

## Greening of Small & Medium Enterprises



*Small and medium enterprises (SMEs) are powerful engines of economic growth of a nation. Empirical evidences suggest that these contribute as much as 70% of the industrial pollution. Individual units may emit small amounts, but cumulatively they add to a substantial figure. Unfortunately, many are not aware of the problem they are causing or even if aware do not have finance to install equipment to arrest pollution. It is imperative to educate entrepreneurs about the impact of environmental issues in their own interest, to avoid inviting penalties or even stronger measures. They should be made to realise that sustainability will lead to profitability through reduced energy consumption. Production of eco-friendly products will enhance profitability, build their image and contribute to long term success. Several success stories of SMEs from all over the world are cited to illustrate the above points. The author argues that the accounting professionals as trusted business advisors of the SMEs, have a key role to play to usher in a green world. Read on...*



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### 1. Role of Small Enterprises in the Economy

Small and medium enterprises (SMEs) have been the engines of economic growth in all countries. According to the UNIDO (United Nations Industrial Development Organisations), *SMEs*

represent more than 90% of global business and account on an average, for about 50% of GDP of all countries and 60% of their employment. However, it goes on to state that these contribute significantly to industrial pollution, i.e., about 70% of all industrial pollution.

## 2. Environmental Behaviour of SMEs

Though the SMEs individually may not have a significant effect on the environment and resource use, they collectively exert a substantial impact. To understand why much improvement has not occurred on the sustainability front, we need to appreciate the dynamics of small business.

An SME is managed in part or in whole by its owner(s). Management is informal, without bureaucratic procedures and structures. In many cases, the environment impact of their operations is not known to them. Where the owner is aware, financial constraints may preclude him from installing protective equipment. Compared with the bigger listed companies that are increasingly under pressure by various stakeholders to report on their sustainability practices, the owner-manager does not have to answer to shareholders and a board and thereby has more freedom and power to implement sustainability practices or, to ignore them.

## 3. Impact of Environmental Concerns on SMEs

### a) Existential Threats

It is unfortunate that many SMEs have ignored concern for the planet at their own peril, as could be seen from the following cases:

- i) In the case of the village of Bichhri in Rajasthan, five small chemical industries operated without effluent treatment plants. Toxic effluents from the industry entered the ground water and the wells of fourteen villages became contaminated as a result. The Supreme Court directed the closure of the factories attached to the property of the polluter and directed the Ministry of Environment and Forests of India to recover the cost of eco-restoration from the industries held liable.<sup>(2)</sup>
- ii) Tanneries operating from Agra were discolouring Taj Mahal and hence the Supreme Court asked them to be shifted away from the Taj Trapezium (an area of

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10400 sq kms in the shape of a trapezium to regulate activities in relation to air pollution)---*M. C. Mehta vs. Union of India* AIR 1997 SC 734<sup>3</sup>

- iii) Several cases where industries were asked to be shut or moved to ecologically safe places are given under *Green Decisions: Summary of some Important Judgments*<sup>4</sup>.

These examples suggest that in spite of stringent environmental regulations and enforcement authorities in place, hazardous industries have continued to grow haphazardly, leading to many environmental problems in India. They highlight the fact that the enforcement agencies in India need to perform their compliance and enforcement duties more diligently, obviating many problems.

### b) Pressure from Customers:

Increased environmental and social awareness on the part of customers has resulted in their shunning of products manufactured by firms polluting the environment or adopting undesirable labour practices, such as employment of child labour. A few instances are cited below:

- i) Many European firms cancelled orders for carpets from India when they came to know that child labour is extensively employed in carpet making.
- ii) The Harkin's Bill introduced in the US Senate seeks to ban the import of products made in foreign countries which are documented users of child labour on a country specific basis. The textile and hand knotted carpet industries of South Asia are among the first targets of such law.
- iii) US blacklists Indian exports again for using child labour
- iv) "AHMEDABAD: India has been blacklisted for the third consecutive year by the US government for engaging child labour

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in its garment export industry, raising doubts over future sourcing deals with global brands. The country was named in the Executive Order List despite several attempts by the exporters to convince the US authorities otherwise.”

“Henceforth, whenever we engage in business with global brands, we will have to prove we are not guilty,” says Rajendra Hinduja, MD of Bangalore-headquartered Gokaldas Exports, whose clients include Nike, Reebok, Old Navy, Abercrombie & Fitch, Adidas, Diesel, Levi’s<sup>5</sup>.

#### 4. Business Imperative for SMEs to Conform to Sound Environmental and Human Practices

SMEs must appreciate that sustainability is neither morality nor altruism but a very mundane business proposition resulting in waste minimisation, energy efficiency, water conservation and pollution prevention, enabling cost savings and thereby profit improvement. The benefits accruing through environmental initiatives will be the most powerful point to drive home the importance of sustainability

to all SMEs. In fact, it is urged that sustainability will have to be integrated as part of an SME’s business strategy adopting a long-term vision closely tied to the strategic benefits and move away from the philanthropy, rather forced-giving, mindset.

ACCA (Association of Chartered Certified Accountants) SME & Entrepreneurship Policy Advisor Tatjana de Kerros says: *It is no longer a question of whether SMEs should invest in sustainability, but how to ensure it is embedded within their strategy to spur competitiveness. Sustainability can be a cost-advantage to SMEs if it focuses on the organisational capabilities and emulates the core competencies of the firm. SMEs are inherently more flexible and adaptive than their larger counterparts, and their size enables to operationalise sustainability with no radical or costly transformation. This can include new operating models, available technology and a new managerial practice that creates difficult-to-trade assets that increases the productivity and performance of the firm.*

CIMA, AICPA and CICA publication *SMEs Set Their Sights on Sustainability* gives case studies from UK, USA and Canada on how SMEs voluntarily embraced sustainability as a business opportunity, for their own success apart from benefitting people at large and enriching the planet.

International Finance Corporation, Ethos Institute and SustainAbility in their report *Developing Value—The business case for sustainability in emerging markets* highlighted the business benefits and risks from social and environmental improvements based on 240 cases from Africa, Asia, Latin America and Central & Eastern Europe. Business Case Matrix depicts the links and interrelationship between 7 sustainability and 6 business success factors:

Business Factors	Sustainability Factors						
	Governance & engagement	Governance Stakeholder	Environmental Process Improvement	Environmental Products & Services	Local economic growth	Community development	Human Resource management
Revenue growth & market access							
Cost savings & productivity							
Access to capital							
Risk management & license to operate							
Human capital							
Brand value & reputation							

In India too, we have several examples of SMEs growing from scratch to enviable heights by adopting sustainability practices. Business Today's *YES Bank SME Awards, 2012* cites inspiring stories of such successful SMEs.

*Ankur Scientific Energy Technologies* [awarded Star SME Overall (Small)] manufactures biomass gasifiers, mostly used for power generation, by burning biomass into gas that then is fed to engines to generate power. *Ankur Scientific* has now become a recognised name in gasifiers in India as well as in Europe and rest of Asia. *Yennai Hydrocarbon* [awarded Best SME-Social and Environmental Responsibility (Small)] uses solar power to run a large part of its Barmer campus in Rajasthan. It has planted more than 200 trees. It empowers people living in and around Barmer by training them in skills required in oil and gas sector. It has set up an oilfield training centre where it provides hands-on training to engineers aspiring for a career in oil and gas sector at a nominal cost. *Molecular Connections* [awarded Best SME for Innovation (Small)] provides innovative technology combining biology, mathematics and IT which enables scientists to wade through a lot of research systematically and properly, structure the information gleaned as well, in order to discover drug targets, which is a term for any substance in the body-usually a protein-whose behaviour can be modified by an external drug leading to a cure. *Omega Electronics* [awarded Best SME Social and Environmental Responsibility-(Medium)] is



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manufacturing elevators that run on *solar and wind power*. It has already installed about 100 such energy-efficient elevators by April 2013.

### 5. Global Reporting Initiative (GRI) Guidelines and SMEs

Framers of the GRI Guidelines envisaged that the guidelines should cover all organisations irrespective of *any size, sector, or location*. The GRI further envisages that reporting is not only to cover the performance of an organisation in isolation, but also encompass all upstream and downstream entities. Reportedly, though over 3,000 sustainability reports have been issued up to 2011, reporting of the performance of supply chain entities have not gathered momentum. Example of ABB cited below should be a good model.

#### *Supplier Sustainability Development Program of ABB*

ABB took steps in 2012 to develop suppliers (who are mostly SMEs) into strategic business partners who share their commitment to sustainability under the Global Supplier Sustainability Development Program (SSDP). Under this programme, the ABB conducted 121 audits and trained more than 1,050 suppliers and 1,255 ABB employees in 2012 focusing on Brazil, China, India and Mexico. A customised internal training program was also launched during the year enabling the ABB employees to achieve certification as sustainability auditors.

The program is structured around a combination of training for both suppliers and the ABB employees, onsite auditing and monitoring of performance improvement plans. ABB Supplier Code of Conduct underpins the SSDP, defining minimum standards regarding fair and legal labour conditions, occupational health and safety, environmental responsibility and business ethics.

Such audits resulted in improved audit performance by suppliers who participated in the training programs. However, audits continue to reveal a number of situations where the ABB's standards were not met. The issues discovered during audit included excessive overtime, inadequate remuneration, poor waste storage and disposal practices, and a lack of appropriate protective equipment for workers. No cases of child labour were detected in 2012.

ABB supply chain or quality managers are assigned to follow up the corrective action plans.

Should a supplier fail to comply with the corrective action commitments, ABB commences a process to de-source that supplier. During 2012, four suppliers were blocked due to unsatisfactory progress with corrective actions. Purchases from these suppliers were suspended pending satisfactory progress by a defined date. Should these suppliers not meet these requirements, the next step will be their removal as the ABB-approved suppliers.

ABB believes that a strong supplier performance ensuring resilient, cost-effective and sustainable supply chains is a key factor in business success and critical to growth plans. It states that the SSDP is helping to embed sustainability principles along the supply chain contributing to its own success. All large companies should initiate such *Sustainability* programmes to speed up the process of greening the world economy.

## 6. Government's Support for Sustainability Measures

Credit Linked Capital Subsidy Scheme of MSME offers 12% capital subsidy for technological upgradation by small enterprises, which includes *anti-pollution measures and energy conservation machinery*.

### *Environmental Training*

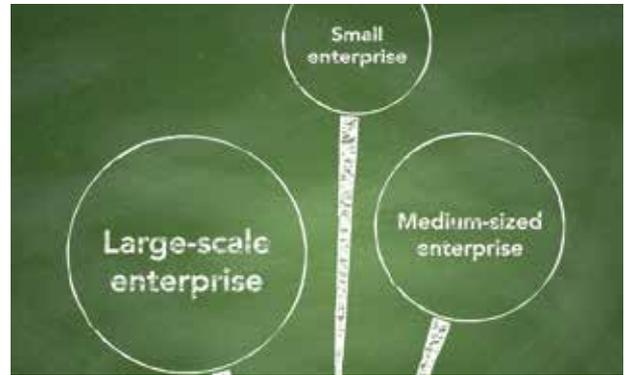
The Government is also organising several training programmes on various aspects of pollution such as air, water, chemical, groundwater, noise, medical waste, solid waste, *etc.*, to sensitise people to environmental issues through the *Environmental Training Unit (ETU)* of the Central Pollution Control Board.

### *Voluntary Guidelines issued by MCA*

The Ministry of Corporate Affairs of the Government of India had issued the voluntary guidelines on corporate governance, which include, *inter alia*, guidelines for the MSME sector keeping in view their special problems.

- Facilitating MSMEs to recognise the business case for adopting responsible business practices
- Preference by public agencies and large players in value chains to MSME suppliers that follow such practices
- Handholding MSMEs during the adoption of the guidelines

Public agencies as well as large enterprises may catalyse the process further by supporting collective



initiatives of the MSMEs in clusters. Capacity of the MSME associations could be built for awareness creation and to carry out collective initiatives.

## 7. Role of Accounting Professionals in Fostering Sustainability

Crucial role that CAs & CMAs can play in guiding SMEs to adopt sustainability practices have been elaborately spelt out in the reports of our sister bodies of UK, USA and Canada mentioned earlier. ACCA Global Forum for SMEs' recommendations contained in its publication *Embedding sustainability in SMEs* identifies a few areas of opportunities and activities for the management accounting professionals and their corresponding institutes. Accountancy institutions in India, *e.g.*, ICAI, may consider these recommendations for adoption.

### What Professional Bodies Can Do

ICAI and other professional bodies can promote the adoption of sustainable practices by providing members, either directly or through partnerships with:

- sources for information about sustainability and relevant regulation
- education on specific sustainability issues for business such as the implications of resource depletion and energy scarcity
- information about the SME aspects of the ISO 14001 and *Global Reporting Initiative* standards and industry-specific regulations
- training in specific environmental-accountancy techniques including environmental auditing, carbon costing, *etc.*
- develop or endorse a bespoke toolkit for accountants on environmental sustainability.

Accounting professionals should be the torchbearers for ushering in greener SMEs in a green world. ■