Hey! What's New? 2024-130

Actions for CFOs to Stay Ahead on ESG

Issues related to environmental, social, and governance (ESG) factors have long been on CFOs' agendas, but a number of developments in the past year have moved them to the forefront, says an article by Anita Dennis in a recent issue of *FM Financial Management* magazine. "Jurisdictional policies, supported by several new or proposed requirements on ESG reporting and disclosure are driving this acceleration, creating a range of considerations for CFOs as they determine how best to address this multifaceted and important area." Denis then offers some tips that finance leaders can follow to help lead change.

Dennis points out that, although some ESG requirements may apply only within specific jurisdictions or industries, some will have a global impact." The EU's Corporate Sustainability Reporting Directive and two new climate change-related laws from the US state of California apply to companies doing business within their jurisdictions.

She believes that the initial standards of the IFRS Foundation's International Sustainability Standards Board (ISSB) will, however, have a more global reach. The US Securities and Exchange Commission's climate-change rules would also have a significant effect for listed companies in the US. As a result, no matter where a company is based, if it has international interests, it may need to report on ESG from as early as the financial year that began January 1, 2024.

Whether or not they are immediately affected by the standards, Dennis urges CFOs to be familiar with sustainability-related risks, opportunities and impacts that have a material financial impact on their organization and where their organization has a material environmental and social impact through their operations, value chain, products or services. "Even those that are not subject to the standards will be affected as organizations reach down their supply chain for information on their business partners' practices."

Failure to understand and comply with applicable mandatory standards could carry significant penalties, noted Rex Gu, FCMA, CGMA, Europe head of finance, Logistics, at Copenhagen-based A.P. Moller - Maersk. "In this sector, adherence to evolving ESG regulations, such as emissions standards for maritime transport, is critical," he said, adding, "CFOs must ensure compliance and enhance the transparency and quality of ESG reporting."

Investors will expect the quality of sustainability-related financial data to be on par with that of financial data, said Jeremy Osborn, FCMA, CGMA, CPA (Australia), D.Phil., global head of sustainability at AICPA & CIMA. When new ESG standards call for independent assurance, CFOs signing off on sustainability-related financial data will be responsible for its accuracy and completeness.

In addition, CFOs, who are used to internal controls over financial reporting, will now have to focus on internal controls over sustainability reporting and the sustainability-related financial data involved, according to Ash Noah, CPA, FCMA, CGMA, vice-president and managing director–Learning, Education, and Development at AICPA & CIMA. "Any report on ESG should be based on data and backed up by evidence and [be] defensible," he said. That may require adding ESG reporting expertise to the finance team and exercising close oversight if drawing on sustainability expertise from external consultants. “Be sure you treat sustainability reporting with the same level of rigor as financial reporting,” he said.

Currently, sustainability information may be managed mainly by the sustainability team, noted Osborn, but he anticipates that the team will collaborate more with finance. And while finance may or may not have ultimate responsibility for collecting the data, it can play an important role in improving ESG data quality, he said.

Given the increasing frequency and pace of market change, CFOs should be aware that the ESG ecosystem is developing faster than regulators can react. Companies will need to proactively address and clearly communicate how sustainability-related risks, opportunities and impacts affect a company’s performance and prospects, cost of capital and access to capital.

For many companies, failure to properly address ESG requirements and stakeholder expectations could be an existential issue, Noah said. “Anything, whether an opportunity or risk, that has a material impact on future cash flows must be on the CFO agenda.”

With so many new considerations and requirements, it can be hard for CFOs to know where to begin their efforts. According to Dennis, “organizations should begin by determining what changes are immediately necessary. That might mean anything from simple compliance with a narrow segment of standards to changing the company’s business model. CFOs can then take a leadership role in providing the information and insights needed to address each company’s unique ESG risks and opportunities.”

For more, check out 4 actions for CFOs to stay ahead on ESG.