How should business approach carbon neutrality?
The solutions and benefits
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Introduction

Over the course of the past decade, a growing proportion of firms have started to pay greater attention to understanding, and managing, their overall carbon footprint. Such efforts are now widespread: according to Ernst & Young research, 82% of firms planned to invest in energy efficiency initiatives during 2011, as part of an increasingly common carbon journey that companies have embarked upon. Several factors weigh into how far along this journey an organization may be, including its industry, the geographic regions that it operates within, and the degree of maturity it has on carbon management. The ultimate target for this journey is a low- or no-carbon world, although such a destination remains a distant goal today. Nevertheless, for some firms, there is already an appetite for getting as close to that goal as possible, by aiming for carbon neutrality.

What does this mean? There is no single, globally accepted standard for carbon neutrality and its constituents to be encompassed within this. However, for the purposes of this report, we take the term to refer to corporations or product lines going carbon neutral. The basic process behind how a business might go carbon neutral is simple. At its core, firms would calculate their overall carbon footprint; reduce that as much as possible, largely through energy efficiency; and then offset any residual emissions that cannot yet be removed, so that their net emissions equal zero. But these simple steps mask much complexity — and a range of key management decisions. For example, companies need to define their own boundaries, time frames and approach to neutrality.

Making a decision to pursue carbon neutrality is a significant one for any firm. This report aims to highlight when and why such an objective might fit, while highlighting key decision-making points. In particular, the following seven questions act as a prompt to draw attention to the considerations involved with carbon neutrality and their implications.

Making the decision: key considerations for business leaders

Does carbon neutrality make sense within our industry and key markets?

One of the first points to assess is the external forces within a given marketplace, not least due to varying degrees of maturity worldwide. Some of the issues here include weighing up energy use, realigning the business to reflect strategic shifts in an industry and preparing for regulatory change. Balancing such issues is also a consideration of the varying perceptions of carbon neutrality by stakeholders across various markets.

Weighing up energy use

For most firms, energy is the source of the majority of their emissions, which in turn makes this a key factor in shaping their thinking on carbon neutrality. At one extreme are the highly energy-intensive sectors, including steelmakers, chemical manufacturers, cement makers and others. “As these industries are often already regulated, and as energy costs are usually prohibitive already, such firms typically prioritize energy reduction or greater use of renewable energy,” says Sudipta Das, Leader for Climate Change and Sustainability Services for Ernst & Young in India. Given this, the above sectors, as well as airlines, natural resource and extractives firms, energy and infrastructure companies, among others, are less likely to consider carbon neutrality as a corporate goal.

At the other extreme, for industries with lower energy use, and especially for firms with consumer-facing brands, the business rationale differs. Some firms will aim to pursue a low-carbon strategy; others will see a reason to go further, toward carbon neutrality. British broadcaster Sky is an example of a firm fitting in this category that have decided to go carbon neutral, seeing scope to enhance their brand at relatively low cost. Other common industries for pursuing carbon neutrality typically include retailers, consumer goods and apparel firms, food and beverage companies, and online businesses. “There’s often a lot of low-hanging fruit, and scope for competitive differentiation. And energy isn’t such a big part of the base cost of these firms,” says Euan Murray, an independent sustainability advisor.

Of course, energy considerations vary significantly by country. This is partly due to the energy mix of a given geography, as well as regulation (see next point). For example, as electricity often accounts for the majority of a firm’s carbon emissions, this makes them reliant on the carbon intensiveness of a country’s national grid. In Australia, for example, coal-fired power accounts for about 75% of all electricity generation. By contrast, in France, about the same proportion of electricity is sourced from nuclear energy. As such, the carbon footprint of a company can be higher or lower, depending on the energy mix of the country where it is based.

In turn, this can make the relative difficulty and costs of going carbon neutral vary from one country to another.

Regardless of a company’s energy usage levels, a fundamental aspect of any carbon strategy should be a focus on energy reduction, whether or not the business chooses to pursue neutrality as a goal.

Realigning the business to reflect strategic shifts in an industry

A further external factor to assess is the strategic direction of a given industry. In some sectors, it is clear that a shift toward low-carbon products is under way. One important example is the building industry, where carbon neutral buildings are becoming more common. To give some examples, Australia completed its first carbon neutral office building in 2010, South Korea completed one in 2011 and Hong Kong’s first will open in 2012. These add to many others across Europe and North America, in both the commercial and residential sectors.

“As these industries are often already regulated, and as energy costs are usually prohibitive already, such firms typically prioritize energy reduction or greater use of renewable energy.”

Sudipta Das, Ernst & Young
Indeed, carbon neutral buildings are likely to become standard requirements in many places, albeit based on varying standards: the UK aims to make all new homes “zero carbon” from 2016, while cities such as Vancouver are changing their building codes to ensure all new buildings are carbon neutral from 2020. Early examples of carbon positive buildings, which produce more energy than they consume, are also emerging, such as a new research center at the University of British Columbia in Canada. As the industry moves this way, there is clearly scope for leading companies to build and enhance their credibility by creating carbon neutral products and branding. “Many building companies are looking at this, because they know it’s the future,” says Eric Mugnier, from the Environment and Sustainability Services at Ernst & Young in France. In general, leaders need to consider the long-term strategic shifts of their market, and whether carbon neutrality can be a part of moving to where their industry is headed.

Preparing for regulatory change
Another external factor is the regulation of emissions. While there is no law in prospect that might directly require a firm to go carbon neutral, regulation can either prompt a few firms to try and do better than proposed carbon reduction rules in order to stand out from rivals, or else limit their attention to simply complying. Within the European Union (EU), for example, the Emissions Trading Scheme (ETS) gives a framework for many energy-intensive businesses to operate within, by setting a specific carbon price and cap. Similarly, individual countries have regulatory programs too, such as the UK’s CRC Energy Efficiency Scheme, or Australia’s recently introduced carbon tax. “Since the proposal of the government’s carbon pricing policies a couple of years back, the focus is higher on carbon reduction rather than carbon neutrality,” notes Mathew Nelson, Leader for Ernst & Young’s Climate Change and Sustainability Services in Australia.

A different consideration is the potential future interest for carbon labeling: various EU countries are watching a trial scheme that launched in 2011 within France, which the country hopes to make mandatory, as part of its 2010 Grenelle 2 law. Earlier, in 2009, Japan launched a trial called “Carbon Footprint System” for carbon labeling. Meanwhile, various large corporates in Switzerland, the US, Canada, Germany and Sweden have all started testing carbon labeling on products. The aim of such labeling is to make the carbon impact of consumer products as easy to compare as, say, calories in food, in order to help consumers choose between products. “This does not require firms to go carbon neutral but firms may seek to choose to do so in order to stand out,” explains Mugnier.

All this highlights the importance of conducting a detailed assessment of regulatory and policy trends, in order to be prepared for future shifts in the marketplace.

Regional perceptions
The above considerations also need to be weighed up from a country or regional viewpoint. Both awareness and stakeholder perceptions of carbon neutrality varies widely across different geographies. Of all regions, Europe is likely to hold the greatest potential upside for carbon neutrality, from a brand and consumer awareness perspective. By contrast, the term “carbon neutral” has become a contentious one in the US, in part due to improper claims by some companies in recent years. Many organizations here have shifted their strategies to purchasing renewables or energy efficiency, rather than carbon neutrality. In regions such as South America, there is simply limited awareness of carbon neutrality in many markets today, with many companies only starting to get involved in sustainability-related issues. “Companies are just becoming aware of their carbon footprint and measuring that. This has not become a strategic issue as yet,” explains Veronique Bakaert, from Ernst & Young in Chile. In Brazil, some leading companies, such as Natura, a cosmetics and beauty products firm, have gone carbon neutral, but the concept remains new. “The carbon neutralization concept is becoming popular in Brazil, although the market is not yet fully developed, with most companies still at the stage of creating an inventory of greenhouse gases,” says Marcos Preto, Director for Carbon Markets for Ernst & Young in Brazil.

2 UBC report, November 2011.
3 Carbon footprints: Following the footprints, The Economist, 2 June 2011.
Case study 1: Going beyond neutral – ITC’s carbon positive advantage

India’s ITC group, a multi-billion dollar conglomerate with businesses from hotels to packaging to IT services, provides a compelling case study of what a business can achieve from a long track record of sustainability. It has now been carbon positive – indicating that it removes more carbon from the atmosphere than it emits – for six years. It has also been water positive for nine years, and solid waste recycling positive for the past four years.

To achieve such goals, ITC has built an entire sideline business around sustainability and social investment. For example, its social and farm forestry program has set up plantations across some 114,000 hectares, as the single biggest contributor to its carbon positive status, while also developing new disease-resistant saplings to aid local communities. Arguably, other companies achieve similar outcomes through buying carbon offsets in reforestation schemes, while ITC handles this directly as part of a wide-ranging sustainability strategy, which spans all its businesses, employees, supply chain and partners.

Meanwhile, it has implemented numerous initiatives to ensure minimal energy consumption, from making all of its luxury hotels LEED Platinum certified to sourcing over one-third (35%) of its energy from renewables.

So why go carbon positive? Many of ITC’s initiatives have stemmed from concerns about rising environmental risk to its business, as a result of climate change. For example, in some businesses, its supply chain is highly dependent on agricultural inputs, making it conscious of climate and water risks. It also believes future regulatory regimes will increasingly constrict carbon emissions. So part of its future competitiveness will depend on its ability to minimize its carbon intensity and adopt a low carbon growth path. Few firms are likely to expand into forestry to help achieve the same carbon positive status as ITC, but many could learn from its wide-ranging actions to build a more competitive low carbon business overall.

Elsewhere, such as in India, awareness and interest in carbon neutrality has grown in recent years. ITC (see case study 1), a major conglomerate, has not only become carbon neutral, but claims to be “carbon positive” by being responsible for removing more emissions than it creates over the past six years. Public interest has been further stoked by efforts by Royal Challengers Bangalore, a popular cricket team, to involve all of its fans in its efforts to become a carbon neutral team. Similarly, awareness and interest in the concept of carbon neutrality is on the rise in the Middle East and North Africa too. BankMed became the first Lebanese bank to go carbon neutral,5 while Doha Bank, a Qatari bank, has committed to doing the same.6 Wild Guanabana, an Egyptian travel company, has gone carbon neutral and certifies that all of its customers’ journeys are carbon neutral too.7

Overall, firms need to weigh up the local and regional considerations for their businesses as part of their overall decision-making process. For some organizations, this might simply result in a change in focus. For example, US internet firm Yahoo originally planned to go carbon neutral in 2007, in part by offsetting emissions, but then changed focus in 2009 to energy efficiency and carbon reduction.

If carbon neutrality makes sense for a firm given the various external forces they face, what are the internal drivers that might bolster this? Some business leaders feel that it is simply the right thing to do. But while this may be a starting point, more fundamental business drivers need to be considered. These tend to break down into various categories:

- maintaining the license to operate;
- managing energy risk;
- differentiating the corporate brand;
- generating new demand; and
- driving innovation and cost-efficiency.

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5 BankMed becomes the first Lebanese bank to offset its greenhouse gas emissions, BankMed statement, 2010.
7 Wild Guanabana – region’s first carbon neutral travel company launches in the GCC, Go Green, 6 September 2011.
What are the internal drivers for carbon neutrality in the context of our overall business strategy?

Maintaining a license to operate

Certain product categories face a direct risk to their ability to remain in a market. The bottled water industry is perhaps the most prominent example of this. Numerous campaigns are trying to ban bottled water, including a number of city administrations in the US, Canada, UK and Australia, citing the environmental impact of bottling and transporting water that is easily available from the tap. In response to this risk, a number of bottled water companies have sought to go carbon neutral, in order to maintain a license to operate. Iceland’s Icelandic Glacial, Norway’s Isklar, and France’s Evian, part of the Danone Group, are just some examples of water brands that have gone carbon neutral to defend against consumer concern over the impact of their products. Rather than being a mere communications tool, carbon neutrality is now a major part of these firms’ corporate strategy.

“It’s fundamentally about maintaining the license to operate,” says Chris Walker, a Leader for Ernst & Young’s Environment and Sustainability Services in the US. Such considerations have also driven a South American wine label, Concha y Toro, to measure its impact, and take one of its wine brands carbon neutral in key European markets. “They’re measuring the emissions of their product lines, in order to label them for retailers in Europe, but also in anticipation of market demand on that side,” says Ms Bakaert. Conducting a risk assessment of key market trends can be a useful tool to respond to them proactively.

Managing energy risk

Another driver is about removing or reducing energy risk for a business, partly due to uncertainty over the future energy costs. A growing number of firms are working to install decentralized renewable energy within their operations, to try to ensure more predictable prices over time, as well as cut emissions. Swedish home furnishing retailer IKEA, for example, is working to move to 100% renewable energy in the coming decade, in order to decouple itself from fossil fuel-based energy. Although simply focusing on carbon reduction can achieve similar benefits, some executives argue that setting a fixed objective of carbon neutrality helps to cement such aspirations within a business, and thus ensure that all parts of the business remain focused on the goal.

Differentiating the corporate brand

A common objective is to stand out within a competitive market. Just as a company might seek to differentiate itself on its speed of service, perhaps, some will see an advantage in having an identity that is cleaner and more environmentally friendly than their rivals. “It’s about leaders in a sector wanting to differentiate themselves, either to their customers, or else to capital providers,” says James Close, from Sustainability and Cleantech Services at Ernst & Young in the UK. One example comes from Tata Steel in India. Although its industry is energy intensive, the firm has created a carbon neutral product, Confidex Sustain, which is a building envelope that has had its carbon footprint neutralized through offsets, the first of its kind in the industry.

Similarly for Marks & Spencer, strategic differentiation within the UK’s retail sector was a clear goal in setting its carbon neutrality target. It will achieve the target in 2012 through the purchasing of carbon offsets (see case study 2). “We saw it as a point of difference, and so set out this strategic vision for the business,” says Rowland Hill, Marks & Spencer’s Sustainability Manager. For others, carbon neutrality might align very closely with their overall brand positioning, such as organic food products. This also relates to a general aim for some firms of enhancing their corporate responsibility efforts. For Denmark’s Danske Bank, this was at the core of its decision to go carbon neutral in 2009. “It became very obvious to us to have a strategy to make a change in our overall emissions, as the next step of our CSR work,” says Kristian Højland, the bank’s Environmental Coordinator. Similar considerations applied for National Australia Bank, which went carbon neutral in late 2010.

Brand considerations are also pertinent in other regions, such as the Middle East and North Africa (MENA). “Companies here are adopting carbon footprinting and neutrality to help act as a catalyst for brand image and organizational efficiency,” explains Saravanan D, from Climate Change and Sustainability Services at Ernst & Young in the MENA region. This is especially the case for local companies with exposure to international markets, he says: “Another key driver is peer pressure. The MENA companies with exposure to markets face stakeholder pressure due to their international peers adopting neutrality.”
One specific marketing challenge is that in most markets, there are few or no independent brands or certifications that firms can apply for, while the requirement varies in those that do exist. Accordingly, the appeal of these needs to be weighed up against their market credibility, much of which is still being established. In 2008, in the UK, a proposed government kitemark system for carbon offsetting schemes was criticized over the nature of the projects it allowed. Accordingly, some firms rushed out new advertising or branding with carbon neutral claims that in turn exposed them to criticism, such as Dell or Fiji Water – an unfortunate setback for what is otherwise a laudable aim. “It’s a real requirement to do it properly, and to be seen to be doing it properly,” says Marks & Spencer’s Hill. The ultimate brand benefits of going carbon neutral vary widely by geography: far more European firms are likely to see an advantage in this, compared with US firms, given the more negative perception of neutrality in the US (see Regional perceptions on p3).

**Generating new demand**

A further consideration lies in the potential of increasing demand for products, if consumers might seek to choose between rival products on an environmental basis. The difficulty lies in assessing the degree to which this might impact demand. In the UK, for example, research from the Carbon Trust suggests that over half (56%) of people would be more loyal to a brand if they could see that it was taking steps to reduce its carbon footprint. In the US, consumer awareness of the term “carbon footprint” rose rapidly in recent years, according to the National Marketing Institute’s consumer trends database, although it is not clear whether this translates into people’s buying decisions.

Elsewhere, such as in the Middle East and North Africa region or across South America, consumer awareness of the concept of neutrality remains low. Certainly, in most markets, few consumers are willing to pay extra for environmentally friendly products. According to a 2011 Nielsen poll, 83% of global online consumers say it is important for companies to implement programs to improve the environment, but just 22% say they would consider paying more for this.

Demand generation may not necessarily involve a firm going carbon neutral itself, but rather positioning itself as a brand that can help its clients do so. Examples include firms such as Siemens and GE, the manufacturing conglomerates, which sell a range of products that in turn help cities and organizations cut carbon emissions. Similarly, German conglomerate Bayer invested €1b for climate-relevant R&D projects between 2008 and 2010, in part to substantially cut its own emissions, but also to develop new materials and technologies that can help clients do the same. One example is the creation of a zero-emissions office building in India, which it opened in January 2011 to showcase how its products can help cut carbon use and achieve neutrality. “The pathway toward carbon neutrality is part of the Bayer Climate Program, which is not limited to the efforts of the group to become carbon neutral, but it looks at how it can indirectly help its customers become carbon neutral by using its products and services,” explains Manfred Marsmann, Bayer’s Head of Corporate Environmental Affairs.

**Driving cost-efficiency**

Cost-efficiency is another driver that is perhaps surprising, given that carbon neutrality typically involves paying for some offsets. But by considering energy efficiency as a proxy for overall business efficiency, neutrality signals the most concrete goal a firm can aim for, removing any ambiguity about the need for cutting waste and thus driving deeper internal energy use reductions.

Alternatively, a firm may use carbon neutrality as a long-term goal to highlight the need to transform its carbon usage and use this as a means for driving greater internal innovation over carbon reduction. UK retailer Tesco has set a target of going carbon neutral by 2050. Its aim is to achieve this through carbon use reduction, rather than relying on offsetting. Part of the rationale is to create an internal shadow price for carbon, which in turn can help guide its investment decision-making. Indeed, setting an internal carbon price linked to an ultimate goal of neutrality can focus minds. “The big difference is that this is real money,” says Murray. “If a company is actually writing a cheque and this comes out of each business unit, then the real costs appear on their profit and loss. It then becomes part of the day-to-day management.”

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10 Low carbon products in demand despite challenging economic climate, Guardian.co.uk, 1 July 2011.
11 LOHAS Consumer Trends Database, Natural Marketing Institute, 2010.
12 Sustainability survey: Global warming cools off as top concern, Nielsen, 28 August 2011.
Case study 2: Making carbon neutrality a central part of Marks & Spencer’s brand value

British retailer Marks & Spencer created a stir in its market in January 2007 when it launched its wide-ranging sustainability plan dubbed “Plan A.” This set out 100 goals to achieve within five years, including a central commitment to go carbon neutral after embarking on a multi-year carbon reduction initiative, as part of a wider transformation of the business. The list of goals has now swelled to 180 commitments by 2015, although it still aims to go neutral during 2012. The retailer’s commitment to Plan A, and related promotion of it, has resulted in it becoming a brand in its own right – and has helped set the firm apart from its rivals by making it a central part of its overall operating strategy. Its efforts so far have also delivered substantial operational efficiencies, totaling £70m in its last financial year, although this will change when it starts paying for offsets for the carbon it can’t cut, or the electricity that it can’t switch to green suppliers.

But while Plan A is now simply a part of Marks & Spencer’s overall operations and brand appeal, it was a significant decision for its board to take at the time. Among some of the key considerations debated during the decision-making process were the potential future costs to the business and to what degree these could be mitigated by efficiency gains, as well as the risk that future regulatory change may impact certain cost assumptions, such as feed-in tariffs for clean energy. Over time, as the scope of the challenge evolved, it has not become any easier.

The first key aim was to reduce relative energy use by 25%, through a wide range of energy efficiency measures, in order to reduce the cost of offsetting. But while this relative gain in efficiency has been achieved, it has been wiped out by the firm’s absolute growth during this time, which in turn has raised absolute energy use. Another setback has been unpredictable changes in the feed-in tariff rates for green electricity, announced after Plan A was already set out. “We will achieve neutrality, but one reason it will be in 2012 and not earlier, is that the amount to offset will be much larger than some believed,” says Rowland Hill. “But if you ask people what they think Plan A means, many would summarize it as carbon neutrality and sending no waste to landfill, so we think it’s so iconic to the success of Plan A that we can’t afford not to do it.”

“The pathway towards carbon neutrality is part of the Bayer Climate Program, which is not limited to the efforts of the group to become carbon neutral, but it looks at how it can indirectly help its customers become carbon neutral by using its products and services.”

Manfred Marsmann, Bayer
Do we fully understand our carbon footprint and carbon reduction strategy?

To pursue carbon neutrality, it is imperative to gain a deeper understanding of the existing footprint first – and to establish plans to reduce this. “Do you have a good handle on your own carbon footprint? Do you know the numbers and the story of what makes up those numbers,” notes Chris Walker from Ernst & Young. “Some firms do this quite arbitrarily, so you need to know how accurately you can defend these numbers and why the boundaries you’ve set are what they are.”

Marks & Spencer’s Hill agrees: “Do the rough calculations first, work out how much on an annual basis it will cost you. People struggle with the concept, because maintaining this is an annual cost and activity, but you need to work out how much this will represent and see if it represents value for money.” This can be a time-consuming exercise. “One of the reasons we wanted a five-year timeline was to work out exactly what our emissions were, and what impact this would make,” says Hill. This requires both new skills and capital input. For example, calculating the emissions resulting from the firm’s fridges varies widely, depending on the different types of gases that any given fridge might run on.

All this highlights the importance of setting up a robust greenhouse gas accounting and reporting system, which in turn can better support any economic impact study relating to the costs of going carbon neutral. As part of this, it is crucial for firms to ensure that their processes for measuring and accounting for carbon use are robust, standards-based and well implemented. Marks & Spencer certify their performance using the British Standards Institute’s PAS 2060 which sets out a framework for an evidence pack to substantiate its claims. “The first point to consider is about the robustness of a firm’s internal processes, in order to make sure they’re not open to attack from the public, or NGOs, or consumer associations,” says Mugnier.

A further consideration is ongoing business growth, which needs to be considered within any economic impact study. For example, when Marks & Spencer planned its carbon neutral target, it aimed to cut its own emissions by 25% first, then switch its electricity purchases toward green energy suppliers, before finally offsetting the remainder. However, over the five-year time frame of this project, while a 25% improvement in energy efficiency was attained, the business continued to grow as well, thus expanding absolute energy usage. Nevertheless, by knowing that the balance will need to be offset, this goal keeps management tightly focused on achieving ongoing efficiency gains. “Ultimately, energy per square foot is the biggest metric for us,” says Hill.

“One of the reasons we wanted a five-year timeline was to work out exactly what our emissions were, and what impact this would make.”

Rowland Hill, Marks & Spencer
Once firms have a clear understanding of their overall carbon footprint, the next major consideration is deciding exactly which aspects of the business could or should aim to go neutral. This is not a trivial decision — and there is no globally accepted guidance as to what is best practice. For example, while all agree that direct emissions (those from sources directly owned or controlled by the company, such as manufacturing processes or vehicles) must be included, treatment of emissions of key suppliers, employees traveling to work, or customers using the products themselves is less clear. All of these considerations form part of the assessment that firms will need to make.

In making this decision, some firms will choose to focus on their existing operations, or their physical buildings, or across specific product lines, as just some of their options. Danone, for example, focuses on its Evian brand, ahead of the Group. Similarly, DHL has established a carbon neutral delivery option for its customers in a range of markets, including Germany and India. For some firms, going carbon neutral on a product line can be a useful precursor to a wider effort, by helping develop the necessary skills and experience required, even though some may argue that such efforts don’t fully qualify as true corporate carbon neutrality. Other industries, such as airlines, offer their customers an easy way to pay extra to offset their flight. In Australia, Qantas, Virgin Australia and Jetstar.com all offer passengers the option to do so, as do Continental and Delta in the US, among a number of others globally.

The scope of neutrality is dependent on how a firm chooses to interpret it. “Carbon neutrality is still an emerging area,” notes Murray. “There’s still a degree of uncertainty about various different standards relating to how everything is measured. And yet we know there are lots of organizations and brands making claims about themselves, their headquarters and products, with a lot of it being quite opaque and confusing.” Examples include firms that offset the carbon footprint of their head office, while then making claims that their entire business is carbon neutral, including their products. Criticism over misleading claims can derail the underlying benefits of such schemes and so companies must be clear about what they are including. In the US, for example, computer manufacturer Dell were criticised for using carbon neutrality parameters that only included a relatively small fraction in terms of total emissions.13

Given such concerns, it is crucial for firms to be transparent about whatever their target parameters are. Danske Bank, for example, has set out a specific methodology for deciding what to include or exclude in its own efforts, which encompass a mix of direct and indirect emissions (see case study 3). As a base principle, whatever a firm decides upon as a target, it needs to be definable and credible to its key stakeholders. Gaining independent assurance of that target is another important aspect of bolstering this credibility.

**Case study 3: Setting the scope of carbon neutrality at Danske Bank**

Danske Bank, a major Nordic Bank with about 21,000 employees, first went carbon neutral in late 2009, to coincide with the UN’s Copenhagen climate summit. Although the summit wasn’t the success many hoped for, the bank has stuck with its commitment as a central part of its corporate responsibility efforts. But as with any firm pursuing carbon neutrality, it has to define exactly what emissions it includes in the overall activities that it neutralizes. The company set out several principles that have guided its decision-making.

The first relates to the volume of emissions, to focus attention on the business areas that accounted for the vast majority of emissions, while excluding others. One example of an exclusion here is staff commuting by train, which accounts for a tiny fraction of the firm’s emissions.

The second principle is about sphere of influence, and the company’s ability to change emissions levels through its own actions. Again, trains don’t make the grade, as these are ultimately outside of the control of the firm, and will emit carbon regardless of whether the firm uses them or not.

Finally, it relates to the bank’s ability to measure actual emissions. Trains are a useful example, as it’s overly complex for the firm to realistically calculate its yearly emissions, based on the varying amounts of train travel its staff might take.

“Those are the three parameters we’ve set up, to decide what we do or don’t include,” says Kristian Højland, the bank’s Environmental Coordinator. What is crucial in all this, though, is that the firm’s decisions are detailed publicly: paper consumption and business travel by air are some of the elements that are included, for example, while employee commuting and their purchase of products and services are not. Some may disagree with its assessments and whether this qualifies as true carbon neutrality, but ultimately it is being open about its choices. “Transparency is what is most important,” says Højland.

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How do we engage with our key stakeholders?

Stakeholders are an important consideration for a decision to go carbon neutral. This starts out with the management team, to ensure that the firm's leadership is on board and are willing to make the necessary decisions involved. Beyond that, it is important to understand the views of shareholders, employees, customers and potentially suppliers.

Management

The first stage involves a firm’s management team. They need to sign off the relevant investment for the initiative and set the tone from the top, which is crucial to drive the project internally. “You need alignment with the CEO, CFO and chief sustainability officer, which properly commits them to doing the right thing,” notes Ernst & Young’s James Close. “It comes back to hearts and minds. You’ve got to win the argument about doing this, and you’ve got to have the leader out front on this.”

All those who have been through this agree: “It is a big decision. You need to get the different departments in a company convinced that it is a good idea, so that they support this,” says Danske Bank’s Højland. “You need your directors to sign off on the strategy, so that you can use this to drive more energy efficient operations. Some people think it’s a waste of money, so it needs a very high level decision.”

Shareholders

Regardless of how closely this fits with a firm’s overall strategy, and investors’ approval of that, most firms may face external shareholders with entirely contradictory views when it comes to carbon neutrality, from environmentally conscious stakeholders pushing for a tougher line on this, to others who might consider it a distraction from the core business. “Then there’s the challenge of communicating to shareholders, who have a traditional view of what makes money, and will ask why you are incurring costs ahead of creating value,” says Close.

The most important consideration for firms is to ensure they engage in dialogue, explaining how the strategy is being developed, to test assumptions and identify potential issues before it is implemented, as part of a detailed and robust stakeholder communication plan. This will help overcome specific challenges, such as the issue that some investors may regard carbon neutrality as a philanthropic add-on rather than a legitimate form of improved efficiency.

“It is a big decision. You need to get the different departments in a company convinced that it is a good idea, so that they support [carbon neutrality]. You need your directors to sign off on the strategy, so that you can use this to drive more energy efficient operations. Some people think it’s a waste of money, so it needs a very high level decision.”

Kristian Højland, Danske Bank

“It comes back to hearts and minds. You’ve got to win the argument about doing this, and you’ve got to have the leader out front.”

James Close, Ernst & Young
Customers
Evidence is mixed on the overall appeal of carbon neutrality to customers. In many markets, varying degrees of skepticism remains over climate change, so firms need to take this into consideration too. Equally, there is a need for basic education, given that the concept of neutrality remains relatively unclear. Both of these factors vary widely. In this regard, the development of carbon neutrality is similar to that of other schemes, such as Fairtrade, in which firms commit to making certain ethical operational decisions, to give consumers a choice. Many argue that consumer awareness will rise over time, with related shifts in purchasing decisions as a result. These shifts can be significant: as an example, a report from The Co-operative Bank highlights that spending in the UK on ethical goods and services, such as Fairtrade, nearly trebled between 2000 and 2010, from £16.1b to £46.7b.14

So far, however, the evidence on customer take-up on climate-related branding is mixed. For industries that have offered clients the opportunity to offset their purchases, such as flights, take-up has been low.15 Similarly, carbon labeling remains in its infancy, with different brands proliferating in various markets, such as Certified CarbonFree in the US, CarbonCounted in Canada and the Carbon Trust Standard in the UK.

Partners and suppliers
Depending on the scope of neutrality that is being targeted, and the nature of the business, suppliers play a significant role in achieving the target. At companies such as Timberland, for example, 96% of its emissions come from its supply chain, rather than its stores and logistics operations.

As part of this, some suppliers may be asked to play a deeper role, which may or may not fit with their strategic objectives. The first challenge lies in explaining to suppliers why this target is being set, and why suppliers should get involved in it too. This can be especially difficult for firms that are first movers in their market, or for firms with limited buying power and thus a reduced influence over suppliers. Therefore, depending on a firm’s size and industry dynamics, this may affect how they tackle the scope of their neutrality aspirations.

Employees
Depending on the depth of the commitment, seeking to go carbon neutral is something that affects all employees, so keeping them involved is crucial. It’s also a powerful engagement tool, in which staff can be empowered to make a significant contribution, suggesting ideas and improvements from across all aspects of the business. It is important to strike a balance on how such initiatives are communicated to staff. While many may be enthused by progress on such a scheme, not everyone will be. Some may hold a view that the money could be better spent elsewhere. In consideration of such issues, Danske Bank focuses on creating a series of stories about its carbon reduction-related efforts across the business, often treated humorously, to avoid taking an overly serious or lecturing tone to its staff.

Can any necessary offsetting be done in a credible way?

Of all aspects of carbon neutrality, carbon offsetting remains the most controversial. During the initial development of the global carbon-offset market, numerous concerns were raised, such as offset schemes that did not yield any actual carbon reductions, for example, or schemes that were sold multiple times. Such teething issues have damaged public perceptions of offsetting in certain markets, such as the US. Compared with a few years earlier, the industry continues to mature as standards and accreditations evolve and more capital flows through it. The World Bank estimates the size of the global carbon market at US$142b in 2010, a drop from 2009 levels but significantly up from about US$31b in 2006.

Concerns over offsetting continue. US sports apparel firm Nike has chosen to stop buying various forms of offsets as part of a wider rethink of its climate strategy and due to concerns about potential controversy (see case study 4). Bayer’s investments are clearly focused on developing and applying new technologies, from energy management systems to new building materials, rather than investing in carbon offsets. “We do not support the compensation market, because it does not make sense today for our business,” explains Mr Marsman. “We have to look for ways in which we can mitigate and decrease carbon, and decouple carbon from our productivity.”

If a company chooses to invest in offsets, it is important to provide an honest and transparent view of the plan that explains the extent of reliance on offsets over time. Timberland makes it explicitly clear in its reporting that the first commitment is to reduce emissions to the “greatest extent possible,” then to invest in renewable energy, while relying on offsets as a last resort. As of 2010, it had cut its absolute emissions by 38% against its baseline, with a target of 50% by 2015, before purchasing any offsets.

Not doing so can be risky. Bottled water company Fiji Water faced consumer worries about the significant environmental costs of transporting water from a South Pacific island to American stores. In response, the firm pledged in 2007 to go “carbon negative” – by buying more offsets than its products generated – as a key part of its response to such concerns. Unfortunately, the firm is facing a class action suit over its carbon offsetting approach. The litigants allege that the company has not gone carbon negative. Regardless of the firm’s actual actions, its brand has no doubt suffered as a result of it not exercising due caution in its planning.

Furthermore, it is crucial to do the necessary due diligence on offsetting providers or projects, in order to select a credible and high quality offset and avoid potential risk. Marks & Spencer plans to invest in Verified Emission Reduction (VERs), focusing on carbon credits calculated according to fully-fledged global standards, such as the Clean Development Mechanism’s Gold Standard (GS) or Verified Carbon Standard (VCS). Timberland purchases its offsets via a broker, investing in a Chinese wind farm that is validated and verified by third parties and that conforms to global standards, such as the GS.

“It is important for firms to verify and check the authenticity of systems, and to have a strong process and team in place to verify the quality of the offsets.”

Sudipta Das, Ernst & Young

“Credibility is everything with this, especially in this more skeptical time.”

Chris Walker, Ernst & Young

17 State and trends of the carbon market, World Bank, June 2011.
18 Fiji Water targeted in ‘Greenwashing’ class action suit, Environment Leader, 29 December 2010.
Whatever the choice a firm seeks to make, it is crucial that this is independently verified and audited, to ensure a third party stamp of approval. “It is important for firms to verify and check the authenticity of systems, and to have a strong process and team in place to verify the quality of the offsets,” says Ernst & Young’s Das. “Credibility is everything with this, especially in this more skeptical time,” adds Walker.

There are three further key considerations for firms: relevance, registration and repetition.

**Relevance**
The first is about linking any offsets purchased back to a firm’s overall strategy and core business. This isn’t a requirement, but it is a factor in explaining the overall rationale of the approach being taken, or a firm’s underlying brand principles and ethos. For example, a logistics firm might choose schemes that are directly related to transport. One example is a scheme in the US that invests in electrifying long-haul truck stopovers, to allow drivers to turn off their engines when sleeping, rather than idling them in order to heat the cabins, but also emitting various gases throughout the night.

**Registration**
The second important aspect is registering offsets to avoid criticism of double counting or fraud. “A lot of firms don’t register and retire their offsets in a recognized registry. This is a key aspect of the skepticism debate: the integrity of the process. How does the public know that the offsets you bought were not resold? This component is vital,” says Walker. “You need to put the offsets into a recognized registry that retires them so that they can never be sold again to claim a true offset. It is vital to the credibility aspect.”

**Repetition**
It is also important to ensure that this is not a one-off task: firms need to recalculate and update their total emissions each year, get them audited, and then offset accordingly. This needs to be repeated annually, especially as the firm grows. It may be tempting to consider offsetting a one-off action, but this is a long-term commitment. “Stick to this. Once you commit, you can’t renege on it. Sometimes it will cost you more one year than another, which hopefully means you will make better decisions,” says Ernst & Young’s Close.

### Case study 4: Rethinking Nike’s climate neutrality target
US sports apparel company Nike was an early convert to the notion of aspiring for carbon neutrality, setting out a long-term plan in 2001 to achieve neutrality by 2015. The aim involved making substantial reductions to the company’s overall carbon footprint, partly through greater energy efficiency, but also through buying carbon offsets and Renewable Energy Certificates (REC, a tradable certificate representing 1 MWh of electricity generated from an eligible renewable energy source).

But as Nike progresses along this path, its strategy for achieving its longer-term objectives is changing in response to shifting dynamics in the market. In 2009, for example, the company decided to stop buying carbon offsets against its business travel, but instead invest these funds in reducing total miles flown, in part through investments in global videoconferencing systems. Similarly, it has decided to stop buying RECs, in favor of greater energy efficiency and distributed energy projects, given that such certificates have become “increasingly controversial.” In its view, these changes, along with concerns over the clarity of what carbon neutrality actually means, have led the company to “re-examine” its goal as part of a larger climate and energy strategy.

In the short term, its decision to stop buying offsets gives a bump to some of its emissions totals. However, this doesn’t imply that the firm isn’t committed to getting closer to such an objective. Between 1997-98 and 2009, it cut its total greenhouse gas emissions from 7.5m tons of CO₂e to 1.53m tons, even as the business continued to expand. And as it outlines in its corporate responsibility report, “Moving forward, however, our preference is to achieve climate neutrality through a combination of energy efficiency and the purchase of more direct forms of renewable energy.”
What is an appropriate timeline to communicate the decision to go carbon neutral?

Given that many firms might seek to gain a communications boost from going carbon neutral, there is often an understandable desire to fast-track announcements. But moving too quickly holds certain risks, not least in terms of the need to take time to get to grips with a comprehensive carbon strategy. One risk lies in simply announcing a decision before fully understanding the implications of it, and then having to backtrack, such as the example of Yahoo. All experts and executives advise on the need to take time to think through the various challenges and to first conduct a detailed assessment of the overall strategy and implementation plan.

A secondary risk from moving too quickly is in rushing a carbon neutral product or business to market, only to realize that it is not credible in some way. Offsetting is a particular consideration here. For example, one specific concern often raised about offsetting is that of “additionality”, which relates to ensuring that the carbon reduction project being bought into would not have occurred without the offset investment. Such concerns can be overcome, but require firms to ensure that they audit and verify any potential schemes, which requires additional time for due diligence.

This highlights that the decision to go neutral remains a complex area, requiring significant effort, due diligence, and carbon accounting. There is scope for better tools and processes to calculate a firm’s carbon footprint, which can make initial efforts to do so very time consuming. On the offsetting front, companies such as Google in the US have noted that current standards for offsets “require a significant amount of work to evaluate the quality of each offset project.”20 “Don’t go too fast and not take the time to fully assess your opportunities and risks first,” advises Christoph Schmeitzky, Climate Change and Sustainability Services Leader for Ernst & Young in France.

Nevertheless, there’s no reason for firms to avoid making a start, at least in terms of planning. “This is a journey for every business. Getting started is the most important thing,” notes Murray, an independent advisor. This is true even if the business is unsure whether outright carbon neutrality is an appropriate goal. While Danske Bank decided to push ahead relatively quickly to achieve neutrality, it only did so after it was aware of its carbon footprint and associated cost implications. Other companies, such as Tesco or GlaxoSmithKline (GSK), a global pharmaceutical firm, have instead chosen to focus on setting a long-term aspiration of carbon neutrality in 2050, but balance this with various short- and medium-term targets to maintain progress. GSK, for example, has set a 25% reduction in CO2 emissions by 2020. Whatever the overall aspiration of the business might be in terms of carbon neutrality, setting specific carbon reduction targets needs to be an intrinsic part of the strategy.

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Conclusion

Setting these short- and medium-term carbon reduction targets are crucial aspects of setting a business on the right track toward achieving future targets and objectives.

Opting to pursue carbon neutrality as a corporate goal is not a light decision for executives, but requires a deep review of the business to assess whether and in what form this makes sense. For many firms, the allure of bolstering their corporate or product brand reputation is a key consideration in seeking to go carbon neutral. But understanding how best to market this message requires careful planning. What is crucial is that the approach they adopt is robust, transparent and based on available standards, such as the British Standards Institute’s PAS 2060, where applicable. Independent verification of this leads to credibility and transparency in the marketplace.

What is crucial is that it is not pursued as a stand-alone exercise, but as part of a broader sustainability strategy that encompasses the whole business. Once a business has decided how neutrality fits with its overall strategy, and done the due diligence behind the scenes, it can then approach any marketing efforts with greater confidence. Ultimately, what is most important here is securing the trust of any audience being marketed to.

As this report has outlined, carbon neutrality may not be the ultimate goal for businesses, but as part of a broader exercise in implementing a carbon reduction strategy, it can be a hugely beneficial tool – either as a longer-term aspirational target, or else simply as an internal benchmark to spur progress on energy efficiency. For a business considering carbon neutrality, it is important to think through the implications of what it might deliver, what risks and benefits could potentially result, and whether it represents value for money.
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