

Public Sector Reporting and Triple Bottom Line

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Sustainability Reporting by the Public Sector

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1. Introduction

I appreciate the opportunity to make a presentation at this seminar on Sustainability Reporting by the Public Sector.

Triple Bottom Line (TBL) reporting is a relatively new topic to the public sector, but one that is rapidly increasing in discussions, if not in actual practice. TBL reporting has now been part of private sector reporting for well over a decade, particularly in the resources industries. Over this time, there have been considerable advances in the preparation of such reports which have also helped to lift their profile with management and accountants. Shareholder oriented groups have also been increasingly active in both their demands for such information and in their investment preferences for organisations that are performing well in these regards.

The progress in the area of TBL reporting is evident through the creation of the Global Reporting Initiative¹ (GRI) and the GRI's plans to prepare a sectorial supplement on TBL reporting for the public sector. In the public sector, considerable efforts have been made to address the environmental area, particularly by national and international accounting bodies. For many, this has been the major area of interest, promoted in no small way by non-government organisations such as Greenpeace.

While there is no agreed definition of precisely what TBL reporting comprises and covers, it is currently fairly widely accepted that, at its narrowest, the term TBL is used to describe the framework for measuring and reporting organisational performance against economic, social and environmental indicators. At its broadest, the term is used to capture the full set of values, issues and processes that organisations must address in order to create economic, social and environmental value and to minimise any harm resulting from their activities². TBL is now generally interchangeable with the notion of 'sustainability' in conceptual terms.

The emphasis today is on sustainability reporting, which is also important for good corporate governance and the concept of 'corporate social responsibility'. As such, there has to be a shift in focus on performance from largely a short-term view to a more medium to longer term outlook. As with its reputation, any organisation has to look outside itself to determine how well it is doing. Not surprisingly, given my position, my focus is largely on accounting and auditing issues. Consequently, I will continue to use the terminology that has been frequently used in accounting literature, that is TBL.

2. Triple Bottom Line Reporting in the Public Sector

TBL has grown in popularity in the private sector by virtue of investors increasingly investing "...in the shares of companies that are believed to be doing the right thing on a range of ethical, social and environmental issues"³. This notion is supported by a recent report by the Association of British Insurers, which concludes:

The growing body of evidence of the financial impacts of socially responsible investing and corporate responsibility activity suggests several important conclusions:

- *the weight of evidence does not support traditional assumptions about the negative impact on risk or returns of introducing social, environmental and ethical investment criteria. On the contrary, incorporating social, ethical and environmental (SEE) criteria can reduce volatility and increase returns;*
- *social and environmental impacts do not fall uniformly across or within sectors – some companies are more or less exposed than others, just as with conventional business drivers;*
- *companies are not equally skilled at managing the impacts, even if they are equally exposed; and*
- *investors and lenders, therefore, need detailed information on specific company exposures, but also strategies and success in managing those exposures.*

The social, technological and economics forces, which have pushed corporate responsibility up the political and business agendas, show no sign of slackening. As SEE issues become more important, investors will need to take more account of them, and investment managers or advisors who fail to do so will be in danger of failing their clients.⁴

In the public sector, Chief Executives of agencies are required to promote proper use of Commonwealth resources⁵. The production and verification of sustainability reports is consistent with fulfilling this responsibility and may contribute to greater transparency and accountability in this regard.

In 2002-2003, the Department of Family and Community Services (FaCS) produced its first TBL Report. They are commended for taking the initiative to produce this report, the first-ever verified TBL report for an Australian Government agency. From the outset of the TBL Report production process, FaCS staff and management requested the ANAO to perform an independent verification of its TBL Report. Auditing of the TBL report showed a strong agency willingness to exhibit transparency and to assure the report was prepared using sound investigation and analysis of the three perspectives of TBL.

The Department of Environment and Heritage will also prepare a TBL report this year that will be verified by my office. I commend the Department for taking this initiative which, I hope, will encourage others to do likewise, where it is cost effective to do so.

The type of information that a public sector TBL is providing to users is an issue of some importance. In the public sector there are two 'streams' of activities and information: departmental and administered. It is therefore important to understand the reporting framework that is being used.

Australian Accounting Standard AAS 29 *Financial Reporting by Government Departments* defines departmental items as those that are controlled by the agency.

These essentially relate to the resources required for that agency to operate. Common examples of departmental items include salaries, payments to suppliers and property, plant and equipment. These are distinguished from tax revenues, user charges, fines and fees, and transfer of funds to eligible beneficiaries (e.g. social security payments), which are carried out by the department on behalf of the government. This latter group is termed 'administered' items.

Schedule 1 of the current Finance Minister's Orders defines Departmental items and Administered items in terms of the outputs and outcomes framework as follows:

- *'Departmental items' cover those assets, liabilities, revenues and expenses over which the entity has control that are applied to the production of the entity's own outputs.*
- *'Administered items' are assets, liabilities, revenues and expenses that the entity does not control and which are subject to highly prescribed rules or conditions established by legislation, or Australian Government Policy in order to achieve Australian Government outcomes.⁶*

It should be noted that the TBL reports only cover the agency's departmental activities. For these areas, it is appropriate for my office to verify the information presented. TBL reporting on administered activities would draw the ANAO into analysing the appropriateness of the Government/Ministerial decision-making. This is outside the scope of the audit mandate. While it may not be appropriate for the ANAO to analyse Government/Ministerial decision-making, agencies that are charged with delivering administered activities are still responsible for the efficient implementation of those programs. This is evidenced by inclusion of key performance measures in relation to these activities in agencies' Budget documents and annual reports. As a consequence, these activities would fall within the scope for ANAO comment. Interested stakeholders would no doubt expect to see some kind of TBL indicators for such expenditure by the relevant agencies in any TBL reporting.

The initiative to undertake TBL reporting within the Australian Government is timely and consistent with the contemporary expectations of transparency and accountability for both financial and non-financial organisational performance. The concept has the support of the accounting profession, clearly indicated by the higher profile being given by the accounting bodies to the concept in recent years, for example, in the various professional publications and conferences. While recognising the wide range of professional skills likely to be required in various elements of TBL reporting, there is concern that accountants need to demonstrate the contribution they can make to such reporting.

In general, apart from the possible changes in internal organisation and management that TBL approaches and reporting might encourage, perhaps the most significant change is the way government might communicate with the community and stakeholders in the provision of its services and operations. This not only relates to the content of the information, but also to how such information is presented and made meaningful to the needs of the community. In principle, such information should serve multiple purposes – reflecting objectives; setting targets; assisting in the evaluation of alternatives to achieve the goals most efficiently and effectively; allocating resources to competing needs; evaluating performance in service delivery

and accountability for public money – in summary, as an integrated performance management framework.⁷ TBL reporting can be seen to be integral to such a framework.

The combination of producing the TBL Report and going through the verification process has already resulted in FaCS making some changes to their work practices. In addition, a number of areas have been identified where future cost savings and efficiencies could be gained through management action towards achieving measurable increased social, environmental and economic performance.

3. Triple Bottom Line Reporting from an Auditor's Perspective

The ANAO initially had a number of reservations around providing a verification statement over FaCS' first attempt to produce a TBL report, as we were concerned that a large number of details might not be verifiable. As such, any adverse audit report could detract from the importance of initiatives taken in the public sector in this respect and might be counter-productive to further progress at that time. However, FaCS' commitment to being open and transparent and their enthusiasm for the verification encouraged the ANAO to undertake this assignment.

The ANAO agrees that TBL reporting should be regarded as part of a comprehensive management reporting framework to all stakeholders. We were therefore pleased to be involved in this project with FaCS, despite the apparent audit risks involved in an uncertain reporting environment.

Verifying TBL information is not an easy task. Some of the difficulties for auditors when verifying TBL information include:

- lack of mandated standards for the preparation and verification of this information;
- lack of available information to assess performance;
- clarity of information presented;
- materiality decisions;
- audit issues relating to publication of the TBL report itself; and
- specialist skills required to verify TBL information.

I will now elaborate upon each of these issues in turn.

Lack of mandated standards

The current accounting and auditing standards frameworks do not include specific guidance on preparing, or verification of, TBL reports. In June last, the Auditing and Assurance Standards Board issued Australian Auditing Standard AUS 110 "*Assurance Engagements other than Audits or Reviews of Historical Financial*

Information". This standard establishes basic principles and standards to be applied by auditors when completing work such as verification of TBL reports.

During the verification of the FaCS TBL report, in late 2003, the GRI Guidelines were the main source of auditing criteria. This was supplemented by the Standards Australia draft standard *General Guidelines on the Verification, Validation and Assurance of Environmental and Sustainability Reports (DR 03422)*. This standard was issued close to the end of the verification procedures.

The GRI Guidelines include key performance indicators for environmental, economic and social performance, and a framework within which to set the key performance indicators. A true 'sustainability report' requires such measures. The GRI issued revised Guidelines in June 2002 and intends updating them again in 2005. The reporting criteria most frequently mentioned in assurance reports are the GRI Guidelines. However, more than half of such reports cite no reporting criteria.

A recent study in the United Kingdom indicated that there is a clear need for integrating corporate social responsibility into the International Organization for Standardization (ISO) management systems⁸. Such an approach would lead to a more standardised global approach to this type of reporting covering key elements such as:

- compliance with all rules and regulations of the jurisdiction in question and relevant international norms pertaining to the environmental, consumer, fair labour standards, human rights, and health and safety protection, as agreed upon through a meaningful stakeholder engagement process;
- processes for meaningful stakeholder engagement;
- development, implementation and communication of corporate responsibility and corporate ethics policies, including those pertaining to anti-bribery and corruption;
- training for socially responsible governance;
- relations with communities, philanthropy, outreach and involvement; and
- measurement and regular reporting to the full range of stakeholders and the general public.⁹

A decision to develop a Standard for Social Responsibility at an ISO Technical Management Board meeting was taken in Stockholm in June last.¹⁰ The ISO's Advisory Group on Social Responsibility recommended that there was a need for a guidance document, and not for a specification document intended for conformity assessment.¹¹ This seemed to be a pragmatic position as there had been some earlier support for third-party certification. The Vice-President, quoted above, opined that:

*A standard that includes Certification today would, in my opinion, defeat it from the outset.*¹²

Lack of available information

The information reported in a TBL is generally non-financial in nature, and may relate to aspects of the organisation that are not accustomed to the rigours of being audited. The organisational areas affected may not be as familiar with requirements being placed upon them to maintain appropriate books and records, as required for financial information, and documentation to support the information presented. An example of this situation relates to where data is being sought about an aspect of the organisation that is not routinely or systematically collected, or is not strictly required (that is, it is provided only on a voluntary basis).

In such instances, it may be difficult for the auditor to gain assurance as to the completeness, accuracy and reliability of the information being presented. However, the International Auditing and Assurance Standards Board (IAASB) has set up a Panel of Experts, chaired by Professor Roger Simnett (University of NSW) who is a Member of the IAASB, both to liaise with the GRI in order to influence the form and content of the next version of the GRI Sustainability Reporting Guidelines so that they will be generally accepted as suitable criteria for assurance engagements, and to develop guidance for assurance practitioners on sustainability engagements.

The Expert Panel, referred to above, has three broad areas of work that are of considerable interest to auditors, as well as to preparers: (1) measurement issues; (2) reporting issues, with the GRI being one model; and (3) providing assurance. Guidance will be provided by the IAASB, as well as by the International Federation of Accountants' (IFAC's) Professional Accountants in Business Committee. The latter Committee has expressed some concern at the current quality of assurance services, as being reported, which needs to be addressed. Despite the difficulties of identifying suitable criteria that are generally applicable and accepted across countries and, indeed, across industries, there appears to be growing international commitment to using accepted standards. This makes the work of the IAASB Panel even more important and worthy of more general support.

Clarity of information presented

As the TBL report is largely based on non-financial information, the latter needs to be presented carefully, in either a narrative or tabular format, so that it is clearly understandable and avoids misleading users of the report. As such, the 'expression' used becomes a very important aspect of TBL reporting. Care is taken, from an auditor's perspective, that there is clarity of information provided with the narrative and tables presenting that information both accurately and ethically.

Consideration of materiality

The verification statement provided after the completion of the ANAO's work to verify the TBL information presented by FACS provides users with assurance that selected data was, in all material respects, found to be complete, accurate and reliable.

The concept of 'materiality' is a important in the auditing profession as it defines the level of assurance provided by the work completed by an auditor. Put simply, the level of assurance provided is not about being 100 per cent accurate, rather it is assurance that the information is 'materially' correct within the parameters set, either by the nature or dollar value of that information.

The term ‘materiality’ is defined in both accounting and auditing standards as follows:

*materiality means, in relation to information, that information which if omitted, misstated or not disclosed has the potential to adversely affect decisions about the allocation of scarce resources made by users of the financial report or the discharge of accountability by the management or governing body of the entity.*¹³

From an auditing perspective, materiality is considered when assessing areas of risk and the impact of errors and/or irregularities noted, during the audit process. As noted, materiality is assessed both in terms of nature and quantum.

A difficulty noted for auditors verifying TBL information is how to practically apply the concept of materiality to non-financial information. To this end, the ANAO ensured that the level of materiality being applied throughout the verification process was clearly communicated to the client, and clearly explained in the verification statement for the benefit of users.

Audit issues in relation to publication of TBL report

There are a number of issues of interest related to the publication of a TBL report.

Currently, the Department of the Prime Minister and Cabinet issues guidelines about presentation and disclosure of agency performance. These guidelines ‘drive’ the content of agency’s annual reports. Should TBL information be included as part of these guidelines, regardless of whether the agency sought to have the TBL information verified, some additional procedures would still need to be undertaken by the ANAO.

This occurs by virtue of the requirements in the Australian Auditing Standard AUS 218 *Other Information in Documents Containing Audited Financial Reports*. This standard requires auditors to check for material inconsistencies between:

- the information contained in the audited financial report; and
- the information contained in other parts of the same document.

Material inconsistencies between these two elements may raise doubt about the audit conclusions drawn from audit evidence previously obtained and, possibly, about the basis for the auditor’s factual findings.

Specialist skills required to verify TBL information

By its very nature, information presented in TBL reports is not all of a financial nature. As such, there are some specific skills that are required to verify this information, which may differ from those required to complete an audit of a set of financial statements or a performance audit.

While the ANAO has identified some synergies between the 2003-2004 financial statement audit of the FaCS and the verification of their 2003-2004 TBL report, we also required assistance from an external accounting firm with acknowledged relevant skills and experience to complete work required on the TBL verification. Over time, the skill sets that these external staff currently provide will need to be

developed within the ANAO, particularly if there is an increase in preparing TBL reports in the Australian Government Public Sector.

4. Developments in Triple Bottom Line Reporting

It is instructive to consider a number of developments, both in Australia and overseas, in relation to triple bottom line and, more broadly, sustainability reporting, which might provide us with greater confidence to consider taking such an initiative in our own organisations.

Recently, CPA Australia's Audit and Assurance Centre of Excellence published a database on their web site of over 160 companies worldwide that publish TBL reports accompanying their financial reports. This database provides information about these reports, including a listing of those providing TBL audit services. The database is designed to support research undertaken by RMIT¹⁴ University's school of Accounting and Law that "...aims to provide a better understanding of how TBL principles are being applied within organisations in Australia and around the world"¹⁵.

This commitment to TBL by CPA Australia shows the increasing importance of this type of reporting as a way of Chief Executives discharging their accountability.

The ACT Government is also looking to implement TBL in its jurisdiction. However, that initiative involves looking to implement TBL budgeting rather than TBL 'ex-post' reporting. The provision of TBL budgeted information is expected to stress the importance and interdependence of economic, social and environment well-being, and provide a better context of informed decision-making about the allocation of resources¹⁶.

The importance of considering the broader impacts of decisions made is becoming more prevalent in an age where shareholders are looking to, and questioning, TBL reports to gain an understanding of the company's broader social impact. While shareholders were previously only presumed to be interested in receiving a return on their investment, they are now increasingly assessing if they are investing in 'clear conscience'¹⁷, and even demanding change where they feel a company is not adequately performing in a financial, social and environmental sense.

There have also been significant developments in the United Kingdom (UK) in relation to both Corporate Social Responsibility (CSR) reporting and its subset, Operating and Financial Review (OFR) reporting.

As with TBLs, CSR reporting is a broader approach to corporate reporting, taking into consideration the entity's broader impact upon its local community, and the global community at large. Gordon Brown, the Chancellor of the Exchequer, recently described the importance of CSR as follows:

Today, our corporate social responsibility goes far beyond the old philanthropy of the past – donating money to good causes at the end of the financial year – and is instead an all year round responsibility that companies accept for the environment around them, for the best working

*practices, for their engagement in their local communities and for their recognition that brand names depend not only on quality, price and uniqueness but on how, cumulatively, they interact with company's workforce, community and environment. Now we need to move towards a challenging measure of corporate responsibility, where we judge results not just by the input but also by its outcomes: the difference we make to the world in which we live, and the contribution we make to poverty reduction.*¹⁸

This initiative has arisen from the Company Law Review, which was later endorsed by the UK Government in its "Modernising Company Law" White Paper in July 2002. This paper included the following three broad proposals to improve corporate governance:

- *a statement of directors' duties;*
- *improved transparency and accountability, with improvements to the quality, timeliness and accessibility of information available for shareholders and others; and*
- *more effective machinery for enabling and encouraging shareholders to exercise effective and responsible control*¹⁹.

In mid 2003, the UK Government announced companies listed on the London Stock Exchange would be required to prepare and publish a statutory OFR reporting in their annual report for financial years beginning on or after 1 January 2005. In May 2004, the UK Department of Transport and Industry's OFR Working Group published both a consultative document and related practical guidance for preparing OFRs²⁰ for which the consultative period ended earlier this month.

The proposed UK requirements include the need for an audit of the OFR. This independent review is critical as it provides stakeholders assurance that the OFR has been prepared in a careful and balanced manner. This independent review is an audit of the process used to prepare the report, rather than of the content of the report itself. As such, users of these reports should have a greater confidence in the review and gain the intended benefits, including that of more informed decision-making, from the provision of this improved information.

The International Federation of Accountants (IFAC) is highly supportive of the need to increase the involvement of the accounting profession to assist in sustainability reporting. Accountants have a particular role to play in the implementation of effective sustainability measures and measuring performance. This is an extension of the traditional financial recording and reporting role. IFAC has nominated a member of their Board to the GRI Board. This member will assist the GRI Board to prepare a guidance paper on Environmental Management Accounting which is due to be released this year.

There is also a Working Group on Environmental Auditing (WGEA) under the International Organisation of Supreme Audit Institutions (INTOSAI), which was formed in 1992 to focus upon auditing environmental aspects of organisational performance, and to assist the demand for environmental auditing expertise²¹. Their work should provide good guidance in the future of performing the verification of the

environmental performance part of sustainability reports. WGEA aims to improve the use of audit mandate and audit instruments in the field of environmental protection policies, by both members of the Working Group and other member Supreme Audit Institutions.

5. Concluding Comments

In conclusion, I would like to reiterate that, via conferences and seminars, such as this one today, there is a growing momentum in both the importance and benefits of TBL and sustainability reporting. A range of international reports and surveys, such as that mentioned earlier in Britain, indicates the growing demand for assurance and predictions that the trend will increase over time. The ANAO is pleased to be taking its place as part of the initial application in the Australian Government Public Sector of this type of reporting, and encouraging enhancement of public sector reporting and governance in this respect. It is still early days for us but we are learning quickly.

While there are some broad-based and more specific public sector issues relating to both the preparation and verification of these reports, the intention to provide users with additional information, providing further transparency and demanding broader accountabilities, is to be commended and supported. However, it is also important that we promote guidance into standards that provide a credible basis for both reporting and auditing. By doing so, we engender confidence in all stakeholders and, consequently, greater acceptance and demand for application of the TBL concept and related notions of sustainability and corporate responsibility.

6. Notes and References

- ¹ The Global Reporting Initiative (GRI) is an independent institution based in the Netherlands, which was established in 1997 by the Coalition for Environmentally Responsible Economies. GRI's vision is "to create the conditions whereby business, government and interest groups work together to achieve sustainable development based on accurate, relevant and shared information about how their activities contribute to this goal." (GRI Business Plan 2003-2005, page 4) The GRI develops and distributes globally applicable Sustainability Reporting Guidelines for voluntary use by organisations. The GRI is also actively involved with business and industry to promote reporting of economic, environmental and social dimensions of organisational activities, products and services.
- ² Audit Activity Report: July to December 2003, ANAO
- ³ S Hoyle, 2004 *Earning Interest on the Principle*, The Age, Melbourne, 14 August
- ⁴ Association of British Insurers, 2004, *Risk Returns and Responsibility*, p.39, available at http://www.innovestgroup.com/pdfs/2004-02-01-ABI_Risk.pdf
- ⁵ Under section 44 of the *Financial Management and Accountability Act 1997*
- ⁶ Parts (a) and (b) of Clause 2B.4 of the *Financial Management and Accountability (Financial Statements for reporting periods ending on or after 30 June 2004) Orders*
- ⁷ 2004-2005 ACT Budget, Supplementary Paper, Framework for Future Budget Presentation Discussion Paper.
- ⁸ P Castka et al, 2004, 'Integrating corporate social responsibility (CSR) into ISO management systems – in search of a feasible CSR management system framework', TQM Magazine, 19 May, 2004, p. 216.
- ⁹ Ibid.
- ¹⁰ Z Patir 2004, *Social responsibility...the way forward in business*, The Global Standard. August, p.4.
- ¹¹ Ibid. p.4
- ¹² Ibid. p.4
- ¹³ AAS 5 *Materiality*, para 5.1
- ¹⁴ Royal Melbourne Institute of Technology University, trading as RMIT University
- ¹⁵ "Triple bottom line – a study of assurance statements worldwide", CPA Australia 24 February 2004, accessed 27 May 2004 of the following site:
http://www.cpaaustralia.com.au/01_information_centre/26_tbl/1_26_0_0_tbl_index.asp
- ¹⁶ 'ACT plan to change reporting practices', *The Canberra Times*, 5 May 2004.
- ¹⁷ K Percy, 2004, 'Shareholder activism reaching new heights', *AM*, 7 May.
- ¹⁸ United Kingdom Department of Trade and Industry, 2004 "Corporate Social Responsibility – a Government update", available at www.csr.gov.au, p. 2.
- ¹⁹ The Company Law Review Steering Group, 2001, "Modern Company Law For A Competitive Economy: Final Report URN 01/942 and URN 01/943", pp 39-40, available at http://www.dti.gov.uk/cld/final_report/index.htm.

²⁰ “*Draft Regulations on the Operating and Financial Review and Directors’ Report A Consultative Document*” and “*The Operating and Financial Review, Practical Guidance for Directors*”, both available at www.dti.gov.uk

²¹ N Carisse, *Making the World a Better Place to Live One Audit at a Time: Improving Governance and Accountability in Environment Protection*, *Journal of Government Auditing*, April 2004