Accounting for Nature as a Stakeholder in an Agricultural Enterprise (Commonly referred to as the Natural Capital issue)

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1. To start a new enterprise, it is usual to set aside some funds for investment. These funds are needed to acquire productive assets (such as land, buildings, plant and machinery) and to pay bills ahead of revenues being generated (working capital). These investment funds (or shareholders' subscriptions in a public company) are accounted for as liabilities in the accounting conventions that prevail (in recognition of the debt owed to the investor).

2. When the productive assets are put to use operationally it is expected that a profit will be made. This profit is the shareholders' property and when it has been declared it appears as a liability on the next balance sheet. If a dividend is paid out this is netted-off the profits retained.

3. If a business is sold on to a new owner or investor, the selling price may be greater than the original investment (or shareholders' subscriptions) plus the accumulated profits. That is, the new owner has paid a premium to acquire the business. The premium so paid is a liability (just like the original funds) and must be offset by an equal and compensating asset. If the physical form of the business has not changed during the transfer of ownership, then the premium is offset by introducing a new class of assets – intangibles. Typical intangibles include goodwill, reputation, brand values.

4. Suppose that in farming we aspire to treat nature as a stakeholder in a way analogous to the current fashion in big business to declare that employees, suppliers, and even local communities are stakeholders in its business. What does this mean and how do we go about accounting for it?

5. Nature is central to all farming activities. As a partner (and a stakeholder) it delivers a bounty in the form of free-issue produce such as grass. As a stakeholder, as with a subscriber, the contribution made by nature must be accounted for as a liability (with its compensating asset being the value of its free-issue bounty – which might be termed as natural capital). Now the question is what kind of liability does it represent?

6. As nature's bounty comes with mere ownership and not as a consequence of operational expenses it is diametrically opposite to the situation whereby shareholders' funds are expended to deliver produce for eventual sale. The free-issue bounty therefore behaves as a negative cost and appears as a negative asset (just like accounts payable). Consequently, to balance assets and liabilities, nature as a stakeholder must be a negative liability.

7. Now let us test the sense of treating nature's stakeholding as a negative liability.

    a. The assistance of nature as a partner in an agricultural enterprise is that it helps (for free) in delivering produce. As a negative liability this help is reflected in the arithmetic effect that it reduces the burden on commercial activities to produce a return on investment.

    b. If farming practices are detrimental to nature in a particular case, nature's bounty will be reduced. For example, overgrazing this year might reduce the grass yield next year significantly. In such cases the arithmetic effect is to increase the burden on operations to make a commercial return - that is destroying the natural environment is bad for business and the accounting convention indicates this.

8. How can the value of Nature's stakeholding be established? As an example, consider a meadow of 7.5Ha. It will be capable of delivering 100 bales of hay. If a bale of hay from an independent producer is priced at £20 then the hay meadow produces £2,000 of benefit in the form of notional revenue per year. The value of this contribution can be established by answering the question: what would I pay (as a one-off amount) to acquire an income stream of £2,000 per year? If I am looking for a 5% return on investment, I might be prepared to pay up to 20x the income stream. Suppose I consider 10x or £20,000 to be a fair offer, then this is the negative liability that should be entered into the balance sheet. In short it is numerically equal to the net present value of the discounted cash-flows of the income stream equivalent to nature's bounty.

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