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**Disclosure of the impact of corporations on society:
Current trends and issues**

Report by the UNCTAD secretariat

Executive summary

There has been growing concern in recent years about the impact that enterprises have on society. A large number of initiatives have been taken by various stakeholders to assess corporations' social impact, and by enterprises to report on it.

Responding to these developments, the Intergovernmental Working Group of Experts on International Standards of Accounting and Reporting (ISAR) at its 18th session identified corporate social responsibility as one of the emerging issues in the area of corporate transparency that could be discussed at future sessions. This followed the recommendations of the 17th session of ISAR for the UNCTAD secretariat to continue its efforts to promote sustainability reporting, which includes financial, environmental and social aspects of enterprises' activities.

This paper has been prepared by the UNCTAD secretariat in order to facilitate the future consideration by ISAR of the re-emerging issue of corporate social responsibility and its implications for accounting and reporting. It provides an overview of the most often used definitions of corporate social responsibility and of the main international initiatives in this area. It analyses major factors that govern corporations' relations with society, such as codes of conduct, international and national law, corporate governance requirements, reputational risk, and public and investor pressure. Furthermore, it summarizes the current state of corporate social reporting and the major initiatives taken by various stakeholders to define an appropriate reporting model. Finally, it discusses some of the issues faced by preparers and users of social reports, such as reporting medium, purpose, format and comparability of social reports, and materiality and verification of data disclosed in those reports.

CONTENTS

	Pages
INTRODUCTION.....	3
I. Corporate social responsibility	3
A. Definition.....	3
B. Relevance to preparers and users of corporate reports	4
II. What governs corporations' relations with society.....	5
A. Main international initiatives for CSR.....	5
B. Codes of conduct.....	5
C. International and national law.....	6
D. Corporate governance	7
E. Public pressure and reputational risk	8
F. Investors' pressure	8
III. Disclosure of corporate social responsibility	10
A. Recent trends in social reporting.....	10
B. Current voluntary corporate reporting initiatives	12
IV. Major issues faced by preparers and users of reports	14
A. Purpose.....	14
B. Comparability of reports	14
C. Reporting medium.....	15
D. Materiality.....	15
E. Verification	16
V. Conclusion	16
BIBLIOGRAPHY	18
NOTES	21

INTRODUCTION

1. Concern about the impact of enterprises on society is a global one. The expectations of consumers, employees, investors, business partners and local communities as to the role of businesses in society are increasing. Guidelines, principles and codes are being developed for corporate conduct.
2. Governments, non-governmental organizations (NGOs) and local communities are demanding increased transparency and accountability, not only in the enterprises' daily business operations but also with regard to how those operations affect society. With the recent financial and accounting scandals and their impact on capital markets and pensions, these concerns have become more acute.
3. Despite this widespread interest, it is still difficult to assess the impact of an enterprise on society, and even more so to benchmark it. Stakeholder groups design benchmarking tools, professional organizations carry out social audits, Governments legislate for mandatory social reports, rating agencies rank enterprises, and enterprises themselves publish an increasing number of reports on their social performance. These numerous efforts notwithstanding, stakeholders are not satisfied with the reports and demand ever more information on the impact that enterprises have on society, and how they align this impact with society's needs.
4. These numerous requests for information from investors and civil society impose a growing burden on enterprises, which struggle to respond to the demand. It is increasingly recognized that one of the solutions lies in harmonized corporate reporting that would produce complete, comparable and verifiable information material for all stakeholders.

I. CORPORATE SOCIAL RESPONSIBILITY

A. Definition

5. Society grants all legal entities, including enterprises, a "licence to operate" by spelling out their rights and duties in laws and regulations. Liberalization and globalization have enabled enterprises to extend their business reach, thus putting them in a position to have an even greater impact on society. Despite the existence at the international level of treaties, agreements and conventions, there is no set of international rules to regulate business activities and their impact on society. This means that the increased power of corporations must be balanced by a sense of ethical business practices. In a world where transnational corporations' economic power compares with that of countries,¹ Governments sometimes find it difficult to balance the need to protect their citizens with the need to attract foreign direct investment.²
6. Corporate social responsibility (CSR) goes beyond philanthropy. Most definitions of CSR describe it as constituting actions whereby enterprises integrate societal concerns into their business policies and operations, including environmental, economic and social concerns. Compliance with the law is the minimum standard to be observed by enterprises. In countries where enterprises' legal obligations are non-existent or not spelt out in detail, it is important that enterprises still make an effort to meet societal expectations. The scope of corporate social responsibility encompasses the direct impacts of enterprises' actions as well as the spillover effects they may have on society. The extent to which enterprises can be held responsible for such externalities is still being debated.

7. Corporate social responsibility is very closely linked to the concept of “sustainable development”. In 1987, the Brundtland Report found that the current model of economic development could not be sustained in the long term, as it depletes natural resources and harms society. It defined “sustainable development” as a “development that meets the needs of the present without compromising the ability of future generations to meet their own needs”.³ This concept of sustainable development depends on three key components: environmental protection, economic growth and social equity. At the 1992 United Nations Conference on Environment and Development in Rio de Janeiro, the leaders of over 100 countries adopted Agenda 21, a blueprint for achieving sustainable development in the 21st century. Governments that agreed to implement this plan in their countries are monitored by the United Nations Economic and Social Council’s Commission on Sustainable Development. Agenda 21 described transnational corporations as playing a crucial role in the social and economic development of a country.⁴

B. Relevance to preparers and users of corporate reports

8. Societal expectations originate from a growing number of interest groups, including shareholders, employees, Governments, non-governmental organizations (NGOs), consumers, and local communities in which businesses operate. A judgement of what constitutes “responsible behaviour” in a particular sector and location can be made only through a dialogue between stakeholders and the enterprises. Transparency and accountability are fundamental to this dialogue. Given the current state of distrust between society and enterprises, corporate claims of good behaviour are met with suspicion if they are not backed by comprehensive and verifiable information. Reporting faithfully on an enterprise’s impact on society helps rebuild trust by demonstrating that the enterprise is open and accountable for the impact of its actions. It also facilitates dialogue and allows stakeholders to identify the problems and design solutions that are acceptable to all parties.

9. Users of accounts traditionally include directors of the board, executive directors, regulators, lenders and investors. Corporate social responsibility is becoming more relevant to them, as directors are under pressure from their investors to disclose in the accounts the impact of environmental and social expenditures, risks and liabilities upon their financial performance. As the number of socially responsible investment funds grows, there is pressure to invest solely in enterprises that can demonstrate the integration of CSR into their operations. Since this type of information is increasingly becoming material to investors, companies need to be able to report on their environmental and social performance in a comparable and verifiable way.

10. Accounting for environmental and social performance is also crucial for the good management of these issues. It has been argued that improved environmental performance means increased operational efficiency and thus increased shareholder value.⁵ The positive link between social performance and financial performance is more difficult to prove, but a number of management theories try to establish it.⁶ For example, improved working conditions and involvement of employees in decision-making can increase productivity and the quality of products/services. This also reduces absenteeism. Improved work environments attract and retain staff, particularly skilled ones, with a consequent reduction in turnover, recruitment and training costs. Consumers also are sensitive to an enterprise’s reputation. If two companies produce similar products for the same price, the one with a good social and environmental track record could benefit from increased sales and a larger market share.

Finally, environmental and social performance can be properly managed only if it is assessed and compared over time.

II. WHAT GOVERNS CORPORATIONS' RELATIONS WITH SOCIETY

A. Main international initiatives for CSR

11. Work has been carried out at the international level to better define the boundaries of corporate social responsibility. Guidelines for enterprises have been produced by the United Nations Conference on Trade and Development (UNCTAD), the International Labour Organization (ILO), and the Organisation for Economic Co-operation and Development (OECD). The United Nations Global Compact is a coalition of United Nations (UN) agencies and enterprises that aim at promoting a selection of these guidelines. Other initiatives include the work carried out at the level of the European Union, which is still at a very early stage.

12. The existence of an increasing number of global conventions and guidelines for CSR and the growing general awareness of CSR issues in developed and developing countries help enterprises to integrate CSR into their everyday business and operations. The number and the diversity of the groups developing these initiatives show great creativity, but they are uncoordinated and so generate confusion. For example, some stakeholders' groups design new CSR tools that duplicate other existing ones, and fail to work on certain types of tools that are most needed but ignored by all. A recent survey of initiatives⁷ has demonstrated that a myriad of tools have been developed to help enterprises integrate CSR into their visions, policies and strategies, but hardly any have been devised to help enterprises report on their impact on society. This has generated confusion for enterprises that are faced with demands from so many initiatives.

B. Codes of conduct

13. There is no consensus on whether corporate social responsibility rules should be voluntary or mandatory. For a while corporate self-regulation and codes of conducts – designed by enterprises to define their environmental and social responsibilities – were seen as the way forward in CSR. The number of codes of conduct increased exponentially over the last decade.⁸ They are based on codes developed by UN agencies, the ILO, the OECD, Governments, industry and stakeholders' groups. However, codes developed by corporations are often limited in scope and application. They tend to be adopted by enterprises in which brand names and corporate image are important. Many enterprises have adopted a code of conduct in reaction to public criticism in developed country markets. These codes often focus on issues that concern the well-being of populations in home as well as host countries. There is a danger that these codes, if implemented uniformly, will have a damaging effect on certain societies, owing to fundamental cultural and economic differences. It can also be argued that the lack of monitoring of the implementation of codes decreases their usefulness in the adaptation of the way in which enterprises conduct business.⁹

14. The difference between a code that is merely a public relations exercise and one that allows real control over business operations is the transparency and effectiveness of its implementation and its verification. Most codes do not have a mechanism for accountability or follow-up.¹⁰ The most commonly used of these processes – the signature of executive officers – is used in less than 40 per cent of the cases. Mechanisms for “whistle-blowers” exist in only 20 per cent of cases and training for compliance in less than 15 per cent. Periodic

review by managers happens in less than 3 per cent of the cases and external verification even less frequently.¹¹ Given this poor record, it is increasingly recognized that voluntary codes of conduct are not enough to ensure a level playing field in corporate social responsibility.

C. International and national law¹²

15. At international and national levels, the legal framework in relation to corporate social responsibility is changing. The legal risk to enterprises with regard to their impact on people and the environment is growing and has a direct impact on the business. Insurers' and investors' perception of the legal risks faced by an enterprise can lead to higher insurance premiums and increased cost of capital. The potential liabilities can affect share prices. In this context, enterprises need to assess and manage this risk, and support the universal application of internationally agreed minimum standards – for example, in the area of environmental protection – thus creating a level playing field.

16. International law, through treaties, agreements, conventions and case law, covers issues such as environmental, consumer and health protection, labour and human rights, fair business practices, and corporate governance. Numerous labour and environmental conventions hold signatory countries responsible for ensuring the application of certain principles.¹³ The OECD Guidelines for Multinational Enterprises, although voluntary for enterprises, politically bind the signatory countries to set up national contact points (NCPs) through which enterprises can be investigated for not abiding by the Guidelines.¹⁴ However, NCPs have yet to function in an effective manner. The number of legislative initiatives undertaken is on the increase, owing to public pressure.

17. Certain national laws apply internationally. The United States' Alien Tort Claims Act makes it possible for foreign citizens to lodge claims against American transnational corporations and American-based foreign parent companies for actions in violation of the law of nations or a treaty signed by the United States. Increasingly, principles of civil liability also give rise to litigation against parent companies of corporate groups.

18. At the national level, laws regulate the relationships between enterprises and society by ensuring the protection of shareholders as well as other stakeholders, including employees and consumers. Certain voluntary CSR initiatives such as codes of conduct included in contracts with suppliers can become legally binding as de facto minimum standards. Social labelling and certification schemes incorporated into supply chain contracts become binding.¹⁵ Published codes of conduct, enterprise reports and press releases may be scrutinized under laws on misrepresentation. Codes of conduct and public statements on an enterprise's values can also constitute a "constructive obligation" as they indicate that the enterprise accepts certain responsibilities, thus creating a valid expectation on the part of stakeholders that these responsibilities will be fulfilled.

19. There are also some legislative developments in the area of social reporting. Certain Governments feel the necessity for increased disclosure and transparency in the area of CSR. Their requirements are generally partial in their coverage and mainly environmental or labour-related. France¹⁶ and Belgium¹⁷ require enterprises and subsidiaries located on their national territory to disclose statistical information on their workforce and its fluctuation, remuneration, health and safety, working conditions, training, labour relations, living conditions, and measures taken in favour of employment. France has also required since 2002 that all enterprises listed on the Premier Marché report on employee, community and

environmental issues, how corporations' subsidiaries respect the ILO fundamental conventions and how corporations promote these conventions among their subcontractors. Other countries, including Denmark, the Netherlands, Norway and Sweden, have introduced mandatory requirements for environmental reporting for certain enterprises.¹⁸

20. The United Kingdom is considering this issue as part of its revised Company Law,¹⁹ although no decision has yet been made. The current proposal includes mandatory operating and financial review (OFR) which would cover an enterprise's objectives, strategy and drivers of performance; a review of the business; the dynamics of the business; the enterprise's approach to corporate governance (values and structure); an account of the key relationships on which its success depends; the enterprise's policies and performance on environmental, community, social, ethical and reputational issues; and receipts from and returns to shareholders. The United Kingdom Pensions Act of 1995²⁰ requires pension funds to disclose "the extent to which social, environmental or ethical considerations are taken into account in the selection, retention and realization of investments". Australia, Belgium, Germany and Sweden have introduced, or are in the process of introducing, broadly similar legislation on socially responsible investment.

D. Corporate governance

21. Corporate governance has been catapulted to the top of the political and business agenda by the recent accounting and management scandals such as Enron, WorldCom, Tyco, Ahold and others. If effective, improved corporate governance would ensure that corporate leadership is efficient, honest, responsible and accountable. Although, it is still argued by some that enterprises are responsible solely to their shareholders, international corporate governance guidelines increasingly recognize that enterprises need to consider all their stakeholders. Principles of corporate governance agreed among OECD countries – the OECD Principles of Corporate Governance²¹ – state that the Board of Directors (BoD) should ensure that the enterprise is in compliance with applicable laws, and is expected to take into account various stakeholders' interests, including those of employees, creditors, customers, suppliers and local communities.²² However, it seems that not all BoDs take into account stakeholders' interests while performing their primary functions, which include guiding corporate strategy and setting performance objectives. A recent survey of 500 businesses in the United Kingdom found that only four out of 10 boards discuss social and environmental issues, only a third have a board member who has an environmental remit and only a fifth have one with an interest in social issues.²³ Boards are also responsible for ensuring that appropriate systems of control are in place, in particular those that monitor risk, including potential environmental and social liabilities.

22. Information is a major concern for BoDs. Board members must have access to accurate, timely and relevant information to support their decision-making. Also, they are in charge of overseeing the process of disclosure to and communications with stakeholders, which helps to improve public understanding of the structure and activities of the enterprise, corporate policies and performance with respect to environmental and ethical standards, and the enterprise's relationship with the communities in which they operate. A number of pronouncements, such as the OECD Principles, the Commonwealth Association for Corporate Governance (CACG) Guidelines,²⁴ the King Report on Corporate Governance 2002²⁵ and ISAR's Transparency and Disclosure Requirements for Corporate Governance stress the importance of communicating with stakeholders. They recommend that enterprises disclose financial and non-financial information, including policies on business ethics and the

environment, governance structures pertaining to those policies, foreseeable risk factors, issues regarding employees and other stakeholders, performance in connection with environmental and social responsibility and the impact of this performance on the enterprise's sustainability.

23. Some of the major stock exchanges require or are considering requiring disclosure of non-financial data on listed enterprises' social and environmental policies and related management systems, as well as on corporate governance. The Australian Stock Exchange (ASX) requires all entities to include in their annual report a statement disclosing the extent to which the enterprise has followed the best practice set by the ASX Corporate Governance Council.²⁶ The New York Stock Exchange (NYSE) submitted to the Securities and Exchange Commission (SEC) in April 2003 a rule amending its corporate governance proposals, which includes new corporate governance standards.²⁷ These recommendations are currently under SEC review.

E. Public pressure and reputational risk

24. The emergence of powerful NGOs, coupled with progress in the area of information technology means that cases of social irresponsibility make front-page news, thus increasing the enterprises' reputational risk. The business community recognizes reputation as a valuable asset since it affects the relationship of the enterprise with its customers, employees and investors. Managers need to take into account that any wrongdoing anywhere in the world can be transmitted to a worldwide audience, and impact on sales, market share, staff turnover, access to capital and market valuation of their enterprise. It is all the more important to assess and manage reputational risk, since a good reputation is easily tainted and difficult to restore. Arthur Andersen's loss of reputation in the wake of the Enron scandal cost the enterprise its very existence.

25. Many of these NGOs demand transparency and accountability on the part of enterprises. One of the most high-profile examples is the International Right to Know Campaign (IRTK), a United States-based coalition of more than 200 environmental, labour, social justice and human rights organizations. This campaign requires enterprises based in the United States or traded on American stock exchanges, as well as their foreign subsidiaries and major contractors, to disclose information on overseas operations along the lines of the United States Emergency Planning and Community Right to Know Act (EPCRA) and other American disclosure standards.²⁸

26. The Publish What You Pay (PWYP) campaign, initiated by George Soros and a coalition of 110 NGOs, demands that Governments, stock market regulators and international accounting standards require international oil, gas and mining enterprises to publish net taxes, fees, royalties and other payments made to Governments of countries in which they operate. The G8 Governments agreed in June 2003 to pilot such an initiative.²⁹ At the public hearing on PWYP at the European Parliament in June, the Committee on Development and Cooperation declared its support for a mandatory approach to delivering transparency of oil, gas and mining company payments to national Governments.³⁰

F. Investors' pressure

27. Institutional investors, either for ethical reasons or because they are concerned with their investments' capacity to create and preserve shareholder value, take an increasing

interest in enterprises' social and environmental performance and risk management. A recent study investigating the relationship between doing business ethically and financial performance showed that enterprises committed to ethical behaviour performed better financially over the long term than enterprises lacking that commitment.³¹ Investment decisions are based on corporate reports, rating agencies' social and environmental screening, and sustainability indexes such as the KLD Domini 400 Social Index, the Dow Jones Sustainability Index or the FTSE4GOOD Index. These indexes track the financial performance of enterprises that have made sustainability a key driver of business strategy.

28. The performance of sustainability indexes indicates that investors value more highly companies that are less exposed to social, environmental and ethical risks. The Domini 400 Social Index, monitoring the performance of 400 US companies, has outperformed the Standard & Poor 500 by more than 1 per cent on an annualized return basis and on a risk-adjusted basis since its inception in May 1990.³² The Dow Jones Sustainable Index (DJSI), which monitors 310 of the largest companies from 23 countries, has grown by 180 per cent since 1993 compared with 125 per cent for the Dow Jones global Index over the same period.³³ Since its launch in 1994, it has also outperformed the FTSE World Index by 17 per cent.³⁴

29. The number and size of ethical investment funds is increasing, although they still represent a small proportion of total managed equity. Socially responsible investing (SRI) is a growing trend that unites investors that are pursuing financial as well as social returns from their investments. Total assets involved in social investing grew from \$40 billion in 1984 to \$639 billion in 1995, and to over \$2.34 trillion in 2001. In the United States, SRI has grown between 1999 and 2001 in an otherwise depressed market. Whereas during the first 9 months of 2001 the total amount invested into mutual funds dropped by 94 per cent, there was only a 54 per cent drop for socially screened funds.³⁵ In Western Europe, SRI has achieved 100 per cent growth rates in the recent years, although it still represents less than 1 per cent of total managed equity assets.³⁶ The trend in SRI funds is to shift from negative screening (i.e. excluding tobacco, alcohol, arms, etc.) to positive screening whereby investors support enterprises that produce or use environmentally friendly products or production methods and engage in socially responsible business practices. Many of these screening methods take into account internationally agreed principles such as the OECD Guidelines for Multinational Enterprises, the Declaration of Human Rights and the ILO Principles.³⁷

30. Investor pressure can take forms other than selective investing. Shareholder activism is another, growing tactic. As part owners of publicly traded enterprises shareholders can initiate dialogue with managers through letters or meetings, and file shareholders' resolutions. Shareholders' resolutions are proposals introduced by shareholders, individually or in groups, that are discussed and voted upon during the enterprise's annual meeting. Proposals have to receive 50 per cent of the votes for the management to comply with them. Resolutions related to social or environmental issues usually do not achieve such a result, but they contribute to raising awareness, attracting media attention and increasing pressure on executive managers.³⁸ It is difficult to assess the impact of shareholders' resolutions as enterprises can choose to implement the changes proposed by the shareholders without acknowledging the pressure they have been under to do so.³⁹

31. Banks also are awakening to reputational risk. Four large banks – ABN Amro, Barclays, Citibank and WestLB – have drafted the "Equator Principles" on project financing in collaboration with the World Bank's International Finance Corporation. These principles

are social and environmental guidelines for project finance in emerging markets, and include safeguards ranging from environmental assessment and natural habitats to indigenous peoples and child and forced labour. Five other banks⁴⁰ have recently agreed to commit themselves to these principles, with another four still considering whether to do so.⁴¹

III. DISCLOSURE OF CORPORATE SOCIAL RESPONSIBILITY

32. Enterprises are under increasing pressure to report on the impact they have on society and on how they manage this impact. Such reports carry a variety of labels, but they are most often called environmental and/or social reports, or sustainability reports. A sustainability report is more comprehensive than an environmental and/or a social report, first because it includes the economic impact of the organizations, and second because not only does it assess the enterprise's impact on society and compare its performance over the years, but also it assesses the sustainability of the enterprise's operations and products in relation to the development of society.

33. As much work has already been done on environmental accounting and reporting by ISAR as well as by other organizations, the focus of this paper will be on the social components of reports.

A. Recent trends in social reporting

34. Modern social accounting first attracted the attention of Governments, businesses, academics and professional accounting bodies in the first half of the 1970s.⁴² This widespread interest withered over the second half of that decade, only to re-emerge in the wake of environmental disasters such as Bhopal and Exxon Valdez. Enterprises have published an increasing number of environmental reports over the last 10 years. While enterprises that have a large environmental footprint were among the first to report on their environmental performance, environmental reporting has gradually caught on with other enterprises. This trend, triggered by the public's concern for the environment, has been supported by the development of laws and regulations that require enterprises to report on their environmental performance in countries, for example Australia, Canada, Denmark, the Netherlands, Norway, Sweden and the United States. Many guidelines on the structure and content of environmental reports were elaborated in the early 1990s. ISAR published guidelines on Accounting and Financial Reporting for Environmental Costs and Liabilities, based on best practices, to ensure that standards setters did not adopt different solutions for the same problems. ISAR also created a set of five core eco-efficiency indicators to help harmonize internationally the assessment of how the environmental performance affects the financial results of an enterprise. International organizations such as the International Auditing Practices Committee of the International Federation of Accountants, the Accounting Advisory Forum of the European Union and the European Federation of Accountants investigated the relationships between environmental and financial reporting.⁴³ Despite a general move towards a standard format for reporting, the variety in the reports is such that benchmarking is still difficult.

35. Over the last five years, other social topics have been added to environmental issues. Today, environmental reports account for 64 per cent of the total number of social reports. Again, this evolution has been triggered by stakeholders' concern, and is supported by an increasing number of laws, regulations and guidelines. A survey of the top 250 enterprises worldwide and the top 100 in 19 countries shows that fewer than 500 of them produced an

environmental, social or sustainability report in 2002.⁴⁴ This represents less than 1 per cent of the 65,000 transnational enterprises in the world.

36. Reporting is not limited to heavy-impact sectors such as chemicals and mining, but is also found in most economic sectors, including food and beverages, communication and media, transport, and utilities. Social reporting is not restricted to Western Europe and North America but is emerging in Latin America, Eastern Europe, Africa and Asia.

37. Enterprises from emerging economies that report on environmental and social issues say that they do so because of their commitment to transparency and accountability, and because measuring their impact on society helps them manage it. These enterprises are subject to less pressure to report from Governments and domestic investors than those based in Western countries. Some even complain that they do not receive any feedback from civil society organizations in their own countries, although this is a complaint that they share with Western-based enterprises. The lack of pressure from developing country Governments also benefits subsidiaries of transnational corporations, of which only a few report on their local engagements and impact on local communities. External pressure to report mainly comes from stock market authorities in Europe or North America and from socially responsible funds.⁴⁵

38. The content and quality of social reports vary greatly, from public relations tools to sophisticated reports of real efforts to integrate societal concerns into everyday business operations.⁴⁶ A recent quality assessment of 100 social reports from around the world concludes that although the average number of pages has increased by 45 per cent, the reports' quality has not increased compared to the quality level in 2000.⁴⁷ The content of social reports is generally analysed in terms of economic, environmental and social issues. Economic performance reporting includes wages and benefits, productivity, job creation, outsourcing, research and development, and investments in training and other forms of human capital – all of which can be quantified. Environmental issues include the impact of production processes, products and services on air, land, biodiversity and human health. The quality of reports on environmental issues, thanks to the existence of a number of recognized environmental metrics such as ISAR's eco-efficiency indicators, is generally better than the quality of reports on social issues.

39. Social issues typically include workplace health and safety, employee satisfaction and corporate philanthropy, as well as labour and human rights, diversity of the workforce and supplier relations. Social disclosure often has an internal focus, with employee data, health and safety, and staff surveys being more commonly reported than data covering local community and wider society issues.⁴⁸ For those social issues for which it is more difficult to set a quantifiable performance metric, the reporting remains scarce and qualitative. For example, only a minority of reports cover human rights, supplier relations, child labour, freedom of association, collective bargaining, fair trade, working hours, the employment of country nationals, how much and where taxation is paid, and funding of pension schemes. Provided that they do not threaten the enterprise's competitive position, disclosure of these issues would be of great interest to employees, customers, host country Governments and socially responsible investors.

40. Some enterprises report on stakeholder dialogue, which usually takes the form of inclusion in their report of stakeholder statements – sometimes negative but mostly positive – staff surveys, and community panels and forums.⁴⁹ However, most enterprises seem to

consider stakeholder dialogue as an end in itself, and rarely do reports show a link between stakeholder engagement and enterprises' decision-making processes.

41. Despite the lack of internationally accepted standards for providing assurance on social reports, enterprises are increasingly seeking external assurance for their reports. A significant number of reports were verified in 2002 by a third party – respectively 29 per cent and 27 per cent for GFT250 and Top 100 enterprises – and verification was made by a major accountancy firm in 65 per cent of cases.⁵⁰

B. Current voluntary corporate reporting initiatives

42. A growing number of initiatives aimed at assessing the impact of enterprises on society are constantly emerging. Specialized consultancies offer their services to enterprises wanting to produce a social report. The methodologies used by these consultancies all differ from one another, which ensures that they keep an edge on the competition. A multitude of CSR performance benchmarking programmes have been developed by stakeholder groups, in addition to rating agencies and sustainability index publishers. These are swamping enterprises with questionnaires. A recent survey of European enterprises shows that although over 80 per cent of investor relations practitioners believe that CSR reporting is a central part of a good investors' relations programme and 75 per cent of them think that CSR is important in a bull as well as in a bear market, the large majority recognizes that questionnaire fatigue is a real problem.⁵¹ Enterprises are asking for standardization of the information requested from them.

43. A few stakeholder initiatives, generally including representatives from the private sector, aim at setting reporting frameworks and indicators that could help to harmonize information requirements. Although they individually contribute to defining certain areas of social reporting, their variety and limited scope work against the establishment of uniform formats and content. They include the Global Reporting Initiative (GRI), the Sustainability Reporting Project of the World Business Council for Sustainable Development (WBCSD), the Business in the Community (BITC) Corporate Impact Reporting Initiative and AccountAbility's AA1000 series. As the purpose of this report is to review more particularly those recent initiatives that concentrate on the social aspects of reporting, initiatives on environmental reporting are not included here.

44. The GRI guidelines⁵² contain reporting principles to be followed by preparers, specify report content and suggest reporting indicators, including 50 core environmental, social and economic indicators and 47 additional ones. The "core" indicators are considered to be significant to most enterprises and material to most stakeholders.

45. The GRI has made a point of being as inclusive as possible in its deliberations, and any interested and committed party could join and participate in the development of the guidelines. Consequently, it has proved difficult to limit the number of indicators. Each of the GRI's technical and governance bodies included representation from business, civil society, accountancy and labour, from various regions – although few developing countries have participated.

46. The number and the diversity of indicators have raised questions in the business community as to the cost of producing a report in accordance with the guidelines⁵³. As a result, most "GRI reporters" choose to use indicators that they feel that are most relevant to them. A number of indicators are in fact a simple disclosure of policies and practices. Apart

from the evident completeness and comparability problem this poses, the fact that not all selected indicators have a clear link to sustainable development or even performance allows enterprises using the guidelines to produce reports that do not address their impacts on society. There are also enterprises that argue that there is a danger that sensitive proprietary information could be disclosed via some of the indicators. In response to these criticisms, the GRI answers that the guidelines are still evolving. It is learning from its own experience and from stakeholders' comments, and its approach is being refined by the development of sectoral standards. To date, 290 organizations refer to the guidelines in their reports, but only eight report "in accordance" with the guidelines.⁵⁴ Such references present another danger in that enterprises could mislead users into thinking that enterprises are complying with the guidelines.

47. Other initiatives are less comprehensive in scope and tackle only a particular aspect of social reporting. For example the WBCSD,⁵⁵ an organization representing the international business community, runs the Sustainability Reporting project which has led to the development of a web-based reporting platform to give guidance to member enterprises in their compilation of sustainable development reports. The users of this platform can find guidance on reporting, monitoring and measuring, as well as an inventory of best practice reports, including triple bottom line, ethical and social, environmental, and health and safety reports. This tool does not, however, provide a reporting framework. Because this initiative informs the user about what is being done by a limited number of reporters rather than prescribing a specific reporting method, it has the potential to generate greater reporting diversity among reporters.

48. BITC is a non-profit organization based in the United Kingdom with about 700 members, including 75 of the United Kingdom's FTSE 100 enterprises.⁵⁶ BITC's Corporate Impact Reporting project recommends a set of 55 core indicators by which an enterprise's impact on society can be measured. Efforts were made to include information that is material. The indicators are subdivided into sets of indicators related to the market place, the environment, the workplace, the community and human rights. These indicators are accompanied by a framework to measure and report on responsible business practices. BITC stresses that this reporting methodology provides a picture of enterprises' CSR activities and performances, but does not allow for comparison and benchmarking. Some of its core indicators have been criticized by some enterprises for being irrelevant to their particular sectors, and so far only twenty UK-based enterprises participate in this initiative.

49. The Institute of Social and Ethical Accountability (or AccountAbility) is a UK-based organization.⁵⁷ Members include enterprises, NGOs, business schools and service providers. It promotes best practices in social and ethical accounting, auditing and reporting, and develops standards and accreditation procedures. The AA1000 is a tool for social and ethical accounting, auditing and reporting. The AA1000 Framework was established in 1999 to provide guidance on how an organization can improve its accountability and establish effective stakeholder engagement. Through training and dialogue, enterprises are encouraged to define goals and targets, measure progress made against these targets, audit and report on performance, and develop feedback mechanisms. The AA1000 Framework, now known as the AA1000 Series, was extended in 2002 to include specialized modules for accountability practitioners such as those on assurance. However, the AA1000 Series has not been recognized by internationally agreed standard-setters.

IV. MAJOR ISSUES FACED BY PREPARERS AND USERS OF REPORTS

A. Purpose

50. Preparers of reports can be divided into two groups. First are those that use international guidelines pertaining to corporate social responsibility (see “Main international initiatives for CSR“ above) to define the content of their social reports or seek the help of professional auditors or consultancies that focus on making the report a monitoring and management tool. Second are those that outsource the task of producing their reports to consultants whose core competency is in communication. The number of enterprises offering reporting services is growing.

51. The methodology used to produce a social report could be an indicator of the level of commitment on the part of enterprises to use the reporting exercise as a tool to assess and modify their business operations in order to improve their impact on society. It is important that when an enterprise aims at modifying its environmental and social impact, it analyses its current impact, sets targets and puts in place management systems that include monitoring and reporting, just as it does for the financial aspects of its business. Reporting to external stakeholders should not be an end in itself but merely the reflection of the enterprise’s business processes and their results. Currently, many environmental and social reports develop the right rhetoric on the responsibility of enterprises to society and its importance to the sustainability of their operations, but very few report on the management systems that are – or should be – in place to support and implement this goal and their impact on performance.

B. Comparability of reports

52. Each enterprise’s social report has its own format and substance, depending on the approach chosen by the reporting enterprise, and its perception of who its stakeholders are and of what their needs are. Many reports try to provide all interest groups with all the information they require in the same document. This leads to a mass of diverse information, which makes it difficult to have a clear picture of an enterprise’s values, commitment to these values and consequent impact on society. It also makes it difficult to compare performances among enterprises.

53. In order to illustrate the variety of reporting formats, we have compared three examples of the most recent social reports published by two oil companies with years of environmental reporting experience and by a bank which was named best sustainability report producer by the Association of Certified Chartered Accountants. Differences in the very names of the reports reviewed indicate the variety in the three enterprises’ approaches to social reporting. The number of pages, which ranges from 34 to 102, highlights the dilemma that corporations face – between reporting in an exhaustive manner and producing a report that is quickly and easily read. All three enterprises use quantitative indicators to report on their performances, but some accompany them with lengthy explanations, which inform the reader in depth but also multiply the number of pages he or she has to get through to form an opinion on the enterprise’s overall performance.

54. The lack of comparability of reports increases investors’ need for benchmarking tools such as rating agencies. The amount of information required by these agencies and the

multiplication of questionnaires to be filled in by enterprises tie up a growing part of their resources.

C. Reporting medium

55. Most social reports are produced as stand-alone reports, distinct from the annual financial reports. This indicates a divide in the preparers' minds between the interests of investors and those of other stakeholders, and between financial performance and environmental and social performance. The distribution and the readership of social reports are uncertain. In an effort to reach out to as many stakeholders as possible, many reporters publish their social reports on their website in a portable document format (pdf) – readers can save and keep the report in its electronic format and make a printed copy of it. Although it still excludes those stakeholders who do not have access to the Internet, this method substantially increases the potential readership while keeping distribution costs low. A growing number of enterprises now publish their reporting information on web pages only. This method has the advantage of enabling enterprises to update their performance information instantly. On the other hand, it decreases the comparability of the data provided, and all information published cannot be verified professionally. From the point of view of the readers, websites can make access to information more difficult and confusing than reports, particularly in the case of a large website with many levels. The Association of British Insurers (ABI) advocates in its Disclosure Guidelines on Socially-Responsible Investment 2003⁵⁸ that disclosure of social, environmental and ethical matters “should be made in the annual report, and not separately as part of the summary accounts or on a web site dedicated to social responsibility”. The ABI views this as a minimum requirement that does not impose an unnecessary burden on enterprises.

D. Materiality

56. Corporate reporting should be comprehensive and take into consideration all material aspects of business operations. Traditionally, corporate reports seem to focus on quantifiable parameters that go into the financial statements. Reporting on the impact of enterprises on society involves various qualitative parameters. This problem mainly affects social reporting, as environmental indicators have been elaborated by a number of organizations, including ISAR.

57. The task of establishing a materiality threshold becomes more complex owing to the variety of qualitative indicators that need to be taken into consideration for social reporting. The varied readership of such reports leads to different information demands. Most reporting guidelines state that the first step an enterprise must take towards social disclosure is to define who its stakeholders are, and establish a dialogue with them in order to determine what information is material to them.

58. Enterprises' efforts to respond to all stakeholders' demands lead to the publication of indiscriminate information, and thus to a lack of readability of social reports. The specific information needs of different audiences could be better addressed through other communication channels. Reports should contain only information that is material to most or all of the stakeholders. In order to make this possible, the definition of materiality may need to be explored to reflect investors' new environmental and social concerns, and to include stakeholders' information needs. It is important, however, to consider the issue of confidentiality of information. Just as in financial reporting practices, social reporting should

not lead to the disclosure of information that could jeopardize the competitive position of the enterprise.

E. Verification

59. Verification of environmental and social reporting is necessary for it to be credible. As in financial accounting, it must be done by competent and independent auditors who were not involved in the production of the accounts. As there are no internationally accepted standards for providing assurance on social reports, verification methods are defined on a case-by-case basis. A few organizations, such as the Fédération des Experts Comptables Européens,⁵⁹ the Global Reporting Initiative and AccountAbility attempt to give guidelines on verification. Although in the majority of cases verification statements are signed by one of the major accounting firms, there are still a large proportion of reports that are audited by certification bodies, consulting or technical firms.

60. In a quest for credibility, report preparers increasingly have recourse to verifiers. However, the lack of audit standards for non-financial information is a major hindrance to that effort. A 2002 survey⁶⁰ shows that the choice of verifier depends on the audience. Enterprises that target their shareholders choose to employ a large accountancy firm. When the favoured audience is the stakeholders, enterprises prefer to use the services of specialist environmental and social consultancies, or NGOs and “celebrities” in the sustainability field. The choice between celebrity endorsement and specialized consultancy verification depends on the willingness of the enterprise to question the effectiveness of its management processes and learn how to modify them. Traditional auditors focus on the accuracy and reliability of data and include detailed disclaimers perhaps because of their professional liabilities, but do not provide the same learning opportunities as specialized consultancies do. On the other hand, their methodologies are more uniform than those of consultancies, and they are skilled at evaluating internal control systems.

61. Verifiers need to understand the business operations as well as environmental and social issues, and have genuine independence, and a robust and transparent approach that allows an enterprise to learn while delivering external credibility. Guidelines are needed for the verification procedure to be followed by external experts and on the preparation of the reports.

V. CONCLUSION

62. Governments and policymakers need to be able to assess the impact of enterprises on society in order to give them licence to operate and ensure that the benefits outweigh the costs. The first step is to determine what information is needed and to ensure that they receive this information in a regular and consistent manner. This report reviewed the various factors driving enterprises to increasingly integrate social concerns in their business operations, and to report on their social performances. These forces are deep rooted and likely to last. The report has then examined the current state of social reporting as well as the major initiatives taken by stakeholders and enterprises to define an appropriate reporting model. The current financial reporting framework takes into consideration primarily economic events that increase or decrease the value of an enterprise’s assets and liabilities. In that, it does not take into account the fact that the value of assets and liabilities of an enterprise is increasingly affected by factors pertaining to corporate social responsibility. Although there are improvements in the practice of social reporting, there are still some major issues to be solved

such as the purpose, comparability and materiality of reports, the reporting medium and the verification of the data provided in them. This report has shown that stakeholders' and enterprises' initiatives are unlikely to solve these issues and result in a harmonization of social reporting.

63. In order to achieve comparability and reliability of social disclosure at the international level, there is a need for a global consensus on social reporting formats and content. Further work seems to be needed in order to improve the comparability and usefulness of information provided in social reports. In particular, it might be useful to focus further discussions on the following two areas:

- The current efforts by companies to respond to the multiple demands for information lead to an increase in the volume of information provided by enterprises, thus increasing the cost of reporting without entirely meeting stakeholders' needs. Is there a need for further work to determine the most relevant qualitative items that would reflect the impact of enterprises' social policies?
- Is there a need for additional input on a social reporting format, in particular in terms of harmonizing its content and improving the comparability of information?

If this is the case, what role can ISAR play in the process of resolving these issues?

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NOTES

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- ⁴ <http://www.un.org/esa/sustdev/documents/agenda21/english/agenda21toc.htm>
- ⁵ UNEP/Sustainability/Business Case, "Buried Treasure: Uncovering the business case for corporate sustainability", 2001.
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- ⁷ This survey, carried out in early 2003 by the World Business Council for Sustainable Development on behalf of the United Nations Global Compact, has not yet been published.
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- ⁹ UNRISD, "Voluntary Approaches to Corporate Responsibility", 2002.
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- ¹¹ Ibid.
- ¹² This chapter largely derives from the International Institute for Environment and Development (IIED)'s report on "Legal Issues in Corporate Citizenship", 2003.
- ¹³ The main ones include the ILO Labour Conventions, the Basel Convention on Hazardous Waste Disposal, the Convention on Biological Diversity, the Montreal Protocol on Substances that Deplete the Ozone Layer, the Vienna Convention for the Protection of the Ozone Layer and the United Nations Convention to Combat Desertification.
- ¹⁴ <http://www.oecd.org/EN/document/0,,EN-document-28-nodirectorate-no-11-37318-28,00.html>
- ¹⁵ See Loi visant à promouvoir la production socialement responsable. Available at http://www.cass.be/cgi_loi/legislation.pl
- ¹⁶ http://www.dgcl.interieur.gouv.fr/bases_juridiques/bilan_social/accueil_bilan_social.html
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⁴⁸ According to KPMG's survey, social topics are addressed at the following rates in GFT250 reports: community involvement, 97%; health and safety, 91%; equal opportunity/workforce diversity, 88%; employee satisfaction, 67%; human rights, 55%; supplier relations, 39%; child labour, 36%; freedom of association, 27%; fair trade/international development, 18%; corruption, 15%.

⁴⁹ KPMG, "International Survey of Corporate Sustainability Reporting", 2002.

⁵⁰ Ibid.

⁵¹ Investors Relations Society, <http://www.ir-soc.org.uk>

⁵² <http://www.globalreporting.org/>

⁵³ By way of comparison, an SME seeking a public listing in Germany would have to pay at least US\$ 100,000 to produce the necessary financial information, most of which would already be in its books. If SMEs had to start to collect non-financial information as well, the costs could be prohibitive, particularly since no methodology is yet agreed and companies are left to themselves to compile and report their indicators.

⁵⁴ Organizations that wish to identify their report as prepared in accordance with the 2002 GRI Guidelines must meet five conditions:

1. Report on the numbered elements in Sections 1 to 3 of Part C.
2. Include a GRI Content Index as specified in Section 4 of Part C.
3. Respond to each core indicator in Section 5 of Part C by either (a) reporting on the indicator or (b) explaining the reason for the omission of each indicator.
4. Ensure that the report is consistent with the principles in Part B of the Guidelines.
5. Include the following statement signed by the board or CEO: "This report has been prepared in accordance with the 2002 GRI Guidelines. It represents a balanced and reasonable presentation of our organisation's economic, environmental, and social performance."

⁵⁵ <http://www.wbcds.ch/templates/TemplateWBCSD4/layout.asp?MenuID=1>

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