The Risky Side of Sustainability

Environmental risk is high profile. The experiences of Shell and Brent Spar, of Union Carbide in Bhopal and the daily lending practice of numerous financial institutions are testimony to that. Environmental risk can be measured as a financial liability arising in various ways from the effects of an organisation on the environment. And yet sustainability involves social and economic dimensions as well as environmental, so what about economic and social risk? This article explores the social dimension of corporate risk and suggests that there are ways both of identifying and managing that risk.

First of all, is environmental risk really all that environmental? Concern about the environment is a social phenomenon. It was almost absent until the 1950s, when Rachel Carson observed that there were no song-birds in spring. The rising tide of concern was viewed at first as extremist, but it is now not just fashionable, but received opinion that the environment matters. So even where the worry is entirely about the non-human world, there is a human and a social dimension.

A typical environmental report covers emissions, waste, energy and resource use as well as health and safety. The reason health and safety is in the list is that many health and safety issues are directly connected with the emissions and other environmental impacts which the report might cover. Yet health and safety matters because people matter – and that is a social phenomenon. I am not sure it is wise to claim, as I have heard a member of the environmental practice of a mainstream auditor do, that all environmental issues simply *are* social issues, but it is well worth while understanding the social component of corporate impacts, simply in order to understand the risks being run.

How can we think about social risk? Social risk is a measure of the gap between the boundary of responsibility which an organisation acknowledges and that perceived by its stakeholders. Who are the stakeholders? They typically include customers, shareholders, suppliers, staff, the community and pressure groups. The actual stakeholder list will vary from company to company, and must be thought through carefully.

So where an organisation has stakeholders which expect a company to take care of the environment or the local community or its staff – or any of a host of other issues – but the organisation does *not* think that these matters are its responsibility, then there is a risk. The risk is that the gap leads to misunderstanding, bad reputation, and possibly legal action.

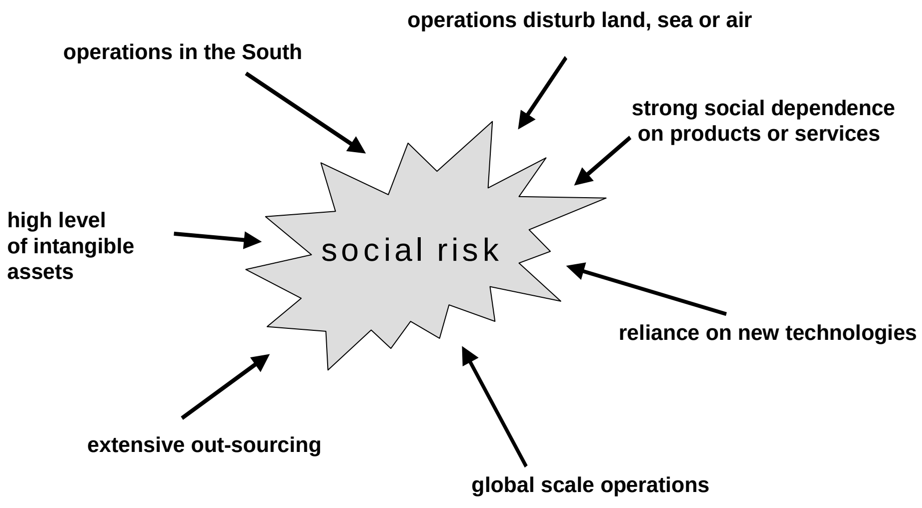
“Increasingly customers employees and shareholders have expectations about businesses’ standards of behaviour on issues like child labour. Businesses which do not meet these expectations may find it difficult to maintain their brand reputation, to recruit and retain the brightest and best staff or to find investors.” **Dr Kim Howells, Minister for Corporate Social Responsibility, DTI**

This approach enables us to clear up some of the confusion between environmental and social issues. It should be evident that the nature of the expectation may be either 'environmental' or 'social', and be subject to social risk. This approach also means that companies should be clear about who their stakeholders are. There may be a temptation to get round some of the issues by deciding to 'define out' a particular pressure group. Unfortunately that is not possible, even if the group contributes nothing to the business in financial terms. This was perhaps the history of Brent Spar. But in the end what matters is their expectation and how far that chimes with the values current in society at large.

So far we have looked at risk as solely a negative phenomenon. In other words, it is better not to have it because you will avoid the possibility of real costs to the business. There is a more positive side to the issue. The converse of a gap between expectations is that there is an agreement between the company and its stakeholders as to what a company should be doing. This creates trust, and trust is good for business. For example, if Gap acknowledged and showed that it was acting upon the concerns of the Living Wage Coalition, which is campaigning for improved conditions for workers in Gap's supply chain, then it might not be fighting such a publicity battle. There might be a possibility of greater customer loyalty.

What kinds of company are likely to be subject to social risk? While at one level the answer must be any company, there are fairly clear categories which are far more prone to such risks than others. The box shows some of the features to look for in deciding the level of social risk.

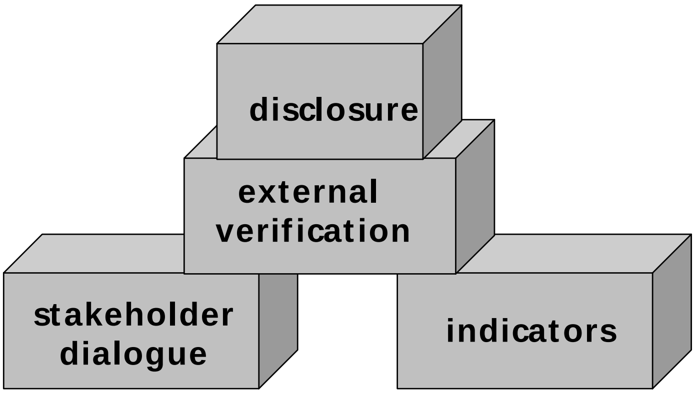
The Origins of Social Risk



Let us suppose that you are working for, or dealing with a company which has a high social risk profile. What should you expect it to be doing to manage that risk?

One way in which companies can manage the risk is to manage their stakeholders more effectively. That means working systematically to identify their stakeholders and to engage them in dialogue. This means not only having large formal meetings with pressure groups, but working with the people and communities affected directly. This process has been systematised as 'social auditing'.

Building Blocks of Social Auditing



Social auditing, in addition to dialogue with stakeholders, involves reporting on that dialogue and on what the company has achieved in relation to its stakeholders and where it is trying to go. A number of major companies, including Camelot, Shell and BT, have been doing this. While the quality of current social reports varies considerably, the practicality of doing it is fairly well established.

One important element of social auditing is that of verification. Verification is about trust. This is as true of environmental – and financial – reports as it is of social reports. Verification should enable a stakeholder to read the report with a greater confidence than if it were unverified. Clearly verification should reduce risk through providing credibility. So how reports should be verified and who should verify them are important questions which need to be answered to reduce social risk effectively.

Most recently, in order to address sustainability, there has been a trend to produce combined social and environmental reports. While these follow in large part the practices established by social auditing, it does emphasize the interconnectedness of the social and environmental issues and of the subtle nature of the risk that avoiding sustainability brings.

This brings us back to the starting point – while environmental risk has been recognised for some time, social risk also exists, but it can be defined and managed. In dealing with risk it is important to have an open mind as to the nature of the risk and a readiness to engage with stakeholders of every sort.