**January 31, 2005**

**Ethics Short Paper**

# "Is legislation needed to force companies to report on their social and environmental performance?"

I believe legislation is needed to force companies to report on their social and environmental performance. First, although many companies oppose the legislation, I believe companies would benefit from the legislation in the long-run and shareholder value would increase as a result of the legislation. Legislation would force companies and analysts not to disconnect corporate and social responsibility ("CSR") from company operations and reporting, forcing companies to make decisions from a broader perspective. Legislation would level the playing field between companies who are already responsible in terms of social responsibility issues and those to take short-cuts for short-term cost or other gains. Finally, although one of my initial concerns with legislation was how standards could be established across industries and sectors, the standards outlined by the "Global Reporting Initiative" appear to be a great basis for U.S. standards/legislation.

There are numerous ways companies could benefit from mandatory CSR reporting. Companies could actually reduce costs. Currently, many companies spend countless hours responding to CSR-related surveys, organized by investors, rating agencies, and other groups. Since there is no standard reporting for CSR issues in the U.S., reporting must be duplicated for numerous audiences. Centralized reporting would be more efficient and thus reduce costs for companies. I am also a strong believer in the phrase, "necessity is the mother of invention." As companies brainstorm ways to appear better in their CSR ratings, they will likely discover more efficient ways to operate. For example, as other countries have passed similar regulations, companies have discovered that they can reduce costs through conserving energy. Resources might also be devoted to developing more eco-friendly processes, which might actually be more efficient. The ideas would likely not be generated without the regulations, and they truly create a win-win solution for companies and the environment. Companies would also generate positive PR from this reporting. I believe that companies do a lot more good things than bad things – the bad things just tend to generate more publicity. A centralized reporting structure would allow companies to showcase the good things they do in their communities in terms of philanthropy, benefits to employees, sponsorship of education, etc. The central reporting would also allow companies to better defend themselves with facts. There are many CSR "scandals," where the two sides of the issue sound vastly different. Standardized reporting would create some common language and authoritative standards and, I believe, this would result in less extreme negative publicity (it would be harder for critics to twist the facts for maximum impact). Also related to PR, reporting would force companies to admit shortfalls in CSR earlier. For both Nike and Exxon, it seems that delaying admitting there were problems resulted in significantly more negative publicity than would have been generated if the companies just admitted the problems and the plans to fix them in the first place. Thus, both through cost reductions and positive PR, companies would benefit in the long-run from mandatory CSR reporting legislation.

CSR reporting regulations would force companies to make decisions and allow analysts to see companies from a broader perspective (rather than just using financial metrics). It would become more difficult for companies to push CSR initiatives to the bottom of the priority list and the budget, because CSR issues would become part of quarterly or annual reporting. Research in Human Resources shows a strong correlation between behaviors and metrics tied to incentives. If CSR issues were actually measured, companies would become more aware of them at all levels. Companies would be more likely to notice what impact the latest cost cut might have on CSR issues, because the CSR issue would actually be a tracked metric within the company. Analysts would also be able to utilize CSR reports as part of assessing the long-term health of the companies they track. It would become much easier to compare companies within an industry on CSR factors if measures were actually reported and tracked. Analyst attention to CSR measures would reinforce the attention paid to CSR metrics through creating an additional incentive, as described above.

Companies today are sometimes faced with trade-offs of creating short-term value for shareholders by meeting quarterly numbers or “doing the right thing” either for long-term company health or for individual stakeholder groups. Some companies have very strong values and usually “do the right thing.” Others live for the quarter and will sacrifice CSR issues for the short-term gain. I think CSR mandatory reporting would level the playing field between those companies who “do the right thing” and those who don’t. There are many CSR situations which go unnoticed for a long time, because there are no official monitoring mechanisms for CSR issues. In the short-term, competitors who are “doing the right thing” are hurt by the short-term advantage gained from the CSR violation. CSR reporting would result in these issues being discovered sooner and would at least allow analysts and shareholders to understand why costs may be higher for the company who does the right thing.

Finally, there are already standards that exist, that would provide at least a great basis for creating CSR reporting legislation in the U.S. The standards set by the “Global Reporting Initiative” are used by over 600 companies world-wide, including Nike, Intel, ABN Amro, and GM. These standards are comprehensive of economic, social, and environmental issues and provide metrics within each of these categories. These measures can be used effectively, regardless of the size or the industry of the companies using the measures. The measures were developed by a broad group of stakeholders, including companies. The measures have been tested. Thus, at least there is a strong starting point to create mandatory CSR reporting requirements in the U.S., which I initially thought might be a major delay in implementing such legislation.

In sum, I believe mandatory CSR reporting requirements would be a positive influence for U.S. companies. They would create positive value and publicity for companies, particularly in the longer-term. They would force companies to see their decisions from a broader perspective. They would level the playing field between companies with strong CSR policies and those without them. Finally, the legislation could be implemented efficiently, since tested standards already exist and have acceptance internationally.