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Does Reporting Work? The Effect of Regulation

Impacts of Reporting: Uncovering the ‘Voluntary vs. Mandatory’ Myth

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1 See Zadek, S & Merme, M (2003) Redefining Materiality London, AccountAbility & See also AccountAbility (2003). State of Sustainability Assurance

2 Rubbens, C., Monaghan, P., Bonfiglio, E., & Zadek, S (2002) Impacts of Reporting. CSR Europe and AccountAbility

Data, data everywhere... making reporting work

Each day more and more companies are signing up to the challenge of communicating their social and sustainability impact. But what is the value of reporting to business and their stakeholders alike? And what, if any, role is there for regulation in making otherwise voluntary reporting initiatives more effective?

These questions are matched by the growing costs of reporting, a surge of reporting standards and guidelines, and concern amongst NGOs and governments about its credibility and effectiveness.

AccountAbility's point of departure here is that the traditional 'voluntary vs. mandatory' reporting debate is one that is clouded by ideology. The question of voluntary vs. mandatory can only be answered in the context of the more important question, what makes reporting effective, and to whom? Posed in this way, the regulatory debate is rightly stripped of its ideological overtones, and framed by the challenge of 'what rules help most'.

There are in fact many instances where business has called for government intervention to 'level the playing field'. An emerging litigious

risk over alleged marketing claims in public reports (e.g. Kasky vs. Nike) has led to calls in some quarters for 'safe harbour' for executives from unreasonable legal disputes that threaten the very future of corporate reporting. In the UK for instance there have been efforts to redefine materiality under the reform of company law.¹ And so more pertinently, one needs to understand what is the right balance between *successful* voluntary and mandatory approaches to reporting. It is then crucial to understand why and how different types of rules in various business contexts (i.e. geographical, sectoral, temporal or issue-specific) enhance or diminish the *effectiveness* of reporting impacts.

Thus reporting is not an end goal in itself. It should instead be considered as one of many tools that can potentially enhance corporate accountability. The intended benefits of reporting are, or should be, to better allow a company to: coherently communicate its position as a good corporate citizen on material issues; influence stakeholder decision-making; and inform organisational learning. Yet in exploring the impact of reporting, the first phase of research by AccountAbility and CSR Europe² concluded that little evidence to date exists of social and sustainability

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reporting providing an effective tool in making a real difference to corporate decisions, practices and outcomes.

Drawing on previous research, phase two of the project will use a learning

consortium to stimulate a much-needed debate between practitioners from business, public bodies, and civil society involved in encouraging and enabling effective social and sustainability reporting.

The Impacts of Reporting Programme

In this second phase of work, three specific areas of focus have been determined for groups of reporting organisations, namely: (i) *regulation*, (ii) *stakeholder engagement*, and (iii) *assurance*. Participating companies include: Aracruz (Brazil); Barloworld (South Africa); BASF (Germany); ConcoPhillips (USA); Dow Chemical (USA); MTR Corporation (Hong Kong/China); Westpac Banking Corporation (Australia); and WH Smith (UK).

Building on learning from the six hypotheses from phase one, a set of normative outcomes will be tested simultaneously across each of these three workstreams amongst companies, opinion leaders and other stakeholders via questionnaire, workshop and survey. Additionally, these propositions will also be considered in relation to three cross-cutting factors that shape and inform an organisation's approach to reporting, namely: *internal* (e.g. culture or longevity of reporting); *context* (e.g. sector or geography); and *standards* (e.g. GRI or materiality).

From discussions with the reporting companies the true impacts of public reports will be mapped, with accompanying supporting evidence (e.g. audited documentation, written testimony etc.), of behavioural change and outcomes. An illustrative example is provided below:

Scenario 1: Disclosure of Equal Opportunities Performance: "In compliance with legal obligations the human resources department within a stock listed company produces performance data on employee equal opportunities. Benchmarking against the sector and societal norms shows the firm's impact is better/worse by comparison. The information is then used by the CSR or sustainability unit for incorporation in its annual report.

Subsequently, outreach by the Investor Relations team results in engagement with a mainstream institutional investor around the public report, which following a reputational risk assessment, decides to invest/divest from the company. This market response, with ensuing governmental and media praise/pressure, results in a whole series of internal discussions by the company. Consequently, the human resource unit's budget is maintained/enhanced to strengthen performance and underlying systems."

A key output from this project will be the development of tools to enable companies to systematically measure and manage the effectiveness of their reporting impacts for the benefit of the business and their stakeholders. The project report will be published during 2004.

For more information on how to participate in phase two of Impacts of Reporting please contact philip@accountability.org.uk.

Shifts in rule making

Dating back over the past three decades or more, regulation of disclosure of corporate responsibility is by no means a new phenomenon.

For example, the 1972 U.S. Community Reinvestment Act (CRA) requires banks to address underserved markets on three levels: disclosure (allowing banks and local parties to identify market gaps), rating, and sanctions against worst performers. Under the CRA, banks have committed US\$1 trillion in loan pledges. The efforts of banks are supported by public funds in the form of loan guarantees, tax credits, and funding for CDFIs (community development finance initiatives), which act as partners with the banks. As a result,

investment by national banks in community development has increased 800 percent over the past six years.³

Indeed, regulation is almost inevitable. Government takes interest in any issue of national/regional importance in order to bring order to the market that enables change, fairness and standardisation (e.g. 'widgets' in beer cans). As such, it is a matter of "when" and "how", and not "if", and so companies and their stakeholders need to reconsider adopting a new public policy position in contributing to the debate.

In this instance, it is already happening not just from the reform of

³ *Ibid*

company law or pension acts in the UK and beyond, but disclosure requirements for stock listing, which inform investor decision-making such as in France and South Africa as discussed by Orse's François Fatoux and the JSE Securities Exchange John Burke in their articles. In addition, the WBCSD & AccountAbility⁴ emphasise that hybrids in types of rules are emerging where corporate responsibility frameworks are a mix of voluntary, statutory or mandatory requirements. Also Halina Ward's article concludes that corporate responsibility is shaping law, and that law is shaping corporate responsibility too, such as the Kasky vs. Nike case in terms of litigation on marketing claims. All of the above are conceptualised by Bebbington et al, in their analysis of 'regime theory' as it applies to environmental reporting in the UK.

Role of standards

In determining what role, if any, there is for corporate standards in the regulation of reporting, one needs to understand how the various standards cover different aspects (e.g. human rights or climate change?) and perform different functions (e.g. aspirational code or disclosure framework?). In so doing we are better able to understand the potential impact of such standards

in terms of their added value and complementarity.

This is important when one is drawing on learning for wider social and sustainability reporting from existing environmental reporting practices around the world. For example, in Scandinavia, which has a relatively long history of mandatory environmental disclosure, a review of the literature suggests that the quality and quantity remains weak due to the fact that reporters follow EMAS-style statements, which are prescriptive but narrow as they focus on pollution at the site level. By comparison in Japan, which is in much earlier stages of activity and only now proposing new environmental reporting legislation⁵ uptake has grown exponentially as companies follow ISO14001-style reporting that as an environmental management standard is more holistic than EMAS and acts as an enabler rather than being prescriptive.⁶ Clearly this has important ramifications with regards to co-use of other social or sustainability standards such as the GRI, a prescriptive disclosure framework, and the AA1000S, an enabling accounting, assurance and reporting standard (which is fully compatible with the GRI)

Support by public policy makers for international efforts on global

⁴ *"Towards an Accountability Framework" (New York, 2003), a presentation by the WBCSD & AccountAbility to the WBCSD Accountability and Reporting Working Group.*

⁵ *Emtairab, T., Corporate Environmental Reporting: Review of Policy Action in Europe (2002), IIIIEE Report, Lund University.*

⁶ *Article posted on Next Step Consulting website (www.nextstepconsulting.co.uk). Original source: Scott, P., "Reporting All Over the World" (Dec 2000-Jan 2001), Environmental Finance.*

standards such as the GRI and AA1000S is thus one way to avoid the patchwork of unrelated national regulations forcing multinationals to develop inefficient data-gathering structures for their mandatory national and voluntary corporate environmental reporting.

Enabling environment by government

Regardless of whether government chooses to create mandatory reporting requirements or prefers a voluntary approach, a review of the literature shows that there needs to be a guidance or protection capacity as well as enforcement role.⁷ For instance, in the US this is the case both for environmental (e.g. Toxic Release Inventory for pollution control) and social issues (e.g. EEO-1 surveys for employee equal opportunities), whereby government agencies such as the EPA and EEOC respectively, offer advice to employers on how to collate and manage the data.

There also needs to be recognition that legislation may protect business from ‘unreasonable’ litigious risk of their

‘marketing claims’ (e.g. Nike vs. Kasky, and The British Plastics Federation vs. The Co-operative Bank). At present many US companies are reluctant to go beyond the mandatory minimum on disclosure due to fear of lawsuits. Another paper by the US Environmental Law Institute⁸ discusses the legal considerations in voluntary reporting. US companies are liable under the US Federal Trade Commission Act in terms of substantiation to what assertions imply to consumers. The paper concludes that a combination of technical, financial, and legal knowledge and expertise, are thus now required to determine the appropriate scope and detail for disclosure of information in a formal corporate report.

This conclusion is highlighted by AccountAbility in its work on ‘redefining materiality’ in terms of balancing the building of trust with legal/competitive constraints. AccountAbility’s Simon Zadek and Mira Merme talk about this further in the closing article here.

Conclusion - use and usefulness of data disclosure

Regulation is a question of balance. It is important to move quickly beyond the misleading “voluntary versus statutory” policy debate. Whether voluntary or mandatory depends on what aspect of reporting we are considering. No one

⁷ Monaghan, P (Forthcoming, 2003) *Literature Review, “Impacts of Reporting: Does Reporting Work? – The Impact of Regulation on Corporate Reporting”*, London, AccountAbility.

⁸ Case, D.W., (2000) *“Legal Considerations in Voluntary Corporate Environmental Reporting”*, *The Environmental Law Report, Environmental Law Institute*.

Regulation must be smart, applied where it adds real value to the quality and usefulness of reporting to the company or to its stakeholders.

disputes the need for financial reporting to be regulated, and of course financial performance is a crucial part of sustainability reporting. At the same time, few would argue that how a company describes its strategy should be subject to regulation, yet the need for such coverage in public reporting is increasingly accepted. Regulation must be smart, applied where it adds real value to the quality and usefulness of reporting to the company or to its stakeholders. Sequencing of rule-making is therefore key, because pre-emptive standardisation can be just as damaging as an “anything goes” approach to reporting and assurance.

Yet, it will be no surprise if many reports continue to go unread, when there is public distrust of what the company says and yet the statement remains unassured. Or because the report content is still not relevant to the company’s stakeholders. And is not communicated to them in the most appropriate way. Here the role of appropriate tools and standards such as the GRI and AA1000S is key.

AccountAbility’s Impacts of Reporting programme will address these challenges by helping companies to make reporting work better for the business and their stakeholders.

AccountAbility Quarterly is the journal of AccountAbility. It seeks to provide colour and insight on the challenges to improving social and ethical accountability and performance. We hope it sparks your interest and helps to inform your position.

About AccountAbility

AccountAbility's mission is to promote accountability for sustainable development. As a leading international professional institute, AccountAbility provides effective assurance and accountability management tools and standards through its AA1000 Series, offers professional development and certification, and undertakes leading-edge research and related public policy advocacy. AccountAbility has embraced an innovative, multi-stakeholder governance model, enabling the direct participation of its organisational and individual members who span business, civil society organisations, and the public sector from different countries across the world.

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