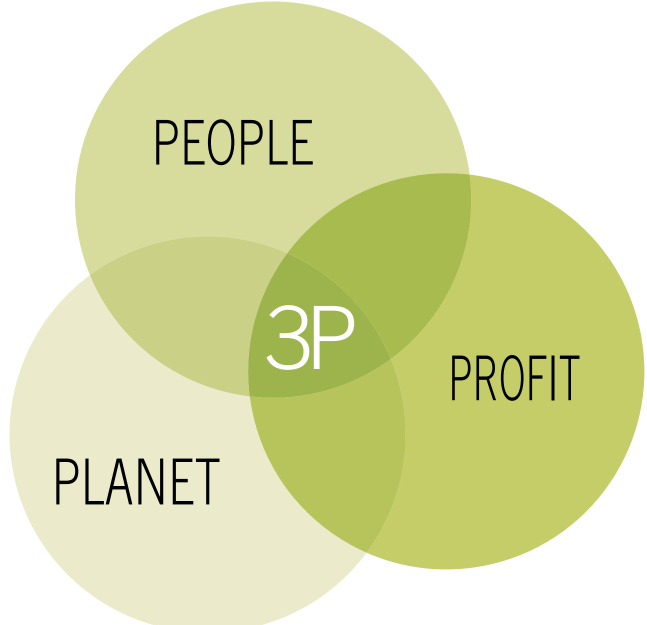
Triple bottom line



The impact on real estate development

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The year is 2020. It's tax time, and your accountant has a list of inquiries regarding your company's capital inflows and outflows to be reported to the IRS, state regulatory bodies, investors, board of directors and your lending institution.

Unlike past decades, when you would simply authorize your in-house accounting staff to release the firm's itemization of all expenses and banking statements, you are struggling with a new requirement: reporting your company's environmental costs in an effort to quantify the environmental impact of your business.

This quantitative analysis not only measures the performance of your company, but also the products it produces, assuming for this article, the entity is a for-profit, single or multifamily housing builder/developer. After including the sum of charitable donations made by your firm, your accountant presses you for your environmental statement. You remain unsure, trying to comprehend what information is required. Then, it hits you: The bottom line no longer can be calculated using simple arithmetic but has morphed into a complex string of formulas. Where do you begin?

The above scenario is a prediction of what is to come; in certain quarters it has already arrived. First coined by John Elkington in 1994, triple bottom line (TBL) dispenses with outdated accounting practices and replaces it with new data on the social, economic and environmental impacts. In the private sector, the term "3P," or "people, planet and profit," aptly describes TBL and its goal of sustainable accounting. As an indication of the concept's growing acceptability, the United Nations adopted a TBL standard in 2007 for urban and community development and has become the dominant approach to public-sector full cost accounting. Yet, quantifying TBL is problematic and often subjective. To help sort out the variables, a nonprofit entity called the Global Reporting Initiative (GRI) has developed guidelines to enable corporations and nongovernmental organizations alike to comparably report on the social impact of their business.

The concept has received growing attention, as evinced in articles published in the Wall Street Journal, The Economist, and the New York Times, to name a few. These publications featured TBL as a new management tool that measures an organization's performance in terms of the 3Ps. In researching for this article and contemplating my actions as a builder/developer, I wondered how TBL could be applied to my business practice. These questions immediately arose: Would builders be subject to the new accounting method of TBL? Are builders' core business operations and products measurable using TBL accounting? And finally, isn't TBL another way of quantifying sustainable development, and if so, where does the lending industry fit in all of this?

First, there is currently no requirement for TBL reporting in the United States for the private-sector construction and development industries. However, I believe builders will eventually be subjected to TBL requirements regardless of size, volume of construction, or profit/loss. I predict that before this decade is over, industries directly tied to impacting the environment will have to perform—and be accountable for—a new system of measuring their overall impact.

Second, as a builder/developer's core deliverables likely account for the majority of its overall impact on the environment (think number of Dumpsters needed to fill debris from the erection of one single-family dwelling), the application of TBL will not only be applied to the business side of operations, but also the impact their construction will have on the environment. The environmental and social aspects are neglected in the profitability equation because they are not required to be quantified, and converting sustainability data into the financials is not easy.

Whether or not the task is easy, it does preclude the importance of adopting performance standards themselves. Nearly half of the world's largest companies (those in the global Fortune 100 and the FTSE 100) now produce some type of social and environmental/sustainability reporting.

And the GRI's format is becoming the standard reporting process for ensuring transparency, completeness, reliability, accuracy, neutrality and comparability, relevance, and clarity. In the immediate past, it was the Wild West, with no standards, no norms, no protocols. As the GRI moves toward a higher level of general acceptance (such as GAAP for financial reporting), it will provide the basis for consistent assurance statements. In due time, this format will likely evolve to include a reciprocal interface with leading green platforms, such as the USGBC's LEED program. At the time of this writing, no such integration currently exists, but the conversion of this (sustainable) data observed in the preceding paragraph ostensibly removes the most challenging barrier to TBL reporting for builder/developers.

Lastly, TBL is another way to document sustainable development—to quantify the good results of a builder/developer's work. Since banks put up most of the capital for development, the lending industry would be the lead agent in demanding TBL from its client-borrowers. Yet, it is the banking sector that has responded far more slowly than other sectors to the new challenges of sustainability. Despite their slowness to adapt, society's drive for sustainable development is full of risks and opportunities for banks. Why banks have been slow to examine the environmental or social performance of their clients may be explained in privacy laws: Banks reason that such an examination would require interference with a client's activities. The role lenders would play in contributing toward sustainable development is considerable due to their intermediary role in the economy. Banks transform money in terms of duration, scale, spatial location and risk, and have an important impact on the economic development of micro and macro economies. This renders lending institutions an important, yet neglected, sector for integrating TBL reporting.

It has been said that the main difficulty in modeling the future is that it is involves uncertainty. What is certain is that our business practices and the (building) products we produce in the future will require a new matrix of accounting and accountability.

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