VALUING RESPECT

BY Shift

ACCOUNTING FOR COMPANIES' HUMAN RIGHTS PERFORMANCE

What can we learn from current practices and innovations?

A DISCUSSION PAPER

About Valuing Respect

Valuing Respect is a global collaborative platform, led by Shift, to research and co-create better ways of evaluating business respect for human rights. Our aim is to develop tools and insights that can help both companies and their stakeholders focus their resources on actions that effectively improve outcomes for people.

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About Shift

Shift is the leading center of expertise on the UN Guiding Principles on Business and Human Rights. Shift's global team facilitates dialogue, builds capacity and develops new approaches with companies, government, civil society organizations and international institutions to bring about a world in which business gets done with respect for people's fundamental welfare and dignity. Shift is a non-profit, mission-driven organization.

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Introduction

The Valuing Respect project starts from the premise that companies have a responsibility to respect human rights, as set out in the UN Guiding Principles on Business and Human Rights (UNGPs)[1]. This responsibility is reflected in a growing array of other international standards, national legislation, industry standards, and investor and civil society expectations. It is concerned with ensuring, to the greatest extent possible, that companies are not involved, through either their operations or value chains, with negative impacts on people's basic human dignity and equality: that is, their human rights[2].

The Valuing Respect project is focused on how to develop better ways to evaluate business respect for people's human rights in practice. The project will produce a range of outputs aimed at helping people inside and outside companies assess what is working, and what is not, in this critical aspect of companies' performance.

This discussion paper makes the proposition that a fundamental paradigm shift is needed in the field of accounting in order to incorporate the societal need for, and value from, business conduct that respects human rights. While there have been a growing number of initiatives in recent years to evaluate companies' environmental and social performance, they have dealt at best tangentially with the ways in which business responses to human rights risks can destroy, protect or create value for both business and society. Yet no aspect of business practice is more relevant for evaluating companies' so-called 'social performance', since negative human rights impacts are by definition the most serious impacts a company can have on people. This paper therefore aims to promote deeper discussion of what this reality could and should mean for the field of accounting.

The paper is divided into two parts. Part A sets the context for the discussion. It looks briefly at today's dominant and emerging paradigms for corporate governance and accounting and the extent to which they accommodate the value of business respect for human rights. In Part B, the paper explores the ways in which accounting models could evolve to better reflect and incentivize business respect for human rights. It considers two main questions:

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1 Office of the UN High Commissioner for Human Rights "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework" (United Nations, 2011); available at: https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf

2 The corporate responsibility to respect human rights extends to all internationally-recognized human rights. Such human rights range from labor rights including freedom of association and collective bargaining, just and favourable conditions at work and fair wages, to freedom from forced labor and child labor, to non-discrimination, the rights to privacy and freedom of expression, the right to clean water and sanitation, adequate housing and the highest attainable standard of health. For more, see: https://ohchr.org/EN/Issues/Pages/WhatareHumanRights.aspx

1. Can (and should) business respect for human rights be better reflected in current financial accounting methods?

The paper highlights two key constraints:

- Measurable costs to business of harm to human rights are frequently missed or misunderstood;
- Benefits to business from respecting human rights are often intangibles that cannot be readily measured.

2. To what extent do (or could) new innovations in accounting accommodate respect for human rights?

The paper looks at the new paradigm offered by integrated thinking and reporting through the <IR> Framework, and reviews the extent to which the following innovations can enable integrated approaches to accounting that adequately reflect respect for human rights:

- Total Impact Measurement and Management
- Sustainability Accounting Standards Board (SASB) standards
- The Embankment Project
- The Social and Human Capital Protocol

PART A: How far do today's paradigms for corporate governance and accounting accommodate the value?

We have been locked for fifty years into a dominant theory of the firm that has driven assumptions about the purpose of companies, governance and accounting…

Our current accounting model is based on a specific "theory of the firm" that the only purpose of the corporation is to maximize shareholder value. At the core of this theory is the idea that a firm's management (the agent) needs to be induced to operate – regardless of any other judgements or desires – in the interests of the shareholder (the principal). This "principal-agent" model is the driving logic of modern accounting.

The "principal-agent" theory of the firm is rationalized by two assertions. The first is that while actors other than shareholders may experience adverse impacts due to business activities, the interests of these other parties are upheld via legally enforceable contracts and by the State. By contrast, no one protects shareholders, who are taking the biggest financial risk as they can only reclaim their capital after others (banks, suppliers, employees etc) have claimed theirs. Second, even in the confines of the shareholder-manager relationship, the theory maintains that managers will naturally have incentives to make decisions that serve themselves and not shareholders (for example, by inflating their own salaries or through so-called 'empire building' that serves their ego). In short, owners of capital are left to defend their own interests – society does not protect them and managers cannot be trusted to do so.

In such a vision of the world, the only social responsibility of business becomes to serve and protect the interests of shareholders, and the only function of corporate governance must be to induce management to do so. Achieving this end entails costs: costs inherent in the risks that shareholders run, and the costs of the measures taken to reduce them, such as the conduct of audits and assurance, or the provision of stock options to incentivize executives. These 'agency costs' in turn influence the price at which shareholders are willing to provide their capital – that is, the 'cost of capital'. The higher the agency costs, the higher the costs of capital.

The purpose of accounting, then, must be to support the functioning of this corporate governance model that serves the principal-agent relationship, the goal of maximizing shareholder value and the management of associated agency costs. Accordingly, the role of financial accounting has been exclusively to furnish investors with what they need to know to make decisions about where to put their money: the so-called 'decision-usefulness' model.

Realities and expectations are now changing with regard to companies' role in society…

Over the past two decades – accelerated by the financial crisis of 2008-9 – we have seen an increasing challenge to this widely accepted theory of the firm, its appropriate governance, and associated accounting methods. This results from:

a. The inescapable fact that capital markets failed to recognize the consequences of treating business impacts on the environment as an external, unaccounted cost. This is a now well-recognized 'tragedy of the commons' where companies' individual and cumulative 'draw-down' on the shared resource system of our environment has led to a systemic threat to the planet – a 'commons' on which we all depend – in the form of climate change.
b. An analogous, and less recognized, tragedy of the commons that results from treating negative business impacts on people as external and unaccounted costs. Business practices that draw down on the 'shared resource system' of human dignity and welfare (for example searching out ever lower wages, benefits and protections for workers; or pursuing land ownership and use that dispossesses poor communities) has led to a systemic threat to social cohesion and stability – a 'commons' on which we all depend – in the form of gross human inequalities.

Faced with these realities, it has become increasingly apparent that financial transactions are a fundamentally inadequate means of capturing the value that is created, sustained or destroyed by an organization and the capital markets, and that the short-termism of today's capital markets is at odds with ideas of long-term value. Moreover, on-going demographic shifts among the owners of capital towards millennials and women have accelerated attention to concepts of value – including environmental and social value – that go beyond current market valuations.

As a result of these changes, views on the purpose of the corporation, governance and accounting are also changing…

These dynamics have led to a resurgence of interest in alternative theories of the firm and their appropriate governance, also with significant implications for accounting methodologies. There has been renewed attention to the idea – one with long historical roots – that the corporation necessarily has a public purpose. In this view, a company's relevant stakeholders extend wider than shareholders alone; the interests of all stakeholders – not just shareholders – should therefore influence a company's understanding of how it creates and accounts for value.

This return to a broader 'stakeholder theory' of the firm has been further supported by analyses of the legal structure of the firm.[3] These argue that shareholders do not, in fact or law, own corporations; they own shares issued by the corporation. They are protected with limited liability, such that their resources and wealth are partitioned from that of the company and vice-versa. Owning shares brings specific rights – such as appointing the board of directors or selling shares – but the corporation owns its assets and liabilities, and so has the sole right to direct those resources toward the objectives of the business. Directors and management are therefore agents of the corporation not of the shareholders. Their fiduciary duty encompasses the valid interests of shareholders in a healthy return on investment, but extends also to other stakeholders and other measures of success.

This vision has direct implications for how we think about corporate governance. It implies the need for a long-term horizon to company decision-making and allows for the legitimacy – even necessity – of certain decisions that do not provide shareholders with maximum returns in any given moment. This approach has long been reflected in the governance requirements for listed companies in South Africa, based on the premise put forward by the King Committee that "good corporate governance requires an acknowledgement that an organisation doesn't operate in a vacuum, but is an integral part of society and therefore has accountability towards current and future stakeholders." The UK's most recent Corporate Governance Code moves in a similar direction with the observation that "[t]o succeed in the long-term, directors and the companies they lead need to build and maintain

3 See, for example, Jean-Philippe Robé, "The Legal Structure of the Firm" Accounting, Economics, and Law Vol. 1 Iss. 1 (2011); available at: http://works.bepress.com/jean-philippe_robe/1/; and Lynn A Stout, "The Shareholder Value Myth" Cornell Law Faculty Publications Paper 771 (2013); available at http://scholarship.law.cornell.edu/facpub/771

successful relationships with a wide range of stakeholders. These relationships will be successful and enduring if they are based on respect, trust and mutual benefit”.[4]

These developments have in turn fueled renewed interest in a ‘stewardship model’ of accounting, which pre-existed the ‘decision-usefulness’ model that focuses exclusively on financial returns to shareholders. Stewardship looks at the wider role of management in monitoring and accounting for the company’s transactions, events and behavior. It offers much greater latitude to accommodate the information needs of stakeholders beyond shareholders, and therefore lends itself more readily to incorporating the information needs of stakeholders concerned with the environmental and social impacts of a business. The current UK draft Stewardship Code would align the role of institutional investors with this same vision, stating it to be: “The responsible allocation and management of capital across the institutional investment community, to create sustainable value *for beneficiaries, the economy and society*" [emphasis added].[5]

Notwithstanding these changes, current thinking and alternative models still fail to adequately reflect the value associated with business respect for human rights.

As we have seen, a growing proportion of those who lead, invest in and regulate business are expressing deep dissatisfaction with the view that a company is owned by its shareholders and has the sole responsibility of maximizing the returns they receive. The renewed debate on the purpose of the corporation has resonated across elite discussion venues from Aspen to Davos to the UN. The trend has arguably been spurred on by the internationally agreed Sustainable Development Goals (SDGs), the broad acceptance by multinational business of the private sector’s critical role in achieving these goals, and the hook the goals provide for advancing a different vision of the role of business in society.

That said, the barriers to real change remain daunting. Many of the most progressive voices in the business and investment fields have struggled to internalize the *structural* changes needed to drive responsible business conduct, finding the narrative of ‘new business opportunities’ and profits en route to the SDGs inherently more appealing. Some have argued that this reflects an excessive focus in the current discourse on ‘win-win’ scenarios, ‘shared value’ propositions, and ideas that investing for social impact can be done with no measurable compromise on financial returns.[6] Conversely, there has been insufficient attention to the many situations where change means the internalization of costs by business with no near-term or tangible off-set through increased revenues

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[4] Financial Reporting Council, “The UK Corporate Governance Code” (July 2018); available at: https://www.frc.org.uk/getattachment/88bd8c45-50ea-4841-95b0-d2f4f48069a2/2018-UK-Corporate-Governance-Code-FINAL.PDF

[5] Financial Reporting Council, “Proposed Revision to the UK Stewardship Code: Annex A Revised UK Stewardship Code” (January 2019); available at https://www.frc.org.uk/getattachment/bf27581f-c443-4365-ae0a-1487f1388a1b/Annex-A-Stewardship-Code-Jan-2019.pdf

[6] Anand Giridharadas, “Winners Take All: The Elite Charade of Changing the World”, (Alfred A. Knopf 2019)

or other benefits, and where real social impact from investments may come at the expense of optimal financial returns.

This suggests that an incrementalist approach to change in how corporate governance and accounting are treated may well be insufficient to meet the modern-day imperatives to measure corporate success in ways that are fully attuned to the needs and sustainability of our planet and of social cohesion and stability. It raises the prospect that we need a more substantial and structural change in how governance and accounting are practised and regulated.

PART B

How might accounting METHODS better accommodate the value of respect for human rights?

So how might accounting approaches more adequately reflect the effects of business conduct on people's human rights? Can they incorporate the idea of value creation from rights-respecting business conduct, and value erosion from rights-abusing or rights-neglecting business conduct? How far can such value be captured for the company itself in terms of resulting profit or loss? How far can it be reflected in terms of the value creation or erosion experienced outside the company – by the people directly impacted by business, and by society at large?

The rest of this paper begins to explore these questions. It looks first at the scope for current accounting models to reflect profit and loss for the company from its human rights-related conduct. Even if incremental changes are inadequate to the task, are there useful and even substantial changes that could yet be achieved through the use of familiar concepts? The paper then turns to some recent innovations in accounting that consider financial value to stakeholders beyond shareholders, as well as other forms of value – to business and society – that reflect companies' broader environmental and social performance. These innovations vary in their application from the cross-industry to industry-specific to company-specific levels; and in the measures they use, from financial outcomes to proxies for financial outcomes to measures that aim beyond financial outcomes. The paper asks what these innovations might offer with regard to the incorporation into accounting of business respect for human rights.

1. Can (and should) rights-respecting business practices be better reflected in standard financial accounting?

A first question arises as to whether, and to what extent, the erosion (or creation) of financial value for the *business* that results from its adverse impacts on human rights (or their effective reduction) could usefully be reflected through existing accounting categories and labels. Notwithstanding that the UN Guiding Principles on Business and Human Rights demand a different focus – centered on the company's impacts on people – it is worth asking whether just accounting for financial benefits/losses to the business itself could bring insights that would incentivize greater prevention of human rights harms.

There appear to be two main reasons why existing financial costs and benefits to business associated with their human rights performance are frequently poorly tracked and/or poorly understood:

a. Measurable costs are missed or misunderstood;
b. The costs associated with intangibles cannot be readily measured.

a. Measurable costs to the business of harm to human rights are often missed or misunderstood.

Existing research has demonstrated a frequent under-recognition of costs to business of involvement with human rights risks and negative impacts. The costs can include reduced access to capital, increased staff turnover, disruption to operations or the supply of goods, and lost business opportunities. There is also growing anecdotal evidence of the converse: that there can be clear financial benefits from operating with respect for human rights. The table at Annex A sets out a number of illustrative examples.

In practice, the tangible costs and benefits related to respect for human rights are often spread across a business at an operational level. They are often not understood as connected to a single root cause of good or bad corporate human rights performance. They are therefore rarely if ever aggregated or viewed holistically. This was well-evidenced in research into the costs to extractive companies of conflicts with communities over environmental and human rights impacts. One company in that research took the unusual step of aggregating the most evident costs to the company from community conflict, and estimated a value erosion of more than $6 billion over two years, representing a double-digit percentage of its annual profits.

Looking at the apparel sector, some ongoing research and pilot work with companies suggests that supply factories that treat workers well can realize benefits in the form of improved worker retention, improved productivity and even improvements in product quality – with measurable financial results that can more than off-set the costs of the original improvements in worker treatment. While the financial amounts concerned are not large, in a thin-margin industry small amounts can be the difference between success or failure for a supply factory. Meanwhile, the retailers and buyers that source from these factories may find measurable improvements in the reliability of their supply, as suggested by the conversely significant disruptions that companies sourcing heavily from Cambodia encountered during the strikes of 2013 over living wages.

Furthermore, the introduction of legislation requiring companies to conduct human rights due diligence on their supply chains may generate other tangible costs where suppliers fail to meet the grade. For example, in the US, Customs and Border Protection officers have begun withholding imports that are alleged to be produced with forced labor, and destroying those where the company cannot evidence adequate due diligence to ensure forced labor is not present. In France, under a new 'Duty of Vigilance' law, companies that fail to develop an adequate human rights due diligence plan can be sued by individuals who suffer harm as a result of this failure. Numerous other human rights due diligence laws are under consideration in Europe.

Notwithstanding these examples, pressing for human rights to be better reflected in traditional financial accounting methods can bring risks. It is easier to identify costs of negative human rights impacts than financial benefits from rights-respecting practices (designed to ensure that negative impacts do not occur). This might skew the accounting picture and make the costs of improving practices seem disproportionate to the (unaccounted) benefits. Equally, while some negative impacts on human rights bring clear costs to the company, some may bring financial benefit. To give the extreme example, there is a financial business case for slave labor. A more mundane example is that poverty wages at supplier factories can help keep costs of inputs down.

Finally, an excessive focus on financial outcomes might encourage the monetization of a company's impacts on people – placing a dollar value on people's lives, dignity and freedoms. While the valuation of human lives is already a part of the actuarial and insurance professions, it raises problems as a proposition in the wider context of business decision-making. These include the question of what kind of cost-benefit analyses it may encourage, as witnessed in the infamous 'Ford Pinto' case, where management judged that it would be cheaper for the company to deal with lawsuits and settlements over customer deaths than to resolve problems with the car's design that resulted in its gas tank exploding in rear-end collisions.

b. The financial costs/gains associated with intangibles cannot be readily measured.

Notwithstanding the evidence of some tangible costs for companies of negative impacts on people's human rights, these impacts – or the avoidance of impacts – more typically lead to intangible costs or gains. These range from long-recognized factors such as effects on the company's reputation, to more recently appreciated forms of value such as trust – whether between managers and workers within the company or between the company and affected communities and groups.

Under current financial accounting methods, intangible assets only show up on the balance sheet when an acquisition occurs that places a value on them. A patent that results from R&D by a company is unaccounted for in terms of financial value while it remains within that company; if it is sold to another company, it appears on the second company's balance sheet in light of that transaction. The concept of 'goodwill' in turn evolved to account for any positive difference, on the acquisition of an entire company, between the purchase price and the fair market value of its tangible assets, recognized intangible assets and liabilities. Yet this aggregates, and creates a 'black box' of, numerous and somewhat unknowable intangibles. It sheds limited light on how specific intangibles might or should be valued.

This has been widely recognized as a significant problem in an era when a listed company's book value is often less than 30% of its market value. There has been considerable creativity in efforts to recognize intangibles in the context of management accounting. Innovations in the form of value-added approaches, human resource accounting, and others, have sought to help managers put a value on different types of intangible. Typically, these have been grouped together under the concept of 'intellectual capital', but often broken down in sub-categories of human capital, structural (or organizational capital) and relational capital. Yet the various models and methods explored hit the challenge that intangibles in these areas carry different value for different companies. This makes it hard to devise a system that combines specificity with breadth of application and therefore comparability across companies.

Efforts to reflect the many intangibles that flow from rights-respecting/neglecting business practices will inevitably hit these same limitations in the context of financial accounting. Many such intangibles can be captured through the lens of the so-called 'social license to operate', which is increasingly understood as foundational to a company's long-term success. Anecdote suggests that the financial implications can become clear in specific instances: for instance, the mine site that it was only possible to sell given the successful transformation of (formerly conflictual) relationships with local communities; or the one factory whose workers showed up to protect it against violent action from workers striking across the region, due to the trusting dialogue management had built with its own workforce. Yet 'social license' and its loss is frequently more amorphous and harder to monetize. Financial accounting methods would seem to offer little by way of methods for systematically assessing its value to a business.

DISCUSSION QUESTIONS

1. To what extent is it risky or counterproductive to attempt to insert human rights measurement into existing accounting models and categories?
   - Does it unhelpfully imply that respect for human rights should be contingent on a business case?
   - Do such efforts distract from the opportunity to find more innovative and impactful forms of measurement capable of capturing the wider value of business respect for human rights?
   - Alternatively, are existing accounting methods a necessary starting point from which new approaches can best evolve and take hold?

2. Could current accounting methods and labels capture tangible financial costs and value erosion for a company from business practices that harm human rights?
   - For example, might we consider land rights claims as contingent liabilities; a facility that is shut down for years due to company/community conflict as a stranded asset; production disruption due to labor unrest as a cost of sales?
   - Could value created from rights-respecting business practices be accounted for similarly through existing accounting methods and labels?

3. Do any of the efforts to reflect intangibles in financial accounting lend themselves to capturing intangibles flowing from rights-respecting (or rights-abusing) business practices?

   - In particular, could they incorporate the intangible value of good (or bad) relationships with stakeholders whose human rights are subject to negative impacts – a category of stakeholder largely or entirely ignored in current methodologies?

   - Does the increasingly acknowledged idea of a 'social license to operate' lend itself as a concept for bundling the intangibles we would associate with respect (or lack of respect) for human rights?

2. To what extent do (or could) new innovations in accounting incorporate respect for human rights?

One way to enable both business leaders and the market to better integrate their social and environmental performance into core decision-making is to move beyond the narrow remit of financial accounting. The various drivers for a different vision of the purpose of the corporation have spurred innovations in accounting and reporting frameworks that can better reflect the environmental and social 'externalities' of business activities and provide a more holistic picture of companies' impact on, and contribution to, society. Understanding these may be instructive for considering how corporate human rights performance might be better captured through new accounting practices and thereby better integrated into business decision-making.

Triple Bottom Line Accounting

Triple Bottom Line (TBL) accounting – developed in the 1990s by John Elkington – laid the foundations for more recent innovations. It built on the methodology of 'full cost accounting: "an accounting method used to determine the complete end-to-end cost of producing products or services…[whereby] all direct costs, fixed, and variable overhead costs are assigned to the end product." TBL accounting seeks to measure the direct and indirect social and environmental, as well as economic, costs of a business activity or project.
However, in a recent Harvard Business Review article, Jon Elkington announced that TBL accounting is due for a strategic "product recall". Elkington argued that:

"Fundamentally, we have a hard-wired cultural problem in business, finance and markets. Whereas CEOs, CFOs, and other corporate leaders move heaven and earth to ensure that they hit their profit targets, the same is very rarely true of their people and planet targets. Clearly, the Triple Bottom Line has failed to bury the single bottom line paradigm. Critically, too, TBL's stated goal from the outset was system change — pushing toward the transformation of capitalism. It was never supposed to be just an accounting system."[7]

This raises the bar for innovation in frameworks for accounting. They must do more than sit alongside traditional accounts based on the shareholder primacy paradigm. They must fundamentally challenge that paradigm and offer a genuinely transformative view of the role of business in our economies and societies.

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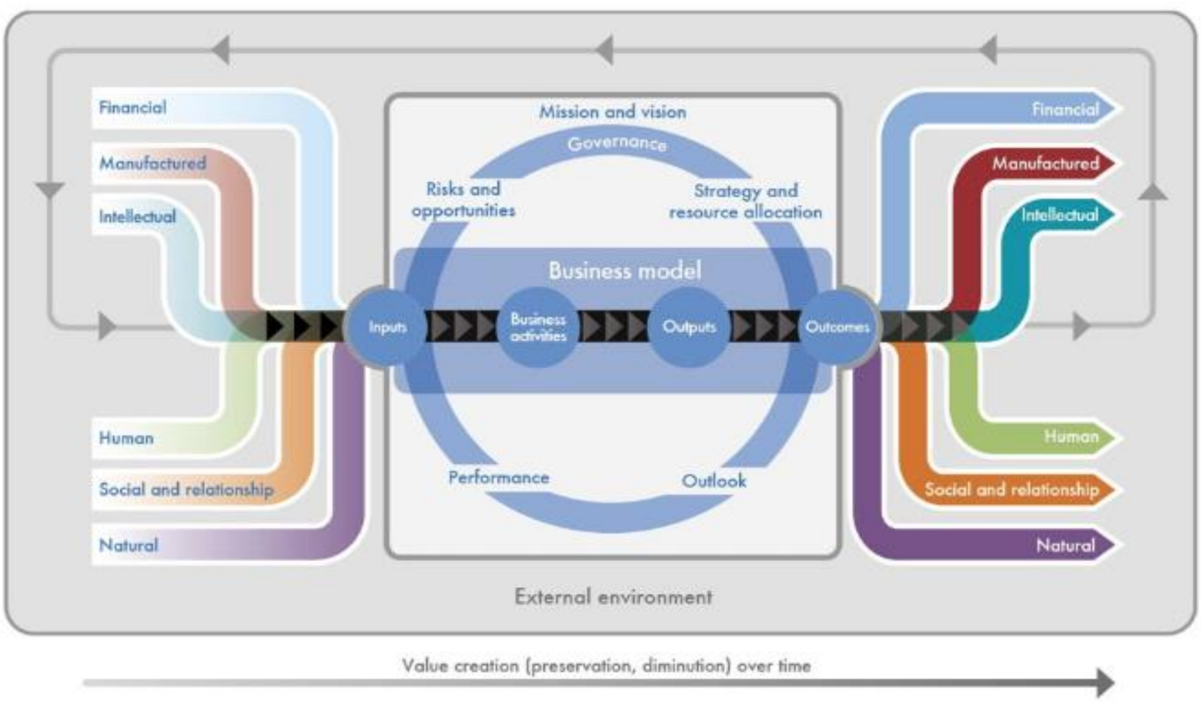
[7] John Elkington "25 Years Ago I Coined The Term 'Triple Bottom Line.' Here's Why It's Time To Rethink It", Harvard Business Review (June 25 2018)

Integrated thinking and reporting

The International Integrated Reporting Council's Integrated Reporting Framework ("<IR> Framework") marked a substantial step forward in this ambition of accounting holistically for a company's impact on and contribution to society. The <IR> Framework aims to create a more cohesive and efficient approach to both corporate reporting and decision-making that reflects the full range of factors that materially affect an organization's ability to create value over time. Alongside traditional financial capital, it recognizes five other capitals that constitute "stocks of value that are increased, decreased or transformed through the activities and outputs of the organization".[8] These are manufactured, intellectual, human, social and relationship, and natural capitals.

The focus of the <IR> Framework as a reporting framework remains on investors – improving "the quality of information available to providers of financial capital to enable a more efficient and productive allocation of capital." Yet it also recognizes that value has two interrelated aspects – value created for the organization itself and value created for others, including stakeholders and



society at large. Further, it defines the concept of value creation to include not only the positive creation of value but also situations where value is preserved or diminished. It recognizes that over

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[8] International Integrated Reporting Council "The International <IR> Framework" (2013)

time it is unlikely that value will be created through maximizing one capital while disregarding others. In other words, they should not be viewed separately and in parallel, but through the relationships between them. The flows and inter-relationships of capitals are captured through the IIRC's well-known 'octopus' diagram:

Image from the International Integrated Reporting Council: *http://integratedreporting.org/what-the-tool-for-better-reporting/get-to-grips-with-the-six-capitals/*

The four innovations explored below seek, in one way or another, to breathe life into this model of integrated thinking and reporting. They range across different levels of application – from the cross-industry to the industry-specific to the company-specific. In each case the applicability, strengths and weaknesses of the model for including the value of rights-respecting/rights-neglecting business practices is considered, as a basis for discussion.

PWC's Total Impact Measurement and Management Framework

The Total Impact Measurement and Management (TIMM) Framework aims to support the measurement, monetization and management of societal impact within four categories: Environmental, Economic, Tax and Social. This last category is of most direct relevance to respect for human rights, and "focuses on measuring the consequences of business activities on key stakeholder groups such as employees, customers and communities"[9] with reference to five areas - health, education, standard of living, empowerment and community cohesion.

The name of the Framework reflects its intent of providing:

- **Total**: a holistic view of social, environmental, fiscal and economic dimensions – that is, the big picture
- **Impact**: a look beyond inputs and outputs to outcomes and impacts and understand the company's footprint
- **Measurement**: a move to quantify and monetize the impacts, thereby putting value into a language that business understands
- **Management**: the evaluation of options and the optimization of trade-offs in order to make better decisions.[10]

[9] PWC "Measuring and Managing Total Impact: A new language for business decisions" (2013); available at: https://www.pwc.com/gx/en/sustainability/publications/total-impact-measurement-management/assets/pwc-timm-report.pdf
[10] Ibid.

The TIMM Framework does not propose standardized metrics for application across companies. Instead, it applies welfare economics to quantify and monetize the positive and negative impacts on society. It uses:

"non-market valuation techniques (e.g. willingness to pay or well-being valuation) to put a monetary value on these impacts. In some cases, these values can be derived from existing literature…national well-being surveys and various forms of primary research. Where no credible and/or relevant literature exists on the social impact, we use secondary and primary data gathering from beneficiary groups (and comparative non-beneficiaries). New emerging approaches also allow us to estimate the social value associated to a business's activities using national life satisfaction data across a significant number of countries."[11]

The framework offers some examples of the types of social impact that could be material to a business, but is flexible and can be tailored to the relevant circumstances of the business in question. Given that it advocates the monetization of impacts, it is geared towards the types of data that are available and lend themselves to monetization. In the context of 'social' issues, this would appear to skew notably towards positive social impacts, albeit the model in no way excludes the costs of negative impacts or financial benefits of their effective management. Furthermore, the five 'social' sub-categories identified could potentially be leveraged to capture a broad range of business impacts on human rights and corresponding risk mitigation measures.

However, the model does not provide for a distinction to be drawn between general social impacts, which might be weighed against other outcomes, and those that rise to the level of harming human rights, where such cost-benefit analyses raise fundamental moral issues. Moreover, the TIMM methodology focuses necessarily at the company level and therefore does not support the standardization of metrics. As such it may enable better management accounting for certain social impacts within a business but does not facilitate comparisons across businesses.

The Sustainability Accounting Standards Board (SASB)

SASB has been a prominent initiative in the United States to identify the environmental and social performance information that should form part of companies' reporting, based on an integrated reporting approach. Their focus remains firmly within a shareholder-centric model that looks for decision-useful information – that is, information about the company's positive and negative impacts on the various capitals that are judged financially material for the company and its shareholders. In short, they look at proxies – or indicators – of types of financial outcome for the business that can be demonstrated from past cases.

[11] Ibid.

SASB's definitions of social and human capitals encompass a range of human rights issues and their standards for different industries include human rights-related topics that are considered likely to have material impacts on companies in the industry concerned.

In some cases, the SASB standards include metrics that could add valuable insights on the likely presence and extent of human rights risk. For instance, the standard for extractive industries asks for disclosure of the percentage of proved and probable reserves in or near indigenous land. But when it comes to the management of such risks, the standards typically fall back on the same weak data points that are prevalent under the 'S' of ESG indices and rankings. For example, the standard for apparel and footwear companies asks for the number of supplier audits conducted, non-conformances found and corrective actions implemented, although research has long since shown these bear little relation to sustained improvements in workers' human rights. In other areas, the standards call for descriptions of a company's human rights due diligence efforts, such as with regard to the human rights of communities in conflict areas where extractive companies operate. Yet they do so at such a level of generality that any real insight into the effectiveness of those systems, the company's progress over time or comparability with other companies will remain elusive.

SASB standards also exclude impacts that may be grave in their consequences for people but unlikely to harm a company's reputation or bottom line based on past evidence. This focus on issues that can be shown to have brought financial consequences to companies in the past secures an empirical basis for the standards. Yet it arguably reinforces blind spots of risk – including future financial risk to companies – since it ignores impacts that could be expected to harm company reputations if brought to public attention, but which have simply escaped such scrutiny to date. Building safety in Bangladesh would not have counted under normal health and safety considerations before the collapse of Rana Plaza. Customer data usage by retail firms has not brought the same scrutiny to date as that of internet service providers such as Facebook, even if it may reasonably be expected to do so in the future. Disclosures about how sexual harassment is prevented and tackled in the workplace have not been a common feature of diversity and inclusion disclosures, albeit the events of recent years have shown that these 'hidden' abuses of women's rights can quickly pose significant risk to a business once uncovered.

The Embankment Project FOR INCLUSIVE CAPITALISM (EPIC)

Another avenue for innovation is to identify new units of measurement that do not involve monetizing impact (as with TIMM), and are not limited to activities or outcomes that necessarily imply a financial cost to the company (as with SASB). The Embankment Project for Inclusive Capitalism (EPIC) looks beyond the boundaries of information that indicates something is financially material and takes a broader view of materiality that extends to the concept of trust. It highlights that 'when businesses can make a stronger case that they are creating long-term value for stakeholders across society, we can begin to restore much-needed trust between them. That's why we need to find a way to measure that value.'[12]

EPIC focuses on measuring three types of value beyond financial value: consumer value, human value and societal value. Human value is defined as 'The value a company creates through the employment and development of people, in terms of its culture, engagement, leadership, know-how and skills'. Consumer value is defined as, 'The functional or emotional value a company creates through goods and services to meet customer needs, including innovation (e.g. product quality and brand).' Societal value is defined as, 'The value created through the relationships between a company and all other external stakeholders, including its environmental, social and economic impacts across the full value chain (e.g. resource efficiency, health and wellbeing, and job creation).'

The companies, asset owners and asset managers involved in EPIC identified four key value drivers in the form of talent, innovation, society and environment, and governance, against which they then sought to agree key metrics. The sub-group focused on talent advanced furthest, honing in on metrics across the five dimensions of workforce costs; the attraction, recruitment and turnover of staff; workforce composition and diversity; training, learning and development; and staff engagement and wellbeing.

While some of the talent metrics around diversity, salaries and benefits touch on human rights issues, by and large respect for human rights appears to have struggled to find a home in the work of the EPIC teams. A subsequent EPIC report acknowledged this openly, noting that: 'Participants…recognized that, increasingly, companies must earn their "license to operate" in society in order to be successful in the longer. But despite this growing consensus, the conversation around societal value has remained relatively abstract. Businesses still have difficulty quantifying the societal value they create.'[13]

The EPIC sub-group working on metrics for the value driver of 'society and the environment' adopted an approach base on the SDGs. Although tackling negative impacts on human rights is central to any company's contribution to the SDGs (no different to tackling their environmental footprint), the metrics identified for the three industries concerned skew heavily towards positive social impacts from job creation and social products and investment. Even SDG 8 on decent work and economic growth, which includes explicit SDG targets on forced labor and child labor, is taken as the basis for measuring only the company's contribution to economic growth by estimating its 'gross added value'.

[12] Coalition for Inclusive Capitalism "Embankment Project for Inclusive Capitalism" (2018); available at https://www.epic-value.com/static/epic-report-web-df894ad112b70406d9896c39f853deec.pdf
[13] Coalition for Inclusive Capitalism "EPIC: An Overview of the Embankment Project for Inclusive Capitalism" (2019)

The Social and Human Capital Protocol

The Social and Human Capital Protocol builds on the model of the Natural Capital Protocol that preceded it, to provide a methodology for companies to identify ways to 'measure and value the social and human capital impacts and dependencies of your whole business or an individual project, product or operation'.[14] Importantly, its focus is within a business – helping decision-makers identify the information they need to 'strengthen their company's social and human capital for the benefit of society and business' – and not on external users of information, although it may also support public reporting. The Protocol defines social capital as 'networks together with shared norms, values and understandings that facilitate co-operation within and among groups' and human capital as 'the knowledge, skills, competencies and attributes embodied in individuals that facilitate the creation of personal, social and economic well-being'. Taken together, the two capitals are characterized as 'resources [that] need to be maintained and enhanced to make society more cohesive and resilient, and to make business more successful'.

The Social and Human Capital Protocol, like the Natural Capital Protocol, looks at the reciprocal nature of both company impacts *and dependencies* on forms of social and human capital. The concept of dependencies facilitates a broader understanding of 'materiality'. If companies depend upon resources and relationships external to the company for their own success, then the interest of management and shareholders in preserving and building those resources and relationships is clear, without need either to express these in terms of financial outcomes, or to appeal to a higher normative expectation of responsible business. At the same time, the Protocol makes clear that, 'understanding impacts and dependencies on social and human capital can highlight potential internalization risks and opportunities for your business.' These may include 'increasing regulatory or legal action; market forces and changing operating environments; new actions by, and relationships with, external stakeholders; and an increasing drive for transparency or voluntary action by competitors who recognize the significance of transparency in future success'.

The goal of the Protocol is to 'help facilitate the mainstreaming of measurement and valuation of people and communities – shifting the improvement of social and human capital performance from an optional extra to a core part of business decision making'. That said, it remains at the level of a guidance framework, 'leaving open the choice of specific metrics and valuation and measurement approaches to users' and focusing rather on techniques for them to pursue this. It therefore does not provide a standardized model or enable comparability across companies, notwithstanding its

[14] Social and Human Capital Coalition "The 2019 Social and Human Capital Protocol" (February 2019); available at: https://www.wbcsd.org/Programs/Redefining-Value/Business-Decision-Making/Measurement-Valuation/Social-Human-Capital-Protocol/Resources/The-2019-Social-Human-Capital-Protocol

declared aim to lay the foundation for the kind of convergence that would make this possible in the future.

The Social and Human Capital Protocol takes important steps in recognizing the particular issues that arise when measuring value in relation to human rights. Its accompanying Social and Human Capital Charter highlights a range of considerations, including that ‘not all social and human impacts can and/or should be monetized’; and that ‘just because it is possible to value an impact does not, by itself, justify trading one impact off against another that may have been valued more highly.’ However, many companies remain relatively unaware of how human rights impacts arise in their operations and value chain, the ways they affect the company’s long-term success, and the costs they impose on society. Given that the Protocol offers only general techniques for companies to apply to social and human capital accounting, it remains likely that these companies will be slow to include human rights impacts when they apply it.

REPORTING 3.0 ACCOUNTING BLUEPRINT

Reporting 3.0 has set out to be a platform for convening experts inside and outside companies to develop and implement a new vision for corporate reporting and accountability. It has developed blueprints specifically aimed at redesigning practices in the fields of reporting, accounting, data and new business models. The Accounting Blueprint developed by its 3.0 Accounting Working Group argues for a ‘New Accounting’ that comprises financial accounting, management accounting and sustainability accounting, and ‘captures the creation of value in different forms, recognizing the use of different capitals’. This is seen to be aligned with notions of multicapital, intercapital or integrated accounting.[15]

The Blueprint proposes twelve ‘Recognized Comprehensive Accounting Principles’ that draw from the principles underpinning a range of current reporting frameworks, and it explores the merits and feasibility of bringing environmental, social and governance information into mainstream financial accounts, as well as the role of today’s management accounting not just in ‘collecting, transforming and reporting data, but more importantly [in] influencing behavior at all levels’ – a critical consideration when it comes to business impacts on human rights.

The Blueprint proposes that ‘New Accounting will prioritize the use of financial information as far as possible, without pushing monetization to unrealistic extremes’. It also highlights that using monetization to capture different non-financial capitals can lead to misleading conclusions, and may also lead to companies focusing on aspects of their performance where numbers can be readily found, at the expense of areas where they have the greatest influence or impact. The Blueprint also

[15] Reporting 3.0 “The Blueprint for New Accounting: Laying the foundations for Future-Ready Reporting” (June 2018); available at https://reporting3.org/accounting-blueprint/

argues for the value of narrative reporting to help ‘in making up for the shortcomings of conventional financial or sustainability statements and improving the understanding of various drivers behind value creation with a longer-term focus’. Ultimately, the Blueprint sees management accounting as playing a leading role within companies in integrating different accounts for different capitals, to build a more holistic view of a company’s performance.

The Blueprint suggests some interesting innovations in service to this strategic vision. Yet it remains a high-level vision that leaves the same questions open as to how and to what extent companies’ human rights impacts and management of those impacts could be effectively reflected in financial accounts, might be better incorporated in the metrics of management accounting, or may suffer risks from quantification of any type and demand a more rigorous narrative treatment. Those answers remain to be discovered.

DISCUSSION QUESTIONS

Should the focus of attention be on methods of internal accounting for human rights that can be tailored to company realities, or on public accounting through standardized measures that can apply across an industry or wider?

- Should both approaches be pursued in parallel, but through different means and allowing for success in different degrees?
- Or should internal management methodologies be pursued first, to build more knowledge and convergence before attempting better external accounting?

How should human rights impacts and risks – and company efforts to reduce them – be understood in the context of the six capitals under the <IR> framework, and the human, social and relationship capitals in particular?

- Can the usual definitions of these capitals be adapted to better reflect the human rights dimension?
- Is it more promising to consider human rights through the lens of risks and value erosion/protection, than through value creation? What problems might it raise to do so?

How feasible (and desirable) is it to quantify the value to affected stakeholders and society of business respect (or disrespect) for human rights?

- Are there certain units of value beyond the monetary that could capture at least some key types of human rights risk?
    - For example, could a useful measure of land-related human rights risk be the acreage or percentage of land used or relied on by a company, where its ownership and usage is contested by poor and indigenous communities?
    - Could a useful measure of progress towards living wages for workers in a company's supply chain be the percentage of the workforce in farms or production facilities that is known to earn above (a) $1.90 per day (the extreme poverty line), (b) the legal minimum wage, and (c) a living wage (as determined by a recognized methodology)?

In any of these efforts, what safeguards may be needed to:

- avoid or substantially reduce the risk of 'off-setting' adverse human rights impacts with positive

Annex A

Costs to business of involvement in negative human rights impacts: some examples

Extractives	Research shows that in the mining and oil and gas sectors, the most frequent costs from conflict with communities arise from lost productivity due to temporary shutdowns or delay. For a world-class mining operation with capex of US$2-3 billion, this can mean a loss of $20 million per week of delay in Net Present Value (NPV) terms. The greatest costs are typically the opportunity costs in terms of the lost value linked to future projects, expansion plans, or sales that do not go ahead. The most often overlooked costs tend to be those resulting from staff time – particularly senior management time – that is diverted to managing conflict. (See Davis, Rachel and Daniel M. Franks. 2014. "Costs of Company-Community Conflict in the Extractive Sector." Corporate Social Responsibility Initiative Report No. 66. Cambridge, MA: Harvard Kennedy School, available at http://shiftproject.org/sites/default/files/Costs of Conflict_Davis & Franks.pdf)
	UK metals and mining company Vedanta Resources' plans to put a bauxite mine in place in India provoked international outrage when the company failed to take into consideration the holy sites and lands of an indigenous tribal group living on the site. Aviva found that a significant proportion of the company's 29% underperformance relative to its peers was due to its lack of focus on sustainability issues, including human rights. Resulting divestment by Aviva and other major institutional investors led to a reported drop in Vedantas' market price of up to a third of its value. Ultimately, the Indian government denied permission for the $1.7 billion project to proceed. (See Final Statement by the UK National Contact Point for the OECD Guidelines for Multinational Enterprises: Complaint from Survival International Against Vedanta Resources, plc, available at www.oecd.org/investment/mne/43884129.pdf ; see also, Bennet, Lessons from the Vedanta case—what next? (January 21, 2014), available at http://bit.ly/VuORZy)
Sectors and investments involving land acquisition	A 2012 study on land tenure disputes (ie, disputes involving local communities' legal or customary title to land) found that "unresolved conflicts over land tenure significantly augment the financial risks for companies in infrastructure, mining, agriculture and forestry." The modeling suggested that "the potential for bottom-line financial damage range[s] from massively increased operating costs – as much as 29 times over a normal baseline scenario… - to outright abandonment of an up-and-running operation" In a

	further 2013 study, analysis of geospatial data from land concessions in emerging market economies suggested "a three in ten chance that a given…concession incurs tenure risk", with the full dimensions of land tenure risk likely to be "appreciably larger" once datasets are improved. (See The Munden Project, "Global Capital, Local Concessions: A Data-Driven Examination of Land Tenure Risk and Industrial Concessions in Emerging Market Economies", September 2013, p 2 and 3.)
	Indian company Tata Motors constructed a car factory with the assistance of the state in acquiring the land. It was intended for building the world's cheapest car – the $2,000 Nano. Instead of rolling out the cars when planned, massive opposition from displaced farmers resulted in the company having to forfeit the $300 million factory, move to another region and delay the launch by at least a year.
	The Singaporean palm oil trading company Wilmar International Limited was the subject of a complaint to the International Finance Corporation (IFC), that an Indonesian subsidiary had paid the police to violently evict people from their lands and had bulldozed family dwellings to make way for a palm oil concession. Wilmar decided to divest from the subsidiary, which many attributed to the ongoing CAO complaint. The day the divestment was announced, Wilmar's shares dropped by 0.65%.
Apparel	The Rana Plaza tragedy of 2013 left over 1,100 workers dead after the building in which they were making garments for mostly western brands and retailers collapsed. This had major repercussions for the industry's reputation and practices. In addition, brand and retail companies that were sourcing from the facility have contributed millions of dollars to efforts to upgrade safety at garment factories in the country, alongside contributions to a compensation fund for victims. (See http://www.ranaplaza-arrangement.org/fund/donors)
	UK sporting goods company Sports Direct's shares dropped 11% and then another 3%, wiping over £400 million from the value of the company, when the company announced poor financial results amid intense scrutiny of its labor practices in the UK. This included findings that workers at its warehouse were being paid below the minimum wage, were subject to an intrusive regime of searches and surveillance and subject to harsh rules of conduct. According to a national newspaper, these revelations, coupled with a worse-than-expected sales performance over a number of months, prompted the worst day's trading for Sports Direct shares for nearly two years.

	(See https://www.theguardian.com/business/2016/aug/15/sports-direct-staff-to-receive-back-pay-unite-hmrc)

Valuing Respect is a global collaborative platform, led by Shift, to research and co-create better ways of evaluating business respect for human rights. Our aim is to develop tools and insights that can help both companies and their stakeholders focus their resources on actions that effectively improve outcomes for people.

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