What CFOs need to know about ESG

Insights from financial services leaders

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Traditional banking companies are still in the early stages of addressing environmental, social, and governance (ESG) related issues, including the reporting and disclosure of related performance. In fact, many financial companies are taking a slow, incremental approach and are looking for practical ways to infuse ESG thinking into their overall risk management programs—specifically focusing on evaluating their customer base, vendors, and third parties around ESG risk.

One reason for the slow, incremental approach is because regulators are just beginning to determine how companies should measure and report their ESG effort. In the meantime, proliferation of ESG-related disclosure standards, frameworks, ratings, and rankings muddies the waters when it comes to measurement and reporting options.

All of this means it's a complex landscape when it comes to ESG for financial services companies. They must look at their own ESG performance, evaluate ESG risks, and perhaps even create ESG-related products.

KPMG LLP and Workiva are collaborating in the marketplace and have engaged in wide-ranging discussions with executives from leading financial institutions about how their organizations are addressing ESG in light of stakeholder, investor, and government expectations. The discussions touch on:

— **Disclosure and reporting**—What will emerge as the standard ESG disclosure document, standard, and/or framework?

— **Data collection**—Challenges organizations are facing in collecting ESG-related data.

— **Where should ESG reside?**—Exploring which function should be in charge of ESG efforts.

While progress has been made toward a more formalized ESG reporting framework for financial services companies, their process will continue to evolve over the coming months and years, as regulators and industry leaders move forward to develop and refine their approach to disclosure and reporting.

Disclosure and reporting

Given the increasing activity among regulators, it is clear that financial services companies will soon have to begin accounting for their ESG efforts and disclose those results to the rule-making agencies, investors, and the public.

Currently, companies have several options around ESG risk documentation. However, the Task Force on Climate-related Financial Disclosures (TCFD) framework is increasingly becoming the preferred option. For instance, the Federal Insurance Office has requested information around what data elements can be gathered relative to ESG. They've highlighted TCFD as a good place to start when evaluating data capabilities and data availability. Standards published by the Sustainability Accounting Standards Board (SASB) are also considered a good set of guidelines to begin evaluating what information should be included in disclosure documents.

Organizations can also refer to the SEC's Asset Management Advisory Committee, which has released a discussion draft on ESG disclosure[1].

Although disclosure requirements are still being developed and remain fluid, financial services companies may want to consider releasing some kind of disclosure, albeit even at a high level. One reason: shareholder interest. To be sure, not all shareholders are at the same point around ESG as a part of their investment strategy—it being a bigger concern for

[1] U.S. Securities and Exchange Commission, Asset Management Advisory Committee, *Recommendations for ESG*, July 2021

some than others. Nevertheless, companies are feeling the need to produce some form of ESG documentation that they can place in front of investors if they need to.

This approach, however, can raise the risk of litigation or pushback from investors if the disclosures can be shown to be inaccurate. Companies will have to balance the risk of early disclosures versus ensuring the accuracy of data, which can still be a challenge.

Data collection

One of the biggest challenges financial services organizations face when it comes to ESG is the gathering, analyzing, and governing of the data necessary for reporting.

Often this data comes from a variety of sources across the organization and in different formats. What's more, sometimes the data collection is done manually, which is time consuming and prone to errors. And other times, the process lacks a management framework, which ultimately leads to a lack of confidence in the accuracy of the data. Consequently, data governance remains a concern when it comes to ESG disclosures. The structure and rigor that would be expected in an SEC filing, for example, isn't there yet.

In response, organizations are trying to think about what they need to do to organize ESG data in a more governed way and leverage existing frameworks and methodologies that can be used for ESG reporting. For example, there has been some interest in organizing data dictionaries for the ESG data required for external- and internal-reporting purposes. And internal audit teams are raising the issue of controls as they begin reviewing ESG disclosures.

In addition, technology solutions are one way to bring the unstructured and structured data together, similar to other reporting, by organizing it and providing it to a risk management system as an output. Some suggest that enterprise resource planning (ERP) software be developed for ESG, bringing in all data sources into one place and allowing for control and auditability.

> **"It's a complex landscape for financial-services companies, when you consider that it's not just the company's own ESG performance, but how the company evaluates ESG risk or creates ESG-related products."**
>
> — **Mark Mellen**
> Director ESG Enablement, Workiva Inc.

Where should ESG reside?

It's fairly certain that all companies will eventually have to account for the ESG programs and results and publicly report their progress. But where within the organization should the main responsibilities for ESG reside?

Right now, there doesn't seem to be a consensus of where ESG reporting should sit. Risk, finance, even human resources are where some companies have put ESG ownership. However, there is a growing expectation the ownership of ESG reporting will eventually move to more functions that traditionally handle other types of regulatory and investment reporting—specifically risk and the controllership. This shift will likely accelerate as the SEC and other regulators begin to focus more on ESG reports and formalize ESG reporting requirements.

Some companies are coalescing their ESG reporting efforts under an existing committee so there is cross-functional representation. The reason is that each of those functions has a role, whether they are bringing data, processes, or controls to the table, based on what they've already implemented for other types of reporting scenarios.

Similarly, some companies prefer all data to be owned across the organization because it allows for different subject matter specialists to work on and develop that data. In this case, there may be an overarching group that collects and warehouses the data. However, it is advantageous to have one source of truth that allows all parties to share data. Data ownership may still reside with those subject matter experts but having all of that data in one platform to enable more efficient and timely decision-making will become more and more important to many companies.

> **"We are definitely seeing more involvement from the controllership function than we have in the past, especially when it comes to governing the data that's being disclosed."**
>
> — **Bryce Wagner**
> Managing Director, KPMG Financial Services Solutions

Key takeaways

Disclosure and reporting—Even without firm disclosure guidelines, some financial services companies may want to begin disclosing ESG information to demonstrate the organization's commitment to the process. Companies should consider using the TCFD or SASB frameworks for their disclosures.

Data collection—Financial services companies remain concerned about ESG data governance. One option is to use the organization's existing frameworks and methodologies that can be adapted for ESG reporting.

Where should ESG reside?—Currently, there's no consensus about where ESG should sit within an organization, with some companies putting the function within risk or finance—even HR. Eventually, ESG will move to the function that handles other types of regulatory and investor reporting.

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