Environmental impact: How finance leaders can add value to sustainability efforts

The science behind climate change comes down to a few crucial numbers: Carbon dioxide levels in the atmosphere (414.72 parts per million in 2021, a record high),[1] global temperatures (which have risen two degrees Fahrenheit since 1880)[2], and ocean levels (3.8 inches higher than in 1993).[3]

The significance of numbers can also extend to many corporate activities associated with sustainability management. New regulations for environmental, social, and governance (ESG) factors are coming into force—and more may be on the way (see "How ESG disclosures may expand the nature of the CFO's role," *CFO Insights*, Jan. 26, 2023). The main thrust of the rules? Requiring companies to provide information on how climate change affects their operations and how their operations affect climate change.[4] Even before the regulatory focus, many investors, stakeholders, and social advocates have been clamoring for more detailed data on individual businesses' risks and impacts.

It's likely that most companies' finance functions will be deeply involved in reporting sustainability information, helping to bring discipline and consistency to a new dimension of nonfinancial reporting. Deloitte's 2022 Sustainability action report: Survey findings on ESG disclosure and preparedness, asked 300 executives which part of management had responsibility for managing ESG disclosures. Thirty-seven percent of respondents cited CFOs, second only to the 42% who chose chief sustainability officers.[5]

Beyond imposing new reporting standards, ESG requirements could potentially change how value is created, generated and captured, mandating that CFOs measure societal impact, rather than relying solely on total shareholder returns (see "The CFO Agenda 2023," *CFO Insights*, April 20, 2023). Sustainability data produced for internal consumption could help CFOs uncover operational inefficiencies, identify new sources of revenue, and shape due diligence assessments of potential acquisition targets. In time, climate-related metrics may routinely be factored into capital allocation, investment decisions, product pricing, and employee compensation.

In this edition of *CFO Insights*, we'll look at how increasing demands for accurate and transparent sustainability numbers offer the potential for finance chiefs to become better business partners to their C-suite peers. With a role that reaches across the enterprise, CFOs may be ideally positioned to drive value from ESG compliance. By keeping the ESG agenda in front of both employees and the board, as well as directing funds to support related initiatives, finance leaders can play a pivotal part in ensuring that sustainability is integrated into how the business operates, innovates, and grows.

Emissions statement

Many typical CFO duties can be categorized as "future-proofing" the organization—helping spearhead such activities as digital transformation, corporate strategy and, now, sustainability reporting and performance management.

In the US, the Securities and Exchange Commission (SEC) has proposed rules that would require registrants to disclose information about, among other issues, the climate-related risks that are reasonably likely to have material impacts on their businesses or consolidated financial statements. Metrics for greenhouse gas (GHG) emissions that could help investors—as well as bankers, customers, and other stakeholders—assess those risks.

In Europe, rules governing sustainability disclosure are already in place. The Corporate Sustainability Reporting Directive (CSRD) took effect in January 2023. The CSRD, which governs ESG reporting for EU-based businesses and some non-EU based companies with regional operations, will apply to about 50,000 companies. Initial filers will have to apply the new rules to results in the 2024 calendar year. In addition, businesses are required to seek limited assurance of sustainability reporting.[6] In time, the requirement will likely ratchet up, with companies required to seek reasonable assurance of that reporting.[7]

The fact is, reporting, particularly regulatory reporting, is typically owned by finance, which also possesses the necessary skills, capabilities, and know how. Some finance departments also have experience in governance and controls principles, decision-making processes, and automation of data collection. Moreover, finance functions like tax, controllership, audit, and risk management will likely play a part in ESG-related reporting. And while it is possible that some chief sustainability officers may not be as familiar with producing regulatory documents or interpreting changing rules, CFOs are typically accustomed to doing so. Finance chiefs may be able to help shepherd those executives through what could be a complicated undertaking.

Chief financial officers are also familiar with presenting data to analysts and institutional investors. As ESG targets and performance get integrated into earnings calls, it is likely that CFOs will be fielding more questions about their companies' sustainability numbers. Having reliable data—and framing it properly—will be important.

Indeed, in the Sustainability action report, CXOs at public companies with minimum annual revenues of $500 million were asked to pick the three outcomes they anticipated from enhanced ESG reporting. Fifty-one percent of the respondents cited enhanced trust with stakeholders. Another 48% named brand/reputation enhancement. Inaccurate reporting could put a dent in those expected gains.[8] (For other anticipated benefits, see Figure 1.)

Figure 1. Anticipated benefits from enhanced ESG reporting vary by industry

Attracting talent and retaining employees are the top anticipated benefits in the life sciences and health care industry. Greater trust with stakeholders and the premium pricing of products are the main anticipated benefits for the oil and gas industry. Increased efficiencies and improved ROI are the top anticipated benefits within the consumer products industry.

EXPECTED BUSINESS OUTCOMES DUE TO ENHANCED ESG REPORTING TOP 3 RANKED RESPONSES	**TOTAL*** n=695	**FINANCIAL SERVICES** n=100	**CONSUMER PRODUCTS** n=100	**OIL AND GAS** n=100	**TECH, MEDIA AND TELECOMMUNICATIONS** n=100	**LIFE SCIENCES AND HEALTH CARE** n=100
Talent attraction and retention	52%	52%	51%	46%	52%	58%
Enhanced trust with stakeholders	51%	52%	51%	58%	48%	49%
Increased efficiencies and ROI	50%	55%	58%	44%	56%	41%
Premium pricing of products	50%	39%	54%	58%	48%	50%
Brand/reputation enhancement	48%	47%	42%	48%	45%	52%
Reduced risk	48%	55%	44%	46%	51%	50%

Source: "Sustainability action report: Survey findings on ESG disclosure and preparedness," Deloitte Development LLC, December 2022

*Deloitte commissioned an online survey of 300 executives at publicly owned companies with a minimum annual revenue requirement of $500 million and conducted interviews to increase the total sample size to 100 in each of the following industries: consumer products; financial services; life sciences and health care; oil and gas; and TMT (technology, media and telecommunications).

Data data everywhere

As some CFOs may know, calculations that miss the mark can stem from inaccurate or insufficient data (see "Now's the time for CFOs to seize the data," *CFO Insights*, May 4, 2023). In certain aspects of ESG reporting, finance leaders may not have direct access to necessary data. Indeed, CFOs will likely need to address a company's GHG output from indirect emissions—that is, those generated outside a company's walls, including:

- Greenhouse gases released in the production of energy a business purchases
- Business travel
- Leased assets
- The use of sold products
- End-of-life treatment/disposal of sold products

Essentially, the finance function and other departments will likely be tasked with collecting data all along the value-chain. CFOs, along with CSOs and procurement departments, often employ a number of estimation methodologies for third-party emissions, including market-level approximations and shared direct measurements.[9]

The problem? It's not always clear if the information from third-party vendors is precise, or if sufficient rigor went into formulating the numbers. An oft-adopted approach is to develop a closer relationship with suppliers, identifying gaps in the emissions information they provide, and working with them to plan and execute improvements to product/service details. In some cases, this may mean guiding them as to how to estimate their own footprints in a consistent manner across each category. Such an approach might require training existing employees or acquiring those with the appropriate skills (see accompanying story, "Labor pains").

Climate business

Building external and internal trust in climate numbers is likely to consume time and resources. The good news is that CFOs have a blueprint for getting there: Section 404 of the Sarbanes-Oxley Act of 2002. Among other things, Section 404 requires companies to establish and maintain adequate internal controls over financial reporting. Similarly, finance chiefs could deploy a SOX-like framework to identify ESG risks, document process flows, and implement internal controls for climate reporting.

CFOs may eventually want to automate the controls on climate reporting. But the benefits of producing nailed-down and transparent sustainability data—decision-grade data—often extend past compliance, and shareholder and stakeholder demands. Ultimately, CFOs and other C-suite leaders may bring ESG data and analysis to bear on a wide array of business processes. ESG may eventually help shape capital allocation and strategic decision-making (from performing due diligence to tying worker bonuses in some part to meeting climate goals). Sustainability may also influence what businesses charge for their products. Indeed, in the Deloitte report, 49% of the surveyed executives indicated that the premium pricing of products was an expected outcome of enhanced ESG reporting.[10]

Longer term, there may be valuable insights from heightened attention on GHG emissions and carbon footprints. Getting a handle on the ESG impact of every step in a company's value chain might uncover inefficiencies that are bloating items like the SG&A budget.

In a recent Deloitte Dbriefs webcast, attendees were asked to name the most significant trigger for their organization's finance function to engage in sustainability, climate, and equity. About one third (33.4%) of respondents said compliance and regulatory impact. But almost as many, 31.6%, cited cost efficiency[11] (see Figure 2).

Figure 2. What is the most significant trigger for your organization's finance function to engage in sustainability, climate, and equity?

Votes Received: 5,422	
1. Cost efficiency	31.6%
2. Topline growth	11.3%
3. Investment and asset optimization	14.6%
4. Supply chain impact	9.1%
5. Compliance and regulatory impact	33.4%

Source: "Finance for a sustainable future: It's an opportunity," Deloitte Dbriefs, January 25, 2023

Making CFOs energy efficient

ESG efforts hold the potential of improving reputation and brand—not just of companies, but also of CFOs. Making meaningful progress in complying with EU and other regulations may require finance teams to continuously adapt and persevere. In their efforts to comply with regulatory requirements, CFOs may want to help their companies take some initial steps, such as:

1. **Becoming familiar with the relevant reporting requirements**, including those in the CSRD and those the SEC is expected to issue.
2. **Performing a materiality assessment and prioritization of internal and external information and metrics linked to sustainability,** leveraging some of the benchmarks already in use by peers.
3. **Defining some guiding principles to help meet short-term and strategic reporting demands**. These may include voluntary disclosures and private disclosures to value-chain partners, investors, and financial institutions. Other strategic reporting demands may be entirely internal, such as strategic planning, budget cycles, and M&A decisions.
4. **Advocating long-term benefits of ESG**. Like communicating about strategy, it can require a constant drumbeat for employees to program sustainability considerations into their everyday decisions.
5. **Setting achievable goals**. While some companies may have set goals for net-zero emissions by, say, 2050, CFOs can use data to set interim milestones and measure against those objectives. Senior executives might also want to embed ESG goals into annual performance targets that cascade through the business.

Of course, it's hard to predict precisely what gains companies might derive from sustainability efforts. Here again, SOX compliance may offer a clue.

When the legislation was enacted, some CFOs might have scrambled to get a handle on how to put in effective controls. Some may have over-engineered process documentation. Some could have found that SOX compliance disturbed the normal workflows of the finance function. Others may have confused financial data with operational data. The eventual implementation of the requisite controls presented some challenges.

Twenty-one years later, SOX compliance is SOP for finance departments (see "Sarbanes-Oxley at 20: For CFOs, it may be time for a refreshing experience," *CFO Insights*, Sept. 8, 2022). The attention paid to internal controls has, in many cases, improved financial processes. And that, in turn, has instilled greater confidence in the numbers released in a company's regulatory filings. Sustainability reporting may follow a similar pattern—and produce a similar result: more trust in the numbers. It's not a bad place to start.

Labor pains

Before CFOs can address potential deficiencies in sustainability reporting, they may first have to address any deficiencies in worker skills.

As chief financial officers look to comply with increased ESG disclosure requirements aimed at addressing climate change, one issue is becoming abundantly clear: finance staffs may feel that they are lacking the experience or knowledge to help support the cause. A recent Deloitte survey found that 87% of finance/accounting senior executives are not completely confident that their organizations are properly staffed to meet the demands of increasing ESG disclosures.[12]

Granted, CFOs can often run up against talent gaps in areas like modeling and financial planning and analysis (FP&A). It may be doubly difficult, however, to find appropriate FP&A skills for a relatively niche discipline like sustainability reporting.

Potential solutions do exist, though. For companies with discrete ESG departments, finance chiefs may be able to tap controllers in that unit to handle some of the higher-end work. In addition, CFOs might be able to upskill the finance department by training existing employees or hiring candidates who possess at least some familiarity with ESG-related issues. The latter may get easier over time as more college students graduate with degrees—or at least specializations—in both accounting and sustainability.

Getting the right talent in place is likely only half of the equation, however. Finance chiefs should address the finance team's mindset and how they can influence the wider enterprise. One way that might get the message across: include ESG goals in performance measurements for finance workers and tie bonuses, at least in part, on meeting those targets. Moreover, finance employees who are well informed about ESG subjects can engage in holistic discussions about sustainability, operational and financial performance with their business counterparts. This, in turn, may generate a positive, ripple effect across the organization.

An emphasis on ESG may offer benefits beyond compliance. For one, a tangible commitment to sustainability—and follow through on the commitment—could energize members of the finance department. And it can probably help with hiring or retention, as well.

Consider one of the results from Deloitte's Sustainability action report.[13] In it, 300 executives of publicly owned companies with at least $500 million in annual revenues were asked to name their top three expected outcomes due to enhanced ESG reporting. The number one response? Talent attraction and retention.

End notes

1. "Climate Change: Global Temperature," National Oceanic and Atmospheric Administration, January 18, 2023.
2. Ibid.
3. "Climate Change: Global Sea Level," National Oceanic and Atmospheric Administration, April 19, 2022.
4. "SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors, Securities and Exchange Commission," March survey 2022"; "Directive (EU) 2022/2464 of the European Parliament and of the Council," December 2022.
5. "Sustainability action report: Survey findings on ESG disclosure and preparedness," Deloitte Development LLC, December 2022.
6. "Global Reach of the E.U. Corporate Sustainability Reporting Directive and the Impact on U.S. Companies," Deloitte Development LLC, 2023.
7. Ibid.
8. "Sustainability action report: Survey findings on ESG disclosure and preparedness."
9. "Companies Are Tallying Their Carbon Emissions, but the Data Can Be Tricky," Wall Street Journal, September 3, 2021.
10. "Sustainability action report: Survey findings on ESG disclosure and preparedness."
11. "Finance for a sustainable future: A new dynamic opportunity," Deloitte Dbriefs, January 25, 2023.
12. "ESG executive survey: Preparing for high quality disclosures," Deloitte Development LLC, March 2022.
13. "Sustainability action report: Survey findings on ESG disclosure and preparedness."

Contacts

Mateus Begossi
Director, Consulting
Deloitte MCS Limited
Deloitte UK
mbegossi@deloitte.co.uk

Anne Morel
Senior Manager, Consulting
Deloitte MCS Limited
Deloitte UK
ajmorel@deloitte.co.uk

Vishnu Narins
Managing Director, Consulting
Deloitte Consulting LLP
vnarins@deloitte.com

Michael Schor
Partner, Risk & Financial Advisory
Deloitte & Touche LLP
mschor@deloitte.com

Dina Trainor
Managing Director, Risk & Financial Advisory
Deloitte & Touche LLP
dtrainor@deloitte.com

About Deloitte's CFO Program
The CFO Program brings together a multidisciplinary team of Deloitte leaders and subject-matter specialists to help CFOs stay ahead in the face of growing challenges and demands. The program harnesses our organization's broad capabilities to deliver forward thinking and fresh insights for every stage of a CFO's career—helping CFOs manage the complexities of their roles, tackle their company's most compelling challenges, and adapt to strategic shifts in the market.

For more information about Deloitte's CFO program visit our website at:
www.deloitte.com/us/thecfoprogram.
Follow us @deloittecfo

Deloitte CFO Insights are developed by Josh Hyatt, Manager/CE Journalist, CFO Program, Deloitte LLP. Special thanks to John Goff, Senior Manager and Editor, CFO Lens, Deloitte Global.