

Facilitating the Move toward Sustainability

An underlying theme of this report is that the environmental future of the planet largely hinges on what happens in Asia and the Pacific over the next 50 years or so. Also, a sustainable future requires conscious efforts on the part of government, the private sector, and citizens to depart from past patterns. So, what are the key choices and decisions that need to be taken to create an atmosphere of policies and behaviors supporting sustainability? There clearly are initiatives that corporations can take that are internal to their own operations and entirely within their control. Some of these will be encouraged by incentives offered by governments, though this will require both economic and environmental policy reform. There also will be tremendous investment demands generated by these changes, and innovations in financial instruments will be needed to pay for new environmental infrastructure and other costs.

The conclusion is that assuring environmental performance can no longer be thought of as purely the realm of the public sector. Businesses in Asia and the Pacific have a big role to play with responsibility for environmental outcomes shared between the public and private spheres.

The first step that many corporations in this region need to take is simply to meet existing standards. Pressures emanating from a wide range of international and national sources will make it progressively harder for businesses to avoid compliance with environmental laws and regulations. The penalties exacted by traditional regulators and by communities and individuals emboldened by new information tools will

make it increasingly difficult for environmental laggards to hide. Undoubtedly, the need for corporations to obtain a “social license” to operate will become ever more important.

Some of the needed changes will incur new costs for the private sector, but there also will be opportunities for savings from eco-efficiency gains as well as to enhance revenues through product differentiation. Some corporations from the region—mostly the larger ones—are already seeing the benefits of utilizing all or part of the “sustainability toolkit” described in this report. The majority of corporations, though, will be expected to begin responding to incentives created by new applications of economic instruments in environmental policies or to opportunities created by a reconfiguration of their relationships with government to accelerate adoption of new environmental management practices.

BALANCING INCENTIVES

It certainly makes sense for governments to make use of market-based environmental policies known to be effective at encouraging corporate innovation to meet pollution and natural resource management standards. The public sector also should encourage the uptake of voluntary tools that can take firms beyond compliance. In the process, it will prove beneficial to both public health and the sustainability of the environment to reassess those laws and regulations that have proven difficult to enforce with an eye toward enhanced policy effectiveness.

Market-based incentives such as penalties for pollution loads exceeding those determined to be consistent with the environment's assimilative capacity or tax breaks on investments in energy-saving technologies can induce changes in the behavior of firms. As suggested in AEO 2001, much of this will be focused on internalizing "market externalities" (ensuring that polluters pay for the damages they cause), "green" tax reform, and the elimination of perverse subsidies.

It is crucial that governments find the most effective means in their country settings for encouraging the adoption of sustainability tools and for furthering innovation. Fortunately, many of the region's largest corporations—especially those with international ties—already recognize the benefits of these tools. The more difficult problem is how to encourage similar practices by millions of SMEs. Supply chain pressures—and the "greening of the supply chain"—can potentially lead to substantial environmental performance improvements through links between MNCs and their Asian and Pacific suppliers. Multinationals appear increasingly to be requiring local suppliers and contractors to meet product and process standards. While product standards tend to be specific to the manufacturing sector, process standards are rapidly accepting ISO 14001 as the EMS template for certification of environmental responsibilities. Likewise, the GRI has emerged as best practice for environmental reporting. Demands on local suppliers to accept process standards as a cost of doing business with MNCs also are increasing accompanied by monitoring and auditing by reputation-sensitive international buyers.

A less common linkage between multinational firms and suppliers is technical collaboration. While the cost of meeting standards and submitting to monitoring may be seen as a substantial burden by some SMEs, MNCs can help to reduce this by providing hardware solutions (such as pollution abatement technologies) or guidance to SME management in relation to developing and implementing sustainability tools. There is

some evidence that this is already happening, especially training for EMS development.

MNCs are not the only avenue for assisting SMEs with technical assistance on sustainability tools. If foreign firms are unwilling to be partners, then industry associations, national governments, and multilateral agencies can fill this role. In most parts of Asia and the Pacific, government agencies will probably be the best vehicles for providing such technical assistance on clean technologies and pollution prevention, for example, although in some countries, firms are more likely to be sensitive to the influence of their trade associations. There are already good examples of government-funded capacity-building programs for EMS in Malaysia, Singapore, and Sri Lanka. Experience has shown, however, that such programs must be firmly grounded in an understanding of applicable market forces and thoroughly blended with other complementary policy measures to be effective.

Governments and multilateral institutions can also assist with the difficult problem of how to deal with environmental management in very small firms and larger SMEs that are not involved in multinational supply chains. Dealing with such firms is difficult mainly because there are so many of them. While their individual environmental footprints may be quite small, the combined effect of millions of small firms can be just as damaging as that of a smaller number of large corporations. Several approaches to direct interventions hold promise for this region. These include EMS tailored to the special needs of SMEs, government-sponsored and field-based "extension" services to provide technical guidance, and eco-friendly industrial estates.

There are examples from developed countries of customized EMS that have been successfully trialed with SMEs. These involve simple "template" systems that specifically address the concerns of small firms about the cost, time, and documentation associated with developing and implementing full EMS. These simplified systems would rely on a checklist approach rather than on comprehensive record

Box 8: Small and Medium-Sized Enterprises and Environmental Compliance

As many governments around Asia and the Pacific have found, trying to get small and medium enterprises (SMEs) to clean up is a difficult prospect. For a number of reasons, conventional regulatory measures are not effective with this group. First, they lack capital, and often cannot afford cleaner production technologies or end-of-pipe measures. Second, many of them lack environmental knowledge and awareness (some are not even fully aware of their harmful environmental impacts). Third, most SMEs lack exposure to public scrutiny and adverse publicity. Meanwhile, the sheer number of such enterprises means that understaffed and underfunded regulatory regimes cannot hope to effectively reach and regulate the group (a problem, it should be noted, that is also experienced in developed countries). And even if enforcement were stronger, countries would risk putting people out of work and shutting down local businesses if they clamp down heavily on pollution.

Part of the answer may lie in trying to get SMEs to comply with voluntary standards, but even here there are problems. The cost of benchmarking to world standards for an SME can be forbidding. To achieve ISO-14001 status, for example, most companies need to hire environmental consultants to guide them through the process. These consultants can cost between US\$30,000 and US\$60,000 per company certification, depending on circumstances. An ISO-14001 audit usually takes three days, followed by a "surveillance audit" at a farther cost of US\$6,000 to US\$12,000 per year. Additionally, another audit is required when the certificates expire after three years.

If an SME wants to go further, the ongoing advisory costs for a comprehensive reporting program can be even more prohibitive. The lowest charges for verifying these reports can easily be twice the cost of actually producing them. And if a company tries a lower cost option, such as using an NGO, it risks not getting its environmental and social reports verified, which defeats the purpose of the exercise. Thus, those SMEs that are considering certification must weigh the considerable costs of meeting international standards with the potential benefits.

Since many SMEs lack awareness and knowledge about potential cost-saving management practices, many governments and donor programs have focused on sharing information and promoting voluntary measures—often working through industry associations. As it is quite common for similar SMEs to geographically cluster, some progress has been made by retrofitting common pollution collection and treatment systems or by relocating SMEs to industrial estates providing such services. With respect to financial constraints, special funds have been established through commercial banks in several countries, namely, Sri Lanka and India. These measures clearly demonstrate that SMEs can improve their environmental performance if they are motivated to try, and are given access to cleaner production assessment methods as well as financing and technologies for environmental management.

Sources: Gunningham, Neil. Compliance, Enforcement and Innovation. Australian National University; Lincoln, Adam. 2001, September. For Good Measure. *CFO Asia*. Hong Kong. <http://www.cfoasia.com/archives/200109-31.htm>

keeping, thereby acting as a kind of self-audit backed by industry-specific environmental guidelines.

Another approach that might be taken by national governments and multilateral institutions to assist very small firms is to apply the self-help model of agricultural extension programs to the problems of environmental management. There are many examples in Asia and the Pacific of farmers organizing to teach other farmers about improving productivity. The agricultural extension training and visit scheme adopted in many developing countries may also be worth emulating.

A third approach is the establishment of industrial zones in which the tools are made mandatory. This will work best in industrial estates, especially where products are bound for export to developed-country supply chains. Both the PRC and Thailand have been experimenting with this idea, and the PRC recently announced that nine economic development zones, five "high-tech" development zones, and four scenery spots have been approved as national demonstration areas in which ISO 14001 certification will be a prerequisite for business operation. Such schemes also lend themselves to the provision

of common waste treatment facilities, and the relocation to industrial estates of SMEs processing similar products (notably the tannery and textile industries) has been undertaken in Indonesia, Pakistan, and Sri Lanka.

ENVIRONMENTAL REGULATORY REFORM

This report argues that the traditional options of command-and-control regulation will not be enough to meet the sustainability challenges provided by the region's continued rapid economic expansion. A recurring theme is that more rapid progress is needed with the application of market-based incentives to encourage private innovation. A full conversion from the current system will only be possible if accompanying reforms are made in public environmental policy. The combination of diminishing government resources and an explosion in industry self-management initiatives is now leading to a reconfiguration of regulatory approaches. This is strongly evident in developed countries, though it appears to have happened largely by policy evolution rather than by design. While there are hesitant signs of such reconfiguration beginning in Asia and the Pacific, most environmental policy in the region remains firmly centered on the command-and-control model rather than on the use of market-based incentives or voluntary measures involving public-private partnerships. Though even the developed world has less than a decade's experience with this new mix of policies, some important lessons are emerging of direct relevance to region.

Serious attention needs to be paid to the wider application of voluntary environmental instruments. Various propositions have been made in recent years about how the supporting policy frameworks for introducing voluntary initiatives might best be designed. The most useful of these suggest that they should build upon a careful linkage between the most important drivers of voluntary corporate

initiatives: (i) cost reduction, (ii) desire to avoid regulatory action, (iii) concern about damage to public image, (iv) expectation of competitive advantage, and (v) pressure from stakeholders.

In this new mode of "co-regulation," there is a genuine sharing of responsibility and authority for administering regulation between governments and industry. The proper role of government becomes setting clear but broad targets for important environmental outcomes or conditions and then stepping back to allow firms wide-ranging freedom to find the most cost-effective methods by which to comply. A good metaphor for this new approach is "steering not rowing." It should also be noted that the introduction of voluntary measures often has faced considerable skepticism and outright opposition from environmental advocacy groups who see these approaches as too soft on polluters and too willing to strike compromises with private firms in order to achieve environmental goals.

Evaluations of developed country use of voluntary environmental instruments have begun to indicate some minimum preconditions for success. In general, it seems that governments need to (i) present a credible threat of regulation should self-policing fail; (ii) maintain capacity for auditing and monitoring; (iii) establish a system whereby offenders can be made personally liable if they fail to comply; and (iv) cultivate an active civil society that can provide indirect oversight and monitoring support to regulatory authorities.

Some regulators in the region are interested in voluntary environmental instruments precisely because they offer policy alternatives that require less administrative structure and rely more on the private sector itself for monitoring and choice of environmental management measures. While meeting the full preconditions would provide the ideal conditions to support a co-regulation approach, there is enough evidence from Asia and the Pacific to indicate that significant progress is possible even with only some of the preconditions in place. For example, despite weak or nonexistent formal regulation, there

are many clean industrial plants in the region. Analysis done under the World Bank's New Ideas in Pollution Regulation project has identified examples in South and South East Asia where factories are less polluting than in the past and where total emissions are falling despite strong industrial growth.

The role of regulation as a credible threat may become less important over time in the Asian and Pacific context as the effectiveness of an increasingly active civil society grows. The preconditions mentioned also may not need to be present where there are powerful self-interests at stake. Such incentives, as previously described, could include (i) protection of reputation; (ii) enhanced market opportunities; (iii) requirements imposed by financial institutions or foreign partners; and/or (iv) the existence of environmental improvements that directly result in cost savings.

While co-regulation and associated voluntary environmental policy instruments may significantly improve corporate environmental performance, this should never be a rationale for abandoning standards and supporting regulations. Governments in Asia and the Pacific should continue to develop and refine their formal regulatory structures and enforcement capacities as complements to these other policy approaches. Furthermore, some environmental goals, such as the control of hazardous and toxic substances, may continue to be best accomplished through strict regulatory approaches. For certain countries where capacity is very weak, informal regulatory approaches could be a short-term strategy for halting environmental decline, until a full blend of formal regulatory structures, market-based incentives, and voluntary measures is put in place.

In some countries of the region, environmental law and policy already allows for use of voluntary agreements. Indonesia, for example, has experimented with the PROPER system of publicly disclosing rankings of company environmental performance according to a five-point scale, and then working with the low performers to adjust

their behavior under threat of sanction and public disgrace. Viet Nam is experimenting with a similar approach. Other measures could include encouraging the establishment of units within industry associations or leading financial institutions that pay attention to environmental performance, perhaps giving them shared responsibility for the development and implementation of voluntary agreements. This has been used in Sri Lanka with some limited success.

Voluntary mechanisms rely heavily on the free availability of information to all stakeholders, though there are still few locations in this region where accurate and timely environmental information is made available to stakeholders by the private sector. Given what seems to be the growing importance of co-regulation, including information-based policies, governments will find benefit in passing legislation requiring the regular publication of environmental data (taking into account proprietary concerns). Examples include "right-to-know" laws, "green rating" schemes (such as Indonesia's PROPER), compulsory annual reporting on corporate environmental performance, and the publication of national registries of voluntary initiatives.

CONCLUSION

The impetus for this report is a sense of urgency. Our planet is facing unprecedented levels of environmental strain, and much of this is the result of the extraordinary economic growth recently witnessed in Asia and the Pacific. The future of humankind and the planet will depend in large measure on how successful the environmental policies and practices are in this part of the world.

The business community's actions hold the key to whether further rapid economic growth in this region can be achieved without undermining the basis for health and prosperity. Times are changing, and the private

sector can expect to face considerably more oversight of its environmental performance by governments, communities, advocacy groups, financial institutions, shareholders, and consumers. These changes are likely to bring higher costs in many cases, but there also will be opportunities for savings and even enhanced revenue generation through eco-efficiency gains and product differentiation. The tools to identify such opportunities are readily available and center on incorporating into business practice far better systems for measuring inputs, outputs, and associated environmental impacts. Working with these forces rather than fighting against them, hiding from them, or paying them off, companies will find ways to help shape the environmental laws that affect them so that they encourage innovation and creative solutions to pollution or natural resource degradation challenges.

National governments need to recognize the growing citizen and consumer demands for better environmental quality and management. This can be especially important for export competitiveness given the rising expectations imposed by importers. Environmental policies need to be reviewed and improved in light of these developments with an emphasis on inducing efficient and innovative responses to problems of waste management and natural resource degradation. New market-based and voluntary policy measures can be used to shape corporate behavior while also creating the conditions needed to engage with the private sector in meeting the rising demands for environmental infrastructure across the region.

As called for in AEO 2001, governments also must do a better job of integrating environmental concerns into both macroeconomic and sector policies and must conduct an active search for new means to finance environmental infrastructure, especially to identify appropriate areas where the private sector can provide services. They can do this with the assurance that while some jobs will be lost in polluting industries, this is likely to be offset by new economic opportunities created by mitigation and clean-up efforts, by the

construction of environmental infrastructure, and by a wide range of new jobs in related service industries supporting such activities.

Development agencies need to recognize the direct links between environmental quality problems and constraints to growth, investment, and poverty alleviation. Past policy advice needs to be informed by these important new trends to take more positive attitudes toward the private sector's role in addressing the environmental consequences of development. There are enormous investment demands, and the public sector alone cannot hope to provide the capital and expertise needed to meet them. New financial instruments will be required that tap into private capital and involve closer public-private cooperation in planning and implementing environmental infrastructure and other investments while continuing to rely on market forces.

Wise companies will anticipate these changes and find ways to shelter themselves from the potential for increased cost and risk by taking advantage of opportunities to raise their competitiveness through operational innovations and product differentiation. Those who are slow to act will find themselves at odds with their governments, communities, and shareholders while also losing market share for their products or services. A new definition of "business as usual" is emerging in which gross neglect of the environment will no longer be tolerated, with both large and small companies expected to exhibit environmental responsibility. Those who step up to this challenge will prosper while those who do not will increasingly find themselves to be out of step with their peers and society at large and their ability to operate threatened by competition and by the heavy scrutiny of governments, shareholders, consumers, and the communities in which they operate. ■