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The Rationale for the Social Contract Accounting Framework

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Social Contract Accounting Framework

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The Social Contract Accounting Framework is an accounting framework that empowers organisations to account for the social impact of their activities. It sets out the principles and guidance for organisations to report on their alignment with the social and environmental objectives of society, in a consistent and meaningful way.

The framework proposes that amongst society's objectives is the provision of sustainable, inclusive prosperity for its members.

Basis of Sustainability Accounting

Huge advances have been made in understanding the context of sustainable use of resources by humans. Scientists have made a compelling case of immediate actions that need to be taken. Politicians have taken a far less compelling response. Individuals and individual organisations have also responded to scientific recommendations but in an uncoordinated way. Social Contract Accounting is a response to the challenges faced by organisations.

For the last 20 years or so, corporate accounting for sustainability has been channelled through initiatives such as the Tripple Bottom Line and Reporting 3.0. The tripple bottom line proposes that organisations should report in three parts: social, environmental and financial. Reporting 3.0 has been pushing to expand the scope of corporate reporting into further areas.

There appears to be growing scepticism about the initiatives. Sustainability has been the dominating partner. It is a colossally complicated and imprecise topic. Accounting principles require consistency and certainty of measurement and reporting. Simple measurement and reporting tools that permit organisations to convey their impact on the environment seem perhaps as elusive now as they ever have. It seems we do not yet have the scientific knowledge and understanding that enables full accounting for sustainability that meets these most basic principles.

Social Contract Accounting proposes an alternative approach. It is predicated on the limited ability of organisations to quantify their environmental impact. It tilts the balance of the tripple bottom line towards accounting for social impact, as the basis on which to provide more measures that are likely to have a deeper influence in corporate behaviour relating to sustainability. It recognises that the current environmental abuse is caused by humans. This provides two routes to motivate a change in behaviour that mitigate the abuse. It can come from external regulation/pressures, and from within. The way it achieves this is explained in the next section.

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Basis of Social Accounting

Two primary methods are currently being applied in accounting for social impact. By and large, all approaches advance the interests of people in an organisation's activities well beyond the current focus on profitable customers, shareholders and management. Social accounting requires organisations to account for their impact on a wider range of stakeholders, including all employees, customers, suppliers, local communities and the wider community, without regard to the monetary flows associated with the activities.

- The **direct method** seeks to measure an organisation's social impact. Generally, an organisation picks the stakeholders it chooses to focus on, and a restricted number of social issues it impacts. Almost all include employees in their focus, some with a greater focus than others. Most include environmental impact, again on a self-selected basis. External advisors usually support a client organisation to widen its focus on stakeholders and on the impacts on which it chooses to focus.

  The direct method of accounting for social impact suffers from similar limitations to environmental accounting. Social impact refers to the impact an organisation's activities has the personal wellbeing of multiple individuals. The impact can be direct, such as selling a service, or indirect, such as stressing an employee. The challenge with quantifying impact on wellbeing is that wellbeing is a composite of many influences. An individual organisation's influence on an individual combines with a huge range of other influences. In the same way that it is not currently possible to quantify environmental impact of an individual entity that accords with minimum accounting principles, it is also not possible to quantify the social impact.

- The **indirect method** has its own limitations. But compliance with minimum accounting principles is not one of them.

  The indirect method measures how closely an organisation's culture aligns with society's social and environmental objectives. This involves assessing the congruence between the organisation's cultural objectives with society's and how closely the organisation's practice aligns with its objectives. The indirect method does not seek to measure an organisation's direct social and environmental impact, concentrating instead on its contribution to society's culture of social and environmental wellbeing. It raises managerial consciousness of the organisation's social and environmental responsibility and practices in connection with assessing its strategy and outcomes.

  Its major limitation is its failure to recognise specific actions that have a significant social or environmental impact which conflict with its culture.

  The indirect method provides a measurable, independently verifiable assessment of an organisation's intent with respect to its social and environmental responsibilities, and the alignment of its actions with its intent. The measure provides investors with insight into the prospects of an organisation's long-term profitability, which is expected to be reflected in its share price. In this way, the indirect method provides financial incentives to organisations to improve the alignment of their activities with the social and environmental objectives of society.

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The Social Contract Accounting Proposal

Social Contract Accounting will provide practical guidance on practice and reporting of the impact of an organisation's activities on social and environmental outcomes within society.

Its recommends use of the indirect method of social accounting, as outlined above.

It proposes to supplement the reported measure of contribution with reporting of social and environmental activities, both in numbers and narrative, sufficient for readers of the accounts to judge factors that are not necessarily reflected in reported social contribution. Some approaches make an adjustment to the measured social and environmental contribution of an organisation to reflect specific activities during the year that have had a perceptible direct impact.

The standards around supplemental reporting will change over time to reflect advances in social and environmental accounting techniques.

A process is underway to bring together propositions from organisations working in this field. The propositions will be circulated for comment by interested parties, and refined as appropriate. The objective is to develop a standardised method of accounting for social and environmental contribution in line with methods for the development of existing accounting standards.