels, preparing to report on Life Cycle assessments (LCA), or monitoring achievements from commitments based on pledges for Net-Zero targets from emissions.

Some of the main challenges in data management for Scope 3 emissions calculation are:

- **Data complexity:** Scope 3 emissions data covers a wide range of metrics, from information related to the suppliers of a company to customer-specific information. Each of these data may have different units of measurement and collection methods, complicating data standardisation and aggregation.
- **Dispersed data sources:** Scope 3 emissions data is often generated in different parts of the organisation and value chain. Integrating this information in a consistent way can be challenging and requires close collaboration between departments.

- **Data quality:** Errors in emissions data can significantly impact the accuracy of reporting. This includes human error, data collection problems, and inconsistency issues. Maintaining data quality requires continuous verification and cleaning processes.
- **Volume of data:** With the growing awareness of Scope 3 calculation, companies are collecting and managing more data than ever before. This can overwhelm existing data management systems and require investments in infrastructure for storing and processing large volumes of information.
- **Verification and Auditing:** To ensure the credibility of GHG emissions calculation, many organisations undergo third-party verification and Auditing processes. Preparing the documentation and data required for these reviews can be an intensive process and requires detailed and transparent documentation.
- **Appropriate technology and tools:** Choosing the right tools and technologies for GHG emissions data management is critical. This includes data management systems, data analysis software, and visualisation tools that can handle the complexity and volume of sustainability data.
- **Associated costs:** Scope 3 emissions data management involves investments in systems, technology, and trained staff. Companies must carefully weigh the long-term costs and benefits of these investments, considering the benefits in terms of improved reputation, efficiency, and attracting investors committed to sustainability.

Even though the companies are predominately focused on measuring and reporting on Scope 1 and Scope 2 emissions on their carbon footprint calculation, **by implementing measurement and reporting on Scope 3 indirect emissions companies will gain more accurate insights into their actual GHG performance.** It will also enable them to elevate their sustainability ambitions in the future and to pledge their Net-Zero targets according to Science Based Target Initiative (SBTi) or to submit their Life Cycle Assessments and, with this, elevate the quality of their environmental performance.

No matter what methodology the company addresses within indirect GHG emissions assessment, **the most important is to provide supporting evidence-based decisions, complementing reports with supporting documents included in evaluations and reports on KPIs**.

By including all three Scopes in their Corporate Sustainability Reports, companies will elevate accuracy in their sustainability performance and demonstrate transparency in reducing carbon emissions, identify the hotspots in across their value chain, and create long-term sustainable goals**. Only a structured sustainability report that translates a company's impact to relevant, measurable, and comparable information to all stakeholders results from applying such a holistic approach within and beyond its operations and value chain.**

3. Solution

The msg Sustainability Reporting Scope 3 (SR3) is a content package created in 2023 to support the reporting of indirect greenhouse gas emissions according to the GHG Protocol.

As previously mentioned, Scope 3 emissions will represent the indirect emissions as they are the result of the activities from assets not owned or controlled by the reporting company. **According to the GHG protocol, there are a total of 15 categories of Scope 3 emissions, which include emissions for both upstream and downstream of the organization's activities.**

Not all 15 categories are standardizable, it will depend on the organization's context and business activities. Within the standardizable ones, the SR3 content package offers the calculation and processing for the following ones:

- Category 1: **Purchased goods and services**
- Category 2: **Capital goods**
- Category 3: **Fuel and energy-related activities**
- Category 4: **Upstream transportation and distribution**
- Category 5: **Waste generated in operations**
- Category 6: **Business travel**
- Category 7: **Employee commuting**
- Category 8: **Upstream leased assets**
- Category 9: **Downstream transportation and distribution**
- Category 10: **Processing of sold products**
- Category 11: **Use of sold products**
- Category 12: **End-of-life treatment of sold products**

In case the customer would like to address or calculate the rest of the categories, **13: Downstream leased assets, 14: Franchises, or 15: Investments**, it can be customizable to their needs.

Non-financial indicators are sometimes more difficult to obtain, especially when it comes to indirect emissions where **the input is not always controlled internally and can depend on third parties such as suppliers, customers, and others.** Additionally, the calculation methodologies can be challenging to perceive as several directives and frameworks are now in place.

The process to create the report consists of three main steps: Data collection and uploading utilizing the predefined templates created by msg, process workflow to upload the data and execute the calculations, and, finally, report creation.

When a customer chooses SR3 as a way to optimize their Scope 3 emissions calculation process reporting process, at the beginning of the project, the content and format of the templates will be discussed to be aligned with the overall structure, teams, type of data available, and other requirements.

As the first step, for each of the standardized categories (categories 1 to 12) and with the aim of accelerating the process of collecting input data, the client has the option to report their input data in these predefined templates.

The purpose of the templates will be to facilitate and improve the data upload and reduce the potential mistakes that usually appear in this process by **using master data, having shortcuts, and containing relevant information among other features**. All of them will be provided by msg, however, these can also be modified according to the needs and requirements.

All templates will have, as an initial requirement, the name, department, and contact of the person responsible for reporting and verifying data. Thus, it will be possible to have more robust traceability of the input, speeding up the Audit process. **All templates will also have background explanations aligned with the GRI, giving an initial context, definitions, and disclosure requirements.** Additionally, the templates will have a clear and summarized explanation of each field to be filled in.

Each of the templates follows a consistent format, featuring tables that can be customized with master data. These templates provide introductory information about the specific KPI being addressed, along with a list of explanations related to the KPI and field definitions.

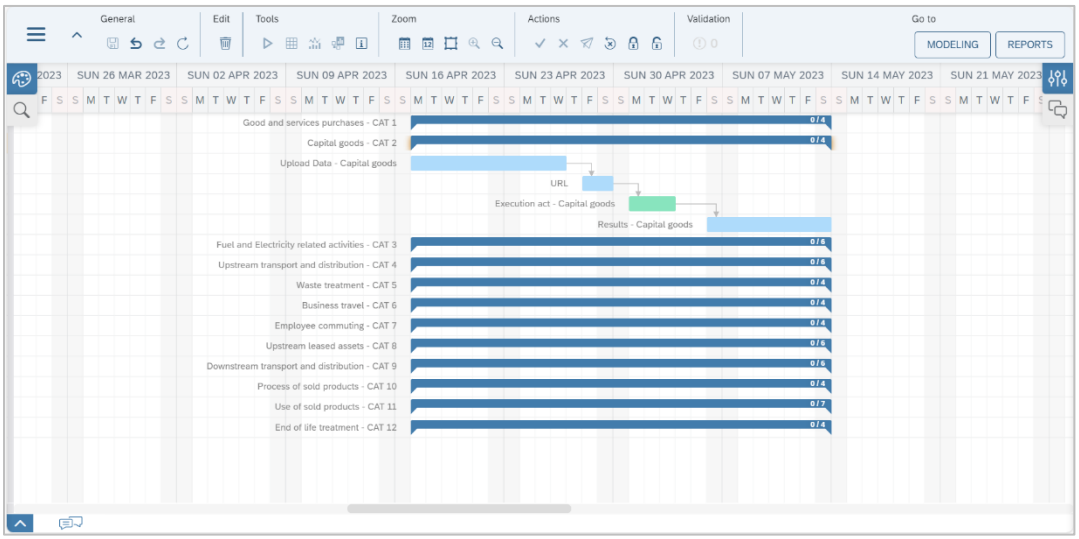
Within the introductory sheet, there is a list of fields contained in each model table of the template. Here, users can find the names of each field, instructions indicating whether they require master data, and additional information to understand their purpose in the tables. Additionally, an example image illustrating how to complete the templates is included.

In the model tables, each cell containing a field has a note comment providing additional information to assist users in completing it.

Once users have input the data into the templates, this information is uploaded to the system to facilitate the calculations defined in the tool. **There is also the possibility to connect the environment to the client's Business Technology Platform (BTP) or data systems, to automatize the process.**

The process used to upload data into the system is referred to as the "Process Template." Within this process template, users can upload data, establish connections, execute calculations, review data, define teams, and access other related features.

Figure 2. SR3 - Process Template

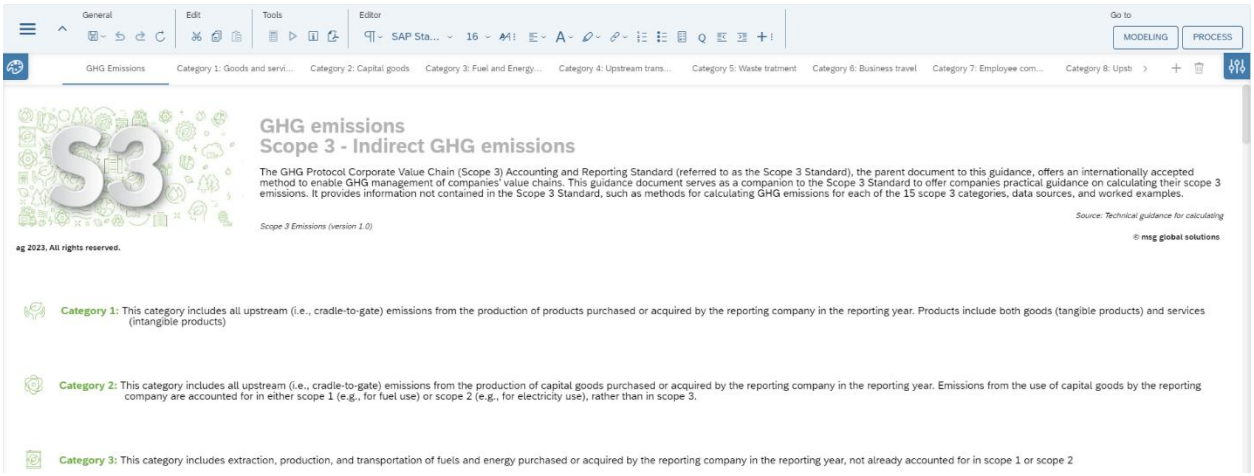


The structure of the process templates for SR3 content is predefined but can always be adapted to the customer's needs.

This is where users can create and define different teams and workflows, consisting of a performer and a reviewer. The performer is responsible for uploading or executing activities, while the reviewer is responsible for reviewing the information. The reviewer can also approve or reject an activity, and in the case of rejection, the performer will receive an email notification. Additionally, once the performer finishes uploading data or completing the activity, the tool will automatically send a notification email to the reviewer.

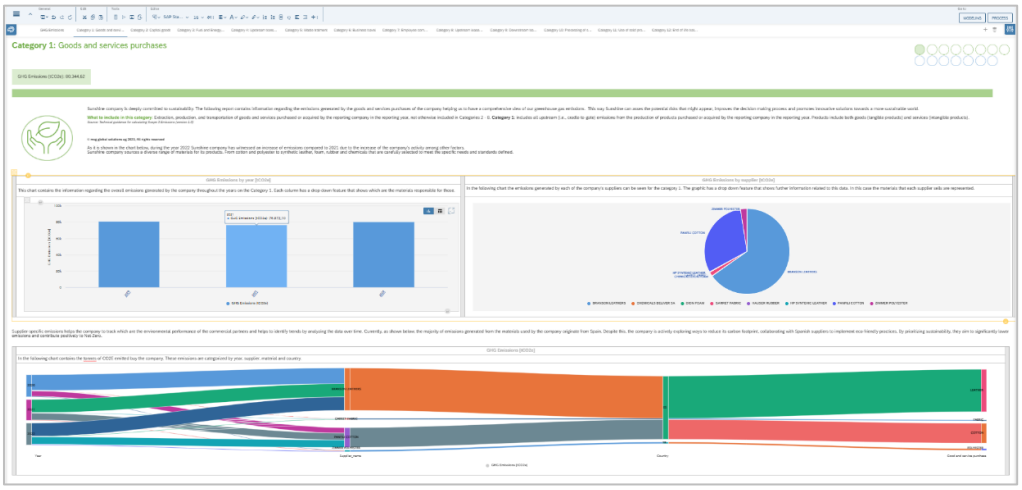
Once the definition of the process template structure is completed, and the information is uploaded, reviewed, and approved, the third and final step of the project involves creating the report with all the desired client information.

Figure 3. SR3 – Report



SR3 Content has also a predefined report with an example of how to disclose the information for each of the categories, in this case, it contains a summary with all the categories together and, apart from that, on a sheet per category. However, just like the previous steps, this report can be fully adapted and customized by the user. Users can utilize all the standard features of a word-processing document, including text editing, copying, inserting images, videos, icons, adjusting font type and size, inserting charts, logos, and more.

Figure 4. SR3 – Reporting graphs



All the data managed within the tool can be visualized and included in the report, represented using various charts, numbers, and units. **Each chart or graph offers a dropdown feature, allowing users to present information with as much granularity as needed, ensuring that the company's data can be effectively represented and explained.**

Finally, this report can be exported to PDF or copied into another format. It's worth noting that in case any data requires recalculation, the charts will automatically adjust accordingly.

4. Conclusions

A sustainability report is key for a company to have a holistic approach and **understand how it is contributing to the global sustainability goals, identifying the hotspots of its carbon emissions across its entire value chain, setting short, medium, or long-term targets, and improving their transparency which will allow it to better address the potential risks and opportunities that they might encounter during the everyday activities.** Moreover, the legislation towards sustainability is continuously evolving, and being compliant with this improves the company's image, business, and relationship with the community.

The SR3 content package designed by msg aims to support companies in addressing their Scope 3 emissions report. It was designed following the GHG protocol standards and its main purpose is to speed up the reporting process consisting of three different steps.

SR3 was designed by assuming that customers will report their input data in predefined templates. However, msg can provide additional support to make the data collection process more efficient. **This support can be given through workshops to help the client identify and collect the input data required for each field. Additional support can also be provided throughout the whole data collection process**.

In addition, msg can help clients identify and assess the key teams for reporting the input data and map out the key departments that will be involved in the reporting procedure.

The SR3 content takes into consideration predefined templates as the main data source. Other integrations and connections with SAP and non-SAP interfaces can be considered later to promote data automation.

In summary, Scope 3 emissions calculations and the inclusion of value chain information in the reporting of the performance of a company has become a necessity: it's a crucial aspect of modern business. The SR3 Content Package equips companies with the tools and guidance needed to navigate the complexities of sustainability data management and

gathering while reporting effectively the scope 3 emissions. The content addresses challenges, promotes standardization, and provides a structured approach that helps organizations contribute to a more sustainable future while enhancing their competitiveness in an environmentally and socially conscious marketplace.