

ESTABLISHING SUSTAINABILITY IN SMALL BUSINESS

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Small businesses that make early moves in sustainability have broad opportunity to be leading changemakers.

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Sustainability has been overlooked by many small companies in the interest of a focus on short-term survival. Although in the past some might have justified this by pointing to the limited resources with which small businesses operate, the development of a sustainability program is increasingly being recognized as a business essential, not a “nice to have.”

By implementing a sustainability program early, small businesses stand a greater chance at success, particularly in response to a crisis such as a pandemic or natural disaster. In adopting sustainability strategies, it's best to start with the fundamentals: Three key pillars of sustainability are society, the economy, and environment—or people, profit, and the planet.

People

The pandemic created a plethora of new challenges for small businesses struggling to survive, including supply chain disruptions, hyperinflation, and labor shortages. Savvy financial leaders with innovation process strategies in place were in a better position to survive the pandemic than those without an innovation process in place.

An important part of an innovation process is placing a strong focus on linkages and relationships. In addition to the resilience and ability to adapt to changing environments, this focus on relationships is key in any good sustainability plan. It presents an opportunity for small business owners to practice social responsibility and to simultaneously build better relationships to support the business.

Customer impacts. In addition to the long-term benefits of committing to sustainable practices, there are also potential short-term benefits that can be realized. Multinational companies have experienced pressure to adopt and comply with sustainable practices, but small companies have lagged in embracing sustainable practices. Yet according to *Forbes*, “77% of people want to learn how to live more sustainably” (bit.ly/3HS3GNr).

Small companies with a clear and focused sustainability compliance plan can establish a competitive advantage with this majority when vying for business within the supply chain of large companies. While some of the practices might involve factors associated with environmental issues that are of long-term concern to customers and employees and equate to greater profits, there's also the added benefit of positive public relations associated with being a responsible steward of the environment. Consumers are more likely to purchase products and services from companies who demonstrate social responsibility.

This commitment can be used to stand out and to instill customer loyalty that will continue during difficult times such as we have all experienced during the pandemic. As Alisha Lyndon, founder and CEO of the consultancy Momentum, wrote in a *Forbes* article, “In a world of digital selling, it is the personal relationships that will become a differentiator” (bit.ly/3pAsYsW).

Supplier impacts. Recent supply chain disruptions have demonstrated to small businesses that more emphasis needs to be placed on mitigating the potential for future disruptions, and sustainability practices are one way to do this. Sustainable sourcing considers the social, ethical, and environmental impact of a supplier in addition to the typical factors such as cost, lead times, and customer service record.

According to Prologis, a company that specializes in logistics solutions, “The importance of sustainability in a supply chain extends beyond going green. A supply chain built on a sustainable platform creates more partnership opportunities because environmental responsibility is a crucial focal point in today's industry. Practicing eco-awareness in every aspect of your business improves your reputation and further legitimizes your organization. A sustainable supply chain also helps improve productivity while saving money at the same time. By using sustainable techniques and resources, you increase the efficiency of buildings, vehicles and machinery at a significant cost savings” (bit.ly/3pztQxM).

Employee impacts. One cause that has been cited for the recent supply chain disruptions is the shortage of labor to produce and transport supplies. News outlets have shown pictures of ships docked and waiting to be unloaded for extended periods of time. There are multiple reasons why the labor shortage exists, but the primary lesson small businesses can learn from the current labor shortage is the need to place greater value on the human capital that's required for their business to operate. A program that emphasizes long-term sustainability over short-term profits will organically prioritize the value of employees.

Companies with a pattern of treating their employees well have retained employees at a higher rate than those who previously treated them as a disposable liability. Companies with a reputation for valuing employees are also in a better position to attract new employees in the highly competitive employee market that has emerged. Further, developing and implementing a sustainability program will also help employers differentiate themselves to employees who value socially responsible initiatives.

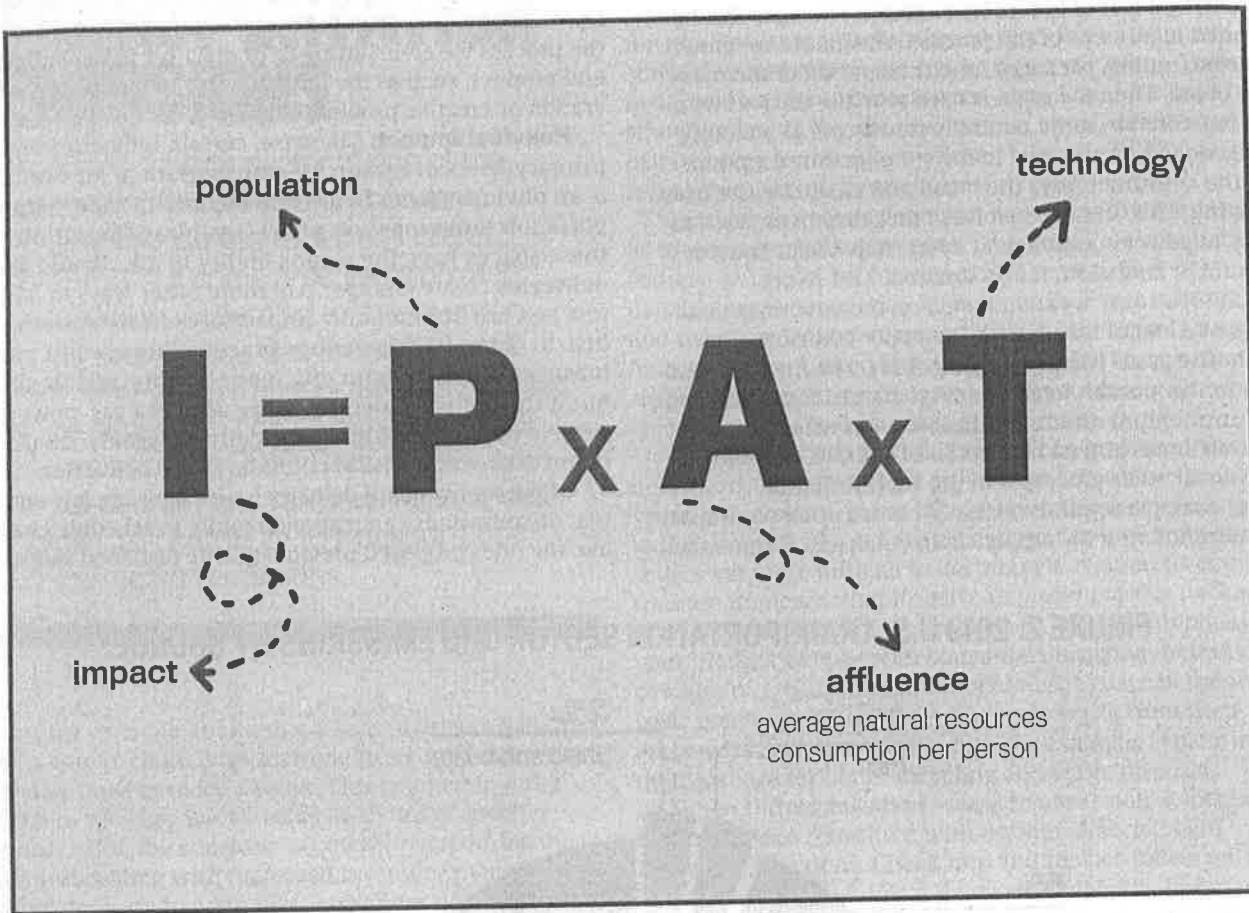
Profit

All management accountants have a common need: to look for and create value for the organization. This quality is what takes the function above and beyond bean counting to exploring how to better communicate the added value of sustainability and how its accurate and timely reporting plays a pivotal part in the financial reporting process.

One of the challenges in achieving profitability through sustainability is the ability to properly communicate what has been implemented and how it has impacted the bottom line. There's a need to clearly convey how the gained efficiencies associated with sustainable practices reduce costs and thereby increase profitability.

Beyond the bottom line. In an examination of this “profit” factor, we can't limit our review simply to the bottom line; we need to also look at the recent trends of

FIGURE 1: THE IPAT FORMULA



Source: Adapted from "Environmental Sustainability in Business: a Brief History," simonesmerilli.com.

adjusting financial objectives in order to achieve higher sustainability goals. The skill and knowledge required to clearly identify the impacts of sustainability on operations and, thus, on achieving profitability enable colleagues in other departments of the organization to communicate that goodwill value to the market.

Management accountants have the opportunity to educate organizational leaders on the ways sustainable strategy and practice lay a foundation for future success. Owners and investors are increasingly recognizing the significance of sustainability and embracing the capital market participants that show evidence that sustainability is one of their value pillars. It's important to target this specific group of thought leaders and to have them come on board and identify sustainability as one of their core targets.

The role of management accountants is to clearly convey information to the organization and its partners and clients so they can see how future earnings could be impacted by following a sustainable approach. There's a critical need for ownership and management to look beyond the bottom line and pursue a wider stakeholder approach, recognizing the benefits of operating an organization that takes environmental, social, and governance (ESG) goals into consideration.

Planet

The recognition of the planetary impact of human activities began with the IPAT formula in the 1970s (see Figure 1). The impact (I) of any group or nations on the environment is given by the interaction of its population size (P), per capita affluence (A, or average natural resources consumption per person), and technology involved in supporting each unit of consumption (T).

While this information helps formulate the human impact on the environment, it doesn't answer the question of how to improve that impact. There are no easy answers, yet all countries, businesses, and individuals need to consider changes they can make to provide sustainable use of shared resources at the global scale.

When we turn to the "planet" factor, we can begin with natural resources. Water, air, soil, and minerals come to mind. We want to be able to grow, harvest, and otherwise acquire resources needed for production yet keep the soil intact and not pollute the water or air. We need clean water in production and clean air to breathe. Because natural resources are utilized to supply useful items for consumers, it's reasonable to turn the lens on the areas of production, transportation, marketing, waste, scrap, and end-user consumption.

One loaf of bread. A common illustration to this end is following a commodity and its impact on the environment. Considering a loaf of bread, for example, it's clear that labor is implied in all steps of the process. The grains are grown, harvested, milled, packaged, and transported to the maker of the bread. Then the grain is used to make the loaf with other ingredients (some naturally resourced) at a facility, packaged, and transported to the store for consumption. Then the consumer buys the bread and creates waste from packaging. This, in turn, involves other resources, such as energy to power equipment at every step. Water is used, from rain or irrigation, for production. And so on.

In 2017, a study was conducted on the environmental impact of a loaf of bread, with the major contributor to greenhouse gases (GHG) being fertilizer. The findings, published in the journal *Nature Plants* (go.nature.com/3IZRQSQ), show ammonium nitrate fertilizer used in wheat cultivation contributes almost half (43%) of the GHG emissions, dwarfing all other processes in the supply chain.

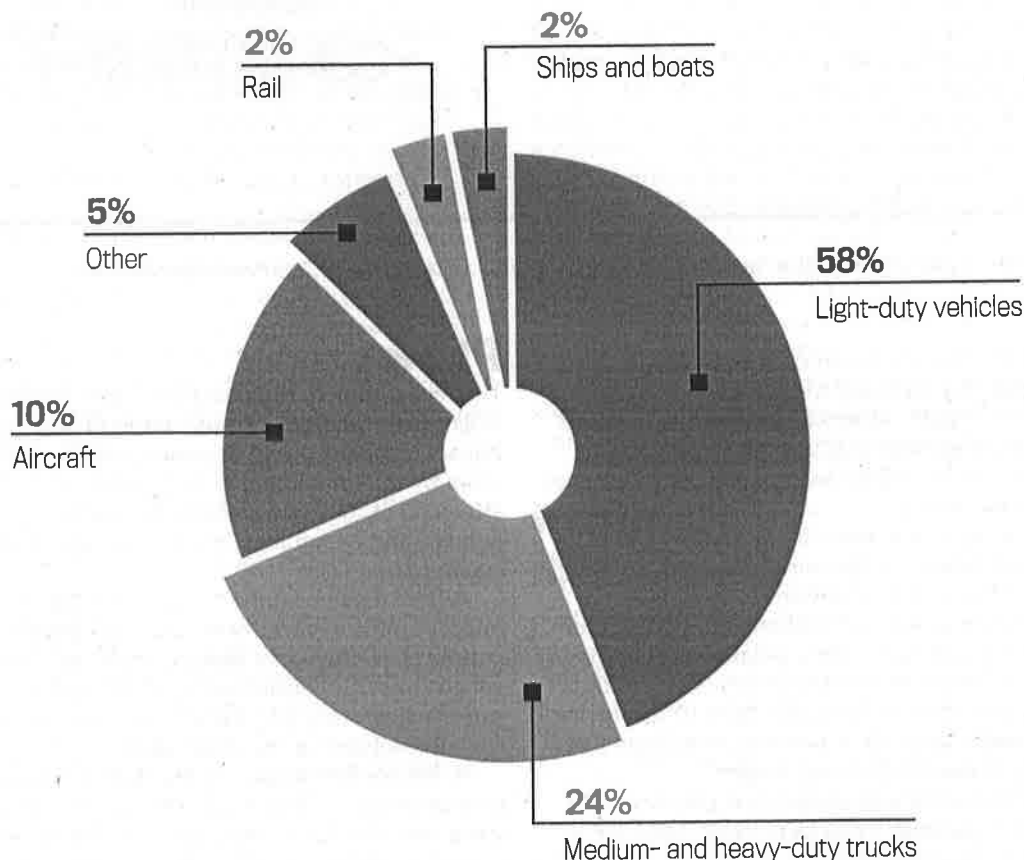
This example reminds us that what we don't see impacts our environment with supply chain concerns. When asked

about the impact of a loaf of bread, many of us would likely point to the packaging and transportation—those are more immediately evident to the customer. But often it's parts of the process we aren't aware of or don't see in the deliverable end product, such as the fertilizer, that demands reconsideration or creative problem solving.

Heaviest impact. Likewise, certain industries are primary users of resources—transportation, for example, is an obvious player in gas and electricity. (See “Transportation Emissions” on p. 55.) Organizations within these spaces have the responsibility to ask, Would fewer deliveries create change? Are there other ways to adjust to a less environmentally impactful delivery system? Just-in-Time (JIT) inventory practices are used in many businesses to help with efficiency, quality, and flexibility, but if the delivery method being used is a gas-powered vehicle making multiple trips daily or weekly, then a better business decision could be fewer deliveries.

Other supply chain delivery issues have already shown that organizations can respond rapidly to schedule changes like the ones proposed previously. One fast-food industry

FIGURE 2: 2019 U.S. TRANSPORTATION SECTOR GHG EMISSIONS BY SOURCE



Note: Totals may not add to 100% due to rounding. Transportation emissions don't include emissions from nontransportation mobile sources such as agriculture and construction equipment. "Other" sources include buses, motorcycles, pipelines, and lubricants. For more information on U.S. GHG emissions from transportation, see the EPA's *Fast Facts: U.S. Transportation Sector Greenhouse Gas Emissions*, bit.ly/3pA0U8Y.

TRANSPORTATION EMISSIONS

The transportation sector is one of the largest contributors to anthropogenic U.S. greenhouse gas (GHG) emissions, representing a prime area for improving sustainability. According to the *Inventory of U.S. Greenhouse Gas Emissions and Sinks 1990-2019*, transportation accounted for the largest portion (29%) of total U.S. GHG emissions in 2019. Cars, trucks, commercial aircraft, and railroads, among other sources, all contribute to transportation end-use sector emissions.

company, for example, found that a lack of drivers had disrupted its supply chain from multiple fresh-food deliveries to deliveries once or twice a week. This resulted in more waste due to spoilage. But by using analytics of specific operational sales, the company is quickly overcoming the spoilage and dealing with increased inventory management with more items on hand to meet consumer needs.

Shifting impacts. In the automotive industry, more vehicle manufacturers are moving toward electric vehicles (EVs) with reduced emissions. (See Figure 2 for 2019 emissions information from the U.S. Environmental Protection Agency (EPA).) Exhaust pipes are also being converted to meet EPA requirements. As businesses consider transportation methods, they can partner with or use vehicles that are making the change to EPA regulations for the threshold years being established. Using EVs could move a business back to JIT. Further, companies could consider stocking more inventory as a cost to avoid adding to environmental issues, or they could use other areas of transportation with a lesser impact on the environment.

Ships have typically been a cost-effective transport method. But delays due to COVID-19 have more than doubled those costs. Considering the damage done from their time spent idling in ports, ships now take a dramatically increased toll on the environment. As a result, shipping methods are now both more costly and deleterious. Organizations have a moment to reconsider whether imported raw materials sources and finished goods, while made at a lesser cost, even translate to a better bottom line anymore. In accounting, we know that dependence on one customer or vendor can impact the survival of a business; small businesses need to be able to pivot and source closer to their customers and factor in the many shifting variables of transportation.

Other options. There's a great deal of low-hanging fruit when it comes to greening a business. Contemporary business practices afford unprecedented flexibility for remote work and distributed workforce structures. Marketing and sales calls can be done via Zoom. Training, installation videos, conferences, and classes have all been shown to be highly effective online. Local area workers can be hired for on-site work in place of implementation teams from far-off headquarters.

Consider the packaging used. According to experts such as sourcegreenpackaging.com, paper can continually be sourced as forests are harvested and replenished, but plastic-coated paper ends up in landfills. Paper is heavier and therefore adds to transportation costs. Paper is a major industry in the United States, and manufacturers have started implementing costs and energy savings via renewable energy use and recycling their products.

On the other hand, while plastics can be reused, their heavy carbon footprint for production takes thousands of years to degrade, and use of nonrenewable fossil fuels adds to the concern. Plastics are cheaper to produce and easy to source yet more difficult to decompose. Numerous countries are implementing (or have in place) plastics packaging taxes that will affect a business cost. Consider supplying your product in bulk with consumers bringing their own containers. Organizations are behind the curve in the most basic green act: better ways to recycle waste from their employees and their community, for example, separating their garbage for better recycling and waste disposal.

When the organization's lease renews, look at locations that have been retrofitted with motion-detected light and water functions. Check into and replace toilets with low-flow capacity. Look at green sustainability-built facilities as your next leased space. Replace florescent lights with LED for energy conservation. These types of actions all help reduce maintenance costs, reduce energy consumption, and improve the health of employees.

While air and water are major concerns, usually government regulations cause a business to meet those regulations. As business managers, we need to exceed those requirements, or we will be continually in a cycle to upgrade our environmental requirements. There are as many ways for a business to exercise care and stewardship of the environment as there are organizations. **SF**

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