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ESG GOVERNANCE: QUESTIONS BOARDS SHOULD ASK TO LEAD THE SUSTAINABILITY TRANSITION

CORPORATE GOVERNANCE
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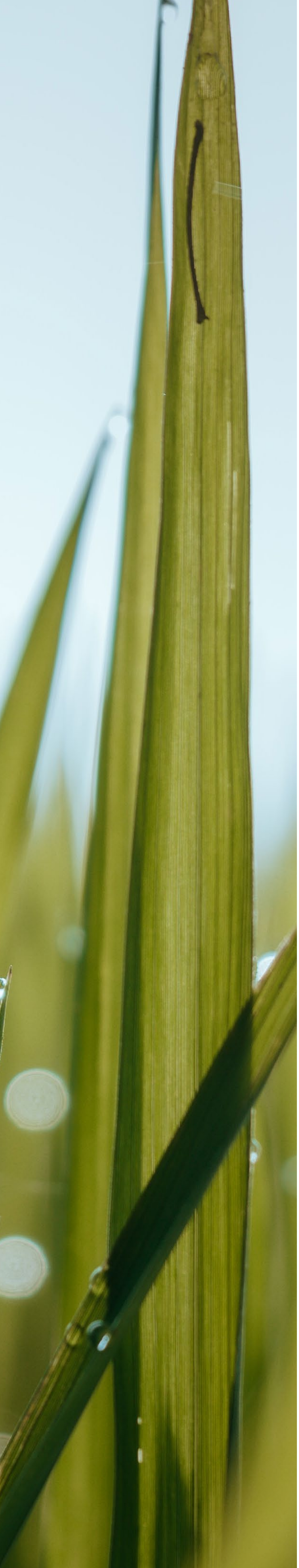
HIGHLIGHTS

Companies' stakeholders from investors to citizens increasingly demand better sustainability performance and disclosures from businesses. Policymakers and regulators are also introducing new legislation on companies' sustainability obligations and value chains. Company boards need to prepare for their enhanced sustainability obligations.

This document, issued by Accountancy Europe, ecoDa and ECIIA, aims to help boards with embedding sustainability – and specifically environmental, social and governance (ESG) factors – into company strategy and business models, and to ensure that proper governance supports this.

The document sets out practical questions that boards should consider in their efforts on ESG, sustainability transition planning, delivery on sustainability objectives and limiting greenwashing risks.

TABLE OF CONTENTS



INTRODUCTION

Company stakeholders — including customers, employees, communities, investors, policymakers and regulators – demand greater accountability and transparency from businesses for their impacts on society and the environment. Investors and civil society are increasingly forceful in their efforts to hold companies – and their boards – responsible.

EU and national policymakers are for their part adapting regulatory frameworks to support – and gradually force – the transformation towards more sustainable business models and economies. This will profoundly impact companies' governance, business practices, operations, and reporting. The mandatory European Sustainability Reporting Standards (ESRS), as a result of the EU Corporate Sustainability Reporting Directive (CSRD) and European Commission's Corporate Sustainability Due Diligence Directive (CS3D)[1] are examples of that.

SUSTAINABILITY: A STRATEGIC IMPERATIVE

Transitioning to a sustainable economy has far reaching implications for businesses. It means new regulatory obligations and reporting regimes, but it is first and foremost a strategic imperative beyond mere compliance. Incorporating sustainability considerations into strategic decisions, operations, value chains and company culture is the pragmatic approach to secure the business' future existence.

Companies which best respond to new stakeholder and market expectations are more likely to gain a competitive advantage, benefit from commercial and business opportunities, improve their environmental, social and governance (ESG) performance and ultimately create long-term value to stakeholders.

OBJECTIVE

This paper aims to help boards with embedding sustainability in company strategy and business models, and to ensure that proper governance supports this objective. It combines perspectives from company directors, internal auditors and the accountancy profession.

HOW TO USE THE PAPER

The paper sets out practical questions for boards to consider, structured in three 'thematic areas':

- business model transformation
- aligning governance with sustainability objectives
- sustainability information, reporting and assurance

This document does not prescribe that all companies necessarily follow the above thematic sequencing. It is ultimately up to the boards to assess how to prioritise their sustainability transition steps. It may also be that for some companies that are more advanced in their sustainability transition only specific sections of this paper will be relevant.

[1] At the time of writing, the CS3D is still in the EU legislative process, subject to final adoption.

BUSINESS MODEL TRANSFORMATION

The business model encompasses everything that is needed for a business' successful operation. This means, for example, its products and services, sources of revenue, the intended customer base, and details of financing. All of these aspects of the business model should be aligned with the company's sustainability efforts.

Board leadership will be instrumental in driving their business' sustainability transition. They must align their company strategy with sustainability objectives, understand their stakeholders' needs and expectations, and oversee ESG risks and opportunities.

REVIEW THE STRATEGY AND BUSINESS MODEL

Governance over sustainability is not about incremental tweaks or a separate sustainability strategy on top of a company's main strategy. It means reconsidering how a company creates value in the short, medium and long term, and conducting a comprehensive review of the company's strategy, business model and its viability.

For some companies this represents some changes in their business model. For others, the level of change needed will be transformational. This will require challenging the company's 'business as usual', and a comprehensive overhaul of operations, processes, value chains, relationships, outsourcing, client acceptance, purchasing, enterprise risk management, understanding future markets, and thinking ahead.

As sustainability affects sectors and companies differently, companies will need to tailor their ESG integration to the specificities of their business model and circumstances. The board's leadership is needed to set the direction and initiate the necessary changes.

STRATEGY

> How is our company's strategy aligned with ESG factors? Are these factors properly translated into objectives, goals, targets, performance indicators, tools and measurement frameworks?

> Who do we consider to be our stakeholders, i.e. for whom and why are we creating value?
>
> *For example, our shareholders, employees, consumers, communities*

> Is our strategy aligned with these stakeholders' interests and expectations? If not, how do we get there?

> What sustainability commitments is our company making – or has already made – and how do we make sure we are delivering on these commitments (consider greenwashing risks)?

BUSINESS MODEL

> Have we assessed our business' ability to create value in the long-term, considering sustainability challenges and opportunities?

> Has management assessed the impact of changing customer behaviours, investor preferences, stakeholder expectations and regulatory developments on our business model?

> What do we need to change to align our business model with sustainability objectives?
>
> *This may include the need to adapt products and services, decarbonise, invest in safe and equitable work practices, or prevent bribery and corruption. For example, if decarbonisation is a key sustainability objective, boards would need to ask what concrete measures the company is taking to deliver on decarbonisation targets, and what supporting tools management has to produce. This may include an information dashboard to allocate responsibilities and accountabilities, track progress and allocate capital and resources to meet those targets.*

> Is our business model worth adapting or should we wind down a particular business line?

UNDERSTAND YOUR SUSTAINABILITY IMPACTS & RISKS

Being aware of the company's sustainability impacts and risks helps to ensure that its sustainability transition efforts are relevant and calibrated for the business. Such awareness is important for the boards, who are responsible for leading these efforts.

Boards need to understand how the company's business activities, including through their value chains, can impact people and the environment. Boards also need to understand the company's own exposures to sustainability factors and how these exposures might create financial risks for the company. ESG risks such as climate change, human rights violations and governance failures can disrupt a company's operations, business models, supply chains, financial position, resilience and viability.

Considering the business' sustainability impacts and risks from both these angles – on the one hand, how the business impacts its surroundings and on the other, how sustainability factors impact the business – is also a requirement in relevant legislation such as the CSRD and ESRS.

?

- Does our company have an appropriate understanding of our value chain's exposure to ESG risks and impacts (upstream & downstream)?
- What action is management taking to assess the key ESG risks that can significantly impact our business?
- What action has management taken to reduce these impacts and risks? How is this process governed and made part of our day-to-day management? What are the targets? Are we meeting these targets?
- Is our company identifying and collaborating with the key players in our value chain to achieve our sustainability goals?
- How might our company strategy need to adapt in light of our identified sustainability impacts and risks?

UNDERSTAND YOUR SUSTAINABILITY OPPORTUNITIES

There are potential business opportunities arising from addressing ESG. These include efficiencies and operating cost reductions, supply chain resilience, and better management of business risks, including liability, regulatory, reputation and market risks. Better ESG performance can help companies win market share, secure profitability, increase company value, develop new products and services, attract investors, top talent and new customers.

- What immediate investments in sustainable practices can we make to gain cost efficiencies?

  For example, reviewing and optimising energy usage, production, waste management and emissions.
- Have we assessed what new finance opportunities/access to capital markets/business collaborations addressing sustainability could bring for our business?
- How does management oversee and support the company's Research and Development processes to adapt existing products/services or develop new ones that align with the company's ESG objectives?
- Are these products/services viable? What will it cost to the company to get return on investment?

ADOPT A SYSTEMIC APPROACH TO SUSTAINABILITY INTEGRATION

The board needs to ensure that the business operates in a wholly connected and consistent way. As the company embarks on its sustainability journey, trade-offs, ethical dilemmas, consistency between targets, key risk indicators (KRIs) and key performance indicators (KPIs), and challenging balancing acts should be expected and courageously addressed at the highest level.

- How do we identify and deal with potential challenges, ethical dilemmas and trade-offs that come with implementing sustainability objectives in day-to-day activities of the business?
- Do we receive adequate feedback on how different company functions contribute to our sustainability objectives, to ensure that we have a complete and comprehensive picture?
- Has management assessed potential conflicting KPIs and KRIs between our financial and ESG performance?
- How does management ensure alignment/compatibility between our financial and ESG related KPIs and KRIs?
- Do we foresee any conflict of interests stemming from board members who only represent shareholders?
- Are ESG aspects integrated in our investment decisions, mergers and acquisitions etc.?

DESIGN TOOLS TO STAY ON TRACK

A roadmap and dashboard are two useful tools to support boards on the sustainability transformation journey.

1. SUSTAINABILITY TRANSFORMATION ROADMAP

Translating strategy into a roadmap will help to monitor progress. It enables to keep track of the changes and assess whether all company's functions, processes and operations are aligned with the sustainability transition plans.

- Who is responsible for the implementation of the business model change?
- Who is responsible for identifying ESG related goals, key milestones, setting appropriate time frames and delivery on these?
- How have investments been allocated to support the business model change?

2. DASHBOARD TO MONITOR PROGRESS

Developing a dashboard will help keep track of progress and assess consistency with the ESG objectives. It could include several factors/indicators/KPIs to assess whether for example remuneration, time allocated for ESG on the board's agenda, capital expenditure and resource allocation are consistent with the sustainability transformation ambitions.

Different dashboard levels focusing on board's and senior management's respective needs could be considered.

A higher-level dashboard for boards would help them track progress, make sure capital and resources are being allocated to achieve the set targets, and challenge management. It could include elements such as key value drivers, targets, milestones, KPIs and trends visualisation.

A more detailed dashboard for senior management would help showcase how ESG considerations are integrated in day-to-day business activities and operations. It could include scenario analyses, measurement criteria, and KPIs to illustrate how ESG targets are being achieved.

It will be key to ensure the cohesiveness between the two different dashboards. For example, the more detailed senior management's dashboard should clearly relate to the board's higher-level dashboard and elaborate in more details on the key focus areas of the board's dashboard.

The dashboards should be kept under regular review. The board should challenge and discuss with management the completeness of the dashboards in the context of evolving scenarios.

- How does management ensure robustness and reliability of information feeding into the dashboards?
- Do we need external assistance or advice to ensure that the dashboards are tailored to our organisation/company and include all the relevant information and criteria?
- Do the dashboards illustrate how ESG targets are being achieved e.g. through feasibility assessments? Should we invite external experts to challenge that?

ALIGNING GOVERNANCE WITH SUSTAINABILITY OBJECTIVES

Governance is fundamental to deliver on a company's sustainability objectives. It is the board's role to ensure that ESG factors are properly integrated into the company's governance, thus enabling the company to make informed decisions, set business priorities and allocate resources.

REVIEW BOARD COMPOSITION

Addressing sustainability will require reviewing the board's composition, diversity and profiles to ensure that the board has the right skillset and mindset to lead the business' sustainability efforts. See more in Accountancy Europe paper – ESG Governance: Recommendations for Audit Committees (2022).

- Do we have the right people around the boardroom table, with the right skillset and mindset, to understand how ESG issues impact our business, strategy, short and long-term plans?
- Does our board composition reflect the right mix of diversity of backgrounds and personalities?
- How are different stakeholder groups' interests reflected in the board composition? Is there a need, requirement or desire to have additional stakeholders' interests represented in the board?

STRENGTHEN GOVERNING BODIES' ESG COMPETENCIES AND EXPERTISE

Governing bodies' competencies and expertise must evolve to make ESG an integral part of a company's broader strategy.

- Do our board and board committee members currently have sufficient competences and expertise to understand ESG topics, and their consequences for our business model?
  This includes identifying potential blind spots such as for example human rights issues in the value chain, access to key raw materials, risks of losing social licence etc.
- What (new) competences and training for existing board and board committee members do we need?
- Can we draw on existing expertise within the organisation to help build up our sustainability and ESG expertise? If not, should we consider consulting external expertise?
- Does management already use qualified external experts to supplement existing in-house knowledge?

COLLABORATE WITH STAKEHOLDERS

Companies need to consider broader stakeholders' expectations as this will enable them to get wider feedback on how the business' operations may affect people and planet. Engaging with relevant external and internal stakeholders will also help companies to ensure that their operations and business model are aligned with these stakeholders' interests and expectations.

Companies should consider various means and formats of stakeholder engagement. They will also need to communicate transparently about their decision making, demonstrate to stakeholders how they are being heard, and explain challenges and issues encountered in considering their interests and how they overcome them.

Boards' leadership will be needed, in particular, to find compromises between divergent needs and interests, considering the company's business model, purpose, value creation processes, production and service lines etc. This is why the board needs to have a solid understanding of how the company and management approach stakeholder engagement.

>	How is management identifying and taking stock of the wider stakeholders' interests, needs and expectations to inform our strategy?
>	Does our stakeholder engagement help us identify which ESG issues are relevant for our company?
>	How does management ensure that stakeholder engagement is recurring, meaningful and effective?

INTEGRATE SUSTAINABILITY IN CORPORATE CULTURE

Integrating sustainability and ESG factors in the business requires a mindset change across functions and a different approach to decision-making – essentially, a revamped organisational culture. The process of embedding sustainability in the corporate culture will be different for each organisation. However, the board's role in fostering and overseeing it will be crucial for any organisation.

Creating an executive sustainability committee at management level or establishing an advisory board are examples of how some organisations approach mainstreaming sustainability into corporate culture, especially on an interim basis or at the early stages.

However, it will be paramount to ensure that the board and governing bodies do not just delegate their duty to act on ESG to such ad hoc functions. The board must assume their leadership, responsibility and accountability for sustainability as for any other aspect of the company's business.

Boards will also need to ensure that ESG considerations cascade further down the organisational ladder towards mid-management levels. Setting the right tone at the top and in the middle will be key to ensure ESG considerations are properly integrated throughout the company culture.

> What is the tone that we are setting at the top and how do we assess whether this tone is generating the desired outcomes?

> How do we ensure consistency between the tone at the top and in the middle?

> How does management promote a culture that encourages consideration of ESG as part of day-to-day business decisions within and between departments?

> Are our recruitment, retention, reward and training practices aligned with the desired culture?

> How do we challenge the usual profiles when it comes to CEO/CFO selection and recruitment? What other qualities, values, ethics, believes and competencies are we looking for on top of the traditional skillset?

This could include for example ESG competencies, proven sustainability track record etc.

> Should we communicate about the organisation's culture to our external stakeholders, and if so, how?

ALIGN PURPOSE, STRATEGY AND CORPORATE CULTURE

Alignment between the company's purpose, strategy and culture is essential to ensure a consistent delivery on the sustainability efforts. Specifically, everyone throughout the organisation should be aligned and have a common understanding of their respective roles in achieving strategic ESG objectives.

> Do all our board members have the same understanding of the company's vision, mission, purpose, values and strategy?

> How do we ensure that different functions across the organisation have a shared sense of the company's purpose and are adhering to our values?

> How do we ensure different departments and functions understand their own roles in achieving the company's strategic sustainability objectives?

> How do we as board members connect with the organisation more broadly to develop our own appreciation of the company culture, in addition to reports from the executive and management?

This may include, for example, company visits, interacting with the workers on the ground etc.

ALIGN REMUNERATION WITH ESG PERFORMANCE

Promoting the right culture to drive the right behaviour is also about incentivising change, including through remuneration. Establishing ESG-based KPIs for executive remuneration schemes will be instrumental in driving sustainability transformation.

- Are our remuneration systems and incentives consistent with our ESG objectives, values, purpose and risk appetite?
- How are we linking senior managers' compensation to ESG performance?
- Should we seek an independent assessment around target-setting, KPIs and ESG performance metrics in our company's executive remuneration schemes?

ALIGN BOARD COMMITTEES WITH SUSTAINABILITY IMPERATIVES

All board committees should take ownership in ensuring that sustainability is truly and fully embedded into the company. Committees should clarify how they see their respective roles in this agenda and report to the board.

Importantly, the board plays a crucial role in driving sustainability transformation and should not simply delegate their leadership on this agenda to a separate board committee. Only assigning sustainability to a separate dedicated function e.g. a sustainability committee risks undermining other board committees' responsibility to get involved with the sustainability agenda.

Sustainability transformation requires collaboration and breaking silos, and coordination across different governing bodies. Collaboration should lead to a comprehensive overview of ESG risks and opportunities, thus facilitating their integration into the business strategy and culture.

- Are board committees' Terms of Reference/charter fit for purpose for our company's sustainability efforts?
- Do board committees allocate sufficient time to discuss sustainability matters?
- How do we ensure that all board committees interact and communicate with each other on their ESG related work?
- Are our board's and board committees' responsibilities, oversight, information exchange and control set up in a way that supports a systemic approach to ESG integration?
- How do we ensure that our board remains on top of our company's ESG integration? Do our board performance reviews reflect that?
- How do the board and committees keep up to date on evolving sustainability risks and opportunities?

DEFINE CLEAR RESPONSIBILITIES AND ACCOUNTABILITY

Clear roles, responsibilities and accountability is key for strong ESG governance. Any confusion in these may lead to duplications, poor performance, non-delivery on the sustainability targets and more.

The board – through its governance model – must define the oversight over ESG controls, risks, KPIs, data, and their relevance for the strategic decisions and the company's purpose.

As a good example, the 'Three Lines' model developed by the Institute of Internal Auditors identifies clear processes and roles to guide organisations toward effective governance, risk management, and internal controls. The model also helps organisations consider the roles needed for effective governance and management of material ESG topics as well as sustainability reporting.

> Are the roles and responsibilities for ESG management clearly defined and communicated?

> How are the different company committees involved in the ESG implementation? For example:
> - How will the audit committee (or another designated committee) provide oversight over sustainability reporting? How will this role interact with the roles of the Chief Sustainability Officer (CSO) and Chief Financial Officer (CFO)?
> - How does the risk committee consider the key ESG risk areas? How does the risk committee (and audit committee) oversee ESG risk mitigation?
> - How does the nominations committee ensure the right skills on the board, access to competencies to deliver on company's purpose and strategy, and attract the right talent? How is it progressing on re-training and recruiting new people?
> - Does the remuneration committee ensure that remuneration is aligned with sustainability objectives? How does it innovate on remuneration to include sustainability KPIs as part of the executives' performance?
>
> *This can happen for example through linking part of executives' compensation to delivery on sustainability targets set at the strategic level.*

SENIOR MANAGEMENT'S ROLE

Senior management identifies, analyses and reports on the risks and opportunities that may affect the organisation's strategic objectives. They are also expected to monitor strategy execution. This means that they have a key responsibility in implementing the company's sustainability transition.

Management should also oversee internal reporting to the board and ensure a high-quality process for preparing the external reporting. Boards need to challenge the information that management presents. Incomplete or selective sustainability reporting risks resulting in greenwashing and loss of trust.

> How do we ensure that the sustainability related roles, responsibilities and accountabilities at the senior management level are clearly defined, communicated and transparent?

> What role will our CFO play in sustainability reporting? How will this role be coordinated across other relevant company functions?

> Do we set clear expectations of the sustainability related information that we need from management?

> Is the sustainability related information that we receive from management adequate, sufficient and clear to support our decision-making?

> Do we consistently and constructively challenge the information that management provides?

BROADEN APPROACH TO RISK MANAGEMENT

ESG-related risks can have a significant impact on company's financial performance and its share price. These risks can impact financial statements in areas such as asset valuation, fair value measurement or impairment and going concern. ESG could also translate into financial risks through legal liabilities or damage to a company's reputation.

To manage these risks, boards will have to consider broader risk categories, identify risks, and understand how they impact their organisation's ability to create value. This entails refining their approach to risk management including physical and transition risks, the impact of stranded assets, environmental litigation and reputational risk.

Risk appetite, risk response, KRIs, KPIs and metrics should be an integral part of the company's enterprise risk management process. Building-up a risk matrix and conducting regular risk assessments will help to identify the right risks, prioritise them and foster a solid understanding of risk environment.

Boards need to be particularly watchful of the greenwashing risk. Greenwashing can result in reputational damage, litigation, fines, legal fees and loss of consumer confidence which will ultimately impact the company's bottom line.

> How are ESG factors considered in current risk categories or the organisation's risk register e.g. strategic, operational, credit, political, etc.?

> How does management ensure that they use the right KPIs/KRIs to consider ESG risks? Do they review them regularly?

> Did we identify any potential green or social washing risks? Which mechanisms do we have in place to prevent green and social washing?

> What risks and liabilities might arise from our company's impacts on society and environment?
>
> *For example, this may materialise through the cost of carbon, fines, customer walkout due to business' polluting activities or damage to the company's reputation.*

> What could be a potential financial exposure of our company's assets and liabilities to negative ESG impacts, e.g. as a result of a climate event? Does the company have the relevant systems and expertise in place to assess that?
>
> *For example, floods pose risks for the real estate sector or for the residential investment trust, draughts can jeopardise an entire sector, e.g. wine producers.*

> What remedial work do we need to undertake to protect our assets against this exposure e.g. through insurance, reduction of operations or changing our energy mix? Can certain ESG risks become uninsurable?

INTEGRATE ESG INTO THE REGULAR CONTROL CYCLE

Sound governance mechanisms, such as adequate policies, procedures, robust internal controls and processes will be key to ensure a comprehensive approach for organisational ESG decision-making and reporting. Boards should oversee and ask questions about the robustness of these tools, to help ensure they are fit for purpose.

>	How does the management ensure that internal controls for achieving sustainability objectives are integrated into the overall governance, compliance, performance measurement and corporate reporting frameworks?
>	How are ESG factors integrated in our enterprise risk management (ERM) and regular control cycle? Is our ERM process fit for purpose to identify, assess and monitor relevant ESG issues?
>	How does management make sure that the controls are identifying actual risks?
>	Are internal controls for sustainability subject to regular review and update?
>	Is the control environment for producing sustainability metrics and targets as strong as the control system for financial metrics, objectives and reports? How can we ‘measure’ or determine that?

SUSTAINABILITY INFORMATION, DISCLOSURE AND ASSURANCE

Having reliable and high-quality information will be crucial both for the company's decision making and external stakeholders. It is also an explicit new requirement from legislation such as the CSRD. It therefore warrants separate attention by the boards.

Understanding the sustainability reporting requirements will help design or challenge the company's strategy, activities, targets, KPIs, KRIs, information gathering, measurement and reporting systems. Compliance and reporting frameworks also help to assess how effectively the company stays on track in achieving the sustainability ambitions and detect what needs to be addressed (gap analysis).

ESRS require companies to report their sustainability information according to the double materiality principle, which means disclosing:

- *how the company impacts people and the environment (impact materiality) and*
- *how ESG issues create financial risks and opportunities for the company (financial materiality)*

ENSURE THE COLLECTION OF RELEVANT, RELIABLE AND HIGH QUALITY INFORMATION

Identifying and collecting the right information will be key to ensure high quality disclosures. This means first identifying the company's data needs. Carrying out a double materiality assessment will help identify which sustainability matters are most relevant to their company and its stakeholders.

Boards need to ensure that the right governance mechanisms are in place for identifying material sustainability matters. The materiality assessment will help determine the relevant sustainability matters to meet the reporting obligations. Focusing on material issues will prevent information overload and unnecessary costs.

DATA COLLECTION

- What systems, including digital solutions, is management putting in place to make sure they are gathering, analysing and measuring the relevant data?
  Including data that we need but is currently not gathered by the existing systems.
- Who is responsible for collecting that data?
- How does management ensure the data's reliability and what controls do they have around this data?
- Is management working towards having a single master data set, aggregating all the necessary relevant/material data as a basis for reporting to relevant stakeholders?
- Is management bringing in external expertise to challenge the completeness and accuracy of information?

DATA SOURCES

- What ESG related data does the company already have and how does management plan to build on it?
- How does management leverage insights from our stakeholder and third-party engagement?
- Has management explored possibilities to find synergies and join forces with industry associations or other companies with similar data needs?
- If information in the external sustainability reporting is based on input from third parties, how does management ensure that this information is trustworthy?
- Did management consider potential discrepancies between our sustainability information and the ESG rating agencies' information about our company or media/employee perceptions?
- Are there any other sources that we need to consider for gathering information?

DISCLOSE YOUR ESG PERFORMANCE

The CSRD aims to bring sustainability reporting to the same level of rigour and scrutiny as financial reporting. Large companies and listed SMEs will have to disclose sustainability information, including forward-looking information, in their management report according to the ESRS.

Stakeholders too expect sustainability and financial reporting to be on par and are increasingly sensitive to potential inconsistencies between both.

For the companies, connecting financial and sustainability reporting is essential to make better decisions, and prevent the risk of inconsistencies and loopholes between the two reports. This also helps to provide a holistic view of all the factors that may affect value creation, and facilitates better integration of sustainability considerations in companies' decision-making.

Boards are in many companies not in charge of the 'on the ground' set-up of the ESG disclosures. However, they should ask questions and challenge those responsible for it to ensure that the disclosures are of high quality and meet requirements.

ROBUSTNESS OF REPORTED INFORMATION

- Who is responsible for sustainability reporting? Given the interconnection between financial and sustainability information, what does this mean for the CFO's responsibility?
- Are we using the same/consistent assumptions and estimations for financial and sustainability reporting?
- How has management determined the timeframes for 'short-/medium-/long-terms'? Have they made sure that these timeframes are incorporated into our internal systems and policies?
- How does management ensure internal control effectiveness over sustainability reporting? Are there weaknesses and what is being done to address them?

MATERIALITY

- How is our company preparing for 'double materiality' assessment and reporting? Are we leveraging risk managers' and internal auditors' expertise for this?
- Is our company's materiality determination reviewed regularly and is it a dynamic process?
- How are we challenging management to ensure all information that is material to our business is disclosed? Who is in charge of controls on completeness of material information?
- How is management making materiality assessments in the value chain?
- Are material sustainability impacts on the company e.g. climate-related impacts incorporated into financial statements?

LEVERAGE INTERNAL AUDIT

Internal auditors must be independent, and in that capacity provide insight and an objective review on the design and operating effectiveness of the sustainability risk assessment, responses and controls. Internal audit (IA) can provide assurance on essential areas of sustainability information. It focuses its efforts on the organisation's critical strategic objectives/risks and sustainability is expected to be one of them. As such internal auditors can help boards answer the questions raised in this paper.

ESG needs to be part of IA's risk assessment, multi-year audit plan, audit engagements and audit reporting, and should not be seen in isolation. When auditing ESG, internal auditors should also assess the board composition, oversight and committee structures, stakeholder management, double materiality assessment and value chain.

The boards should ask relevant questions to make sure that IA fulfils its role and full potential in supporting the company's sustainability transition.

LEVERAGING IA'S VALUE FOR COMPANY'S ESG INTEGRATION

- Is our IA department involved in the company's ESG transformation, and how? Do we sufficiently leverage their insights and advice?
- Did we ask our IA department to assess the company culture change to ensure that ESG is embedded in the whole organisation?

LEVERAGING IA'S ROLE TO MITIGATE ESG-RELATED RISKS

- Does our IA department integrate ESG in its risk assessment and audit plan?
- How does IA collaborate with internal ESG teams to ensure that ESG risks are properly managed and reported?
- Is the IA department skilled enough (and expected to have a certificate) to evaluate the risks and internal controls linked to ESG matters?
- Did we discuss with the IA department how they identify greenwashing risks and report to us?

ENSURING ALIGNMENT BETWEEN IA AND EXTERNAL ASSURANCE

- Are all assurance providers (internal and external) coordinating their work, not missing any risks, and ensuring that proper controls are in place and no significant gaps?
- How are we planning to challenge the reports of each assurance provider? Do we understand any discrepancy reported?

SELECT AN EXTERNAL SUSTAINABILITY ASSURANCE PROVIDER

The CSRD requires companies to obtain limited assurance on their sustainability reporting from an independent auditor/ external assurance provider. The company's statutory auditor needs to express a (negative) opinion on the sustainability reporting, with an option for Member States to allow another statutory auditor or an independent assurance services provider (IASP) to express an opinion on sustainability reporting instead.

The governing body must select the assurance provider, and assess their quality and independence. Audit committee needs to be involved in the assurance provider selection, monitoring their independence and work, including the audit report. The audit committee will need to make sure the assurance provider has appropriate ESG competencies and knowledge of relevant audit processes.

Which criteria do we/the audit committee use for the selection of the sustainability assurance provider?

- How is the independence of the assurance provider assessed and ensured?
- How well does the assurance provider understand the business and the sector we operate in?
- Is the external assurance provider sufficiently experienced on sustainability matters?

For example, their qualification, track record, own ESG strategy etc.

STAY IN TOUCH

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