



Developing a Sustainable Procurement Strategy

Aligning indirect procurement with carbon negative ambitions

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Introduction

Background

In January 2020, [Microsoft committed to operate carbon negative](#) by 2030 and to reduce its Scope 1, 2, and 3 emissions by 55 percent. In response to these public commitments, Microsoft Procurement partnered with its supply chain counterparts and the central sustainability team to introduce language into the [Microsoft Supplier Code of Conduct](#). The following language contractually obligates our suppliers to 1) disclose their greenhouse gas (GHG) emissions and 2) provide a plan to reduce those emissions.

Suppliers must disclose complete, consistent, and accurate scope 1, 2 and 3 greenhouse gas (GHG) emissions data and/or components required to calculate GHG emissions data, via [CDP](#) or an alternative method that Microsoft will provide. If requested by Microsoft, suppliers must provide plans to reduce greenhouse gas (GHG) emissions in alignment with Microsoft's requirements. The timing of supplier conformance to this requirement may be determined by Microsoft standards and requirements that are set forth in their contract with Microsoft.

While the Supplier Code of Conduct applies to all suppliers across Microsoft, the remainder of this document describes the program for indirect suppliers¹ only. There are separate supply chain teams at the company that have distinct programs for engaging their supply base. These programs are aligned to the unique demands of the direct procurement space.

Emissions overview

- Scope 1 emissions are the direct emissions that your activities create—like the exhaust from the car you drive, or for a business, the trucks it

¹ By indirect, we mean suppliers providing things like consulting, marketing, and technical services. We are not referencing suppliers who support manufacturing, commonly referred to as the direct supply chain.

drives to transport its products from one place to another or the generators it might run.

- Scope 2 emissions are indirect emissions that come from the production of the electricity or heat you use, like the traditional energy sources that light up your home or power the buildings owned by a business.
- Scope 3 emissions are the indirect emissions that come from all the other activities in which you're engaged, including the emissions associated with producing the food you eat, or manufacturing the products that you buy. For a business, these emission sources can be extensive, and must be accounted for across its entire supply chain, the materials in its buildings, the business travel of its employees, and the full life cycle of its products, including the electricity customers may consume when using the product. Given this broad range, a company's Scope 3 emissions are often far larger than its Scope 1 and 2 emissions put together.²
- Additional details on how to account for carbon emissions can be found on our [environmental sustainability resources site](#).
- Microsoft's Scope 1, 2, and 3 emissions can be explored in [our sustainability report](#).

² Brad Smith. "[Microsoft will be carbon negative by 2030](#)." January 2020.

Supplier strategy

What are we asking suppliers to do?

In order to meet Microsoft's carbon reduction target, Procurement will be requiring its suppliers to reduce their total emissions (Scope 1, 2, and 3) by 55 percent compared to a 2019 baseline. The 55 percent reduction amount will be standard across all suppliers to ensure fairness. However, suppliers can voluntarily choose to reduce more, as interested. Additionally, suppliers will be required to submit plans detailing how they intend to reduce their emissions and actual reduction progress will be monitored.

We chose 2019 as the baseline year to arrive at a number that was both accurate and recent. Given the global COVID-19 pandemic, it did not make sense to look at data from calendar year 2020 as business travel was reduced, the majority of employees were working from home, and overall revenue potentially affected. The most recent year of "normal" data would then be calendar year 2019.

Microsoft contracts with thousands of suppliers in the indirect space. In order to focus our time on creating the greatest impact, Procurement is engaging with only a subset of its indirect suppliers on sustainability. Only suppliers comprising our top tiers of spend, which translates into 80 percent of our indirect supplier emissions, will be managed towards the disclosure and reduction requirements.

How we support suppliers in their efforts

Assessing supplier maturity

The maturity of our suppliers varies. For example, some companies already had a [science-based target](#) and dedicated environmental, social, and corporate governance (ESG) departments while others had never heard of carbon accounting. To better understand where they were at on their

sustainability journey, we asked suppliers to complete a brief maturity assessment on their company’s sustainability goals, initiatives, and external engagement. We then plotted that data against their impact on our overall emissions to group our suppliers into quadrants.

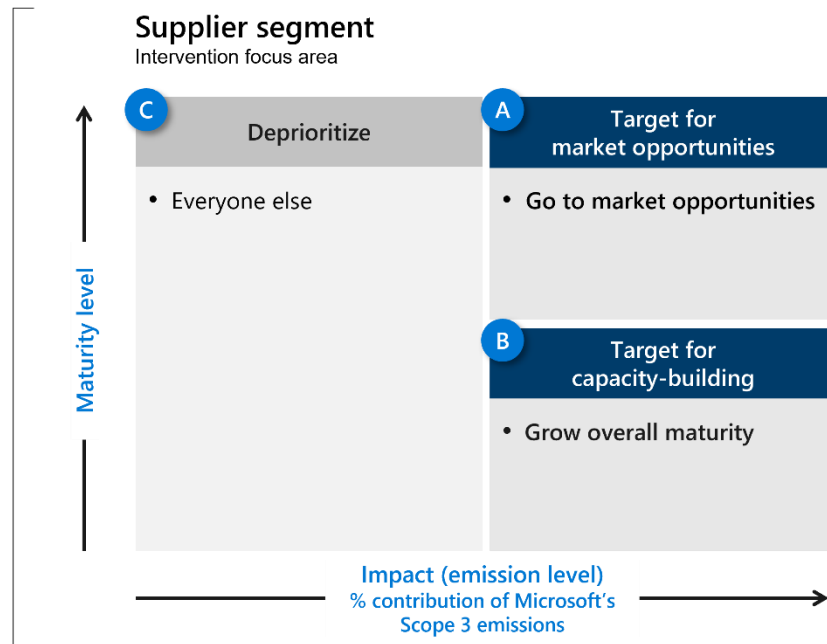
Maturity segmentation

Suppliers segmented by two dimensions

- **Maturity level** derived from assessment
- **Emissions impact** derived from CDP data

Segmentation can then be used to

- **Prioritize** suppliers
- **Define high-level intervention** roadmap



- Quadrant A: Suppliers on the top right have a significant impact on our emissions and are also very mature in the sustainability space. We partner with these suppliers on piloting new reduction program offerings as well as on go-to-market (GTM) opportunities.
- Quadrant B: Suppliers on the bottom right have a significant impact on our emissions but are just starting out with sustainability. Procurement leans in to engage with these suppliers on learning to support their emissions disclosure and reduction.

Actioning supplier feedback

After we rolled out the new requirements through the Supplier Code of Conduct in July 2020, we conducted listening sessions with a range of suppliers across size, industry, and geography. The most common feedback was that a focus on carbon disclosure and reduction was new and that suppliers would require support in meeting these objectives. In order to meet this need, we took several actions.

- **Webinars:** We conduct periodic webinars with our suppliers via Teams on topics ranging from GHG accounting to navigating the CDP portal to

explaining the details of Microsoft sustainability requirements. These webinars also provide a good opportunity to keep sustainability top of mind for suppliers. Attendance typically ranges from 40 to 60 people per live session with most attendees having responsibility for sustainability at their company.

- **1:1 meetings:** We conduct one to two individual meetings with each supplier annually. These meetings are valuable in building relationships with our suppliers and understanding what they need to succeed in the sustainability space.
- **Resources:**
 - **GHG accounting:** Looking across the sustainability industry in 2020, simple but comprehensive public learning resources to help suppliers understand greenhouse gas accounting were lacking. Resources were either too technical or narrow in scope. In response, we engaged with ENGIE Impact and CDP to build true 101 material. These materials are now hosted on [Microsoft's sustainability site](#) and received over 5,000 clicks in the first six months.
 - **Emissions reduction:** Given the importance of supplier emissions reduction to Microsoft's own carbon negative goal, Microsoft is also developing educational materials for suppliers on how to reduce their emissions. Resources on energy efficiency and renewable energy are published on [Microsoft's sustainability site](#). Other resources and initiatives on various emission scopes and categories are either internal or currently under development.

How we enforce these requirements

Although it is contractually required for suppliers to report their carbon emissions, Microsoft's achievement of its Scope 3 emissions reduction goal is intended to be a collaborative effort. For both emissions disclosure and emissions reduction, our first step will be to provide suppliers with a time period for remediation if they are non-compliant. This will allow us to meet with them to understand the drivers of the problem and to offer our help in identifying solutions. If non-compliance continues, further review and assessment will be conducted, ultimately ending with a process to migrate work to an alternative supplier.

Supplier data and data validation

Supplier data

Suppliers in the indirect Procurement space report emissions data via [CDP \(Carbon Disclosure Project\)](#). We supplement the available CDP data with industry emissions factors to cover our spend with non-disclosing suppliers. Suppliers who disclose their emissions are also asked to submit an emissions reduction plan to Procurement and to refresh it annually. This plan describes the actions that a supplier will take to reduce their emissions leading up to 2030.

We are building functionality into our internal supplier portal to capture this reduction information from suppliers. Once they submit their plan, we aggregate the data in Power BI to assess and monitor our forecasted progress to the 55 percent reduction goal. Following is a mock-up of the data we ask for.

Yearly Reduction Timeline: Emissions Reduction Action Plan to 2030

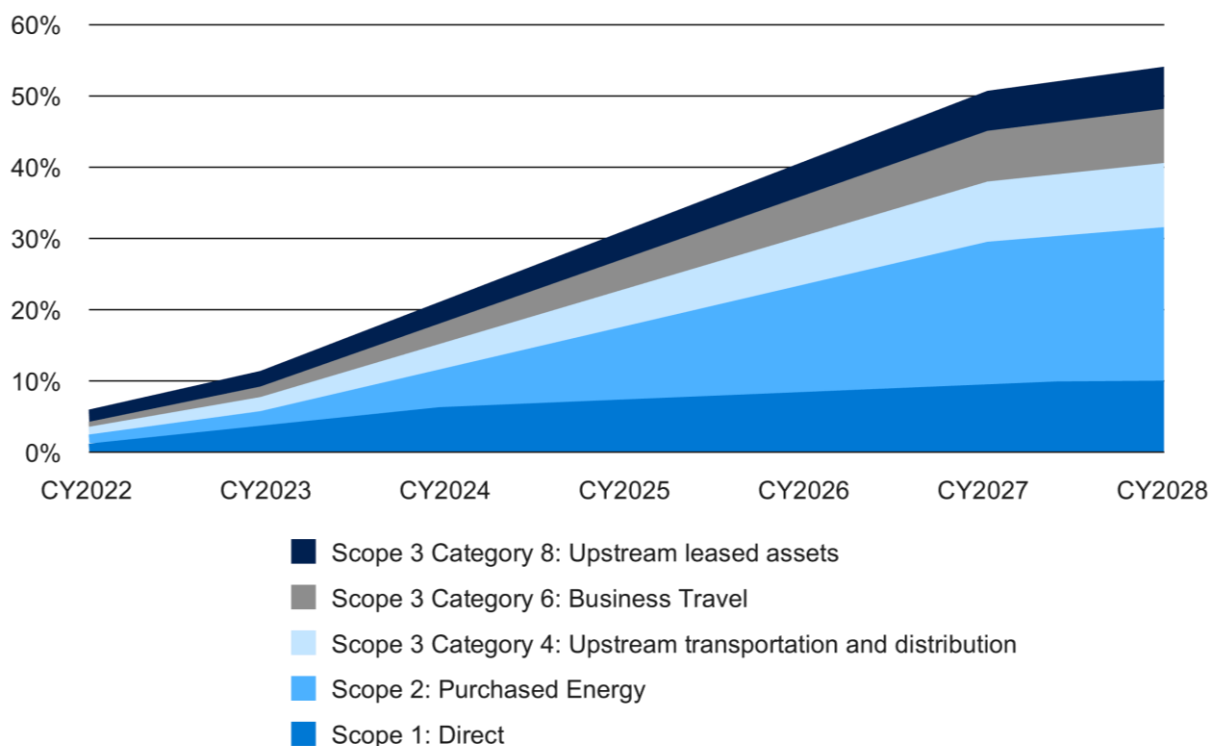
			FY 23	24	25	26	27	28	29		
			CY 22	23	24	25	26	27	28		
Yearly Emission Reduction % of Total Footprint			7.3%	9.9%	15.5%	10.5%	10.5%	2.4%	2.2%		58.3%
Scope (and category)	Emissions Reduction Lever	Associated Emissions Impact								Total Emissions Reduction % Per Scope/Category	Total Emissions Reduction % of Total Footprint
Scope 1: Direct	Initiative: (EXAMPLE): Electrification of company fleet vehicles	Impact: (EXAMPLE): Total Reduction of 50% on Scope 1	10.0%	10.0%	10.0%	10.0%	10.0%			50.0%	10%
Scope 2: Purchased Energy	Initiative:	Impact:	10.0%	10.0%	20.0%	10.0%	10.0%			60.0%	30%
Scope 3											18%
Category 1: Purchased goods and services	Initiative:	Impact:	15.0%	15.0%	15.0%	15.0%	15.0%			75.0%	2%
Category 2: Capital goods	Initiative:	Impact:			30.0%	30.0%	30.0%			90.0%	2%
Category 3: Fuel and energy related activities (not in S1 or S2)	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%			40.0%	1%
Category 4: Upstream transportation and distribution	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%		50.0%	1%
Category 5: Waste generated in operations	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 6: Business travel	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 7: Employee commuting	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 8: Upstream leased assets	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 9: Downstream transportation and distribution	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 10: Processing of sold products	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 11: Use of sold products	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%

Category 12: End of life treatment of sold products	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 13: Downstream leased assets	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 14: Franchises	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%
Category 15: Investments	Initiative:	Impact:		10.0%	10.0%	10.0%	10.0%	10.0%	10.0%	60.0%	1%

Individual supplier emissions reduction action plan template (mock-up only—not real data)

Visibility to and understanding of suppliers’ emissions reduction plans will be critical for meeting Microsoft’s overall reduction target. Progress against these plans will be monitored via reductions reported in future year CDP submissions. If a supplier says that it will purchase renewable energy, we expect to see a reduction in that supplier’s Scope 2 emissions in the next CDP reporting cycle.

Yearly progress towards total emissions reduction %



Example emissions reduction forecast visual (mock-up only—not real data)

Supplier data validation

The Supplier Code of Conduct language requires Microsoft’s suppliers to submit accurate data and our assumption is that, by submitting such data, they are acting in good faith and meeting their contractual obligations. Microsoft does reserve the right, however, to audit suppliers’ submissions.

Microsoft prioritizes completeness and accuracy in our greenhouse gas accounting, and this focus extends to our suppliers' greenhouse gas accounting as well. Organizational greenhouse gas accounting is a new activity for many of our suppliers, and it involves various assumptions, calculation methodologies, and data sources. Additionally, Scope 3 emissions are more complicated to account for than Scope 1 and 2 emissions. In the coming year, we will focus on expanding procedures to confirm the completeness and accuracy of supplier reporting, including data validation procedures at an aggregate level and review of suppliers' individual submissions.

Sourcing process

It is important that Microsoft use its buying power as a company to support our corporate social responsibility (CSR) commitments like sustainability. We are in the process of implementing several changes to our sourcing process, including an adjustment to how we view pricing, described following.

Carbon price

In January 2021, Microsoft released its inaugural [environmental sustainability report](#). A key learning Brad Smith, President and Chief Legal Officer, cited is the need to integrate a carbon price into the company's contracts: "Contracts today do not include a price on carbon, or the cost of getting and keeping carbon out of the atmosphere—and they must."

In order to integrate a carbon price into our contracts, Microsoft will take advantage of its existing carbon fee model. Specifically, we will highlight the anticipated carbon tax associated with supplier bids as a quantitative decision point during the request-for-proposal (RFP) process.

To do this, suppliers will be asked to disclose the estimated emissions associated with their bid as part of the RFP response. Alternatively, Microsoft can derive these project-level emissions from supplier-specific emissions intensity figures submitted to CDP. We will then multiply this emissions amount by our internal per metric ton of carbon tax amount to get the total carbon tax associated with the project.

The carbon tax cost will be presented to the business owner, alongside the cost of the actual project work, as an additional quantitative decision factor.

	Bid amount (USD)	Project emissions (metric tons)	Carbon Tax (USD)
Supplier A	\$20,500,000	1389 (emissions intensity x bid amount)	1389 x per metric ton cost of carbon tax
Supplier B	\$25,700,000	694 (emissions intensity x bid amount)	694 x per metric ton cost of carbon tax

The intent of surfacing the carbon tax is to enact behavior change within the various business groups through:

1. Incentivizing the business owner to choose a "greener" supplier.
2. Providing reinforcement to suppliers of the importance of making progress on emissions reduction.

Looking ahead

Sustainability is a journey for Microsoft and its suppliers. We intend to refine the processes we have established and stand up new ones to meet additional program needs. As we move forward in the next few years, we are going to be focused on several areas.

- **Emissions reduction:** If we are going to meet our 55 percent Scope 3 reduction goal, we need to be active partners with our suppliers in reducing emissions. What we mean is that we need to provide resources to support suppliers in making actual reductions. We described earlier in this document the learning materials we released on energy efficiency and renewable energy. Similar materials can be created for other scopes. We intend to continue to make these resources publicly available to help others learn from our experiences.
- **Industry influence:** Although emissions related to business travel represented less than 5 percent of our total emissions, we know that we can have a larger impact with our investments and partnerships. We have made two investments in sustainable aviation fuel (SAF) with airline partners KLM and Alaska. This year, we expanded this work by becoming a founding member in the [Sustainable Aviation Buyers Alliance \(SABA\)](#) and participating in the World Economic Forum's "Clean Skies for Tomorrow." We are actively supporting the development of an SAF certificate which will set GHG accounting standards for the use of SAF to reduce emissions by both customers and airlines in the future.
- **CSR alignment:** In addition to sustainability, Microsoft also has commitments in other CSR areas like accessibility and diversity, equity, and inclusion. We need to do more work in the next year to align our tools and processes within Procurement across all three of these areas to ensure we are creating a streamlined experience for suppliers and internal stakeholders.
- **Procurement tools and processes:** As described previously, we launched several templates this year, like our supplier emissions reduction action plan, in temporary formats like Excel. We will be spending the next few years integrating these new frameworks into our internal tools to create better user experiences.

To learn more about Microsoft's sustainability journey, go to <https://www.microsoft.com/en-us/sustainability>.

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