ADDING VALUE AND CREDIBILITY TO ENVIRONMENTAL REPORTING AND THIRD PARTY STATEMENTS

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There are over a hundred U.S. corporations producing voluntary annual environmental reports. An increasing number of firms have contracted with third parties such as accounting or environmental consulting firms to conduct audits to verify the accuracy of these reports. These "third party statements" are an attempt to enhance the overall credibility of their environmental disclosures. In March of 1996 the IRRC (Investor Responsibility Research Center) and GEMI (Global Environmental Initiative) completed a joint project to evaluate the value of third party statements to key stakeholder groups.

The joint research project concludes that third party statements do not add "much, if any, incremental value to corporate environmental reports" and that the study team "did not trust any" of the potential attesting organizations. The report indicates that these reviews ***could add value***, if they are based on sound environmental standards and performed by credible outside organizations.

There is currently underway an initiative by several large, nationally recognized institutions to develop standards and perform credible third party statements. This paper discusses the evolution of environmental reporting, its current status, and innovative new research to provide a framework for credible and effective reporting.

SARA Title III is limited to a specific list of chemicals exceeding a volume threshold at manufacturing sites in certain industry categories. Although somewhat limited in scope, the law had a profound impact on industry in general. For the first time corporations clearly saw that they had**,** if not a moral duty, a legal obligation to report on the potential environmental impact of their operations. Technically, release *quantity* does not directly translate to environmental *impact*, but the information has been used by the public and the media as a measurement of trends and *perceived* impact.

Not surprisingly, stand-alone corporate environmental reports first appeared around the same time as the emergence of SARA Title II requirements. Many of these early efforts were glossy, public relations productions filled with beautiful pictures, but few facts and almost no negative information. Public reaction was not always positive, and the term "Greenwash" was born[1]. No mechanism existed to verify public disclosures of EHS information and these reports did little to dampen public skepticism. A coalition of social investors, environmental groups, religious organizations and public interest groups met in 1989 and established a set of principles for corporate environmental activity, known initially as the Valdez Principles. The objective was to promote corporate environmental responsibility and was initially greeted with industry distrust. Later renamed the CERES Principles (Coalition for Environmentally Responsible Economies), reporting

standards have been modified, and approximately 50 companies are signatories.

Partly in response to CERES, industrial groups such as GEMI (Global Environmental Management Initiative)[2] and PERI (Public Environmental Reporting Initiative)[3] undertook initiatives to define responsible corporate reporting. Recently, the number of standards on the content environmental reporting has grown dramatically. In addition to GEMI and PERI there are:

- UNEP (United Nations Environmental Programme Guidelines)[4]
- CICA (Canadian Institute of Chartered Accountants)[5]
- WICE (World Industry Council for the Environment)[6]
- Stakeholder Alliance (Center for Advancement of Public Policy)[7]
- EPA's ELP (Environmental Leadership Program)[8]

In addition to specific standards on reporting**,** there are a number of environmental principles and codes of practice. Some are global[9]; Some are country/ industry specific.[10] Liability disclosure practices are also under development by financial accounting organizations and regulators[11]. A number of organizations have evaluated corporate reports[12] and the United Nations has developed a 5 stage model to rate different reporting styles from Stage 1 "green glossies" to Stage 5 "sustainable development" reporting[13].

Combined, these standards, principles and practices provide a detailed framework for the *content* environmental reports. Reports are now evaluated on the number of charts and tables and the comprehensiveness of the data, not on their professional editing and attractive photographs. Glossy productions without hard data are now considered to be worse than no EHS report at all. Technically, release *quantity* does not directly translate to environmental *impact*, but the information has been used by the public and the media as a measurement of trends and *perceived* impact.

Progress Towards Improving Disclosure Credibility

In addition to greater standardization on the content of environmental reports, there is a growing movement to improve the *credibility* of EHS information reported.

Corporations in the past have used external auditors to verify key disclosures to stakeholders. In the United States financial statements are, as a matter of routine, audited by accounting firms under standards enforced by the Security and Exchange Commission and guidance established by accounting organizations. Utilizing this precedent, a number of corporations began using outside organizations such as consulting firms to provide third party audit statements similar to financial audit verifications. This has met with mixed results.

In 1996 the Investor Responsibility Research Center (IRRC) in collaboration with the Global Environmental Management Initiative (GEMI) investigated the value of third party statements.[14] The focus group's research concluded that third party statements do not add "much, if any, incremental value to corporate environmental reports" and that the study team "did not trust any" of the potential attesting organizations. The report indicates that these reviews *could add value*, if they were based on sound environmental standards and performed by credible outside organizations. More recent research by SustainAbility[15, 16] also verifies that third party statements are no guarantee to credibility.

There are essentially no standards by the SEC for the verification of environmental disclosures in 10K reports. Even with respect to the required disclosure in the three environmentally-related areas identified above (i.e., compliance costs, legal claims, and trends), the SEC has take a relatively low profile. Enforcement has traditionally been quite sparse, although a new memorandum of agreement between

EPA and the SEC may change the picture. As a result, the amount and quality of information reported varies widely from company to company. For example, a survey of mutual funds specializing in socially responsible investments found that their research staffs do not rely on 10K information for environmental information.[17]

The public distrust of EHS information can even extend to disclosures or verifications by the regulatory agencies. In the absence of any standards for performing these attestations, the credibility of an attesting organization can be a factor in determining the perceived trustworthiness of information. But, whom does the public trust?

The public will not rely on any single organization completely. It is a question of degree and other factors such as perceived competency or the organization relative to the issue under consideration. For example, clerical leaders have a high degree of public trust, but they are not recognized as being experts in the technical skills to conduct EHS audits. Research has shown that prestigious universities have among the highest trust levels of any organizations[18]. They also have the technical skills to conduct EHS evaluations. Surprisingly, universities have not been prominent in EHS attestations in the past. For example, in the IRRC research, universities were not even considered in the study since the corporate reports that they evaluated were not audited by university faculty.

University Involvement

Universities are reluctant to become involved in "endorsements" unless there are clearly established ground rules that will ensure that the reputation of the university is not compromised. These constraints are the foundation for the reputations that universities enjoy. The key point is that *universities could become involved,* if they had a significant role in the development of fair and comprehensive standards. There is precedent for this approach. For example, Yale University has been involved in timber certification programs - particularly relevant to this issue because it involves environmental concepts and standards.

Standards developed by a university team would add credibility to any third party statement, regardless of the type of firm conducting the attestation. Universities, if involved in the development of the standards, would also be more likely to participate in the attestation process themselves.

Third party reviews may represent a potential opportunity for universities at several levels:

- The development of standards of practice;
- Teaching opportunities in the identification and resolution of current industry issues;
- The multidisciplinary nature of the problem: environmental, legal, accounting, and business management;
- Synergy with emerging ISO certification issues;
- Opportunities for collaboration with other organizations; and
- Potential for research grants and funded investigations.

Clearly, success is a win for the students, faculty and university. Success would add value and credibility to the corporations that use this approach. But, there are hurdles. The reason that major universities have such high credibility is that the public believes that academics are technically competent and can not be "bought by corporations."

Corporations, on the other hand, want to know that they will be dealt with fairly. They recognize that they provide funding and input, but they will exert little control over the process. The lack of control in the high profile area of stakeholder reporting may make executive management understandably uncomfortable. Corporations are, however, likely to receive fair treatment from university faculty with established technical

credentials and a reputation for objectivity. Additionally, the use of advisory councils, a common practice by university researchers, will also help to broaden and balance the research.

APPROACH

The Concept

There currently are no recognized standards for performing third party audits for the attestations appearing in a growing number of corporate annual environmental reports. In the absence of standards, attestations have little credibility with stakeholders. The problem is compounded because the majority of third party reviews are conducted by consultants, raising the issue of conflict of interest since they may perform other services for these clients. Accounting firms, on the other hand, are traditionally viewed as capable of objective certification of company reports based in part on the preponderance of standards for financial attestations.

The object is to provide corporations with a method to demonstrate to external and internal stakeholders that their disclosures of environmental, health, and safety (EHS) information are comprehensive, accurate, and credible. Success would bring the credibility and accuracy of environmental attestations in line with those currently in place for financial attestations. With generally accepted standards in place, any technically competent organization would be able to provide credible attestations.

This approach utilizes both the multidisciplinary expertise and the credibility that universities uniquely enjoy. What has been missing until recently is a mechanism to identify a network of the best expertise and to establish a collaborative effort.

The Need for Collaboration

The development of standards for third party statements is a significant undertaking. It involves the integration of a number of disciplines and areas of investigation:

- Audit methodology, verification and evaluation
- Metrics
- Ethics
- Risk communication
- Environmental sensitivities (i.e., avoiding the “greenwash factor”)
- Public relations
- Legal considerations (e.g., SEC disclosure requirements)
- Environmental accounting
- Financial and managerial accounting
- Report design, editing, and production

While a single, large university would have expertise in all of the above areas, a collaborative effort among a number of universities has a number of advantages:

- The issue is multifaceted - different institutions have different strengths
- It encourages openness and stakeholder input
- It improves the credibility of the deliverables
- The standards are more likely to be accepted as universal guidelines
- There may be regional or country specific issues
- Professors from a number of universities may choose to provide attestation services

Without a network, it is likely that the research could be fragmented and not as effective or accepted by industry. Additionally, a collaborative effort also strengthens the ability to obtain research grants from the widest variety of contributors. If, for example, the work were only funded by industry, the perception may be created that the sponsors have unduly influenced the outcome, possibly to the detriment of some stakeholders.

The Need for Voluntary Standards

Voluntary standards have distinct advantages over mandatory requirements.[19] If, for example, industry perceives that the object of the research is to develop new mandatory requirements, cooperation from industry would be extremely difficult, if not

impossible, to obtain. Without industry's active involvement, the standards would never reach a stage of refinement to be useful to anyone. The only practical approach is to focus on voluntary standards.

This voluntary approach is conceptually similar to ISO 14000 standards development: corporations are motivated by competitive advantage in international markets. The proposed approach is also similar to that supported by the World Wide Fund for Nature (WWF) in the creation of the Forest Stewardship Council (FSC). The FSC was created to provide a framework for forest certification to eliminate the confusion caused by multiple certifying systems.[20] Additionally, this approach would not deter receiving grants from government agencies. For example, the EPA endorses the concept of voluntary standards to support rulemaking compliance activities and partnership programs with industry.[21]

The need for a Networking Mechanism

A non-profit organization, Center for Environmental Innovation (CEI) supports collaborative research projects among universities. The purpose of this 501 (c)(3) corporation is to encourage innovation in environmental programs through collaborative research efforts with leading educational institutions around the globe. CEI is directed by a Board consisting of faculty from a number of leading universities.

For a current list of universities involved contact the author at (480) 922-1620 or Ann Rappaport, Assistant Professor, Tufts University (617) 627-3211. CEI is currently assembling a multidisciplinary team to conduct research on standards, protocols, and techniques for EHS reporting. The outcome of this project may lead to other research and related activities.

Benefits

- *Greater trust* between stakeholders and corporations
- *Improved communications* to all stakeholders
- More *reliable information* for a corporation's current and potential investors
- *Additional information* of particular interest to socially responsible investors
- *Comparisons* among corporations simplified by more standardization in reporting practices
- Information disclosures through *collaborative* vs. confrontational *approaches*
- *Guidance* on the content of annual environmental reports and other disclosure documents
- *Cost effective* third party audits
- A source of additional *competitive advantage* to corporations with positive track records
- *Opportunities* for allied university programs
- *Improved relations* with regulatory agencies

About the Author

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