



Have you considered auditing your organization's Sustainability?

Internal Audit Financial Services

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The race has begun ...

... and is not about to end anytime soon.



ESG (environmental, social, governance) or sustainability has risen to the top of the regulatory agenda. Fears that it would fall off the radar due to the COVID-19 pandemic have been quashed as the crisis has highlighted that business sectors are deeply interconnected across borders, that societies of all types and wealth levels are vulnerable, and that the environment is under increasing strain. There is strong momentum to change the financial services landscape for the better. However, firms need to balance improving their ESG credentials with the need to survive the impacts of the crisis and manage issues such as credit risk, cost reduction and consolidation.

ESG or sustainability is a broad concept which covers amongst others the areas of Corporate Governance, Human Rights, Labor Practices, Environment, Operating Practices, Customer Issues, Community Involvement and Development. An organization's sustainability process flows throughout all hierarchical levels of an

organization, from its strategic goals down to its operational practices. Given the overarching character of the concept, it is of the essence that initiatives regarding ESG or Sustainability are consistently managed, meaning that organizations should evaluate their ESG impacts, risks and opportunities across the entire value chain. When assessing the risks linked to ESG, organizations should think beyond the 'traditional' reputational risk. Issues and malpractices related to ESG can pose environmental, compliance, financial and reputation risks that can severely damage the company.

For banks and insurers, the financial risks of climate change are in sharp focus as regulators set out expectations for stress testing, ESG disclosures and climate risk management. Asset and fund managers are being required by regulators and investors to embed sustainable investment throughout their businesses and to consider the full spectrum of ESG.

Sustainability can be measured by three central factors: Environmental, Social or Governance (ESG) criteria. These factors can have negative impacts on assets, the financial and earnings situation, or reputation of businesses and therefore have to be considered as risks.

Environmental risks

Examples:

- Supply chain collapse, sea level rise, droughts (physical risks)
- Loss of basis for business model due to pricing of fossil fuels or electric vehicles (transitional risks)

Governance risks

Examples:

- Non-compliance with tax law
- Corruption or attempted bribery
- Inappropriate senior management compensation
- Lack of proper data protection

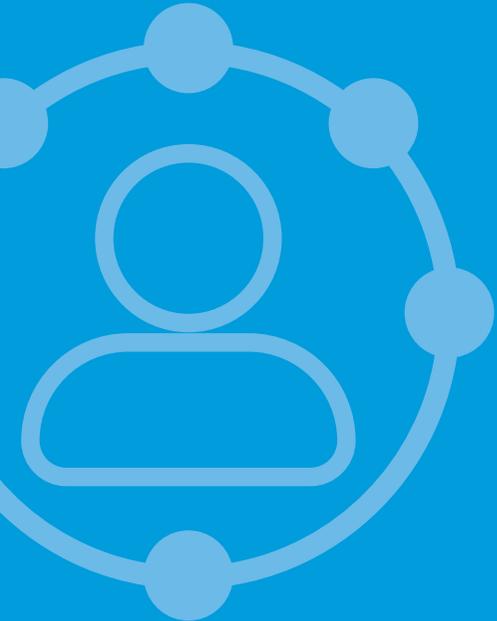
Social risks

Examples:

- Non-compliance with labor standards
- Inadequate payment of labor
- Lack of industrial safety standards and health protection for employees
- Lack of product safety



What is internal audit's role on Sustainability?



Sustainability should be on everyone's agenda, including the one of an internal auditor. Management can commit their internal audit function to get comfort over the ESG processes and data. They can support management in answering relevant questions as:

- Do we know who the company's stakeholders are, and their expectations regarding the organization's ESG responsibility?
- Do we have a clear view on all ESG risks, including compliance risk related to existing and forthcoming national and international legislation, and are those regularly re-assessed?
- Do we have a proper ESG culture that goes hand in hand with our ESG initiatives?
- Do we measure our ESG activities, based on KPI's linked to the ESG strategy?

To that end, internal auditors should take an holistic view at ESG, by assessing the feasibility and credibility of the company's strategy and objectives, screening its due diligence procedures, evaluating the quality of the ESG policies and procedures, and in particular, verifying whether the ESG culture of the organization is sufficient to successfully implement all of the aforementioned elements.

Internal audit should examine aspects at both an operational and strategic level, across different departments. A company's internal audit activity should go beyond simply identifying risks. It must also include identifying root causes, potential risk management strategies and preventive controls. Additionally, internal audit must ensure that governance, risk management and internal controls are operating effectively throughout the organization. In order to so, they can rely on KPMG's Sustainability Audit Methodology.



KPMG's Sustainability Audit Methodology



KPMG has developed an internal audit work program combining different elements of well-known standards, which serve as a basis for good practices, supplemented by our internal expertise in the area of internal audit and ESG.

The methodology is built to assess Sustainability initiatives around three core areas: Define, Execute and Monitor (see Image 1 on page 5).

- In their assessment, internal auditors should assess aspects that define the company's ESG policy like high level oversight, risk assessment, due diligence procedures and awareness and implementation actions.
- Moreover, internal audit should also carefully consider ESG execution; being the tools and technology that the organization has put in place as well as the controls and other follow-up activities.
- Finally, the organization should have installed proper monitoring measures to respond to internal and external issues and should report in accordance with stakeholders' expectations.

In order to facilitate an assessment of the organization's maturity, the elements of the Sustainability audit methodology are evaluated based on their presence, expected level of quality, consistency in comparison with other measures and, their degree of implementation throughout the organization.

We highlight that focus areas vary based on sector and stakeholder demands. KPMG's work program can be tailored to organizations' focus areas and definition of ESG.

Our KPMG audit methodology takes into account the international internal audit standards as prescribed by the Institute of Internal Auditors (IIA).

Internal audit can also leverage on this methodology for facilitating ESG risk workshops, ESG health checks or gap analyses.

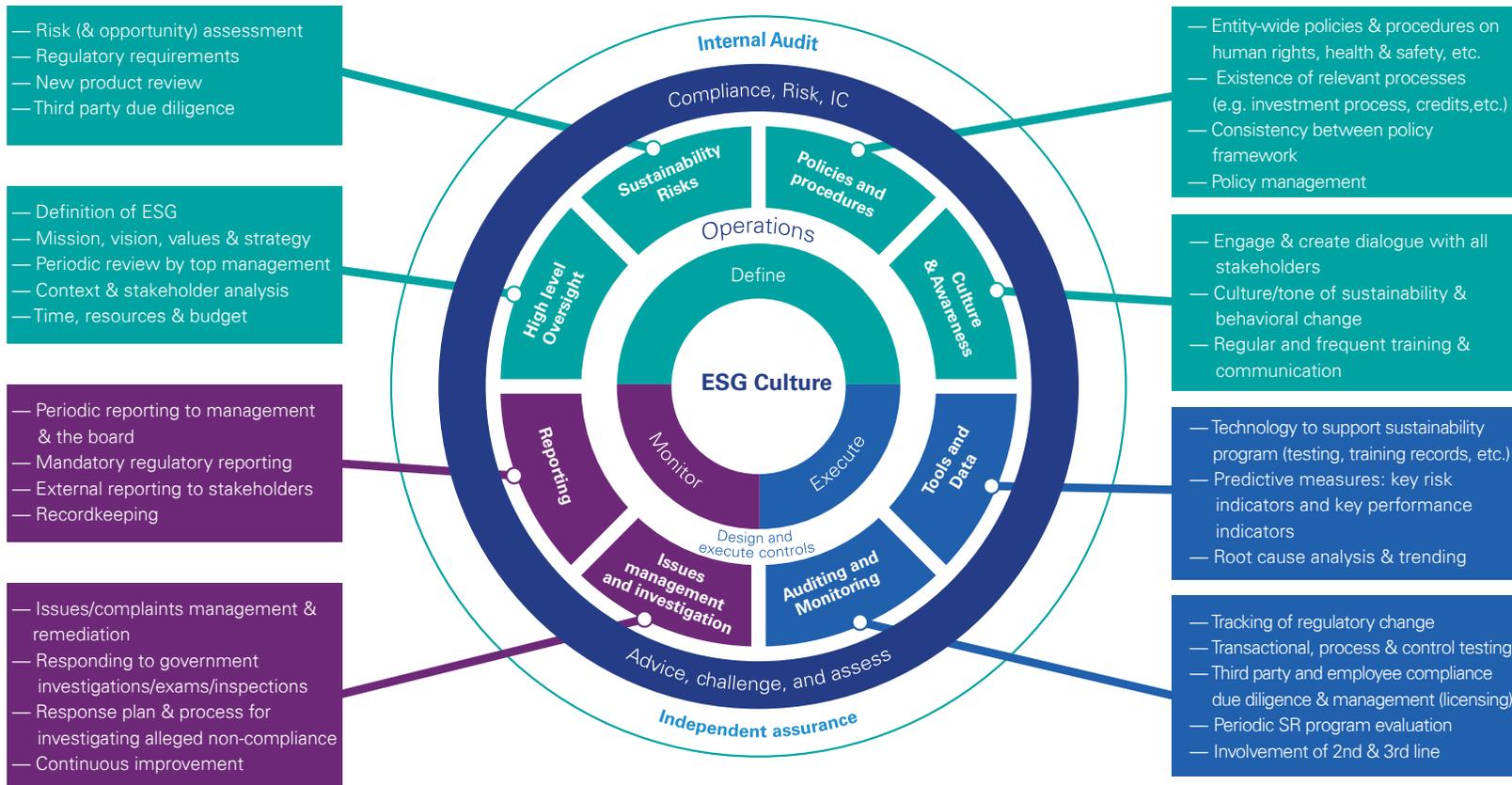
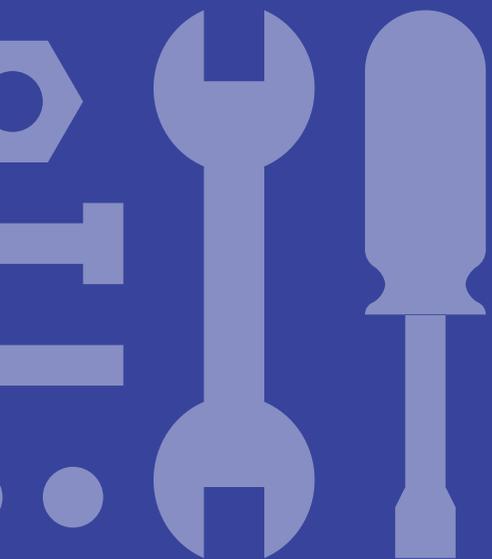
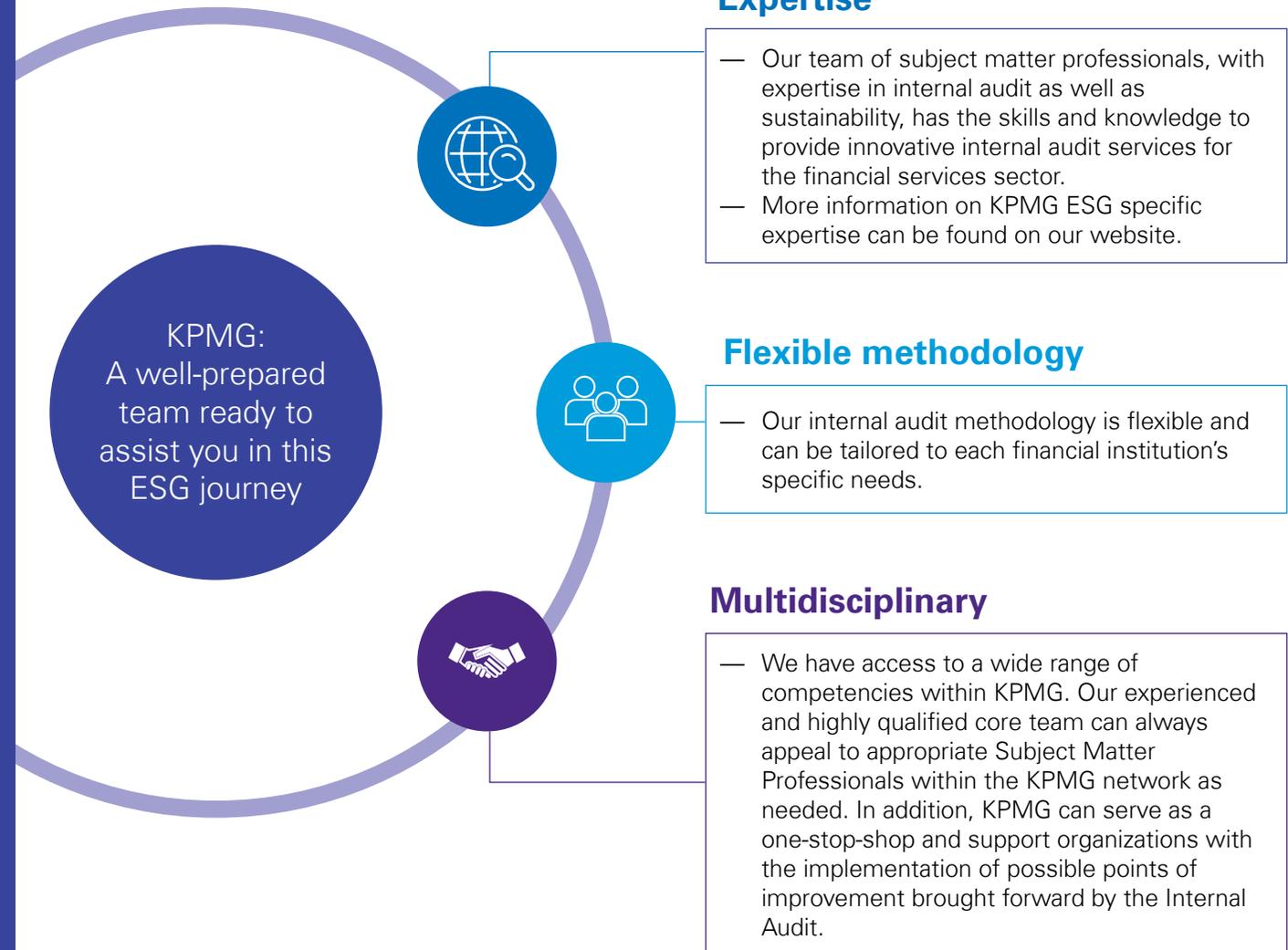


Image 1. Assessing Sustainability: Define, Execute and Monitor.

We can support you in this process to help you grow.



KPMG has profound experience and a tested methodology to deliver solutions across the spectrum of internal audit as well as Sustainability advisory services. We differentiate ourselves through the following:



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