



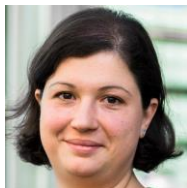
Eyes on the Horizon: Embedding ESG into your Fraud Risk Framework

Andra-Aurora Horwat, 30 November 2023




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Speaking to you today



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Goals of this session

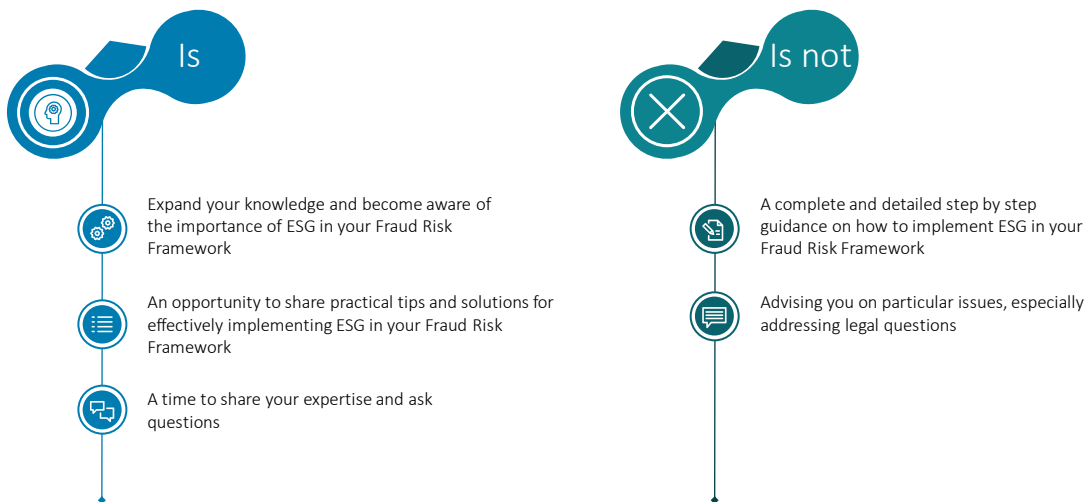


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What this workshop...



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Agenda



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ESG

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ESG – Overview

Navigating environmental, social and governance dimensions

ESG is a framework that helps stakeholders understand how an organisation is managing risks and opportunities related to environmental, social, and governance criteria (sometimes called ESG factors). ESG takes the holistic view that sustainability extends beyond just environmental issues. As such, **Fraud Risk Framework is addressing the governance risk – the “G” in ESG**

ESG

Overview

- **Environmental** pillar is broad and covers all manner of impacts on the environment and our natural resources focusing on issues from climate change, water stewardship and biodiversity
- **Social** pillar addresses the company’s interaction with stakeholders (both inside and outside of the organization) such as talent, suppliers, contractors, and consumers, covering topics such as human rights, modern slavery, safety and well-being
- **Governance** pillar evaluates the impact of a company’s corporate governance decisions with a focus on enhancing companies’ accountability and transparency to investors and other stakeholders, and how environmental and social topics are embedded within

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Sources: How can CCOs help companies tackle ESG? | Deloitte Switzerland; #1 What is ESG? (deloitte.com)

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Trends in the Area of ESG

From debate and development to widespread adoption

2010's > Groundwork for ESG corporate practices through debate and policy development

➔

2020's > Holistic view capturing ESG, significant adoption and regulation

2020's > Putting into action, widespread adoption as the new norm

Key Trends

- Embedding ESG into organisational practices and strategies is non-negotiable for key stakeholders including investors, customers and supply chains
- Significant and complex regulatory requirements and reporting standards
- Seen as a driver of new growth opportunities and long-term value creation
- Expanding regulatory requirements and reporting standards
- Growing emphasis on ESG ratings, disclosures and benchmarking
- Increasing Greenwashing and ESG Fraud Risks due to rising pressure
- Increasing Litigation and Reputational Risk
- Increased reliance on ESG data, therefore increased scrutiny on data quality and external validation
- Holistic view of the company’s performance/impact – increasing relevance on supply chain and vendor due diligence

<p>Environment</p> <ul style="list-style-type: none"> • Heightened focus on climate change, water stewardship and biodiversity • Transition to clean energy, carbon neutrality goals, greenhouse gas accounting • ESG-related regulatory changes and commitments 	<p>Social</p> <ul style="list-style-type: none"> • Broad recognition of social issues’ significance • Emphasis on diversity, equity, and inclusion • Employee well-being and mental health in the spotlight 	<p>Governance</p> <ul style="list-style-type: none"> • ESG-linked to corporate responsibility and decision-making • Shareholder engagement on governance gains momentum • Multicommittee/-board ESG frameworks within corporation on the rise
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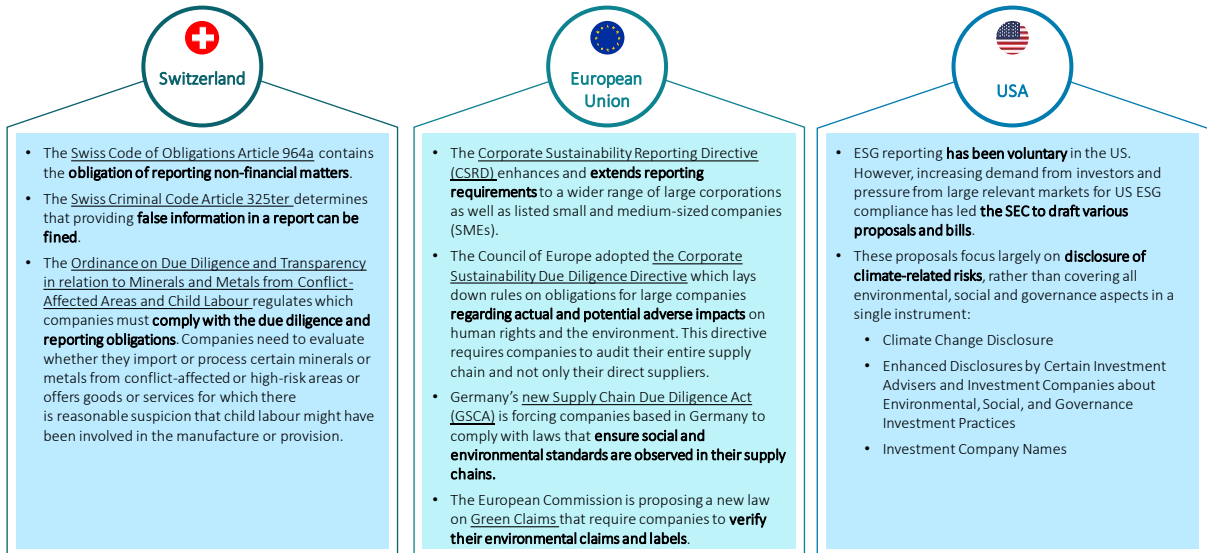
Sources: Emerging Trends in ESG Governance for 2023 | Deloitte US; 3 paradigm shifts in corporate sustainability to new era of ESG | World Economic Forum (weforum.org); How can CCOs help companies tackle ESG? | Deloitte Switzerland

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Regulatory Requirements in the Area of ESG

International comparison on the approach of ESG regulations



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Sources: [ESG disclosure regulations](#) | [Deloitte US: The SEC Plans to Finalize ESG-Related Rules in 2023](#) | [ACA Group \(acaglobal.com\)](#), [Corporate sustainability reporting](#) | [European Commission \(europa.eu\)](#)

ESG in the Fraud Risk Framework



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Importance and relevance of addressing fraud risks

Understanding the challenges and trends of the fraud landscape

Fraud enablers

The eminent risk of external fraud increases the risk of internal fraud as most of external fraud is linked to internal weaknesses, e.g., cyber-attacks or conflicts of interests.

Effective prevention

A robust framework is essential to minimize the risk of loss due to fraud since a lack of internal controls contribute to nearly 1/3 of internal frauds.²

Collateral damage

Fraud can have wide implications for continuous growth and success, destroy an organization's reputation, undermine relationships with suppliers / customers / financial institutions / financial markets and damage employee morale / attrition.



Legal responsibility

Swiss law and best practices expect the Board of Directors to take responsibility for the internal control system, dealing with risk and compliance.¹

Inherent business risk

Fraud is an ever-present danger to all organizations and one of the most significant threats to their viability.

Financial losses

Fraud can cause enormous financial damage with losses amounting to 5% of revenues annually in many organizations.²

¹ e.g., Swiss Code of Obligations or Swiss Code of Best Practice for Corporate Governance
² "Occupational Fraud 2022: A Report to the Nations", Association of Certified Fraud Examiners

The Role of Audit Committees in the ESG Fraud Risk Framework

Ensuring that ESG-related fraud risks are effectively assessed, controlled, and mitigated

ESG Fraud Risk Assessment

- Assess the consideration of ESG-related risks in the current fraud risk assessments
- Evaluate management's antifraud programs and controls
- Review disclosures regarding deficiencies, material weaknesses and fraud in internal controls
- Understanding the independent auditor's fraud risk assessment process and findings

Specific Fraud Risk Identification

- Identification of responsibilities and decision-takers
- Identification of potential fraud schemes, methods, and potential perpetrators
- Evaluation of likelihood, impact, and mitigation strategies of identified risks
- Do not consider the existing control environment when discussing potential fraud schemes as fraudsters may work to circumvent those fraud prevention controls

Compliance Monitoring and Cross-Functional Collaboration

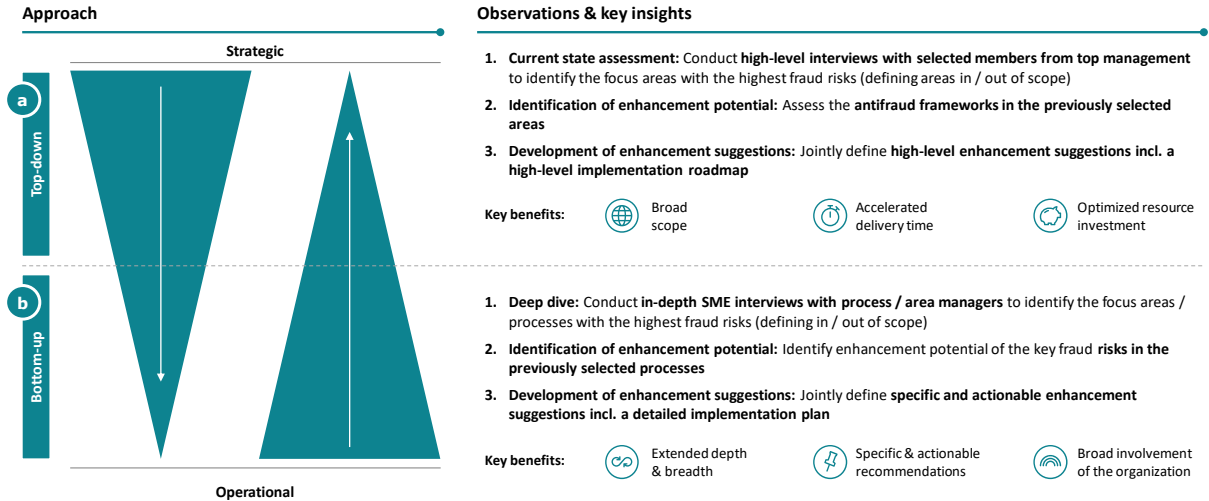
- Ensure ESG-related data accuracy and integrity
- Establish robust ESG-related disclosure controls and procedures
- Safeguard against management's ability to override or manipulate
- Monitoring of ESG compliance with evolving regulations and standards
- Ensuring cross-functional working group with technical knowledge and members from diverse departments
- The UK Corporate Governance code is recommending that ESG oversight moves within the remit of the audit committee

Continuous Improvement and Consideration of Emerging Risks

- Reviewing and testing of antifraud programs and ESG-related internal controls
- Assess emerging risks based on changes in the internal and external environment
- Consider changes in the economy, new ways of doing business, new products or services, technologies, and evolving stakeholder expectations

In general, there are two approaches to Fraud Risk Assessments — Top-down and Bottom-up

It is essential to incorporate ESG-related risks in the wider Fraud Risk Assessment



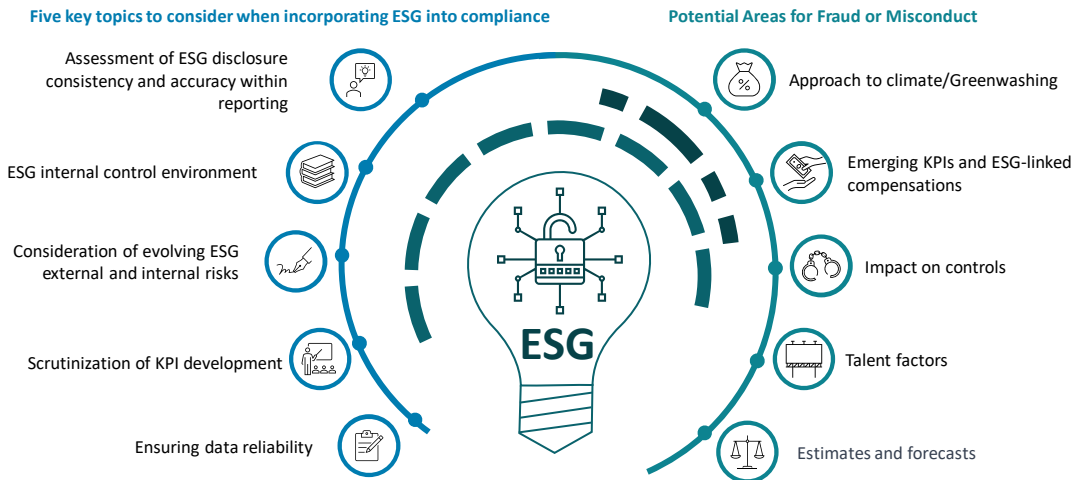
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ESG in the Fraud Risk Assessment

Insights on ESG in compliance and associated risks



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Source: Emerging Fraud Risks to Consider: ESG | Deloitte US: How to Integrate ESG into Your Risk Management Framework (insightsforprofessionals.com) 14

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Greenwashing



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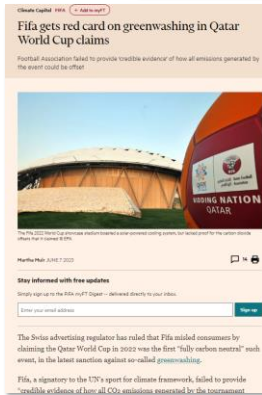
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Greenwashing related news are growing

Deutsche Bank's DWS to pay \$25mn to settle SEC probes

Asset manager's settlement with US regulator includes historic \$19mn penalty over greenwashing allegations



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Banks behind 70% jump in greenwashing incidents in 2023 -report

Reuters

October 3, 2023 6:21 PM GMT+2 Updated 6 days ago

LONDON, Oct 3 (Reuters) - The number of instances of greenwashing by banks and financial services companies around the world rose 70% in the past 12 months from the previous 12 months, a report on Tuesday showed.

European financial institutions accounted for most of those instances, and much of the greenwashing involved claims about fossil fuels.

Environmental, social and governance (ESG) data firm RepRisk recorded 148 cases from the banking and financial services industry globally in the 12 months to the end of September 2023, up from 86 during the previous 12 months.

EU to crack down on greenwashing with 'proportionate' penalties



Draft plan addresses inflated claims about products' environmental credentials

Companies will have 10 days to justify green claims about their products or face "effective, proportionate and dissuasive" penalties, under a draft EU crackdown on greenwashing seen by the Guardian.

Inflated claims by firms about their products' environmental bona fides have grown along with public awareness of global heating in recent years.

One EU survey in 2020 found that 53% of environmental product claims were "vague, misleading or unfounded". Authorities suspected 42% of green product gambits of being "false or deceptive" in another survey the same year.

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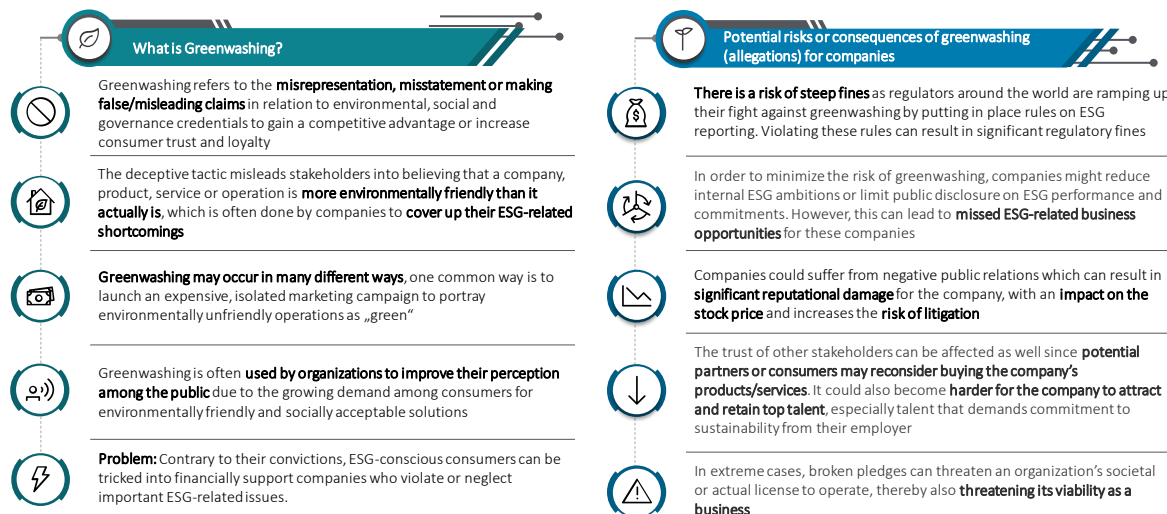
Source: EU to crack down on greenwashing with 'proportionate' penalties | Environment | The Guardian; Banks behind 70% jump in greenwashing incidents in 2023 -report | Reuters; Banks behind 70% jump in greenwashing incidents in 2023 -report | Reuters; Deutsche Bank's DWS to pay \$25mn to settle SEC probes | Financial Times (ft.com); Fifa gets red card on greenwashing in Qatar World Cup claims | Financial Times (ft.com); Swisscom, Coca-Cola and others accused of greenwashing - SWI swissinfo.ch

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Greenwashing—Definition and Risks for Companies

Greenwashing has gained prominence in recent times as businesses strive to adopt more eco-friendly practices



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How to prevent Greenwashing

Safeguarding your brand from Greenwashing



© 2023 Deloitte AG. All rights reserved. Source: Greenwashing: Navigating the Risk (harvard.edu); Research: How Some Companies Avoid Accusations of Greenwashing (hbr.org); Greenwashing and how to avoid it | Deloitte Netherlands

ESG outlook

Increasing ESG litigation risks for compliance managers

The evolving disruptors in environmental, social and governance settings are shaping new trends in the disputes markets and trigger new litigation risks



To do's

- Ensure compliance with legal obligations, including ESG-related regulation
- Consider ESG in fraud assessments
- Consider media or social judgements on ESG topics, those can outweigh legal prejudices responsibilities
- Follow trends which are moving towards holding the board and/or Audit Committee accountable for climate change cases



Watchout

- Approach the setting of new targets and declaring ESG success with caution and consider the associated risks
- The wording and definition of corporate ESG targets have become an important factor
- Avoid overcommitting to ESG targets as they can be challenging to fulfil (e.g. net zero carbon claims)
- Shareholder activism is on the rise, resulting in investors becoming more outspoken and ESG-conscious if companies fail to meet their ESG commitments



- Litigation risks are increasing and are influencing the responsibilities of companies (ESG/Sustainability-related litigation has not just increased against states, but also against companies and their executive bodies)
- Strong focus also on greenwashing allegations

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Source: Seminar Sustainability and ESG – Litigation Risks, 16.05.2023, Associated Institute of the University of Zurich & Cooperation Partner of ETH Zurich; The disruption factor: How the disputes market is reacting to disruption, 2022, Deloitte UK; Emerging Fraud Risks to Consider: ESG I Deloitte US

Q&A



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