



PEMPAL Internal Audit Community of Practice (IACOP)

*Audit in Practice (AiP) and Central Harmonization Unit Challenges (CHU)
Working Groups meeting in Budva (Montenegro) from 3 to 5 June 2025*

***“What IA can contribute to ESG and
link to the
UN principles on sustainability”***

DR. MANFRED KRAFF

5 JUNE 2025 (VIA VIDEO)



Agenda



1. What is ESG ?
2. What is the link to UN principles on sustainability ?
3. What is the link to EU policies (e.g. the Green Deal) ?
4. What can IA contribute to ESG ?

1. What is ESG ?

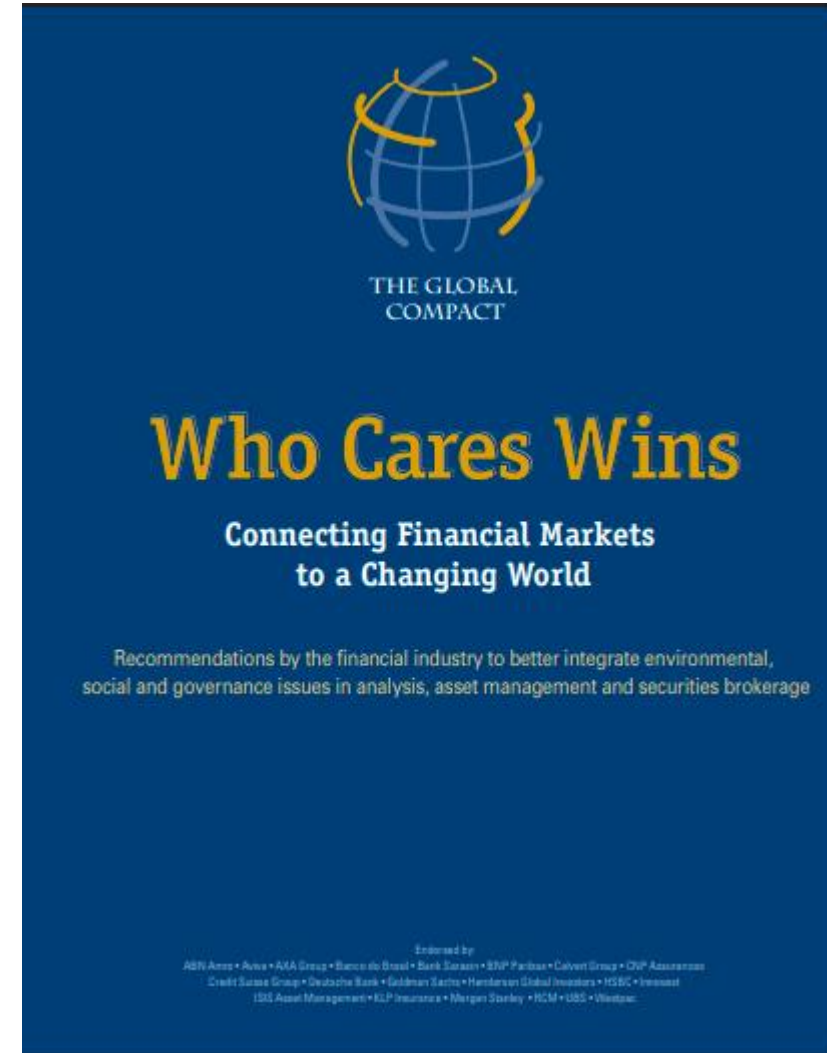
- **Investment decisions** are based on:
 - Predominantly - the potential for financial returns for a given level of risk
 - Occasionally - many other criteria
- **ESG is shorthand for an investing principle** that prioritizes:
 - Environmental issues,
 - Social issues, and
 - Corporate Governance
- **Investing with ESG considerations** is often referred to as:
 - Sustainable, responsible or ethical investing, or
 - Impact investing (in more proactive cases)



1. What is ESG?

Important milestones:

- **2004:** The term ESG first came to prominence in a report titled *"Who Cares Wins"* (joint initiative of financial institutions at the invitation of the UN)
- **2023:** The ESG movement grew from a UN corporate social responsibility initiative into a global phenomenon (representing more than US\$30 trillion in assets under management)
- **2030:** Global ESG assets are on track to surpass US\$40 trillion (about 25% of projected US\$140 trillion assets, despite challenging environment)

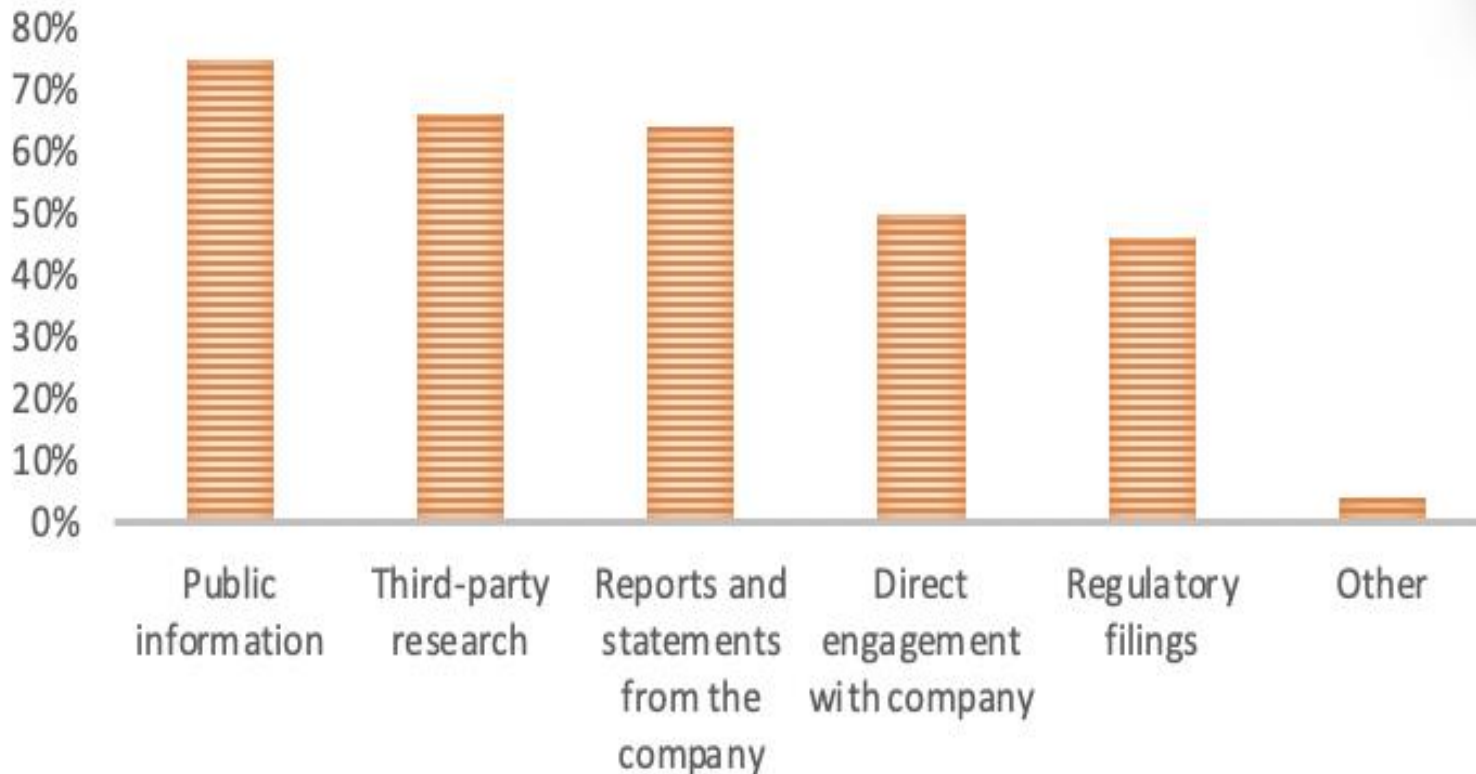


1. What is ESG?



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INVESTORS RELY ON ESG DATA FROM



Despite regulatory advances (2,400 ESG regulations worldwide), **major challenges** still exist:

- Absence of clear global standards creates variability in ESG reporting
- ESG reports are not always aligned with financial statements
- Heterogeneity in ESG-reporting makes it difficult to compare performance of different entities

2. What is the link to UN principles on sustainability?

Adoption of the "2030 Agenda for Sustainable Development" by all UN members in 2015:

- Creation of 17 Sustainable Development Goals (SDGs)
- Aim of SDGs is peace and prosperity for people and the planet – while tackling climate change/preserving oceans and forests
- SDGs highlight the connections between the environmental, social and economic aspects of sustainable development



2. What is the link to UN principles on sustainability?

- ESG and SDGs are interconnected and aim for a sustainable future
- ESG focuses on sustainable and responsible corporate practices
- SDGs outline targets for social/economic/environmental progress worldwide

➔ By aligning their objectives with ESG and SDGs, states and organisations can contribute to both:

- sustainable business practices and
- a more sustainable world



2. What is the link to UN principles on sustainability?

ENVIRONMENT



SOCIAL



GOVERNANCE



3. What is the link to EU policies (e.g. the European Green Deal)?

The **EU has been at the forefront** of “sustainability reporting”:

- Introduction of comprehensive ESG legal acts and frameworks
- Companies concerned must understand and comply with the ESG regulations/directives
- Companies looking to stay ahead must be leaders in sustainability, setting the standard for corporate responsibility, and aligning with investor and consumer expectations

The **political situation changed substantially** after the election of the new European Parliament and the nomination of the new European Commission (end of 2024):

- 2024 was still a landmark year, in particular due to the “European Green Deal“, with a series of pivotal EU ESG reporting regulations/directives being adopted
- In 2025 initiatives were/are launched to cancel or modify substantially EU ESG reporting regulations/directives



3. What is the link to EU policies (e.g. the European Green Deal)?

Fundamental EU ESG reporting legal acts and frameworks:



ESG
INITIATIVE

- **Corporate Sustainability Reporting Directive (CSRD)** – Expands sustainability reporting requirements for EU and non-EU companies, enhancing the consistency and comparability of sustainability information
- **Corporate Sustainability Due Diligence Directive (CSDDD)** - Companies must identify, prevent, mitigate, and account for adverse sustainability impacts in their operations and value chains
- **Carbon Border Adjustment Mechanism (CBAM)** - Introduces a carbon price on certain imports to prevent carbon leakage and encourage cleaner industrial production
- **EU Taxonomy Regulation** - Establishes a classification system for environmentally sustainable economic activities, guiding investment towards more sustainable projects
- **Sustainable Finance Disclosure Regulation (SFDR)** - Mandates sustainability reporting for investment managers in the EU, aiming to increase transparency in how financial market participants integrate ESG risks into their investment decisions
- **'Fit for 55' Package** - A comprehensive plan to reduce EU greenhouse gas emissions by at least 55% by 2030, incorporating various legislative measures to support this goal

4. What can IA contribute to ESG?



WHITE PAPER

INTERNAL AUDIT'S ROLE IN ESG REPORTING

Independent assurance is critical to effective sustainability reporting

The Institute of Internal Auditors | Global

“...(ESG) issues, are quickly evolving — from activist investor groups and inquisitive regulators pushing for change to governing bodies and C-suite executives struggling to understand and embrace the concept.”

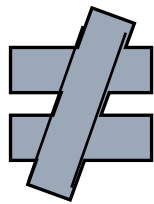
IIA Global published in May 2021 a White Paper that provides:

- An insight in the growing sustainability movement
- An overview of **risks related to ESG reporting**
- An outline of **internal audit's role in ESG reporting**
- An analysis how internal audit can support ESG objectives and add value

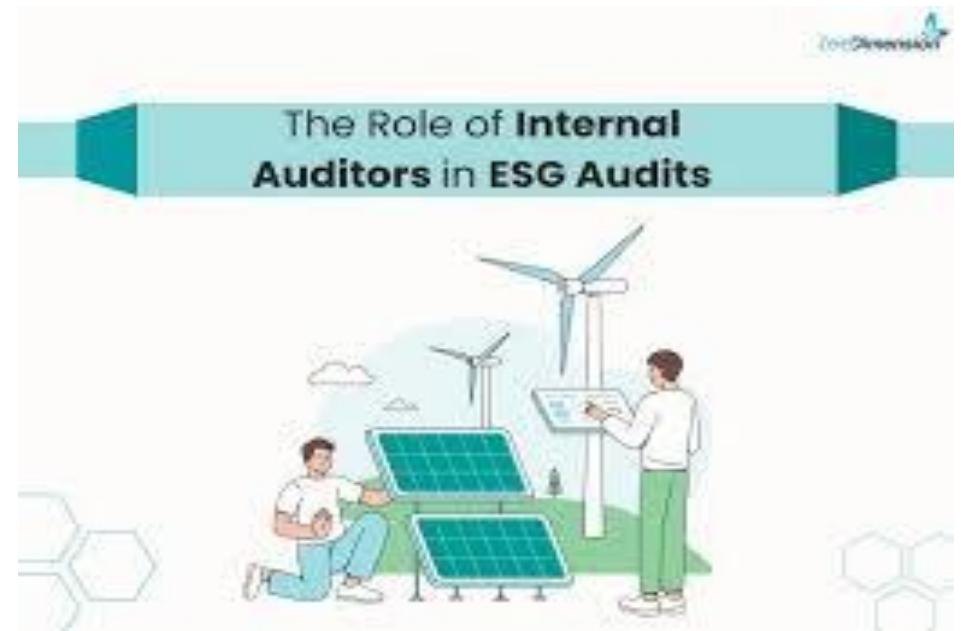
4. What can IA contribute to ESG?

Important new risk area

- Pressure for organizations to:
 - make public commitments to sustainability and
 - provide routine updates to ESG-related strategies, goals, and metrics (i.e. systems or standards of measurement)that are accurate and relevant



- ESG reporting is still immature:
 - No single standard for what should be reported
 - Not a lot of definitive guidance



4. What can IA contribute to ESG?

*“What is clear is that strong governance over ESG [...] requires alignment among the principal players as outlined in **The IIA Three Lines Model**.*

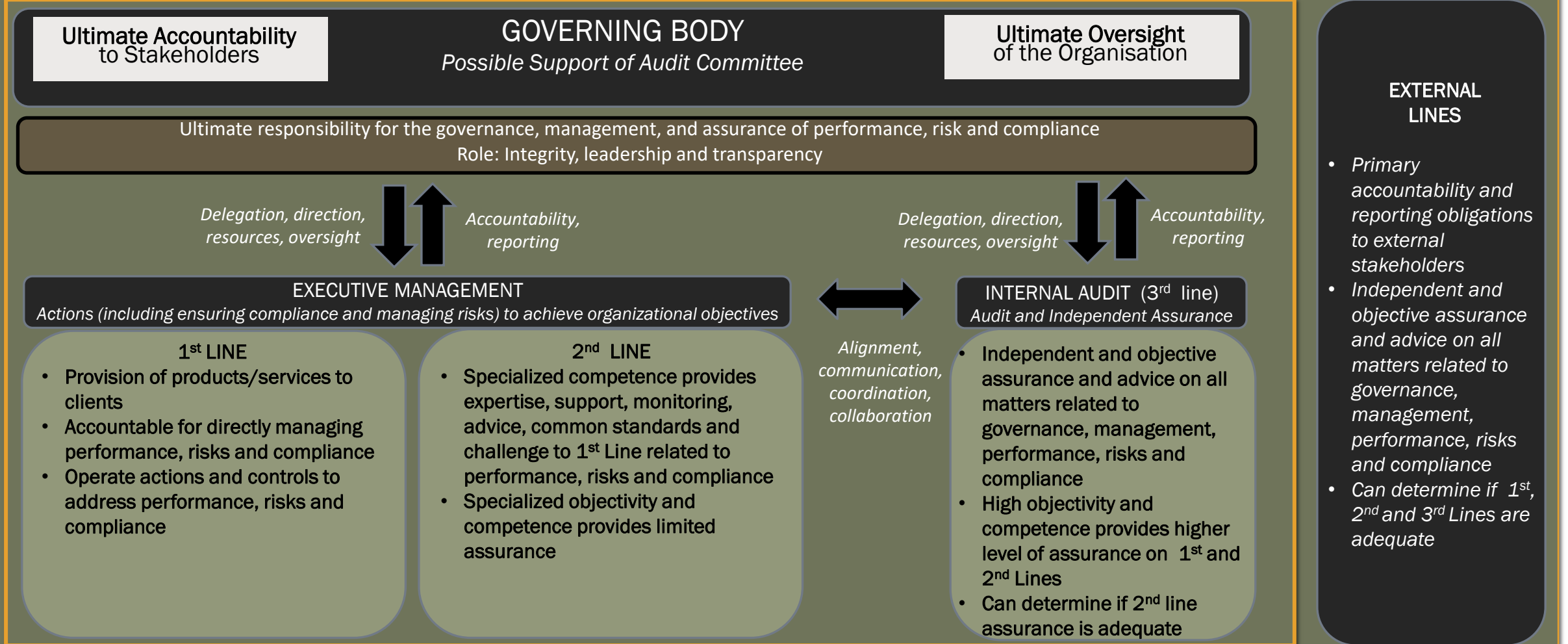
*As with any risk area, internal audit should be well-positioned to support the governing body and management with **objective assurance, insights, and advice on ESG matters.**”*

*“A **properly funded, qualified, and independent internal audit function** should provide assurance and advice over ESG strategy and ESG reporting.”*



4. What can IA contribute to ESG?

"Three Lines Model" of the Institute of Internal Auditors



4. What can IA contribute to ESG?

Assurance over ESG reporting is of particular importance and should include at minimum the following components:

- Review reporting metrics for relevancy, accuracy, timeliness, and consistency – main risk: “greenwashing”
- Review reporting for consistency with formal financial disclosures – main risk: Qualified or adverse opinion for the financial statements
- Conduct materiality or risk assessments on ESG reporting - main risk: difficulty to define “tolerable deviation(s)”
- Incorporate ESG into audit plans – main risk: expertise

Advisory services:

- Build an ESG control environment
 - Recommend reporting metrics
 - Advise on ESG governance
- } main risk: expertise



4. What can IA contribute to ESG?

“Internal audit is one of the few functions that can look at ESG reporting enterprise-wide to identify what is already working and recommend what still needs to be done.”

Anthony J Pugliese, President and CEO of IIA Global and Member of the International Integrated Reporting Council of the Value Reporting Foundation



4. What can IA contribute to ESG?

Knowledge Centers Environmental, Social, and Governance

Aiming to advance the professional practice of environmental, social, and governance (ESG) auditing through thought leadership, education, professional guidance, and advocacy.

Environmental, Social, and Governance Resources



ARTICLES

Basics: Governance and Audit Committees

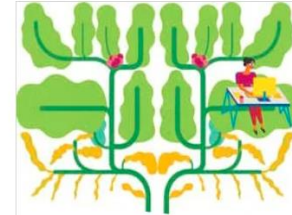
Audit committees enhance governance through best practices.



ARTICLES

Five Years Later

Applying pandemic lessons to tomorrow's crises.



ARTICLES

Risk: Defending Nature's Balance

A how-to for assessing nature-related risks.



ARTICLES

The Client's Side

Communication is key to auditor-client collaboration.



GLOBAL PERSPECTIVES AND INSIGHTS

Global Perspectives & Insights: Social/Human Capital/Culture

Internal Audit's Strategies for Navigating Change



Global Knowledge Brief

Social/Human Capital/Culture

GLOBAL KNOWLEDGE BRIEF

Social/Human Capital/Culture: Part 3: Tomorrow's Internal Auditors

Internal Audit's Strategies to Maintain Long-Term Effectiveness



ALL THINGS INTERNAL AUDIT

All Things Internal Audit: Unmasking Greenwashing

Edith Wong & Brian Wilmot discuss Greenwashing in Internal Auditing.



Global Knowledge Brief

Social/Human Capital/Culture

GLOBAL KNOWLEDGE BRIEF

Social/Human Capital/Culture: Part 2: A Culture Audit Roadmap

Internal Audit's Role in Culture Audit Effectiveness



GLOBAL PERSPECTIVES AND INSIGHTS

Global Perspectives & Insights: Sustainability

How internal audit approaches sustainability risk.



Thank you very much for your attention!

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Do you have questions or comments?

