

The Transparency Trap

Leading practices for promoting consistent communications across reporting channels

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In a world increasingly conscious of the eco-friendliness of corporate policies and practices, businesses should target transparency in communications regarding environmental risks and liabilities. Under pressure from all sides to do this – from shareholders, stakeholders, regulatory bodies and the general public – companies need to incorporate consistent messaging in all corporate communications. At the very least, financial statement disclosures should be consistent with representations submitted to regulatory bodies. These should also align with information released as part of “corporate social responsibility” or “sustainability” public relations campaigns.



Incorporate consistent messaging in all corporate communications.

To accomplish these objectives, companies need to take a coordinated and centralized approach to communicating environmental and social performance internally and externally. By establishing such a centralized strategy, companies can reduce the risk of stakeholder activism, shareholder resolutions, misrepresentation and possibly litigation, while simultaneously promoting a better brand image and mitigating risk to shareholder value.

The Need for Adequate and Consistent Communication

Companies today face unprecedented scrutiny of their environmental and social policies and performance. Factors contributing to this trend include global concern about climate change; growing awareness of business consumption of scarce natural resources; the changing legal, regulatory and accounting requirements; and mounting demands for transparency from regulatory bodies and the public.

Companies need to avoid even the appearance of attempting to downplay or hide their risks or liabilities. Yet despite new and more stringent guidelines, the interpretations and corresponding communication of environmental risk or liability vary considerably. As a result, companies need to proactively establish and follow practices that help make their environmental and social communications both adequate and consistent across all channels, including financial statements, voluntary performance reports, Web sites and press releases.

Specifically, as companies increasingly issue voluntary reports on environmental and social performance and post such reports on their Web sites, they should bear in mind that this distribution may be considered “public” and could be subject to compliance with public disclosure requirements.

In July 2008, the Securities and Exchange Commission (SEC) voted unanimously to issue guidance to public companies posting information on their Web sites in compliance with securities laws. The Internet

and its uses have changed significantly since 2000, when the SEC last issued Web site-related guidance.

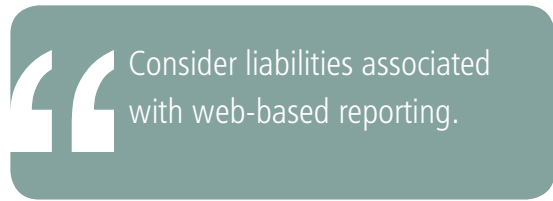
“The last time the SEC issued guidance in this area, the idea of ‘social networks’ had not yet been developed, and creating a social network where shareholders could meet and exchange views was barely imaginable,” says SEC Chairman Christopher Cox. SEC guidance clarifies the liability framework for certain types of Web-based disclosure, including “the clarification that the anti-fraud provisions apply to statements made by the company (or a person acting on behalf of the company) in blogs and electronic shareholder forums.”

A leading practice for mitigating risk of inconsistent communication is structuring a centralized approach to communicating environmental risk and liability that would create greater consistency and transparency, while mitigating the risk of fraud. By accomplishing this, companies can minimize risks associated with conflicting communications and in the process, gain a better understanding of the true costs of their actions, operations and activities that impact the environment and society. This should enable them to make more strategic capital budgeting decisions when investing in technologies and processes that reduce consumption and waste. This should even help overall return on investment in environmental policies.

Risks of Inaccurate or Non-Aligned Environmental Communications

As a direct result of the public’s intensifying interest in environmental and social issues, companies that accurately disclose environmental and social obligations and exposures can mitigate the risk to their brands, as well as overall shareholder value. The consequences of not being transparent are increasingly grave. Shareholders are taking aggressive action upon real or perceived misstatements of environmen-

tal risk. Indeed, waves of shareholder resolutions and litigation about environmental and social issues have swept through a number of industries.



In the energy industry, companies need to be conscious of public perceptions about their contribution to climate change, since litigation has arisen from such perceptions. A lawsuit brought by Gulf Coast property owners against 26 energy companies charged that they contributed directly to global warming, which created the environmental conditions that led to Hurricane Katrina’s devastating strength.

In the consumer goods industry, businesses must be aware of how environmental communications impact the public’s perceptions of their brand. Consumers are increasingly attentive to such issues as green manufacturing processes, packaging and general environmental social responsibility.

Environmental scrutiny is particularly intensive in the financial services industry. Given that these firms have in the past set the standards for measuring, evaluating and disclosing risk, stakeholders and shareholders expect them to do the same in the environmental arena. Banks are under pressure to disclose how they assess the environmental policies of loan candidates when making lending decisions, and disclose how much of their portfolios are financing “dirty” industries. By consistently reporting on their environmental risks, financial services firms seek to improve their brand images as well as their stock prices.

Communicating Environmental Performance

For these reasons and more, companies need to take a structured and sustainable approach to identifying, assessing, measuring and reporting environmental and social sustainability matters. Leading practices include:

Creating a command center for policies, procedures and communications

Companies need to create a central point of responsibility for aligning and coordinating internal and external reporting supported by the appropriate infrastructure. These include technologies or systems that reduce the manual nature of reporting associated with environmental matters that could result in “multiple versions of the truth” that are at risk of discovery if the company receives an action against them. Indeed, leading companies are placing responsibility for all risks related to “sustainability” under the same umbrella, since these also suffer from the same communication disconnects as environmental risks.

Incorporating multifunctional expertise. Under this command center, enterprises should assign roles and responsibilities, and include multifunctional expertise, including but not limited to legal, finance, accounting, engineering and operations. Marketing and advertising professionals and others involved in producing voluntary reports should coordinate with strategic and operational leads to ensure future performance targets such as reductions of energy and water usage are achievable and aligned with business priorities and operational requirements. Environmental remediation and legal professionals should support the controller in regulatory financial statements to ensure that communications in voluntary reports are consistent with those provided in mandatory reporting.

Implementing a formal process for collecting data on environmental performance

Once a centralized organizational structure has been established, companies need to put formal written policies and procedures in place for collecting data on environmental performance. This includes undertaking an operational analysis to understand where environmental and social risks and liabilities may occur. Standardizing processes, policies and procedures for identification, assessment, measurement and reporting of those risks should also be implemented. Companies must make sure the team supervising how this data is being collected and those who calculate performance metrics have active involvement from corporate leaders with a broad view of these metrics, and they understand the strategic implications of the metrics and their operational achievability.

Continuously monitoring disclosure regulations.

Regulations evolve rapidly. The Financial Accounting Standards Board recently issued new standards that impact accruals of environmentally related conditional asset retirement obligations. As the U.S. Financial Accounting Standards Board and the International Accounting Standards Board work to reduce differences between U.S. Generally Accepted Accounting Principles (GAAP) and the International Financial Accounting Standards (IFRS), the result is that environmental liabilities are trending towards being recorded at their fair value, which may increase the materiality of environmental exposures.

The Federal Trade Commission (FTC) is also investigating product and service labeling more frequently with regard to environmental truthfulness and accuracy. The federal government is considering passage of climate change regulation. However, companies should be aware that until these and other regulatory bodies define precisely what metrics should be

used and how they should be measured and reported upon, relevant reporting standards and appropriate metrics for communicating environmental risks and liabilities will remain largely in flux.

Being aware of the complexity of the regulatory environment. Because so many different government agencies are getting involved in regulating environmental matters and disclosures, companies must be vigilant in identifying and working with all the agencies to which they must report. These can range from the FTC, which oversees labeling issues, to the Department of Homeland Security, which tracks companies based on the chemicals they store onsite.

“Consistency is essential for both external reporting and internal business planning.”

Emulating processes established for Sarbanes-Oxley compliance. The current environment for sustainability communications is characterized by a disclosure paradox. Increasingly, shareholders and stakeholders are requesting communications on performance, but companies are struggling with a lack of consensus on relevant reporting standards and measurement criteria. Their protection is ensuring the establishment of consistent policies, processes, procedures and documentation of compliance. Companies are increasingly focusing on their governance structure and integration into business processes, since it is imperative to establish formal evaluative processes of performance against targets.

Many companies are adopting a Sarbanes-Oxley Sections 404 and 409-like approach to managing environmental and social sustainability communica-

tion. This includes developing and implementing a comprehensive approach to the collection, processing and disclosure of environmental and social sustainability performance. This may be achieved through leveraging existing environmental, health and safety management systems to systematically collect and report on performance, while enhancing components to address not only internal and regulatory reporting requirements, but also financial and voluntary reporting.

The management system should be strengthened by developing protocols to provide for consistency across all tasks, whether collecting data or assigning probabilities to liability assessments. The policies, procedures and controls should facilitate accurate and timely reporting and presentation, so relevant data is reported internally or externally. The management system should also contain adequate anti-fraud programs and controls, since anti-fraud provisions apply to statements made by the company in blogs and electronic shareholder forums. The operational effectiveness of the management system may be improved through providing adequate infrastructure, which includes assigning dedicated personnel who have specific responsibility for communication of environmental and social sustainability performance and technology.

Aligning corporate communications channels. Because of the high public relations value of eco-friendly and green initiatives, actions and even intentions, companies are publicly announcing the positive contributions they are making to environmental causes. However, they should be careful that these communications are aligned with what they have said about environmental legacy liabilities in their financial statements, as well as with their public actions.

Preparing for the future. Companies need to constantly look ahead to anticipate how mandates will affect them in the future. The issue of materi-

als management – or understanding the entire life-cycle impact of using regulated substances to create, consume or dispose of a product or service – has come to the forefront of the European Union’s environmental agenda. If nanotechnology, used by many companies throughout the world, was to be banned or regulated, companies need the capability from both technological and organizational perspectives to understand the full ramifications of their exposure to report on it. Any time a company is using a material or process that has the potential to be declared environmentally harmful, the company must take a long-term view of what it may have to disclose down the road.

First Things First: Deciding Who’s in Charge

The jury is still out in terms of who should “own” internal and external communications of environmental and social sustainability performance. Although many companies are beginning to appoint a chief sustainability officer (CSO), these individuals can come from a wide variety of backgrounds and are not necessarily supported with the appropriate constituencies to champion the agenda or dedicate resources to support day-to-day requirements within the organization. The CSO should interact regularly with the most senior executives. After all, top business leaders – even those not directly involved in making claims about environmental policies or practices – are ultimately held accountable for ensuring that environmental communications are both adequate and consistent.

Accomplishing all this will not be easy. Companies need to get on top of current mandates, plus it is likely that many of today’s voluntary disclosures on natural resource consumption and resource efficiencies and performance will become tomorrow’s reporting requirements.

Because there is currently consensus on what should be reported and how, companies need to begin proactively clarifying their environmental and social performance objectives and targets, evaluating what is achievable based on the type and severity of their risks. They need to put the appropriate systems, controls, policies and procedures in place to ensure they are being consistent in all types of disclosures.

Consistency is essential for both external reporting and internal business planning, since this is the information needed to make critical decisions about environmental policies going forward. By doing this, companies should reduce their risk of inadequate disclosures, shareholder resolutions and litigation, while promoting a better brand image and ultimately creating a positive impact on shareholder value.

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