ESG reporting – a strategic approach to success

Environmental issues, social issues and corporate governance are key to being future proof across many sectors. That means ESG isn't just a buzzword, rather a bona fide strategic topic. Especially as pressure from stakeholders and international regulators mounts. KPMG expert Corina Wipfler, Head of ESG Assurance Services for financial institutions, discusses its importance with journalist Peter Jankovsky. Corina's colleagues at the Zurich headquarters – Cyrill Kaufmann, Director of Corporate Audit and Head of ESG Assurance Services for corporate clients, and Roderik Olde Kalter, Head of the Enterprise Performance Management team – also comment on the need to adopt ESG guidelines and reporting technologies. The key takeaway? Companies must act now and embrace a smart approach towards ESG reporting requirements.

Fotos: Geertjan van Beusekom

FROM LEFT TO RIGHT

Roderik Olde Kalter
Director, Management Consulting, Head of Enterprise Performance Management

Corina Wipfler
Partner, Financial Services, Head of ESG Assurance Services for financial institutions

Cyrill Kaufmann
Director, Corporate Audit, Head of ESG Assurance Services for corporate clients

Peter Jankovsky ESG is on everyone's lips, but we're also witnessing a bit of ESG fatigue. What's your take on that?

Corina Wipfler Ignoring its importance simply isn't an option, especially since Switzerland has announced its ambition to achieve net-zero greenhouse gas emissions by 2050. This highlights yet again the need to incorporate ESG in your strategy. It's understandable that some people consider the package of regulations demanding and are getting rather tired of it. Preventing or overcoming this fatigue is essential, because it's not so much about compliance as it is about remaining profitable in the future. New markets and opportunities are opening up as we speak. It's good to see that a lot of companies are really taking it seriously, going beyond compliance. They're on the right track.

Cyrill Kaufmann What we're also seeing is that younger employees are thinking more about sustainability now than they did 10 years ago. And often in a way that goes beyond the basic requirements. I consider that a powerful driver for change.

We can't ignore the fact that regulatory pressure is increasing enormously. Which regulations are the most pressing for Swiss companies?

Corina Wipfler Under Swiss law, public interest companies must report on environmental matters, social issues, employee-related issues, human rights and combating corruption. There's also a disclosure about climate risk, which establishes a link to the internationally recognized recommendations of the TCFD, the Task Force on Climate-related Financial Disclosures. Additionally, the law requires companies to assess whether they need to report on child labor and perform conflict minerals due diligence. Further, the Swiss legislator just announced an expansion of non-financial reporting requirements.

Cyrill Kaufmann Added to that, of course, is the new European regulation, the Corporate Sustainable Reporting Directive, or CSRD for short – including the EU Taxonomy. Most companies now focus on this set of regulations as it is the most comprehensive. Other regulations can be relevant as well, depending on the size or the industry, such as the regulation on deforestation, the CBAM (Carbon Border Adjustment Mechanism) or the CSDDD (Corporate Sustainability Due Diligence Directive).

Corina Wipfler For financial institutions, FINMA is working on a circular regarding nature-related financial risks.

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Cyrill Kaufmann
Director, Corporate Audit, Head of ESG Assurance Services for corporate clients


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All in all, it sounds like a complex jungle.

Cyrill Kaufmann True. Companies should conduct a regulatory assessment to identify all ESG regulations that could affect them and create a plan for tackling them efficiently. And since this landscape is changing on an ongoing basis, they should update this assessment regularly.

The million-dollar question is: how to deal with this complexity?

Roderik Olde Kalter In my view, companies should opt for central coordination combined with local knowledge. If a firm is active in different countries, it essentially needs expertise in each jurisdiction related to the respective regulations.

Corina Wipfler A good starting point is to assess in which country the company is affected, to what extent and which regulations are in force there. Once you have an overview, you can work out your approach and the standardized interpretations necessary for your group.

Cyrill Kaufmann In addition, companies should opt for an efficient approach by connecting certain regulations and thinking about what comes next. Combining several steps at the same time rather than just taking care of them sequentially definitely pays off. We help our clients with that, based on the knowledge we've gathered from numerous experts monitoring legislation in the various countries.

In which sectors is ESG reporting most difficult?

Roderik Olde Kalter The consumer and manufacturing industries – which have complex supply chains – are the ones that face major challenges. But a bank, for example, can also invest in 200 different manufacturing companies and is required to disclose those stakes in its balance sheet. Things can get complicated there as well. On the other side of the spectrum, the professional services sector is likely to be less burdensome because the complexity of supply chains hardly plays any role there. While all industries will be affected by new regulations, some will face bigger challenges than others.

Let's talk about reporting work and the requirement to audit those reports. What is your main advice in this domain? And what's the story behind "limited assurance"?

Corina Wipfler When our clients are preparing a CSRD report, we're usually called in at a very early stage of the project as auditors. My advice to any company would be to get their auditor involved from the beginning, since timely feedback on milestones (double materiality assessment, draft report, etc.) is more helpful at the start than later in the assurance process. The ISAE 3000 standard provides for two different assurance options. One is "limited assurance" and the other is what we refer to as "reasonable assurance". The first one is less extensive and has less depth of focus. It concentrates on interviews, data analyses and limited samples. In a reasonable assurance engagement, auditors take a very close look at the processes. We test the effectiveness of controls and IT systems. But most companies aren't ready for reasonable assurance yet, just limited assurance.

«Fully integrated reporting will bring together financial data and non-financial information. This will create further opportunities for companies to implement AI solutions to increase efficiency.»

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Director of Corporate Audit and Head of ESG Assurance Services for corporate clients

Cyrill Kaufmann For now, the CSRD requires limited assurance, which will indirectly become mandatory for many Swiss groups reporting under the CSRD from fiscal year 2025 if they have subsidiaries in the EU. A requirement calling for reasonable assurance is expected in a few years. The Swiss government has announced that it also intends to introduce a requirement for limited assurance. That means that companies in Switzerland should start reviewing their data and processes immediately in order to be prepared and avoid unpleasant surprises. Most of them, international listed companies at least, are currently getting ready. Waiting isn't an option since the challenge is considerable. Essentially, the goal is to bring non-financial reporting up to the same level as financial reporting in the medium term.

Corina Wipfler One of the challenges we see is that companies haven't yet formalized sustainability reporting processes to identify risks in the process or put in place appropriate controls to ensure robust and reliable reporting. Another challenge is data availability and quality.

Many say that the majority of Swiss SMEs – the lion's share of the Swiss economy – are lagging far behind in terms of digitalization and ESG. How do you see it?

Roderik Olde Kalter It is understandable that Small and medium-sized enterprises (SMEs) do not always have the same budget available to invest in technology. The benefit for SMEs is that, in addition to the materiality thresholds, the various regulations are phased in, so that smaller organizations do not have to comply until later. This will allow them to benefit from what large companies have already done. For example, more mature software solutions will be available in a few years' time, while general familiarity with implementation methodologies will have improved. As a result, the cost of compliance will be lower than it is today.

Corina Wipfler The success of the Swiss economy is based, among other things, on its ability to innovate and its affinity with technology. Having said that, SMEs face a serious challenge because larger companies are also exerting pressure on SMEs in their role as suppliers. Time is of the essence: many Swiss companies that are not listed on the stock exchange must also comply with the EU's CSRD regulations by the 2025 financial year. My advice is that companies shouldn't only be focusing on finding their way through the jungle of ESG regulations – instead, they should be thinking first and foremost about the meaning and purpose of the whole exercise. In other words, they must seriously think about how to incorporate ESG into their strategy and that, in turn, can also help find new business opportunities.

One of the key issues is handling an overwhelming amount of data. Can you offer any good advice on this?

Roderik Olde Kalter The first step is knowing what needs to be reported where and by which deadline. Specifying the organizational implications is next: How should the processing of ESG data be anchored in the company? Who will be in charge? Will it be the head of the respective country? Or will it be done at group level? The third step is to clarify who will be accountable/responsible for collecting, consolidating and storing data as well as for finalizing the resulting ESG reports. After that, they can start thinking about automating ESG reporting. There are hundreds of tools available in this area, but existing solutions, such as those for financial reporting, are often well suited to collecting and consolidating ESG data. Moreover, the majority of the required functionality is often already present in existing systems. So, which combination of these existing tools is the smartest for automating ESG reporting? That's the most important question. When advising our clients, we discuss in detail what their specific ESG requirements are and which tool best supports which step of ESG reporting.

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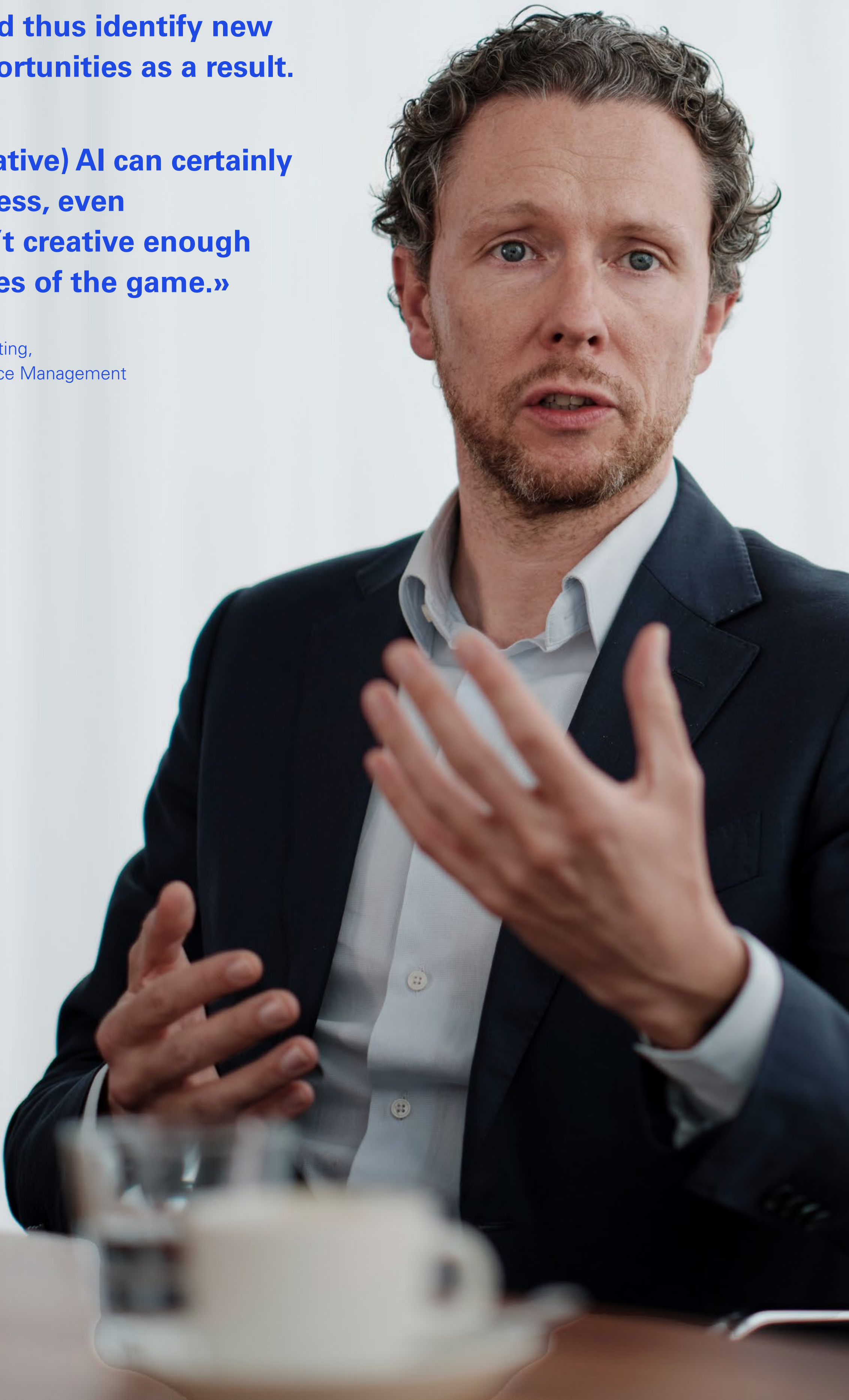

How many ESG reporting tools does a company usually need?

Roderik Olde Kalter The key steps in ESG reporting are data collection, harmonization, consolidation, calculation and reporting, all of which are governed by standard workflows with appropriate internal controls. In my experience, it takes a combination of three to four solutions. Just like it does for traditional financial reporting. You may also need an additional tool to enhance the visual presentation. This doesn't include specific tools designed to collect or calculate specific source data, like an add-on to calculate the amount of greenhouse gases emitted per country. Or in case of deforestation: how do you source and process satellite images as evidence? That's why it's so important to understand your company's needs up front and then decide on the right combination of tools.

When a company starts collecting data automatically, which ESG data sources should be first on the list?

Roderik Olde Kalter One of the first data sources to automatically interface will likely be greenhouse gas (GHG) emissions. For example, many existing systems already have built-in functionality that calculates GHG emissions and makes the data available for reporting purposes. While significant efficiency gains can and should be achieved by automating data generation for the many different ESG data sources, I don't believe it will be possible to achieve 100% automation. There will always be certain text, qualitative declarations or details that require manual work.

ESG sounds like a costly undertaking?

Roderik Olde Kalter Investing in the automation of ESG reporting puts pressure on margins. Many small and medium-sized companies don't necessarily have the resources to make these investments and we can't ignore that. At the same time, ESG also offers opportunities to generate new revenue streams, such as sustainable products and services, which typically have higher margins.

Cyrill Kaufmann Swiss companies urgently need to invest in technology and a specially trained workforce in order to comply with the EU's CSRD regulations. What we're hearing from our clients is that most of them expect that they'll need 25–30 percent more reporting capacity and that finding the right people is very challenging. Many companies rely on external consultants. We support companies in this regard: we can upskill their workforce by providing ESG reporting know-how through workshops and other training courses.

Looking at the future, what do you expect for ESG?

Cyrill Kaufmann We will move towards fully integrated reporting. Going forward, this will bring together financial data and non-financial information. This will create further opportunities for companies to implement AI solutions to increase efficiency. That will allow employees to focus on the why and how of ESG as well as on analyzing and planning ESG sustainability targets and achieving them.

You mentioned AI, a term that is en vogue these days. Can it help when providing ESG assurance?

Cyrill Kaufmann We can use AI to analyze the digital systems implemented on the client side in the world of financial auditing. When it comes to ESG, however, clients still collect a lot of their data using Excel spreadsheets and emails. That currently makes it difficult to apply AI consistently, automate tests and find anomalies. We do apply tools such as sentiment analysis of sustainability reports and media research. We also use analytics tools whenever we have to deal with large volumes of data such as information from external sources, greenhouse gas emissions or emission factors.

Roderik Olde Kalter AI will offer significant opportunities. For example, algorithms can expose promising product-market combinations and thus identify new ESG growth opportunities as a result. They can also be used to collect a wide range of online data that can be used as evidence for specific ESG KPIs. There are also benefits in the area of text and content generation, i.e. reducing the effort employees currently have to put into writing ESG reports and commentaries. But while (generative) AI can certainly support the process, even generative AI isn't creative enough to dictate the rules of the game.

Cyrill Kaufmann But it might just do precisely that tomorrow or the day after (laughs).