

The 20 Critical Questions Series

What Directors should ask about ESG

Updated 2022

Five Pivotal Questions

1. Has the organisation released any statements about its commitment to tackling climate change and helping to end poverty and other deprivations while (a) improving health and education (b) reducing inequality (c) spurring economic growth? If the organisation has not issued an ESG statement or report, has the governing authority considered whether (a) it should (b) whether competitors are doing so (c) the mood of major shareholders with regard to ESG?
2. Is ESG integrated with the organisation's strategies and if so what standards has the organisation adopted for ESG reporting eg the Sustainability Accounting Standards Board (SASB) has developed a set of industry specific standards for 77 industries grouped into 11 sectors?
3. Has the organisation established internal processes to verify accuracy and completeness of ESG data as part of its overall assurance arrangements?
4. How does the organisation ensure reliability and integrity of financial and operational information contained in ESG public reporting including both raw data and any accompanying research? Are associated disclosures presented (a) fairly in accordance with an established framework (b) consistent with recognised criteria that investors and asset managers are using?
5. Does the organisation have auditing arrangements in place for ESG reporting by either a specialist external auditor or as part of the internal audit plan?

ESG Foundations

6. Do the organisation vision and values specifically reflect a commitment to establishing and maintaining a leading practice ESG approach? Does the board and audit committee have ESG as part of their agendas?
7. Does the organisation have an approved policy and framework for ESG that seeks to make sustainable living commonplace and includes such things as:

Environmental

- › Sustainability.
- › Water usage and water safety.
- › Deforestation.
- › Use of natural resources.
- › Waste and pollution.
- › Greenhouse gas emissions and climate change.

Social

- › Social responsibility.
- › Community support.
- › Health and safety.
- › Relationships with employees, suppliers, customers and communities.
- › Equal opportunity and diversity.
- › Economic inclusion.
- › Stakeholder opposition.

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- › First Nations people.
- › Modern slavery and workers.
- › Modern slavery in supply chains.
- › Heritage destruction.
- › Animal welfare.

Governance

- › Transparent and accountable corporate governance.
- › Internal controls and assurance.
- › Responsible corporate behaviour and ethical decision-making.
- › Executive remuneration.
- › Shareholder rights including board diversity.
- › Responsible marketing and advertising.
- › Illegal business activities.
- › Corruption and bribery at home and international operations.
- › Wage theft.

8. Does the organisation have a specific senior person responsible for ESG? Does the organisation have a senior level management committee with ESG as part of its agenda?
9. Has the organisation formally assessed ESG risk and developed action plans to remediate identified exposures outside the organisation's defined risk appetite? Does this include action plans with clear accountabilities for (a) potential ESG damage to the organisation's intangible value (b) reputation (c) ability to operate?
10. Does the organisation have an approved ESG plan? Does this include clear performance measures with targets? Is there adequate budget to effectively manage ESG and remediate risks?
11. Where legislated or voluntarily applied, are ESG risks in operational areas (a) understood and periodically reinforced (b) managed or mitigated (c) appropriately reported with clear rules established to ensure the integrity of reporting? Is there ESG awareness training for the workforce including contractors and suppliers? Are ESG requirements built-in to employee job descriptions and contractor contracts?
12. Is there regular dialogue with stakeholders and investors to ensure the organisation clearly understands current and evolving external expectations in relation to ESG risk?
13. Is there a robust and transparent whistleblower process in place that can address reported ESG issues? Is the process periodically communicated to the workforce including contractors and suppliers? Does it have clear channels for reporting ESG issues?

ESG Controls

14. Does the organisation comply with its legal and regulatory ESG obligations? How does the board and audit committee know there is compliance with ESG obligations?
15. Is inappropriate ESG outside predetermined parameters monitored through consistent 2nd line control arrangements or as part of internal audit coverage? Are there sanctions specified and actively imposed on employees, contractors and suppliers who breach ESG requirements?

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ESG Response

16. Is ESG covered in the crisis management plan or business continuity plan? Is there a media plan to deal with the media following an unforeseen ESG issue becoming prominent in the media? Are there effective and tested processes in place to quickly respond to ESG issues that may arise? Is an up-to-date record of these kept? Is there regular follow-up to ensure appropriate action is taken in a timely way? Is there a formal escalation process for rapid reporting to senior management, the board and audit committee?
17. Are there competent resources readily available to investigate ESG issues and rapidly remediate exposures and risks?

ESG Review and Audit

18. Is there an integrated 3 lines of assurance approach to assurance activities over ESG? Does this include monitoring organisation compliance with good practice ESG principles through periodic assessments or audits?
19. Are reviews and audits of ESG arrangements reported to senior management and the audit committee in a timely way?

ESG Reporting

20. Does the organisation produce a publicly available annual report detailing its ESG performance and results of ESG performance measures? Are results reported to senior management, the board and audit committee in a timely way?

The Big Question

How does the board and audit committee know it can be confident ESG is effectively managed and there is compliance with legal and regulatory obligations?

ESG Defined – Environmental, social and governance – the three central factors in measuring sustainability and impact on society of investment in an organisation to help determine future financial performance.

- › The environmental criteria look at how an organisation performs as a steward of the natural environment e.g. greenhouse gas emissions, water usage, and waste and pollution, including both outputs and inputs.
- › The social criteria examine how an organisation manages relationships with its employees, suppliers, customers and the communities in which it operates e.g. employee relations, diversity, health and safety, and community support.
- › Governance relates to an organisation's internal processes and leadership including executive remuneration, internal controls and assurance, and shareholder rights including board diversity, ethical decision-making, and deterring corruption and bribery.

Fast Facts – More than 80% of mainstream investors now consider ESG information when making investment decisions. There are currently \$23 trillion of assets being professionally managed under responsible investment strategies, an increase of 25% since 2014 which exceeds the gross domestic product of the entire USA economy.

Acknowledgement

Some content has been sourced from 'Powering Audit Committee Outcomes – The Essential Guide' by Bruce Turner (Internal Audit Foundation 2020)

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