

Why Sustainability Counts for Professional Accountants in Business



**International Federation
of Accountants**

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**WHY SUSTAINABILITY COUNTS FOR
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WHY SUSTAINABILITY COUNTS FOR PROFESSIONAL ACCOUNTANTS IN BUSINESS

Sustainability presents both a challenge and an opportunity for the professional accountant in business (PAIB). The PAIB needs to recognize that individuals, societies and governments are increasingly interested in the environmental, social and economic impacts of enterprises and that PAIBs are likely to have an increasing role in meeting those concerns. To help them meet these challenges PAIBs should focus on their continuing professional development (CPD) needs and carefully consider, attain and refine the skills they will need to meet the expectations of them as qualified professionals.

This information paper provides an overview of enterprise sustainability and sets out the business/financial case for addressing sustainable development at the enterprise level in terms of the risks that sustainable development poses and the opportunities which it brings. The paper also seeks to identify the main sustainability related roles which the PAIB might occupy, today, tomorrow or at some more distant future time. The paper is published simultaneously with a theme booklet in which high profile PAIB explain how sustainability issues impact them.

What is Sustainability?

The notion of enterprise sustainability is rooted in the wider concept of sustainable development. There are many competing definitions of sustainable development but arguably the foremost is that of The Brundtland Report.¹ This report implored the present generation to take immediate action to avert the risk of causing irreversible ecological damage. It defined sustainable development as “development which meets the needs of the present without compromising the ability of future generations to meet their own needs.”

This definition means taking account of the wider and longer term consequences of decisions. It means thinking about the impact of economic activities—things bought, investments made, waste thrown away, pollution generated—on the natural and human resources on which they depend. It means ensuring the productive capacity of these resources is not irreparably damaged, and that resources are not depleted faster than they can be replenished. In practical terms, this means taking into account the consequences of economic decisions on the natural environment, on economic development, and on the social conditions in which people live and work.

Sustainability and Corporate Social Responsibility (CSR) are terms that have often been used inter-changeably. Sustainability, however, is more of an over-arching concept which seeks to promote continuous long term growth in all the various forms of capital available to us—financial, natural and social. By contrast many see CSR as a more limited concept, focused on shorter-term issues and activities such as legal compliance, philanthropy and improvement in workforce conditions. In general it might be said all organizations aspire to being responsible but few would claim to be truly sustainable.

¹ *Our Common Future*, United Nations World Commission on Environment and Development (1987), <http://www.brundtlandnet.com/brundtlandreport.htm>

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Capital maintenance, the central tenet of the sustainability concept, explains that an activity is unsustainable if, when continued, it would undermine and eventually exhaust the basis for its own existence. For accountants, the implications should make absolute and immediate sense.

Sustainability and Business Strategy

Many of the world's largest and most respected companies, including all of the ten largest companies by revenue listed on the Fortune 500 list in 2005² together with Microsoft, IBM, HSBC, Anglo American, Roche and countless other companies of all shapes and sizes, have publicly stated that sustainability forms a key part of their business strategy. There is an increasing trend for organizations operating in the public sector (government departments, agencies and state-owned enterprises) to do likewise.

Exhibit 1 shows how Anglo American, a leading global operator in the mining and natural resources sectors, sees sustainability as a core part of their business strategy.³

Exhibit 1: Sustainability and Business Strategy
“Sustainable development principles are central to our business strategy.” Source: <i>Anglo American plc Report to Society 2003</i> , http://www.angloamerican.ca/s/AboutAngloAmerican.asp#Sustainable

While sustainability often forms part of an organization's mission or strategy, enterprises often vary in what they view as the main challenges to embedding and integrating it into day-to-day operations. Making sustainability part of the way a company operates means learning to look at its business through a new lens. Organizations in the public sector face similar challenges. The sustainability lens reveals the world through the eyes of its stakeholders and helps an organization to understand the many ways, good and bad, that operating activities affect and are affected by society, the economy and the environment.

What is the Business/Financial Case for Engaging with Sustainability?

Sustainable development is an issue which is high on the political agenda of many governments. Political agendas beget regulatory regimes and fiscal instruments, both of which impact directly on the business community, whether large or small. Sustainable development, or rather some of the constituent aspects of sustainable development—such as avoiding environmental damage and ethical sourcing of products—are on the agendas of a wide range of consumer organizations and non-governmental organizations (NGOs). Failure to engage with the challenges of sustainable development therefore poses risks—strategic, business and reputational—which all organizations should consider. Some, by virtue of the industry sectors they operate in, are more exposed and responsive than others. Failure to address these risks could certainly increase the cost of capital and, at the extreme, could result in an enterprise losing its license to operate.

² Fortune Global 500 2005, <http://money.cnn.com/magazines/fortune/global500/>

³ Aspects of Anglo American's annual sustainable development reports are independently assured by KPMG.

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However, sustainable development also presents organizations—particularly private sector businesses—with opportunities to modernize and innovate. Exhibit 2 contains a number of examples of the benefits of both adopting a sustainability agenda and reporting publicly on their progress.

Exhibit 2: The Business Case for Adopting a Sustainability Agenda
Paul Monaghan, Sustainable Development Manager at the Co-op Bank says, “We have calculated ethical and ecological benefits of sustainability reporting to be in excess of £40m profit contribution to products and services. Producing a sustainability report has enabled us to manage a whole host of ethically and environmentally motivated risks much more robustly.”
Baxter International, the US healthcare company, analyzes its basic environmental compliance costs and other response programs and compares them with the savings it derives from environmental initiatives. In 2003, Baxter reported savings of \$69 million as compared with total environmental costs of \$22 million.
British Telecom, in their 2003 sustainability report point out that, “our environmental program, which includes energy efficiency and fuel savings, has saved BT more than £600 million over ten years.” BT also point out that their strong focus on social and environmental issues has been a crucial factor when it comes to bidding for new contracts: £900 million in their 2004 financial year.

As noted above, attention to social, environmental and economic aspects of economic activity and performance is increasing from customers, suppliers, investors, NGOs and the community.

In a sense each group’s support gives the enterprise a license to operate without which, the enterprise may find its ability to operate effectively impaired and its performance damaged over the long term. Thus a company that misbehaves may face a doomsday scenario in which they will find fewer and fewer trading partners, consumers will stop buying their products, host nations will withdraw their license or impose fines, local communities will withdraw their support and possibly become hostile, and workers will become de-motivated and unproductive. In addition, investors will stop buying their stock, existing shareholders will sell, banks will increase their lending rates and the cost of capital will increase.

At the organizational level, sustainability is often argued to be about long term viability. Organizations will not have a long term future if they cannot be profitable, efficient and ethical. This suggests that the importance of long term viability is best observed via the long term investment decisions of insurance companies and pensions providers, but all multi-national companies look to grow long term shareholder value. Exhibit 3 demonstrates how three of the world’s largest companies see the pursuit of sustainability as critical to maximizing long term shareholder value.

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Exhibit 3: Sustainability and Long Term Shareholder Value

“Toyota strives to continuously improve its environmental record while seeking growth as a profit-making business. These two imperatives are not in conflict. In fact, Toyota sees environmental sustainability as a prerequisite for long term business sustainability. To quote the report, “To ensure that our vehicles continue to contribute to economic growth, Toyota has positioned the environment as a priority management issue.”

Source: 2004 Toyota North America Environmental Report,
<http://www.toyota.com/html/hybridsynergyview/2005/spring/enviroreport.html>

“Profitable growth and acceptance of our responsibility in respect of the environment and society go hand in hand at DaimlerChrysler. We also understand that sustainability is an essential element of our corporate activities and necessarily contributes to the interests of our customers, employees, shareholders, and society-at-large. At the same time we align such activities with our global, international, regional, and community undertakings.”

Source: DaimlerChrysler Sustainability Profile 2005,
http://www.daimlerchrysler.com/Projects/c2c/channel/documents/699381_sustainability_profile2005_e.pdf

“Sustainability is central to our business. Why? Because our fundamental purpose is to maximize shareholder value on a long term basis.”

Source: BP (2005), <http://www.bp.com>

There is a growing body of evidence supporting the business case for sustainability. But, as with much business research, it is often inconclusive and short on fully quantitative support. As mentioned above, many companies and public sector organizations have made sustainability an integral part of their business strategy. An increasing number of studies and reports provide evidence, largely anecdotal but some quantitative, that sustainability makes sound business sense. It follows, therefore, that accountability and transparency, governance and reporting, risk management, and finding sources of competitive advantage are the primary business drivers of sustainability. All of these activities are in the domain of the PAIB.

What Role Does the Professional Accountant in Business Play in Sustainability?

The PAIB has a role to play in understanding, demonstrating and achieving the efficiencies that organizations can gain from sustainable business practices. The pursuit of sustainability depends on the generation, analysis, reporting and assurance of robust and accurate information (both financial and non-financial). Hence, it is important that the PAIB gain an understanding of the concepts of sustainability and the challenges it poses in achieving long term growth in shareholder value or value for money.

The role of the PAIB in sustainability extends beyond the obvious one of collecting, analyzing and reporting sustainability-related information. Many PAIBs fill a variety of other positions

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within organizations, including senior management, in which they exert a more direct influence on strategy and decision making.

The PAIB, directly or in a supportive capacity, can help organizations embed sustainability issues into strategic planning and its execution. The PAIB can also help overcome the various cultural, organizational and economic impediments to sustainability. For example, decisions are often made on a short term basis and typically on the basis of incomplete or imperfect information which excludes external and intangible costs and benefits. The PAIB is well placed to encourage longer term thinking and provide a more complete information package to decision makers.

Sustainability accounting is the term normally applied to methodologies designed to financially quantify the impacts of enterprise activity on the natural environment and the social stakeholder community.

Sustainability reporting (triple bottom line reporting is usually classed as the main approach to sustainability reporting) seeks to communicate material on how sustainability impacts on stakeholders in the form of a publicly available report. It should also cover management's general philosophy regarding sustainable development.

Sustainability assurance is the activity of expressing an independent expert opinion on the reasonableness of a sustainability report.

Sustainability management is the organizational activity associated with identification of key sustainability challenges and impacts, and the effective management of them so as to minimize risk exposure.

Specific Activities and Roles

The specific role the PAIB will play in sustainability will vary by organization and position within the organization. These roles might include:

- Developing policies to address sustainability issues, their application and the monitoring of them across the organization and in managing the associated operating risks;
- Involvement with the design, operation and monitoring of purchasing policies, standards and management systems relating to the supply chain;
- Supporting stakeholder engagement processes with readily accessible and reliable information, and assisting with the collation and analysis of stakeholder feedback;
- Identifying those voluntary environmental or social codes appropriate to their business or integrating operation of the codes with an existing management information system;
- Supporting benchmarking by providing relevant and reliable information in accessible, meaningful and comparable ways;
- Providing effective support for businesses affected by emission trading schemes, by collecting and interpreting information, monitoring and controlling market activities;

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- Maintaining and expanding their knowledge of regulations, taxes and subsidies applicable to the business with which they are involved, so as to provide timely information about relevant environmental and social issues; and
- Supporting the data preparation and reporting mechanism and contributing to the associated interpretation and decision-making.

The enterprise drivers of sustainability—accountability and transparency, governance and reporting, risk management, finding sources of competitive advantage—all impact the work of the PAIB. Risk management in particular is now acknowledged as a major driver behind corporate engagement with sustainability issues.

Concluding Comments

The opportunity for the PAIB lies in:

- Helping organizations address sustainability issues;
- Supporting organizations' efforts to engage, build and maintain relationships with stakeholders; and
- Managing sustainability related risks for investment purposes.

The challenge lies in ensuring that PAIBs are fully equipped to measure, record and interpret sustainability related information issues and, are sufficiently informed about sustainability to preserve their place in the mainstream of business decision-making.

With skills in information collection, analysis and reporting, and an understanding of the assurance process, PAIBs are well-placed to help organizations meet the challenges of sustainability. It is for accountants to recognize this and assume this role, building their knowledge of sustainability and drawing on other expertise where necessary.

Sustainability presents both new challenges and new opportunities for the PAIB. With the increasing importance attached to environmental protection and social responsibility, many of the issues raised by the quest for sustainable development are business risk issues, an area commonly of concern to the PAIB. Devices such as tradable permits and other mechanisms described in this paper will require accounting expertise. PAIBs, especially those working for organizations with significant environmental or social impacts, will be involved with the measurement, recording and interpretation of sustainability-related information. Future management information systems and controls will need to include environmental and social data, emphasizing the benefit of an integrated approach. The PAIB is well placed to provide the necessary coordination.

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The PAIB Committee Sustainability Project

The outputs of the PAIB Committee's three year sustainability project will be:

- An Information Paper entitled, "PAIB—At the Heart of Sustainability," issued in parallel with this paper in which high profile PAIB explain how sustainability issues impact them; and
- More detailed guidance on best practice in sustainability accounting, reporting and assurance.

More information about the PAIB Committee Sustainability Project can be found online at: www.ifac.org/paib



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