Master Class
Intellectual Content

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SILC Master Class
12 Hour Program

Learning Objective:

To learn how to create a customized ESG reporting template that reflects the mission, philosophy, and business objectives of the organization.

To help provide ESG assessment tools for due diligence when reviewing potential investments.

To give stakeholders a strong starting point and the ability to have greater clarity while navigating the complexity of sustainability reporting and assessment.

Core Components and Overview of Fundamentals (Six Hours)

C-1. Comprehensive Foundation
- a. Create a framework, e.g., Six Capitals, Triple Bottom Line
- b. Standard setting bodies and metrics

C-2. Industry-Specific Customization
- a. Define value and risk factors, e.g. COSO, Interbrand
- b. Sustainability Accounting Standards Board (SASB) guidelines

C-3. The Public Perspective
- a. Synthesize stakeholder goals into external stakeholder objectives
- b. U.N. Sustainable Development Goals (SDGs) and target indicators

Elective Components (Six Hours)

E-1. Single-Issue Standard Setting Organizations (Select two)
- a. Climate change (science-based targets)
- b. DEI
- c. Forced labor
- d. Biodiversity
- e. Other (add upon request)

E-2. Legal Requirements and Constraints (Select two)
- a. U.S. Securities and Exchange Commission carbon disclosures
- b. European Commission value chain disclosures
- c. Legal definitions of “carbon neutral” and “net zero”
- d. Legal definitions of “organic” and “free range”
- e. Other (add upon request)

E-3. “Black Box” Ratings (Select two)

a. Bloomberg
b. FTSE Russell
c. ISS Global
d. Moody’s
e. MSCI
f. Refinitiv
g. RepRisk
h. S&P Global
i. Sustainalytics
j. Other (add upon request)

ICYMI: Adding Age (A) to DEI Is a Good IDEA
Published March 2023 by the CPA Journal
Author: Richard Kravitz, MBA, CPA, Editor-in-Chief, CPA Journal

Just as the number of young students entering the profession has been shrinking, increasing numbers of older CPAs have been leaving due to forced retirement. Programs that expand diversity, equity, and inclusion are intended to expand the pipeline; however, the replacement rate of CPAs continues to decline. Even the pursuit of DEI is not without controversy, as advocates believe that older individuals are actively blocking other underrepresented groups from getting ahead.

This article looks at these challenges to the profession and suggests some commonsense solutions. It also highlights the negative impact that the loss of seasoned, knowledgeable, industry experts has had on independent audits, including the increase in critical audit deficiencies and adverse audit assessments recently observed by the SEC, PCAOB, and AICPA ("SOX 404 Disclosures, An Eighteen Year Review," Audit Analytics, July 2022, https://bit.ly/3fCBDt8).

The Impact of Fewer Qualified Auditors on Adverse Audit Assessments

The loss of knowledgeable, experienced CPAs with strong industry-specific expertise has been cited as a principal reason for the increase in audit deficiencies observed in PCAOB inspections. In its most recent report, the PCAOB identified auditor inexperience and the shortage of highly trained accountants as the number one reason why adverse Internal Control over Financial Reporting (ICFR) is now at its highest level since the inception of SOX in 2002 (Audit Analytics, 2022, pp. 1–3). The increase in adverse audits was detailed further by Audit Analytics:

The number of adverse ICFR management reports increased to 1,595 in 2021, up from 1,401 in 2020. The number of adverse ICFR management reports represents 23.7% of all management reports filed for fiscal year 2021, up from 21.7% in 2020. This is the highest percentage of adverse management reports filed since the inception of SOX 404. (https://bit.ly/3fCBDt8, p. 5)

The number one internal control issue cited in adverse ICFR Management Only Reports was the lack of trained accounting personnel resources. The Audit Analytics report further noted that "A lack of trained accounting staff was cited as a control issue in 48.7% of adverse auditor assessments and 71.5% of adverse management assessments." (https://bit.ly/3fCBDt8, p. 1)

Audit Analytics also highlighted the negative impact that inexperienced auditors have had in the financial services sector. Adverse auditor assessments of ICFR increased to 5.8%, and the percentage of adverse internal controls doubled, from 9.5% to 18.8%, between 2020 and 2021 (https://bit.ly/3fCBDt8, p. 1). Investments in high-risk SPACs

and other instruments over the past two to three years have resulted in a wave of restatements and hundreds of billions of dollars of lost stakeholder value. John Coffee, Corporate Governance Law Professor at Columbia University School of Law, argues that "restatements are indicators of fraud," which further undermines public confidence in auditors and in the integrity of corporate financial reports (Gatekeepers, Oxford University Press, 2006, p. 64).

Employee Benefit Plans Depend on Auditor Expertise

Experience matters, and the lack of expertise in the audits of employee benefit plans (EBP) is now a critical challenge for the profession. The number of EBP auditors has declined by around 40% since 2011, with an expectation of another decrease of about 40–50% in the next 10 years (Adam Lilling, conversation with author, 9/30/2022). The amounts involved are staggering; as of mid-2021, according to the Investment Company Institute, 60 million Americans held almost $8 trillion in employer-sponsored 401(k) plans.

Serious deficiencies in EBP audits were disclosed recently by the AICPA, which led to its release of new guidance for EBP audits (SAS 136, Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA, effective 12/31/2021). The objective of this standard is to "overcome … the lack of expertise and inexperience in audits by their members of employee benefit plans" ("Experience Matters: New Standard for ERISA Plan Audits Address Persistent Deficiencies," Beth Garner, BDO USA, LLP).

Substandard audits, as evidenced by these increases in critical audit deficiencies, have the potential to color the public's perception of the value that CPAs provide through independent audits—raising questions about the public's trust and confidence in our institutions.

The Aging of the Profession

When a generation of talented professionals with specific expertise retires, it can represent a risk to public safety if there are not sufficient knowledgeable trained professionals to replace them.

Mandatory retirement ages are common at U.S. CPA firms; the average is between 64 and 65. Unfortunately, over the past decade, the retirement age of CPA firm partners has remained stable, or inched up a year or two higher in the largest firms (Rosenberg Practice Management Survey, 2021; see https://www.cpajournal.com/2022/01/19/state-of-the-profession/); thus, the careers of the most knowledgeable experts in the profession often end once they reach this age.

The average age of partners in CPA firms in America remains between 52 to 53 years old. This means that, unless there is a sea change in mandatory retirement

requirement, the majority of U.S. CPAs will be forced to retire within the next decade or so. This applies across firms of all sizes, as reported in the 2021 Rosenberg Practice Management Survey:

In firms whose net fees are less than $2 million, around 18% of firms use age 65 as the required age for retirement. But what is more revealing is that year over year, the number of partners scheduled to retire within the next three years has doubled to over 15% of the labor force. …

In firms whose net fees are between $2 million and $5 million, a little over 50% of the firms have a mandatory retirement at age 65. About 15% plus of partners are expected to retire in the next three years. …

In firms whose net fees are between $5 million and $10 million, over ¾ of the firms have mandatory retirement which is on average at age 65. However, some firms require partners to retire at age 62. Only in one firm is mandatory retirement at age 70. About 14% of partners are expected to retire over the next three years. …

In firms whose net fees are between $10 million and $20 million, almost 18% of partners plan to retire in the next three years.

In firms whose net fees greater than $20 million, 95% of firms have mandatory retirement at around age 65; 12% to 13% of partners within these firms are expected to retire within the next three years. (Rosenberg Practice Management Survey, 2021, pp. 194, 181, 155, 116, 155)

Could Regulation Increase Public Confidence?

Although some may tout regulation as the answer to the shortage of qualified auditors, John Coffee, corporate governance law professor at Columbia University, would disagree: "No amount of regulation or legislation can protect the public absent an effective gatekeeping function" (Gatekeepers, pp. 17-18). According to Coffee, while accountants, attorneys, actuaries, and analysts represent the "4 As" of the gatekeeping profession, only CPAs can certify that the financial reports of publicly traded corporations are fairly presented in accordance with generally accepted accounting principles, based on the franchise given only to CPAs under the Securities Acts of 1933 and 1934 and the Investment Company Act of 1940.

The fact is that 90 million Americans hold shares in U.S. publicly traded corporations, as well as nonpublic investments made through their retirement fund advisors. A significant reduction in the number of highly talented, knowledgeable, and expert CPAs could raise serious issues about the integrity of corporate financial reports, as well as the effectiveness of the $54.9 billion public company auditing market (Ibis World, https://bit.ly/3H15V46). In an age of distrust, the potential impact of a loss in

confidence in the financial integrity of business enterprise could be considerable, especially in today's uncertain economic climate.

Who Would Hire a Retired Partner?

No one describes the inability of older people to get hired, or the crisis that is hitting the labor market, better than Wolf Richter:

Ageism is a real problem. And it could also be responsible for the low labor force [participation] getting stuck at this level. Boomers are now between around 56 and 76. This is a huge generation. And in tech, when the hiring manager is 32, and you're 56, it's tough getting that job; when you're 62, it's even tougher just to get anyone's attention. Some succeed, but many don't. Many of these people, often with a superb job history, may never get a job in their field again. Many of them made enough money to where they don't have to work. They'd like to work, but it's tough getting ignored or rejected time after time because of age. And they give up "actively" looking for a job, and thereby they're removed from the labor force. They were dropped from the labor force due to ageism, not because they wanted to retire. And they might tell everyone, after they give up looking, that they're "retired," when in fact, they'd love to work in their field but are locked out. (Wolf Richter, Wolf Street Report, July 8, 2022)

The Intersection of DEI and Ageism

Professors Michael S. North and Ashley Martin studied the advances that are being made in workplace diversity and inclusion, including the support for women and racial minorities. Their research focused on how these efforts are outpacing and, in some cases, hindering support for older workers. In nine studies, Martin and North found that people who hold egalitarian beliefs "harbor more prejudice toward and allocate fewer resources to older individuals as compared to other discriminated groups" (A.E. Martin and M.S. North, "Equality for (almost) all: Egalitarian Advocacy Predicts Lower Endorsement of Sexism and Racism, but not Ageism," Journal of Personality and Social Psychology, vol. 123, no. 2, pp. 373-399, 2022, as reported in NYU's Stern Business alumni magazine, Spring 2022, p. 11).

Martin and North further report that age-based retirement expectations by multiple disadvantaged identities highlights that older people need to "step aside." The authors "argue that egalitarian advocacy—efforts to create equal opportunity for all groups—predicts greater likelihood to support 'succession–'based ageism, which prescribes that older adults step aside to free up coveted opportunities (e.g. by retiring)." (Martin and North, 2022) The researchers concluded that ageism not only gets left out of our conversations surrounding diversity, equity, and inclusion (DEI) efforts, but in some cases it is actually implicitly or even explicitly endorsed by DEI efforts.

Including All Generations

The acute shortage of qualified, experienced, and industry-expert CPAs is not easily being tempered by new entrants to the profession. But just as COVID has transformed the employment landscape and made working remotely an accepted practice, might a model be created that could eliminate the discriminatory impact of forced retirement and improve knowledge transfer to the next generation of professionals? In a recent book entitled The 100-Year Life, authors Lynda Gratton and Andrew Scott argue that "retirees" have one-third of their lives to contribute to society and the public good (Bloomsbury Business, 2017).

There is room for all; but who will lead? This author has observed that, within Japanese and Dutch corporations for example, there are incredible roles within an organization for individuals to mentor, train, and educate young professionals in addition to their traditional roles. The result is a win–win. Older professionals have more personal time to spend with family and other pursuits, maintain meaningful employment, and—most importantly—transfer the expertise and knowledge that was built over a long career to the next generation of professionals. Adding "age" to the factors of diversity, equity, and inclusion is an idea whose time has come.

Finding the Right ESG Framework: Which Standards Setters Should You Choose?
Published November 2023 by the CPA Journal
Author: Michael Kraten, PhD, CPA, Director of Accounting Program Initiatives, C.T. Bauer College of Business, University of Houston

On March 18, 2022, Wolters Kluwer's Expert Insights published "The 5 biggest hurdles to effective ESG [environmental, social, and governance] reporting." Unsurprisingly, "multiple ESG frameworks" was the No. 1 hurdle. The authors declared that "While no single, global standard for ESG reporting exists, there sure are a lot of regional or industry-specific standards to choose from … the long and short of it is, to meet investor demand, adequately showcase your organization's sustainability in a comparable way, and meet the criteria for ESG credit scoring, your organization will have to choose one or more frameworks to adhere to."

This is not an isolated sentiment. On May 13, 2021, the Financial Times published, "Measuring what matters: the scramble to set standards for sustainable business." The authors noted that, "the current measurement and reporting landscape can be frustrating and confusing. In fact, more than three-quarters of respondents to our FT Moral Money questionnaire thought there were too many different measurement standards."

Indeed, according to the Financial Times, "by 2018, more than 600 ESG ratings and rankings existed globally, according to consultancy SustainAbility." But how many of these ratings are actually in widespread use? And for firms with limited resources, which sets of ESG standards should be selected by their management accountants?

The purpose of this article is to assist organizations that have decided to incorporate ESG metrics into their management accounting and reporting systems, but that need guidance about selecting their standards from among the hundreds of available options. This advice is directed to CPAs in the private sector that work for such organizations, as well as CPAs in public practice that provide advisory services about the data management function.

Standards versus Regulations

A July 2018 CPA Journal article by this author, "Transforming Integrated Reporting into Integrated Information Management," relied on a model called "the Integrated Reporting Framework" to define a schematic data framework for an internal ESG data management system. This model, known colloquially as the Six Capitals Model or the Octopus Model, was the primary product of a standards-setting organization called the International Integrated Reporting Council (IIRC).

What happened to the IIRC since 2018? It merged with the Sustainability Accounting Standards Board (SASB) in 2021 to create the Value Reporting Foundation (VRF). One year later, the VRF consolidated into the International Financial Reporting Standards (IFRS) Foundation.

Some CPAs, pondering this dizzying array of organizational changes, might conclude that companies should ignore such entities and simply create data management systems that produce data that is required by regulation (or law). There are however two obvious concerns that make this approach infeasible:

- New regulations often reflect the priorities of the political party that currently holds power. The United States, for instance, was a central member of the Paris Climate Accords during the Obama administration, a withdrawn non-member during the Trump administration, and (once again) a central member during the Biden administration. A data management system that is based on governmental rules would thus be “whipsawed” by such political volatility.

- The design of new laws and regulations is often informed and influenced by the experiences of standard setting organizations. For example, Exxon Mobil has relied heavily on the standards of the International Petroleum Industry Environmental Conservation Association (IPIECA). This trade association was founded during the 1970s, long before the emergence of contemporary ESG laws and regulations. Thus, its political lobbying influence would be negated if energy companies like Exxon Mobil ignored its trade association’s industry standards and simply reacted to legal and regulatory changes.

To be sure, information management systems must be capable of producing external reports that meet government requirements. But because of these two concerns, it is more practical to utilize professional standards to define the parameters of an ESG information management system than the transitory laws and regulations that may exist at any specific point in time. The preferred approach (i.e., to use standards over laws and regulations) is analogous to utilizing FASB standards to define bookkeeping practices instead of relying upon IRS taxation or SEC disclosure regulations to do so.

Which Standards Do Companies Actually Use?

To answer this question, it’s instructive to review the actual choices of a representative set of companies across industry sectors. The food and beverage, oil and gas, and media and entertainment industries represent a suitably diverse trio.

McCormick & Company, headquartered in Maryland, produces spices for food and beverage industry customers across all (small, medium, and large) segments. Which ESG standards setters do they reference in their 2022 Purpose Led Performance (PLP) report (https://bit.ly/3QsvfVi)?

The indices and data section refers to four standards setters: the Global Reporting Initiative (GRI). SASB, Task Force on Climate Related Financial Disclosures (TCFD), and the United Nations (UN).

Halliburton is obviously a very different type of organization; as one of the world's foremost crude oil production service companies, its customers are focused on the large end of the energy industry sector. Which ESG standards setters do they reference in their 2022 Annual & Sustainability Report (https://bit.ly/44Z0g7F)?

Once again, the data tables section refers to four standards setters: the GRI, SASB, the TCFD, and the UN.

The Walt Disney Company is a global entertainment and media firm, based in California, that sells its products and services directly to consumers (i.e., B2C) and also distributes them to a wide variety of small, medium, and large retailers (i.e. B2B). Which ESG standards setters does Disney reference on its "ESG Report Center" guide to its Corporate Social Responsibility (CSR) Reports (https://bit.ly/3OMBtxZ)?

It explicitly cites four sets of reporting frameworks: the GRI, SASB, the TCFD, and the UN.

Thus, across this very diverse array of organizations, there is a consistency in the standards setters chosen. Based on these results, one can answer the following two questions:

- How many ESG standards setters do we really need? The answer is four.
- Which standards setters, out of the hundreds of available options, should we choose? The answers are the GRI, SASB, TCFD, and UN.

But why is this true? And is it likely to remain true?

The Four Needs

It's important to note that users of ESG reporting data represent a variety of stakeholder groups with different types of needs. Users, for example, may include internal or external stakeholders who (each) may face a variety of less or more urgent risks. Furthermore, some of these stakeholders may focus on industry specific considerations, whereas others may not.

It can be helpful to define four specific types of metrics that serve these different types of needs. Although data users do not necessarily require one single standards setting organization to focus on each need, a "one standards setter for each need" market structure represents an efficient solution. The four needs are as follows:

- Metrics to manage extreme risks

- For all other non-extreme scenarios, metrics that address the risk impact from the perspective of external stakeholders
- Metrics to address the needs of internal stakeholders, some of which are universal across all entities
- Metrics to address the needs of internal stakeholders, others of which are specific to industry sector.

Each of these four needs is structurally unique and self-evidently relevant to the users of ESG data. Thus, it is unsurprising that firms as different as McCormick, Halliburton, and Disney have settled on four standards setters to help define their ESG metrics.

The Four Leaders

Each of the four leading standards setters has focused on meeting a specific need. Although there are significant overlaps, each entity approaches the design of its standards in a unique manner.

The GRI promulgates standards that address universal concerns for internal stakeholders. Its approximately three dozen standards focus on such ubiquitous topics as Market Presence (202), Procurement Practices (204), Energy (302), Waste (306), Training and Education (404), and Security Practices (410).

SASB promulgates standards that address industry specific risk factors by publishing customized guidance in 77 distinctly defined industry sectors. These industries vary widely, encompassing such diverse sectors as asset management and custody activities, healthcare delivery, and cruise lines.

The UN promulgates standards that address the risk concerns of external stakeholders. Its 17 categories or “goals” also vary widely, encompassing such diverse factors as quality education, affordable and clean energy, and decent work and economic growth. Its 169 metrics or “target indicators” are grouped into these 17 categories.

Because climate change appears to represent the most significant extreme risk facing humanity, the TCFD presently maintains a predominant position among standards setters. The TCFD has expanded the traditional focus on metrics by developing standards for the practice of enterprise risk management in general and scenario analysis in particular.

Why have the GRI, SASB, TCFD, and UN become so widely accepted in the ESG field? It’s because they have each been successful in addressing one of the four needs of ESG reporting. They are likely to remain so for the foreseeable future because their four needs collectively encompass the gamut of concerns that challenge internal and external stakeholders.

Of course, it is always possible that other standards setters will emerge and eclipse the current cohort. The International Sustainability Standards Board (ISSB), for instance, has been created by the IFRS Foundation to develop sustainability disclosure standards and recently released its first two efforts in this arena. At the present time, however, the ISSB is not cited in the ESG reports of American firms.

Likewise, it is always possible that new government laws and regulations may begin to drive the ESG reporting sector. Currently, though, it appears likely that government will move more slowly than the private sector.

Even in the European Union (EU), where ESG disclosure laws are more prevalent than in the United States, the Corporate Sustainability Reporting Directive (CSRD) only went into effect in January 2023. However, all EU member states must now “transpose” the CSRD into their national legal systems, with actual disclosure requirements not required until 2024.

ESG Report Design

So what sources should a CPA turn to if their CEO asks you to design an ESG report? And how often may you need to revise your choices?

If a trio of firms as diverse as McCormick, Halliburton, and Disney can all agree on using GRI, SASB, TCFD, and UN, anyone can. One can explain these choices by explaining that these metrics encompass the needs of both internal and external stakeholders, risks that are both high priority (i.e., extreme) and low priority, and challenges that are both universal and industry specific.

Will the choice of standards setters be permanent? Possibly not; after all, some other entity may eventually emerge that does a better job of addressing the full array of user needs than the GRI, SASB, TCFD, and UN. Recall that FASB itself replaced the Accounting Principles Board (APB) in the 1970s when it became evident that a newer entity was needed.

Nevertheless, unless this occurs, or unless a pair of ESG entities merge with each other, it is likely that these four standards setters will serve as the primary sources of ESG metrics in the near future. There is too much logic to having “four leaders for four needs” for the current paradigm to change significantly.

The Dawning of a New Era: the European Union Corporate Sustainability Due Diligence Directive (CSDDD) Is About to Enter into Force
Published June 13, 2024 by McAlan LC
Author: Allen Campbell, JD, MBA, Founder & Chief Executive Officer, McAlan LC

We've always known this would be The Big One, and now it's becoming reality. The CSDDD has passed the legislative hurdles. It now awaits only publication in the Official Journal of the European Union, 20 days after which it will enter into force. Member States will then have two years to transpose the Directive into national law and communicate the relevant texts to the Commission. One year later, the rules will start to apply to companies, with a gradual phase-in between three and five years after entry into force. The European Commission will issue a set of guidelines to help companies comply with the Directive.

In the words of the Commission,

"The aim of this Directive is to foster sustainable and responsible corporate behavior in companies' operations and across their global value chains. The new rules will ensure that companies in scope identify and address adverse human rights and environmental impacts of their actions inside and outside Europe."

Overview: This is a massive legal instrument. As stated by the Commission, here are the key aspects of the Directive:

The benefits of the new rules:

For citizens:
- More protection of human rights, notably including labor rights.
- A healthier environment to live in.
- Increased trust in businesses.
- More transparency, thus enabling informed choices.
- Better access to justice for victims.

For companies:
- Harmonized legal framework in the EU – a level playing field for companies to compete.
- Greater customer trust and employees' commitment.
- Better awareness of companies' negative human rights and environmental impacts, less liability risks.
- Better risk management, more resilience and increased competitiveness.
- Increased attractiveness for talent, sustainability-oriented investors and public procurers.
- Increased incentives for innovation.
- Improved access to financial resources.

For developing countries:
- Better protection of human rights and the environment.
- Sustainable investment, capacity building and support for value chain companies.
- Improved sustainability-related practices.
- Increased adoption of international standards.
- Improved living conditions for people.

Company obligations:

- “Corporate due diligence duty”: The main elements of this duty are identifying and addressing potential and actual adverse human rights and environmental impacts in a company’s own operations, in its subsidiaries, and, where related to their value chains, those of its their business partners.

- Climate change-related obligations: Large companies must adopt a transition plan for climate change mitigation aligned with the 2050 climate neutrality objective of the Paris Agreement as well as intermediate targets under the European Climate Law.

Which companies are in-scope:

- Large EU companies: Legal obligations are imposed on about 6,000 companies with over 1000 employees and over EUR 450 million turnover (net) worldwide.

- Large non–EU companies: Obligations are also imposed on about 900 companies with over EUR 450 million turnover (net) in the EU.

- Small and medium size enterprises: Micro companies and SMEs are not directly covered by the proposed rules. They will however be massively affected indirectly by virtue of being in the supply chains of in-scope companies. The Directive does provide some support and protection for them.

Estimated compliance costs:

Businesses will have to bear:

- The costs of establishing and operating due diligence procedures.

- Transition costs, including expenditures and investments to adapt a company’s own operations and value chains to comply with the due diligence obligation, if needed.

Enforcement:

The rules will be enforced through:

- Administrative supervision: Each Member State will designate an authority to supervise and enforce the rules, by means of injunctive orders and effective, proportionate and dissuasive penalties (notably fines). At the EU level, the Commission will set up a European Network of Supervisory Authorities that will bring together representatives of the national bodies to ensure a coordinated approach.

- Civil liability: Member States will ensure that victims get compensation for damages resulting from an intentional or negligent failure to carry out due diligence.

The Political Context:

Sustainability is often understood to be the same thing as ESG (the environmental, social and governance factors of a business). In less than about 30 years, sustainability/ESG has become a dynamic new force in the global business ecosystem. The CSDDD is in the tradition of ESG, but it is only focused on the “E” and “S”, and does not deal with the “G”. (The G component was in the first version of the CSDDD, the Mandatory Due Diligence [MDD] Directive.) Does this mean, as many people have argued, that the G component is less important than the E and S components? Does it suggest that the G component will gradually run out of gas? Time will tell.

The CSDDD is on the cutting edge of sustainability. Europe has been the leader in sustainability regulation. The CSDDD is a truly progressive law, and it was the recipient of hard political bargaining. The European Commission finally adopted it on May 24th. As stated above, it mandates behaviors. It follows and is in the tradition of the recently enacted EU Corporate Sustainability Reporting Directive, which mandates reporting. Mandating reporting and behaviors can be seen as a one-two punch.

A few days ago, only weeks after the Commission acted, elections were held throughout Europe, and the results showed significant gains for hard-right and right-leaning parties. Only time will tell whether the changing political winds in Europe – or elsewhere – will impact this due diligence legal initiative.

In the meantime, here in the US, the State of California is quite progressive with respect to sustainability and has enacted three laws within the last twelve months. Like the EU’s laws, the California laws have major effects on companies that are not domiciled there.

Recommendations:

For more than two years we have been urging companies to pay attention to this legislation, to consider its ramifications for operations and supply chains, to begin re-thinking their business models and practices, and to gear up accordingly. More than ever, that is excellent advice.

Remember too that there will be opportunities for forward-thinking companies.

In effect, over the next few years, all sizable companies will find themselves affected by what I call Value Chain Sustainability laws. They will impact the global trading system. It seems likely that some collaboration will be necessary. We recommend that companies explore possible collaborative responses, possibly in cooperation with the EU and its Member States.

The Time is Now: A Breakdown of the Costs, Benefits, and Opportunity of Labor Sustainability Reporting
Completed: April 23, 2024
Author: Mark Doan, Junior Year Student, St. John's School, Houston, Texas

The costs and risks of reporting on labor information disincentivize many companies from issuing reports. However, companies should focus less on the costs and more on the benefits and increasing need for reporting. Ultimately, the modern demands for information make reporting a crucial lifeline and an invaluable opportunity for companies that wish to both stay in the competition and bolster their reputations.

The business costs of acquiring information about labor conditions and the potential legal risks of releasing such information discourage many companies from issuing reports.

When seeking to collect labor information, many companies hire sustainability auditors to inspect their facilities and those of their suppliers. (See End Note 1) Companies often also purchase or develop data analytics software to observe overall trends in their workplaces such as employee satisfaction, working hours, and wages. (See End Note 2) Companies, regardless of the methods they employ, are ultimately required to set aside money and resources to gather this information. Furthermore, the time dedicated by staff members to reporting takes away from time that could be spent conducting more immediately profitable operations. As corporate reporting remains optional in many countries, companies are discouraged from incurring further costs when the benefits of publicizing their information also remain unclear. (See End Note 3) Companies willing to dedicate resources to analyzing their operations face the secondary challenge of dealing with information that could hurt them if publicized. If the data suggests labor conditions that do not align with standards set by major organizations such as the International Labor Organization, SASB, GRI, and the United Nations, informed consumers will likely reduce demand for the company's goods and services. (See End Note 4) In addition, poor results may bring about legal cases against the companies, harming their reputation and magnifying costs. Further legal risks may also emerge if companies attempt to falsify or cover up original information in their reports. In an attempt to avoid potentially costly business and legal risks, many companies will withhold information entirely. Thus as the benefits of reporting are unclear for many companies and the costs to business, reputation, and further legal risks are present, companies are not sufficiently convinced about reporting on their labor conditions.

Companies, however, should feel pressured into releasing labor information as significant benefits exist. Corporate reporting conveys to consumers and stakeholders an attentiveness to detail as companies are comprehensively articulating labor conditions across their supply chains. By dedicating resources to investigating and reporting on the well-being, safety, and fair compensation of their employees,

companies demonstrate an awareness of the impacts of their industry and goods or services. Reporting further educates companies about the sustainability and efficiency of their operations. For example, reporting can prompt companies to identify and replace lagging machinery and equipment consequently boosting production efficiency and worker safety. Additionally, reporting can help companies improve their workplace governance and dynamics by providing employees with opportunities to voice their concerns through feedback systems such as interviews and surveys. Furthermore, companies through reporting create opportunities for themselves to strengthen their regulatory compliance and minimize the chance of future catastrophes. (See End Note 5)

Ultimately, in this age of information where content is highly accessible and demanded, the costs to companies of not reporting on labor conditions outweigh the costs of getting started. Primarily, companies are at risk of falling behind in the evolving marketplace if they withhold information from the public about their labor sustainability. The urgency of sustainability has grown significantly, especially among younger generations, and is influencing consumers' decisions. (See End Note 6) Failing to make demanded information accessible to these consumers, especially as other companies are beginning or have been doing so, isolates companies from the main competition and will gravely detriment business activity in the coming years. Furthemore, due to the informational age, the opportunities presented by reporting on labor sustainability are growing in scale and the refusal to seize them will severely stunt companies' progress. Companies that employ web marketing methods such as social media promotions and website advertising expand their online following. By making information about the quality of their labor conditions available to young, receptive audiences, companies are presented with significant opportunities to improve their credibility and attract more business. Additionally, as news headlines and updates circulate more quickly today, companies are increasingly at risk of being called out for various labor violations. In their reports of labor conditions, though, companies can proactively inform public audiences of the measures they have taken to address various concerns before it is too late to defend themselves. Thus, companies should report on labor conditions as they will benefit significantly and because the modern age of information demands it from them.

In this highly competitive marketplace, the costs and risks of reporting on labor conditions are intimidating to companies and appear as if they are not worth incurring. However, companies must be aware that significant benefits are available to them if they make such information accessible to modern, interested audiences. Even further, the easy access and consequent high demand for information has made reporting on labor sustainability both a growing benefit and a necessity for today's companies.

Sidebar: The Turnaround of Sime Darby Plantation

On December 30, 2020, the United States Customs and Border Patrol issued a withhold release order on palm oil and its derivative products produced by Sime Darby

Plantation Berhad in Malaysia based on information that the company was employing forced labor along the production process of its goods. According to the CBP's investigation, Sime Darby Plantation was exploiting the labor of their foreign, migrant workers through the harvesting of fresh fruit bunches that were used to make palm oil. Over the three months provided to them by the U.S CBP to eliminate forced labor practices and sufficiently demonstrate a stance against coercive labor, Sime Darby Plantation hired an ethical trade consultancy to audit and investigate its premises and working conditions. Following its investigation, the company released this information to the United States government and its consumers in its latest sustainability report. Furthermore, the company designated twenty million dollars to repay the fifteen to nineteen thousand active and former migrant workers who were trapped in debt bondage. Ultimately, on February 1, 2023, the CBP lifted its two-year import ban on Sime Darby Plantation's palm oil products, allowing for formal trade with the company to resume.

The withhold release order placed on Sime Darby Plantation due to suspicions of labor rights violations emphasizes the significance of a company's labor practices. As demonstrated in the case of SDP, a failure to recognize signs of labor rights violations can isolate a company from consumers. Fortunately, for SDP, as a result of its leaders' initiative to rid forced labor from their operations, transparency of information, and pronounced commitment to sustainability, the company rescued itself from complete failure and maintained its position in the global marketplace. However, to avoid the risks of incurring costs such as reputational damage and profit losses, companies should get ahead of the game by being transparent with their consumers about labor conditions and being aware of the status of their operations from the start.

End Notes

(1) "What is a Sustainability Audit?," ESGTheReport, Published November 15, 2021. https://esgthereport.com/what-is-a-sustainability-audit/. (The three main types of sustainability or ESG audits are external/third-party audits, internal audits, and self-evaluation audits. Companies through audits are informed about their sustainability and profitability, more prepared when stakeholders question their sustainability, and more aware of potential areas for improvement.)

(2) "What Is Sustainability Data Management and Reporting Software?" Published September 29, 2022. https://novisto.com/what-is-sustainability-data-management-and-reporting-software/. (Companies turn to sustainability data management and reporting software to overcome challenges such as complex data gathering, changing reporting frameworks and requests, uncertainty with quality of data, and difficulties in analyzing ESG risks and opportunities. Acquiring and renewing such up-to-date and efficient software, while it improves data collection efficiency, can be financially intimidating for emerging companies.)

(3) Michael Kapoor. “European Businesses Poised to Lead Global ESG Reporting Rollout.” Bloomberg Law, December 27, 2023, https://news.bloomberglaw.com/esg/european-businesses-poised-to-lead-global-esg-reporting-rollout.; “At Least 10,000 Foreign Companies to Be Hit by EU Sustainability Rules.” Wall Street Journal, Published April 5, 2023. https://www.wsj.com/articles/at-least-10-000-foreign-companies-to-be-hit-by-eu-sustainability-rules-307a1406. (The European Union, via its Corporate Sustainability Reporting Directive (CSRD), requires at least 50,000 European companies to report on their ESG matters and around 10,000 non- European companies, of which a third are in the United States, to do the same. Only Brazil has announced plans for its companies to meet International Sustainability Standards Board (ISSB) standards and the UK, Australia, and Japan have considered incorporating such standards into their regulatory frameworks, however, no other nations have explicitly committed.)

(4) Anne Field, “Conscious Consumer Spending Could Be At A Tipping Point.” Forbes, November 30, 2023, https://www.forbes.com/sites/annefield/2023/11/30/conscious-consumer-spending-could-be-at-a-tipping-point/?sh=7fe5139421ad.; Kim McCann, “Conscious Consumerism is Transforming Industries.” The Consumer Goods Forum, October 4, 2021, https://www.theconsumergoodsforum.com/blog/2021/10/04/conscious-consumerism-is-transforming-industries/. (Sustainability-minded or socially-conscious consumerism describes the modern consumer's appetite for sustainable business practices, goods, and services and has been growing vastly over the past decade largely on account of peoples' knowledge about the state of the world and access to company information. In 2023, the socially responsible marketing consultancy Good.Must.Grow reported a Conscious Consumer Spending Index value of 57, its highest value in the past three years.)

(5) Gokul Shekar, “The 9 benefits of ESG reporting for modern businesses.” illuminem, Published August 31, 2023.https://illuminem.com/illuminemvoices/the-9-benefits-of-esg-reporting-for-modern-businesses.; Barbara Strozzilaan, “The value of sustainability reporting and the GRI Standards.” Global Reporting Institute, https://www.globalreporting.org/media/jzylu3ek/the-value-of-sustainability-reporting-and-the-gri-standards.pdf. (The most commonly cited benefits of sustainability reporting to companies include enhancing business activity through investor attraction, reputation strengthening, increased cost efficiency, awareness of innovation opportunities, and employee and developing stakeholder trust. Reporting also has more long-term benefits such as anticipating down-the-line disruptions, goal setting, and laying down the framework for a company's sustainability-focused strategy and activity.)

(6) Anne Field, “Conscious Consumer Spending Could Be At A Tipping Point.” Forbes, November 30, 2023, https://www.forbes.com/sites/annefield/2023/11/30/conscious-consumer-spending-could-be-at-a-tipping-point/?sh=7fe5139421ad.; Kim McCann, “Conscious Consumerism is Transforming Industries.” The Consumer Goods Forum,

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Richard Kravitz, MBA, CPA, Editor-in-Chief, CPA Journal

Richard "Rick" Kravitz is an award-winning senior publishing and online media executive whose focus is on strategic growth and transformational leadership. His focus is on business strategy [mission, purpose], and new product development; flawless execution in migrating traditional print publications to online media; monetizing results. His specialty areas include legal publishing, and creating advanced sequential learning programs and platforms for global online study.

Rick has a strong background in publishing and content management. He holds the position of Editor-in-Chief of the CPA Journal at the New York State Society of CPAs, where he also serves as the Managing Director of Content and Publishing. At the Texas A&M University School of Law, he works as an Adjunct Professor.

Prior to these roles, Rick was the Managing Director of Premium Content and VP of the Professional Publishing Division at Summit Business Media / The National Underwriter Company. he also served as the Executive VP of Business Development at Wolters Kluwer law and business, he demonstrated expertise in building top publishing companies and expanding digital media portfolios. Furthermore, he held the position of Managing Director at Wolters Kluwer Law Legal Tax International and President of Panel Publishers, as well as Senior Vice President and Group Publisher at Aspen Publishers at Wolters Kluwer Legal & Regulatory US. He is known for his contribution to revenue growth, new product development, and successful acquisitions throughout his career.

Rick has a Master of Business Administration (MBA) degree, which he obtained from NYU Stern School of Business. He pursued his MBA from 1976 to 1978, with a focus on accounting, marketing, and finance. Before that, from 1971 to 1974, he attended New York University's college of arts and sciences, where he studied economics and Spanish literature. In addition, Rick Kravitz has obtained the certifications of CPA, CGMA, Fellow Cr.FA., and MBA from a licensed profession.

Michael Kraten, PhD, CPA, Director of Accounting Program Initiatives, C.T. Bauer College of Business, University of Houston

Michael Kraten, PhD, CPA is currently serving as the Director of Accounting Program Initiatives at the University of Houston. He designs and teaches the graduate elective courses in sustainability accounting and entrepreneurship accounting, and is also developing innovations for financial accounting courses that apply Artificial Intelligence capabilities to remote learning activities.

He is the winner of the TXCPA's state-wide Outstanding Accounting Educator Award for large colleges in 2024. He serves on the Board of Directors of TXCPA Houston, the Leadership Council of the TXCPA, the Editorial Advisory Board of the CPA Journal, and the Advisory Board of the Center for Professional Accounting Practices at Fordham University.

He is a management consultant who maintains specialties in valuation, risk management, business modeling, sustainability, decision analysis, forensic analysis, educational gaming, and strategic planning. He is also deeply involved with several development initiatives that address the "pipeline" challenge of attracting students to the Accounting profession.

He began his career in the assurance and consulting practices of Deloitte. After serving as a Consulting Partner at BDO, then the sixth largest global accounting firm, he co-founded a series of boutique consulting practices. In academia, he previously served as Professor of Accounting and Chair of Accounting, Economics, and Finance programs at Houston Baptist University.

Earlier in his academic career, he taught for the Universities of Connecticut and Massachusetts in the U.S., Maastricht University in the Netherlands, and elsewhere. He has also presented his work at Dartmouth College, Deloitte University, Harvard Law School, Johns Hopkins University, and Yale University.

He has authored or co-authored more than thirty peer reviewed articles in the Journal of Banking and Finance, the International Journal of Accounting, Research in Accounting Regulation, the CPA Journal, the Journal of Financial Planning, and elsewhere. In addition, he has authored numerous book chapters, newsletters, and podcasts for Wiley, Routledge, Henry Stewart, Kaplan, and others. He also authored a book on Business Planning and Entrepreneurship for Business Expert Press.

From 2014 to 2023, the Social Science Research Network (SSRN) ranked him in the All-Time Top 10% of global researchers. His top-ranked article, entitled "Libor Manipulation," was published several months before the global banking scandal exploded in the public business press.

He earned a PhD in Behavioral Accounting from the University of Connecticut and a MPPM in Public and Private Management from Yale University. He also earned a BBA in Public Accounting from Baruch College, CUNY.

Allen Campbell, JD, MBA, Founder & Chief Executive Officer, McAlan LC

Allen Campbell, JD, MBA, Founder and CEO of McAlan LC, is a leading light in Sustainability with a deep understanding of the theory and practice of ESG. Informed by legal, financial and business experience, he is an authority on Value Chain

Sustainability legislation. He is an effective communicator and a skilled negotiator, and is adept at helping businesses and stakeholders “do ESG” well.

Allen understands that ESG, compliance and risk management are inherently intertwined. He is the creator of the R-ESG Model, which integrates Resilience (both business resilience and personal resilience) with ESG. He is also the creator of other proprietary systems for managing risk, compliance, ESG and resilience.

Allen is a graduate of the College of Wooster (AB), Columbia University (JD) and the University of Chicago (MBA) where he studied under three Nobel laureates. He started his professional life as an attorney with the Taft law firm (featured in the Dark Waters environmental justice movie). He was later an investment banker in New York in the corporate finance department of Bear Stearns, a major bracket investment bank that pioneered what became known as “private equity”. He then spent a year in Cambridge, Massachusetts as a full-time strategic advisor to the the chief executive of Arthur D. Little Inc., a leading international consulting firm, and the president of its ADL Enterprises unit. He then came to Dallas where he directed the corporate finance department of the regional investment banking firm Schneider Bernet & Hickman.

With all that educational and professional background, Allen became an entrepreneur.

Allen has founded, co-founded, owned or co-owned, many companies, including an investment research business whose quantitative work won many industry awards, and magazine companies that published American Visions, the official magazine of the African American Museums Association, and Marlin, about big game sport fishing. Allen created Murex Corporation, a biotechnology leader in the war against AIDS. Murex invented and commercialized the acclaimed Single Use Diagnostic System for HIV-1 (“SUDS”), which was the first, and for years the only, product approved by the U.S. Food and Drug Administration’s (FDA) for rapid HIV testing. Murex became International Murex Technologies, which became a publicly held company, and was thereafter acquired by Abbott Labs.

Mark Doan, Junior Year Student, St. John’s School, Houston, Texas

Mark Doan is a Junior Year student at St. John’s School in Houston, Texas with interests in economics and business. In the summer before his Junior year, Mark spent three months working at a local deli where he engaged in business operations and observed economic principles firsthand. Mark also attributes his interests to the countless hours spent listening to business podcasts in the car with his father.