ENVIRONMENTAL ACCOUNTING AND REPORTING

From 2013, environmental reporting will become part of the Paper P1 syllabus and, therefore, an examinable topic due to its relevance to many discussions around accountability, transparency and sustainability - key themes of the paper. This article outlines what environmental reporting is, where it can occur and its advantages and purposes

For the 2013 exams onwards, a small but quite significant change applies to the Paper P1 syllabus in Section E of the *Study Guide*. It is in E7(a) and the change is the addition of the words: 'and environmental reporting'. So E7(a) now reads:
Describe and assess the social and environmental effects that economic activity can have (in terms of social and environmental 'footprints' *and environmental reporting*).
Although aspects of E7 have been examined before in Paper P1 exams, it was appropriate to include the issue of environmental reporting as an explicit topic in Paper P1 because of its relevance to much of the discussions of accountability, transparency and sustainability that are important themes in Paper P1.

WHAT IS ENVIRONMENTAL REPORTING?

There is a debate in business and society about the limits of business accountability. Put simply, this concerns two profound questions: 'for what should accounting actually account?' and 'to whom is a business accountable?' This debate is reflected in models such as the stakeholder/stockholder continuum and in Gray, Owen and Adams's seven positions on corporate responsibility. A common traditional belief is that businesses need only report upon those things that can be measured and that are required under laws, accounting standards or listing rules.

A range of other pressures has increased on businesses in recent years, however. Among these is the belief that business are 'citizens' of society in that they benefit from society and so owe duties back to society in the same way that individual human citizens do. Many people no longer believe that businesses are able to take from society without also accounting back to society (and not just to shareholders), on how it has behaved with regard to its environmental impacts. This article is about how companies account for their environmental impacts using environmental reporting.

WHAT DOES IT CONTAIN?

In recent years, then, a belief has arisen in businesses and in society that reporting has a wider role than that expressed in the traditional 'stockholder/shareholder' perspective. Importantly, one need not hold to the 'deep green' end of the argument to hold these views: there are strategic reasons why a wider view of accountability may be held and, accordingly, why initiatives such as environmental reporting may be supported.

I covered the subject of environmental 'footprint' in an earlier technical article (March 2009) but to recap, it concerns both the environmental consequences of an organisation's inputs and outputs. Inputs include the measurement of key environmental resources such as energy, water, inventories (especially if any of these are scarce or threatened), land use, etc. Outputs include the efficiency of internal processes (possibly including a 'mass balance' or 'yield' calculation) and the impact of outputs. These might include the proportion of product recyclability, tonnes of carbon or other gases produced by company activities, any waste or pollution.

These measures can apply directly (narrowly) or indirectly (more broadly). A direct environmental accounting measures only that within the reporting entity whereas an indirect measure will also report on the forward and backward supply chains which the company has incurred in bringing the products from their origins to the market. For example, a bank can directly report on the environmental impact of its own company: its branches, offices, etc. But to produce a full environmental report, a bank would also need to include the environmental consequences of those activities it facilitates through its business loans. Where a company claims to report on its environmental impacts, it rarely includes these indirect measures because it is hard to measure environmental impacts outside the reporting company and there is some dispute about whether such measures should be included in the bank's report (the bank may say it is for the other company to report on its own impacts).

Reporting on environmental impacts is, therefore complicated, and is often frustrated by difficulties in measurement. In broad terms, environmental reporting is the production of narrative and numerical information on an organisation's environmental impact or 'footprint' for the accounting period under review. In most cases, narrative information can be used to convey objectives, explanations, aspirations, reasons for failure against previous years' targets, management discussion, addressing specific stakeholder concerns, etc. Numerical disclosure can be used to report on those measures that can usefully and meaningfully be conveyed in that way, such as emission or pollution amounts (perhaps in tonnes or cubic metres), resources consumed (perhaps kWh, tonnes, litres), land use (in hectares, square metres, etc) and similar.

GUIDELINES FOR ENVIRONMENTAL REPORTING

In most countries, environmental reporting is entirely voluntary in terms of statute or listing rules. In effect, however, it has become difficult to resist for large companies concerned about their reputations, certainly in highly developed countries in which large companies experience high political visibility.

Because it is technically voluntary, companies can theoretically adopt any approach to environmental reporting that they like, but in practice, a number of voluntary reporting frameworks have been adopted. The best known and most common of these is called the Global Reporting Initiative (or GRI).

The GRI is a reporting standard in that it prescribes and specifies how the company should report on a wide range of social and environmental issues. It arose from a number of organisations (some non-corporate) in the US seeking to enhance their reporting in the late 1990s. Its website describes itself in the following way:

The Global Reporting Initiative (GRI) is a non-profit organisation that promotes economic, environmental and social sustainability. GRI provides all companies and organisations with a comprehensive sustainability reporting framework that is widely used around the world.

As it evolved over time, the GRI became more influential, including in Europe and elsewhere, until many large companies adopted it as a framework for ensuring the breadth of their reporting categories. Some companies now openly say they report their voluntary information under GRI while others base their reporting on GRI guidelines without saying explicitly that they do so (perhaps wishing to adopt its provisions selectively).

WHERE DOES ENVIRONMENTAL REPORTING OCCUR?

Environmental reporting can occur in a range of media including in annual reports, in 'stand alone' reports, on company websites, in advertising or in promotional media. To some extent, there has been social and environmental information in annual reports for many years. In more recent times, however, many companies – and most large companies – have produced a 'stand alone' report dedicated just to environmental, and sometimes, social, issues. These are often expensive to produce, and contain varying levels of detail and information 'quality'.

Companies use a range of names for these 'stand alone' reports. Often linked to the company's marketing and public relations efforts, some companies include the word 'sustainability' in the title (perhaps 'sustainability report'), others include a range of social measures in addition to the environmental information (such as jobs created, skill levels in the workforce, charitable initiatives, etc). Some companies employ a wording in the title intended to gain attention and stimulate interest. Barclays, the UK bank, refers to its 'Citizenship report', for example, and GlaxoSmithKline, the pharmaceuticals company, produces a 'Corporate responsibility report'. Others combine environmental reporting with social and governance reporting to produce an 'ESG' (environment, social and governance) report.

ADVANTAGES AND PURPOSES OF ENVIRONMENTAL REPORTING

Because of the complex nature of business accountability, it is difficult to reduce the motivations for environmental reporting down to just a few main points. Different stakeholders can benefit from a company's environmental reporting, however, and it is capable of serving the information needs of a range of both internal and external stakeholders.

Some would argue that environmental reporting is a useful way in which reporting companies can help to discharge their accountabilities to society and to future generations (because the use of resources and the pollution of the environment can affect future generations). In addition, it may also serve to strengthen a company's accountability to its shareholders. By providing more information to shareholders, the company's is less able to conceal important information and this helps to reduce the agency gap between a company's directors and its shareholders.

Academic research has shown that companies have successfully used environmental reporting to demonstrate their responsiveness to certain issues that may threaten the perception of their ethics, competence or both. Companies that are considered to have a high environmental impact, such as oil, gas and petrochemicals companies, are amongst the highest environmental disclosers. Several companies have used their environmental reporting to respond to specific challenges or concerns, and to inform stakeholders of how these concerns are being dealt with and addressed.

One example of this is the use of environmental reporting to gain, maintain or restore the perception of legitimacy. When a company commits an environmental error or is involved in a high profile incident, many stakeholders seek reassurance that the company has learned lessons from the incident and so can then resume engagement with the company. For the company, some environmental incidents can threaten its licence to operate or social contract. By using its environmental reporting to address concerns after an environmental incident, society's perception of its legitimacy can be managed.

In addition to these arguments based on accountability and stakeholder responsiveness, there are also two specific 'business case' advantages. The first of these is that environmental reporting is capable of containing comment on a range of environmental risks. Many shareholders are concerned with the risks that face the companies they invest in and where environmental risks are potentially significant (such as travel companies, petrochemicals, etc) a detailed environmental report is a convenient place to disclose about the sources of these risks and the ways that they are being managed or mitigated.

The second is that it is thought that environmental reporting is a key measure for encouraging the internal efficiency of operations. This is because it is necessary to establish a range of technical measurement systems to collect and process some of the information that comprises the environmental report. These systems and the knowledge they generate could then have the potential to save costs and increase operational efficiency, including reducing waste in a production process.

In conclusion, then, environmental reporting has grown in recent years. Although voluntary in most countries, some guidelines such as the GRI have helped companies to frame their environmental reporting. It can take place in a range of media including in ‘stand alone’ environmental reports, and there are a number of motivations and purposes for it including both accountability and ‘business case’ motives.

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