

NEW ACCOUNTING RULES COULD FORCE MORE ENVIRONMENTAL DISCLOSURE

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Sustainable investment groups are hailing a pending new requirement in the accounting industry that would force businesses to take more environmental liabilities into account in their financial statements. If finalized, the new mandate would be particularly relevant to companies that face Clean Air Act asbestos removal requirements, as well as those that could be liable under EPA's toxic cleanup rules.

Shareholder advocates argue the pending accounting rules point to a broader trend forcing companies to account for environmental requirements that pose financial risks. But industry groups are opposing the new requirement, arguing it would force companies to report hypothetical liabilities they do not currently face.

The Financial Accounting Standards Board (FASB) is expected to soon finalize a new interpretation of accounting rules with direct applications for a company's environmental mandates. The FASB is a professional organization that establishes industry standards known as generally accepted accounting principles (GAAP).

The new interpretation will apply to companies that face the potential for future environmental liabilities, but do not have any current legal obligations. Existing accounting standards do not require a company to disclose these future obligations in their financial statements sent to the Securities & Exchange Commission (SEC). However, the new approach would require disclosure if it is "reasonably" possible to estimate the future cost to the company, the draft interpretation says.

One source who is following the new accounting requirement calls it a "revolutionary new approach" to reporting a company's environmental remediation liabilities. "Historically, GAAP have not required disclosure of environmental

cleanup obligations for company-owned properties in the absence of pending or probable regulatory enforcement or litigation,” the source said in an interview conducted by e-mail.

In its proposed interpretation issued in June of last year, FASB cited as an example a company that acquires a factory that contains asbestos, which is subject to disposal regulations including those under EPA’s national emission standards for hazardous air pollutants.

“The entity has several options to retire that factory in the future, including demolishing, selling or abandoning it. The entity is able to estimate the initial fair value of the liability for the special handling of the asbestos using the present value embodied in the acquisition price,” the board notes in its *Proposed Interpretation of FASB Statement # 143, Accounting for Conditional Asset Retirement Obligations*.

Other liabilities might include a company’s future solid waste disposal requirements. For example, power plants might have to dispose of utility transformers that contain polychlorinated biphenyls.

But the proposal would not affect potential risks that cannot be assigned any dollar value. For example, companies would not have to report the possible costs of future climate change rules under the new interpretation.

Observers had expected the FASB to finalize the interpretation sometime last year, but the board has not done so and still has the option of withdrawing it. Officials with the FASB did not return calls for comment.

Some investor advocacy groups are hailing the proposed interpretation, which comes in the midst of their campaign for requiring more disclosure of environmental liabilities.

“It really seems to go in the right direction,” one sustainable investment source

says. For a company, “the idea is, we’re exploiting that asset, we’re retiring it, and sometime it’s going to cost some money.”

The new approach addresses concerns these groups have raised in the past about “mothballed” facilities that a company shuts down indefinitely without demolishing them, in order to avoid toxic cleanup requirements. Now, a company would have to disclose these liabilities at the outset, the source notes.

And the source adds the interpretation will have added weight because of the new scrutiny for corporations after the passage of the Sarbanes-Oxley Act, which Congress approved in 2002 following corporate accounting scandals at Enron and other companies. The law’s provision for CEOs to certify the accuracy of financial statements will help ensure that companies follow strict accounting procedures, including these new FASB requirements, the source says.

Yet numerous companies, including chemical plants and electric utilities, argue the FASB requirements would be inappropriate, since they are based on liabilities that may or may not appear in the future. For example, they argue a company could shut down a facility indefinitely without incurring any costs.

American Electric Power argued in public comments in July of last year that the FASB interpretation “provides examples that are contradictory and cannot be applied consistently. In addition, we believe the examples could lead an entity to record a liability when its legal counsel has determined it does not have a current legal obligation.” *Relevant documents are available on InsideEPA.com.*

Meanwhile, investors recently filed shareholder resolutions asking companies to improve their environmental reporting, specifically on the issue of climate change. The resolutions ask companies to disclose the impact of possible future greenhouse gas regulations on their financial bottom line. These resolutions will be addressed during spring shareholder meetings.

Until now, these shareholder groups have focused their climate change resolutions

campaign mainly on power companies and oil companies. They say they achieved a measure of success last year after the nation's four largest electric utilities agreed to submit reports detailing the impact of possible future climate change rules on their operations.

Now, shareholders are trying to broaden their campaign by targeting additional industry sectors they believe would be impacted by climate change mandates (*Clean Air Report*, Dec. 16, 2004, p12).

Some of the corporations where groups have filed shareholder resolutions include auto companies Ford Motor Company and General Motors Corp.; the banks Wachovia and Wells Fargo Bank N.A.; the manufacturing companies Corning Inc., Dow Chemical Company, Great Lakes Chemical Corp. and Nucor Corp.; and the utility First Energy. Shareholders are also filing resolutions with a long list of oil companies, with particular attention to Exxon Mobil Corp. Finally, they are filing several resolutions at real estate investment trusts and homebuilding companies. --
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