Foresight: The CPA Podcast

Season 3 Episode 4: Why CPAs are the best choice to produce sustainability reports

Neil Morrison: Welcome to Foresight: The CPA Podcast. I'm Neil Morrison.

The conversation around sustainability can quickly become political, even philosophical. We heard that in our conversation last episode with Guy Cormier. The CEO and president of Desjardins Group argued that it's time to give capitalism a do-over. More specifically, he argued that the financial system is shifting away from shareholder capitalism towards stakeholder capitalism, and he says, that's a good thing. You may think that's debatable, but is it a debate CPAs need to have?

According to Armand Capisciolto, the answer is no. Armand is the national accounting standards partner at BDO Canada and the interim chair of the Canadian Accounting Standards Board. I asked him for his reaction to Guy Cormier's argument about the rise of stakeholder capitalism.

Armand Capisciolto: It's an interesting one because I've heard people say that there's a disconnect between what shareholders want and what other stakeholders want. I'm not sure I agree there's a disconnect because those other stakeholders have an impact on the company. If you're not taking care of the planet or not thinking about doing things in an environmentally friendly way, consumers will take notice, and consumers will make different decisions, and those different decisions might be not buying your product. If they make a decision to not buy your product, well, I think that impacts the shareholders.

If we look at a drought, I think historically we've always thought about drought as being a food crisis, and they are. But a drought also has an impact on the production of hydroelectricity, which has an impact on what companies can do. If they don't have power, they can't produce things. So now suddenly, this climate issue, it now becomes a company performance issue. Because that company, if it can't produce product because it doesn't have enough power, they're not going to be profitable.

But it's broader than just that one company. We need all companies that rely on supply chains, and they rely on supply chains that are global, need to care about what's happening in the climate in all countries everywhere on the planet because that could have an impact on their supply chains. So, if we look at a drought in China that impacts manufacturing in China, well, that might be a key component part for a company. Now if that company doesn't have a key component part, it can't build inventory. If it can't build inventory, it can't generate revenue. I think if we start thinking about those things, well, again, caring about the planet, caring about climate change is caring about the company because we operate in a very integrated society. Nothing's in a vacuum, and therefore, we have to think about the impact that climate, social issues, whatever the issue is, although it might be indirect, it does impact almost every company.

Neil Morrison: If you were asked four years ago if you would be talking about sustainability and carbon footprints, what would you have said?

Armand Capisciolto: Probably not.

Neil Morrison: What were you working on five years ago?

Armand Capisciolto: Well, five years ago, I was doing the job I do now. I'm what I'll call a technical accountant. I deal with complex accounting issues and very much engaged in the day-to-day interpretation of accounting standards, interpretation of IFRS. So, I was doing my job, doing what I do, thinking about accounting, thinking about financial reporting. I wasn't oblivious to climate issues and social issues and everything that gets encompassed in this discussion about sustainability or ESG, obviously, but I wasn't putting two and two together that this impacts what I do on a daily basis in my work life.

How I started getting more involved in this, again, because my responsibilities at BDO relate to interpretation of IFRS, and because I was on the Accounting Standards Board and we deal with IFRS issues at the Canadian Accounting Standards Board, when the IFRS Foundation said, "Well, we're going to create standards that deal with sustainability and create a new board, the International Sustainability Standards Board," well, IFRS is involved so, "Well, Armand, that seems like something you should look at." I think at first, I was like, "Okay, how does this have to do with what I do on a day-to-day basis?" The more I got into it, the more I realized, "Wow, this has a significant impact on what I do on a day-to-day basis," in a couple of different ways.

The first way that I think how it impacts what I do on a day-to-day basis is, at the end of the day, why do we produce financial statements? You think, well, what's the purpose of financial statements? Well, it's to provide investors, providers of capital with information so they can make appropriate investment decisions. The more I got into sustainability, I started realizing, wow, investors are asking for this information about sustainability, information about climate risks, information about social risks. These are the same people that read the financial statements that I'm involved with either as an auditor or providing accounting advisory support or even as a standard setter.

When you start thinking about that, you start thinking, well, if an investor's relying on this information, the information, it needs to be providing a consistent narrative. What you're saying in the financial statements needs to be consistent with what you're saying in your sustainability report. If you're identifying a climate risk, you're saying, "Well, there's a risk here to the company." How does that not impact the financial statements? Because if there's a risk to the company, that could ultimately impact performance. So, I started seeing this connectivity between financial reporting or traditional financial reporting, financial statements, which is what I do, it's my job, it's what I'm passionate about, and the sustainability reporting.

I always like to use a simple example when I talk about the connectivity of financial statements, something really easy for people to understand property, plant, equipment. It's a very basic concept for people to think about. Well, if a company is making a statement about being net zero by 2040, so that's, what, 17 years away, and they have high carbon emitting assets on their books, and I look at the financial statements and they're amortizing those over 40 years and saying there's 40 years of life left, I start wondering, well, one of those two things can't be correct. They're either not going to be net zero by 2040, or those assets that they say have 40 years left only have 17 years left or less years left.

So when I think about an investor or a user of this information, if things aren't matching, if there's inconsistencies between those different documents, that's just a red flag for them. So now it starts impacting accounting estimates, impacting accounting interpretations, impacting journal entries. I think that's been my evolution and my journey related to this topic as a CPA, just someone doing his job, doing my day to day, and not thinking about it. But once I was exposed to the issues and to the relationship, it just became obvious to me that this is very much aligned with one of the core competencies of a CPA being financial reporting.

Neil Morrison: Are we at a stage where auditors are looking at those two things, let's say, look at financial statements and then also look at the sustainability report and really comparing it, looking at it side by side to see, are they saying the same thing in these two documents?

Armand Capisciolto: I think it's early days for auditors considering this because, first, a lot of companies are reporting voluntarily right now, or a number of companies are, but not every company is. So, companies haven't had to think about that yet, but they are. They will have to going forward. As I said, if a company is saying something on its website but that's inconsistent with what's in the financial statements, I would expect an auditor to note that there's some inconsistency and identify that.

When I look at what securities regulators are doing, I think it was in the US, the Securities and Exchange Commission published a sample letter that they were going to send to US filers that had a bunch of questions. The questions were all about climate risk and different things like that. But none of them were specifically about the financial statements. They were about, “Well, you’re saying this on your website, but we don’t see that in your regulatory filings. Or you’ve identified this risk. How does this impact the company?”

So I, as a skeptical auditor reading that sample letter, looks at it, well, they’re asking questions about the website. They’re asking questions about risks. They’re really asking questions about the financial statements and the consistency of those other documents, those other statements they’ve made with the financial statements. So, when I see something like that, I think companies and auditors need to start looking at these things side by side and saying, are they consistent? Where they’re not consistent, just like I said, that’s a red flag for an investor, that should be a red flag for a regulator, that should be a red flag for an auditor of something that maybe needs a little bit of a deeper look.

Neil Morrison: I’m wondering, if we’re going beyond financial statements, why are CPAs the right profession to do this? For example, why shouldn’t it be MBAs who generate this narrative?

Armand Capisciolto: It’s a great question, and I think one that I’ll start off with as a CPA, well, CPAs are great at everything, so why not? But now the serious answer. The serious answer, I think, and this is my perspective on this... Again, it comes from that financial reporting background, involvement in standard setting, and thinking about, well, why do we have standards? Why do we have financial statements? It’s generally to provide information for providers of capital to make investment decisions, whether they’re investing in a company, in the equity of a company, or lending to a company.

Because investors are now looking at information beyond the financial statements and specifically sustainability-type reports, I look at this information as not that different than the financial statements. What do we as CPAs add to financial statements? Well, we add credibility to the information that’s in the financial statements. Through the application of accounting standards in the financial statements, that makes the financial information more credible than through providing of assurance. As auditors, we provide an additional layer of credibility to that information.

So, when I think about that core competency of CPAs, of adding credibility to information and specifically information that is used by the providers of capital and knowing that the providers of capital are making investment decisions based on sustainability information now, or it’s one piece of the information that they’re using to make investment decisions, I believe is very much aligned with our core competencies as accountants. That there is information investors are relying on, accountants will add credibility to that information through the rigor of applying standards.

Standard setting is happening, and regulators are putting rules in place and eventually through the providing of assurance over that information.

Neil Morrison: That helps me to understand the advantage and the value that a CPA brings to it over something like an MBA, a non-professional degree. But if we're looking at sustainability standards in particular, I'm wondering, why is this something for CPAs to work through and not something that, let's say, environmental scientists are the ones setting the standards and checking to see if the standards are being met?

Armand Capisciolto: I think they are involved. Again, I'll make the analogy to preparing financial statements. When we prepare financial statements and audit financial statements, there are various things that we rely on other experts for. Companies have pension plans. We rely on actuaries to determine those amounts. There's fair value determinations that we rely on chartered business valuators for assistance with.

What I think CPAs do well is bring people together, bring people with different skill sets together, and we understand what the providers of capital want. Again, when I look at sustainability reporting, we bring that skill set of bringing people together and understanding what investors want. One of the key disclosures when we talk about sustainability reporting are GHG emissions. It's probably not an accountant doing those calculations. We're using people who have that expertise in auditing it. But then what we would bring to the table is, how does that tie in with all of the information needs and that consistent narrative of all of the reporting to investors that the company is doing?

Neil Morrison: The way you talk about it, I find it very interesting because it feels like essentially what you're arguing is this really isn't that much of a departure. It seems like something big has come, a big change has come to the profession, but you really make it seem like it it's not much of a departure. It's more similar to what they've always done than it is a shift.

Armand Capisciolto: Well, I think it's a big change, but I don't think it's a big departure.

Neil Morrison: Tease those two apart for me.

Armand Capisciolto: When I think about the change, why it's a change is with regulation, with standards is going to become mandatory reporting, consistent reporting. That means more companies are going to be reporting. So that's a significant change in that what we think about companies needing for providing information to various stakeholders. Again, I always focus on providers of capital because that's my background. So that's the change. The big change is the new information request, and that new information request is different than financial statements. So that's a change.

But what we do with that information, how we prepare that information, how we audit that information, yes, we will need some different skill sets or apply different skill sets and bring different experts into the mix. But it's not that different than preparing financial statements and auditing financial statements. I know some people are going to listen to this and say, "Wow, he's really understating it." It's not that different from a core competency standpoint. Yes, it is very different from a detailed level of knowledge, but from a core competency standpoint, to me, this is very much aligned with what we do as CPAs.

Neil Morrison: You often speak about this at various forums. You've done it for CPA Canada. What sort of response do you get?

Armand Capisciolto: I think there's a mixed response, to be honest. I think when we talk about sustainability and specifically some of the climate issues and some of the social issues related to it, I think it's unfortunate that politics sometimes comes into play. So, you get some negative pushback because of that. To be honest, that-

Neil Morrison: What do you mean by politics gets into it? What do you mean by that?

Armand Capisciolto: Well, I think at the end of the day, people have different views, and I think political views have influenced people's thoughts on things like climate change regardless of what scientists say. That's one of the reasons that I talk about it the way I talk about it, about the dollars and cents of it. Because when I'm talking to accountants about, well, we're just doing what we do, adding credibility to information, we're doing what we do, providing assurance over information that investors, by the way, want. If the investors don't get this, regardless of what your views on the issues are, that company or your company may not be able to raise the money it wants to raise or do business with the companies it wants to do business with.

So take your political views out of it, take all of that away, and let's just focus on the economics of it. Investors are asking for this, and therefore, as accountants, it's something we just have to acknowledge. Investors want this. Therefore, it's not a choice to deal with this or not deal with this. It's not a choice for many reasons, in my opinion. But when I think about it from a pure accounting kind of financial reporting standpoint, if investors are asking for it, companies have to provide the information. As CPAs, we're in the information business, and therefore, we should be part of this. That's how I try to deal with it, when I get pushback, is really focusing on the economics, investors want it, it has an impact on a company's performance if they do or don't respond to these risks that they're facing.

Neil Morrison: It sounds convincing to me. Personally, I find it very interesting the way you are able to just remove it from the higher-level discussions, like the one we had in our last episode with Guy Cormier and bring it down to just the core of what a CPA does. It sounds convincing to me. Do you find people… does it relax their shoulders? Do they manage to get out of whatever level of opposition they might have, whether it's coming from a political sense or even if it's just coming from a sense of being overwhelmed by this big change that's coming?

Armand Capisciolto: I think it does. I think the other thing beyond the kind of different views on it that also gets pushed back on it is the cost. Well, this is going to cost a lot to do this. How do we deal with that aspect of it? I think the other thing that I would say that comes up in the discussions that I find positive is, it's not a cost. It's an investment. If you don't do this, and I think your last conversation with Desjardins Group, so financial institutions, if they believe this is a critical aspect of doing business going forward, well, if I'm trying to raise money from them, I'd better be doing this. If I can't raise that money, what does that mean to the business? Or if I want to sell my product to customers but they don't want to buy from me because I'm not doing what they believe to be the right thing to do, I'm not going to have revenue and my business isn't going to last.

I think one of the things, when we talk about sustainability, a lot of people focus on the sustainability of the planet, the sustainability of society, and 100% that is, in my opinion, the most important aspect of it. But when I'm talking to people about the accounting matters, the audit matters, I'm probably emphasizing it's also about the sustainability of the business, it's sustainability of the company. I think, again, if we focus sustainability on the company and realize that, for a company to be sustainable, we have to do things that are sustainable for the planet as well, to me, it just becomes a no-brainer once you put those two things together.

Neil Morrison: Armand, I really enjoyed this conversation. Thank you so much.

Armand Capisciolto: Oh, it's been fun.

Neil Morrison: Armand Capisciolto is the national accounting standards partner at BDO Canada and the interim chair of the Canadian Accounting Standards Board. Now, where Armand encourages CPAs to see sustainability as just part of the nuts and bolts of the accounting profession, on our next episode, we're going to be speaking with an unapologetic champion for CPAs embracing sustainability in their practice. Roopa Davé is a partner in KPMG's Sustainability Services Practice.

Roopa Davé: I think the thing that is very exciting for me is the potential for CPAs to impact topics like climate change that are big and global and have major impacts on society, so really that ability to add purpose to our day-to-day work.

Neil Morrison: That is Roopa Davé, a partner in KPMG's Sustainability Services Practice, speaking on the next episode of Foresight: The CPA Podcast. If you like this podcast, please give it five stars in your podcast app. Review it, subscribe, or follow it, and please share it. All this really helps others to discover us.

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