Accounting for ethical, social, environmental and economic issues: towards an integrated approach

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1. Overview

This executive summary is concerned with the measurement and reporting of sustainability performance and its integration into the strategic management of an organisation. This short executive summary gives an overview of our research and findings.

The project involved two stages:

1.1 Examination of corporate reporting on sustainability performance

A sample of 100 Australian and 100 British companies’ external reports (both annual and, where available, discrete sustainability reports) covering the 2003 calendar year were collected. In addition to investors and analysts, the main audience of annual reports, the key stakeholders to which sustainability reports are addressed are: employees, customers, local communities, State authorities, the media, NGOs and pressure groups (see Adams 1999, 2002). Content analysis of the reports was undertaken by a single coder to identify the reporting of performance information using coding categories which focused on the nature of the disclosures made.

1.2 Case studies on the use of sustainability performance data

Interviews were conducted with four British and three Australian companies, selected on the basis that they are known as best practice organisations (with respect to collecting and reporting of sustainability information in a form which augments decision making), to examine the process of developing KPIs and the way in which sustainability performance data is used in management functions such as decision making, strategic planning, performance management and risk management.

Our findings indicate a low level of reporting on sustainability performance and a diversity of approaches to integrating sustainability performance data into strategic management processes. The low level of reporting on performance indicates that the performance – reporting portrayal gap identified in one company in Adams’ (2004) detailed case study is a widespread problem.

2. Objectives

Sustainability reporting and sustainability issues have received increased attention from corporations, the media, policy makers and the accounting profession. Much of this attention has however focused upon the sustainability information reported by corporations rather than on the sustainability impacts which companies are not reporting or how sustainability information is taken into consideration by management in their decision making processes.

3. Findings

3.1 Corporate reporting on sustainability performance

4. Conclusions

5. References

Acknowledgments

Researcher's contact details

1. BHP Billiton and Rio Tinto are included in both the Australian and UK sample.

2. An initial sample of 10 companies were reviewed by the authors and the coder to develop consistency in the accuracy of the coding categories and application of the instrument.

3. The analysis included cutting and pasting all observations under each category - hence further analysis of the disclosure content could be undertaken.
In filling this gap, this project explored two aspects of the manner in which organisations are addressing sustainability issues:

(i) the extent to which organisations’ sustainability performance related information discharges the organisations’ duty of accountability on ethical, social and environmental issues to external stakeholders; and,

(ii) how sustainability related data is being collated by organisations and integrated within the organisation’s strategic management and decision making processes.

3. Findings
The findings of the two stages of the project are reported below.

3.1 Corporate reporting on sustainability performance
We identified all disclosures concerned with the improvement or measurement of social and environmental performance. Once identified the disclosures were analysed and coded into seven categories:

1. Commitment to performance measurement or improvement: disclosures that expressed a commitment by the organisation to measure or improve overall social or environmental performance. Policy statements which did not specifically refer to improving performance were not included.

2. Quantified measures of performance (e.g. tons of CO2 emitted): disclosures that provided quantified measures of performance. For example, a disclosure in category 1 could have provided a statement with respect to a commitment to improve processes that impacted upon greenhouse gas emissions, whereas a category 2 disclosure would record the level of emissions.

3. Identification of specified targets: disclosures that identified specific targets for social and environmental performance. This category documented quantified targets rather than general statements for improved performance.

4. Performance against targets: disclosures of quantified data on performance against stated targets.

5. Future performance targets: disclosures that provided details of performance targets beyond the current year.

6. Acknowledgement of measures used within a management system: observation or acknowledgement that measures were incorporated within the management systems.

7. Identification of social and environmental performance factors impacting on decision making or change processes: disclosures that highlighted where social and environmental performance was influential in decision making processes, or where they resulted in changes in business practices.

A summary of the analysis of reports are provided below in Table 1.

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The results of the analysis reaffirm prior research highlighting that the majority of larger companies now disclose some information on social and environmental issues. However, with respect to performance reporting, most companies are only providing general, unspecified disclosures. For example, the following disclosure (Category 1) by the 3i Group was observed within their annual report for 2003:

"As an international business operating in 14 countries with around 750 employees worldwide, 3i aims to conduct its business in a socially responsible manner. It is committed to being a responsible member of the communities in which it operates and recognises the mutual benefits of engaging and building relationships with those communities... Environmental, ethical and social responsibility issues and standards are also taken into consideration in every aspect of the business." (3i Group, Annual Report, p 25)

The majority (75%) of British companies provided at least one instance of reporting quantified data on social and environmental performance (Category 2). Alarmingly 71% of Australian companies provided no quantified data on performance. Similarly 83% of Australian and 41% of British companies failed to identify specific targets (Category 3), whilst 88% and 57% respectively failed to identify performance against targets (Category 4). With regard to future performance targets (Category 5), 85% of Australian and 54% of British companies failed to provide any information. Only 23% of the Australian and 32% of our British sample acknowledged that performance measures were incorporated within their management systems (Category 6).

Examples of disclosures in category 6 include this from AstraZeneca in their 2003 Corporate Responsibility Report:

"During the year, we continued our programme of priority audit of main suppliers. In total, 14 sites were audited at our major chemical suppliers. Two potential new chemical suppliers were also audited and at one of these, we identified the need for an improvement in standards before any work could be commissioned by AstraZeneca. CR (Corporate Responsibility) is also being integrated into the regular business control meetings that are being introduced into our purchasing practice. In 2003, approximately 150 meetings that took place included CR considerations. (Emphasis added.) (AstraZeneca, 2003 Corporate Responsibility Report, p11)

Cadbury Schweppes noted that environmental performance data and employee opinion surveys were used in decision making (Category 6) though they gave little information as to how they were used:

"Working to a Group-wide Environmental Management System, we actively manage environmental issues and set detailed local performance targets with a factory audit programme based on a three year cycle. (Cadbury Schweppes, 2003 Environmental, Health and Safety Report, p 4). Approximately a third of the British sample provided disclosures indicating that social and environmental performance data is used in the decision making processes of the organisation (Category 7). AstraZeneca disclosed changes to products (Category 7):"
During the year, we completed a strategic strengthening of our product portfolio with a range of new high quality medicines that will drive AstraZeneca’s future success. Planning for the new products has included making necessary changes to our manufacturing processes and increasing the size of our sales forces (and consequently the distance travelled on business). Despite these changes, improvements in efficiency and lower carbon intensity of our fuel sources, coupled with a reduced use of our CFC driven inhalers, led to total emissions from all sources decreasing by 2% in 2003. We are still working hard to meet our target of a 10% reduction in our global warming potential over the 2001/2002 reference point by the end of 2005. (Astra Zeneca, 2003 Corporate Responsibility Report, p. 9)

BAE took such disclosure a step further and identified how performance information was then utilised and how it affected the business processes (Category 7). Regular employee opinion surveys are an important barometer of how well we manage the needs of our people. For example, in 2003, acting on feedback from our 2002 survey, our Australian business developed and implemented an Employee Recognition and Performance Scheme to reward good performance. Our next survey will be conducted in 2004. (BAE, 2003 Corporate Social Responsibility Report, p. 30)

Overall we observed that whilst many companies were providing some information on social and environmental performance, a limited number of issues were covered and many organisations failed to provide insight into how they were incorporating the information into management decision making.

Despite the low level of reporting found in the first stage of our project, the findings from our best practice case study organisations indicate that they are integrating environmental indicators, and increasingly also social indicators, into strategic planning, decision making, risk management and performance measurement. We also found the focus and key issues are organisation specific with considerable diversity in terms of the motivation for data collection and sustainability reporting, the scope of the data collected, the use of the data in decision making, and overall development of performance indicators relating to sustainability reporting. To provide some insight into the diversity of approaches, vignettes of two case study companies are provided:

One of the companies has a good reputation as a socially responsible bank, due in part to their active pursuit of community banking and subsequent involvement in the local communities. Until recently the company has been a relatively small and tight knit organisation which relied heavily upon a well developed sense of a ‘corporate culture’ to maintain its focus on the community. With considerable growth over the last ten years, there has been a significant increase in staff numbers and geographical spread which has subsequently placed pressure on the effectiveness of the ‘corporate culture’ to maintain the community focus. Management are now exploring the use of the Balanced Score Card (BSC) and use of Key Performance Indicators (KPIs) to formalise company interactions with the community as a response to an erosion of the effectiveness of the reliance upon the ‘corporate culture’.

A second company with significant environmental impacts has reported on the environment for nearly a decade and issue annual sustainability reports. Five years ago the organisation appointed a sustainability team to further develop the external reporting. One of the identified problems was the consistency and comparability of the information provided from the various regions and difficulty faced by the group Head Office in verifying such information. The team has therefore spent considerable time developing and defining metrics for the measurement of environmental performance. This has resulted in an improvement in data collected enabling Head Office management to access comparable data. However there have been some adverse consequences. For example, the data collection is predominantly driven by the external reporting process where a memo is sent annually from Head Office to site staff responsible for collecting the specific data, bypassing the regional managers.

The Head Office sustainability team are now actively pursuing means to enable more regular data collection and greater usage of the data by the regional managers.

These two cases are illustrative of the very different issues, approaches and concerns that we encountered in our case study companies. Whilst all seven companies were in some way engaging in sustainability management or reporting, we found no consistency in the approaches taken and the subsequent outcomes observed. Ad hoc development of such internal systems appeared to be motivated by various factors in the companies’ history. Even between companies in the same industry group there were very different approaches and priorities. All of the case study companies had arrived at integrating sustainability issues into management processes for different reasons and had gone about it in different ways. It was integrated into different aspects of management operations with different emphasis in each organisation, and the aspects of sustainability which were important to each organisation and their experience with the different dimensions of sustainability varied.

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Given the different emphasis in each case study company, it was no surprise that their views on where they should go in the future also varied. At the time of the interviews the finance department of one company had started to investigate the possibility of introducing environmental accounting and another company wanted to do more work on ethical screening of the parent companies of suppliers and improve the way they measure what they do in the community.

4. Conclusions

Our findings indicate a low level of reporting on sustainability performance and a diversity of approaches to integrating sustainability performance data into strategic management processes.

The low level of reporting on aspects of social and environmental performance and targets for performance in the top 100 British and Australian companies indicates that performance is not being adequately managed. Given the importance of shareholder confidence in all aspects of management and the importance of accountability to key stakeholders on material social and environmental impacts to the long term success of an organisation, this is an issue on which professional accounting bodies could assist companies. Accountants could be trained in social and environmental data collection, reporting, verification and use. Professional bodies could provide guidance on social and environmental data collection processes and reporting formats.

Our case study ‘best practice’ organisations have recognised the importance of integrating sustainability performance data into their strategic planning, risk management and decision making processes and are making significant progress in doing so. However, the diversity of their approaches and the low level of reporting on performance indicate that British and Australian companies would benefit from greater guidance on this aspect of their work. Whilst our seven case study companies, with the resources and the know-how to do so, are committed to continuing to develop their approaches to integration in this way, the majority of British and Australian companies would clearly benefit from further guidance in this respect. Professional bodies could extend the training given to accountants on use of financial data in strategic planning, risk management and decision making to the use of social and environmental data. Accountants would then be in a better position to assist organisations in achieving long term success.

On the role of companies in educating society, the corporate environment director from one company said: ‘I think we have an educative role in terms of explaining the consequences of the use of our product, what kind of things you can do to use it sensibly, but not the sort of societal shift which would move you towards a society which is actually looking at consuming less. I don’t mean just consuming less electricity but the whole gamut of consumer society. You are talking about a different kind of economics there, and I think to ask an investor owned utility to do that is difficult. It is the role of public education.’

Our results highlighting the lack of reporting on performance and targets indicate that many companies are not fulfilling their educative role of informing their stakeholders of the consequences of using their products and services. The lack of education and training of accountants in this regard is hindering the reporting and use of social and environmental performance data. Without this basic data the success of any wider public education will be limited.
5. References


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