

Taking Professional Care of The Nature: The Environmental Audit

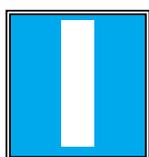
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< EXECUTIVE SUMMARY >

◆ Organisational response to the environment and the role of the accounting profession for the environmental protection are fairly recent developments. Environmental issues are business issues and have considerable implications for 'audit' in all its semblance leading to a separate specialised area viz., 'environmental auditing'. Within a short span of time, the environmental auditing has moved from being considered a marginal topic, to an increasingly central

role in the deliberations of the international accounting profession. It is seen as an essential element in any organisation's environmental response. In view of their core competencies in the field of auditing, chartered accountants can play a significant role in the 'environmental protection' - which is one of the essential objectives of the environmental auditing. This article has been intended, inter alia, to provide a good introduction to the business and environmental agenda and auditing.

INTRODUCTION



In 1998-99, a company has reportedly established a soft-drink manufacturing unit in Kerala. By 2002, the unit has not only begun dumping foul smelling waste slurry on the nearby land, but also succeeded in contaminating the water to the extent that it turns white on boiling and is unfit for drinking, washing or even bathing. Over 1000 families have been affected in the surrounding villages within a radius of 5 kms., of

which a quarter are adivasis and the rest dalits and non-adivasis. It is also reported that the tribals in that area protesting peacefully for over 60 days now demanding that the factory from which over 39 lakh ml of beverages are crated out daily, be closed down. The slurry was earlier sold as fertilizer to ill-informed farmers. Later, as buyers turned wiser, it was given off free. Now, it is dumped forcibly[§].

The above news item, to say the least, is a tip of the iceberg of environmental impact by the business enterprises. No doubt that the financial reporting system is

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In this article references have been given to several companies in India and abroad. These references are by no means exhaustive of the many laudable environmental protection / management efforts at companies in many different industries throughout the world. Further, references to the companies are made purely on an academic viewpoint and by mentioning these examples, the author or the Editorial Board of the Institute, is not necessarily endorsing their environmental protection / management approaches.

[§] Based on *Earth Watch* column in *The Hindustan Times*, New Delhi, dated 16.6.2002

taking care internal and external requirements of financial information of the stakeholders of business (and non – business) entities including the one whose environmental impact was given in the previous paragraph. Furthermore, there is auditing function ensuring that the income statement and the balance sheet give the *true and fair view* of the income and financial position reported.

The auditing function therefore plays an important role in verifying whether an organisation is profitable or not, whether the financial position is sound or not – which are important information for the stakeholders. Such information is commonly referred to as ‘the bottom line’, for example the bottom line of an income statement gives an amount of money, which reflects either, a profit or loss. The bottom line, however, does not reflect environmental consequences (e.g. pollution) that may have been incurred in the process of doing business, as these are often difficult to measure in financial terms. The auditing function, which has established itself

ducted in the best interest of such stakeholders had faced a challenge to verify and attest whether the affairs of the organisation were conducted in the best interest of the environment or not. The environmental audit is a response to such challenge which is an attempt to provide information on the environmental performance of an organisation, and thus include environmental issues in the decision making process.

Environmental auditing originated in the United States in the 1970s as a way of checking whether a company was complying with a multitude of new environmental laws and regulations. More recently, it is used as an extremely valuable tool for assessing a company’s environmental management systems, policies, and equipments. It provides the company with recommendations on how it can improve its environmental management practices, and reduce the impact that a company is having on the environment. In addition, improved environmental practices often save money in the long run.



WHAT IS ENVIRONMENTAL AUDITING

The Confederation of British Industry[§] has defined *environmental auditing* as the systematic examination of the interactions between any business operation and its surroundings. This includes all emissions to air, land and water; legal constraints; the effects on the neighbouring community, landscape and ecology; the public’s perception of the operating company in the local area - *Environmental audit does not stop all compliance with legislation. Nor is it a ‘green-washing’ public relations exercise....Rather it is a total strategic approach to the organisation’s activities.*

Environmental audits can happen at many different levels, for example in commerce, industry, municipalities, and governments, and on a less formal level,

as one of the most important discipline for the purpose of promoting and protecting the stakeholders and ensuring that the affairs of the organisation has been con-

ducted in the best interest of such stakeholders had faced a challenge to verify and attest whether the affairs of the organisation were conducted in the best interest of the environment or not. The environmental audit is a response to such challenge which is an attempt to provide information on the environmental performance of an organisation, and thus include environmental issues in the decision making process.

[§] Confederation of British Industry *Narrowing the Gap: Environmental Auditing Guidelines for Business* (London: CBI) 1990

as a school adopting a recycling programme, or more complex changes, such as a supermarket chain introducing energy saving practices, the cumulative effect will benefit all of us.

OBJECTIVES OF ENVIRONMENTAL AUDITING

Environmental auditing has three broad objectives:

- ⊗ Compliance with regulatory codes;
- ⊗ Assistance in acquisition and disposal valuations; and
- ⊗ Corporate development towards green missions.

The following table shows the broad characteristics of these three objectives:

GENERAL CATEGORY	SPECIFIC AREAS
Compliance	<ul style="list-style-type: none"> - Legal conformity - Anticipated conformity with liability for new regulations - Review of mitigative and ameliorative programmes
Acquisition /disposal	<ul style="list-style-type: none"> - Sale of facility - Acquisition of facility - Valuation/appraisal of property for; - Insurance - Loan security
Corporate Development	<ul style="list-style-type: none"> - Monitoring of corporate environmental policy and procedures - Establishing baseline for development of 'green' corporate environmental programmes. - Assessing control system adequacy - Implementing and reviewing corporate environmental programme measure (mitigation and remediation) - Assessing risks in unregulated areas - Improving product or process quality through response to environmental; impacts (especially buildings, landscape, large engineering works)

CATEGORIES AND FORMS OF ENVIRONMENTAL AUDIT

Environmental audits can be divided into two categories:

1. *Cyclical auditing programmes*, where auditing is con-

ducted on a scheduled cycle of occurrences. This form of audit will be a central product of an environmental unit. Specialists drawn from inside the company or from outside consultants may carry it out.

2. *Single audits for special purposes*. These are more likely to be done by outside consultants.

Within any specific management strategy, the following audits may be seen as the same in essence, differing only in terms of their objectives, scope, the risks they seek out to assess and the management decisions, which they assist and inform:

⊗ Corporate audits, which consider the workings of the entire corporation;

⊗ Activity audits, which consider one activity of the corporation;

⊗ Risk audits, which consider safety, occupational health, and/or risk to employees and the public;

⊗ Compliance audits, which test industry compliance with relevant environmental and safety standards;

⊗ Energy Audits

⊗ Waste Audits

⊗ Site Audits; Reviewing every aspect of a site or spot checks on sites having actual or potential problems

⊗ Issues Audit: Review corporate performance in a particular area – e.g., in the case of Oil India or Sardar Sarovar Narmada Nigam Ltd., tropical hardwood

forests and impact on habitats

⊗ Activity Audits: Reviewing a particular activity or process, especially one that spans sites, business units and countries.

⊗ Process Audits: Related to the above and designed to ensure that policies, processes, documentation, responsibilities, monitoring and appraisal are in place

AUDITING

- ⊗ Takeover / Merger Review: Assessment of potential subsidiary, associate or partner against corporate standards and any actual and potential legal issues
- ⊗ Emerging Issues Audit: Future scenario assessment, anticipatory and intended to assess the intensity of the organisation's ability to respond to new challenge.

And, as the environmental management system develops, these audits will be closely related to:

- ⊗ Process Safety Audits: Hazards and risks arising from processes, safety and accident provisions.
- ⊗ Occupational Health Audits: Exposure and conditions for the workforce
- ⊗ Quality Audits: Not only the product in use but the environment in relation to Total Quality Management.

Some issues in the changing institutional framework (pressures for environmental change in business)[#]

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| <ul style="list-style-type: none"> • Voluntary Agreements on CFCs • Voluntary Agreements on CO₂ • Eco-labelling / Eco Logo • Waste Disposal • Contaminated Land • Packaging • Returnable containers • Recycling • Environmental Disclosures • Environmental Audit | <ul style="list-style-type: none"> • Sustainable Development • Ethical Investment • Green consumerism • Control of Road Transport • Energy Taxes • Tradable Pollution Permits • Greener employees • Public Pressure • Organisational Environmental Policy • Supplier Audits |
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THE ENVIRONMENTAL AUDIT PROCESS

The environmental audit process calls for a flexible and iterative process that, at its most broad form, encompasses the following:

- ⊗ A basic study of the existing situation;
- ⊗ A decision on the scope and coverage of the audit;
- ⊗ Early identification considerations without risking change. These must respond to environmental considerations without jeopardising core corporate objective; nor should corporate objective endanger environmental aspirations. Actions to develop environmental consequences may be three types:

- Ameliorative options, whereby negative impacts may be reduced in either quality or quantity;
- Mitigative options, whereby the negative impacts may be balanced by other actions which lessen or reduce its impact; or
- Compensatory options, whereby the negative impact may be tolerated in return for other forms of action to ease harm.

- ⊗ A systematic assessment of options. There must be a protocol for determining and assessing environmental options and their effects, as well as related corporate programmes, option appraisal is carried out to determine the relative attractiveness of different approaches. An option appraisal matrix is a concise method of arraying and distilling choices for decision, and for comparing their costs and benefits within a brief context. These appraisal matrices are discussed in further depth in Chapter 8.

- ⊗ Careful filtering of options. All the values, analyses, facts and interpretations must be reviewed to focus on the most relevant factors and issues. The emphasis must be on significance: which choices can lead towards a positive environmental outcome within the context of other considerations?
- ⊗ Repeated refinement and fine-tuning of the audit. Over time, new factors and considerations will be identified in relation to different options. There must be a method by which new findings are brought into the appraisal of options throughout the option

appraisal process.

- ⊗ Accurate and objective reporting to decision-makers. Findings and observations must reflect:
 - The best available technical knowledge of relevant factors and issues, and their repercussions; and
 - An accurate combination of the views, perceptions and values of different stakeholders within and outside the organisation.
- ⊗ Precise and timely public disclosure to stakeholders who have key powers in the decision-making process and to the public. Reporting corporate experience to

[#] Source: Accounting for the Environment: Rob Gray with Jan Bebbington and Diane Walters, Paul Chapman Publishing Ltd., London, 1993

Monitoring Systems (including Audit and Review)

- Performance against legal standards
- Performance against consent levels
- Performance against forthcoming law
- Performance against organizational ethical policy
- Performance against environmental policy
- Performance in all areas of environmental policy
- Analysis of complaints
- Highest standards audits / reviews
- Analysis of employee suggestion boxes
- Review of regular organizational data on wastes, emissions, leaks, accidents etc.
- Review of who gets the information and when. What is done with it?

Source: Accounting for the Environment: Rob Gray with Jan Bebbington and Diane Walters, Paul Chapman Publishing Ltds., London, 1993

the public leads to greater public understanding and the development of the science of audit. Indirectly, it benefits the organisation by establishing its reputation as a contributor to environmental improvements.

- ⊗ Diligent monitoring. During implementation of the chosen option(s) there must be systematic verification, to test projections and to permit useful and timely adjustments to the environmental strategy.
- ⊗ Timely adjustment and redefinition of the corporate systems. Environmental monitoring and auditing may require the alteration of a plant's operations or of the design of a new installation.
- ⊗ Systematic evaluation of the audit procedure.

As can be seen from the above, environmental audit is part of an organisation's overall decision-making process. By placing environmental objectives alongside other objectives, such as those related to finances and productions, the audit system is knitted into business operations.

TOWARDS A SUCCESSFUL ENVIRONMENTAL AUDIT

1. *Get support!* Best results are achieved when the environmental audit has wide support, and the changes it recommends are backed by everyone involved. Get permission for the environmental audit from the relevant authorities; involve as many people as possible and share the results of the environmental audit widely.

2. *Don't be dismayed:* Most answers to the questions will probably be "No, we don't do this" or "No, we haven't, not yet" - the purpose of environmental auditing is to identify where improvements can occur, not to pass or fail the institution concerned! If a great deal of work needs to be done, don't be daunted. Everything cannot change overnight, and change must be manageable, so pace yourself. The audit may lead to a two month, six month, one year or five year plan.
3. Build on environmental successes from the start. Every organisation has something right in its existing environmental performance
4. Gain and sustain top management commitment from the start. Ensure that your successes are fully understood by top management and the external stakeholders of the business
5. Set and achieve attainable short and mid-term target, which can be published by key middle and senior corporate managers
6. Make environmental audit part of the normal route to the top for ambitious younger managers
7. Build environmental auditing into the reporting cycle and use this as a basis for dialogue with insurers, investors and community groups.
8. From the start, use positive audit to inject good news into the environmental programme.
9. When possible, convert environmental benefits into financial cost savings and investor attractiveness, and these into the reporting cycle.
10. Rely on, manage and use the technical experts. You are the client and represent the corporate interest.
11. Corporate learning curve. Environmental goals need to be acquired and assimilated alongside financial, operational and personnel goals
12. Admit mistakes and shortcomings and agree goals for putting environmental problems right.
13. Respect your critics and develop methods of working their concerns.
14. Concentrate on discovering points where environmental performance can be converted directly into core financial and quality strategic targets.

PLANNING AN ENVIRONMENTAL AUDIT

An audit cannot be designed as a ready-made package to suit all circumstances. This framework will help you in researching and developing an audit to suit your particular needs.

- Identify the situation, or place, in which you will audit, e.g. the school grounds, the home kitchen, and the office.

- Select the area/s or issue/s that you will audit, e.g. waste management, energy, water or biodiversity.
- Identify key questions to focus your investigation within each issue, e.g. how do we attempt to reduce and reuse products, and recycle waste?
- For each key question identify additional questions to investigate the issue in more detail. The Enviro Facts listed below will provide background information to help you identify appropriate and meaningful questions. In developing these questions it is useful to consider the impacts of using a resource in your particular situation, and both before, and after your situation, for example:
 1. How much paper is used in the school?
 2. What are the environmental effects of afforestation and paper mills?
 3. What are the environmental effects of the waste paper?
 Work out remedial action, i.e. what can you do to improve the way in which resources are used.

INITIATIVES ON ENVIRONMENTAL AUDIT

World trade and globalisation depend on responsible business practices, if they are to win public confidence and deliver global prosperity. That is where codes of conduct come in, whether towards the environment, labour or other ethical rules. Almost all of the world's 100 largest multinational enterprises have issued environmental codes or policy statements on health and safety.

A close look at these codes shows that OECD companies are making a strong effort on environmental and labour issues. In fact, almost all of the world's 100 largest multinational enterprises (MNEs) have issued environmental codes or EHS (Environment, Health and Safety) policy statements. Mining, forestry and paper, for example, focus, though not exclusively, on rules of behaviour for environmental management, health and safety standards.

Apart from individual companies, trade bodies also promote standards of business conduct. Well-known initiatives include the Business Charter for Sustainable Development drawn up by the International Chamber of Commerce, the Responsible Care Initiative of the chemical industry to improve its environmental, health and safety performance, and the Charter for Good Corporate Behaviour drawn up by Keidanren in Japan.

Non-governmental organisations (NGOs), too, have issued sets of global principles, such as the Consumer Charter for Global Business developed by Consumers International, which links 200 consumer groups in more than 80 countries, or the Clean Clothes Campaign, a European initiative directed at the textile industry.

Supplier codes are particularly prevalent in the retail and

Environmental Charter of a school

AT ALL TIMES, THE PUPILS, STAFF AND FRIENDS OF SCHOOL WILL TRY TO:

- * Teach everyone about the importance of caring for the environment;
- * Keep the school and grounds clear of litter;
- * Save energy by switching off unwanted lights and heaters, and keeping doors and windows closed;
- * Recycle as much as possible, and use products with a recycled content;
- * Develop and improve the school grounds and plant more trees;
- * Keep the school a non-smoking zone

textile industries in United States of America and European Union. Here, prospective suppliers and contractors are often screened for child labour abuse and may be asked to sign up to a code as part of any contractual arrangement. Chemical firms in the Responsible Care Initiative factor environmental principles into their procurement decisions. Indeed, their suppliers must provide safety, health and environmental information on their products.

Nevertheless management practices are evolving. A number of organisations, ranging from accounting and audit firms such as to more specialised monitoring firms like Bureau Veritas, and NGOs, now provide external verification services. Also, auditing and monitoring standards are being developed. A large and growing number of internationally active companies are engaged in the process of adopting standardised and certifiable ISO 14001 or EU environmental management systems. They also disclose information about their performance through health, safety and environmental reports. For labour issues, similar standardised management systems are under development, e.g. Social Accountability 8000; Global Reporting Initiative.

There is also extensive government involvement in "voluntary" initiatives for corporate responsibility, both at the national level and through international organisations. The types of involvement include legal and regulatory incentives, tax expenditures, contribution to compliance expertise and so on. Recently India became a signatory to the *Stockholm Convention on Persistent Organic Pollutants (POPs)*. This meant eliminating the dirty dozen chemicals identified under the treaty.

ROLE OF CHARTERED ACCOUNTANTS IN ENVIRONMENTAL AUDIT

In order to be proactive to the requirements of the business environment, Indian chartered accountancy

profession has to the occasion raise once again as efficient and effective *environmental auditors* for protecting and promoting the interest of the stakeholder of business and non-business organisations. In view of their education, training and continuing professional education, the chartered accountants are capable of playing the following important roles (of course with appropriate fine tuning of their skills to meet the specific requirements of the type of the organisation for which they conduct the audit) in the environmental audit field:

- ✳ Effective internal environmental auditors for conducting continuous environmental audit or can conduct external—periodical or special purpose—environmental audit
- ✳ Ensuring compliance with the regulatory requirements both present and future
- ✳ Assisting organisations to formulate environmental policies to ensure their long term survival and development and monitoring adherence to such policies
- ✳ Acting as energy auditors (which is one of the important forms of environmental audit)
- ✳ Conducting—either on their own or along with other technical experts—other types of environmental audits such as waste audits, sites audits, activity audits etc., which have been explained earlier in this article.
- ✳ Important drivers of sound environmental management system of organisations through process safety audits, occupational health audits and quality audits.
- ✳ Systematic evaluation of the environmental protection options available to an organisations to ensure a holistic view of the environmental challenges being faced by the stakeholders
- ✳ Through proper Environmental Audit Reporting, they can keep the stakeholders informed about the environmental impacts of the operations of the organisations concerned, protective measures being taken by those organisations and more importantly the possible strategic impact of such impacts and protective measures.

NEED OF THE HOUR

The environmental challenge provides a much more formidable and permanent target for business than socialism or communism ever did, because a healthy environment is a necessary prerequisite for a healthy business. The environmental agenda is no longer one of ethical or social sentiment, or of mere do-gooder investment on the part of business organisations. It is now at the heart of corporate strategy. Without a secure base of environmental resources, no business organisations anywhere on the planet are safe from legal, political or financial pressures.

The central and state governments of India have been

taking appreciable efforts to protect the environment in form or the other. They range from *pollution clearances* at project planning stage by enterprises to *pollution control monitoring* by state and central pollution control Boards. Nevertheless, it is suggested that the Government of India has to make it mandatory of environmental audits for companies to begin with and all other business organisations in due course. To maintain uniformity and quality of environmental audits by professional accountants, it would be appropriate that the Institute of Chartered Accountants of India may come up with a detailed technical guide on the conduct of environmental audit. The Institute may also conduct appropriate training / education programmes to develop a new breed of auditors in our country viz., *environmental auditors*. For our country, environmental audit has to be taken as a movement rather than as *another type of audit*.

CONCLUSION

Environmental audit is undoubtedly the one area of environmental awareness that any organisation ignores at its peril. It is also massive, complex, amorphous and rapidly developing area. Environmental audit touches many areas of current, proposed and possible future environmental regulation and serves, for all organisations, as a first step towards environmental sensitivity and as a regular and essential part of environmental management systems.

Nevertheless, if business ever required all its skills at planning and innovation, it is surely in the area of environmental. We will never face a more difficult problem than to ensure that our products, factories, processes and distribution systems are not only undamaging to the environment, but in some way or other even enhance it. That is the standard to which our children and grandchildren will hold us.

Resource Section

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