Building Trust in Sustainability Reporting and Preparing for Assurance:

Governance and Controls for Sustainability Information

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Governance and Controls for Sustainability Information

This guide highlights how to establish effective governance arrangements and controls to build confidence in sustainability information to:

Enable sustainability disclosures to be issued at the same time as financial statements,

Reduce the likelihood of modified assurance conclusions or audit opinions, and

Meet investors' expectations that sustainability reporting is prepared with the same rigor and ethical approach as financial statements.

CFOs and finance functions, and those in specialized roles such as sustainability or ESG controllers together perform critical roles in enhancing the quality and relevance of sustainability-related information. By applying financial reporting expertise and know-how they help companies extend and apply their existing financial reporting systems, processes, and tools leading to an integrated governance and internal control environment for financial and sustainability reporting.

Companies are working diligently to establish governance structures, and the processes, systems, and controls needed to support reliable and decision-useful sustainability information required by the International Sustainability Standards Board's (ISSB) global baseline, the European Union's Corporate Sustainability Reporting Directive (CSRD), and other jurisdictional requirements.

However, companies and their investors need a step-change in the quality of information to support robust sustainability reporting and assurance to improve the understanding of sustainability risks and opportunities and align sustainability and financial reporting in terms of quality, timing, and connectivity.

A systematic annual cycle of governance and control activities enables companies to prioritize their efforts to enhance the maturity of data and reporting processes and systems providing the foundation for addressing both technical and change management-related challenges. Ultimately, effective governance and controls for sustainability reporting are needed to reduce the likelihood of modified assurance conclusions or audit opinions, particularly in the early years of implementing new disclosure standards and requirements.


BUILDING TRUST IN SUSTAINABILITY REPORTING:
The Urgent Need For Integrated Internal Control

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Why is Integrated Internal Control Needed?

Trust in high-quality information is the lifeblood of capital markets. It is also essential for good decision-making and business success.

Investors expect high-quality financial information and are now demanding the same for sustainability information. Reliable and connected financial and sustainability reporting and sustainability-related financial disclosures enable companies and investors to make economic decisions based on high-quality information. Increased confidence in sustainability information and its integration in mainstream reporting also helps companies avoid perceptions of greenwashing and regulatory or legal action.

Given the financial effects of climate change and the sustainability transition and the rapid move to mandatory sustainability reporting and assurance, boards and management must establish an integrated internal control environment for financial and sustainability reporting that is within an effective corporate governance and risk management framework underpinned by senior leadership commitment to sustainability and other objectives.

Business leaders, regulators, investors and others are turning to the accountancy profession to:

- Enhance and validate the systems and processes that can generate quality sustainability data.
- Ensure the integration and connectivity of sustainability and financial information to facilitate understanding of the financial effects of sustainability risks and opportunities and support the disclosure of sustainability-related financial information.

Through an integrated internal control environment based on an integrated mindset, companies will achieve greater connectivity of functions, processes and systems leading to enhanced data quality to improve decision making on strategy, risk, opportunity management and governance-related matters. This is the foundation for transitioning to a more sustainable business model and enhancing investor and stakeholder confidence in sustainability performance.

New Expectations with Mandatory Reporting

The quality of information expected on sustainability risks and opportunities and performance is increasing because of new standards and requirements for mandatory sustainability-related disclosures, including:

- The IFRS Sustainability Disclosure Standards which are a global baseline for investor-focused disclosures. Connected information, including connectivity between sustainability-related financial information and financial statements, is a key requirement
- Jurisdictional legislation and standards, including the European Union's Corporate Sustainability Reporting Directive (CSRD) and European Sustainability Reporting Standards (ESRS), and in the U.S., the proposed SEC climate change disclosure rules and recently enacted climate reporting laws in California. These jurisdictional requirements also require assurance of sustainability disclosures.

These new standards and legislation all require sustainability disclosures to be issued at the same time as the financial statements and for the same reporting period. Significant efforts will be needed by all companies in scope to ensure that their internal governance, processes and systems are up to the task. The EU's CSRD also requires companies to disclose how their risk management and internal control systems incorporate sustainability reporting processes.

How is Integrated Internal Control Achieved?

An integrated control environment involves the finance function, internal audit, external assurance supporting senior management and the board's need for high-quality information for decision-making, effective governance and oversight and external reporting. The *COSO Internal Control—Integrated Framework* (or equivalent) is already widely used by companies to improve confidence in information, processes and systems particularly related to internal control over financial reporting (ICFR).

ICFR processes and systems can be modified and applied to sustainability reporting to enhance comparability, consistency and reliability of information and to incorporate material financial and non-financial related sustainability information into the financial reporting cycle. This also benefits the independent external assurance practitioner in obtaining assurance on that information.

An integrated internal control environment establishes robust data collection, processes, and controls through:

- **Effective governance** to set "tone at the top" with a purposeful, organization-wide commitment to drive sustainability and a culture that applies the same level of rigor to the measurement and reporting of sustainability information as that applied to the financial reporting. Responsibilities for the oversight of sustainability and integrated reporting will increasingly be with audit committees who will have to coordinate with other relevant board committees (see *Key Questions for Audit Committees Overseeing Sustainability-Related Disclosure*).
- **Risk and materiality assessments** aligned to the strategy and business model to identify the data needed to meet business objectives and regulatory and stakeholder needs. A risk assessment also allows the allocation of resources within reporting and control processes to those areas that pose the highest risk of material misstatement.
- **Sustainability reporting policy and process development** to create methodologies to generate consistent data and standardized and controlled processes based on sustainability accounting policies, chart of accounts/ledger, disclosure controls and procedures for material sustainability metrics and disclosures. This is particularly important for consolidation and group reporting and defining KPIs for integrated dashboards.
- **Robust data management and reporting systems** to ensure data accuracy, consistency, reliability, timeliness, and integrity. Sustainability data is ideally incorporated into existing financial or enterprise resource planning systems where process capability already exists, such as automated data feeds and controls from invoices, employee payroll and delivery documentation, or through direct measurement and real-time data collection.
- **Continuous improvement framework** to regularly review and improve sustainability data and reporting processes.

This guide expands on *Building Trust in Sustainability Reporting, The Urgent Need for Integrated Internal Control* which highlights why an integrated internal control environment is essential to enhancing the quality of sustainability information and achieving the integration and connectivity of sustainability and financial information to improve the understanding of the financial effects of sustainability risks and opportunities.

Governance and Controls for Sustainability Information

EXTERNAL SUSTAINABILITY REPORTING REQUIREMENTS

The IFRS Sustainability Disclosure Standards issued by the International Sustainability Standards Board (ISSB) as well as the European Sustainability Reporting Standards (ESRS) and other jurisdictional requirements for sustainability disclosures include specific requirements in relation to transparency of the governance, risk and internal control environment.

ESRS 2: General Disclosures, Disclosure Requirement GOV-5, *Risk management and internal controls over sustainability reporting*, requires a company to disclose the main features of its risk management and internal control system in relation to the sustainability reporting process.

IFRS S1, *General Requirements for Disclosure of Sustainability-related Financial Information*, requires disclosures to enable primary users to understand the governance processes, controls and procedures used to monitor and manage the organization's sustainability-related risks and opportunities. IFRS S2, Climate-related Disclosures requires disclosure of the governance processes, controls and procedures an entity uses to monitor and manage climate-related risks and opportunities.

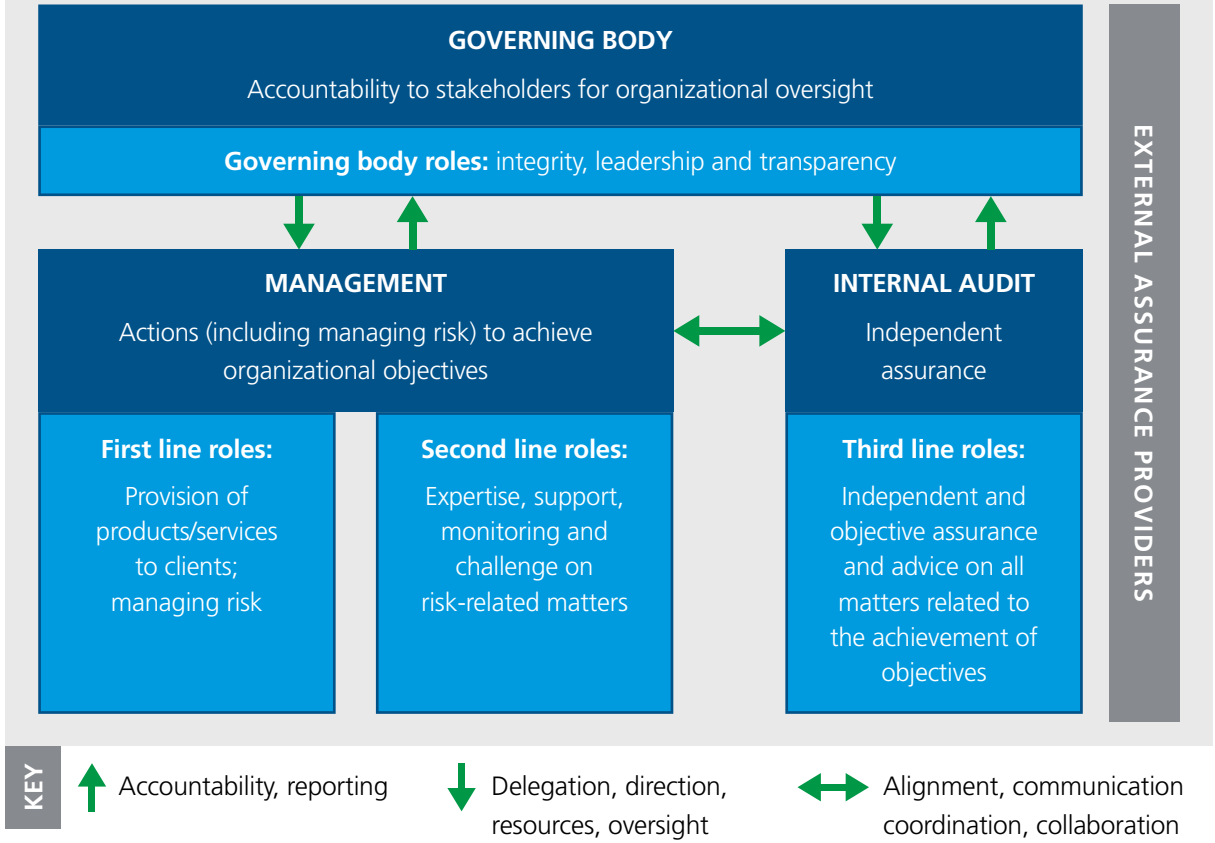
Organizing the Governance and Control Environment

Many companies use the Institute of Internal Auditors' Three Lines Model (also referred to as the Three Lines of Defense) to clarify roles for all governance and internal assurance activities, including those relating to enhancing the quality of sustainability information.

The model helps ensure robust governance structures, clear allocation, and segregation of internal control roles and responsibilities. Where a three lines approach is not implemented effectively, multiple uncoordinated risk and control activities will create inefficiency and potentially lead to inconsistent and unreliable reporting.

Once the structures, policies, and processes are established, these need to be effectively communicated throughout the organization via various channels, as well as in relevant external disclosures to investors and other stakeholders.

THE IIA'S THREE LINES MODEL



THE GOVERNING BODY

The governing body, (typically a board of directors including the Supervisory Board in a two-tier governance arrangement) is accountable for governance, risk management, and internal control including sustainability reporting and assurance. As part of this role, the board can assess the maturity of the company's preparedness in the context of its own needs and investor and other stakeholder expectations. This involves ensuring management has implemented robust processes and systems related to the delivery of business and sustainability objectives and the sustainability reporting process including the collection of data and preparation and presentation of sustainability information. This approach helps ensure that sustainability disclosures are aligned with the organization's priorities and internal key performance indicators.

Organizing the Governance and Control Environment

Boards typically delegate oversight responsibilities to a specific committee with the appropriate expertise. Given its experience in statutory financial reporting, the audit committee is increasingly delegated responsibilities to oversee the sustainability reporting process or work jointly with another board committee in this regard.

IFAC, AICPA&CIMA (2024), *State of Play of Sustainability Disclosure and Assurance, 2019-2022* shows that only 56% of companies covered in the research disclosed board-level oversight of sustainability reporting (41% delegated to the audit committee), and 22% board level oversight of sustainability assurance (79% delegated to the audit committee).

Key Questions for Audit Committees Overseeing Sustainability-Related Disclosure

To support audit committees in expanding their existing financial reporting oversight responsibilities to sustainability-related disclosure, this IFAC resource highlights key questions for audit committees to guide them in overseeing sustainability-related disclosure and assurance.

THE FIRST LINE

The first line owns and manages risks and performs internal controls. It includes employees from many different teams including line functions such as research and development, production, procurement, human resources, and sustainability, and executive and management teams. Where the finance team is the process owner for sustainability-related disclosures, some finance team members will also be internal controls performers and hence part of the first line, as they are for financial reporting.

In these first-line roles, the finance function must work cross-functionally and collaboratively with key functions and relevant business units to increase the maturity of systems and processes through:

- Transactional systems for accounting and collection of sustainability data
- Disclosure systems and reporting processes and analytics
- IT architecture and automation of processes and controls, and
- Interpreting rules and standards, and ensuring reporting is in accordance with sustainability reporting standards and requirements.

THE SECOND LINE

The second line includes specialist group functions responsible for risk and compliance which oversee the risk assessment and monitor the risk management and internal controls processes. These functions provide expertise, expert challenge, and oversight and monitoring over sustainability disclosure processes and may support design, implementation, policies, enforcement, and testing the readiness of information for reporting. Importantly, they provide advice to the first line on the design and performance of the controls and gather evidence and management attestation which underpin disclosure of the basis of preparation and presentation to the board or the audit committee. In smaller organizations where a separate function does not exist, the CFO/financial controller and finance team may need to also perform a monitoring and oversight role.

Specifically, the second line

- Approves both the local risk assessment and the design of local controls to ensure control objectives are met,
- Assesses the corporate group's overall risk profile in the context of local risk assessments, and recommends mandatory control objectives to reduce risk, and
- Consolidates the control environment for the various first line processes and activities to enable reporting about the status of the control environment to the audit committee, and in the annual report, if required. Some first line functions only need to perform controls for some control objectives given their local risk assessment.

Organizing the Governance and Control Environment

THE THIRD LINE

The third line is the internal audit function (where it exists). Internal audit operates independently of the first two lines, and its main roles are to ensure that the first two lines are operating effectively and to advise on improvements. The board and management can use the internal audit function to provide objective assurance on processes and controls by reviewing and assessing management attestations and supporting the external assurance process by sharing documentation. Where an internal audit function does not exist either internally or outsourced, the finance function could to some extent operate as the third line. However, the finance function cannot reliably monitor the controls it has designed and/or performed, as it lacks independence of operational management.

A top-down versus bottom-up approach

A company can develop and design controls for sustainability information top-down or bottom-up, or a mixture of both.

- A top-down method is likely most appropriate for when the entire company's business model is primarily based on a single product with a common risk profile, as well as a common system infrastructure. This can make implementation and monitoring easier and faster although there is a risk that those who perform the controls locally may not think the controls are relevant or well-designed. Local errors may not be addressed, which could increase the risk of misstatement.
- A bottom-up method is likely most appropriate for a business model based on many products and segments with a multi-pronged system infrastructure. Typically, the company has different risk profiles across the various first line functions, with each function typically designing its own controls. Although it could take longer to design and implement and may be more difficult to monitor, controls can be owned locally, leading to better buy-in and local expertise.

Applying Financial Reporting Practices

Extending internal controls over financial reporting (ICFR) processes to processes and systems for collecting sustainability data and for sustainability reporting and disclosures increases information reliability and reduces the overall cost of implementing reporting standards and requirements.

This involves implementing automated processes supported by systems and relevant controls including leveraging existing enterprise resource planning and management and reporting systems that provide data governance, controls, and audit traceability. This also benefits the independent external assurance practitioner when obtaining assurance on sustainability disclosures.

EXTENDING ICFR PROCESSES TO SUSTAINABILITY DATA

Increases sustainability information quality at the same time as reducing the overall cost of compliance

Enables the validation of the non-financial data and processes through alignment with financial information and reporting processes

Makes it easier to incorporate material and connected financial and non-financial related sustainability information into the financial reporting cycle

For material sustainability risks and opportunities and disclosures, a sustainability reporting compliance process should be incorporated into the ICFR process over time as sustainability reporting processes mature. The control environment for sustainability information needs to consider both validity and completeness, as well as reliability and quality of information sources, as is the case for financial reporting.

Annual Cycle of Governance and Control Activities

The key elements of an effective governance and internal control system for sustainability information can be captured in an annual cycle. Where a company has a well-functioning internal control environment for financial reporting (ICFR), developing internal controls for sustainability information can be an extension using the same principles. However, the approach to the materiality assessment and the risk assessment are distinctly different for the control environment for sustainability disclosures.

The annual cycle is an ongoing process, as with annual financial reporting. Greater effort is likely needed in the first year, but subsequent years can focus more on maintenance, review, and adjustments. The early stages typically require resources and investment to implement or review policies, processes, technology, and roles and responsibilities. Automated processes supported by policies, systems, and relevant controls around data accuracy, completeness, and reporting reduce the levels of manual intervention and the likelihood of errors.

A company can implement the steps in stages. A phased-in approach can involve delaying the development of Standard Operating Procedures (SOPs) or performing controls monitoring. A phased-in solution may reduce the maturity of the control environment, and the external assurance practitioner may need to undertake more substantive testing and procedures.

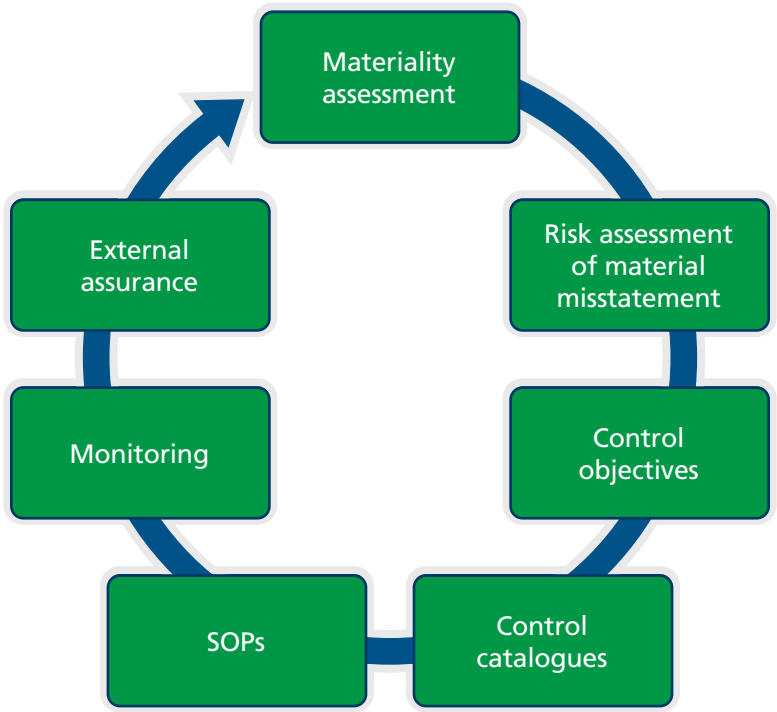


Figure 1: Annual cycle of control activities

The audit committee or relevant board committee should understand and approve the overall approach including the company's risk assessment and control framework in relation to sustainability information and reporting. Adequate information on the status of the control environment can be shared with the external assurance practitioner. The external assurance practitioner will communicate findings from their assurance engagement in a management letter, including any significant matters and deficiencies in internal control, which can inform improvements.

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MATERIALITY ASSESSMENT

The materiality assessment is a key requirement of most sustainability reporting standards and regulations and determines the basis for what companies report on, including the sustainability topics to address and prioritize. Importantly, it provides input into the development of the risk assessment and internal controls approach. The audit committee should approve the materiality assessment, review it annually, and communicate the outcomes of its work to the Board.

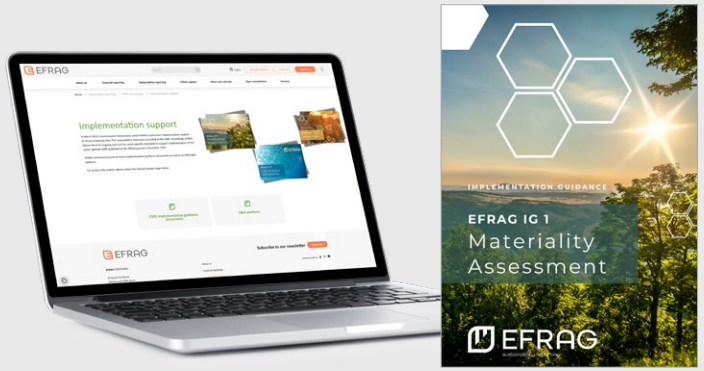
A MATERIALITY ASSESSMENT CAN BE BASED ON FINANCIAL AND IMPACT MATERIALITY

Companies make disclosures based on material sustainability topics and risks and opportunities. Material matters include those that affect financial position and performance, or the impact of a company's activities on the environment and society.

The IFRS Sustainability Disclosure Standards and proposed US SEC Climate Disclosure Rule are investor-focused materiality, which involves a company disclosing material sustainability-related information to enable primary users to assess the effect of sustainability risks and opportunities on the company's financial position, financial performance and cash flows over the short, medium, and long-term.

The GRI Sustainability Reporting Standards set out a process to identify and assess impacts on an ongoing basis and determine material topics for both financial and value creation reporting.

The EU CSRD and ESRSs, and China's proposed climate disclosure regulation, require "double materiality assessments", where both the financial materiality and the impact materiality on others are considered on equal terms in the materiality assessment. ESRSs specifically require a company to assess whether to disclose material impacts, risks and opportunities, and their financial effects (see EFRAG's Implementation Guidance 1 – Materiality Assessment).



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RISK ASSESSMENT OF MATERIAL MISSTATEMENT

The outcome of the materiality assessment determines which Disclosure Requirements (DRs) to report on and provides the basis for the risk assessment for the reporting process and the scope of the control environment and underlying data, technology, and process requirements.

Given the diversity in sustainability topics and complexity of the data collection and reporting process across many DRs particularly for larger companies, it is important to prioritize effort and investment in the most material and high-risk DRs, including those that are most likely to be reported incorrectly.

A focus on material DRs is critical to targeting resources to enhance governance and controls and to ensure reporting on the organization's sustainability priorities. Under the CSRD, for example, EU requirements and standards identify more than one thousand data points, including qualitative DRs. However, not all these requirements and data points will be deemed material to report but are subject to the materiality assessment.

Consequently, a pragmatic approach to the risk assessment is to assess the relative importance of each DR, and then to assess the likelihood of the material misstatement of each material DR. This approach helps to prioritize DRs, establish adequate sustainability reporting processes, systems and controls for material DRs, and focus discussion with the Audit Committee on material matters.

The Characteristics of Disclosure Requirements Vary

DRs can be both qualitative, such as the interaction of sustainability risks and opportunities with strategy and business model, business conduct policies, or descriptions of the internal control environment, or quantitative, such as greenhouse gas emissions, energy consumption, percentage of employees with disabilities, or fines for violation of anti-corruption laws. DRs can also be both current and anticipated.

A definition of each material DR should be established, for example in a sustainability/ESG data manual, which also defines roles, processes, and systems for collecting information for each DR, and how these are reported. Definitions could be included as an extension of a company's existing internal financial data manual. For example, to support GHG emissions reporting, a process and data manual will include definitions of data points, roles, KPIs, units, and related evidence (see the guidance on *Enhancing Greenhouse Gas Reporting*).

Common validity and completeness errors for sustainability information, particularly for metrics, are often caused by imprecise definitions in a data manual and/or adherence to these definitions at the group and local levels.

The risk assessment determines the extent of the controls, validation, subsequent monitoring, and what further investigation may be required. The assessment will also inform which DRs will be incorporated into the ICFR process in the context of the maturity of the underlying sustainability information to bring about an efficient internal use of resources.

It is necessary to understand data management and the process of collating the information, including how information is sourced, managed, and transformed into a reporting and analytics tool. Subsequently, it is possible to identify where the risks in that process are for material misstatement and apply relevant controls, improve data governance structures and systems, and understand residual risk.

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In the first year, a DR is evaluated based on the inherent qualitative risk of the DR inaccuracy, given the nature of the DR and its gross risk before applying internal controls. Key assessment factors include the extent of and ease of evidencing the data (e.g., GHG emissions scope 1 or employee information can be derived from current systems) or reliance on estimates (e.g., emissions or employees in the value chain or ocean spills) that may require documented and evidenced assumptions. There can be greater risks associated with estimates, including those used in developing a climate transition plan and those based on less precise definitions than primary data sources that provide actual data such as from external sources, like invoices. Additionally, information about the IT and system set-up for each DR can be included, given that a lack of a system may make it more likely the information will not be collected reliably or completely.

In subsequent years, more qualitative and quantitative information can enhance the risk assessment, making it more comprehensive. For instance, the internal and external assurance practitioner's management letters and the internal control status report from the previous year are useful in improving the risk assessment. These observations can reveal that some activities may be harder to perform and implement than they appear on paper, which is also the case in the financial reporting internal control system.

CONTROL OBJECTIVES

One of the most important outcomes of the risk assessment of the individual DRs is the identification of control objectives. The control objectives are derived based on the question:

WHAT CAN GO WRONG OR HAS GONE WRONG?

Clear control objectives direct the control design, and employees understand the purpose of the controls. To establish an efficient control environment, the control objectives for each DR should only be focused on areas that are likely to occur or lead to material misstatement. Areas where the impact of incorrect reporting is immaterial should be excluded.

Examples of what can go wrong include using incorrect conversion tables when calculating energy consumption, mixing up units, or inaccurate employee numbers. In relation to qualitative DRs, a lack of information about lobbying activities or violation of human rights in certain subsidiaries or the value chain can be problematic. Consistency issues across financial and non-financial reporting also need to be considered including the potential financial effects of a net-zero transition plan.

Clear control objectives also help to ensure the controls are not in reality activities. Controls and activities are sometimes confused, but controls result in evidence of a control being performed with a satisfactory outcome, and any errors prevented from occurring. Control objectives also guide what evidence of the control performance is needed as outlined in control catalogues or manuals.

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CONTROL CATALOGUES

Once the control objectives and the structure of the control environment have been clarified, a control catalogue can be established to identify the controls needed to mitigate risks across the first line.

As for financial reporting, a control catalogue will typically include:

- Control number and name
- Control objective
- Control activity
- Evidence that the control has been performed with a satisfactory outcome
- Control frequency (depending on how often information is collected)
- Control performer and control owner (not necessarily the same person)
- SOP reference (if the company works with Standard Operating Procedures)
- Quality of control – how well is the control designed (on a scale that can be consolidated)
- Control maturity – how effectively implemented is the control (on a scale that can be consolidated)

The demands for evidence to support financial information can be replicated in sustainability information to various degrees. This requires understanding the value of evidence and documentation, and whether it will need to be corroborated further. Strong evidence is:

- From reliable external sources.
- Controlled effectively (within an established control framework).
- Direct and not inferred from other material or sources.
- Documented.
- Original or in a form in which the audit or assurance trail will show any changes.

If there are signs of weakness in the evidence, for instance, because measurement or calculation is manual, evidence strength can be increased by collecting additional supporting evidence from different methods or sources.

Much sustainability information is highly documentable and can be relatively easily evidenced – not least because it is often strongly linked to financial processes and

information. For instance, certain categories of GHG emissions Scopes 1 and 2 are linked to purchases of fuels and electricity. Such information can be supported with external documentation and can be of comparable quality to financial information. Context from the financials and production information can provide good starting points for testing completeness. Evidence (invoices, observations, measurements, calculations etc) for historical information is generally more accessible.

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Some elements of qualitative information are also documentable, such as a net-zero transition plan approved by the board, with associated policies and actions in place (proving adherence can be more challenging). Forward-looking disclosures can be supported by documenting the methods, assumptions, and information sources that form the basis of the disclosures on the same lines as evaluating evidence relating to accounting estimates.

Some sustainability information may be more difficult to substantiate and rely on estimates. For instance, depending on the company's relationship to those within its value chain, it can be challenging or even impossible to prove the completeness of most value chain information, as it can be difficult to obtain strong evidence of how much wastewater has been released into a waterway if there is no measurement or continuous monitoring, or prove the completeness of safety incidents. However, establishing corroborative evidence may be possible.

Controls undertaken less frequently (e.g., annually) can be more limited in their effectiveness. Where processes and controls are not monitored during the year, there is limited ability to deal with errors before reporting, and it is more difficult to provide evidence of the performance of the control to external assurance practitioners until much later in the reporting cycle. Semi-annual or quarterly information collections and controls (execution and documentation) lead to better evidence-building, and eventually, improved timeliness of reporting and an opportunity to remediate control deficiencies prior to year-end.

Control catalogues are often established and managed in defined Governance, Risk & Control systems, which are often incorporated in ERP systems. A spreadsheet or SharePoint database could be used as an initial solution, especially if the company and its processes are not complex although ICFR processes and systems should be leveraged where possible to reduce cost.

STANDARD OPERATING PROCEDURES (SOPS)

The Control catalogue is the basis for developing the SOPs, which are more detailed versions of control catalogues. SOPs describe each control in detail, perhaps with screenshots, so individuals in subsidiaries and local entities can perform the controls and capture the required evidence. If a company is taking a phased approach to enhancing the maturity of sustainability reporting processes, developing SOPs can be done over time.

If a corporate group has many different systems operating in its local entities, local SOPs can detail how the local entity has chosen to fulfill the control objectives. In this scenario, the second line evaluates all the local SOPs to ensure they meet the control objectives and identifies valid evidence with success criteria.

To prepare for external assurance, a detailed substantive review of evidence, including from local entities, will be required, and SOPs will most likely be needed. Data flow diagrams can support the control design approach.

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MONITORING PLAN

When the first line has performed the controls, the second line ensures the controls are performed as described, that the evidence exists, is adequately documented, and is valid. A monitoring plan is typically agreed by the audit committee and identifies which topics and legal entities (the parent and subsidiaries) and entities in the value chain are visited and monitored so that evidence for the controls can be validated.

Most companies do not have the resources or will choose not to monitor all controls every year in all subsidiaries particularly where there are many smaller subsidiaries or many suppliers. A monitoring rotation plan can be established to rotate entities for validation testing.

The external assurance practitioner should be kept informed of the monitoring plan to help coordinate activities and optimize resources. Internal audit also undertakes monitoring so it can provide an assessment of the internal control system maturity in both first and second lines. One of the most important inputs to this assessment will be the internal and external assurers' management letters.

The monitoring plan could also be represented in a diagram. On the X-axis each legal entity including the parent, the subsidiaries, and entities in the value chain is assessed on how material it is for the group's report. This assessment can be done per DR, or as a whole.

The Y-axis represents an estimate of how likely it is that the individual legal entity is not effectively performing the controls to a satisfactory level. This could be based on a range of factors including past experience of issues, local skills, IT limitations, and the likelihood of fraud.

The location of the parent, subsidiary or entity in the value chain and its maturity in implementing controls can also be considered as part of the materiality consideration (y-axis). For example, Transparency International's Corruption country list (2023 Corruption Perceptions Index - Explore… - Transparency.org), which shows the rating of the individual countries in relation to corruption can help with identifying subsidiaries and value chain entities that might be at most risk from an ineffective governance and control environment and hence increasing the risk of material misstatement.

If the company is taking a phased, multiyear approach to enhancing its internal controls, monitoring can be delayed until there is a process to monitor.

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Monitoring is essential to establish whether the system of internal controls is operating effectively to support reliable reporting of sustainability information. It can also provide evidence of the internal control environment's maturity to the external assurance practitioner. If a reliable system of internal controls is in place and operating effectively this can reduce the risk of material misstatement and enable the external assurance practitioner to reduce the extent or change the nature of substantive procedures necessary to obtain sufficient appropriate evidence.

The gross and net (residual) risks should then be reported to the audit committee to assist it in evaluating the appropriateness of the monitoring plan compared with board's risk appetite.

Where access to information from entities in the value chain has not been forthcoming or timely, it may be necessary to disclose data gaps and proxy estimates.

INDEPENDENT EXTERNAL ASSURANCE

Independent external assurance provides confidence in the reliability of sustainability information reported and will be required in some jurisdictions. For example, the CSRD requires independent assurance over ESRS reporting in the European Union starting with limited assurance.

The level of assurance obtained in a limited assurance engagement is substantially lower than in a reasonable assurance engagement. Reasonable assurance amounts to essentially providing a level of assurance like a financial statement audit opinion where the auditor expresses an opinion on whether the financial statements are fairly presented. The main difference between these types of assurance engagements related to the nature and extent of procedures undertaken throughout the planning, risk assessment, response to assessed risks, and reporting on the engagement.

The nature of procedures performed, the extent of assurance engagement documentation, and the evidence an assurance practitioner seeks will generally be greater for reasonable assurance. A combination of limited and reasonable assurance may also be used for different disclosures and the assurance report will identify what has been subject to assurance.

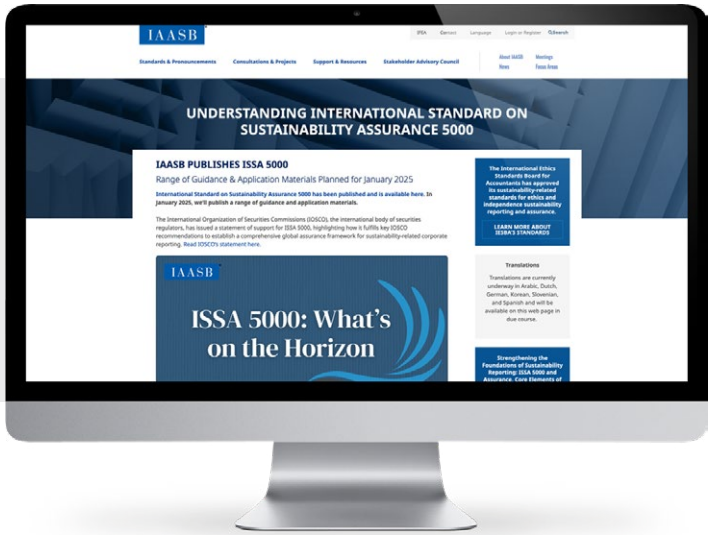
The assurance engagement involves evaluating information, systems, and controls, gathering evidence, and performing procedures to meet the objectives of the assurance engagement.

The assurance practitioner obtains knowledge about the company including its system of internal control for the preparation of sustainability information. This informs the practitioner of their ability to obtain sufficient appropriate evidence, including the reliability of the information to be used as evidence.

The weaker and more ineffective a company's governance and internal control environment, the more likely its assurance reports will include modifications. This is more likely to be the case in the early years of new sustainability reporting requirements as sustainability reporting and assurance practices evolve and reflect differences with the maturity of the financial reporting process. A key difference in sustainability assurance is that reporting requirements, such as under IFRS Sustainability Disclosure Standards and ESRSs, incorporate requirements on the governance and internal control arrangements for sustainability reporting. Assurance practitioners will need to test those arrangements to conclude on the related disclosures included in the sustainability information reported. *Sustainability Assurance: What to Expect* describes the types of modified assurance conclusions and levels of assurance.

Boards need to ensure a rigorous process for selecting an independent assurance practitioner based on their independence, assurance, subject matter competence, and compliance with ethical and quality management requirements.

IAASB International Auditing and Assurance Standards Board



A NEW GLOBAL STANDARD FOR SUSTAINABILITY ASSURANCE

The International Auditing and Assurance Standards Board (IAASB) has developed the International Standard on Sustainability Assurance (ISSA 5000) for both reasonable and limited assurance engagements on sustainability information, covering the entirety of an assurance engagement from acceptance to reporting. Together with global ethics standards, it provides a global baseline for consistency in high-quality assurance engagements.

ISSA 5000 sets the essential requirements for assurance practitioners to apply in accepting, conducting and reporting on assurance engagements on sustainability information, along with authoritative guidance on applying the requirements, including in testing, analyzing, and evaluating new sustainability-related datasets, processes, and controls.

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IFAC and its members work together to shape the future of the profession through learning, innovation, a collective voice, and commitment to the public interest.

About WMBC

We Mean Business Coalition works with the world's most influential businesses to take action on climate change. The Coalition is a group of seven nonprofit organizations: BSR, CDP, Ceres, Climate Group, CLG Europe, The B Team and WBCSD. Together, we catalyze business and policy action to halve emissions by 2030 and accelerate an inclusive transition to a net-zero economy. Find out more at wemeanbusinesscoalition.org

About GAA

The Global Accounting Alliance comprises 10 of the world's leading accounting institutes, working together to promote quality services, share information and collaborate on important international issues, especially with IFAC.

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