Journal of Management and Sustainability; Vol. 5, No. 2; 2015
ISSN 1925-4725 E-ISSN 1925-4733
Published by Canadian Center of Science and Education

# Sustainability Reporting: An Accountant's Perspective

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Received: April 11, 2015 Accepted: April 28, 2015 Online Published: May 31, 2015

doi:10.5539/jms.v5n2p92 URL: http://dx.doi.org/10.5539/jms.v5n2p92

**Abstract**

The current state of sustainability reporting lacks useful information for decision-making. Specifically, this paper examines the sustainability report of a major multinational organization from the perspective of accounting and the qualities of information as defined by the U.S. Financial Accounting Standards Board and the Global Reporting Initiative. Fifty-eight graduate accounting students were assigned an exercise that involved analyzing Wal-Mart's 2013 Corporate Social Responsibility report within the context of the GRI's Principles of Quality Reporting. The results indicated that the Report failed to provide useful information for stakeholders and was more of an instrument of public relations. While the Report failed to meet many of the GRI's Principles, the students believed the most serious flaw was the absence of cost and segment information. Without mandates the only viable mechanism to improve sustainability reports is for GRI to certify those reports that strictly adhere to the Principles of Quality Reporting.

**Keywords:** sustainability, sustainability reporting, sustainability reporting qualities, corporate responsibility reporting

## 1. Introduction

Assume that a publically traded company has eight manufacturing facilities worldwide. One of their facilities is a coal-fired facility that accounts for 35% of the Company's carbon footprint. The Company has settled several substantial lawsuits brought by the EPA. The Board of Directors is currently entertaining options presented by upper-management regarding the future of the facility.The first option is to sell the facility, assuming a buyer can be found. The second option is to retrofit the plant to meet current environmental mandates. A third option is to continue operations as usual. The fourth option is to simply shutdown the plant and shift manufacturing to another facility or discontinue the product line. Upper-management has completed and presented to the Board an evaluation of each alternative using such investment techniques as internal rate of return, payback and net present value

Each alternative would materially affect the stakeholders. The effect differs depending on the stakeholder group. For example, an employee could lose their job, a city lose tax basis and revenue generated by the facility, shareholders' earnings per share and dividend distribution could be either increased or decreased, and creditors could be affected, particularly if the Company is close to any debt covenants. Where would a stakeholder uncover information regarding such a business decision? The financial statements may not disclose the information since no recordable event has occurred and disclosure is not required since the Board has not taken any action as they are only evaluating possible alternatives. The Company's Sustainability Report is unlikely to disclose the alternatives being considered.as there are no guidelines requiring this type of disclosure. Most sustainability reports would not disclose this type of information. A review of many sustainability reports listed in the GRI database revealed that most do not disclose negative events such as pending or settled litigation involving environmental or social issues. For example, Wal-Mart, the world's largest retailer does not disclose any litigation in their 2013 Sustainability Report even though in May, 2013 Wal-Mart agreed to an $81 million settlement with the EPA. Also, there were numerous instances of litigation regarding discrimination, none of which were mentioned in their Sustainability Report.

There is a notable lack of economic, environmental and societal information that would be of value to various segments of stakeholders. This appears to be the case whether sustainability information is provided in an integrated report or a standalone report. In order to achieve "buy-in" of stakeholders, and create useful information the GRI's Principles of Quality must be followed. Shareholders, creditors, and employees have a direct and immediate interest in the information provided by sustainability reports.

Shareholders purchase interest in companies in order to receive dividends and the market appreciation of the stock. Monies spent to reduce carbon footprint and other sustainability goals should be subject to the same disclosure criteria as any other financial and nonfinancial information presented by companies. An examination of current practice reveals that vital information associated with sustainability efforts are not presented. Information such as active and pending litigation related to sustainability are not presented. Therefore investors do not have the necessary information to make informed decisions regarding sustainability investments. Creditors need to consider liquidity, solvency or both to make decisions about a company's ability to meet their obligations. As with shareholders there is little information provided either in the company's financial reports are sustainability reports to measure the effect of sustainability spending to fully assess the liquidity and solvency of a company. Current practice does not yield useful decision-making information in sustainability reports.

Until total cost and benefits are quantified and presented in sustainability reports stakeholders do not have sufficient information to make informed judgments regarding the effect of sustainability spending. Without this, stakeholders must rely on subjective sources derived from public relation releases and management discussions. . Management makes decisions regarding the company sustainability position and spending unless the stakeholders explicitly express their disagreement.

## 2. Information Qualities

In statement of Financial Accounting Concept 8 (SFAC 8), Chapter 3, "Qualitative Characteristics of Useful Financial Information," the Financial Accounting Standards Board (FASB) identified the qualitative characteristics of accounting information that distinguishes what accounting information must possess to be useful for decision making. The fundamental qualities for decision-usefulness are relevance and faithful representation. To be relevant, information must possess predictive value, confirmatory value, and be material. To have faithful representation, information must be complete, neutral, and free from bias. The qualities which enhance relevance and faithful representation are comparability, verifiability, timeliness, and understandability. In SFAC 8, Chapter 1, "The Objectives of General Purpose Financial Reporting," the FASB states the purpose of financial reporting is to provide financial information about the entity that is useful in making decisions about providing resources to the entity.

The FASB's objective is to provide information that is useful for decision-making, which allows for historical and future data. A comparison of the SFAC 8 characteristics and the reporting qualities set forth by GRI reveal very similar objectives but does not yield the same results. The GRI guidelines and the current sustainability reporting practice has little to no value when predicting what an organization will accomplish in future periods. Current sustainability reporting focuses on information that provide past and current results. Table 1 describes the reporting qualities as provided by GRI.

Table 1. GRI's reporting qualities

| Quality | |
|---|---|
| Accuracy | Definition: The reported information should be sufficiently accurate and detailed for stakeholders to assess the reporting organization's performance |
| Balance | Definition: The report should reflect positive and negative aspects of the organization's performance to enable a reasoned assessment of overall performance. |
| Comparability | Definition: Issues and information should be selected, compiled, and reported consistently. Reported information should be presented in a manner that enables stakeholders to analyze changes in the organization's performance over time, and could support analysis relative to other organizations. |
| Reliability | Definition: Information and processes used in the preparation of a report should be gathered, recorded, compiled, analyzed, and disclosed in a way that could be subject to examination and that establishes the quality and materiality of the information. |
| Timeliness | Definition: Reporting occurs on a regular schedule and information is available in time for stakeholders to make informed decisions. |
| Clarity | Definition: Information should be made available in a manner that is understandable and accessible to stakeholders using the report. |

Source: www.globalreporting.org

## 3. Case Assignment

The following case exercise was administered to 58 graduate students in two classes. The students ranged in age from their 20s to their 40s. Each student had an undergraduate accounting degree or its equivalent and 52 were currently employed in accounting. They were asked to evaluate Wal-Mart's 2013 Corporate Responsibility Report from the perspective of a shareholder and creditor. Each student was given a copy of Walmart's 2013 10k submission and Corporate Responsibility Report. The case was a significant part of their final exam grade.

### *3.1 Case Assignment 1*

Evaluate the 2013 Wal-Mart sustainability report from the perspective of an investor.

For each of the following decisions rate the Report for decision usefulness.

Use the following scale.

1 = No usefulness

2 = A little useful for some decisions

3 = Useful for some decisions

4 = Useful for most decisions

5 = Useful for all decisions

Address these questions from the perspective of an investor:

1. How much does the cost of achieving sustainable goals affect earnings per share?
2. Is there a particular product or geographical segment that is producing the greatest carbon footprint?
3. How do the results presented in the report relate to other measures, such as a percentage to sales?

### *3.2 Case Assignment 2*

Evaluate the 2013 Wal-Mart sustainability report from the perspective of a creditor.

For each of the following decisions rate the Report for decision usefulness.

Does the report provide any useful information for the decision?

Use the following scale.

1 = No usefulness

2 = A little useful for some decisions

3 = Useful for some decisions

4 = Useful for most decisions

5 = Useful for all decisions

From the perspective of a creditor:

1. Does sustainability efforts affect liquidity ratios?
2. Does sustainability costs affect debt/equity ratios?
3. Is the cost of segment sustainability have a negative impact on ratios?

### *3.3 Assignment 3*

Rate the Wal-Mart Sustainability Report as to adherence to the GRI Reporting Qualities.

For each of the GRI Reporting Qualities rate how Walmart adheres/or does not adhere to the specific qualities. Use the following scale.

1 = Did not comply

2 = Sporadic compliance

3 = Somewhat complied

4 = Complied

5 = Went beyond mere compliance

## 4. Results

Table 2 provides the results of the three assignments. Assignment 3 average rating was 2.0, indicating that the information presented in the sustainability report is not particularly useful. All students believed that the report is more of a public relations ploy whether than a meaningful source of information. This conclusion is derived from the average rating of 2.5 for assignment1 and an average rating of 1.5 on assignment 2. This is partially due to the students being accountants and generally values quantitative over qualitative measuresTwo students gave a rating of 1 to assignment 3 as it pertained to the quality of "Timeliness"which when questioned stated that they had misread the scale. These were not counted in the above average. Table 3 gives the breakdown of how the students perceived the 6 reporting qualities. Again, this reinforces how little credibility accountants gives the Wal-Mart Sustainability Report

Interviews with the students after the due date for their submissions revealed that they had little confidence in the sustainability report. Generally this was due to the omission of environmental and social lawsuits that were either settled or in litigation for 2013, the amount of discretion on selecting indicators and the apparent "selling" of efforts and goals that predominated the report. Students also did not believe that the sustainability report was useful due to a lack of cost information. Students also pointed out that the length of the report (approximately 160 pages) made it very difficult to pull out needed information (that often was not there). The students did believe that using the 10K in addition to the sustainability report greatly improved the usefulness in making decisions

Table 2. Assignment results

| Assignment | Average Rating | Range |
|---|---|---|
| Evaluate the 2013 Wal-Mart sustainability report from the perspective of an investor. | 2.5 | 1 - 4 |
| Evaluate the 2013 Wal-Mart sustainability report from the perspective of a creditor | 1.5 | 1 - 4 |
| Rate the Wal-Mart Sustainability Report as to adherence to GRI Reporting Qualities. | 2.0 | 1 - 3 |

Table 3. Reporting qualities results

| Quality | Rating |
|---|---|
| Balance | 1.0 |
| Comparability | 1.5 |
| Accuracy | 3.0 |
| Clarity | 2.0 |
| Reliability | 2.0 |
| Timeliness | 4.5 |

## 5. Conclusions

Care has to be taken when reading a sustainability report. More often than not the content does not meet GRI's Principles of Quality Reporting. Wal-Mart was chosen as it is the largest retailer in the world, and presumably has sufficient funding and a management information system sufficient to extract and compile data to provide a comprehensive sustainability report. . Wal-Mart's sustainability report was more lengthy (174 pages) than their 10K SEC submission (145 pages) and yet the actual discussion and reporting on the GRI indicators do not begin until page 162. A review of the performance indicators reveals that they did not report on 45 of the indicators, including PR9," Monetary value of significant fines for noncompliance with laws and regulations concerning the provision and use of products and services;"PR7, "Total number of incidents of noncompliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion and sponsorship by type of outcomes;" and PR8, "Total number of substantiated complaints regarding breaches of customer privacy and losses of customer data." Most would agree that indicators PR7, PR8 and PR9 would be useful information to stakeholders. This raises the question as to why Wal-Mart chose not to disclose noncompliance issues. The answer may be found by researching sources, such as, the EPA Enforcement Database.

Wal-Mart agreed to a significant legal settlement with the EPA in May of 2013. The EPA database reported the following; "Walmart has resolved civil violations of the Resource Conservation and Recovery Act (RCRA) and the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA). The U.S. Environmental Protection Agency's (EPA) Environmental Appeals Board has approved a Consent Agreement and Final Order between Walmart and EPA requiring the company to take significant actions to ensure future compliance and pay a civil penalty. In related actions, Walmart also pleaded guilty today in cases filed by federal prosecutors in Los Angeles and San Francisco to six counts of violating the Clean Water Act and in Kansas City, Missouri to violating FIFRA." This type of information is not presented in the sustainability report or a 10K submission.

This paper is not an indictment of Wal-Mart but rather uses Wal-Mart as an example of the failure of GRI Guidelines for Sustainability Reporting. How does a stakeholder determine how useful a company's sustainability report is for informed decision making? These issues are particularly disconcerting to third party assurance providers, many of which are public accounting firms.

There are signs that can raise a red flag as to the "Greenwashing" of a report. First, excessive length of the report may indicate that considerable positive narrative is presented. Second, the number of indicators reported on may provide some insight into the reports usefulness. Are the reports receiving assurance from an independent third party? A fourth sign, and perhaps the most important red flag, is whether the company reports on indicators PR7, PR8 and PR9 which are relevant to all firms regardless of industry membership.

Sustainability reports are most informative when used in conjunction with the company's 10K SEC submission. Companies need to provide cost/benefit data and segment information to answer important stakeholder questions. Does the company use funds in the most advantageous manner? Which geographical areas or products contribute greatest to the company's carbon footprint? The GRI is providing a valuable service but without legal mandates little standardization can be achieved. In the interim, the GRI should consider certifying reports based on more stringent requirements.

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