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Measuring impact to make a difference

Singapore Management University

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Impact-Weighted Accounts (IWAs) quantify impact and aims to help managers make better decisions

From now until 9 September 2022, the Impact Economy Foundation (IEF) will be holding a public consultation ahead of it writing the first draft of the Impact-Weighted Accounts Framework (IWAF). The goal of the IWAF is to guide organisations to create their own Impact-Weighted Accounts (IWAs) to quantify and measure how their activities “affect societal welfare and the natural environment”.

“IWAs are a way to measure the impact a firm’s operations have on their stakeholders,” explains Ethan Rouen, Faculty Co-Chair of the Impact-Weighted Accounts Project at Harvard Business School. “We think of these stakeholders as, for example, the environment, employees, and customers. You can think of impact-weighted accounting as an earnings report for these groups, not dissimilar from what you would give to shareholders in terms of the content you want to convey.

“To make it comparable, we use academic research to convert the impact into dollar values. This allows comparability across different topics, which improves managerial decision making. It’s hard to think about the tradeoffs of a project that mitigates carbon emission from one that would improve the lives of employees, but when we attach dollar values to it, it starts to make it clearer the best strategy we can use.”

WHY IWAS?

In an IEF webinar earlier this month that launched the beginning of the public consultation, IWAs were articulated as being a tool to 1. Identify; 2. Measure; 3. Attribute; and 4. Aggregate impact information.

Adrian de Groot Ruiz, Executive Director of the Impact Institute and a Board Member of the IEF, illustrates with an example of methane emissions:

> *“A ton of methane has approximately the same global warming potential as 21 tons of carbon. If you reduce methane emissions by 10 tons a year, that’s equivalent to 210 tons of CO2. The social cost of a ton of carbon is around 150 dollars [so] 210 tons of CO2 is equivalent to 31500 dollars of global warming savings.*
>
> *“If you install [equipment that reduces this much methane emission], your clients and suppliers should share some of the credit for your products. You can attribute to yourself maybe 50 percent, so you have $15750 of benefits in carbon. And if you do that for the various impacts, then you can have a complete picture in which you can also compare two different projects or investments.”*

Through rigorous academic research, impact can be quantified for societal welfare and different types of value (financial, intellectual, human etc.) and the effects on different stakeholders.

For senior management, understanding IWAs can be a way to do a better job.

“If you're a CEO or a board member, it can feel very uncomfortable when your stakeholders ask about climate change, biodiversity, labour rights, equality, about gender etc. This provides you a way to become more in control and make decisions in a good and informed manner,” notes de Groot Ruiz.

IT’S NOT AS EASY AS (SCOPE) 1-2-3

Quantifying an organisation’s impact into a dollar value is difficult given the wide range of issues and the lack of a widely accepted methodology. Even within the relatively focused issue of greenhouse emissions, Scope 3 emissions are sometimes a bone of contention.

Whereas Scope 1 covers direct emissions from resources owned by an organisation, and Scope 2 accounts for indirect emissions such as purchased electricity, Scope 3 includes things such as business travel, waste disposal, and transportation both upstream and downstream of a company’s value chain.

While including an organisation’s Scope 3 emissions into its IWAs would be good sustainability practice, company executives are wary of the negative impression projected by an enlarged carbon footprint.

“From our conversations with some organisations, they keep on saying, ‘If you require us to report our Scope 3 emissions but our competitors are not reporting that, it only makes us look bad because our emission amounts will be much larger,’” says Hao Liang, Associate Professor of Finance at the SMU Lee Kong Chian School of Business. “However, if all companies report Scope 3 emissions, they could help each other better understand the whole ecosystem. This will better incentivise companies to join this more standardised way of reporting and act more sustainably.”

Rouen observes that much of ESG is currently about risk mitigation, which he points out as insufficient. He asserts that IWAs provides the tools to “not just ask whether we're limiting our risk, but also to understand how business can start having a lasting, meaningful, and positive influence on those societies that give them their license to operate”.

“The question should never be, ‘Is this method perfect?’ It should be, ‘Is it good enough to achieve our goals?’ And while the methodology will continue to evolve, as we get more buy-in and feedback and data, I'm confident that the answer to this question is ‘Yes’.

“IWAs can achieve the goal of understanding a firm's impact on stakeholders in a way that reshapes the conversation.”

Ethan Rouen, Adrian de Groot Ruiz, and Hao Liang were speakers at the webinar "Launch of public consultation – Impact-Weighted Accounts Framework (IWAF): Paving the way to long-term value creation for all" that was held on June 2, 2022.

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