Social audits

MODULE 5 | PART E.3 | STUDENT COMPANION

A **social audit** is the process an organisation uses to find out whether particular stakeholder groups see it as meeting its social responsibilities: its social contract. It is not the same as independent assurance of a sustainability report. It covers the organisation and its supply chain.

Area	Typical questions
Labour practices	Working conditions, health and safety, training
Fair operating practices	Fair competition, anti-corruption, and acting responsibly along the value chain
Consumer issues	Honest marketing and contracts, safe products, handling complaints, protecting customer data

Frameworks include: ISO 26000; SA8000 (Social Accountability International); ILO labour standards; the Ethical Trading Initiative Base Code; Sedex's SMETA audit; the Higg Index; WRAP; and the amfori code of conduct, whose principles cover freedom of association and collective bargaining, fair pay, health and safety, young workers, no bonded labour, ethical business behaviour, no discrimination, decent hours, no child labour, no precarious employment, and protection of the environment.

Case note - Ali Enterprises, Karachi: on 11 September 2012 a fire at the garment factory killed more than 250 workers; many were trapped, and reports described locked exits and barred windows. On 20 August 2012 the factory had been certified under SA8000, with the audit reportedly carried out by a local subcontractor of the certifying firm. **Lesson:** an audit is a snapshot. It works best alongside genuine worker voice, follow-up and a willingness to act.

Sources: ILO (10 September 2016); Social Accountability International Q&A (December 2012); Clean Clothes Campaign reports.

Governance mechanisms

1. **Policy and strategy**
   Sustainability policies, strategies and risk indicators built into corporate strategy, benchmarked and reviewed
2. **Formal structures**
   A board sustainability committee; environmental managers reporting to the board
3. **Stakeholder engagement**
   Find out what matters, give feedback on strategy and performance, agree what can change
4. **Recognised standards**
   ISO 14001: policy, then plan, implement, check and correct, review. ISO 26000: social responsibility guidance
5. **Linked pay**
   Executive pay tied to sustainability targets signals leadership is serious

Why it's hard

Responsible behaviour depends on culture, so regulation alone rarely changes much. Disclosure rules, such as the ASX recommendation on environmental and social risk, are only the start.

Environmental management accounting

MODULE 5 | PART E.3 | CONCEPTS AND A WORKED EXAMPLE

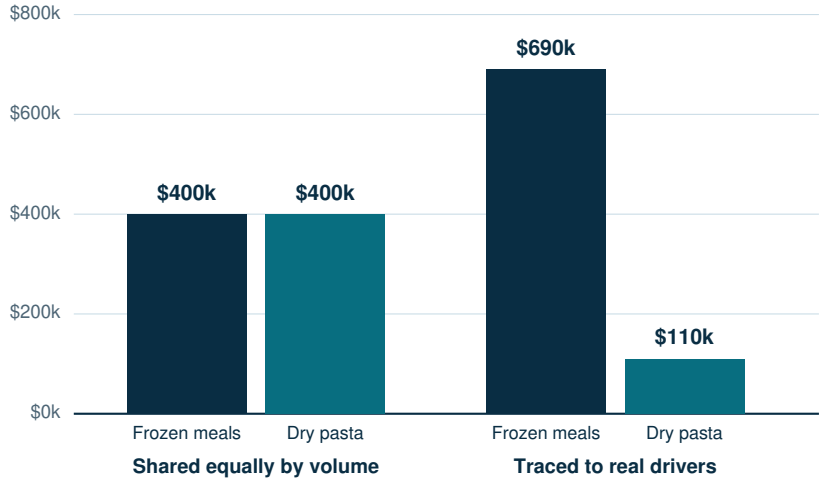
IFAC describes environmental management accounting as managing environmental and economic performance through management accounting systems that use **physical information** (flows of energy, water, materials and waste) and **monetary information** (related costs, earnings and savings). It pays special attention to materials, because they drive most environmental effects.

Prevention	Appraisal	Internal failure	External failure
Spent to stop environmental harm happening	Spent checking compliance with environmental policies	Spent eliminating harm the organisation caused, before it leaves the site	Relating to damage caused outside the organisation
Example: Redesigning a process to use less solvent	**Example:** Testing wastewater against licence limits	**Example:** Treating contaminated water on site	**Example:** Restoring a damaged wetland downstream

Scope choice

Count only costs recognised today, or extend to externalities as well

Hidden in overheads



The drivers

Frozen meals use about 90% of refrigeration energy ($600k) and create about 75% of trade waste ($200k)

The effect

Pasta was overcharged by $290k; frozen meals looked more profitable than they were, and their manager had no reason to save energy

Bluegum Kitchens is an imagined company; figures are illustrative.

- **Remedies:** separate cost categories for clear environmental activities; label less obvious environmental costs; use activity-based costing to check allocation bases.
- **Limits:** records rarely hold future environmental costs or intangible costs, such as sales lost to environmentally aware customers.

Circular economy and reporting practice

MODULE 5 | PART E.3 | CONCEPTS

Circular economy

Instead of take, make and throw away, a circular economy keeps materials and products in use for as long as possible. The original three Rs, **reduce, reuse and recycle**, have widened to include **redesign, repair, renew and recover**. Countries such as the Netherlands, China and Japan encourage circular thinking through policy, and accounting systems that track materials through repeated cycles are still developing.

What surveys and awards tell us

Surveys show sustainability reporting is standard practice among large companies worldwide. But most of it is voluntary, so organisations can select what they include, and they tend to select favourable information. Reporting awards try to raise the bar: judges often praise reports that admit disappointing results and explain how they will be fixed. Financial reporting, by contrast, is tightly regulated and leaves little room to experiment.

Practice questions

MODULE 5 | PART E.3 | TRY THESE BEFORE THE WORKED ANSWERS

Question 1 - Bluegum Kitchens, next year

Bluegum Kitchens currently shares these environmental costs **equally** between its two product lines. Work out (a) the current allocation, (b) the allocation traced to real drivers, and (c) which line is overcosted and why that matters.

Cost	Annual amount	Frozen meals' share	Dry pasta's share
Refrigeration energy	$640,000	85%	15%
Trade waste charges	$240,000	70%	30%
Packaging waste disposal	$120,000	40%	60%

	Frozen meals	Dry pasta
(a) Shared equally		
(b) Traced to drivers		

(c) Which line is overcosted, and why does it matter?

Bluegum Kitchens and all costs in these questions are imagined teaching examples.

Question 2 - Which cost category?

Cost	Category
(a) Training staff to handle chemicals safely	
(b) An annual independent audit of waste licence compliance	
(c) Cleaning up an oil leak in the factory yard before it reaches the drains	
(d) Compensating a farmer whose creek was polluted by the factory's runoff	
(e) Installing bunded storage to contain any spills	
(f) Laboratory testing of stormwater samples	

Worked answers

MODULE 5 | PART E.3 | WORKED ANSWERS - ATTEMPT THE QUESTIONS FIRST

Question 1 - Bluegum Kitchens, next year

Cost	Frozen meals	Dry pasta
Refrigeration energy ($640,000)	85% = $544,000	15% = $96,000
Trade waste ($240,000)	70% = $168,000	30% = $72,000
Packaging waste ($120,000)	40% = $48,000	60% = $72,000
(b) Traced to drivers	$760,000	$240,000
(a) Shared equally	$500,000	$500,000

(c) Dry pasta is overcosted by $260,000 under equal sharing, and frozen meals are undercosted by the same amount. Prices and profitability judgements are distorted, and the frozen meals manager has little reason to cut refrigeration energy or trade waste. Note that packaging waste is driven mainly by pasta, so driver-based costing also shows the pasta team where to act.

Question 2 - Which cost category?

Cost	Category	Why
(a)	Prevention	Stops harm before it happens
(b)	Appraisal	Checks compliance
(c)	Internal failure	Eliminates harm caused, before it leaves the site
(d)	External failure	Damage caused outside the organisation
(e)	Prevention	Stops spills from causing harm
(f)	Appraisal	Testing against standards