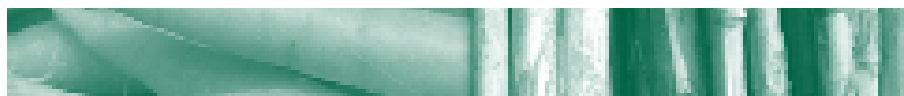


CARROTS AND STICKS FOR STARTERS

Current trends and approaches in Voluntary and
Mandatory Standards for Sustainability Reporting

KPMG's GLOBAL SUSTAINABILITY SERVICES AND UNITED NATIONS ENVIRONMENT PROGRAMME (UNEP)

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Forewords

KPMG is pleased to present this report as a collaborative effort with UNEP, which through a variety of initiatives is one of the leading promoters of sustainability and sustainability reporting.

Sustainability reporting has now become mainstream amongst leading corporations, as confirmed by the KPMG International Survey of Corporate Responsibility Reporting 2005, published in collaboration with the University of Amsterdam. This survey found that more than half of the top 250 companies in the Fortune 500 list issue separate sustainability reports.

With 75% of companies citing economic reasons for producing reports, it is also clear that sustainability reporting is strongly linked to business drivers. It is a key element of sustainability management and a powerful driver of internal change.

Not surprisingly, sustainability reporting has attracted the attention of regulators, and a variety of different regulatory approaches has evolved, mostly voluntary, and some mandatory. The debate on these different approaches will continue to evolve, taking into account regional priorities.

External assurance on reports is an important ingredient in this context. It provides comfort to stakeholders and to management and directors in mitigating potential business risks posed by sustainability issues. Assurance approaches and standards also continue to evolve and move towards global harmonization.

As the G3 version of the Global Reporting Initiative (GRI) framework for sustainability reporting is being launched, we enter a new era in the quality of non-financial reporting. The rate at which leading companies world-wide took up sustainability reporting over the last ten years have been impressive. A majority of the top 100 companies in financial capitals in Europe, Japan, United States and Canada publish sustainability reports today. In growing numbers they explicitly acknowledge the GRI.

The debate on the "ideal" sustainability report and its users continue amongst seasoned reporters. Still, we have some basic, foundational work to do in introducing to thousands of large companies the value of systematically quantifying non-financial performance, using it as a management tool and communicating about it publicly. In developing economies, the challenge remains building capacity. This was clear from discussions when UNEP hosted government officials in a workshop discussion on this theme in 2005.

Do we need more regulation to dramatically increase the numbers of reporters globally and ensure some universal level of consistency, reliability and comparability? While debates on corporate governance and transparency have led to heightened regulatory interest in non-financial disclosure, it is clear that regulation by itself cannot provide all the answers. It needs to be balanced by market measures and voluntary action.

There is both a public and a business case for non-financial disclosure and sustainability reporting in particular. Triple bottom line reporting is not a goal in itself. Its value lies in mobilising better informed managers and employees in cleaning up and improving. Its value also lies in supporting better communication between them and external stakeholders about what markets and society expect.



Sustainability reporting is thus not an isolated activity, but part of the larger challenge of integrating corporate responsibility into business strategy and operations.

We hope that this report will be a guide to companies and governments in their next steps on this unfolding journey in a rapidly globalizing economy.

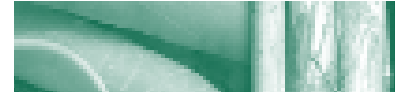
*George Molenkamp, Chairman
KPMG's Global Sustainability Services™*



I thank KPMG for its contribution in this publication, developed in a partnership with UNEP. It presents a valuable overview for both public officials and corporate citizens of the market place.

*Achim Steiner, UN Under Secretary
General and Executive Director,
United Nations Environment Programme*

1. Executive Summary



This report provides an overview and analysis of current trends and approaches in mandatory and voluntary standards for sustainability reporting.

It summarises arguments in favour of both voluntary and mandatory approaches, and suggests key considerations for public and private sector decision-makers in addressing different regulatory approaches and possible policy mixes. It also provides a listing of reporting and related standards in mainly OECD countries, including the European Union (EU), as well as the emerging market economies of Brazil, India and South Africa. The report does not provide legal advice or legislative recommendations. Rather, the intention is to inform further discussion and decision-making at a time when the future direction of sustainability reporting and its private / public use remains a lively debate. Ultimately, decision-makers in government and private organisations will have to make decisions based on their specific contexts and input from local stakeholder groups.

In brief, the report presents the following:

- A summary of arguments in favour of voluntary and mandatory standards. Some of the main arguments in favour of voluntary standards are that sustainability reporting is young and evolving and will therefore require time to mature. Mandatory standards will stifle innovation and not ensure moral buy-in. In addition, public regulators are often not acquainted with company or industry issues or might avoid difficult issues for political reasons. Some of the main arguments in favour of mandatory standards are that not enough companies are taking up voluntary approaches, that the use of regulated guidelines and codes can add to the credibility of reports and help ensure a minimum level of disclosure. It is also argued that voluntary reports tend not to disclose negative information, and that mandatory reporting will ensure the development of a central and comparable source of data for use by investors and other stakeholders;
- A summary of mandatory and voluntary reporting and related corporate social responsibility (CSR) standards from the selected countries, as well as a selection of global and national assurance standards (whilst some key assurance standards are listed, they fall outside the scope of this report);
- An overview of selected initiatives, standards and experiences in the following OECD countries / regions and emerging market economies: Brazil, Denmark, European Union, India, Japan, South Africa and the United States of America;
- Suggestions on key considerations for public and private sector decision-makers in addressing different regulatory approaches and possible policy mixes as they explore how reporting initiatives can be initiated or expanded. It is suggested that governmental decisions should be informed by, amongst others, the following:
 - A familiarity with sustainability reporting, including the main drivers for reporting as well as the current consensus on what would constitute best practice;
 - An understanding of the main global standards that are currently driving reporting processes. The GRI has clearly established itself as the main reference in terms of providing a reporting framework, and is supported by other complementary standards such as AA1000. A new ISO 26000 standard on Social Responsibility, currently under development, may also recommend communication in the form of sustainability reporting.
 - A realisation that reporting is only the tip of the iceberg and that – for both reporter and legislator – the emphasis should be on performance; and

- The knowledge that the voluntary versus mandatory debate does not imply an “either / or” position, but rather finding a balance between regulation in certain high risk or high impact areas, and allowing industry associations or individual companies to make decisions in other areas.
- Detailed review of quantity and quality of sustainability reporting in the specific country, as well as helping to ensure that relevant government departments remain up to date with the latest developments in the field of sustainability reporting;
- Consideration of draft legislation: governments that contemplate introducing some form of legal requirement for sustainability reporting have many options available, including the following:
 - Stipulating a basic minimum requirement of sustainability reporting and making such reporting compulsory through a “comply or explain” arrangement;
 - Delegating the responsibility to make decisions in this regard to stock exchanges and / or industry associations; or
 - Introducing incentives for corporations to issue sustainability reports.

It is suggested that the following actions could be considered by public officials:

- Detailed review of existing legislation and other regulatory requirements with reference to the following:
 - Comparison with GRI sustainability reporting requirements (principles, disclosure items and sustainability indicators, stakeholder engagement and due process);
 - Distinction between duty to disclose information to government and public disclosure;
 - Evaluation whether existing company law encourages only conventional, historical cost accounting or also encourages forward-looking, strategic reporting on business prospects (trends, factors affecting future performance), business drivers and risks; and
 - Current practice with regards to external auditing / verification / assurance.

Suggested prerequisites for balanced regulation highlight the importance of a publicly recognised set of performance indicators (of which the Global Reporting Initiative provides a global reference framework), independent verification, stakeholder engagement, the role of government in enforcing a level playing field and the importance of incentives. The conclusions also highlight the importance of international cooperation and collective action, avoiding a proliferation and fragmentation of national level guidelines.

How strange a thing

How strange a thing this Art of Writing did seem at its first Invention, we may guess by the late discovered Americans, who were amazed to see Men converse with Books, and could scarce make themselves to believe that a Paper could speak...There is a pretty Relation to this Purpose, concerning an Indian Slave; who being sent by his Master with a Basket of Figs and a Letter, did by the Way eat up a great Part of his Carriage, conveying the Remainder unto the Person to whom he was directed; who when he read the Letter, and not finding the Quantity of Figs answerable to what was spoken of, he accuses the Slave of eating them, telling him what the Letter said against him. But the Indian (notwithstanding this Proof) did confidently abjure the Fact, cursing the Paper, as being a false and lying Witness. After this, being sent again with the like carriage, and a Letter expressing the just Number of Figs, that were to be delivered, he did again, according to his former Practice, devour a great Part of them by the Way; but before meddled with any, (to prevent all following Accusations) he first took the Letter, and hid that under a great Stone, assuring himself, that if it did not see him eating the Figs, it could never tell of him; but being now more strongly accused than before, he confesses the Fault, admiring the Divinity of the Paper, and for the future does promise his best Fidelity in every employment.

From The Secret and Swift Messenger (1641) by John Wilkins, quoted in Eco (1990:1)

2. Introduction



Whilst people would agree today that a written letter cannot, by itself, count figs and give an account of the exact number (see excerpt on previous page), many people would probably be of the opinion that some pieces of writing could reflect reality accurately and objectively.

Sustainability reporting is one example of such writing that is intended to provide an objective account of the economic, social and environmental performance of an organization. This report supports the view that – ultimately – such an objective account is impossible. Sustainability reports – whether based on voluntary or mandatory standards, externally verified or not, issued to fulfil the letter or the spirit of a legal or corporate governance requirement – can never provide an unadulterated, “pure” version of an organisation's performance. It will always be informed by a particular context, existing organisational positions, policies and perceptions, and will again be read by readers with different agendas who will quite often arrive at conflicting interpretations of the same “factual information”. At the same time, the position that classifies all sustainability reports as “greenwash” and therefore, as fundamentally flawed, subjective, manipulative and untrustworthy, is opposed.

Reporting debates in the United States (USA) and in Europe in the 1960s and 1970s were ignited by a new awareness of external responsibilities unfulfilled by governmental institutions and ones that business needed to account for. Early experiments with social reporting – Sozialbilanz or bilan social (a legal requirement in France since 1977 and practiced in the Netherlands since the 1960s) – paved the way for the introduction of the environmental report or Ökobilanz in

countries such as Germany, Austria, Denmark and Switzerland (Hibbitt, 2004). During the 1980s ethical investment funds in the UK and USA started screening companies based on their social and ethical performance. Following the 1989 Exxon Valdez disaster, the US-based Coalition for Environmentally Responsible Economies (CERES) developed The CERES / Valdez Principles on behalf of the Social Investment Forum. These principles introduced a tough set of environmental reporting guidelines. The 1990s saw increased reporting with more comprehensive coverage. This was epitomized for example by the Body Shop International's first Values Report (1995), in which it reported on environmental, animal protection and social issues. In 1997, CERES and UNEP launched the Global Reporting Initiative (GRI) process to develop guidelines for reporting on the triple bottom line: economic, environmental and social performance. The aim was to elevate sustainability reporting to the same level and rigor as annual financial reporting. As a multistakeholder global process, the GRI has been described by some as an example of a “global public policy network” or a form of “civil regulation”; a concept preferred to the concept of “voluntarism”, which stands accused of encouraging an unhelpful “either/or” opposition between “voluntary” and “mandatory” approaches (Sabapathy, 2005: 248).

Surveys in the Anglo-Saxon world of reporting trends in the 1990s showed

that up to that time most companies focused on disclosure of human resource issues. Human resource reporting was much more predominant than environmental reporting, since much disclosure in this terrain was mandatory rather than voluntary (Hibbitt, 2004: 79). Environmental reporting increased due to more governments focusing on heavy polluting industries and introducing compulsory registration of materials (a form of green accounting) and inventory of toxic releases. Also, the development of new environmental management standards such as the European Eco-Management and Audit Scheme (EMAS) encouraged reporting.

Developments in reporting ranged from legalistic and technical requirements under company law and accounting rules to managerial innovations and new demands by stakeholders, all of which resulted in the birth of the concept of the comprehensive “corporate sustainability report” in the 1990s. It was a decade that was described by the London-based think tank SustainAbility as the “Transparency Decade”; when a series of major incidents forced early pioneers to “come clean” and issue economic-social-environmental reports (SustainAbility and UNEP, 2002: 6).

SustainAbility has suggested that the first decade of the 21st century might become the “Trust Decade”. This decade was to be based on ever-increasing transparency, accountability and reporting. The most important

changes that have been identified over recent years are the growth in the number of reporting companies, the shift from environmental to integrated sustainability reporting and the rapid increase in the volume of information (both printed and online). However, with an estimated total of more than 50,000 multinational corporations in the world, even 2,000 reporting companies still constitute a small percentage. While the growth rate in numbers of reporters has slowed recently, early uptake in sustainability reporting has been impressive – in particular considering the companies producing them. The database of CorporateRegister.com suggests that the number of corporate non-financial reports has grown from less than 50 in 1992 to 1906 in 2005. Early growth has been strongest in the USA, UK and Japan. Impressive growth has been seen in France more recently, related to the introduction of mandatory reporting legislation.

Today the debate on the future of sustainability reporting is to a large extent a debate on who the target audience or key user groups are. Challenges identified by SustainAbility and UNEP relate to the following issues: the need to link sustainability issues with brand and corporate identity, the continuing disinterest of most financial institutions and the so-called “carpet-bombing” syndrome of bombarding readers with more information, rather than more insight (SustainAbility and UNEP, 2002: 6). The 2004 edition of the biennial Global Reporters Survey of Corporate Sustainability Reporting by SustainAbility and UNEP does mention that there is more interest from the financial community and that corporate governance has been put more firmly on the agenda. At the same time it raises concerns about the ability of

reporters to identify material and strategic risks, as well as the ability to link financial and non-financial aspects of corporate reporting (SustainAbility, UNEP and Standard & Poor's, 2004).

Debates on target audience and purpose have also sharpened consideration of the value of reporting not only as an accountability mechanism but also as a management tool for which there is a business case to be made. The benefits of sustainability reporting from a company point of view include improved financial performance (there is a growing body of empirical evidence that indicates a positive link between social and financial performance), enhanced stakeholder relationships, improved risk management because of an increased understanding of non-financial risks, as well as improved investor relations (institutional investors are increasingly focusing on non-financial performance when they make investment decisions, and there is a global increase in ethical investment funds). For regulators, the expected value in sustainability reporting lies in the contribution by better performing companies to sustainable development goals and the value of transparent communication of performance information, good and bad, in a standard format to enable monitoring and benchmarking progress.

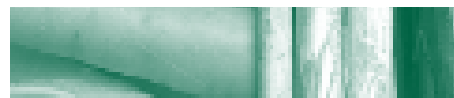
The next section provides a summary of arguments in favour of both voluntary and mandatory standards for sustainability reporting. The subsequent chapter provides an overview of reporting standards in 19 selected countries and the European Union, and a few case studies based on a closer examination of standards in selected countries. Finally, the conclusion presents suggestions for public and private organisation

decision-makers and consideration on how governmental reporting initiatives could be expanded. The report does not provide legal advice or legislative recommendations. Rather, the intention is to inform further discussion and decision-making at a time when the future direction of sustainability reporting and its private / public use remains a lively debate. Ultimately, decision-makers in government and private organisations will have to make decisions based on their specific contexts and input from local stakeholder groups.

To conclude this introductory section, it is important to highlight the differences between *performance* and *reporting*. Even if based on advanced sustainable development management and information systems, a sustainability report is always a secondary account of the actual performance of an organisation. Within the context of this report, the role of government can be twofold:

- To legislate in terms of sustainability performance with some requirements for disclosure; and
- To legislate in terms of reporting – such reporting can be specific, e.g. to report on specific indicators linked to an individual piece of legislation, or can be broad-based, referring to the need for a general account of sustainability performance.

It is difficult to divorce these two components from each other, and all references to mandatory standards in this report should be viewed in this context. However, it should be noted that it is possible to have legislation relating specifically to reporting practices, rather than to performance per se.



3. Voluntary and mandatory reporting standards

Mindful that the “mandatory versus voluntary” opposition is criticised by many as an unhelpful ‘either/or’ assumption, and that ideal solutions lie in some policy mix of the two, our following analysis sets out the pro’s and con’s of both in order to provide a clear point of departure. This is why we speak of “carrots and sticks for starters”. The sustainability reporting regulation debate is still young, the main course still has to be prepared.

Our research for this report revealed more than a 100 reporting requirements and standards in the selected – mainly OECD – countries that address one or more components of a sustainability agenda. Of these, approximately half can be classified as mandatory standards. However, these requirements remain largely fragmented and in most cases do not fit an integrated strategy to regulate sustainability reporting. Quite often laws were promulgated without any reference to sustainability reporting, yet – after the fact – such laws can be classified as a “legal requirement” for sustainability reporting because of the nature of the issue addressed.

Various approaches can be undertaken to encourage sustainability reporting.

On the one hand the legislator can be passive and leave it to market forces or supranational bodies to drive organisations to report on sustainability issues or they may support various non-governmental initiatives in their attempts to promote reporting. On the other hand the legislator can choose to introduce one or more of the following:

- Mandatory regulations with an obligation to report;
- Incentives for companies to report;
- Voluntary rules or guidelines relating to performance; or
- Transfer the regulatory power to self regulating authorities like the NYSE or a stakeholder panel whose statutes can either be voluntary or mandatory.

A number of stakeholders have called for sustainability reporting to be a mandatory requirement aimed at increasing corporate accountability, the argument being that most companies will generally not report of their own accord or, when they do, such reporting will be incomplete and rarely material to stakeholder interests (Doane, 2002).

Probably the most comprehensive example of a mandatory approach is France’s Nouvelles Régulations Economiques (NRE, operative since 2003), which require all companies quoted on the stock exchange to issue

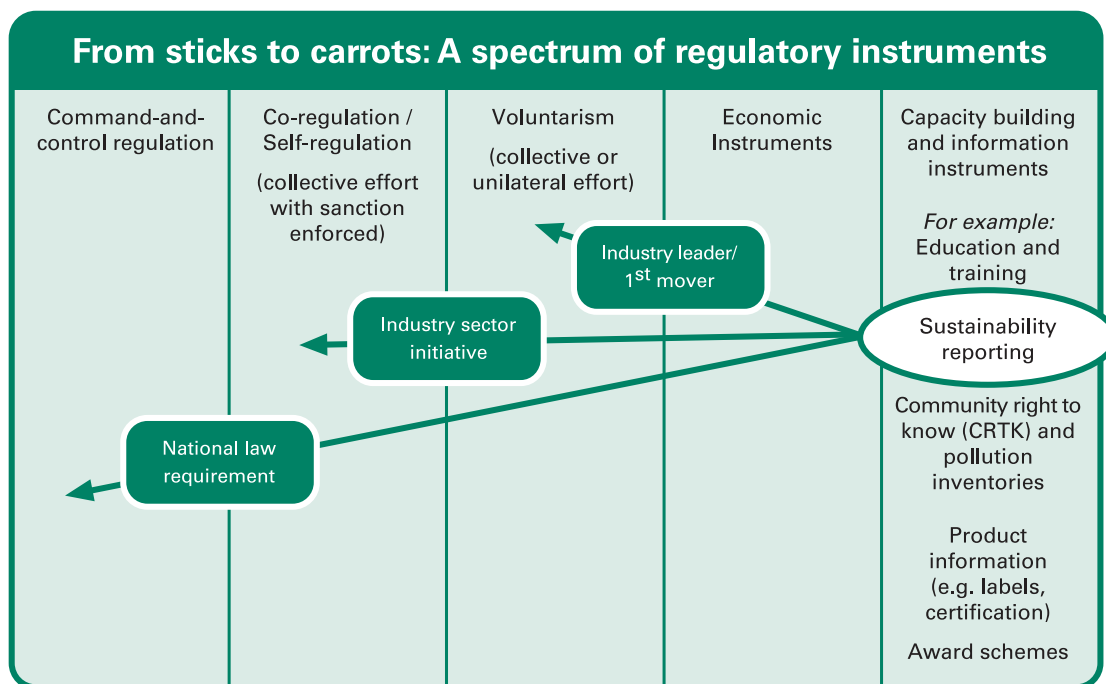
social and environmental information with their annual reports. Yet the effect of such legislation on the quality of reporting and its ability to influence performance is thus far uncertain. An examination by the Paris-based consulting firm Utopies found that most small caps and 20 companies on the SBF 120 Index (the 120 most actively traded stocks listed in Paris), ignored the requirements altogether, that two thirds of the companies on the SBF 120 Index reported on less than 40% of the required indicators, and that only 10 blue chip companies tried to comply with the spirit of the law (Utopies, Sustainability & UNEP, 2003 and 2005).

With reference to mandatory environmental disclosure in the USA and Canada it has been suggested that “because of materiality levels, very little detail is provided on the environmental issues governed by accounting standards. Also, accounting standards relating to environmental matters are so narrowly focused that assurance about conforming to them is not very meaningful” (Buhr, 2003). Elsewhere, environmental management standards seem to drive reporting. Mandatory disclosure on environmental issues through local or site-level reporting has been introduced with environmental legislation during the mid-1990s in the Netherlands, Sweden, Denmark and Belgium.

To further explore the debate about mandatory and voluntary regulation it is important to define what regulation means. Regulation is often narrowly defined as that which is enshrined in law. Yet from a legal perspective,

regulation should be seen as a continuum ranging from traditional command and control type regulation to industry codes of conduct or agreements and non-enforceable contracts with regulators (Bebbington

et al, 2003). They can be listed along a spectrum of "regulatory instruments", following Gunningham and Grabosky (1998) as in the table below which indicates the position of sustainability reporting within the broader context:



The assumptions behind command and control regulation are that it can be clearly defined, breaches rarely arise and can be easily uncovered when they do arise. Furthermore, the imposition of a sanction must provide a deterrent to non-compliance. If one or more of these assumptions do not hold, the regulation will begin to fail. To make the regulation work it is critical that the necessary control, inspection and prosecution processes are in place. In order to avoid these costs regulators try to find other ways to regulate through tools like voluntary

agreements, incentives and "comply or explain" regulations (Bebbington et al, 2003).

The debate between proponents of voluntary and mandatory reporting standards is a complex one. Vested interests and perceptions often lead to conflicting positions. Corporations usually argue strongly in favour of voluntary standards. NGO's, pressure groups and trade unions often demand mandatory standards, since they do not believe that corporations will disclose material information

objectively unless they are required to do so by law. Pertinent here is the lack of trust that the public and different stakeholders have in large organisations. Also relevant are questions concerning the responsibility of the director towards either shareholders or a broader range of stakeholders.

In the remainder of this chapter various arguments in favour of both positions are discussed briefly.

3.1 Voluntary standards and self-regulation

Many corporations support the GRI process – voluntary but with an intergovernmental endorsement - and its main output, the GRI Sustainability Reporting Guidelines. The business lobby and companies in general argue against a legal duty to report against certain standards, stating that it is crucial that there remain different standards – already in existence – by which social and environmental reporting can be measured. In practice this multitude of standards enables businesses to consider the applicability of any particular standard and choose to follow the most suitable practice. Accordingly, they argue there is no need to consolidate or introduce another standard.¹ Furthermore, it has been argued that uniform procedures would affect the substance found in reports. Standardisation, either directly through regulation or indirectly through certification procedures, might stunt creativity and level activities to an average, as well as entailing high bureaucratic costs.

It is further argued that mandatory external verification does not necessarily increase the credibility of reporting. Third parties can verify formal aspects such as figures and procedural conformity, but accountability for the “real” performance rests with the company and its own credibility. The option to consult a third party for advice or auditing should perhaps be left to the discretion of companies.

Many companies acknowledge that guidelines are evolving, yet claim that sustainability reporting is a relatively new area and will take considerable time and effort if it is ever to be considered as valuable and credible as financial reporting. The notion of it being mandatory is opposed on the basis that this would obstruct much of the good work currently in progress: businesses should be allowed to develop guidelines, work out how to interpret sustainability information and elevate it to the same level as financial reporting. It is argued that only when this has been achieved will such reports require independent verification, since accountants and auditors need to be familiar with the criteria used to compile them.

A further argument against mandatory or standardised reporting is that the investment world does not necessarily demand standalone, standardised reports. Mainstream investors, socially responsible investment (SRI) funds, analysts and main stakeholder groups have their own questionnaires, criteria and needs for additional specific information. Even with common reporting protocols they argue that investors are likely to request additional information.²

Voluntary – including negotiated – action is one of the fundamental principles of CSR. Voluntary measures and initiatives give businesses the opportunity to develop appropriate company- or sector-specific approaches and models of social

responsibility. Approaches that are developed inside companies and sectors are better accepted than requirements imposed from outside. This realisation is reflected in existing initiatives – for instance on social codes of conduct, at the level of the International Labour Organisation (ILO) and the United Nations – which are all based on the principle of voluntary implementation of responsibility together with economic success.³ As the largest global corporate citizenship initiative in the world, the UN Global Compact requires participating companies to produce an annual “Communication on Progress”, encouraging use of the GRI sustainability indicators when reporting on their activities. This requirement is both an integrity measure and tool for promoting learning, while joining the initiative in the first place is a voluntary decision (Van der Lugt, 2005).

Closely linked to the concept of voluntary standards is that of self-regulation. The remainder of this subsection summarises the advantages and disadvantages of self-regulation.

¹ For example, see the response of GlaxoSmithKline to the Green Paper of the EU. For an overview of all responses made to the EU Green Paper visit http://europa.eu.int/comm/employment_social/social/csr/csr_responses.htm which has more than 200 opinions from individuals, NGO's governments business initiatives, churches and companies.

² One of the problems that rating organisations, investors and NGOs face is that information required for benchmarking is often not presented in a form that analysts can readily use. As there is no standard sustainability report format or content, questionnaires are invariably issued to obtain the required data, and these are not generally well received. Questionnaires are often dismissed because they are time consuming and received too frequently. BT for example has noted an explosion in the number of questionnaires received over the last three or four years and estimates that it is currently spending around £25,000 annually completing questionnaires on CSR. In April 2004, the London Stock Exchange announced that it is collaborating with UKSIF to reduce the growing burden of surveys and questionnaires from rating organisations. As a result there is a growing demand for a more efficient channel of communication with which to standardise reporting and establish issues of material interest to stakeholders, ideally in the form of a single, uniform questionnaire. For more information, visit <http://www.londonstockexchange.com/eng/products/irs/cre/>. In the USA, a possible solution to the problem of survey fatigue has been found by SRI World Group Inc, in the form of OneReport, a global electronic reporting network through which companies make their social, environmental, economic and corporate governance information available to all interested parties. Participants already number 22 Fortune 100 companies, including DuPont and Shell (ICAEW 2004: 52).

³ This is the opinion of the Economic and Social Committee on the EU Green Paper: Promoting a European framework for Corporate Social Responsibility.

In addition to the question of how or whether to regulate sustainability reporting, it should be asked who should regulate and at what level:

- Governmental regulation or self-regulatory authorities?
- At the international level, or at national level?

Issues to be addressed include how self-regulation should be applied, the conditions under which self-regulation is appropriate, and if appropriate, how self-regulation should be structured to maximize its advantages and minimize its disadvantages.⁴

3.1.1 Advantages of self-regulation

Listed below are a number of potential advantages that self-regulation offer in the realm of corporate regulation. Although these refer to the broad area of regulation, within the context of this report they should be applied to the specific debate about sustainability reporting.

Proximity

Self-regulatory organisations are generally rooted in the industry being regulated, enabling access to more detailed and current industry information which can be especially helpful in rapidly changing sectors. By comparison, government regulators are often playing “catch up.” Being closer to the action, self-regulators are better situated to identify potential problems.

Flexibility

Self-regulatory organisations can act with greater flexibility than government regulators: they are not subject to the same procedural and due process hurdles or political constraints as government. Governmental regulators are often not inclined to deal with politically unpopular or highly complex issues, so these issues may be more suitably delegated to self-regulatory bodies.

Compliance

Self-regulation may generate a higher level of compliance. The greater the involvement of industry in setting the rules, the more reasonable the rules are likely to appear to individual firms. Self-regulation may also generate rules that solve regulatory problems in a fashion that is more sensitive to industry practices and constraints, and hence it may be easier for firms to comply with them.

Collective Interests of Industry

Self-regulation can harness the collective interests of the industry. This may be another way that self-regulation promotes compliance, as competitors can effectively “police” each other.

3.1.2 Disadvantages of self-regulation

Although self-regulation has important advantages, there are a number of identified drawbacks:

Conflicts of Interest

The same proximity that can help the self-regulator acquire useful information can be a disadvantage

because of conflicts of interest.

Knowing an industry better does not mean that a self-regulator will necessarily have the proper incentives to regulate it more effectively.

Inadequate Sanctions

The greater flexibility afforded to self-regulatory organisations also means they may have the discretion to administer only modest sanctions against serious violators.

Under-enforcement

Conflicts of interest and flexibility may also make it more likely that compliance will be insufficiently monitored. If industry interests are in conflict with societal interests, enforcement by self-regulators might be less than optimal overall.

Global Competition

In a global marketplace, an industry's collective interest may be defined by competition with foreign markets. If foreign markets are not equally burdened with regulation, then aggressive self-regulation could disadvantage domestic firms. This provides yet another reason to question whether self-regulators will make decisions that will benefit society.

Insufficient Resources

Although the funding of self-regulatory bodies may not be susceptible to the whims of legislatures, underlying conflicts of interest could leave self-regulatory bodies with less than sufficient funding.

⁴ The following section draws mainly on conference proceedings from “The Role of Government in Corporate Governance,” held by the Centre for Business and Government, John F. Kennedy School of Government, Harvard University in 2004.

3.2 Mandatory standards

The most vocal call for mandatory action on corporate sustainability issues comes from the NGO community. In an official response to the final report of the 2004 EU Multi-Stakeholder Forum, some of the leading and most influential NGOs stated their opinion on what public policies they would expect in Europe (<http://www.foeeurope.org>):

"Our common goal is to improve business practices to increase positive impacts and reduce negative impacts on society and the environment. Voluntary initiatives are not enough to reverse the unsustainable impacts of corporate activities or to meet the standards set by existing agreements such as the ILO declaration, OECD guidelines, the Millennium Development Goals and human rights treaties ... Ensuring corporations are legally accountable to their stakeholders is essential. Only binding legal measures will establish a general incentive for responsible corporate behaviour that matches their general incentive to be profitable. This requires rights for stakeholders to hold companies to account for their impacts and duties on companies and their directors. It also needs effective monitoring and verification of business performance. Furthermore, only those approaches to responsible behaviour elaborated in concert with all stakeholders will bring sustainable results."

With regards to reporting it is stated:

"Accountability requires high and consistent levels of transparency about business activities and products which cannot be achieved by voluntarism only. Stakeholders need meaningful disaggregated information about the impacts of companies and products on human rights, society and the environment. This implies mandatory social and environmental reporting, disclosure of payments and lobbying to public authorities, and provision of comprehensive point of sale information about products and services. Reports must be based on common reporting standards for all companies and there must be public access to information on company and product CSR performance."⁵

3.2.1 Advantages of mandatory reporting

The following outlines the most common arguments in favour of mandatory reporting.

Credibility

The use of recognised practices and tools, or the publication of a sustainability report or equivalent that has been prepared using recognised guidelines should enhance the credibility of information provided in response to stakeholder concerns and interests.

⁵ From "NGOs call on Commission and Council to shift gears after Multi-Stakeholder Forum: European CSR process must move from dialogue to action", 2004 (<http://www.foeeurope.org>).

Changing the corporate culture

Mandatory requirements foster openness and transparency with respect to sustainability issues previously lacking in corporate culture. Mandatory requirements would place CSR issues, and social and environmental issues in particular, squarely on the agenda of corporations.

Incompleteness of voluntary reports

Voluntary reports often fail to address certain issues, notably on fundamental human rights issues and key aspects of a company's environmental performance.

Comparability

There is no standardisation of the information found in reports because of the varying choices and approaches of different companies. It is often argued that the voluntary nature, progressive character and number of standards envisioned in initiatives such as the GRI and other national and international initiatives, are unlikely to result in the standardisation of sustainability reporting practices.

Non-disclosure of negative performance:

Positive information and messages tend to be emphasised in most sustainability reports. The reports are also time and event specific. Firms may disclose information when it suits their interests, but not when it may negatively influence perceptions, or relate to future earnings and potential cash flows negatively (Walden and Schwartz, 1997).

Legal certainty

In addition to NGOs and individuals calling for mandatory reporting requirements, business has often 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 – see box) has led to calls in some quarters for a "safe harbour" for

executives from unreasonable legal disputes that threaten the very future of corporate reporting. In the UK there have been efforts to redefine materiality under the reform of company law. In the end the Operating and Financial Review (see next section for a discussion) replaced the concept 'materiality' with the need to report on non-financial issues 'to the extent necessary'.

The Nike v Kasky case

The case filed against Nike by Marc Kasky, a Californian activist, over claims that statements the company made in letters to newspapers and press releases relating to work conditions in some of its suppliers' factories were 'misleading advertising', raised considerable interest and concern around the potential legal precedent that could be set. It was to be determined whether company statements on human rights and other public policy issues – in reports, labels or other forms of communication – should be considered 'free speech' and thus protected under freedom of speech guarantees, or 'commercial speech', thus not falling under the US First Amendment and subject to regulations on false advertising. Lower courts sided with Nike but the California Supreme Court overruled them in May 2002. The California Court ruled that any communications with an audience that might include Nike product purchasers was 'commercial speech', including statements of important public policy positions. Nike appealed to the US Supreme Court which refused to rule on this point, and Nike agreed to settle the lawsuit and pay US\$1.5 million to the Fair Labour Association – an independent coalition that seeks to improve factory conditions and monitoring. In response, Kasky has agreed to withdraw the suit. It is argued that the Nike case could deter companies from reporting, for fear of being sued, or that it might undermine the ability to insist on accurate reporting. It is also argued that the case could rapidly accelerate the take-up of agreed standards on reporting. The case settlement has left the legal merits of both sides untested. Nike has advocated the need to level the playing field through the implementation of standards and universally applied processes for accountability and reporting. It is interesting to note that Domini Social Investments submitted an Amicus brief to the Supreme Court in support of Kasky, arguing that social disclosure should be subject to the same legal requirements as financial disclosure (www.domini.com/common/pdf/Amicus-Brief-4-03.pdf).

(Source: ABC of the main instruments of Corporate Social Responsibility, Industrial relations and industrial change European Commission, Directorate-General for Employment and Social Affairs, 2004 Employment social affairs)

Market failures – theory of regulation

The argument for CSR is that socially responsible corporate behaviour leads to superior returns for the company and social welfare for all in the long term. If this is true the reporting and disclosure of material sustainability issues is relevant for investors. It could therefore be assumed that market forces will drive companies to report on their sustainability performance. A rule of law requiring sustainability reporting or at least the public disclosure of information on CSR issues would thus only be advisable where the market for the information to be disclosed is characterized by market failures (Baums, 2004). In this case, an appropriate state intervention in the market process could lead to an increase in social welfare. Market failures can arise because of externalities, asymmetric information, the dominant position of a market participant, or the production of “public goods”.

If there is asymmetric information concerning the status of a company or a market, an investor will only be willing to make an investment if he is adequately paid for bearing the remaining risk. It could therefore be assumed that companies will report and disclose information in the interests of maximizing profits and returns. Adequate, voluntary disclosure resulting from market forces seems, at least in the short to medium term, unlikely, given the often conflicting interests of management. The pressure from shareholders, creditors and financial institutions to disclose information on sustainability issues is unlikely to be anything like the pressure there is to disclose financial information, and is therefore unlikely to encourage the emergence of sufficient voluntary reporting.

Reduction of non diversifiable market risk – free rider problem

Sufficient disclosure by all companies is even more important in a market characterized by diversified investors (Macey, 2002), as the general market risk cannot be reduced by diversification and therefore diversification does not eliminate the need to disclose company data. Therefore, if all companies seeking capital on a market refrained from disclosing relevant investment information on a regular basis, the investors would either refuse to invest in the market or demand a high-risk premium. As a result at least some companies – even without regulatory disclosure requirements – would disclose the relevant information. Other companies, in contrast, would attempt to hide risks and get a “free ride” on the risk reduction provided by the reporting companies (free rider problem). All companies would be punished with a corresponding risk premium, which they would have to pay instead of increased disclosure costs. Yet the “dishonest” companies would benefit from the reputation of the “honest” companies up to a certain point; hence the market will attribute equal risks to both (Baums 2004).

Cost savings

It is advisable to gather public information at a central source for distribution to investors. In the absence of mandatory disclosure, investors might engage in duplicative and inefficient searches for information about public companies.

However, as the OneReport initiative has demonstrated, this could potentially also be achieved through self-initiative.

Standardisation

The economic literature names another advantage of required disclosure that only arises if the legislator promulgates mandatory rules: the advantage of standardization. (Adams, 2002). This relates to dependability, often cited as one of the advantages of command-and-control regulation, namely the ability to specify expected behaviour. An investor must compare a number of investment alternatives before deciding on an investment. It is to the investor's advantage if the information relevant for the investment decision is presented in a standardised format that can be readily compared. Standardised formatting saves investors, communities, consumers and employees' time and money, and explains why listing prospectuses or annual reports should follow identical guidelines (Baums, 2004).

Equal treatment of Investors

Another argument in favour of mandatory sustainability reporting is the equal treatment of investors. Legally required corporate disclosure encourages equal treatment of investors with regard to the information disseminated pursuant to law. If certain groups of persons are privileged in the disclosure of information, other groups will be prejudiced. The equal distribution of information to investors has also been supported and demanded by several corporate codes.

The German Corporate Governance Code (GCGC) provides that:

"The company's treatment of all shareholders in respect of information shall be equal. All new facts made known to financial analysts and similar addressees shall also be disclosed to the shareholders by the company without delay."

(GCGC, supra note 32, at no. 6.3).

As has been mentioned before, care should be taken not to reduce a government's ability to intervene as a choice only between support for mandatory standards or voluntary standards. Governments can play an important role in terms of creating an enabling environment for companies to report. Governments can encourage reporting through participation in debates about reporting, issuing country specific reporting guidelines and conducting national peer reviews.

3.2.2 Disadvantages of mandatory reporting

Arguments against mandatory regulation and a mandatory approach to sustainability reporting often cite the following shortcomings that the approach is likely to show (based on Gunningham and Grabosky, 1998: 44 – 47):

Knowledge gap between regulators and industry

The mandatory approach requires regulators to have comprehensive and accurate knowledge of the workings and capacity of the industry.

Once size does not fit all

The mandatory approach will undermine tailored responses to stakeholder demands, seeking to force industries of very different natures, sizes, capacities and local contexts into the same box.

Inflexibility in the face of change and complexity

The mandatory approach fails to keep track with rapidly changing circumstances and changing technologies, and in this relatively early stage of sustainability reporting – a complex and changing subject – the introduction of mandatory legislation is premature.

Lack of incentive for innovation

The mandatory approach will undermine innovation and take away the incentive to go beyond compliance, forcing a re-active, tick-box approach that would result only in more bureaucracy and filing of documentation.

Constraints on efficiency and competitiveness

The mandatory approach runs the risk of adding costs whilst undermining efficiency and competitiveness, introducing different national level requirements and indicators that will place a tremendous burden on companies that operate in an increasingly global business environment.

4. Overview of selected standards



This section summarises key reporting guidelines, initiatives and regulations with reporting requirements, relevant corporate social responsibility standards, as well as voluntary and mandatory assurance standards.

4.1 Voluntary standards

The tables are based on desk research and do not represent a comprehensive list. Not all of them refer to integrated, comprehensive sustainability reporting. In the case of mandatory standards, many are linked to a single issue with limited disclosure requirements.

Country/Region	Standards, Codes and Guidelines
International	<ul style="list-style-type: none"> <li data-bbox="831 779 1465 1339">■ The Global Reporting Initiative (GRI) provides the most recognized global standard with its framework for sustainability reporting. The GRI describes itself as a multi-stakeholder process and independent institution with the mission to develop and disseminate globally applicable Sustainability Reporting Guidelines. Its Guidelines are for voluntary use by organizations for reporting on the economic, environmental, and social dimensions of their activities, products, and services based on reporting principles. The third revised or G3 version of the Guidelines is complemented by sector specific supplements that provide, among others, sustainability indicators specific to the needs of sectors such as tourism, finance, telecommunications, mining, logistics, apparel and the public service. The GRI Secretariat, based in Amsterdam, is a UNEP Collaborating Centre. www.globalreporting.org <li data-bbox="831 1384 1465 1644">■ The AA1000 guidelines from AccountAbility provides guidance on how to establish a systematic stakeholder engagement process that generates the indicators, targets and reporting systems needed to ensure its effectiveness in impacting on decisions, activities and overall organizational performance. This process model is complemented by the AA1000 Assurance Standard (see next section). www.accountability.org.uk <li data-bbox="831 1688 1465 2114">■ The International Standards Organisation (ISO) has developed over 15000 standards to date. With the ISO 9000 (quality) and ISO 14000 (environmental management) series, ISO has entered the terrain of management and organizational practice. ISO 14001 on environmental management systems recommends reporting, as opposed to the EMAS standard (see below) that requires reporting. ISO14063 on “environmental communications” offers guidance on what should be considered in developing an environmental communication program. The ISO is currently in the process of developing a guidance standard on Social Responsibility (ISO 26000).

Country/Region	Standards, Codes and Guidelines
	<p>Its guidance on 'communications' may have important implications for sustainability reporting world-wide. www.iso.org</p> <ul style="list-style-type: none"> ■ The Association of Chartered Certified Accountants (ACCA) has published a Guide to Best Practice in Environmental, Social and Sustainability Reporting on the World-Wide Web (ACCA & CorporateRegister.com, 2001). The ACCA global sustainability reporting awards have been replicated in many national level equivalents, advancing the quality of reporting world-wide. www.accaglobal.com ■ The Organisation for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises include Section III on "Disclosure", which encourages timely, regular, reliable and relevant disclosure on financial and non-financial performance. www.oecd.org ■ The largest global corporate citizenship initiative to date, the UN Global Compact provides a network of UN agencies, business, labour, NGOs and public institutions working to promote companies internalizing ten principles in the areas of human rights, labour, environment and anti-corruption. Since 2004, the initiative expects its company participants to annually submit Communications on Progress (COPs), using reporting indicators such as those of the GRI. A simplified COP template has been created for use by small and medium-sized companies (SMEs). Supported by the GRI, the Global Compact also published a practical guide on COPs. www.globalcompact.org ■ A global initiative of the International Council of Chemical Associations (ICCA), Responsible Care is a longstanding initiative of the chemical industry to improve health, safety and environmental performance, and to communicate with stakeholders about their products and processes. The new Responsible Care Global Charter, launched in 2006, includes provisions for improving monitoring and communication on progress against performance commitments by member companies. www.responsiblecare.org

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"> ■ The guideline SA8000 of Social Accountability is a uniform, auditable standard for social accountability (labour standards in the supply chain) with a third-party assurance system and is based on the core conventions of the International Labour Organization (ILO). www.cepa.org
Europe	<ul style="list-style-type: none"> ■ EMAS - The EU Eco-Management and Audit Scheme (EMAS) is a management tool for companies and other organizations, requiring them to evaluate, report and improve their environmental performance. The scheme has been available for participation by companies since 1995 (Council Regulation (EEC) No 1836/93 of June 29, 1993) on a voluntary basis. Following a site-based approach, EMAS requires companies to set environmental goals, to report on their site-level performance against these goals and to have their reporting ("environmental statement") examined and externally verified by an accredited environmental verifier. http://ec.europa.eu/environment/emas/index_en.htm
Australia	<ul style="list-style-type: none"> ■ Australian Minerals Industry Framework for Sustainable Development "Enduring Value" - Minerals Council of Australia guidelines for sustainable development requiring a commitment to public sustainability reporting on an annual basis from members, with reporting metrics self-selected from the Global Reporting Initiative (GRI) Mining and Metals Sector Supplement or self-developed. A commitment to independent verification of reports is also required. www.minerals.org.au ■ Triple Bottom Line Reporting in Australia - A guide to reporting against environmental indicators, published by the Department of Environment and Heritage, consistent with the Guidelines of the Global Reporting Initiative (GRI). www.deh.gov.au ■ Greenhouse challenge program - Industry members commit to preparing emissions inventories and forecasts, identifying and undertaking abatement plans and reporting progress against the action plan annually. They also agree to their progress being subjected to independent verification where appropriate.
Denmark	<ul style="list-style-type: none"> ■ New guideline for Intellectual Capital Statements is a key to knowledge management. www.videnskabsministeriet.dk ■ The Social-ethical Accounts is a guideline for private and public companies that wish to draw up a report on their social and ethical initiatives. www.bm.dk

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"> <li data-bbox="379 421 1016 546">■ The Etikbasen / CSR Scorecard 2002 is a public database on the internet where companies can report on their CSR initiatives and performance. www.csr-scorecard.org <li data-bbox="379 584 1016 741">■ The Social Index is a tool for measuring a company's degree of social responsibility on a score from 0 to 100. It requires external verification and certification to use the Social Index for external reporting. www.detsocialeindeks.dk
Finland	<ul style="list-style-type: none"> <li data-bbox="379 770 1016 927">■ The Finnish Accounting Standards Board (FASB) issues guidelines that deal with the disclosure of environmental expenditures and environmental liabilities as a part of the legally required financial accounts.
India	<ul style="list-style-type: none"> <li data-bbox="379 958 1016 1115">■ Corporate Responsibility for Environmental Protection (CREP), a charter promoted by the Central Pollution Control Board of India, an initiative which requires compliance by leading resource intensive industries. www.cpcb.nic.in/Charter/charter.htm
Italy	<ul style="list-style-type: none"> <li data-bbox="379 1146 1016 1240">■ The Study Group for Social Reporting (GBS) provides social reporting standards. www.gruppobilanciosociale.org <li data-bbox="379 1285 1016 1402">■ The Associazione Bancaria Italiana/Istituto per il Bilancio Sociale Guideline" (ABI) has published guidelines for social reporting in the financial sector. www.abi.it <li data-bbox="379 1451 1016 1576">■ The CSR-SC project enables organizations to voluntarily participate and adopt a 'social statement' according to pre-defined guidelines and a set of indicators.
Japan	<ul style="list-style-type: none"> <li data-bbox="379 1608 1016 1688">■ Environmental Reporting Guidelines have been issued by the Ministry of the Environment. www.env.go.jp <li data-bbox="379 1738 1016 1823">■ Environmental Performance Indicators Guidelines for business issued by the Ministry of the Environment www.env.go.jp
Norway	<ul style="list-style-type: none"> <li data-bbox="379 1868 1016 2024">■ The Confederation of Norwegian Enterprise (Næringslivets Hovedorganisasjon) has developed two checklists: for social responsibility ("Sunn vekst") and for human rights based on international human rights conventions and standards. www.nho.no

Country/Region	Standards, Codes and Guidelines
South Africa	<ul style="list-style-type: none"> <li data-bbox="831 421 1465 539">■ The Second King Report on Corporate Governance (King II) is a non-legislated code on good corporate governance. It includes a detailed section on integrated sustainability reporting. www.iodsa.co.za <li data-bbox="831 584 1465 741">■ The launch of the Johannesburg Stock Exchange (JSE) Socially Responsible Investment Index (SRI Index) encourages companies in the FTSE/JSE All Share Index that choose to participate to report publicly on sustainability related issues. www.jse.co.za/sri
Sweden	<ul style="list-style-type: none"> <li data-bbox="831 763 1401 882">■ The Swedish Accounting Standards Board (Bokföringsnämnden) provides guidelines on environmental information in the Directors' report section of the annual report. www.bfn.se
The Netherlands	<ul style="list-style-type: none"> <li data-bbox="831 920 1465 1106">■ The Assurance Standards Committee (RJ) provides guidelines for the integration of social and environmental activities in the financial reporting of companies. Furthermore, the RJ provides a framework for the publication of a separate report on these activities.
United Kingdom	<ul style="list-style-type: none"> <li data-bbox="831 1128 1465 1413">■ In 2006 the Department for Environmental, Food & Rural Affairs (DEFRA) published their 'Environmental Reporting Guidelines – Key Performance Indicators (KPIs)', designed to assist companies with new narrative reporting requirements relating to environmental matters, as contained within the 'Contents of Directors Report' of the Company Law Reform Bill. http://www.dti.gov.uk/bbf/financial-reporting/business-reporting/page21339.html <li data-bbox="831 1451 1465 1704">■ Announced by the UK Prime Minister at WSSD in 2002, the Extractive Industries Transparency Initiative aims to increase transparency in transactions between governments and companies within extractive industries. It requires disclosure of information on payments by companies and revenues received by the governments concerned. www.eitransparency.org
North America: United States of America, Canada	<ul style="list-style-type: none"> <li data-bbox="831 1733 1465 2054">■ The Global Sullivan Principles of Social Responsibility is a code of conduct to encourage participating companies and organizations working toward the common goals of human rights, social justice and economic opportunity. Encouraging reporting, the principles conclude with the statement: "We will be transparent in our implementation of these Principles and provide information which demonstrates publicly our commitment to them." www.thesullivanfoundation.org/gsp/default.asp

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"><li data-bbox="368 421 1016 837">■ The Coalition for Environmentally Responsible Economies (CERES) developed the CERES (previously “Valdez”) Principles following the 1989 Exxon Valdez disaster. This ten-point code of conduct also introduced specific environmental reporting guidelines. Embedded in the code of conduct was the mandate to report periodically on environmental management structures and results. A driving force behind the launch of the GRI process in 1997, CERES continues to encourage corporate environmental responsibility through working with endorsing companies on meeting their commitment and reporting along the GRI Sustainability Reporting Guidelines. http://ceres.org<li data-bbox="368 875 1016 1032">■ One of the early initiatives, the Public Environmental Reporting Initiative (PERI) was established in 1993 by a group of nine North American companies. PERI issued reporting guidelines to help organizations improve their environmental reporting.

4.2 Mandatory standards

Country/Region	Standards, Codes and Guidelines
European Union	<ul style="list-style-type: none"> <li data-bbox="831 416 1476 987">■ The EU Modernization Directive (2003/51/EC) requires organizations seeking a stock market listing to disclose risks associated with capital assets and requires financial regulators to assess those risks (in line with Commission Recommendation 2001/453/EC). Setting minimum mandatory standards for EU countries, the Accounts Modernization Directive (2003) requires all large companies (not just quoted ones) and medium-sized ones to include in their annual reports a fair review of the development and performance of the company's business and its position, including - "to the extent necessary for an understanding" - information on environmental and employee matters. Large companies are also expected to produce non-financial key performance indicators. The EU demands sustainable development disclosures from all member countries since January 2005. So far 23 countries have transposed the law to national level. <li data-bbox="831 1021 1476 1182">■ The application of the International Accounting Standards (IAS) at EU level (EC regulation no. 1606/2002) requires organizations to account for changes to asset values stemming from environmental factors if they are financial (e.g. trading permits). <li data-bbox="831 1216 1476 1377">■ Based on the Integrated Pollution Prevention and Control Directive (IPPC), Member States are required to register emission data from large companies (so called IPPC installations) and report data to the Commission.
Australia	<ul style="list-style-type: none"> <li data-bbox="831 1406 1476 1960">■ Corporations Act 2001 requires companies that prepare a director's report to provide details of the entity's performance in relation to environmental regulations. On July 1, 2004, the Corporate Law Economic Reform Program (Audit Reform & Corporate Disclosure) Bill 2003 (CLERP 9), extended this to the operations and financial position of the entity and its business strategies and prospects (Section 99A [1]). In 2005 both the parliamentary Joint Committee on Corporations and Financial Services (PJC) and Corporations and Markets Advisory Committee (CAMAC) undertook enquiries into CSR and the desirability of mandatory requirements for companies to report on the social and environmental impact of their activities. CAMAC has produced a detailed CSR discussion paper (November 2005) with an overview of regulatory requirements.

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"> <li data-bbox="371 416 1011 600">■ Financial Services Reform Act 2001 was promulgated in March 2002 and requires fund managers and financial product providers to state “the extent to which labour standards or environmental, social or ethical considerations are taken into account in the selection, retention or realization of the investment.” <li data-bbox="371 645 1011 763">■ National Pollutant Inventory requires industrial companies to report emissions and inventories for specific substances and fuel to regulatory authorities for inclusion in a public database. <li data-bbox="371 808 1011 1025">■ ASIC Section 1013DA Disclosure Guidelines, Australian Securities and Investments Commission - guidelines to product issuers for disclosure about labour standards or environmental, social and ethical considerations in Product Disclosure Statements (PDS). The guidelines complement the Financial Services Reform Act mentioned above. <li data-bbox="371 1070 1011 1285">■ New South Wales (NSW) Greenhouse Gas Abatement Scheme - Electricity utilities and certain large end-users of electricity (e.g. metal refineries) in the state of NSW are required to comply with greenhouse gas emissions benchmarks, and to report annually on their compliance. Annual external audits are also required. www.greenhousegas.nsw.gov.au
Belgium	<ul style="list-style-type: none"> <li data-bbox="371 1312 1011 1397">■ Article 4.1.8 of VLAREM II stipulates that certain companies have to issue an annual environmental report (only applicable for the region of Flanders). <li data-bbox="371 1442 1011 1527">■ The Bilan Social requires organizations’ reporting of data on the nature and the evolution of employment (e.g. training).
Canada	<ul style="list-style-type: none"> <li data-bbox="371 1559 1011 1677">■ The Securities Commission requires public companies to report the current and future financial or operational effects of environmental protection requirements in an Annual Information Form. <li data-bbox="371 1722 1011 1841">■ The Bank Act requires banks and other financial institutions with equity of US\$1 billion or more to publish an annual statement describing their contributions to the Canadian economy and society.
Denmark	<ul style="list-style-type: none"> <li data-bbox="371 1863 1011 1948">■ The Green Accounts Act requires certain listed companies to draw up green accounts and include a statement from the authorities.

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"> ■ The Danish Financial Statements Act requires reporting on intellectual capital resources and environmental aspects in the management report if it is material to providing a true and fair view of the company's financial position.
Finland	<ul style="list-style-type: none"> ■ The Finnish Accounting Act requires companies to include material non-financial issues in their directors' report of the annual/financial report and refers to the previously mentioned guidelines for good practice.
France	<ul style="list-style-type: none"> ■ Law n°2001-420 related to new economic regulations / Nouvelles Régulations Economiques (NRE operative since 2003) - Art. 116: environmental and social reporting is mandatory for publicly quoted companies, which are in many cases holding companies. The mandatory requirement on CSR reporting was introduced through an amendment in the New Economic Regulation Act. The amended NRE indicates that listed companies will be required to report on social and environmental performance in their financial statements. More detailed requirements followed in the enforcement order, issued a year later. The requirements are based on a list of forty indicators, many of them inspired by the GRI performance indicators. Some indicators were also taken from the "French social report", a list of social data required from all companies to show compliance with labour regulation. ■ "La note de cadrage" (framework memo) and "L'étude d'impact" (impact study). These documents accompany the 2001-420 law and provide guidelines to help companies implement the legal requirements. ■ The CJDES Bilan Societal is a tool for internal and external information exchange. By means of completing a questionnaire, companies can report on their social profile and performance.
Germany	<ul style="list-style-type: none"> ■ The Bilanzrechtsreformgesetz (BiReG) - New law that extends reporting duties of German companies to non-financial performance indicators such as environmental or employee issues.
India	<ul style="list-style-type: none"> ■ Sec 217 (1) of the Companies Act states that there shall be attached to every balance-sheet laid before a company in general meeting, a report by its Board of Directors, with respect to issues such as conservation of energy, technology absorption and foreign exchange earnings.

Country/Region	Standards, Codes and Guidelines
Japan	<ul style="list-style-type: none"> ■ The Law of Promotion of Environmentally Conscious Business Activities requires “specified entities”, to publish an environmental report every year. ■ The Pollutant Release and Transfer Register Law concerns reporting of releases to the environment of specific chemical substances and promoting improvements in their management.
Norway	<ul style="list-style-type: none"> ■ The Norwegian Accounting Act (Regnskapsloven) requires the inclusion in the Directors' Report of several social, environmental and health and safety issues and the implementation of measures that can prevent or reduce negative impacts and trends.
South Africa	<ul style="list-style-type: none"> ■ National Black Economic Empowerment Act (No. 53 of 2003): Sets out a national framework for the promotion of black economic empowerment (BEE) – this act requires progress reports to be submitted to government. ■ Employment Equity Act (No. 55 of 1998): Seeks to eliminate unfair discrimination in the workplace and implement affirmative action for “designated groups”: black people, women, or people with disabilities. Annual reporting on progress is required.
Spain	<ul style="list-style-type: none"> ■ The 'Resolución de 25 de marzo de 2002' (el Instituto de Contabilidad y Auditoría de Cuentas) states that organizations are obliged to include environmental assets, provisions, investments and expenses in their financial statements. ■ In addition, the National Accounting Plan for the Electricity Sector specifies environmental issues in more detail.
Sweden	<ul style="list-style-type: none"> ■ The amendment to the Annual Accounts Act (Årsredovisningslagen) states that certain companies have an obligation to include a brief disclosure of environmental and social information in the board of directors' report section of the annual report.
The Netherlands	<ul style="list-style-type: none"> ■ The Environmental Protection Act includes a section on environmental reporting for the 'largest polluters' of the country. To date, over 250 companies each publish two reports a year: one public report and one governmental report. However, since deregulation this requirement has been simplified and the public report is no longer required.

Country/Region	Standards, Codes and Guidelines
United Kingdom	<ul style="list-style-type: none"> <li data-bbox="826 412 1458 824">■ The Business Review is a legal requirement for all UK listed companies to provide a narrative within their Annual Report on the company's strategies, performance and risks. This is a requirement of the EU Modernisation Directive. The Business Review requirement was initiated instead of a mandatory Operating and Financial Review (OFR), which remains a voluntary standard. The result of a lengthy public debate over the last three years, the OFR text requires directors to consider factors such as environment and community issues (factors and trends) insofar as these are relevant for understanding not only the past but also future performance of the business. <li data-bbox="826 864 1458 1021">■ As part of the UK listing requirements, the Combined Code requires businesses to report on governance and internal control. The Turnbull guidance provided further details on the requirements for reporting on internal control. This was updated in 2006 by the Flint Review.
United States of America	<ul style="list-style-type: none"> <li data-bbox="826 1052 1458 1178">■ The EEO-1 Survey requires annual filing by the US Equal Employment Opportunity Commission regarding employment records, including the racial and gender profiles of employees. <li data-bbox="826 1218 1458 1536">■ The Sarbanes-Oxley Act (formally the Public Company Reform and Investor Protection Act, 15 USC 7245 7256, 2002) imposed several new reporting requirements for US-listed companies to increase corporate transparency (mainly corporate governance). Its Section 404 requirements for top executives to sign off on detailed internal controls, have been accused of imposing too heavy a regulatory burden on companies, for example, by not explaining the scope of internal and external checks required. <li data-bbox="826 1576 1458 1872">■ The Securities & Exchange Commission (SEC): Under Regulation S-K, the SEC requires "appropriate disclosure...as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries."

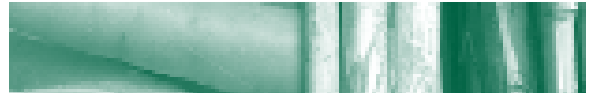
Country/Region	Standards, Codes and Guidelines
	<p data-bbox="408 421 1007 636">In addition, disclosure is required for any material estimated capital expenditures for environmental control facilities and for select legal proceedings on environmental matters. For foreign issuers in the United States, Form 20-F requires companies to “describe any environmental issues that may affect the company’s utilization of the assets.”</p> <ul style="list-style-type: none"><li data-bbox="376 680 1007 896">■ The Toxic Release Inventory (TRI) requires companies with more than 10 full-time employees to submit data on emissions of specified toxic chemicals to the Environmental Protection Agency. In addition, the SEC requires disclosure on legislative compliance, judicial proceedings and liabilities relating to the environment in Form K-10.

4.3 Global and national assurance standards

Country/Region	Standards, Codes and Guidelines
International	<ul style="list-style-type: none"> <li data-bbox="831 544 1476 920">■ The International Standard on Assurance Engagements (ISAE) 3000: Assurance Engagements other than Audits or Reviews of Historical Financial Information was developed by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC). IFAC is the body responsible for issuing international accounting and auditing standards for the accounting profession. ISAE 3000 came into force in December 2003 and is now being used by accounting firms to guide their assurance engagements on sustainability reports. <li data-bbox="831 965 1476 1305">■ In March 2003, the UK-based AccountAbility issued the AA1000 Assurance Standard (AA1000AS). AccountAbility used a phased multi-stakeholder process to develop AA1000AS, a standard that covers the full range of an organization's disclosure and performance based on the three core principles of "materiality", "completeness" and "responsiveness" to help ensure that reporting and assurance meets stakeholders' needs and expectations. www.accountability.org.uk
National standards	
Australia, New Zealand	<ul style="list-style-type: none"> <li data-bbox="831 1357 1476 1762">■ Standards Australia has published the Standard DR03422: General Guidelines on the Verification, Validation and Assurance of Environmental and Sustainability Reports. Work on this Standard was carried out by the joint Standards Australia and Standards New Zealand Committee QR-011 Environmental Management Systems. A marked difference between this Standard and the AA1000, AUS and ISAE 3000 standards is the definition and use of the terms verification and validation. DR03422 has been issued as an Interim Standard for a period of two years, after which it will be reviewed.

Country/Region	Standards, Codes and Guidelines
	<ul style="list-style-type: none"> ■ Australian Auditing Standards (for accounting firms) can be applied to the audit and review of sustainability reports. AUS102.44 states that "Australian Auditing and Assurance Standards, while developed primarily in the context of financial report audits, are to be applied, adapted as necessary, to all audits of financial and non financial information, to all other assurance engagements, and to all audit related services".
Germany	<ul style="list-style-type: none"> ■ The German Institute of Chartered Accountants (IDW) has developed a Standard for Assurance Engagements of Sustainability Reports.
Japan	<ul style="list-style-type: none"> ■ The Japanese Institute of Certified Public Accountants (JICPA) published the "Environmental Report Assurance Services Guidelines (Interim Report)" in 2001.
Sweden	<ul style="list-style-type: none"> ■ The Swedish Institute for the Accountancy Profession (FAR, www.far.se) issued a draft recommendation Independent Assurance on Voluntary Separate Sustainability reports in February 2004. An updated version of the recommendation, in compliance with ISAE 3000 and with references to AA1000AS will be launched in December 2006.
The Netherlands	<ul style="list-style-type: none"> ■ The Royal Dutch Institute for Registered Accountants (NIVRA) issued an Exposure Draft Standard RL 3410 Assurance Engagements relating to Sustainability Reports early 2005. The Exposure Draft is designed to comply with ISAE 3000 while incorporating the principles of AA1000AS and drawing on the GRI Sustainability Reporting Guidelines.

5. Case Studies from five regions



The following case studies have been prepared with contributions from KPMG's national Sustainability practices as well as Rever Consulting in the case of Brazil.

Each brief case provides a slightly different approach and focus area. The following countries and regions were selected:

- Brazil: an emerging market economy that has been prominent in the global sustainable development debate. Whilst not showing substantial activity in terms of sustainability reporting, the Brazilian experience nevertheless provides valuable information and experience on progressively introducing reporting from a community engagement focus to core business focus.
- European Union (EU): a complex and regulated entity, with its Accounts Modernisation Directive but also many other pieces of legislation that could be interpreted as requiring components of sustainability reporting.
- Denmark: a Nordic country that has made commitments to sustainable development and has backed this up with mandatory reporting standards.
- United States of America (USA): a major economy with extensive regulation that apply to a variety of issues related to sustainable development. Because of listing as well as legal requirements in the USA, and the fact that the large USA-based multinational corporations have operations in both the developed and developing world, these requirements are relevant and should be taken into consideration worldwide.
- Japan: One of the strongest economies in the world, Japan has been using its manufacturing, information and communications technology sectors not only to lead in areas such as quality and environmental management. It is also leading the sustainability reporting trend in Asia, with over 130 GRI reporters from the Japanese corporate world.
- South Africa: an emerging market economy from Africa whose transition to democracy has been accompanied by a lively CSR debate and much activity in the field of sustainability reporting. South Africa provides an interesting combination of mandatory requirements based on legislation on issues related to sustainable development as well as mandatory ("comply or explain") requirements linked to its corporate governance standards.

■ India: With an economy that has seen a boom in business processing, information technology and manufacturing, India presents a valuable example of the introduction of new management tools such as sustainability reporting in a developing world context. This happens against the background of a tradition of corporate philanthropy, and current debates on how to internalise social responsibility and distribute the benefits of economic growth more widely.

5.1 Brazil

(This section was contributed by Rever Consulting, Brazil)

The roots of the present movement of social reporting and corporate social responsibility in Brazil go back to the late 1980s, ignited by a series of social and political developments as the country struggled to establish a democracy and fight corruption. With the socio-political experience emerged a growing consensus on the importance of the business sector to the country's social well-being. By the 1990s, various foundations, institutes, think tanks and civil society organizations with strong ties to the business community focused on private-sector conduct, ethics and social responsibility. The Fundação Instituto de Desenvolvimento Empresarial e Social (FIDES) introduced a voluntary model for reporting and a few companies began to systematically publish information regarding community involvement, environment and the treatment of workers. The widespread practice of

publishing a "balanço social" only gained significant momentum in 1997, thanks to the leadership of social activist Herbert de Souza in a targeted campaign to mobilize the business sector. This led to a model developed by the Instituto Brasileiro de Análises Sociais e Econômicas (IBASE; more below).

Legislation for Social Reporting

Requirements for social reporting emerged as early as 1975 under the military regime with the Decreto Lei no 76.900 – the Annual Report of Social Information (Rais in Portuguese). This was an obligatory reporting requirement for all companies, regardless of size, to release basic labour statistics and consolidated numbers concerning company staff. It is still valid today.

It was only in the 1990s that the growing momentum of social reporting led to a political initiative to make reporting mandatory. In May 1997 the Federal Congress Representative Marta Suplicy (PT/São Paulo) introduced the bill Projeto de Lei Nr 3.116/97 to the Federal Congress. This foreseen law was to require all companies with over 100 employees to publish a "balanço social" using criteria taken from the French social reporting legislation.

The preamble to the bill stated the rationale for making reporting mandatory. It was argued that elaborating a social report serves to stimulate reflection by the company concerning its social impact. It was also felt that the social report would

facilitate assessment of the use of fiscal incentives and other expenditures related to workers. Finally, the preamble argued that it would help identify effective human resources policies, and serve as a reference for effective action among companies of different sectors as well as action on social policy (Law Project Nr 3.116/97, Federal Congress, Brasília, May 14th 1997). The three members of congress that supported the bill, however, were not re-elected and were not able to see the bill through to become law. In 1999 the initiative re-emerged, supported by Congress Representative Paulo Rocha (PT/Pará). Today the initiative is still being considered at the Economy, Industry and Commerce Commission of the Federal Congress.

On the municipal level, the period from 1997 to 1998 saw several interesting pieces of legislation concerning social reports and corporate social responsibility being accepted in cities such as São Paulo, Santo André, Porto Alegre, Santos, João Pessoa, and Uberlândia. The legislation in São Paulo's was most notable, due to the scope of the legislation in a city with such a wide range of economic activity. Passed in October 1998, resolution Nr 05/98 (project Nr 39/97) created the "Company Citizenship Seal of São Paulo City." The seal was intended to distinguish quality in social reporting. A commission was formed to develop a social reporting model and to award the seal to companies meeting its requirements.

The mandatory versus voluntary reporting debate

The emergence of legislative measures to require social reporting stimulated extensive debate among organizations involved in the corporate social responsibility movement. Arguments cited followed those highlighted in the earlier section of this report. Some sought to establish a baseline requirement for all companies to report on social aspects of company performance. Brazilian companies had a history of non-transparency. Most companies disclosed very little information regarding their operations or investments. The national lobby of accountants led a strong lobby to pass the legislation for mandatory reporting, anticipating increased activity for their sector. The Federal Council of Accountants (CFC) passed a resolution in 2004 concerning the requirements of the "balanço social" in the hope of pre-empting and influencing expected legislation.

Others were concerned that mandatory regulation would undermine the very innovation and drive that defines the movement. A majority of those involved in the corporate responsibility movement, even those coming from NGOs, were opposed to mandatory standards. Many felt that it was too early to tell what effective reporting really entails. The vice-president of the Industrial Federation of São Paulo (FIESP) said: "The problem is so much is still unknown. When pressured to launch new legislation, typically the government doesn't enforce it and prays no one will use it." The requirement for social reporting was felt to be misguided because it didn't contribute to establishing an ethical commitment with society. It was also feared that creating this type of obligation could stagnate the pace of voluntary action.

The IBASE Model

Still used today, the IBASE model has several distinctive characteristics: it was created entirely by a non-governmental organization, it is strictly quantitative without details of policies or practices, and it demands uniformity of information to facilitate comparison. The IBASE model has evolved marginally since its launch, concentrating instead on increasing the number of companies reporting. Today the information requested includes (as a percentage of payroll expenditures or operating revenues) internal expenditures on health, taxes, pensions, culture and leisure and external investments in culture, education, health and sanitation. Furthermore, the model asks for expenditure on environmental projects both related to company operations and external projects. Particularly controversial has been employee data related to the number of Afro-Brazilian employees, the number of employees with disabilities and the number of women employed.

In 2005, a total of 165 companies published social reports using the IBASE model and 64 received the IBASE seal. In 2006 IBASE announced stricter standards for obtaining the seal. To evaluate company performance IBASE will submit company reports to NGOs representing interests related to the environment, workers' rights, consumers' rights, and diversity, and also collect comments from the general public.

The Ethos Model

In 2001, the Ethos Institute of Social Responsibility launched its "Guide for Social Responsibility Annual Report and Statement." The complicated title reflected the difficulty to abandon the traditional term "balanço social" or social statement for "annual report", mindful of the global trend. The 2001 Guide sought to bridge the gap between the national standard of the IBASE model and international standards, in particular the Global Reporting Initiative (GRI), to elevate the level of quality, consistence, and credibility of company reports. Absent from the IBASE model were the concept of stakeholder engagement, a comprehensive representation of indicators along the triple bottom line, and qualitative indicators with non-financial data such as company policies and management systems. The Ethos Guide was seen as an intermediate step for companies towards fully adopting the GRI standard. It followed the same format of the GRI framework, with a selection of economic, social and environmental indicators. Subsequent versions have added aspects related to future targets, the topic of corporate governance, and specific information on stakeholder engagement processes.

Promoting the guide, Ethos and a group of business organizations have launched a Social Reporting Award prestigiously hosted by the São Paulo Stock Exchange (BOVESPA). In the third year of the awards, 167 companies competed. A study performed by a leading business

school in Brazil, the Dom Cabral Foundation (FDC), identified key conclusions based on a qualitative analysis of the reports submitted:

- Some stakeholders clearly lack coverage in the existing reports: particularly subcontractors, competitors, and investors;
- Issues regarding unions, dismissals, retirement, corruption and bribery are usually avoided; and
- Difficulties, polemic or negative occurrences, and unmet targets are seen as negative points that should not be included, though this tendency showed some indications of change in 2003

Finally, the study indicates that social reporting in Brazil is still not seen as part of a wider process related to performance. It concludes that the social report or "balanço social" is still seen as a one-way marketing tool by the majority of companies. Few indicate the target audience or the circulation of their reports. In addition, few companies offer feedback mechanisms or effective channels of communication to obtain more information.⁶

BOVESPA Corporate Sustainability Index

In 2005 BOVESPA launched a Corporate Sustainability Index (ISE – Índice de Sustentabilidade Empresarial) to identify corporations with high levels of economic, financial, social and environmental excellence. This index is similar in nature to the Dow Jones

Sustainability and FTSE4Good indices. A questionnaire developed by the Center for Sustainability Studies of the Business Administration School of São Paulo (CES-FGV) is used to distinguish between companies of the BOVESPA's 150 most liquid stocks in terms of their performance, considering environmental, social and economic aspects. Through "cluster analysis" to identify companies with similar performance, the ISE lists a maximum of 40 companies with leading performance.

The environmental, social and economical dimensions are evaluated considering four areas: policies, management, performance and legal compliance. Additionally, the questionnaire looks at the nature of the product and corporate governance measures. While voluntary in nature, companies have shown a great deal of interest to enter the index. Development of the index resulted in vigorous debate between what is good practice internationally in this type of index as well as in the local business context, resulting in a rigorous questioning of corporate activity, policy and performance.

Conclusion

From a cultural history of dependency due to inequality, companies in Brazil continue to struggle to understand the implications of being a powerful agent in a context of unmet social demands. The first signs of an invigorated movement formed around a campaign to eliminate poverty. Ironically, after nearly a decade of progress the theme returned as President's Lula chief focus

⁶ For more information, visit www.domcabral.org.br

for mobilizing the business sector. It is of no great surprise then that most of Brazil's social reporting focuses on social investments made by companies. While this might be seen internationally as "greenwashing" with social projects, within the Brazilian context companies are responding to society's predominant demand to address conditions faced by a majority of the population.

Responding to such a demand, however, is a dangerous proposition for companies. By doing so they assume a role that they are far from capable or equipped to fulfil in the long term. These societal issues are too varied and too complex and most importantly not the central focus of their operations. The tendency among companies is to simplify the social question into a single response - education, concentrating resources in activities that make little difference when considering the educational needs of the country.

Recent developments such as the Ethos guide for reporting and the BOVESPA index for sustainability have directed companies toward international standards and practices. Company reporting in Brazil still does not reflect a serious consideration of core business operations. Largely absent is a treatment of impacts on stakeholders or a serious consideration of materiality. Content focuses largely on activities dealing with social issues where companies have only an indirect impact.

This creates an unfortunate situation for both companies and society. When responding reactively to societal problems, demand quickly exceeds the capacity for companies to respond. At the same time, societal stakeholder misses engagement where company decision-making can have significant impact. Still, Brazil does not operate in isolation. As companies become more exposed to international pressure, they will need to focus on "issues" that are related to their core business.

5.2 Denmark

Denmark has mandatory requirements for stand-alone environmental reports and annual accounts, but not for triple-bottom-line reporting. Approximately 1,000 to 1,200 companies are required to submit green accounts and the rate of compliance is one hundred percent. Despite the fact that only 29 of Denmark's 100 largest companies issued a sustainability report, the reports produced are rated among the highest in various studies (ACCA, 2004, KPMG, 2005).

The majority of the current legislation on sustainability accounting was introduced under the former Social Democratic government. The government also took the initiative to develop guidelines for voluntary reporting of intellectual capital, social and ethical reporting, and sustainability reporting. As this area is not a priority for the current liberal government, new legislation and developments are not expected in the foreseeable future.

The Green Accounts Act

The Green Accounts Act regulates stand-alone environmental reports. It was adopted by the Danish Parliament in 1995 as an amendment to the Danish Environmental Protection Act and introduced as a statutory requirement by the Danish Ministry of Environment and Energy. Its primary objective is to increase public and corporate interest in environmental issues and to encourage enterprises to adopt more active and targeted environmental initiatives. The Green Accounts Act is effective from fiscal year 1996. Under this act approximately 1,200 companies in nine specific sectors - including iron and steel, processing, oil and gas, chemicals, animal processing and power generation - have to publish Green Reports (Green Accounts). Approximately 200 companies do so voluntarily.

Companies have substantial freedom in how they present environmental information in the Green Reports, which must be submitted to both local and national authorities. The report consists of three elements: general company information, a director's report which must inform readers with no expert knowledge, and a resource consumption report. The resource consumption report reflects a material flow-based approach to reporting on inputs and emissions/releases of polluting substances.

Contrary to best practice trends, management is not required to sign the report. If an audit is performed, although this is not a requirement, it

must be included in the report. The annual statement and EMAS report may be allowed as a substitute for the Green Report. The Act was reviewed in 2001 and recent developments, as well as evolving perceptions in Danish society, were taken into account. Requirements have been extended to include more information on waste and waste handling and the environmental behaviour of the company. To improve credibility, local authorities are now required to draw up a statement as part of the accounts on whether the company's activities are consistent with information held by local authorities. Although discussed, verification has not been made mandatory, to avoid further financial burden (Hibbit 2004).

In 1999, the Danish EPA conducted an investigation among 550 firms that submitted Green Reports. The investigation found that five out of six accounts provided the legally required information. Although companies incurred administrative costs for the production of the accounts, about half of them claimed that the beneficial spin-offs of the report made the financial cost worthwhile. A total of 40% of the companies indicated that they had achieved environmental improvements. The study also found that investors have begun to refer to Green Reports when evaluating firms. Only half of the investigated group's "neighbours and general consumers" knew of the Green Reports. The Danish law on Green Reports does not include any direction on environmental information in monetary terms (Nyquist, 2003).

Danish Financial Statement Act

Requirements for environmental reporting within the annual report and accounts are stated within the Danish Financial Statement Act (section 99) as an introduction to the EU Recommendation of 2001. Denmark is one of only a few countries to have introduced parts of the EU Commission Recommendation on disclosure in annual reports into legislation, since 1 January 2002.

The Danish Financial Statement Act requires listed companies and state owned public limited companies to report on intellectual capital resources and environmental aspects in a management report, if it is material to providing an accurate view of the company's financial status. Section 99 of the Act provides that this review should, *inter alia*, describe the enterprise's impact on the environment and measures taken for the prevention, reduction or resolution of environmental damage. From 2005 companies are furthermore required to supplement the management report with information on non-financial aspects that are relevant to the company's activities, including environmental and human resource aspects. The law is intentionally not very specific, but does contain criteria for relevance and includes suppliers and contractors.

Specific requirements of the EU Recommendation for disclosure of environmental policies and environmental performance, however, are not implemented.

Moreover, management has the option to exclude environmental information from the annual report if it is deemed to be immaterial.

In the event that management wishes to disclose more thorough and specific information on environmental issues, the Danish Financial Statement Act provides the opportunity to disclose such information in a supplementary report that must be clearly separated from and placed after the statutory components of the annual report.

Although there is some overlap between the Green Accounts Act and the Financial Statement Act section 99, there are two major differences: reporting under the Green Accounts Act is at site level whereas reporting in the management review section, as demanded by the FSA, is at enterprise level. Secondly, issues identified as having a material impact for Green Accounts are based on a technical review, whereas environmental issues in the management review are assessed for materiality from the perspective of providing a true and fair review of the company's operations and affairs (Hibbit, 2004).

The Social Index

The Social Index, launched in 2000 by the Danish Ministry of Social Affairs, is a self-assessment tool for measuring to what extent a company focuses on employment and social inclusion policies as part of its social responsibility. It is based on an employee questionnaire. The collated information is used to determine a company score (a number between 0 and 100). An external and impartial assessor (inspector) verifies that the score is reasonable. Companies that achieve a score greater than 60 on the Social Index, and which are verified by external experts, are entitled to use the Social Index Label on their products and reports.⁷

CSR Scorecard

The Consumer Information Centre within the Ministry of Economic and Business Affairs has an ethical database, the so-called "CSR scorecard" – for which companies can voluntarily file information about themselves and how they deal with recognised labour standards.⁸

Guideline for Intellectual Capital Statements

This guideline explains the intellectual capital statement concept, content and structure. It aims to help individual companies or public organisations develop knowledge management strategies and communicate these results in external intellectual capital statements. Through questions, checklists, examples and good advice, the guideline leads companies systematically through the process of preparing intellectual capital statements.⁹

⁷ For more information, see www.detsocialeindeks.dk.

⁸ For more information, see www.csr-scorecard.org.

⁹ For more information, see www.videnskabsministeriet.dk.

5.3 European Union

Commitment by the European Union (EU) to sustainable development is confirmed in the treaties of Amsterdam and Lisbon, as well as the 2001 Green Paper and 2002 Communication by the Commission on CSR. Sustainable development and CSR have been high on the public policy agenda at both EU and national levels in recent years. Supranational in character, EU law is binding for all member countries and can be seen as providing the minimum legal standard for reporting requirements in Europe. Current EU reporting regulation has been closely related to a series of directives designed to harmonize the accounting rules for financial reporting in EU countries. These are the 4th Directive (annual accounts) which dates from 1978 and the 7th Directive (consolidated accounts) which applies since 1983.

Most of the recent developments considered in this study have been undertaken within the EU's "Financial Service Action Plan" (FSAP), which has aimed to have a fully integrated financial market place from 2005 onwards. They are therefore not only of interest to EU member countries, but all possible future members as well as those economies in which companies seek either financing from European investors or listing on European stock exchanges. The difficulties and

experiences faced by the member countries in transposing the supranational law into national law are likely to be of value to countries that wish to align their reporting regimes with those of the EU.

The text below describes some of the steps undertaken by the EU and the consequent impact on sustainability reporting in the member states.¹⁰

European Commission Recommendation of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies (2001/453/EC)

The Commission Recommendation (unlike a Directive, a Recommendation is not mandatory) of 30 May 2001 is intended to encourage member states to comply with its recommendations as well as any national legislative requirements. In recognition of the needs of investors, the Recommendation urges a stronger consideration of environmental issues in annual reports and annual accounts, with an explicit reference to sustainable development (albeit directed at environmental issues). The Recommendation provides guidance on how to apply the 4th and the 7th Directives with respect to environmental issues, and refers to the general rules on recognition, measurement and disclosure in these Directives. It is possible to follow the Recommendation without being in conflict with the Directives. Certain countries in Europe have, however, implemented rules from the Directives which are not in accordance with the Recommendation.

The importance of the Accounting Directives has recently decreased somewhat among listed companies. The reason for this is that as of 2005 these companies must prepare their consolidated financial statements according to the international accounting standards (IAS).

With regard to recognition and measurement, the general view is that legislation in most countries is in accordance with the Commission Recommendation, but measures have not been taken to introduce the Commission Recommendation where such legislation does not exist. This is partly due to the fact that many countries have already introduced a number of the rules, as these are included in the 4th and 7th Accounting Directives.

Most of the issues regarding recognition and measurement are covered by IAS 16, 20, 36, 37 and 38, which have already been introduced to a certain degree in many countries. In the remaining countries they apply to all listed companies since January 2005 due to EU Regulation No 1606/2002. In IAS, however, the environment is not emphasised as a special area and is addressed along with other issues.

Status of Implementation

Four countries - Denmark, Finland, France and Portugal - have introduced elements of the Commission's recommendations into their legislation. In Finland and Portugal, requirements for disclosure in annual reports have been integrated in national accounting

¹⁰ It refers mainly to the PricewaterhouseCoopers (PWC) study "Implementation in Member States of the Commission Recommendation on Treatment of Environmental Issues in Companies' Financial Reports" (2001/453/EC) undertaken on behalf of the European Commission, the study "Integration von Klimachancen und Risiken in die Finanzberichterstattung" undertaken by the NGO Germanwatch with support from the German Ministry of Environmental Affairs, and the research report "Open Disclosure - Sustainability and the listing regime" by Mark Mansley from Claros Consulting.

standards. In France, the government has introduced specific requirements with respect to reporting on social and environmental issues in listed company annual reports, with the New Economic Regulations Act (NRE) and related order (20/02/2002).

In Denmark, issues for disclosure in the annual report have been determined by a general requirement in the Danish Financial Statements Act. Medium-sized, large and all listed companies have to describe their impact on the environment as well as measures introduced for the prevention, reduction or reversal of environmental damage. However, more specific requirements for the disclosure of environmental policies and performance are not enforced. Moreover, environmental information can be excluded from a company's annual report if it is deemed immaterial by management (see more detailed case study on Denmark). None of the remaining member countries have introduced disclosure criteria for annual reporting. Most countries recognise that environmental issues, in line with other issues, should be described to the extent that they are material to the company's financial performance.

The Prospectus Directive

The Prospectus Directive, introduced in 2003, was transposed into national law throughout the EU by July 2005. The Directive aims to ensure that issuers of securities have a uniform prospectus that is valid throughout the EU. Once this prospectus has been approved by a home market regulator, a company

will be able to use it to offer securities for sale anywhere in the EU, and the issuer need only publish shorter prospectuses with only the details of the securities when raising further capital (for example when issuing bonds).

Although annex 1 of appendix A does not explicitly mention sustainability issues, the directive demands (under point 8 – property plant and equipment) *“A description of any environmental issues that may affect the issuer's utilisation of the tangible fixed assets.”*

The Directive has been controversial, particularly in the UK where it is perceived to weaken existing rules on disclosure and to conflict with the Combined Code on Corporate Governance. There is concern that the Directive may limit the discretion of domestic regulators to demand enhanced disclosure, in particular on non-financial issues such as climate change and human rights.

In response to the issue of the Combined Code on Corporate Governance, the EU has stated that corporate governance issues are not affected as the Directive only formally concerns initial disclosure requirements (European Commission Press Release IP/02/1209 of 9 August 2002). Despite this, it has been argued that there is a conflict if the initial rules for prospectuses set one standard and ongoing disclosure requirements set another. In addition, the proposed

Directive imposes an annual requirement to update and maintain prospectus information (Mansley, 2004: 9) which the Directive fails to explain.

Regulation on the Application of International Accounting Standards (IAS)

According to the Regulation (EC) no. 1606/2002 of the European Parliament and Council (19 July 2002) on the application of international accounting standards, financial reporting for listed companies' consolidated accounts must comply with accounting standards issued by the International Accounting Standards Board (IASB) and adopted for use in Europe. Sustainability related references are included in the IAS Standards 36 (Impairment of Assets), 37 (Provisions and Contingent Liabilities) and 38 (Intangible Assets). Tradable emission rights will be reported on and accounted for under IAS 38 and allocated free of charge under IAS 20, as government grants.

Modernisation Directive

Sustainability oriented information in the annual report is so far required in Germany, Denmark, France, United Kingdom, Sweden and the non-member country, Norway.

The EU demands sustainability disclosure from all member countries since January 2005. The EU Accounts Modernization Directive 2003/51/EC amended with reference to the EU Commissions' recommendations (Article 46 of the 4th Accounting Directive) states:

“The annual report and the consolidated annual report are important elements of financial reporting ... The information should not be restricted to the financial aspects of the company's business. It is expected that, where appropriate, this should lead to an analysis of environmental and social aspects necessary for an understanding of the company's development, performance or position. This is consistent also with Commission Recommendation 2001/453/EC of 30 May 2001 on the recognition, measurement and disclosure of environmental issues in the annual accounts and annual reports of companies. However, taking into account the evolving nature of this area of financial reporting and having regard to the potential burden placed on undertakings below certain sizes, Member States may choose to waive the obligation to provide non-financial information in the case of the annual report of such undertaking.”

EMAS – Eco-Management and Audit Scheme

The EU Eco-Management and Audit Scheme (EMAS) is a management tool for companies and other organisations to enable effective evaluation, improvement and reporting on environmental performance. EMAS aims to encourage companies to develop environmental programmes and management systems, and to report publicly by way of triennial statements (similar to environmental reports). It has had great success in Germany due to tax advantages, but less so in other countries and take-up of the scheme is levelling off. The scheme has been available for participation by companies since 1995 (EEC Council Regulation No 1836/93 of

29 June 1993) and was originally restricted to companies in industrial sectors (ACCA and CorporateRegister.com, 2004).

Implementation experiences of the new requirements for the annual reports

The results of a PwC study (2004) indicate that it takes time for new legislation to become clearly understood and followed. This is often the result of a general lack of environmental knowledge within top management and finance departments who are closely involved in preparing annual reports. At the level of implementation there are also differences among member states. In France there is opposition to the EU legislation, especially from companies that did not have any environmental management systems in place beforehand and find it difficult to report under the new requirements. In Spain, where the legislation is not as specific as in France, some sectors (for example energy) have voluntarily started to set up standards for the inclusion of environmental data in financial reporting. This was done in order to be able to benchmark performance within the sector. The following obstacles confront companies and countries when implementing the new EU legislation and rules (PricewaterhouseCoopers, 2004):

- The new legislation resulted in a surplus of detailed information in the annual report on topics that were of limited relevance to the financial performance of a company;
- An inadequate awareness and understanding of environmental

issues among top management, the finance department and accountants, since this is not an area typically covered in the annual report;

- Companies already reporting on issues in other environmental report formats resisted the idea of additional reporting in the financial report;
- The Commission Recommendation failed to align with instruments of environmental management, especially EMAS; and
- Matching the new requirements with the changing requirements of the CSR movement or international reporting standards.

Conclusion

The content of sustainability-oriented financial reporting practices should generally improve with the application of IAS and additional reporting requirements in annual reports. Nonetheless, there remain important concerns. The data reported is not standardised, which can pose difficulties for comparative reviews. Although the legal requirement for companies to report on their environmental performance is rapidly increasing in Europe, the varying degree and quality of local interpretation means that investors find it difficult to rely on information being quantitative, comprehensive and comparable.

5.4 India

The level of sustainability reporting in India is at an infancy stage and still evolving. While currently there are no officially recognized guidelines or reporting standards on sustainability reporting (by accounting or regulatory bodies), there has been an increasing trend amongst companies to publish a variety of information relating to themes such as community, corporate social responsibility, environment, health and safety. Indian companies therefore present diversity in content and format under the overall umbrella of sustainability reporting.

Traditionally, while many organizations both in the public and private sector practice some sort of corporate social responsibility programmes, reporting has not been a common practice. A survey conducted in 2003 by Partners In Change showed that 70 per cent of the participating companies do not have a CSR policy, but are nevertheless doing 'good work'. However, over the past few years there has been an increasing awareness and activity in the CSR field and many companies have started some reporting on sustainability issues, albeit in limited and diverse formats.

There are many reasons for this change in mindset. Foremost is the increasing globalization of business. As more Indian companies expand internationally and acquire interests overseas, whilst at the same time there is a rapid increase in foreign investment in Indian corporates, demands on transparency from a more 'global audience' have put pressure on

Indian companies to start reporting on sustainability issues.

Within India there has also been a change in the mindset and attitudes of stakeholders on issues relating to environmental and social responsibility. Recently government faced public protests and pressure to refuse entry by foreign ships that were brought to India for decommissioning, as they contained large amounts of asbestos and other harmful substances. While the general public opinion on sustainability issues is still evolving, it suggests that companies taking the first steps can expect intense public scrutiny, which again highlights the need for transparent reporting on operations.

Another significant push factor has been the role of government as a stakeholder. India has historically had stringent laws on labour, environment, health and safety. However, their enforcement could have been much more efficient. Over the past few years the government has become increasingly proactive in addressing enforcement. Intense media attention and scrutiny on corporate social responsibility has also led to companies taking more cognizance of their activities and engagement with stakeholders.

Reporting patterns

Many organizations in India have certified environmental management systems, based on ISO 14001. Consequently, data on environmental indicators are more readily available and many companies start reporting by

issuing environmental reports which also include health and safety data. It is only after this initial phase that companies in general start developing reporting formats that conform with the GRI Guidelines. In accordance with global trends, some Indian companies have also started seeking independent assurance on their sustainability reports.

Reporting under environmental legislation

One of the fundamental features of India's ancient philosophy has always been respect for the environment. The Indian Constitution is amongst the few in the world that contains specific provisions on environmental protection. State policy principles explicitly enunciate the national commitment to protect and improve the environment. The national environmental policy framework is the responsibility of the Ministry of Environment and Forests. Implementation is undertaken by the Central Pollution Control Board (CPCB) and the State Pollution Control Board (SPCB) at the federal and state levels respectively. The Department of Environment at the federal level supports the SPCBs. The Environment (Protection) Act of 1986, considered as the "Umbrella Act", was formulated for the protection and improvement of the quality of the environment and prevention, control and abatement of environmental pollution. The act is also an 'enabling' law, which articulates the essential legislative policy on environmental protection and delegates wide powers to competent authorities to frame necessary rules and regulations.

- In terms of this Act, the federal government has provided that each covered organization should submit an annual 'environmental audit report' (in a prescribed format) to the relevant SPCB.
- Reporting in the environmental statement includes parameters such as water and raw material consumption, pollution generated (along with variations from prescribed standards), quantities and characteristics of hazardous and solid wastes, impact of pollution control measures on conservation of natural resources and on cost of production, and additional investment proposals for environmental protection

At this stage the statement is not required to be audited. The legal requirement on its preparation and submission helps ensure that data on environmental measures is collated, categorized and analysed by all businesses covered under the legislation. Many organizations in India have started to audit these statements internally with a view to improving their environmental performance and as a matter of good practice.

Reporting under the Companies Act

The Companies Act in India governs the overall regulation of companies in India and includes sections on disclosure and reporting on various aspects of company operations. Section 217 of the Act stipulates that the Board of Directors Report (attached to every balance-sheet tabled at a company annual general meeting),

shall contain information on conservation of energy. The latter is expected to include:

- Energy conservation measures taken;
- Additional investments and proposals, if any, being implemented for reduction of the consumption of energy;
- Impact of the measures taken above for reduction of energy consumption and consequent impact on the cost of production of goods; and
- Total energy consumption and energy consumption per unit of production in respect of specified industries.

Reporting on social matters

Traditionally there has been a very thin line of demarcation between socially aware entrepreneurship and philanthropy. Businesses today are becoming more aware of the business case, that social responsibility is not limited to acts of charity and that it requires internalization and systemic expression.

In 1980 Tata Steel released a "Report of the Social Audit Committee" which explored whether the company had fulfilled the objective contained in the Articles of Association regarding its social and moral responsibilities to consumers, employees, shareholders, the local community and society. Since then there has been a growth and consistent improvements in the

quality of reporting. Many companies issuing CSR corporate communications now actively report on the social dimension as well. Yet in the absence of any locally recognized standard there is no clear guidance on social reporting.

While there are no clearly defined means for public disclosure, every factory in India is required to report information relating to labour and employment, working hours, accidents, health and safety. Reports must be submitted to the relevant state governments in a prescribed format under the Indian Factories Act. While there is a statutory obligation to report data to the relevant authorities, publication of this information is not mandated under current legislation.

Reporting developments

In the absence of formal reporting frameworks in India, companies are becoming increasingly oriented towards global standards on sustainability reporting, in particular the GRI. As part of the G3 revision process, the GRI Reporting as a Process Working Group (RPWG) met in Mumbai, India, on 6 – 8 September 2005 at the headquarters of Air India. The meeting was attended by the GRI Reporting as a Process experts team, GRI staff and Indian stakeholders. It included a full day meeting with Indian companies, including representatives from the Tata Group, ITC, Air India, Taj Group of Hotels, Shell, Ambuja Cement, Confederation of Indian Industries, Ernst & Young and KPMG. The purpose of the meeting was to articulate the reporting experiences of

Indian companies, in order to help inform the thinking of the RPWG. Previously, the GRI also presented a reporting training meeting in cooperation with the Confederation of Indian Industries.

Meetings such as the above enable a better understanding of the Indian context of reporting and ways of applying the international framework standard domestically. Discussions confirmed that sustainability reporting in India often starts as a voluntary initiative, in the midst of limited pressure from local NGOs to publish sustainability reports. Reports are often produced and used for internal purposes. Indian stakeholders also expressed a strong emphasis on the principle of "Sustainability Context", viewing the local sustainability context as essential in determining relevant report content. The Mumbai meeting expressed strong support for an Indian national annex to the GRI, in order to help Indian organizations report on their specific sustainability challenges.

Conclusion

The progress of sustainability reporting in India is slow, but a significant and sound start has been made. For example, Tata Steel ranks among the top 100 reporting companies in the SustainAbility / UNEP / Standard and Poor's Global Reporters 2004 Benchmark Survey of Corporate Sustainability Reporting.

In India there are various drivers behind the increase in dialogue, discussion and publication of sustainability reports, drivers that are very different

from other parts of the world. For example, pressure from the NGO sector is low in India when compared to other countries. Pressure originates rather from increasing involvement in the global business environment.

An increasing number of companies in India use the GRI guidelines. From the Tata group, eighteen Tata companies have produced or are in the process of developing sustainability reports. Other GRI users include Dr. Reddy's Laboratories, Ford India Limited, Paharpur Business Centre, Jubilant Organosys and ITC. Others such as Toyota Kirloskar Motors Pvt. Ltd. and Sony India Pvt. Ltd. are also issuing CSR reports.

In summary, the main challenges for sustainability reporting in India are the following:

- Lack of a specific sustainability/CSR reporting legislation or guidelines;
- Companies find it challenging to report how they conduct business in the absence of clear guidance based on local conditions;
- Following early experimentation, efforts need to be focused and standardized. Typically companies tend to report their community initiatives on a few pages in their Annual Reports, rather than providing detailed information on internal practices and issues such as transparency, risk, and social or environmental impacts; and
- Synergizing social and business interests needs top priority. Corporate philanthropy needs to transform into the realm of core business and corporate social responsibility.

5.5 Japan

Japanese companies are among the top performers globally in terms of environmental management systems and publishing sustainable development reports.

- In 2004, a total of 7,155 companies were certified under ISO 14001. This makes Japan by far the leading economy in this field, ahead of Germany in second place with 2,500 certifications (Hibbit, 2004: 521).
- With regard to the relative numbers of sustainability reports from the largest companies by country, Japan takes the lead with 72% of the top 100 Japanese companies reporting. This is substantially higher than for example

the 49% in the UK and 32% in Germany (Hesse, 2004: 48).

- Japan has the greatest number of companies using the GRI Guidelines (available in Japanese) and has an active GRI national forum.
- Japanese companies are notable in that most of their reports conform to published guidelines – whether governmental or GRI – enabling effective comparison (ACCA and CorporateRegister.com, 2004).
- Japanese companies voluntarily report environmental policies, achievements and costs but do not consistently provide hard data on emissions, energy use and water, and also need to improve reporting on social performance.

The reporting regime

With the exception of some environmental issues, there are no mandatory accounting or company law requirements for sustainability issues to be covered in annual accounts or reports, or stand-alone reports in Japan. Early publication of guidance by the Ministry of the Environment (Eco-Friendly Corporate Activity Indicators, 1992) and The Voluntary Plan (1992) of the Ministry of the Economy, Trade and Industry are believed to have had a remarkable influence in promoting the production of environmental reports (ACCA 2004).

In 2001 the Japanese Ministry of Environment published formal guidelines referring to environmental issues, consisting of three parts:

Environmental Reporting Guidelines; Environmental Accounting Guidelines and Environmental Performance Indicator Guidelines.

The latter two parts of the guidelines are of particular importance for the financial and economic aspects of reporting and disclosure. They tend to establish on a quantitative comparative basis the assessment of environmental costs (monetary) and the physical impact of environmental protection actions companies have undertaken. The content of the reporting is therefore similar to the eco-efficiency indicators developed for and published in a manual by UNCTAD-ISAR (Hesse, 2004: 48; UNCTAD, 2004).

The environmental guidelines are to be used in the preparation of stand-alone reports. The document provides comprehensive guidance on environmental reporting and was drafted by a committee of twelve individuals with a strong representation of the accountancy profession, business and academia.¹¹

No regulatory or political pressure has been placed on Japanese companies, and no plans exist to force Japanese companies to follow the guidelines. The guidelines make no recommendation on whether the companies should report site-based, regionally or globally or seek external verification. However, the Japanese Ministry of Environment plans to establish a third party review scheme for environmental reports on a voluntary basis. It is estimated that the number of environmental reports published for domestic corporations

larger than SMEs will increase within the short term. Japan is now planning to establish a simplified certification scheme for SMEs, which will require the publication of public environmental reports (ACCA and CorporateRegister.com, 2004).

The success of the entirely voluntary system in Japan has been explained in the context of social and cultural considerations, such as the close working relationship between major Japanese companies and the government, as well as the importance for many companies of setting a good example.

5.6 South Africa

South Africa is one of the few developing economies and the only country in Africa that shows significant reporting activities (ACCA and CorporateRegister.com, 2004). It has included some finalists in the Global Reporters benchmark surveys published by SustainAbility and UNEP over the last four years. In part due to its political history and transition to democracy in the 1990s, the country has taken a leading role in the sustainability reporting movement. There is increasing support from the business community, financial institutions and government, and a growing recognition of the GRI guidelines and the country's own reporting regime.

According to KPMG annual surveys on sustainability reporting trends in South Africa over the last ten years, corporate sustainability has steadily shifted from an initial focus on philanthropy and environmental management towards the inclusion of health, safety, labour,

¹¹ An English version of the guidelines is available at www.env.go.jp/en/index.html.

community and broader socio-economic issues. The 2004 survey determined that improvements have been made on the level of disclosure on sustainability issues, including significant levels of reporting on employment equity, ethics and corporate social investment. However, significant room for improvement continues to exist with respect to issues such as the frequency and severity of environmental incidents, accounting for the value of CSI contributions and levels of preferential procurement.

Current reporting practice

Sustainability reporting trends by the top 100 companies in South Africa						
	1997	1998	1999	2000	2001	2002
<i>Annual financial reports</i>						
Environment	48%	49%	52%	55%	49%	68%
Health and Safety*				52%	40%	68%
Social/community investment				60%	45%	68%
Human capital development				84%	87%	68%
Code of ethics/conduct				81%	–	78%
Sustainability issues				57%	–	85%
<i>Separate public reports</i>						
Sustainability reports				10%	16%	20%

*2000, Top 100 Industries (source, KPMG)

KPMG South Africa: 2004 Sustainability Reporting Survey

An increase in corporate social responsibility awareness and activity and sustainability reporting, and the emergence of an effective reporting regime, is underpinned by a commitment to transformation in South Africa. The Apartheid boycott debate of the 1980s has been a factor in inspiring the social responsibility, accountability, transparency and disclosure debate driven under the Sullivan Principles initiative and others in the USA.

This emerging market economy is still going through an economic transition following its political transition to a democratic government in 1994. There remains extreme disparity in the distribution of wealth, with thirty to forty percent of the population unemployed. There are also strong labour laws protecting employees, supported by the largest labour confederation, COSATU.

South African companies with dual listings on the London Stock Exchange are required to comply with the more rigorous corporate governance requirements in the UK.

In order to address the lagging economic transformation, the South African government has among others, issued a mining charter and a financial sector

charter. Mining rights are duly reflected in the charter compliance requirements. In terms of the financial sector charter, the key issues that management has to address are: ownership and control of companies, human resource development, procurement, corporate social investment, access to financial services and empowerment financing. Adherence to the charter is closely monitored by the government.

The Second King Report on Corporate Governance

The Second King Report on Corporate Governance 2002 (known as King II) represents a formal review of South African corporate governance arrangements, similar to the Combined Code in the UK. It lays down key principles for use in reporting, with reference to the GRI Sustainability Reporting Guidelines. A key section of the code, referred to as Integrated Sustainability Reporting, states that:

“every company should report at least annually on the nature and extent of its social, transformation, ethical, safety, health and environmental management policies and practices.”

The Second King Report also specifies matters requiring particular consideration, including:

- Health and safety practices (including HIV/AIDS);
- Environmental governance, including use of Best Practice Environmental Option Standard;

- Social investment and black economic empowerment;
- Human capital development and equal opportunity; and
- The development and implementation of a company Code of Ethics, and disclosure of adherence to that code.

Compliance with certain aspects of the King Report has been made compulsory for listed companies (such as the separation of Board Chair and CEO positions) while compliance with other aspects such as non-financial reporting are not compulsory. In all cases, listed companies have to report on whether they comply with the recommendations of King II and if not, why not, exposing listed company practice to public scrutiny. In addition, there is no clear preference for glossy, stand-alone reports, although the use of the GRI is encouraged.

Disclosure and Accounting standards

In addition to King II, steps have been undertaken to set South African Accounting standards in compliance with the International Accounting Standards. All Johannesburg Stock Exchange (JSE) listed companies must comply with these generally accepted accounting principles which include the recognition of environmental and social risks, similar to those of IAS 36, 37 and 38.

JSE SRI Index Listed Companies

The JSE Socially Responsible Investment (SRI) index, launched in May 2004, is the first SRI index in an

emerging market. It can be compared to national indices such as the Ethibel Sustainability Index (Belgium), Humanix Ethics Index (Sweden), FES (Spain) and international indices such as Eurosif (Europe), the Dow Jones Sustainability Index (DJSI) and the FTSE4Good Index.

The JSE SRI index was developed as a means of measuring company policies, performance and reporting in relation to corporate governance and the triple-bottom-line. All 154 companies listed on the FTSE/JSE All Share Index were invited to participate in 2004, with 74 companies choosing to participate and 51 companies being accepted onto the index. In the 2005/6 cycles, 59 companies qualified to be included on the Index. The JSE SRI Index has acted as a significant motivator for companies to increase their reporting on sustainability issues, with many companies producing their first stand-alone sustainability reports specifically to obtain listing on the index.

Summary

South Africa has chosen a combined approach to encourage reporting on sustainability issues: the integration of mandatory, new generation, international accounting standards into its financial reporting practices, as well as a self-regulatory, triple bottom line reporting approach that makes sustainability reporting mandatory for all listed companies (through the application of a "comply or explain" approach) whilst encouraging the voluntary use of the GRI guidelines. Speaking at the launch of the 2nd revised version of the GRI Guidelines

at the World Summit on Sustainable Development (WSSD) in Johannesburg in 2002, Mervyn King (chairperson of the IOD's King committee) indicated that he foresees more governments introducing mandatory requirements on sustainability reporting, but that the "how" or format of reporting will probably be left to voluntary choice by the reporting organisation.

5.7 United States of America

Non-financial reporting originated in the USA in the late 1980s in response to the disclosure of a wealth of publicly available information driven by legislation (the 'right to know' legislation).

In the USA, the Coalition for Environmentally Responsible Economies (CERES) has played a pivotal role in advancing the notion of environmental, and later sustainability, reporting since its formation in 1989. The Sullivan Principles also encouraged USA multinationals to report progress on activities to advance social responsibility. Pressure from socially responsible USA investors was another factor in pushing the growth in reporting throughout the 1990s. The number of companies reporting rose steeply between 1990 and 1995, but in recent years has reached a plateau. Since 1995, the proportion of reports with external assurance has doubled, although this figure is low in comparison with other parts of the world. Institutional investors, including

pension funds, are playing a leading role in promulgating the non-financial reporting agenda. This often involves using proxy voting policies to encourage public companies to disclose material environmental and sustainability information. USA companies are also driven by the desire to reduce the burden of filling out duplicative investor surveys (ACCA and CorporateRegister.com, 2004).

The USA system for reporting and disclosure on sustainability issues is dominated by the disclosure requirements stated by the Securities and Exchange Commission (the SEC) – an example of a statute-based self-regulatory mandatory reporting regime for companies. In this case study we explore some of the advantages and disadvantages stated in the light of the above. It is intended to be of particular relevance to the debate on whether to delegate regulatory power to the stock exchange control.¹²

The USA is globally the most important capital market and has the strictest rules for disclosure of information by listed companies. Disclosure of information is one of the pillars of USA securities regulation. As early as 1971 the SEC demanded disclosure of environmental data in SEC filings.

Empowerment/mandate of the SEC

The basic USA securities laws authorize the Securities and Exchange Commission to require the disclosure of information "necessary or appropriate in the public interest or for the protection of investors" (Securities Act, Section 2b). This mandate applies

to information disclosed in conjunction with the registration and public offering of securities, solicitation of proxy votes, and periodic public reporting.

Disclosure requirements thereby serve a dual purpose: protecting investors from fraud and inefficiency in the pricing of securities and promoting responsible corporate management.

The public interest mandate of the Securities and Exchange Commission has been extended with the National Environmental Policy Act (NEPA) of 1969, (Public Law 91-90, 83 Stat.852, 42USC§4321 et seq.1970) which states that the protection of the environment is a national policy. Congress hereby authorized and directed the Securities and Exchange Commission, as a federal agency, to include environmental protection in its mandate to issue regulations in the public interest. The Conference Report to NEPA states that while NEPA does not repeal existing legislation and is supplemental to the authorization of federal agencies, "this section does not, however, obviate the requirement that the federal agencies conduct their activities in accordance with the provisions of this bill unless to do so would clearly violate their existing statutory authorizations" [Conference Report 91-765, 91st Congress, 2 US Code and Administrative News, 2767, 2771-2 (1969)].

The SEC was thus directed to take environmental protection into account when enacting disclosure requirements and other securities regulations, other than when this is

¹² In this section, special recognition is given to the work of Repetto et al (2002), as well as the excerpt of the UNEP FI conference on Environmental Disclosures in North American Financial Statements (2003) and "Open Disclosure" by Mark Mansley (2004), as well as a speech by Simon Thomas from the Environmental Law Institute on 19 January 2005.

clearly incompatible with the protection of investors and the promotion of efficiency, competition and capital formation. In the settlement of a case arising from a rule-making petition brought against the SEC by the Natural Resources Defense Council, on the issue of whether the SEC should require broad disclosure of environmental information, a USA District Court determined that NEPA did not impose any specific mandate on the SEC to require environmental disclosure but did compel it to take environmental considerations into account.

The SEC definition of materiality

In addition to extensive specific disclosure requirements set forth largely in Regulation S-K, the SEC Acts administer a far more general obligation on companies to disclose all material information, in order to avoid misleading statements. Companies and their officers can be penalized for presenting false or misleading facts or omitting to disclose a material fact, including criminal prosecution, civil penalties, withdrawal of registration, and liability to investors suffering as a result. In 1975 the SEC clarified its position that the disclosure of material environmental information is required under securities law and that this requirement would be enforced (SEC, Securities Act Release No. 5627; 14 Oct. 1975).

A materiality filter has been applied to much information that is specifically required to be disclosed, including environmental information. The SEC explicitly states in the SEC Staff Accounting Bulletin No.99 that

numerical benchmarking cannot be relied upon as a materiality threshold. Rather, "a matter is material if there is a substantial likelihood that a reasonable person would consider it important" [17CFR§211, 12 August 1999]. The Bulletin quotes a decision by the USA Supreme Court that a fact is material if there is a substantial likelihood that the fact would have been viewed by a reasonable investor as having significantly altered the total mix of information made available [TSC Industries v. Northway, Inc, 426US 438, 449 (1976)].

The Bulletin cites examples of misstatements or omissions that might be material although quantitatively small in financial terms. Among these are misstatements bearing on the integrity or competence of management, such as a company's compliance with environmental regulatory requirements (Repetto, 2002).

There is considerable debate in the USA around the issue of materiality. Despite the SEC guidance that the qualitative information can be material, companies readily point to "materiality" as an explanation for limited disclosure of information on environmental and social factors. This is compounded by the fact that the USA case law states that in the absence of a specific regulation to disclose defined information, it is difficult to press companies to disclose on the basis of general principles (Mansley, 2004).

However, the SEC often applies the following rule of thumb regarding

materiality. If the amount at issue is more than 10% of the number against which it is measured, then it is material; if it ranges from 5–10% of the number against which it is measured, it may but often not be material; and if it is less than 5% of the number against which it is measured, it is presumed not material (UNEP FI, 2003).

5.7.1. The SEC Disclosure System

In order to fulfil this broad mandate the SEC has issued regulations, instructions, interpretative and explanatory releases that have created an extensive and highly integrated disclosure system.

Environmental disclosure in the S-K Filings for listed USA companies

These disclosure requirements (Regulation S-K [CFR§§229.10 – 229.702(1998)]) consist of a basic information package that must be disclosed to all investors as well as additional in-depth information that is presumed to be of interest primarily to securities analysts, institutional investors and sophisticated individual investors.

These requirements have been standardised to a large extent in a number of disclosure stages specified in the Securities and Exchange Acts: i) information in a prospectus or similar document; ii) information contained in a statement accompanying the registration of securities with the Securities and Exchange Commission; iii) information contained in proxy solicitations in conjunction with the

election of officers and votes in annual meetings; and iv) information contained in required annual, quarterly, and special ongoing reports filed with the SEC and made available to the public.

Some disclosure requirements apply specifically to information of an environmental nature but do not preclude the firm's obligation to comply with the more general requirement that all material information must be revealed (SEC Release No. 33-6130; 44FR56925). For example, if a company publicly discloses its environmental policies, it must ensure that statements made are accurate and sufficient to make the information not misleading.

Item 101

Item 101 of Regulation S-K requires companies to disclose any material effects that compliance with any enacted or adopted environmental regulations will have on capital expenditures, earnings and competitive position for the current and next year, and any future years for which the impacts might be material.

Item 101 c) xii) of Regulation S-K specifies:

“Appropriate disclosure also shall be made as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries. The registrant shall disclose any material estimated capital expenditures for environmental control facilities for the remainder of its current fiscal year and its succeeding fiscal year and for such further periods as the registrant may deem material.”

In an interpretive release, the SEC made it clear that in the future, companies may have to determine and disclose estimates of environmental compliance costs if they expect such costs to be material and significantly higher than current costs (SEC Release No. 33-6130; 44FR56924, 3 Oct. 1979).

Item 103

In addition, though not targeted exclusively at litigation arising out of environmental matters, Item 103 of Regulation S-K requires disclosure of pending material legal proceedings:

“Describe briefly any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject. Include the name of the court or agency in which the proceedings are pending, the date instituted, the principal parties thereto, a description of the factual basis alleged to underlie the proceeding and the relief sought. Include similar information as to any such proceedings known to be contemplated by governmental authorities.”

The instructions to Item 103 stipulate, inter alia, that

...No information need be given with respect to any proceeding that involves primarily a claim for damages if the amount involved, exclusive of interest and costs, does not exceed 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis

"...Notwithstanding the foregoing, an administrative or judicial proceeding ... arising under any Federal, State or local provisions that have been enacted or adopted regulating the discharge of materials into the environment or primary for the purpose of protecting the environment shall not be deemed "ordinary routine litigation incidental to the business" and shall be described if:

A. Such proceeding is material to the business or financial condition of the registrant;

B. Such proceeding involves primarily a claim for damages, or involves potential monetary sanctions, capital expenditures, deferred charges or charges to income and the amount involved, exclusive of interest and costs, exceeds 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis; or

C. A governmental authority is a party to such proceeding and such proceeding involves potential monetary sanctions, unless the registrant reasonably believes that such proceeding will result in no monetary sanctions, or in monetary sanctions, exclusive of interest and costs, of less than \$100,000...."

Item 303 Management Discussion and Analysis

Another Regulation S-K disclosure requirement with considerable potential significance for environmental information is Item 303. This specifies the requirements for the Management Discussion and Analysis, a narrative explanation that accompanies the financial reports. It requires a disclosure and discussion of any known trends, commitments, events or uncertainties that will have a material effect on the firm's financial condition or operation results. This shifts the burden of proof onto management, in that known uncertainties must be disclosed unless management can determine that a material effect "is not reasonably likely to occur" (SEC Release No. 33-6835; 54FR22430, 24 May 1989).

Environmental disclosure for foreign listed companies

For foreign listed companies a different approach is taken. In form 20-F, which specifies listing requirements for foreign companies, firms are requested to: "Also describe any environmental issues that may affect the company's utilization of the assets."

It is this rather broad statement that caused BP to make the following disclosure in its annual report to the SEC for the fiscal year ended 31 December 1998:

"In December 1997, at the Third Conference of the Parties to the United Nations Framework Convention on Climate Change in Kyoto, Japan, the participants agreed on a system of differentiated internationally legally binding targets for the first commitment period of 2008-2012. The range in Annex I countries (OECD, former Soviet Union and Eastern Bloc countries) is from -8% to +10%. The USA agreed on a reduction of 7%, and the European Union on a reduction of 8%, on 1990 levels of emissions of greenhouse gases. Projections of the increase in emissions without any reduction measures are estimated at 32% for the USA and 19% for the European Union. If these targets are to be met a major reduction in the use of fossil fuels would be required, and this would be likely to have a significant effect on BP Amoco's main businesses, but the Group does not expect that it will be affected differently from other companies with comparable assets engaged in similar businesses."

Significantly, BP did not make any such disclosure in its annual reports in the UK. It is believed that there are several other examples of UK companies providing more extensive disclosure of environmental risks in their reports to the SEC than is provided in their UK annual reports.

The SEC also mentions the environment in its industry guides, although only for the real estate sector. Despite the fact that smaller companies have a less onerous set of reporting requirements generally, they are still required to report on environmental matters.

Sarbanes-Oxley Act

Following the corporate scandals of Enron and Worldcom reporting and disclosure requirements in the USA were elaborated with the introduction of the mainly corporate governance focused Sarbanes-Oxley Act into SEC regulations. Though it does not explicitly regulate the disclosure of environmental or social information it could enhance transparency and liability by influencing the obligation to report and disclose sustainability information.

Relevant sections of the Sarbanes-Oxley Act are:

- Section 401 requiring Disclosure of Material Correction Adjustments and Disclosure of Off-Balance Sheet Transactions;
- Section 404 requiring Disclosure of Management Assessment of Internal Controls; and
- Sections 302 and 906 requiring Officer Certification Requirements.

Environmental Co-Operative Agreements

An innovative development in the USA is the use of voluntary reporting guidelines within contractual arrangements between government

and industry. In Wisconsin, an environmental co-operative agreement was signed in February 2001 between the private utility Wisconsin Electric and the Wisconsin Department of Natural Resources. It requires Wisconsin Electric to prepare an annual environmental performance report in accordance with GRI Sustainability Reporting Guidelines. As part of the agreement, Wisconsin Electric must demonstrate measurable improvements in environmental performance, implement an environmental management system and expand its stakeholder involvement program. In exchange, Wisconsin Electric will benefit through permit streamlining, alternative monitoring and more flexible operations. According to the GRI Secretariat, this is the first specification of the guidelines in a legal agreement.

Summary

At the most fundamental level, USA disclosure requirements require that all material information regarding securities offered for sale to the public must be promptly revealed. Material information is commonly defined as information that investors would regard as significant in their decisions to buy or sell a security. Materiality is broadly defined and not subject to numerical thresholds. In the USA, information that has a bearing on the competence or integrity of management, including non-compliance with extant laws and regulations, can be material even if financially insignificant. The securities regulations of the USA are mandatory in the public interest.

Through the National Environmental Policy Act the public interest is defined to include environmental protection and the responsibility of the SEC is extended to take environmental objectives into account when formulating rules and regulations.

However, there is little evidence in its actions that the SEC has accepted a broader responsibility other than to protect investors and to promote efficient capital markets. There has rarely been environmental enforcement by the SEC. The SEC disclosure requirements are litigation-oriented and the wording used in the regulations is often subjective.

The review of disclosure requirements relating to environmental information in the securities regulation of the USA reveals essential similarities and particular differences in relation to other reporting regimes described in this report.

The reporting requirements that have emerged from the UK Operating and Financial Review (OFR), the Business Review, and the EU Accounts Modernisation Directive have distinct synergies with the system that has existed within the USA for at least 25 years. The EU Modernisation Directive also requires an assessment of environmental factors "to the extent necessary" for shareholders to understand the factors underlying the performance of the business over the past year and the main trends and factors likely to affect future performance. This is very similar to the SEC 10-K filing requirement that the

Management Discussion and Analysis (MD&A) include environmental matters in instances where the reporting of these would "alter a reasonable investor's view" of the reporting entity. It is also apparent that in the Directive as well as its transposition into national law in the EU member states, materiality is defined in terms of the interests of shareholders.

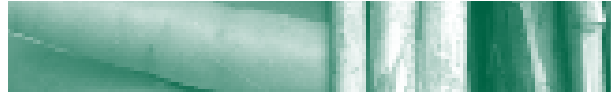
The key issue in both the USA and Europe is establishing materiality when the costs associated with corporate consumption of environmental goods and services are largely external and are therefore not captured by conventional accounting standards. Where environmental costs and liabilities are evident, such as land remediation costs, existing accounting standards regarding provisions, liabilities and the impairment of assets should ensure that they are disclosed. However, where the costs are uncertain or external, the disclosure requirements in the EU and the USA allow directors considerable discretion as to whether they should be reported or not, which impacts on the levels of environmental reporting.

The discretion afforded to directors in these matters lends itself to a diverse approach to reporting on environmental performance. This makes it distinctly challenging for stakeholders to make meaningful comparisons between companies on the basis of environmental performance.

Overall, the USA example of environmental disclosure demonstrates several important aspects.

Firstly, it is significant that the largest financial regulator in the world recognises the importance of environmental factors and requires some disclosure. Secondly, the concept of a link to other regulators, such as the EPA, is valuable and innovative. Finally, however, the USA experience highlights the difficulties of a rule-based approach to environmental disclosure. The fact that materiality will be frequently used as an excuse not to disclose, is an argument for stronger guidance.

6. Conclusion: Where to start...



There is the story of a traveller who needed directions to a town he wanted to visit. He lost his way on one of the many dirt roads in a rural area, and approached one of the locals to direct him to where he wanted to be. After many attempts to explain the route, and with the local also getting increasingly confused, he finally said: "Sir, if I wanted to go there, I wouldn't start here!"

Reaching the destination of increased quantity and quality of sustainability reporting will be a complex journey, and no-one can choose their point of departure. The journey will be different for every country, depending on what exists already in terms of regulation and buy-in from different stakeholders, as well as the decision on what would be required in terms of the final destination.

These decisions should be informed by, amongst others, the following:

- A familiarity with sustainability reporting, including the main drivers for reporting as well as the current consensus on what would constitute best practice. This requires realisation of the potential value of reporting not only as a monitoring and accountability mechanism, but also as part of a performance process and management instrument that can be used as an internal diagnostic tool to enhance performance;

- An understanding of the main global standards that are currently driving reporting processes. The GRI has clearly established itself as the main reference in terms of providing a reporting framework, and is supported by other complementary standards such as AA1000. A new ISO 26000 standard on Social Responsibility, currently under development, may also recommend communication in the form of sustainability reporting. The standard-setting environment also has a competitive component, hopefully always within the "cooperating to compete" framework. Organisations should realise that a leading position is not guaranteed indefinitely. Continuous cooperative efforts to find better solutions, as well as critical assessments of new standards or contributions will benefit all reporters worldwide;
- A realisation that reporting is only the tip of the iceberg and that – for both reporter and legislator – the emphasis should be on performance; and
- The knowledge that the voluntary versus mandatory debate does not imply an "either / or" position, but rather finding a balance between regulation in certain high risk or

high impact areas, and allowing industry associations or individual companies to make decisions in other areas.

When one looks at how sustainability reporting has evolved over the last few decades, it should also be clear that current best practice does not necessarily present a blueprint for the future. Critical debates about the future of sustainability reporting should be encouraged, and should not be constrained by current reporting formats and procedures. For example, if sustainability reporting will be fully integrated with financial reporting in the future, it is conceivable that core indicators will evolve over time and that it would be possible to present them in an annual report alongside the income statement and balance sheet (perhaps through the introduction of a balanced sheet!). At the same time, what is currently known as a sustainability report (i.e. a standalone hard copy or online report) is likely to evolve into a process of sustainability communication. This might lead to the overall integration of sustainability reporting with financial reports, the replacement of a standalone report by a series of shorter reports, fact sheets, position statements and stakeholder engagement processes. Clearly, such developments will have a severe impact on the ability of governments to regulate in this area. For an organisation like the GRI these potential developments will also present some real opportunities, but also tough choices.

Convergence between financial and non-financial reporting raises the

question of reporting "on what?" and "to whom?". With respect to the what, the GRI provides an internationally recognised, comprehensive index of current consensus on what should be measured in the process of organisation-level sustainability reporting. Yet whilst the distinction between core performance indicators and additional performance indicators as well as industry sector-specific supplements provide some further guidance on selection, it is still up to each reporting organisation to decide what is most "relevant" or "material" for it to report on. To start with, industry best practice and governmental legislation on individual issues make reporting against certain disclosure items and fundamental indicators a given. Beyond this, the level of detail of disclosure and addition of information on other disclosure items and indicators, as well as the format in which it is presented, becomes a matter of preference from the view of the supposed target audience or report user (the whom). It is here that the "level of significance" or "perceived relevance / materiality" of certain issues and indicators often depend on the stakeholder category and background of the potential report user. This applies to report users externally and internally.

The following table sets out different functional areas and related stakeholder categories within the market and society, the enterprise and government.

<i>Market and Society relevant stakeholder group</i>	<i>Enterprise (firm, corporation, company) relevant department/division</i>	<i>Government (local, national, supranational public authority) relevant ministry/department</i>
Credit providers, investors, stock exchange	Shareholders, Finance, Accounts	Finance, Treasury
Labour confederation	Human Resources	Labour, Health, Education
Research community	Research & Development	Science & Technology
Partners (incl. supplier network), clients, business organisation, industry association	Operations and Logistics, incl. sourcing, purchasing, supplies, sales	Trade, Commerce, Industry, Energy, Natural Resources, Environment
Environmental NGOs	Environmental Management	Environment
Consumers and community organisations, media	Marketing, Communications, Public Relations	Consumer Protection, Welfare

Table 1: Different providers and users of reported information, inside and outside the enterprise

The above table serves to remind us of the different users of reported information, all with different interests depending on their background and where they operate. Users from the same interest and operational area are likely to share special interest in reporting against similar indicators and disclosure items. The company environmental manager, environment ministry official and environmental NGO representative may very well have the same passion for the environment and certainly a greater shared understanding for environmental issues compared to the financial manager.

This highlights the challenge of integration and communication across work areas that the sustainability reporting – financial reporting debate poses.

The financial accountant may display very little understanding for environmental management, and may only begin to understand as environmental risk translates into financial risk, liabilities and losses (or profits) as a result of penalties, fines and law suits (... or making inroads into new environmental services and niche product markets). This grey area – overlap between the green and the red - is one that has been grappled with by both UNEP and UNCTAD's Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) since the early 1990s (see UNCTC ISAR, 1991 and UNEP IE, 1994).

We therefore see the need to bridge the gap between communities of expertise, which needs to happen within business as well as within government. It refers to, by example, the gap between "accounting for the environment" or "full cost / green accounting" on the one hand and on the other hand, disclosure on

environmental issues through annual accounts according to company law and accounting GAAP. The one is interested in the environment and material efficiency, whilst the other is interested in the environment only insofar as it manifests itself in affecting the financial measurement of economic events at a material level (Gray and Bebbington, 2001: 222).

The related question for the company director and the public regulator is whether reporting on a sustainability issue should be done on the basis of a risk-avoidance strategy, on the basis of a business case, on the basis of decision-usefulness or on the basis of the "community right-to-know". As highlighted in corporate governance discussions so often in recent years, the dilemma for the company directors is the extent to which their fiduciary responsibility to their shareholders requires them to ignore or incorporate long term sustainability-related, non-financial information in the Annual Report. This dilemma has been central in the debate in the UK over the last two years surrounding the development of the Operating and Financial Review (OFR) and the Business Review as required under the EU Accounts Modernization Directive.

"In 1990, two years before the first Earth Summit... Government support for public reporting did not exist. Few, if any, governments were aware of the importance of non-financial reporting or were forward thinking enough to encourage companies to take responsibility for their environmental and social impacts... (Today) the picture has changed completely. Environmental reporting is no longer news... mandatory environmental reporting has been introduced in some countries, including Denmark, France, The Netherlands, Norway and Hong Kong... Non-financial reporting guidance provided by government has led to higher quality reports emerging from those countries... governments can play an instrumental role in stimulating a culture of reporting and providing national frameworks..."

(ACCA and CorporateRegister.com, 2004: 10, 12, 16).

The regulator may take a decision against mandatory legislation requiring comprehensive sustainability reporting. Yet the viability of most regulatory instruments is substantially dependent on the availability and quality of relevant information. The practical application of economic instruments is heavily reliant on information, for example about the quantity of emissions (Gunningham and Grabosky, 1998: 82). Running certain economic instruments may require the introduction of mandatory reporting for monitoring purposes. Examples are pollution taxes and tradeable permit schemes. In the case of the latter, government needs to ensure reliable measuring, accounting, auditing and reporting of emissions, as well as accurate record keeping of the location and monetary value of permits. This brings us back to the role of variants of product-based, issue-based and site-based reporting, and the desirability or feasibility of linking these requirements up into a comprehensive reporting framework.

Arguing a confining case for policy mixes that incorporate a broad range of instruments and institutions, as well as the principle of low interventionism in the design of regulation, Law Professor Neil Gunningham (1998: 191) advises as follows: "...a number of measures should be seen as prerequisites for government to successfully regulate large companies at a distance, giving them the flexibility they demand, while achieving both improved environmental and economic outcomes, and community acceptance".

The measures he sees as prerequisites are the following:

- Measuring outcomes by independent and transparent performance indicators;
- Independent third party oversight underpinned by access to information;
- Community empowerment, including the transparency and institutionalised dialogue necessary to bring this about;
- Government oversight and an underpinning of effective sanctions, and
- Credible incentives for industry participation.

In the context of reporting, these prerequisites again highlight the importance of a publicly recognised set of performance indicators (of which the GRI provides a global reference framework), independent verification, stakeholder engagement in for example determining what is relevant or material, the role of government in enforcing a level playing field and, last but not least, the importance of incentives.

To conclude, we suggest that the following actions could be considered by public officials:

- Detailed review of existing legislation and other regulatory requirements with reference to the following:

- Comparison with GRI sustainability reporting requirements (principles, disclosure items and sustainability indicators, stakeholder engagement and due process)
- Distinction between duty to disclose information to government and public disclosure;
- Evaluation whether existing company law encourages only conventional, historical cost accounting or also encourages forward-looking, strategic reporting on business prospects (trends, factors affecting future performance), business drivers and risks; and
- Current practice with regards to external auditing / verification / assurance.
- Detailed review of quantity and quality of sustainability reporting in the specific country, as well as ensuring that relevant government departments remain up to date with the latest developments in the field of sustainability reporting;
- Consideration of draft legislation: governments that contemplate introducing some form of legal requirement for sustainability reporting have many options available, including the following:
 - Stipulating a basic minimum requirement of sustainability

reporting and making such reporting compulsory through a "comply or explain" arrangement;

- Delegating the responsibility to make decisions in this regard to stock exchanges and / or industry associations; or
- Introducing incentives for corporations to issue sustainability reports.

The introduction of incentives seems to be of particular interest, given the complexities of existing legislation and the unlikelihood that regulators will be able to incorporate all forms of existing legal requirements, combined with areas where there are gaps, into new legislation. The latter task will be too complex and the issue is – at least currently – not perceived to be critical enough by all decision-makers to warrant this. Examples of possible incentives include the following:

- If a sustainability report is issued companies could be relieved from the obligation to report separately to individual government departments, provided that they include all appropriate indicators in their report – the issue of whether such reports would have to be verified externally would have to be discussed; and
- Relief from litigation – based on the example of the Federal Sentencing Guidelines in the USA - companies could

perhaps qualify for reduced fines in cases where they have publicly disclosed material sustainability risks in sustainability reports and clearly indicated an action plan for addressing such risks.

Finally, there is the issue of collective governmental action to consider. Within this context, participation in intergovernmental discussions and initiatives should be encouraged, with specific emphasis on the need for governments with substantial experience in this area to share their experiences and know-how with others. The role of institutions such as the United Nations and the GRI will be critical to help ensure informed discussions, continued success and progress in this area.

When in May 2005 the UNEP Division of Technology, Industry and Economics hosted a workshop on reporting policy and legislation trends with representatives of a group of OECD governments and the emerging market economies covered in this report, participants had two concluding messages:

- Firstly; in developing countries much awareness raising and capacity building remains to be done on non-financial reporting as a management tool and as legislative subject. In many developing countries pressure for non-financial disclosure from the finance and investment community is still non-existent.

- Secondly, participants noted the need to improve the links between micro-level / company reporting, national / macro level reporting and international / global level reports and institutions (e.g. international agreements and UN declarations on issues such as the Millennium Development Goals). They welcomed the fact that the GRI has incorporated and integrated many elements of key international texts into its principles and guidelines.

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