Mandatory corporate environmental reporting: Does it really work?

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- ***How many of the top 100 Australian companies reported under mandatory corporate law requirements?***
- ***How did they report under this legislation?***
- ***Was the information reported useful to the relevant stakeholders?***

This article analyses the results of the beginning of a longitudinal study, begun in 1999 (Bubna-Litic and de Leeuw, 2000), which looks at the compliance of companies reporting on their environmental performance under mandatory corporate law requirements. The two reports in this study are known as the Thin Green Line reports, 1999 and 2002.

There is increasing evidence to show that environmental damage caused by a company can have financial effects on the company. Other than these financial effects, do the directors see their responsibility as being guardians of the earth on which they operate? That is, are we seeing a move toward sustainability?

This study, conducted in both 1999 and 2002, concludes that more directors of the top 100 companies are recognising some responsibility under the obligatory reporting requirement. In 1999, 71 per cent of companies reported and, in 2002, 90 per cent of companies reported. There has been a two per cent increase in the reporting of positive effects and a four per cent drop in the reporting of negative effects. This may mean the companies are either not reporting negative incidents or their work in environmental management has reduced negative incidents.

In both North America and Europe, mandatory environmental reporting requires reporting by some companies, some of the time. Generally companies are obligated to report when they trip usage or emission thresholds under various licensing regimes. In the United States, the Toxic Release Inventory requires all companies with more than ten full-time employees to submit data on their use, manufacture and/or emissions of approximately 600 different toxic chemicals to the Environmental Protections Agency. This information is freely accessible by the public.

In Europe, the EU Directive on Freedom of Access to Environmental Information requires all public authorities with responsibilities for the environment to make environmental information available to any person who requests it. OECD countries are also party to the Pollutant Release and Transfer Registers (PRTR) which call for firms to report periodically on the release and transfers of a variety of substances considered high risk. Although the PRTR system is not compulsory, it exerts a powerful incentive for companies to reduce releases and transfers through making this information available to the public.[1]

Individual European countries, including the Netherlands, Denmark, Norway and Sweden have passed legislation which aims to increase environmental reporting.[2] France introduced new rules requiring all publicly quoted firms to include data on environmental and social impacts in their annual financial reports in 2002[3] and the CORE Bill currently before the UK parliament calls for legally enforceable environmental and social reporting from British companies annually turning over more than five million pounds.

The UK has also recently introduced an assurance standard AA1000 relating to sustainability reporting for business. Australia and Norway[4] are the only two countries to have introduced a mandatory requirement for all public companies to report annually on their environmental performance in their directors' reports.

In Australia, s 299(1)(f) was introduced into the Corporations Law by the *Company Law Review Act 1998* (Cth), in an attempt to encourage greater accountability and transparency in a company's environmental performance. The first year of reporting was the 1998/1999 financial year. Until 2002, the section read:

> Section 299(1):
>
> General information about operations and activities:
>
> The Directors' Report for a financial year must:
>
> (f) if the entity's operations are subject to any particular and significant environmental regulation under a law of the Commonwealth or of a State or Territory — details of the entities performance in relation to environmental regulation.

This unamended version of s 299(1)(f) did not include a verb which initially caused major concerns in boardrooms around the country.[5] The legislation was also criticised for not defining 'significant'. It was amended in 2002 to include a verb; however, both Thin Green Line studies were based on the top 100 companies reporting under the old version of the section. In the first reporting year, the majority of Australia's top 100 companies understood it to require them to report on their environmental performance, where their performance is subject to environmental regulation.[6] Ever since it was introduced, industry has argued that it shouldn't be in corporations legislation. They said that the appropriate place is in environmental legislation. The fact that it remains mainstreamed in the *Corporations Act* is testament to parliament's resolve to put environmental issues on the boardroom agenda.

Three years on, the number of companies reporting their environmental performance is increasing, particularly in industry sectors which have voluntary environmental reporting codes. The resource sector, for example, developed The Minerals Industry Code in 1996, and 43 companies are currently signatory to this voluntary environmental management code.

Aims of the project

This article compares the response of Australia's top 100 companies to s 299(1)(f) in 1999 and 2002. The study addressed the following questions:

- How many of the top 100 Australian companies reported under this legislation?
- How did they report under this legislation?
- Was the information reported useful to the relevant stakeholders, such as shareholders, creditors, bankers, employees, community, and government?

An additional question in the 2002 study relates to the separate environmental reports published by some companies:

- How does separate environmental reporting by the top 100 companies in 2002 compare to the criteria detailed in the Global Reporting Initiative guidelines and Public Environmental Reporting framework?

Methodology

The companies' response to s 299(1)(f) were assigned to one of the following six categories:

Table 1: Categories of s 299(1)(f) and other environmental reporting

Category	Description of Category
1	No mention in directors' report
2	Minimum requirement
3	Minimum and some extra detail
4	Minimum and positive detail
5	Minimum plus positive detail
6	Minimum plus positive and negative detail, plus a mention elsewhere in the annual report or in a separate report

The categories described above are a generally hierarchical ranking system. The categories comment on whether reporting has occurred and the level of detail included in that reporting. Generally, the higher the categorical ranking the more comprehensive the reporting statement by a company. However, it is possible that a company ranked category five contains more comprehensive environmental reporting than that of a company ranked category six. For example, the reporting by a company which produced a separate report and so received a six may be inferior to that of a company which received a five, as it did not have a separate report, although it included comprehensive environmental information in its directors' report.

Category one companies had no mention of environmental regulation or performance in their directors' reports, contravening s 299(1)(f). Companies rated category two provided the minimum requirement with no legislative detail. Category three-rated companies provided the minimum requirements together with some extra detail, such as relevant environmental laws. Companies rated category four contained category-three information, plus details of positive environmental activities. A company achieved a category five rating if it provided category-four information with the addition of details of non-compliance, or a recognition by the company that even if there has been no non-compliance with regulation, there may still be negative impacts from a company's activities. Companies rated category six provided category-five information and additional information contained either in the annual report or in a separate environmental report. Twelve companies provided separate environmental reports and seven provided an additional environmental section in their 2002 annual report.

Results

Summary of 1999 report

In the 1999 reporting year, many companies found s 299(1)(f) difficult to come to grips with. They didn't understand what was meant by 'particular' and 'significant'. They were not sure whether they were affected and, as monetary values were not included, they were unsure what was. They also questioned the significance of including this information in the directors' report. According to one major industry body, the Australian Industry Group, 'the intent of the section is to convey to stockholders, investors and stakeholders the environmental exposures the company or organisation faces in its day-to-day operations and how it manages its risks'.[7]

General guidelines were issued by ASIC in relation to the environmental reporting requirements under s 299(1)(f) as follows:

- Prima facie, the requirements would normally apply where an entity is licensed or otherwise subject to conditions for the purposes of environmental legislation or regulation.
- The requirements are not related specifically to financial disclosures (for example, contingent liabilities and capital commitments) but relate to performance in relation to environmental regulation. Hence, accounting concepts of materiality in financial statements are not applicable.
- The information provided in the directors' report cannot be reduced or eliminated because information has been provided to a regulatory authority for the purposes of any environmental legislation.
- The information provided in the directors' report would normally be more general and less technical than information which an entity is required to provide in any compliance reports to an environmental regulator.

ASIC declared it would take a hands-off approach to enforcement of s 299(1)(f) when it was first introduced and it continues to do so.

Despite this uncertainty, in 1999, 71 per cent of the top 100 Australian companies included a statement of their environmental performance in their directors' report and 53 per cent included more than a minimum response. However this left 29 per cent of the top 100 Australian companies who did not respond to s 299(1)(f) and made no mention of their environmental impacts or responsibilities in their directors' reports.

The response to s 299(1)(f) in 2002

Before comparing the results from 2002 with the results from 1999, it should be noted that the composition of Australia's top 100 companies has changed. Of the top 100 companies in 1999, only 59 were in the top 100 in 2002. The property trusts sector saw the largest number of new entrants. The number of property trusts in the top 100 companies significantly increased, from eight in 1999 to 19 in 2002.

This 2002 investigation of the top 100 Australian companies has indicated a raised corporate consciousness of environmental responsibility demonstrated by the larger number of companies that have made reference to environmental reporting in their directors' reports. In 2002, 90 of Australia's top 100 companies reported, compared with 71 of the top 100 companies in 1999. Notably, more companies provided some extra detail (category three) with their statement of environmental performance: 25 companies in 2002 compared to 18 in 1999.

Of the companies that did not include a statement responding to s 299(1)(f) in their directors' report, one company, Rio Tinto, provided a separate environmental and social report. Two companies from the financial sector chose not to include a statement of their environmental performance in their directors' report. Argo Investments and Computershare. Publishing and Broadcasting Limited (PBL), Lihir Mining, Foodland, Coal and Allied, AXA Australia Diversified Property Trust, Westfield America Trust and Westfield Trust were the other non-disclosers, although Westfield Holdings, the parent company of the Westfield Trusts, did provide a category-three statement.

Table 2: Comparison of the results in reporting from 1999 and 2002

Category	1999	2002
One	29	10
Two	18	25
Three	18	25
Four	8	12
Five	10	9
Six	17	19
Total reporting	**71**	**90**
Those not reporting	**29**	**10**

Table 3: Change in reporting category of the companies that reported

Category	Percentage Top 100 reporting in 1999 in each category	Percentage Top 100 reporting in 2002 in each category	Percentage increase or decrease
2	25.4%	27.7%	+2.3%
3	25.4%	28%	+3.4%
4	11%	13%	+2%
5	14%	10%	–4%
6	23.9%	21.1%	–2.8%

Environmental risks and/or performance of a negative nature were highlighted by a small number of companies. This is in contrast to the results in 1999 when the percentage of category-five companies out of the total number reporting was 14 per cent. In 2002, the percentage was 10 per cent. The significance of this difference is clearly seen in Table 3 which compares the change in each category of reporting in 1999 and 2002 and notes the total percentage increase or decrease. It should be noted that in this table the percentages are based on the companies which actually reported. It doesn't include those companies which did not report.

Why has the number of companies falling into category five dropped? There are a number of possible reasons for this. Companies may prefer not to disclose their negative environmental impact because of fear of reputation damage. Reporting negative detail such as non-compliance with regulation may also have a perceived negative financial impact, or it may be perceived that costs outweigh the benefits. Companies may be uncertain about possible repercussions from the regulators, or they may consider that they would lose a competitive advantage. Companies may also have been uncertain whether stakeholders are even interested in information about a company's negative environmental performance, or how the company is planning to improve its performance. Further research needs to be undertaken to determine why the number of companies reporting on their negative environmental impacts has decreased in 2002 compared with 1999.

Analysis of the results

Meaning of 'significant'

The mandatory reporting requirement under s 299(1)(f) is activated when an entity's operations are subject to any particular and significant environmental regulation under the law of the Commonwealth or of a state or territory. The legislation does not provide any indicators to the completeness, accuracy and amount of detail required in the information to be provided.

The only guidance in relation to the meaning of 'particular and significant' from ASIC is their guideline (a) which states: 'Prima facie, the requirements would normally apply where an entity is licensed or otherwise subject to conditions for the purposes of environmental legislation or regulation'. These general guidelines on environmental performance disclosure are in contrast to the guidelines ASIC has recently developed to assist in complying with the new clause in the *Financial Services Reform Act 2004* (Cth), which requires disclosure on the extent to which labour standards, and environmental, social and ethical considerations are taken into account in the selection, monitoring or disposal of underlying investments in a fund's portfolio.[8] These latter guidelines are very prescriptive and perhaps a similar approach to s 299(1)(f) would result in more comprehensive and useful information being disclosed.

Section 299(1)(f) has been described as 'deficient, vague and uncertain'.[9] In 1999, companies focused their response to s 299(1)(f) in terms of what was 'significant' on listing legislation and licences to which they were subject. Thirty-two companies out of 53 in categories 3-6 regarded as significant regulation any licences that they were subject to and any legislative requirements that applied to them. This would have been of little value to their shareholders. Some expanded on this by detailing which of their activities were regulated. The analysis from the first Thin Green Line report found that what was important to stakeholders was 'how the company manages its risks, what positive environmental activities it is involved in, and if there have been incidents of non-compliance, how they have rectified the problem and what is in place to prevent future incidents'.[10] From the analysis of the companies reporting in 2002, it seems that there has been a shift towards this and a move away from simply listing legislation to which they are subject. In 2002, there seems to be a large focus on the issues of non-compliance, breaches and fines. Forty-five of the top 100 companies mentioned this. Many companies talked about their risk-management processes, including environmental management systems (EMS), having environmental performance monitored by their boards, environmental audits, both internal and external, and risk assessments. Others talked about environmental incidents, community complaints, community involvement and examples of remediation. One noticeable change from the 1999 report was the inclusion by one company of its supplier policy and a number of companies had independent verification of their statements. The results from 2002 indicate a trend for companies to focus on their positive environmental commitment and it was rare for companies not to take the opportunity to report and focus on the positive aspects of their environmental performance. This is no better highlighted than when looking at the category-two companies' often brief statements. For example, NRMA, while 'not subject to any…', stated that it had 'adequate systems in place' as did Bendigo Bank. APN News & Media, as well as not being 'subject to…', stated that they were 'committed to compliance'. Under category 4, Metcash also highlighted 'staff education programs'.

Conclusion

Section 299(1)(f) imposes a reporting obligation on companies. However, it can be concluded that many companies, mindful of misinterpreting their obligations, are including only the most minimal of comment, which may be well short of details that could be considered useful to stakeholders. The 1999 report concluded that references to regulations and licences are too general to be useful and that what is necessary is the effect that such regulations and licences have on a company's activities. Stakeholders also need to be satisfied of a company's risk management, its positive environmental initiatives and, if there were breaches, how they have been assessed, by whom and how they have been rectified. In 2002, individual companies' self-introduced severity ratings were, as in 1999, one of the most valuable items of information. There also appears to be a trend towards companies developing environmental risk-management strategies. The increased reporting by the banks was an encouraging result. The 2002 study has found that more companies are tending to emphasise the positive and are focusing less on the negative, which is a change in direction from the 1999 report. One of the most encouraging findings of this second report is the reporting by companies of the focus on environmental matters at board level, specifically through audit and compliance committees of the board.

It is well recognised now that stakeholders incorporate a wide grouping comprising shareholders, creditors, bankers, employees, the public, contractors and suppliers and that these stakeholders have an expectation that companies are transparent in their operations and will report annually on their environmental performance. The public environmental reporting (PER) guidelines released by Environment Australia in 2000 aimed to provide companies with a framework for environmental reporting. Although these guidelines do not focus specifically on s 299(1)(f) and are not mandatory, they provide an indication of what Australian regulators consider best practice for company environmental reporting. However, the analysis in this report has led us to the conclusion that the PER guidelines have had little discernable impact on the quality of environmental reporting under s 299(1)(f). The quantity of environmental reporting by Australian companies has increased over the past four years, indicating support for continued regulation of environmental disclosure of publicly listed companies. Perhaps stronger, more prescriptive regulation would have an even greater net positive effect on company environmental reporting.

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Notes

1 Emtairah, T, 'Corporate Environmental Reporting — Review of Policy Action in Europe', Report of the International Institute for Industrial Environmental Economics, Lund University, Sweden, 2002, p 19

2 ibid

3 ibid

4 Rudd, A, 'Environmental disclosures through financial reporting in Norway: Does it make a difference?', Paper presented at the 10th International Conference of the Greening of Industry Network, Gutenborg, 2002

5 Bubna-Litic, K and de Leeuw, L, 'The Thin Green Line-1999 Annual Reporting of Section 299(1)(f) Environmental Reporting', UTS Faculty of Law Report, Sydney 2000 (ISBN 186 36558322000)

6 ibid

7 Australian Industry Group, 'Information to Assist in Complying with Section 299(1)f) Corporations Law: Mandatory Environmental Reporting', Paper presented at the Mandatory Environmental Reporting Conference, Menzies Hotel, Sydney, 18 May 1999

8 Walsh, M, 'ASIC Guidelines on Ethical Investment Policy Have Arrived', *Ethical Investor,* Issue 31, March 2004, p 28

9 The Parliamentary Report of the Joint Statutory Committee on Corporations and Securities, 21 October 1999

10 Bubna-Litic and de Leeuw, op cit