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## *Relevance of ESG in the Enterprise Risk Management Framework*



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(July, 2021 Batch)  
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Environment, Social and Governance ("ESG") has become the most relevant criteria for regulators, investors and credit rating agencies to rate companies and make business decisions today.

According to one of the world's largest asset management corporations, ESG has become one of the key requisites for making investment decisions by institutional investors. They are willing to an ESG pathway beyond the mandatory legal

requirements. ESG parameters rate companies on sustainability, gender diversity and inclusion, management structure and the composition of the board.

In today's dynamic business environment, ESG-related risks have started to become an essential part of the Risk Governance framework across organisations. ESG framework is not merely focusing on value creation in the short run but has an integral and



more important role in achieving profitability through sustainable value creation in the long run.

Thus, an effective way of managing ESG-related risks is by integrating ESG parameters into the organisation's Enterprise Risk Management (ERM) framework.

The COSO framework has highlighted the importance of aligning risk in strategy across all levels in the organisation. The framework has identified five essential components for effective risk management in the organisation.

1. **Governance and Culture for ESG-related risk:** The governance and culture of an organisation impact its overall philosophy. A mature risk governance and culture framework ensures that the board is well aware of ESG-related risks and the organisation has defined the responsibility for ESG-related risks. A good practice could be incorporating ESG-related risks into the company's mission and vision and creating an opportunity for

sustainable future growth. For example, incorporating net-zero carbon emissions in the organisation's vision and developing sustainable measures for its implementation.

2. **Strategy and Objective for ESG-related risk-Setting:** Business objectives should be aligned against ESG-related risks while forming business strategies and setting goals. Today's organisations need to redefine their strategic objectives against sustainability measures and review



the ones considered unsustainable. The senior leadership must take a proactive approach by incorporating ESG into the organisation's strategic objectives. ESG-related risks with a significantly higher materiality impact need to be considered on a priority basis.

### 3. **Performance for ESG-related risk:**

- a. **Risk Identification:** ESG-related risks must be at the centre of the risk identification process. Organisations need to develop tools and integrate the same into the ERM framework to ensure that the risk

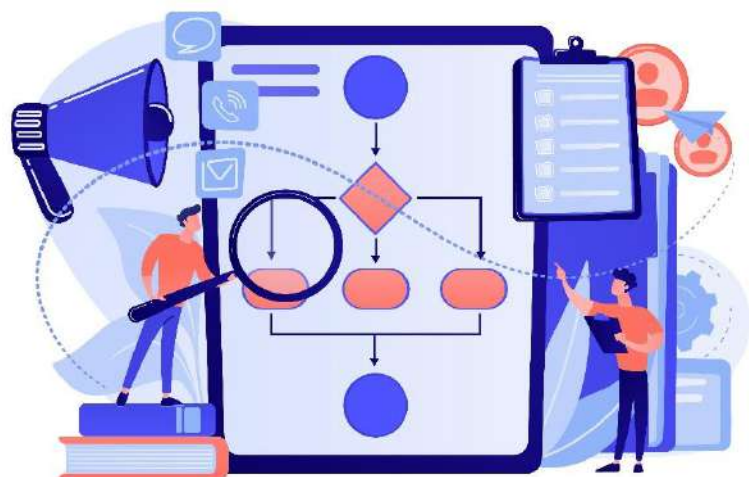
catalogue of the organisation is appropriately updated with the same.

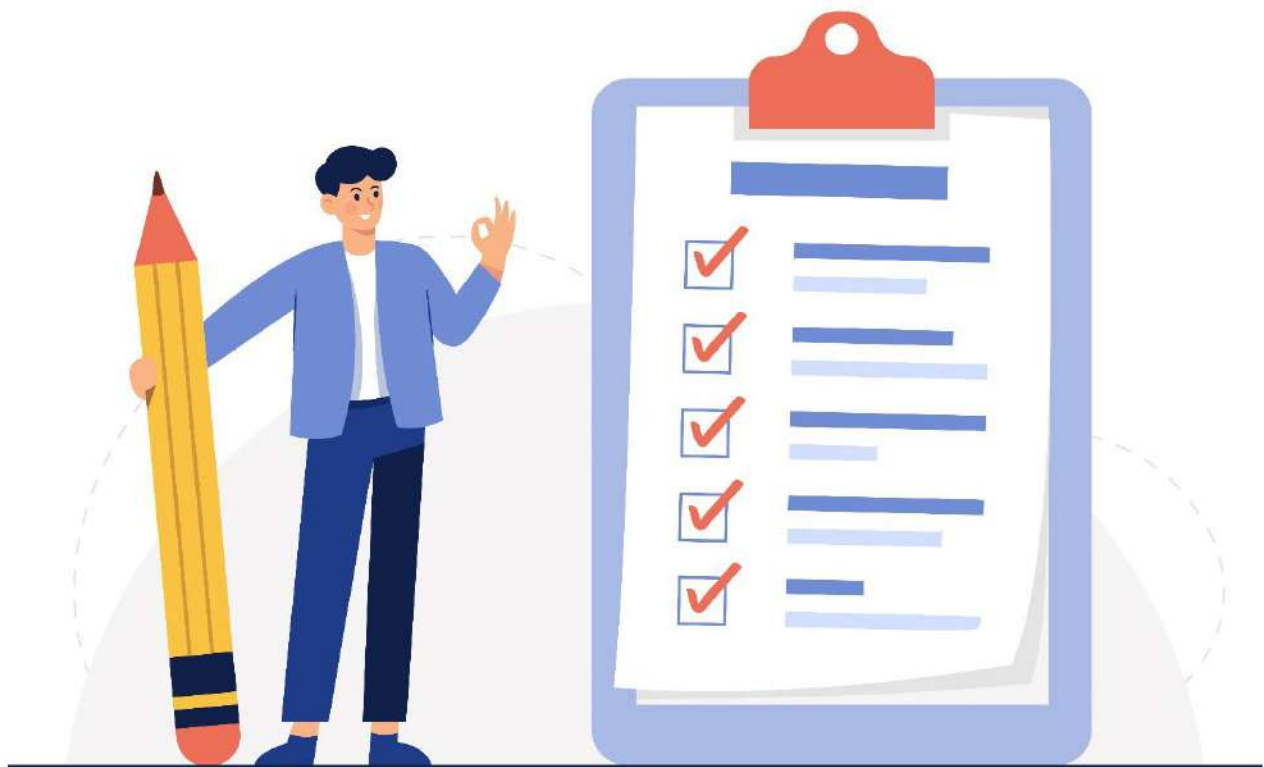
- b. **Risk Assessment:** Organisations need to continuously identify all ESG-related risks and update their risk catalogue. Applying a risk-based approach to identify risk will help organisations do prioritise planning basis the impact and

likelihood of the risk, which will help position them for adequate Risk Management.

- c. **Risk Response:** An effective way to respond to ESG-related risks would be to align the organisation's strategic objectives to ESG-related risks. This could include a thorough review of the organisation's entire value chain to identify effective, sustainable practices to ensure value creation and sustainable growth.

4. **Review and Revision for ESG-related risk:** A continuous monitoring and assessment of the





ESG-related risks will help organisations identify growth opportunities and realign their approach to objectives accordingly. Organisations can also develop specific tools to identify any ESG-related changes in the business environment and report them to the Chief Sustainability Officer(s) for immediate consideration.

5. **Information Communication and Reporting for ESG-related risk:** Applying the ESG-related risk to the reporting parameters will help create accountability for organisations beyond the legal requirements. Institutions, such as the Sustainability Accounting Standards Board (SASB), the Global Reporting Initiative (GRI), and the Task Force on Climate-related Financial Disclosures

(TCFD) are working to form standards and define materiality to facilitate the incorporation of these factors into the ERM process to make disclosure and reporting more effective.

*(The views and research are personal and do not represent any organisation or Institution.)*

