GLOBAL PERSPECTIVES & INSIGHTS

Sustainability

PART 1: Preparing for the Next Wave of Sustainability Regulations

PART 2: How the Focus on Sustainability Is Driving Data Governance

PART 3: Change Management Strategies for Successful Sustainability Governance

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Part 1:

Preparing for the Next Wave of Sustainability Regulations

About the Experts

Mandi McReynolds

Mandi McReynolds is an award-winning author with nearly two decades of experience leading ESG teams across four industries. As the vice president of global ESG and chief sustainability officer at Workiva, McReynolds helps executives around the world drive business value and societal impact through transparency, accountability, and innovation. McReynolds also co-hosts ESG Talk, a weekly podcast featuring candid conversations with business leaders exploring the intersection of sustainability, finance, and GRC.

Introduction

The future is here

When it comes to sustainability reporting regulations, change has arrived. New mandates from bodies that include the European Union and the U.S. Securities and Exchange Commission mean that sustainability reporting controls and compliance are now critical concerns for organizations.

This new regulatory regime promises to influence how organizations approach sustainability reporting and could well influence sustainability-related goals. In the meantime, the added level of public information available on sustainability efforts is expected to continue to drive asset management investment decisions.

This brief addresses how internal auditors can support their organizations in managing the new wave of regulation.

Understanding New Regulations

Disclosure Rules Expanding Globally

From voluntary to mandatory

Until recently, corporate sustainability reporting was typically voluntary, allowing organizations to choose which standards or elements of standards they wanted to follow and how or where they wanted to report on them. Yet with more than 500 formal and informal standards and frameworks available, organizations grappled to determine which guideline or combination of guidelines best suited their needs, while those who rely on financial statements struggled with a lack of comprehensiveness or comparability in reporting.

That will now change, at least to some extent, with the European Union and the United States adopting robust new disclosure regulations and the International Sustainability Standards Board providing baseline guidance that is expected to be adopted in numerous jurisdictions. The list of countries requiring some level of reporting on climate and sustainability efforts is expanding rapidly, including major economies such as Brazil, Canada, Japan, New Zealand, Singapore, and the United Kingdom. New guidelines that are expected to drive change include:

- The European Union's Corporate Sustainability Reporting Directive (CSRD) became effective for FY2024 reports published in 2025. It is made up of five environmental standards, four social standards and one that applies to governance, and it generally applies to larger companies, based on revenues, assets, or employees. The rules apply to some non-EU companies, and listed small and medium-sized companies can use simplified versions of the regulations.
- The U.S. Securities and Exchange Commission (SEC) recently finalized significant new reporting requirements for publicly traded companies on climate-related information that must be included in registration statements and annual reports, including:

Material climate-related risks, and activities to mitigate or adapt to such risks.

- Information about the registrant's board of directors' oversight of climate-related risks and management's role in managing material climate-related risks.
- Information on any climate-related targets or goals that are material to the registrant's business, results of operations, or financial condition.

What's more, the SEC rules require disclosures by some filers of Scope 1 and Scope 2 greenhouse gas (GHG) emissions. Scope 1 emissions are those directly controlled by the company. Scope 2 emissions are indirect emissions typically related to energy the organization has bought from another source. Companies are also required to issue attestation reports on the required disclosures. Compliance is phased in based on the SEC registrant's filing status and the content of the disclosure.

It should be noted that not all businesses are embracing the new regulations. Legal challenges to the new SEC regulations were filed in at least six U.S. Circuit Courts, with at least one succeeding in staying the new rules. In light of the various legal challenges, the SEC voluntarily issued its own stay pending judicial review.

New regulations are not limited to national jurisdictions and new sustainability reporting guidelines also are expected to influence how organizations approach sustainability reporting, and the quality of information stakeholders will see. Examples include:

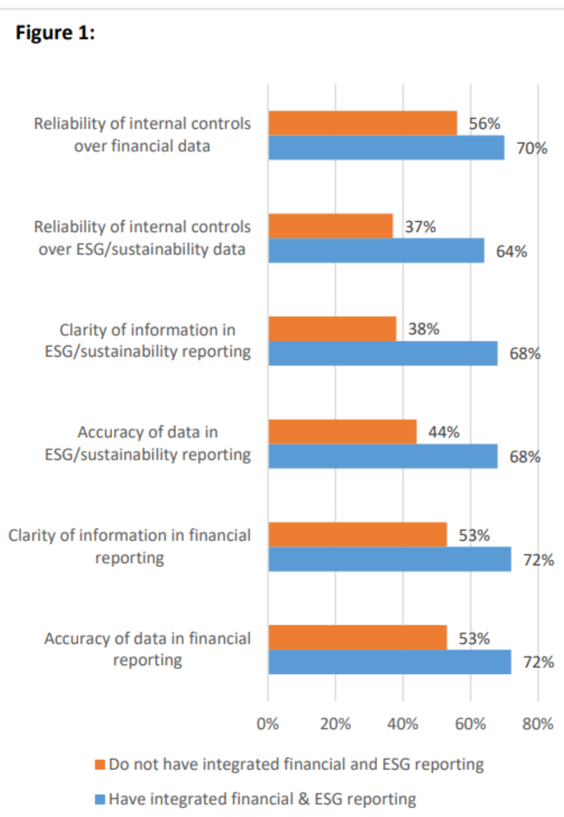
- A pair of new California laws — the Climate Corporate Data Accountability Act and the Climate-Related Financial Risk Act— are expected to have a broad impact because they apply to any large company that does business in the state, including private entities. In 2026, companies will have to begin reporting on Scope 1 and 2 emissions in the prior fiscal year. Starting in 2027, they will have to report Scope 3 emissions, which are those associated with their supply and value chains, for the previous year.
- Although they are not mandates, new guidelines from the International Sustainability Standards Board (ISSB) are expected to influence sustainability reporting worldwide, with nearly 400 organizations from 64 jurisdictions promoting their adoption. The ISSB's initial standards include IFRS S1, General Requirements for Disclosure of Sustainability-related Financial Information, and IFRS S2, Climate-related Disclosures. The ISSB was created by the IFRS Foundation to develop a comprehensive baseline of sustainability disclosures that meet the needs of investors and financial markets.

Getting the Right Start

Planning for Success

These new guidelines have clarified the field to some extent, but they have also added more complexity. According to Workiva's 2024 Executive Benchmark on Integrated Reporting, 74% of executives believed that complying with regulatory requirements will become significantly more challenging in the next year.[1] For example, one Workiva customer was preparing to address 35 different ESG regulations in the coming year, based on its jurisdiction and the locations where it does business, according to Mandi McReynolds, vice president of global ESG and chief sustainability officer. Even if companies have no mandates and are able to use a common principle like the ISSB standards, they may choose to follow a stricter standard if it can enable compliance in a wide range of regions as new rules continue to roll out. New standards may also raise stakeholder expectations, so that organizations may be expected to comply with guidelines that aren't technically mandated for them.

McReynolds recommends that organizations can enhance their abilities to comply with new expectations if they follow these steps as they gear up for compliance:



2024 Executive Benchmark on Integrated Reporting, Workiva, 2024

- **Prepare for complexity.** Understanding standards may not be the only complication that organizations face. When asked about the most significant hurdle to integrating financial and ESG/sustainability reporting, 52% of executives in the Workiva study pointed to the complexity of data collection. When it comes to having the resources to tackle new complexity, beyond the existing talent crunch for finance and accounting professionals, organizations are also struggling to find people with sustainability expertise who can tackle increased data complexity and reporting needs.

- **Leverage existing approaches.** Instead of seeing sustainability reporting as a completely new task, organizations would do well to approach sustainability regulation the same way they already address financial reporting, McReynolds advised. In both cases, there is global agreement on the need to report, but rules will be different in various countries, regions, and states. Organizations can examine the strengths and weaknesses of their financial reporting and apply what they learn in sustainability reporting.

1. 2024 Executive Benchmark on Integrated Reporting, Workiva, 2024.

- **Don’t neglect the value.** While organizations may see sustainability disclosure as a significant new compliance burden, they should begin the process with an understanding of the potential value that a more holistic and integrated view of financial and sustainability performance can offer. Workiva found that companies that engaged in integrated reporting were more confident in the accuracy and clarity of data in their financial and sustainability reporting as well as the reliability of internal controls over financial and sustainability reporting, for example (see Figure 1), and that companies that integrate reporting are more attractive to investors.

A New Focus on Controls

Aligning on Rigorous Reporting

Mind the gap

While there is growing alignment on the need to apply the same rigor to nonfinancial reporting that is seen with financial reporting, the chasm between executive and manager views on how well we're doing is wide. According to the Workiva survey, 62% of executives strongly agree that their company applies the same diligence to ESG reporting as it does to financial reporting, but only 32% of managers say the same. They also aren't aligned on whether the company has tapped someone internally to oversee ESG-specific reporting and initiatives. Eighty-seven percent of executives say they have, but only 67% of managers do.

Workiva Global ESG Practitioner Survey

"An important responsibility of the internal audit function is to assess and monitor the performance of an organization's controls," according to COSO's guidance on internal control over sustainability reporting, which notes that this monitoring function applies to internal controls over sustainability reporting as well as over financial reporting. The monitoring function, "extends to any risks that could affect the organization achieving sustainable business objectives," it said. The COSO study includes:

- References that explain and underscore the internal audit function's important role in sustainability reporting.
- Issues for organizations to consider as they build and maintain effective controls over financial and sustainable business information.
- References to internal audit's role in offering objective assurance on the effectiveness of sustainable business risk management, reporting, and related regulatory compliance, as well as other key efforts related to sustainability.[2]

At Workiva, internal audit and finance have worked together to address necessary improvements in controls over nonfinancial data, McReynolds said. And while quantitative data is important, the teams also discussed how to manage qualitative data in sustainability reporting. Qualitative data might be important in assessing a range of new considerations, such as governance, the organization's impact on its community, and its success in DEI efforts. It might consist of interviews, focus groups, surveys, or even photos or drawings, based on the issues involved. Organizations will need to identify what information they have available to them and then how to gather and assess it. McReynolds recommends performing a gap assessment now to identify what's missing and what areas need better information-gathering processes, and then determine how to measure the data. Internal audit can also team with risk management to identify material sustainability-related threats and opportunities and whether they are immediate or emerging.

2. "Achieving Effective Internal Control Over Sustainability Reporting (ICSR): Building Trust and Confidence Through the COSO Internal Control—Integrated Framework," COSO, 2023.

Companies should also be able to determine what information they don't need. One important determination regarding the SEC rules is whether GHG emissions relate to something that is within the organization's direct control, in which case the emissions must be reported as a Scope 1 or 2 emission. If not, they are a Scope 3 emission that need not be reported. As an example, Workiva leases buildings, but it has no control over the properties or their energy use, so it determined their emissions were a Scope 3. In the gap analysis, "be clear on whether the company has operational and financial control," McReynolds said, "because you may not have to pursue that data." This process can also help organizations make smart decisions about metrics to ensure that they are aligned to areas that are truly material to the business. "You have to take a strong stand on what's material, otherwise you could be chasing too many metrics," McReynolds said.

Investors clearly continue to put stock in sustainability reporting: Workiva found that 82% of investors consider ESG in their investment decisions. "You must understand what is important to your investors and stakeholders," McReynolds said. Customers, as well, want more information on sustainability from organizations in their supply chain.

The Value of Internal Auditors

Experienced Reporters Leverage Independent Assurance

Avoiding surprises

A Workiva Global ESG Practitioner Survey of practitioners in organizations that have been reporting on sustainability the longest found that they were more likely to involve their internal audit or risk management teams in the process, indicating an appreciation of the value of internal audit's contributions.[3] Because internal auditors often provide early warnings on risk and potential threats, their input will be crucial as organizations navigate an unfamiliar reporting and risk environment, McReynolds said. When it comes to compliance, "it's important for it to be a team sport," she said. As the demand for financial and sustainability reporting increases and companies move into a low carbon economy, "they will want their internal audit and risk professionals right there at the table with them," she said. "Internal audit will be an incredible partner on the team."

Among other things, internal audit can provide an initial look at updated control, risk, and reporting processes so that companies have a chance to improve them before they are made public. "Internal audit and external professional service firms, acting as consultants, have significant expertise in considering risks and assessing system effectiveness, sometimes called 'readiness assessments,'" according to COSO. "These assessments can bring forward the steps that an organization may take to improve its systems in a way that parallels the techniques used for mainstream financial reporting."

Organizations should consider having an internal audit before an external one, McReynolds recommends. If the organization has an external audit without gaining insights from internal audit, it may be faced with unpleasant surprises that could have been fixed sooner. If internal audit performs an audit of controls and reporting first and reports the results to the audit committee of the board instead, further action can be taken and the company can be better prepared for its external audit. "It's great to have an internal auditor with you as you navigate the new world of ESG audits," she said.

Internal auditors and their organizations can also benefit from leveraging technology for their compliance needs. Executives are likely to be on board, considering that 83% thought generative AI would help organizations comply with regulation, and more than half of institutional investors use generative AI to evaluate financial and ESG performance, Workiva found. At the same time, virtually all ESG practitioners surveyed saw technology as crucial in successfully managing ESG reporting and thought access to technology and data would be key to decision making to advance ESG strategy going forward. "Companies will have to have conversations around technology innovation investments they should be making to comply with regulations and streamline the work and complexity they are facing," she said.

3. 2023 Global ESG Practitioner Survey, Workiva, 2023.

Conclusion

The value of perspective

Looking ahead, internal audit should ensure that sustainability reporting considerations are incorporated into their audit plans. "Start now if you haven't already done so," McReynolds said. In its advisory role, internal audit can provide advice on designating sufficient resources to address new reporting goals or mandates and on building up internal controls and data collection to the same level of trust as internal controls over financial reporting. Internal auditors can also provide perspective on how the board receives sustainability information. Organizations may want to review and update various committees' charters to include their sustainability responsibilities and determine whether sustainability efforts would be reported to the full board or to a separate sustainability committee, the audit committee, the nominations and governance committee, or another committee. "Internal audit can be a huge partner in managing these considerations," McReynolds said.

PART 2

How the Focus on Sustainability Is Driving Data Governance

About the Experts

Hassan NK Khayal, CIA, CRMA, CFE, cCAE

Hassan NK Khayal is the senior internal audit specialist at the Mohamed bin Zayed University of Artificial Intelligence in Abu Dhabi. He was featured as one of *Internal Auditor* magazine's 2020 global Emerging Leaders as an up-and-coming star of the internal audit profession. In addition to his other professional certifications, Khayal holds certifications in robotic process automation, quality management, health and safety, environmental management, information security, energy management, and food safety.

Grant Ostler, CIA, CPA

Grant Ostler is an industry principal at Workiva and has more than 35 years of experience, primarily in the disciplines of auditing, enterprise risk management, and process improvement. He served as CAE for almost two decades for entities ranging from Fortune 500 companies to pre-IPO companies, building internal audit functions from scratch and leading the implementation of U.S. Sarbanes-Oxley of 2002 Section 404 compliance programs for three companies.

Introduction

The need for assessment

Increasingly, organizations are embracing concepts associated with sustainability, at least in part in response to demands for greater transparency and accountability about actions that impact shareholders, employees, the communities in which companies operate, and the overall environment. While sustainability actions have long been voluntary and organizations could often adapt suggested guidelines to their own needs, new mandates, such as those from the **European Union** (EU) and the **U.S. Securities and Exchange Commission** (SEC), mean that sustainability reporting controls and compliance are now critical concerns for organizations.

As a result, companies will need to assess their approaches to sustainability reporting and data governance, whether they do so to comply with new or expected rules and stakeholder expectations, or to understand and track the value of sustainability efforts. This brief will discuss the use of nonfinancial data in sustainability reporting, as well as internal control, the value of leveraging technology, and other key considerations.

New Types of Data

Transparent Sustainability Efforts

Cyber risk demands enterprisewide approach

While organizations may be well-equipped to collect information from traditional data sources — such as financial records or operational metrics — for many types of sustainability data, these sources will not satisfy emerging reporting needs. To provide transparency on sustainability efforts, organizations will need to collect and report on information, such as nonfinancial data, that they have not consistently monitored or gathered in the past. Nonfinancial data falls into a variety of areas that affect or contribute to an organization's sustainability, and this data can vary significantly depending on an organization's industry and other factors. A few common examples include:

Greenhouse gas (GHG) emissions. Organizations are being asked by regulators and other stakeholders to quantify direct GHG emissions based on their own energy consumption, transportation, or other uses and, potentially, indirect emissions related to their supply chain and suppliers. Reporting these emissions is a key requirement in the EU and SEC rules, as well as other guidelines. Understanding and mitigating GHG emissions is essential for addressing climate change and aligning with global targets, such as those outlined in the Paris Agreement, notes Hassan NK Khayal, senior internal audit specialist at the Mohamed bin Zayed University of Artificial Intelligence in Abu Dhabi. Organizations will no longer be asked to report only on their own sustainability efforts but also may be expected to make choices about vendors and suppliers and their sustainability efforts. He adds there is a growing movement seeking reporting on an organization's customers' emissions. This can be challenging, because companies don't always have control over who uses their products or services. It still may need to be considered, as organizations would not want to be associated with a customer that is notorious for bad environmental practices.

Responsible usage of natural resources, such as water, land, and raw materials. This reporting can provide benefits beyond simple compliance. "By tracking and reporting on resource consumption, organizations can identify areas where efficiency improvements are needed and minimize the environmental impact," Khayal says.

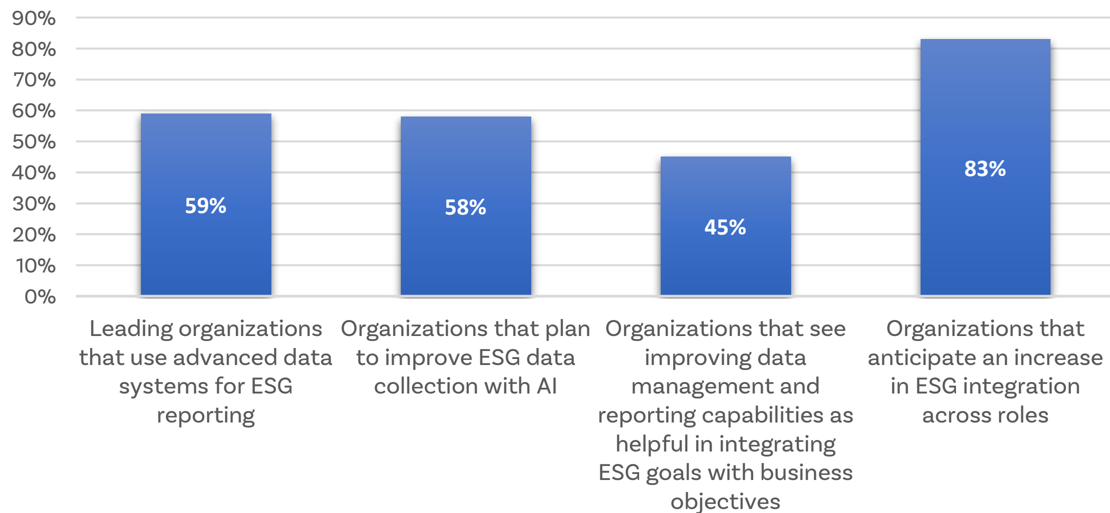
Assessing the social impact of the organization's activities. This includes adding reporting on areas such as diversity, equity, and inclusion efforts, community engagement, and philanthropy.

Internal auditors should be aware that, with nonfinancial information, "data wrangling is a big challenge," says Grant Ostler, industry principal at Workiva. While financial data is relatively easily retrievable from a traditional enterprise resource planning system and comes in tabular, structured form, sustainability data typically comes from disparate sources across the organization and is often unstructured with a variety of taxonomies involved.

In Sarbanes-Oxley-related work, for example, internal auditors usually are not tapping into the human resources or expense reporting systems. "There's a system there, but because it's not material to the financials, it's never been in scope for Sarbanes-Oxley work," he says. "Now with new integrated reporting requirements, it's going to become significant if the organization uses the expense reporting system to determine employees' overall travel mileage so they can determine the impact on greenhouse gas reporting." Ostler says it's likely some of those systems have never been subjected to internal audits. "If our experience with Sarbanes-Oxley is a good indicator, the quality of the IT general controls for those systems are probably lacking in some ways and will require remediation to be ready for the scrutiny of the assurance process." If data has been kept in a spreadsheet or other nontraditional system, it may be hard to determine the completeness and accuracy of that data.

There's good reason to make this effort, however, because companies that effectively manage and accurately report on nonfinancial sustainability considerations over time can build trust with stakeholders and across the company's culture, according to Khayal, as well as affect the wellbeing of society at large. Gathering and reporting nonfinancial data enables organizations to reveal nuances that offer a more accurate picture of sustainability achievements. By reporting nonfinancial data, such as resource use and emissions, stakeholders and the company, itself, will get meaningful data that presents a realistic picture of its activities.

Exhibit 1



Source: "Addressing the Strategy Execution Gap in Sustainability Reporting: 2024 ESG Organization Survey," KPMG, 2024.

Internal Control Considerations

The Importance of Quality Data

Assessing control effectiveness

Internal audit already plays a crucial role in advising on all control requirements and the control environment. As organizations increasingly recognize the significant role nonfinancial disclosures play in value creation, internal auditors can be strategic partners in ensuring reliability and accuracy. Internal audit can evaluate control effectiveness to mitigate risks related to nonfinancial reporting in areas such as data accuracy, integrity, and completeness. Internal auditors also can assess the reliability of procedures to ensure data is accurately captured, verified, and communicated to stakeholders.

In addition, "internal auditors are well-positioned to help process owners understand what good data quality looks like for them," Ostler says. That's especially important with attestation on the horizon. "When you have a third party looking at your data, that's not the time when you want to find out you have a problem," he explains.

Sustainability practices are already reasonably mature at some organizations. In this case, internal auditors may initially have a more traditional role in auditing those practices and may spend most of their time on ensuring compliance with new and emerging regulations. But for organizations who are in the early stages of sustainability practices and reporting, internal audit will likely take on a more advisory and collaborative role, gearing audit plans to, and advising on how sustainability initiatives align with, organizational objectives. "Internal audit can be the bridge between the sustainability department, which wants to focus on its objectives, and the finance area, which wants to drive profits," Khayal says. "We have a bird's-eye view of the organization as a whole, so we can bring together departments that otherwise may not be in communication."

One key aspect of internal audit's role can be to assess the adequacy of the existing control framework from a sustainability reporting perspective. This includes identifying whether further controls may be needed to comply with new or expected requirements for nonfinancial data. This should be handled in collaboration with stakeholders across the organization, according to Khayal, including sustainability teams, compliance, and senior management, to understand their specific reporting needs and risk objectives related to sustainability and social responsibility. "Effective sustainability reporting will require a holistic approach," Khayal says. "The aim is to collect the correct data and metrics and leverage them in a meaningful way. When you have five or six perspectives, you can see the true story that the data tells and can recognize actions required for further improvement."

Integrated Reporting

Facilitating Consistency and Completeness

Internal audit as a catalyst

When they first take on sustainability reporting, organizations may handle financial and nonfinancial reporting separately. Going forward, internal audit can validate the integration of sustainability reporting processes with financial processes to ensure consistency and completeness. That means aligning data validation, collection, and reporting timeliness and coordinating reporting and disclosure across reporting domains.

"Internal audit can be the catalyst," Khayal says. He points to several key areas where internal audit can help organizations address important considerations:

- **Regulations.** Organizations will have to navigate a complex landscape of rules governing the collection and use of nonfinancial data. While many may be used to addressing local laws, as wider-ranging and more comprehensive mandates emerge they will have to consider state, federal, and regional rules, as well as sector-specific rules for some industries.
- **Legal.** Internal audit can offer assurance and advice to address a variety of considerations, including:
    - **Compliance with existing laws.**
    - **Verification of the integrity and accuracy of data.** This also includes possible independent assurance.
    - **Privacy and confidentiality.** Nonfinancial data can include sensitive personal and corporate details. Organizations will have to comply with data protection laws such as the EU's General Data Protection Regulation and the California Consumer Privacy Act.
    - **Risk management.** Threats to sustainability information include security breaches and related reputation risk, as well as noncompliance.
    - **Stakeholder communication.** Internal audit has a role in ensuring the organization communicates accurately, transparently, and in accordance with regulatory requirements.
- **Ethics.** Sustainable data governance practices should uphold principles of fairness, transparency, and respect for stakeholders. That effort will include obtaining informed consent for data collection and ensuring that the data is accurate and protected from outside access and misuse.
- **Practical.** Internal audit can advise companies on establishing clear policies, procedures, and controls over data collection and storage and how it is accessed and shared. It also can consult on roles and responsibilities for data owners and on data security to prevent breaches and unauthorized access and advise on standards for quality assurance and validation.

"By addressing these considerations and proactively managing compliance concerns, organizations can establish robust data governance frameworks for sustainability information that promote accountability, transparency, and responsible data management practices," Khayal says.

Leveraging Technology

Addressing Reporting Needs

A new approach to data and data collection

Internal auditors can encourage their organizations to harness the power of technology to address sustainability reporting needs. The technologies Khayal considers most important in addressing sustainability reporting include:

1. Data analytics and visualization, which allow organizations to analyze and visualize large volumes of sustainability data from diverse sources and accomplish more comprehensive reporting. Data analytics tools identify trends, patterns, and outliers, providing valuable insights for decision making and risk management. Data visualization is so useful that Khayal challenges his team to use it in all presentations.
2. Automated reporting platforms, which make it possible to streamline the task of collecting, aggregating, and reporting sustainability data, thereby reducing manual efforts and enhancing accuracy and timeliness. "Automation can allow internal auditors to spend time on something unique and strategic that a computer can't do," Ostler says.

   Khayal's team is using tools that can generate audit reports once the internal auditors have performed the audit testing. Other departments can automate their own systems and more easily share sustainability data with the audit function. Internal audit can help to evaluate the effectiveness of these automated systems by ensuring they comply with regulations.
3. Blockchain and distributed ledger technologies, which can enhance transparency. Blockchain is a more advanced form of audit logs or trails that makes it possible to trace data to its origin and enable internal audit to ensure it has not been altered along the way. "It can add greater accountability in sustainability reporting by providing irrefutable records of transactions and data exchanges," Khayal says. Internal audit can advise on the implementation of blockchain solutions.
4. Environmental monitoring technology can be integrated into the sustainability reporting process to create an audit trail. Remote sensing technologies, for example, allow organizations to monitor and gather data on environmental factors that can be used in reporting. Khayal's organization, which has 8,000 vehicles, used remote technologies to sample 50 of them, tracking their fuel consumption, emissions, and time spent in traffic. The data can be used for reporting and in determining how best to maximize the vehicles' efficiency.
5. Artificial intelligence (AI) and machine learning, which can analyze large data sets, identifying patterns, correlations, opportunities, and risk, quickly making connections that otherwise might have been missed. Internal audit can leverage AI-driven analytics to assess the effectiveness of risk management strategies, identify emerging sustainability risks, and recommend proactive measures for mitigation. Ostler's team uses generative AI to help identify risks and controls to address them. "It can help us understand a broader perspective and use our judgment to assess those risks," he explains.
6. Digital collaboration platforms and continuous monitoring and assurance. Digital collaboration can facilitate communication with different stakeholders, making it easier to address sustainability reporting issues and data privacy and security requirements. Continuous monitoring and assurance enable organizations to track sustainability performance in real time and assess the effectiveness of risk control and mitigation efforts.

Organizations are undergoing a significant change in how they approach data and data collection. With so much of it available due to automation, data analytics, and AI, it can be challenging to identify meaningful information, analyze it

correctly, and manage and use it effectively, Khayal notes. Organizations that leverage their technology effectively can enhance their capabilities to assess and address new sustainability reporting needs. Technology solutions should be aligned with organizational goals to enhance their effectiveness and better illustrate the value they can offer, according to Khayal.

It's wise to consider technology first, Ostler adds. "It's difficult to make the best use of technology when you're thinking about it at the last minute," which can happen when an organization waits until a process is designed before building controls. Because the controls are being introduced at the last minute, they will likely be manual and not as efficient or practical as controls built into processes upfront. "There's a lot of functionality in the technology that's not being leveraged today," he says. Internal auditors should not take on a first- or second-line role, but they should get involved early and partner with other professionals to identify risks and appropriate controls as processes are being developed for capturing, processing, and reporting nonfinancial data. Being involved throughout that effort will reduce rework, Ostler explains, and provide better backend results.

Conclusion

Internal audit can play a critical role in sustainability data governance by ensuring it is reliable, accurate, and complete, that it maintains data integrity, and complies with appropriate laws and regulations. The function can identify needed improvements in data management and offer valuable strategic insights on aligning data collection and governance with the organization's objectives, risk management priorities, risk appetite, and regulatory requirements. Its independent assessments and audits of nonfinancial data can identify risks, opportunities, and areas for improvement, ultimately enhancing organizational resilience and sustainability.

"We are the idealists who look at how things should be five or 10 years from now," Khayal says. "But unless we speak up today, these things won't get done in five or 10 years." It's becoming more obvious that achieving organizational goals depends on meeting the needs and expectations of stakeholders and the world in which companies operate, he says. "To do that, we need to satisfy their requirements, which more and more include ethical considerations on sustainability." Organizations should recognize the value of meeting new reporting requirements. That value may lie simply in avoiding penalties and reputational risk due to noncompliance, or it may be found in taking advantage of tax benefits, improved reputation, or new business opportunities that valid sustainability efforts and reporting can offer.

PART 3

Change Management Strategies for Successful Sustainability Governance

About the Experts

Matej Drašček, PhD

Matej Drašček is an international speaker and author specializing in internal audit and ethics. He has served as a lecturer for various universities and faculties and has contributed numerous professional and scientific articles on topics such as internal auditing, business ethics, and strategic management. His recent book, *Ethical Decision-Making in Management*, was published by Routledge, New York.

Mandi McReynolds

Mandi McReynolds, chief sustainability officer and vice president of Global ESG at Workiva, has 15 years of experience leading sustainability teams across four industries. McReynolds helps global companies drive business value and make a positive societal impact through transparency, accountability, and innovation. She is a co-host of ESG Talk, a weekly podcast series featuring business leaders around the world.

Mark Mellen

Mark Mellen is an industry principal at Workiva, the world's only unified platform for financial reporting, ESG, audit, and risk. Previously at Deloitte, Mellen has more than 15 years of experience advising organizations on managing risk, especially focused on matters related to sustainability and ESG. At Workiva, he works cross-functionally to help enhance and integrate the ESG capabilities of the platform.

Introduction

Internal audit inclusion advocacy

From both a regulatory and cultural perspective, few risks have evolved more rapidly than those related to sustainability. Indeed, organizational culture has evolved — especially through the pressure of investors and government policy — to where many organizations today feel a social responsibility for their role in the global movement toward a cleaner, more sustainable, and more equitable future. This shift takes the form of detailed sustainability reporting practices, direct measures to improve factors such as carbon footprints and wasteful practices, and updated corporate governance structures.

However, even with an overall willingness to address sustainability risks, there still can be challenges in the early stages. While sustainability is hardly a new concept, its scale can cause uncertainty — and from such uncertainty can come delays or even resistance. Part 3 of The IIA's Global Knowledge Brief Series on sustainability highlights the form some of these changes might take, as well as examines internal audit's vital role in supporting the organization through the change process.

Sustainability Goals

The Goal is the Journey

Understanding the drivers of change

The push to create a sustainable organization often begins when the company starts receiving pressure from one or more of the three main areas:

1. Regulators.
2. Investors.
3. Customers and stakeholders.

In previous years, the push would be for general action. “I’ve had some interesting conversations with both large companies and academics in the marketplace regarding how companies historically have just sort of been rolling things forward on sustainability,” says Mark Mellen, industry principal at Workiva. “That’s better than nothing, but that’s not really achieving anything.”

Today, however, the conversation has advanced to include action toward a measurable goal. The clearest example can be seen on climate goals. “A lot of the regulation currently regarding corporate sustainability is climate first, which is why I think we’re seeing a trend of climate-first goals,” Mellen says. “And even if the regulation doesn’t specifically require goals to be set, I think it’s forcing companies to look at setting goals, because it is meeting expectations for investors that look at not just standardized disclosures, but also how companies set goals and manage performance.”

Although climate-focused goals are most obviously applicable to certain sectors such as energy and heavy industries, boards should realize sustainability goal setting is becoming an expectation that manifests in some form regardless of region, organization size, or industry. “I’ve worked in this space for 15 years, and I’ve seen this trend permeate every industry,” says Mellen. “Even if companies don’t have a real great opportunity to have an impact on the climate space, there’s still an expectation that they set goals and manage what they can. Even something like carbon emissions produced by running computers has relevancy.”

Forms of change

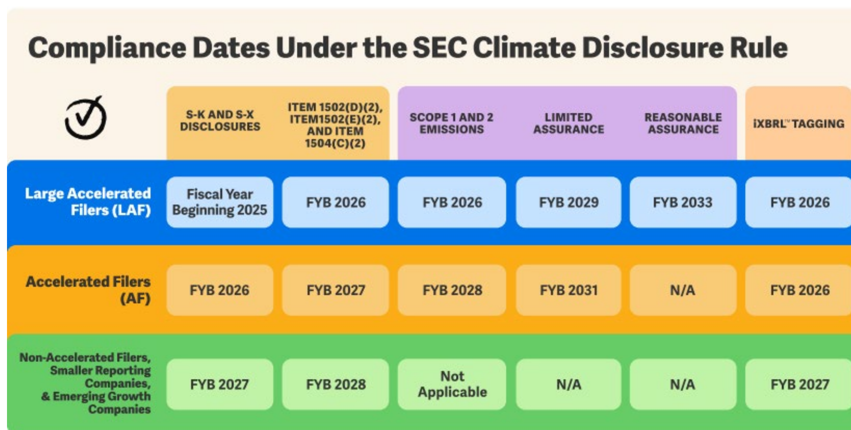
Organizational responses to meet established sustainability goals vary. Approaches may encompass:

- Creating standalone sustainability strategies.
- Integrating environmental, social, and governance (ESG) goals into the overall strategy.
- Incorporating sustainability in remuneration KPIs.
- Making sustainability part of ongoing strategic and operational controls.
- Including sustainability in reporting schemes for internal and external stakeholders.
- Forming separate organizational units for sustainability goals.
- Developing policies addressing various aspects of sustainability (e.g., waste management, emissions).

Regarding any of these approaches, the first steps involve the implementation of various strategies, processes, and procedures. Often, these can be augmentations of pre-existing strategies and policies through some form of program management. According to Mellen, such management will include its own system of governance processes, reporting procedures, and best practices to monitor program statuses. Over time, monitoring also can be leveraged to adjust — or completely reset and recast — established goals.

Time is of the essence to make these adjustments, especially regarding climate disclosure rules. According to the current state of the U.S. Securities and Exchange Commission's new Climate Disclosure Rule, large accelerated filers will be required to report on S-K and S-X disclosures by the beginning of fiscal year 2025, with Scope 1 and 2 emissions following fiscal year 2026 (for more details on other filers (see Exhibit 1). In Europe, the Middle East, and Africa regions, climate reporting has been mandatory since 2022, while the Asia Pacific region adopted a phased-in approach that was fully implemented in fiscal year 2023.

Exhibit 1:



Compliance Dates Under the SEC Climate Disclosure Rule

	S-K AND S-X DISCLOSURES	ITEM 1502(D)(2), ITEM1502(E)(2), AND ITEM 1504(C)(2)	SCOPE 1 AND 2 EMISSIONS	LIMITED ASSURANCE	REASONABLE ASSURANCE	iXBRL™ TAGGING
Large Accelerated Filers (LAF)	Fiscal Year Beginning 2025	FYB 2026	FYB 2026	FYB 2029	FYB 2033	FYB 2026
Accelerated Filers (AF)	FYB 2026	FYB 2027	FYB 2028	FYB 2031	N/A	FYB 2026
Non-Accelerated Filers, Smaller Reporting Companies, & Emerging Growth Companies	FYB 2027	FYB 2028	Not Applicable	N/A	N/A	FYB 2027

Source: Executive Summary: A Snapshot of the SEC's Climate Disclosure Rule | Workiva

Forms of risk

Although there should be a degree of familiarity with elements of sustainability-related changes such as reporting policies and structures due to policies already in place, there are inherent risks involved that could cause uncertainty. For example, concern could arise around related reporting variables, including:

1. New data gathering methodologies.
2. Data analyses.
3. Establishment of organizational buy-in.
4. Resource management.

In addition to these areas, a more subtle risk also exists regarding long-term competitive advantage. "Competitive advantage is defined by an organization's ability to outperform its competitors and deliver added value to customers," says Matej Draščec, assistant professor at the University of Ljubljana, Faculty of Economics, in Slovenia. "This principle should also apply to sustainability. Sustainability initiatives must be linked to what the organization does best, which would also lead to financial gain, and finally should enhance the organization's competitive advantage."

"Goals aren't driven by compliance," agrees Mandi McReynolds, vice president of global ESG at Workiva. "They're informed by the environment, the regulation, but in the end, they're working towards what is the performance of the company.

Investment in sustainable innovation, reducing emissions to provide cost savings, investment in innovative energy saving technology — this is where the new economy is going."

While all these areas should be relevant to the ongoing sustainability conversation, the most relevant risks — especially early — are in the planning and implementation of strategies and policies.

During early implementation of strategies, ownership might be of particular relevance for many organizations, largely because of a lack of understanding of the shared responsibility of sustainability initiatives, says Mellen. "A lot of organizations today have suitable governance systems in place in some shape or form, but the question is do they leverage that and the right representatives from each part of the business to be involved," he says. "It's a question of communicating shared ownership. For example, if we're talking about a strategy to get to net zero, that might be owned by one person, but a lot of people are responsible for helping attain the success of that goal." Drašček agrees. "The goal is to embed sustainability into everyday processes and significant decision-making," he says. "This integration can often be achieved without major changes, ensuring sustainability is incorporated into every major business process. I view sustainability as akin to ethics: It should not be confined to a separate policy or department but should permeate every aspect of the organization."

In the ESG realm, establishing that shared ownership mentality also should go beyond just the boundaries of the organization. This should include the establishment of clear communication lines between all stakeholders, including supply chain partners, applicable communities, and external audit parties, among others. For initiatives such as data gathering for reporting, these lines are particularly critical.

"I think that's part of what's really unique when we think about ESG," says Mellen. "From an ESG perspective, that data comes from so many different places, even beyond the organization's four walls. When you begin to understand that, you start to see these governance structures with representation from every part of the organization."

The larger and more complex the organization is, obviously the more intricate these lines can be, which in and of itself should be considered a risk. "From a size perspective," Mellen says, "if you have 500 locations that have to help in achieving net zero, that obviously should also factor into how the organization might put robust processes into place."

Internal Audit Roles

Where to contribute the most value

Looking for opportunities

As with any risk, internal audit's unique place in the organization allows it to provide value that no other function can easily accomplish. Internal audit can provide value in a consulting role, and as a traditional assurance provider. For example, as a consultant, internal audit can identify critical success factors for sustainability implementation. According to Drašček, these can include:

1. Leadership buy-in and support.
2. Skilled implementation.
3. Alignment between specific initiatives and general strategy.
4. Effective planning.
5. Good communication.
6. Ability to manage organizational change.
7. Adequate funding for strategy implementation.

Another one of internal audit's most important roles in this space, Mellen says, is in the ongoing communication of governance structures, including structures both for meeting specific goals (such as net-zero emissions) and the general ESG program overall. This can include not just clarification of existing structures to the board and audit committee, but also communication of new governance structures as ESG-related risks necessitate new committees composed of executive leadership.

Senior management also benefits from ongoing internal audit communication. For example, internal audit can clarify sustainability-related questions to management such as:

- Do we have a clear view of all sustainability risks and opportunities, including compliance risks and regulatory expectations?
- Are we prepared to address future legislation or regulatory expectations?
- What is the organizational maturity of our current sustainability culture, and where should it be?
- What public commitments does the organization have regarding sustainability, and do we currently have the data to support such commitments?

Additionally, it can advise on risk management systems related to the sustainability program, including the processes and controls that should be in place. This is key not just at implementation, but also well after so that ongoing monitoring can be done in a repeatable, transparent fashion.

To provide this value when planning and executing on established risk management processes, internal audit also must commit to an ongoing program of continual learning. Areas of understanding can include:

- How controls should work.
- Testing processes.
- Regulatory environments.
- Relevant data analytics.

Although some resource management might need to be considered, relevant tools and data needed to fulfill these criteria often are already in house. “It depends how mature an organization is, but often minimal additional resources will be needed,” says Mellen. “The organization may have the data already, whether it’s broad ESG data or energy and emissions data in a system today, and you can automate the extract of that kind of information into an analytics engine. Organizations that are in those heavy industries, for example, will have technology in place that would enable internal audit to go in and look at anomalies and energy consumption to help establish carbon footprint ratings for reporting.”

Beyond tools in the organization, it is also easier than ever — thanks to artificial intelligence — to find additional relevant resources online. Drasček, for example, recommends internal audit stay abreast of the sustainability-based research being continually published in academic journals. “To avoid spending excessive time on reading research,” he says, “internal auditors should leverage AI tools to summarize articles and distill key information. Some AI tools focused on academic research include Jenni, Scite, Scholarcy, and ChatGPT.”

Peer relations

Sustainability is a shared responsibility that should unite parties both within and outside the organization. This mindset, especially when it comes to initiatives such as climate change, can even unite competing organizations through a mutual sharing of knowledge and best practices. This is something where internal audit — via its own communication channels established through initiatives such as quality assurance assessments — can play a key role.

“Because ESG and things like carbon accounting are newer to organizations, there’s more of a willingness to share best practices amongst organizations and even talk about it in front of auditors,” says Mellen. “The reality of any potential of attaining many of the 2050 goals cited by regulations requires industries to work together to solve a lot of these problems.” Many of these goals, he also says, are likely insurmountable for an organization on its own.

Independent third parties should also not be discounted for their ability to both share knowledge and help forge inter-departmental relations. For example, third-party input through the evaluation of a pre-assessment, or “readiness assessment” conducted by the internal audit team can be extremely valuable. “We did this within our own organization,” says McReynolds, “then we had a third party provide verification and limited assurance. This was a really good step for our team, because it allowed the internal audit team and the sustainability team to come together to learn from one another to work through a process together.”

Conclusion

Establishing buy-in

Sustainability is a complex subject and is only becoming more so by the day, so it is unreasonable to expect internal audit to be a subject matter expert on the topic overnight. However, the key through line of all internal audit-related value is not so much educating stakeholders on sustainability itself, but rather educating stakeholders on the importance of sustainability. In other words, internal audit is instrumental in establishing buy-in.

An essential aspect that ties into all these steps is the need to be politically savvy within the organization when it comes to sustainability, says Drašček. Sustainability is often perceived as a pet project, a regulatory/compliance issue, or merely a good PR strategy. Internal auditors should leverage their organizational power — without which change is impossible — to convince decision-makers that sustainability is not only an ethical business practice, but also a sound financial strategy.

For those meeting resistance, there are a few simple strategies internal audit can use. One is through straightforward documentation on the priority of the risk. “I would suggest assembling a list of all of the relevant regulations that are coming down the pike related to the organization or related to the customers of the organization, and share that kind of information with executives,” Mellen says.

Internal audit can communicate both issues and potential benefits in equal measure, which caters to the profit mentality that often drives businesses on a basic level. Sustainability is not something that just has to be done, but something that the organizations should actively want to do.

For example, according to a 2022 report from the IBM Institute for Business Value, customers are considering sustainability more than ever before in their buying habits. Findings include:

- 51% of survey respondents said environmental sustainability is more important to them than it was 12 months ago.
- 49% said they have paid a premium for products branded as sustainable or socially responsible in the last 12 months.

Beyond direct monetary advantages, there are more downstream benefits to consider as well, such as:

- Increased appeal for new hires, especially younger generations.
- Improved organizational resilience through removal of inefficiencies.
- Increased innovation.
- Increased appeal from potential investors.

The road to sustainability is a journey, one not without challenges as the organization commits to change. But through positive, regularly involved internal audit support, it should be clear to every stakeholder from the C-suite down that it is a journey well worth pursuing.

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