

An Excitant Technical Paper

# Designing an Effective Environmental Balanced Scorecard:

**Avoiding mistakes that undermine  
sustainable thinking. Incorporating your  
Environmental and Social Strategy into  
your Balanced Scorecard so  
you embed it in your organisation.**

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## 1 INTRODUCTION

**First a warning:** If you are simply looking for ways to measure carbon footprint, this paper may not help you (yet).

However, if you are an organisation that believes in a sustainable environmental approach; if you want to embed environmental and sustainable thinking into the way you think and act as a business; if you want to design an environmental balanced scorecard that communicates and supports such thinking and action, then read on.

This paper explains how to represent your environmental and social impact and describe your environmental and social strategy. It explains **where you measure and managing** environmental and social impact and how you can improve how you communicate the importance of environmental and corporate social responsibility.

Our Managing Director, Phil Jones, first used an environmental perspective in a strategy map for balanced scorecard design in 1998, when working for Norton & Kaplan. Since then we have continued to use it ever since, with a wider scope, to capture both social and environmental impact in a wide variety of organisations.

This paper assumes some basic knowledge of modern balanced scorecard design. This includes: strategy maps, balanced scorecard perspectives, the cause and effect model, and the principle of 'Objectives before measures'. These are explained briefly in this paper, but should you wish to find out more, please visit the Excitant Website and look at our Balanced Scorecard 101 articles. [www.excitant.co.uk](http://www.excitant.co.uk)

## 2 EMBEDDING ENVIRONMENTAL & CSR THINKING

Today, organisations want to embed sustainable, environmental thinking into the way they think, behave and work. They want to avoid superficial “green-wash”. They want to make a difference. They also want an environmental reputation, but one that comes from their values, behaviours, and culture, rather than simple claims of environmental impact. They want to be able to demonstrate their environmental and social credentials. It can make a significant impact on how customers perceive the organisation and how markets and investors value the organisation. It is important to the people who work there as well.

This paper explains how to incorporate an environmental impact perspective into your strategy map and balanced scorecard. It explains how to capture, measure and manage environmental and social impact on your balanced scorecard.

The importance of an organization’s impact on the environment and the demands for environmental management reporting has made it easy to argue for a dedicated environmental impact perspective in the balanced scorecard. The Kyoto agreement, ratified in 2005, established national greenhouse gas emission targets with various governments passing laws to ensure reporting of the environmental impact.

Environmental issues are now being incorporated into annual financial reports (Institute of Chartered Accountants and the Environment Agency 2009). Carbon trading has been introduced in the EU (EC directive 2003). ISO 14001 the standard for environmental management systems makes it clear it is designed, ‘with the commitment of your entire organization...to address the delicate balance between maintaining profitability and reducing environmental impact’.

There are taxes on the disposal of waste & landfill (HMRC 2010) and new standards for recycling are being introduced across industries. Individual industries such as paper, electrical components and forestry have introduced their own standards for sustainability. Using an environmental impact perspective also helps to dispel the misconception that the balanced scorecard model is ultimately profit driven.

For many organizations their environmental impact is only a part of their wider corporate social responsibility (CSR) agenda. The CSR agenda includes the organization’s impact on its community and the parts of society it interacts with. It can include charitable and philanthropic work. It includes the consequences of the organization’s approach to ethics. It includes the supply chain, with many organizations having codes of conduct to ensure a responsible approach towards suppliers considering their rates of pay and their working and living conditions.

Increasingly shareholders are looking at the CSR records of companies to determine whether they should invest in them or withdraw their funds. Porter and Kramer (2011) suggest that truly integrating CSR thinking into your business and your supply chain will be the next way to create sustainable economic value in organisations.

Many organisations already think this way. They have moved beyond the 'greenwash' of appearing to take on environmental issues, and take such issues to the heart of how they work and think. Having a social and environmental impact perspective within your strategy map and balanced scorecard, that is tightly linked to your strategy, is becoming mandatory.

**3 AVOIDING THE MOST COMMON MISTAKE**

There is a common mistake made when designing environmental balanced scorecards. If you are designing or deploying an environmental scorecard and make this simple mistake you will waste time, undermine your sustainable intentions and miss a real opportunity to improve.

**3.1 THE SIMPLISTIC ADDITION OF AN ENVIRONMENTAL PERSPECTIVE**

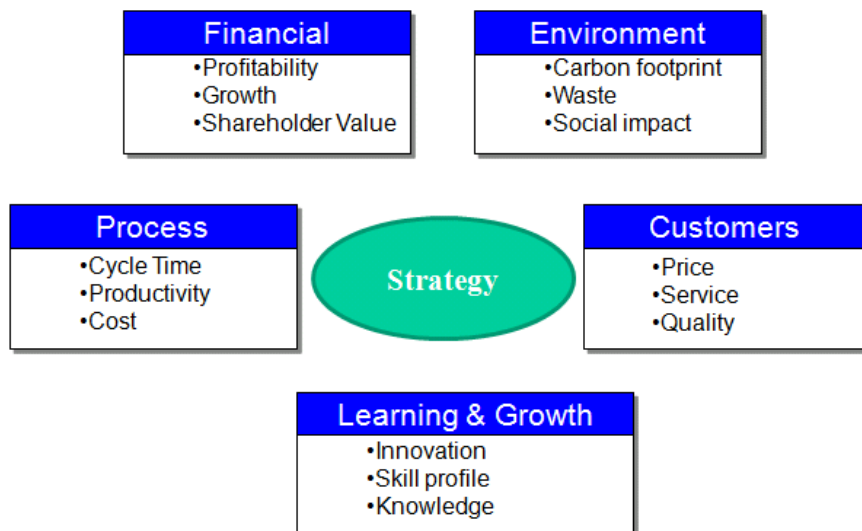
The logic seems to argue for a dedicated environmental perspective in the balanced scorecard. It appears to address Kyoto, environmental legislation, and its demand for management reporting. It seems obvious to add an extra environmental perspective, alongside your other perspectives, in your balanced scorecard.

The mistake is this:

*Simplistically adding an “environmental perspective” to your organisation’s balanced scorecard.*

Sorry, but it will not work. It will create more problems than it will solve and undermine your environmental credentials. Figure 1 shows a typical approach where an additional perspective has been added.

**Figure 1. Adding an additional environmental perspective does not work.**



Yet many make this basic mistake when starting to incorporate environmental reporting into their balanced scorecard. They simply add an environmental perspective to their scorecard, without thinking what it should contain and how other perspectives might be affected.

As a consequence everything and anything that mentions the environment is now added into this perspective. It becomes an unstructured collection (read dumping ground) for anything that contains the words environmental or sustainable. It does not work. Placing **everything** associated with environmental issues into that environmental perspective is a massive mistake that will cause three problems.

### 3.2 THE CONSEQUENCES OF THE SIMPLISTIC APPROACH

These problems are:

- 1) Everything associated with environmental and sustainable thinking is now isolated in a separate perspective, rather than them being a part of what everyone does. It divides, rather than integrates. Environmental issues are separated.
- 2) It focuses attention on environmental impact, carbon footprint, but it fails to address the drivers and enablers and thinking behind the environmental or social impact. It tells you the result, but not what to do about it, how to do it, or why?
- 3) It loses the cause and effect story that the strategy map and balanced scorecard should have, so you can't tell the story of your environmental and social strategy. How will your capability skills and knowledge change the way you work, so that you have a lower environmental impact? Your story is lost.

Adding a simplistic environmental perspective undermines your sustainability and your environmental credentials. Instead of focusing attention on environmental thinking, capability and action, it undermines them. Precisely the opposite effect to the one you originally intended.

This is also true when you are dealing with corporate social responsibility (CSR). Do not simply add a social responsibility perspective and incorporate everything into that.

### 3.3 IT REQUIRES DEEPER THOUGHT AND ATTENTION

The answer is to *only* use the environmental perspective to capture environmental *impact*.

You should capture the causes and drivers in your *other* balanced scorecard perspectives (Financial, customer, process, learning and growth and value). These are where you describe and embed responsible, sustainable thinking, behaviours and activities into your organisation. Together these tell the story of your strategy for environmental and social responsibility. They provide the basis from which you communicate, monitor and manage this aspect of your organisation.



Managing environmental issues requires more thought than merely adding an environmental perspective and putting anything associated with the environment into that grouping. First, you need to reflect different ways in which environmental and social *impact* is thought about (as a strategic issue. Secondly you need to capture the diversity of drivers of environmental and social impact through the existing perspectives. This makes sure that the thinking is more deeply embedded in your strategy.

Putting absolutely everything associated with environmental topics within that single perspective often happens when the environmental perspective omits “impact” from its name. As a consequence it is seen merely as a topic “Environment” rather than a consequence of the organisation’s activities as in “Environmental impact”. The cause and effect relationship is lost. Anything associated with environmental or social issues is placed in the perspective and the whole causal structure collapses. This also misses a great opportunity to embed environmental and CSR thinking into the entire organization.

If you are using strategic themes it can also be a mistake to create a separate theme that covers environmental issues alongside the other strategic themes that the organization may have.

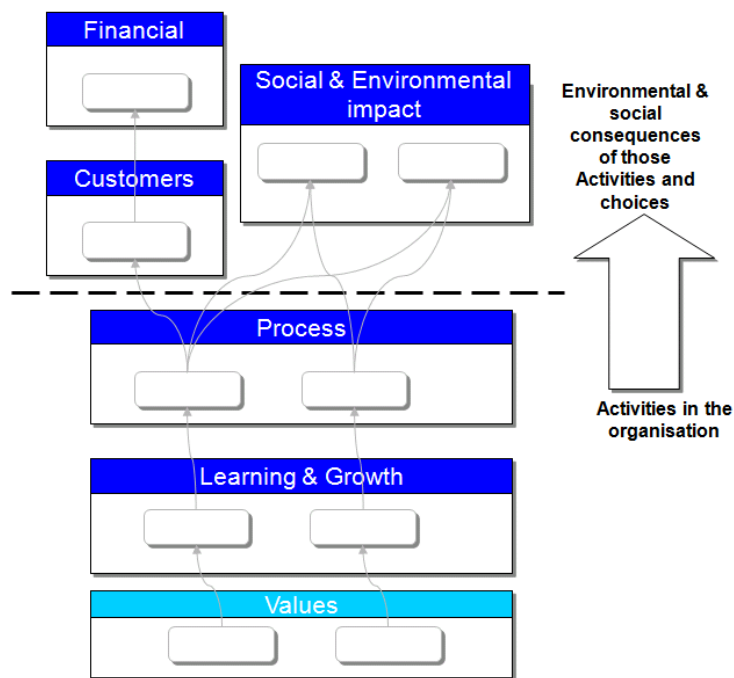
Treating all environmental issues separately, whether in their own dedicated perspective or in a theme, effectively isolates the topic and forces them to be seen as a side issue. Whilst the intention might be to signal their importance you are actually side-lining them, taking them away from the other objectives and removing any embedded thinking.

This is solved by what I call the ‘render unto Caesar’ approach. Rightly, environmental aspects associated with the processes and the learning and growth of the organization should be put in the objectives within the process and learning and growth perspectives. If you wish to bring them out as a set, then treat them all as a theme that spans many objectives.

4 THE CORRECT APPROACH: USING ENVIRONMENTAL IMPACT

The correct way to use an environmental perspective is to capture the Environmental and Social *impact*. The other perspectives then capture aspects of your environmental strategy appropriate to their perspectives. The environmental impact perspective is treated as a separate perspective, alongside the other organizational outcomes of financial and customer objectives (see figure 2).

**Figure2. The environmental Impact perspective captures the consequences of the organisation’s activities**



This split of objectives into perspectives means that to consider the underlying drivers of the environmental impact we need to ask questions relative to each perspective.

From the process perspective, what do we have to do really well to limit our environmental impact?

From the learning and growth perspective, what underlying skills, knowledge, experience, behaviours, culture do we need to learn and grow and develop to achieve these process objectives and influence our environmental impact objectives.

This is the ‘render unto Caesar’ approach. We place aspects of the environmental strategy in each perspective according to that perspective’s view, be it the organisation’s activities or building the capabilities that, say, improve your environmental credentials.

#### 4.1 UNDERSTANDING CAUSE AND EFFECT

It is important here to understand that the perspectives represent a cause and effect model. This model is, in essence, very simple. We will only achieve our financial objectives if we satisfy our customers' needs. To satisfy the customers' needs (Customer perspective) we have to focus on the few things that we have to do (Process perspective) that will ensure our customers objectives are satisfied. We then have to ask what are the few things that we need to learn and grow and develop as an organisation to make sure that we deliver our process objectives so our customers are happy and we make money.

Of course we have to do this economically, so the costs from our process objectives, and learning and growth objectives, must not exceed our revenue, otherwise we will not be profitable.

In the same way our activities must limit their environmental impact. Therefore, just as revenue and costs are the consequence of our strategy and our activities, so is our environmental and social impact.

The focus of attention in this perspective is the impact of your activities environmentally and socially. So you will ask,

'What environmental impact do you wish to have?' or 'What impact do you wish to have on society/suppliers/your community?'

To tease out the direct financial implications for your organization you can also ask, 'What are the financial consequences for use of achieving these objectives?'

To move from this perspective to the process perspective, you would ask, for each environmental or social impact objective:

'What are the few things we have to do really well to ensure we achieve this objective?'

The navigation through the objectives from this perspective is identical in principle to the other perspectives. You should expect to iterate up and down the cause and effect story, as you develop the objectives their characteristics to ensure the story remains consistent and is told in the correct way.

#### 4.2 OBJECTIVES BEFORE MEASURES

Notice throughout this explanation we are talking about objectives in each perspective. This is a fundamental aspect of balanced scorecard development. The strategy map contains

objectives from which measures are later derived. Objectives are developed before measures, so we do not constrain our thinking merely to what we believe we can measure.

The perspectives contain objectives for each perspective. Each of the objectives will have its characteristics developed. It is from these characteristics that we can choose what we want to measure and how to measure it. This principle is known as “objectives before measures”

### 4.3 THE ENVIRONMENTAL IMPACT PERSPECTIVE

As a result, the Environmental Impact perspective only captures the objectives that represent the environmental and social *consequences* of the organization’s activities. The existing lower level perspectives identify what the organization is doing to improve these outcomes or results.

If you wish to split out the social impact and environmental impact of this perspective because they are each especially significant, please do. Just be aware of the emphasis that that provides.

Changing the name of the perspective to say, ‘CSR perspective’, again has implications for the message that you communicate, potentially downgrading environmental impact and emphasising all activities. What matters most is that you model and capture the impact appropriately and communicate your message correctly.

Figure 2 shows how the perspective contains objectives that relate to the environmental and social impact and separately the lower perspectives capture the drivers and causes of environmental and social change. Here you are embedding the drivers within the rest of the strategy.

Where your customers have environmental demands, place their demands as an objective in the customer perspective. You are effectively creating an embedded strategic theme of environmental and social thinking and action.

## 5 DETAILING THE ENVIRONMENTAL AND SOCIAL IMPACT

Do be aware when you are talking about environmental and social impact that there are various forms of impact. So how do you represent the variety of social and environmental issues?

### 5.1 ENVIRONMENTAL IMPACT

When developing objectives in this perspective you are interested in capturing the impact of the widest operations of the organization on the wider environment. Your considerations should include the whole supply chain from first and second tier suppliers through to end users. You need to include the whole life cycle of products from production through to re-use and re-cycling or disposal. In some industries such as the wood/paper supply chain, industry standards have emerged for quantifying and improving the impact on the environment. Some countries now have carbon trading and rules limiting the emission of greenhouse gasses and other air pollutants. In other areas such standards are still emerging. Make sure you consult with industry bodies to monitor standards as they are developing.

Ensure you look at the wider impact on the environment. This might include your use of electricity, water, chemicals, and the sustainability of sources of raw material. There is a temptation to convert all impact to the CO<sub>2</sub> consumption or carbon footprint, but this should be avoided, as some conversion is still in discussion and other impacts are not appropriate. First identify the impact of the material so you are clear what your primary footprint involves, be that, say, chemicals disposal, water consumption or transportation miles. This way means you can address the primary source of the impact. Only when you have this should you consider the second stage of conversion, where appropriate, to a carbon footprint, or another standard if such is available.

### 5.2 SOCIAL IMPACT

With social impact, as with the customer perspective, it is absolutely vital you identify which particular groups in society you might be affecting before you start detailing any impact. This perspective requires you to look beyond your immediate customers, and also beyond their customers. You might look at the impact on the wider population around your organization. You might include impact on the local economy and how you, as an organization, contribute to that group in terms of charitable contributions, help with developments or supporting part of the economy. You might be the impact beyond your immediate customers, for instance a pharmaceutical company might be thinking about the effect of the care of a patient on that patient's family, or the consequential health costs if a patient deteriorates. You might affect your suppliers, where ever they are located in the world.

Again take a two stage approach: make sure you identify the groups that might be affected by your organization and then establish the various impacts on them. Make sure you are thinking of objectives from both their perspective and yours. For instance you might want to foster good community relations (process perspective) with the effect that you are able to gainfully employ people with learning disabilities and so help their development and contribution to society.

With social impact it is useful to adopt the same approach as with the customer objectives: that is to identify archetypes and look at the processes they go through as a result of your social, or environmental, interventions. Then deduce your impact on their lives within that framework.

### 5.3 ENVIRONMENTAL IMPACT DIRECTLY ON CUSTOMERS

As you think through this perspective you will come up with some objectives that fall into the customer or financial perspectives and should rightly fall in those perspectives. You may, for instance, alter the environmental impact of a customer and their supply chain. Here you would include objectives in the customer perspective that reflected that customer's demands upon you, eg 'Lower my carbon footprint'. In the environmental perspective you might wish to include the total carbon footprint saved for your customers by your products or services.

You might also have demands on your environmental performance from legislators or regulators and again it may be appropriate to include this in the environmental perspective or to treat the regulator as a customer. Make sure you include one. Do not double count.

### 5.4 FINANCIAL COSTS (OR BENEFITS) OF ENVIRONMENTAL THINKING

You can also include the direct costs or direct financial benefits of your environmental activities in the financial perspective. That is, how much do your improvements to how you handle environmental issues cost to implement and ultimately save for the organization? Where there are direct costs incurred by the organization associated with the environmental or social impact, then those costs would rightly fall into your financial perspective objectives. Similarly with savings you have achieved. Whether these are captured in the financial perspective of the highest level strategy map, or highlighted in a lower level strategy map, would depend upon their importance within your strategy.

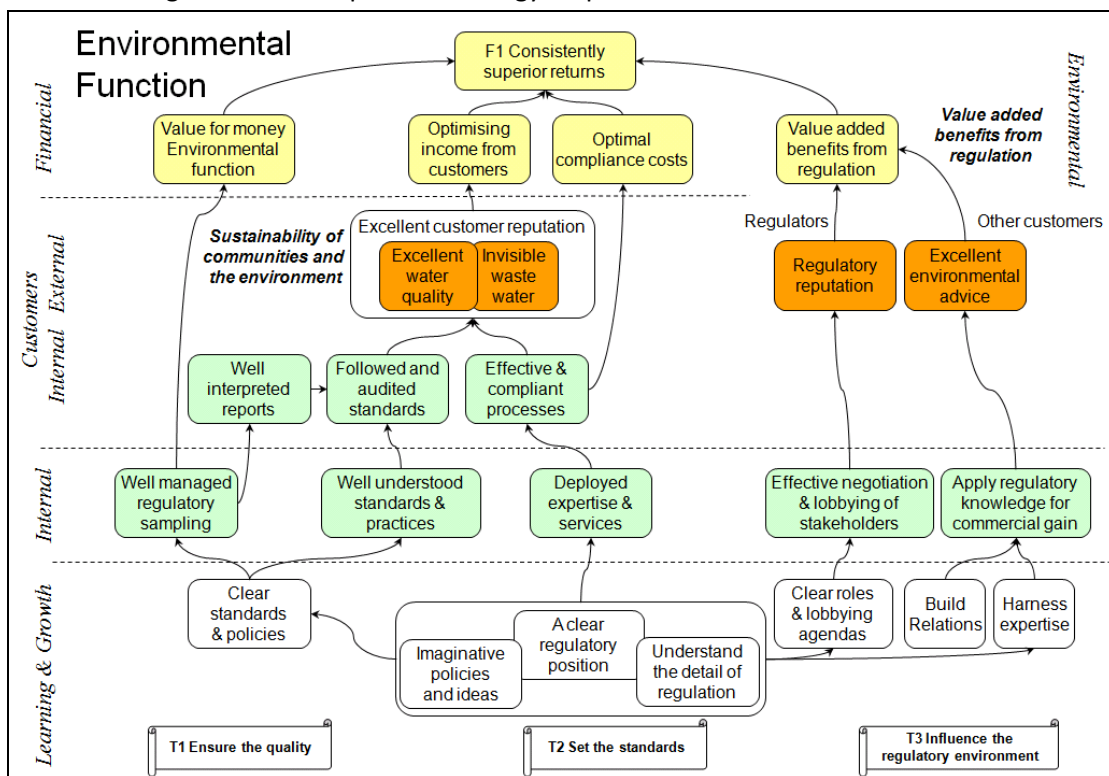
Where you have saved environmental costs for other people that are not reflected in your revenues, for instance you have saved costs for your customers; again these would be captured in the customer perspective with an objective that might say 'Reduce my

environmental costs’. In each case be clear from whose perspective the savings have occurred.

5.5 REPUTATIONAL IMPACT FOR REGULATORS

One aspect of environmental impact can be the reputation with regulators. Figure 12.3 shows how the regulatory department of a water utility company saw their role in influencing the regulator, getting benefits from how the regulation applied to them as an organization and how this would ultimately affect their share price.

Figure 12.3 Example of a strategy map for an environmental function.

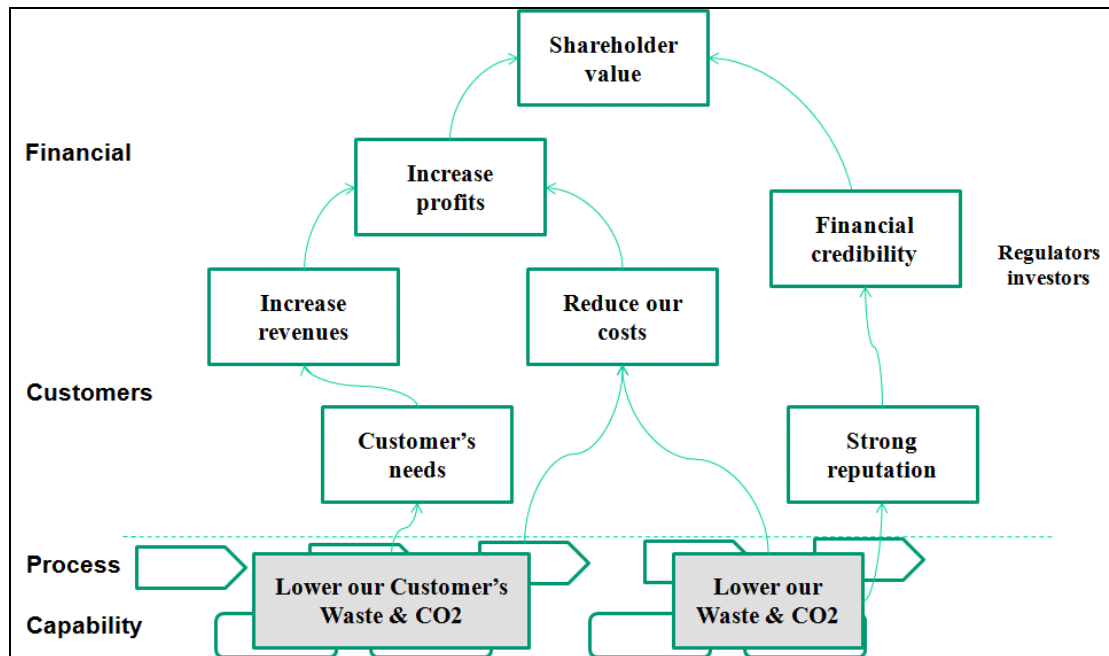


This environmental regulatory department sought to develop their capability across three themes, ensuring the quality of the water, setting the standards by ensuring water quality standards were understood, and directly influencing their regulatory environment. In each theme they identified capabilities they need to develop as well as processes that they wish to improve.

5.6 REPUTATIONAL IMPACT FOR INVESTORS AND FUNDERS

Many organizations see their environmental activities as having an influence on their shareholder value through their reputation with the investor community and shareholders. Figure 3 shows a generic example of this.

Figure 12.2 Environmental reputation can have financial implications [on separate page, landscape]



This organization believes that its environmental credentials influence investors' perceptions, and their regulator's comments, thereby positively influencing their share price.

Clearly the opposite can occur. With BP in 2010 when the oil spill in the Gulf of Mexico caused the share price to drop considerably due to the consequences of both the clear up and the potential fines, their activities adversely affected the share price and value of the organization.



## 6 INTEGRATING SOCIAL AND ENVIRONMENTAL THINKING INTO YOUR STRATEGY

The most effective way to communicate your environmental intentions is to include appropriate words in the objectives of your strategy map. You can show in the lower strategy map perspectives how you bring that impact about. When working with the Environmental Services department of Peterborough City Council nearly half of their objectives included the words sustainable or environment reflecting their intention to be a city with a reputation for its environmental credentials, including reminders in the objectives helps to communicate the message.

In another client, a manufacturer of buildings, they chose not to show their environmental credentials in their top level strategy map. Their credentials were embedded within their objectives and in their lower level strategy maps. For them, sustainable buildings and environmental thinking was already a natural part of their culture and way of working. They designed buildings that had a low carbon footprint to build, were efficient to run and had a long life span, incorporating solar panels and very effective insulation into the designs.

Whichever way suits you, make explicit choices about how you bring your environmental and CSR credentials to the fore.

## 7 MANAGING ENVIRONMENTAL ISSUES IN DIFFERENT WAYS

There are various ways to think about environmental management. Each can be represented in your overall strategy map but you may choose to have a strategy map that looks explicitly at your environmental management. In this case here are five themes directly associated with your environmental thinking and activity. Each one of these themes will have aspects that reflect capability, information, culture and behaviour (learning and growth perspective) and aspects that are about what you do (process perspective).

### 7.1 MONITORING THE ENVIRONMENTAL CONTEXT

You may well be monitoring the environmental legislation to ensure you comply and monitoring environmental trends to anticipate how the technology is moving. This is analogous to monitoring the environmental context. It represents your process for monitoring legislation.

In the learning and growth perspective you may need additional skills, knowledge and capabilities.

Fail to identify changes in the external environment or regulation and there may well be financial costs and consequences.

### 7.2 COMPLYING WITH THE ENVIRONMENTAL LEGISLATION

You will need to ensure you are in compliance with existing legislation and will include processes for monitoring your compliance with the legislation as well as identifying which operational processes need compliance attention.

The learning and growth piece may be about embedding environmental thinking in the activities of production or maintenance and would be represented in the learning and growth perspective.

Fail here and there will be financial costs. The customers here are your regulators.

### 7.3 REPORTING STATUTORY ENVIRONMENTAL COMPLIANCE

You may need to demonstrate and prove your compliance with the standards or legislation and will need an effective environmental compliance reporting process. I put this here to distinguish it from normal organizational compliance practices.

Again you may need to develop environmental auditing skills or some other environmental reporting capabilities that you may need to build into your learning and growth perspective.

There are costs with reporting compliance. There are costs with carbon trading in both the trades and the transaction costs.

#### 7.4 INNOVATING WITH YOUR ENVIRONMENTAL ACTIVITIES

You may wish to be innovative with your environmental activities and improve how you help lower your impact on the environment. It may even be a source of competitive advantage as environmental issues become more important. This is about doing it better.

If you have an R&D process (which some call an innovation process) and that is aimed at improving sustainability then you will also need to develop your organization's R&D skills (L&G). If it is about including environmental capability and thinking into your existing R&D process, then the process remains the same, but new skills, competencies and capabilities will be needed.

This is likely to directly impact your customers and the revenue aspects of the financial perspective.

#### 7.5 PROMOTING YOUR ENVIRONMENTAL CREDENTIALS

Many organizations have learnt to promote their environmental and CSR credentials to positively influence both customers and investors. Here you are taking advantage of your credentials and promoting them.

It is useful to think of this as the public relations process for your environmental or CSR activities. If you add to your environmental credibility, then you may improve your share price, attract new customers or win awards that add to your credibility and value.

## 8 CONCLUSION

The emphasis in this perspective is the impact of the organization's activities on the environment and on those stakeholders affected by the organization's wider CSR activities. The perspective captures the impact. The organizations actual environmental and CSR activities should be embedded within the objectives in the lower perspective of the strategy map. Embedding your thinking in the objectives should ensure that they are not seen as an add-on.

As with any perspective, the ultimate test is whether the content of the perspective helps you communicate the overall story of your strategy and its environmental and CSR credentials.

## 9 ABOUT EXCITANT

Now you have some of the insights our approach and how it creates a sustainable strategic performance management approach in an organisation.

Thank you for taking the time to read this case study. We are happy to talk about what you found and the potential implications for your organisation's strategy.

To find out more, or to have a conversation about how performance management could be improved in your organisation, simply send us an email or pick up the phone.

### 9.1 ABOUT EXCITANT

We are a niche consultancy. We specialise in Fourth Generation Balanced Scorecards that improve how you manage strategy and performance. We are experts in making Balanced Scorecards work as a tool of strategy and performance. We help you to manage such organisations better, so you can get the best out of your people and measurably improve your financial performance and results.

### 9.2 WHAT MAKES US DIFFERENT?

- We want to pass our skills to you, our clients, as quickly and effectively as possible. That way you get sustainable results and we get a good reference site.
- We don't hold back. We ask hard questions and push our clients to uncover and address the deeper elements that stop performance happening.
- Deep expertise. Our skills are based on practical experience and research, so you can improve and develop.

### 9.3 TO EXPLORE THIS FURTHER

For more information or to have an informal discussion about your needs, call Excitant directly and ask for Phil Jones. The number is 08456 809 208 (in the UK) or from outside the UK +44 1780 784 887. Or send our Managing Director, Phil Jones, an email via [info@excitant.co.uk](mailto:info@excitant.co.uk), Thank you.