

The logo of the New Zealand Institute of Chartered Accountants is a crest featuring a shield with a scale of justice, a quill pen, and stars. A banner at the bottom of the shield contains the Latin motto "SEMPER ET UBIQUE FIDELIS".

NEW ZEALAND  
INSTITUTE OF  
CHARTERED  
ACCOUNTANTS

A PLEA TO THE  
ACCOUNTING PROFESSION

# GOVERNANCE FOR SUSTAINABILITY

DISCUSSION PAPER PREPARED BY THE SUSTAINABLE  
DEVELOPMENT REPORTING COMMITTEE 1 DECEMBER 2009

*This discussion paper was written by the New Zealand Institute of Chartered Accountants' Sustainable Development Reporting Committee, comprising Gary Swift (Watercare Services Ltd) as Chair, Amanda Ball (University of Canterbury), Judy Brown (Victoria University), Peter Casey (Auckland Regional Holdings), Shaun Collins (Cogent New Zealand Ltd), Raechel Cummins (Kaipara Ltd), Tony Gray (Hastings City Council), Richard Maher (The Answer Company), Leah Murphy (Ministry of Transport) and Jamie Sinclair (Sinclair Group).*

***“If sustainability issues were to be neglected by current and future members of the accountancy profession, there is a risk that accountants’ involvement in areas such as management systems, strategic planning, statutory requirements and tax, internal and external reporting, as well as assurance, will be diminished. This would be a loss to society as well as to the accountancy profession.”<sup>1</sup>***

The accounting profession has significant power in society and plays an important role in the governance of corporate organisations. However, the profession has yet to fully engage in the sustainability debate. There is significant legitimacy risk if the profession does not move in this direction and there are clear gaps in the governance for sustainability that should be filled by the accounting profession. Effective governance of sustainability is crucial to its successful implementation for business and to deliver consequential benefits to society. This discussion paper, argues that failing to move rapidly into the sustainability governance space carries significant risks to accountants.

- If the accounting profession doesn’t act swiftly, it may be marginalised by other professions, such as engineering and environmental consulting, that are presently jockeying for governance positions.
- Opportunities may be lost, resulting in diminished capacity to generate and sustain accountancy businesses.
- There may be a risk to the accounting profession’s longstanding reputation for its contributions to business, other organisations and society in the public interest.

## **Governance for sustainability**

***“Governance for sustainability means identifying the governance systems that help society move towards sustainable development.”<sup>2</sup>***

To understand what governance is, it helps to understand what it is not. Governance is not government. Governance in contemporary society goes beyond the view of governance as something governments do.

Government focuses on the impact and actions of the state, but the responsibility to uphold democracy and encourage distributive and procedural justice is a shared responsibility through a variety of mechanisms at multiple levels, including business organisations<sup>3</sup>. Therefore, to gain a deeper understanding of governance, it is important to consider the wider society, and not just how the government interacts with society.

What does this interpretation of governance, with its emphasis on a wide range of responsible stakeholders, imply when sustainable development is the end goal?

Widely accepted ideas about sustainable development involve the integration of economic, social and environmental aspects into development giving them (at least) equal weight. Governance for sustainability, therefore, concerns how society is structured to give equal importance to social, economic and environmental concerns. Of course, this idea is complicated in an increasingly globalised world. Many issues are complex and can no longer be dealt with by states or governments acting independently, for example, the taxation and regulation of multi-national companies.

Balancing the economic, social and environmental aspects of any decision requires compromise and the recognition of conflicting interests and objectives. Due to the diverse range

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<sup>1</sup> Institute of Chartered Accountants in England and Wales, (2004).

<sup>2</sup> Jordan, (2008).

<sup>3</sup> Paavola, (2007).

of issues and stakeholders, there are conflicting priorities in most sustainability-related policy settings. For example, a tax on pollution raises issues of environmental protection, property rights, economic competitiveness and concerns about distributive justice. Therefore, to progress sustainability governance, this conflict must be acknowledged and attempts made to resolve it. Conflict resolution raises issues of justice, power and legitimacy. The distribution of power in society impacts on how sustainability-related issues are expressed, how decisions are made and how results are weighted.

To summarise, governance for sustainability does not legitimise a single, one-dimensional world view. Rather, it must identify how decisions affect various groups in society and the environment, and then involve those affected in ways that recognise their diverse perspectives.

## Accounting and the governance for sustainability

Traditionally, accounting is seen as a “process of representing an objective financial and economic reality.”<sup>4</sup> This rather dry definition does not do justice to the significant social power wielded by accounting as a process, and the accounting profession, but it does place accounting within a reality bounded by economic reasoning and based on financial transactions. Using this idea, a logical governance space for accounting is within the engines of the economy: the business sector.

Although business wields significant power, it must play by the rules. Beyond regulatory requirements, the onus also falls on society to define and accept how business is conducted. In other words, legitimate business operations need a ‘social contract’ or a ‘licence to operate.’

Because of this, business is dependent on stakeholder negotiation and trust, more so now than ever before. Accounting, as the means by which we measure, interpret and

validate corporate behavior and performance, is therefore a powerful force in global governance.

If the traditional role of accounting is viewed as the role of accounting and accountants, then the potential of the profession is severely limited. The Sustainable Development Reporting Committee takes the view that accounting and the accounting profession have governance roles broader than the outcome of economic transactions. This broader role fits within the governance for sustainability.

## The accounting profession, sustainability and risk

*You are not in a business, you are in a profession. Unhappily, some of you have stopped thinking in those terms.<sup>5</sup>*

Notwithstanding the challenges of linking accounting and sustainability in a practical way, the current perspective of practicing accountants is mixed. A survey by the Institute of Chartered Accountants in England and Wales (ICAEW) found that just over 56 percent of their members thought that accountants need to know more about the principles of sustainability if they are to take an independent and proactive approach to their work.<sup>6</sup> Analysis by Gray and Collison (2002) also suggests that many practising accountants do not view sustainability as a core, structural issue.

A significant barrier that might explain these results is that existing accounting rules afford little room for environmental or social considerations. Sustainability implies quantifiable and non-quantifiable social and environmental impacts. Ascribing values to these impacts is a “hard” technical solution to a “soft” non-technical problem.<sup>7</sup>

Accounting, as a profession, faces significant challenges before it can fully engage with the sustainability agenda. There are however, opportunities, if it does so, and there is a professional and ethical imperative to move quickly.

The neutrality and objectivity of accounting is established and reinforced through its own standards, by governing bodies (both domestic and global), and educational and ethical

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<sup>4</sup> Boyce (2000).

<sup>5</sup> Supreme Court Justice Willard Estey, CA Magazine, (3 July 1991).

<sup>6</sup> ICAEW, (2004).

<sup>7</sup> Boyce (2000).

requirements. All of this is underpinned by the notion of accountants as objective servants of the public interest.

Interviews with accounting practitioners conducted by Gray and Collison (2002) indicate a strong client focus, but little reference to public interest or wider accountability. If accounting is limited to the role of support for another institution (the corporate entity), it is difficult to see how this can be constituted as meeting the public interest, especially so in a sustainability context, where there are, arguably, several relevant “publics”.

This narrowing of the public interest is not consistent with the influential role and power of the accounting profession. If the focus of accounting systems and accountants continues to be financial accountability, the accounting profession will become marginalised. There are two main reasons for this.

First and foremost, society will expect more. Regardless of how the profession defines “public interest”, society sees accountants as a link between the corporate sector and society. Where there are widening gaps between the expectations of society and corporate performance (as measured by accounting), the profession will lose status.

Secondly, the advancing sustainability agenda, requires more non-financial organisational risks to be identified, managed, and reported on. If the accounting profession is not able or willing to participate in this expanded governance role, it will be filled by others. These “others” are unlikely (initially at least) to have the professional infrastructure, ethical foundations, and diversity of skills found in the accounting profession. This will result in a net loss to society.

If we accept that there will be some legitimacy risk for the profession as the principles of sustainability become mainstream, then two questions are pertinent.

1. Where are the existing, or potential, gaps in the sustainability governance that can be filled by the accounting profession?
2. How can the profession fill these gaps?

## Filling the gaps

### Conflict resolution

Governance for sustainability as it applies to corporate organisations is particularly prone to the balancing of conflicting objectives. There is tension between the need to encourage innovation and corporate risk taking for economic growth, and the need to regulate negative social and environmental impacts<sup>8</sup>.

Governments have limited regulatory space to identify and manage these conflicts and to ensure the most significant environmental, social and economic issues are addressed by organisations. This governance gap can be filled by the accounting profession in two ways that are aligned with its existing skill and social mandate.

Firstly, effective stakeholder engagement is necessary to identify conflicting views, enable their expression and to facilitate appropriate responses. Accountants often work across an organisation and deal with both internal and external stakeholders, such as lawyers, bankers, and shareholders. It would be a logical step for accountants to structure and facilitate effective stakeholder dialogue.

Secondly, the profession could lead the development of professional, globally recognised standards to identify material issues beyond those that pertain to direct and immediate financial implications. This would help bring a more sustainability focussed mindset to business performance and value.

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<sup>8</sup> Gouldson and Bebbington (2007).

<sup>9</sup> Gouldson and Bebbington (2007).

## Decision making and democracy

The world beyond numbers and decisions based on economic transactions is plagued with subjectivity. Measuring the value of an ecosystem, fresh water, the social connectedness of the community, for example, is subjective and contestable. There is not likely to be one “right” answer.

Accountants are responsible for much of the information upon which decision making is based. Therefore, if the objectives of accounting information can be refocused to enhance debate, rather than on determining the “right” answer, a more democratic and just answer may result. There are obvious efficiency issues with this approach, but the needs of a multi-faceted society arguably demand a participatory and multi-dimensional approach.

If accounting analysis results in contestable outcomes that inform, rather than prescribe, and is coupled with effective engagement mechanisms (as referred to in the previous paragraph), then it will influence social processes away from technocratic decision-making and towards a more dialogue-focused approach to decision-modeling and analysis<sup>9</sup>. This would result in a strong step forward in governance for sustainability.

## Communications and reporting

Comprehensive and accurate internal and external organisational reporting that addresses stakeholders’ environmental, social and economic concerns is key to governance for sustainability. Accountants are beginning to look at sustainability reporting and they recognise it corresponds with their skills in financial reporting and assurance. However, they are doing this only at the margin. If the goal is for non-financial information to be reported to the same standards as financial information<sup>10</sup>, then there are significant institutional challenges to overcome, including:

- expansion of the standard-setting process to include non-financial impacts, measurement and reporting
- broadening accounting education beyond economic, transaction-based value impacts.

These are significant changes. However, if incremental steps are not taken, someone else will fill the gap – most likely engineering and environmental consultancies. The accounting profession may lose the chance to influence an area closely aligned with their existing skill set.

## A call to action

The accounting profession has significant power in society and plays an important role in the governance of corporate organisations.

However, the profession has yet to fully engage in the sustainability debate. The Sustainable Development Reporting Committee warns that there is significant legitimacy risk if the profession does not move in this direction and that there are clear gaps in sustainability governance that should be filled by the accounting profession.

If no action is taken, the status and power enjoyed by the profession will be diminished. Accounting will become a marginal activity dealing only with the economic aspects of organisational value.

So, a plea to the profession: the power is in your hands – embrace this challenge and future-proof the accounting profession by ensuring its norms, values, networks and education support a sustainable world view. There is no other.

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<sup>10</sup> ICAEW, (2004).

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