



## Introduction

In 2019, the Chartered Institute of Internal Auditors included climate change as one of the big focus areas for Internal Audit departments to consider when preparing their Annual Plan. Unfortunately, all four of the Big 4 audit firms; Deloitte, KPMG, EY and PwC failed to recognise this as a growing risk area. This is despite four large UK business being referred to the Financial Reporting Council over their inability to appropriately disclose all Climate Change risks in their Annual Report. Each on of these businesses was audited by a 'Big 4' firm.

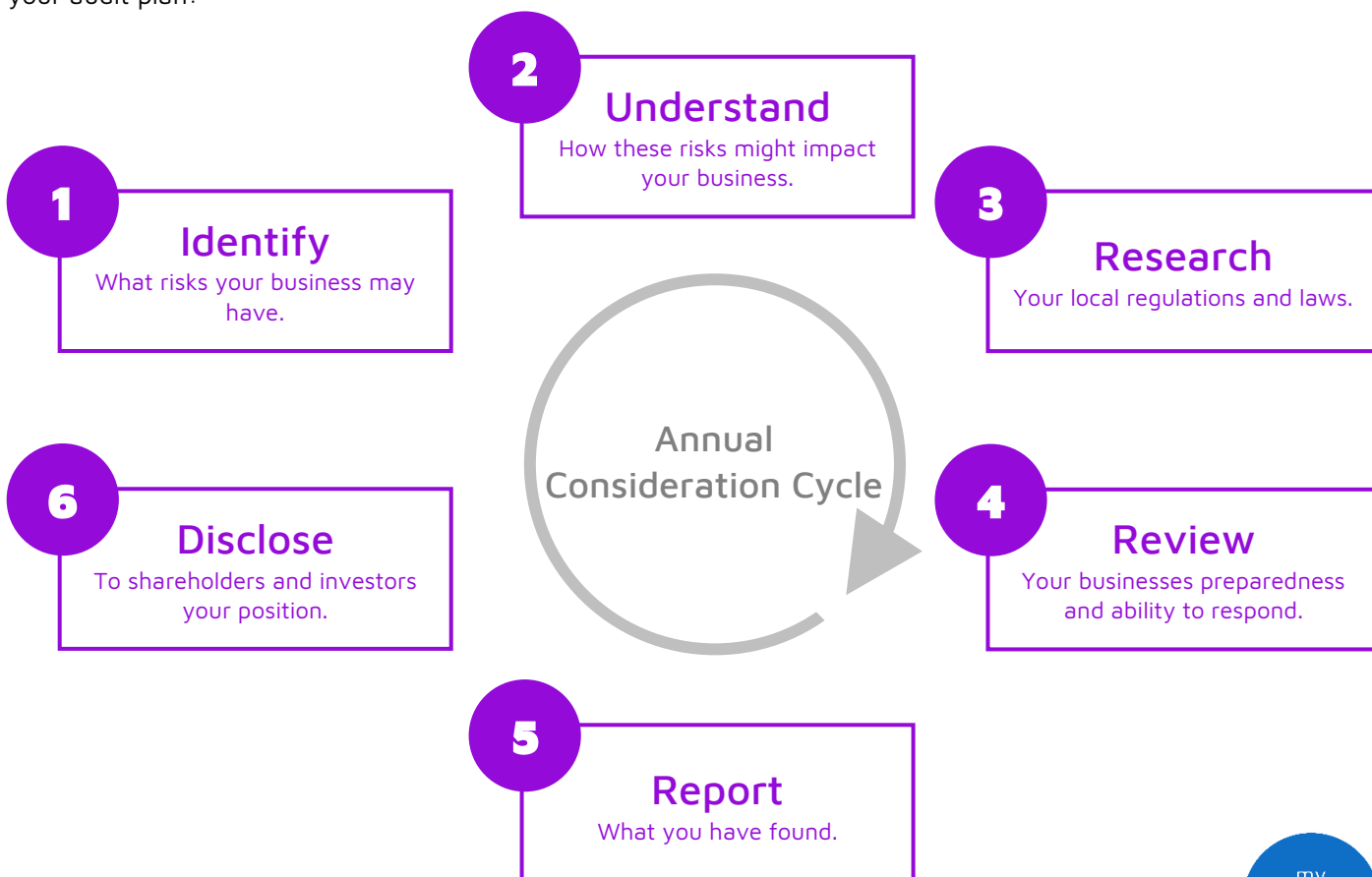
In addition, accounting bodies such as the AUSB are considering including requirements for business to account for climate change within in their company's books, meaning this will need to be audited during a financial statement review, and it will be open to investors for questioning.

So are you prepared to consider Climate Change and its risks within your business? Our guide here leverages off resources from each of the Big 4 audit firms, accounting bodies, and other external sources to provide a beginners guide for what Climate Change risks you should consider when developing your audit plan.

## This document

We've tried to keep this simple, but please keep in mind, regulations and reporting requirements vary between countries. Our guidance is generic in nature and research should be done to ensure you are adequately addressing your local laws.

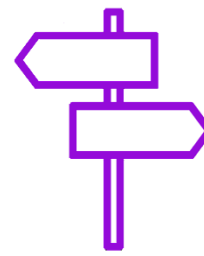
We will step through each of the following stages to help you consider all your Climate Change risks when building your audit plan:



# Guidance

## Climate Change

Risk and Audit Plan Considerations



1

## Identify

What risks your business may have

It may sound quite obvious, but understanding your what climate change risks your business may have can actually be a lot harder than you may first think. It is important to challenge your business and think outside the box, as some risks may actually be more realistic than first thought.

We have included below some of the main climate change risks which may be applicable to your business:



Intense Rain



Flooding



Drought / Heatwave



Sea-Level Rise

2

## Understand

How these risks might impact your business.

A systematic approach to understanding how your business is impacted by each of the risks is essential to ensuring we have covered all basis. The best way of doing this is to use your company's organisation chart / structure. A simple questionnaire can then be use to help understand the impact. This questionnaire is similar to what may be used in a Business Continuity Plan and will assist with your review in **Step 4**.

### Climate Change Impact Questionnaire

<b>Business Area</b>			
<b>Purpose</b>			
<b>What are the key activities performed</b>	<b>Activity</b>	<b>Frequency</b>	
		Daily	
		Weekly	
		Monthly	
		Half Yearly	
<b>Which activities would be susceptible to a climate risk?</b>	<b>Risk</b>	<b>Activity</b>	<b>How / Why</b>
	Rain		
	Drought		

# Guidance

## Climate Change

### Risk and Audit Plan Considerations



<b>For each of the activities susceptible to a climate risk, do we have a backup plan?</b>	<table border="1"> <thead> <tr> <th>Risk</th> <th>Activity</th> <th>Backup</th> <th>Details of the plan / evidence</th> </tr> </thead> <tbody> <tr> <td>Rain</td> <td></td> <td>Y / N</td> <td></td> </tr> <tr> <td>Drought</td> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Risk	Activity	Backup	Details of the plan / evidence	Rain		Y / N		Drought			
	Risk	Activity	Backup	Details of the plan / evidence									
Rain		Y / N											
Drought													
<b>If we have a backup plan, how long could we 'survive' under the plan?</b>  <b>If there is no backup plan, how long could we continue?</b>	<table border="1"> <thead> <tr> <th>Activity</th> <th>Survival Time</th> <th>What would be our biggest setback?</th> </tr> </thead> <tbody> <tr> <td></td> <td>X weeks, hours, etc</td> <td></td> </tr> <tr> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Activity	Survival Time	What would be our biggest setback?		X weeks, hours, etc							
Activity	Survival Time	What would be our biggest setback?											
	X weeks, hours, etc												
<b>Are any are business areas which are reliant on our activities?</b>	<table border="1"> <thead> <tr> <th>Activity</th> <th>Reliant Business Area</th> <th>What are they reliant on?</th> </tr> </thead> <tbody> <tr> <td></td> <td></td> <td></td> </tr> <tr> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Activity	Reliant Business Area	What are they reliant on?									
Activity	Reliant Business Area	What are they reliant on?											
<b>Are we reliant on any other business areas?</b>	<table border="1"> <thead> <tr> <th>Business Area</th> <th>Activity</th> <th>What are we reliant on?</th> </tr> </thead> <tbody> <tr> <td></td> <td></td> <td></td> </tr> <tr> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Business Area	Activity	What are we reliant on?									
Business Area	Activity	What are we reliant on?											
<b>What customers may be impacted by our risks?</b>	<table border="1"> <thead> <tr> <th>Customer</th> <th>Internal / External?</th> <th>How are they going to be impacted?</th> </tr> </thead> <tbody> <tr> <td></td> <td></td> <td></td> </tr> <tr> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Customer	Internal / External?	How are they going to be impacted?									
Customer	Internal / External?	How are they going to be impacted?											

This questionnaire is certainly not comprehensive, but provides a great starting point as to:

- What risks are we susceptible to;
- How long can we live with the risk;
- Do we have a back up plan;
- Who is reliant on us;
- Who are we reliant on; and
- Who are our customers.

Using tools such as Survey Monkey will help ensure this is completed in a quick and easy way.



Using the above information, we can now build a Dynamic Risk Assessment.

KPMG has used the Dynamic Risk Assessment tool to effectively map climate change risks, their impact, and level of severity. Furthermore, the map also shows the interrelationships between each of the activities.

The example provided on the following page is extracted from the KPMG report "Understanding social and environmental risk" and was prepared for the City of Sydney to help develop its Climate Strategy.

A copy of the report can be downloaded by clicking on the report.



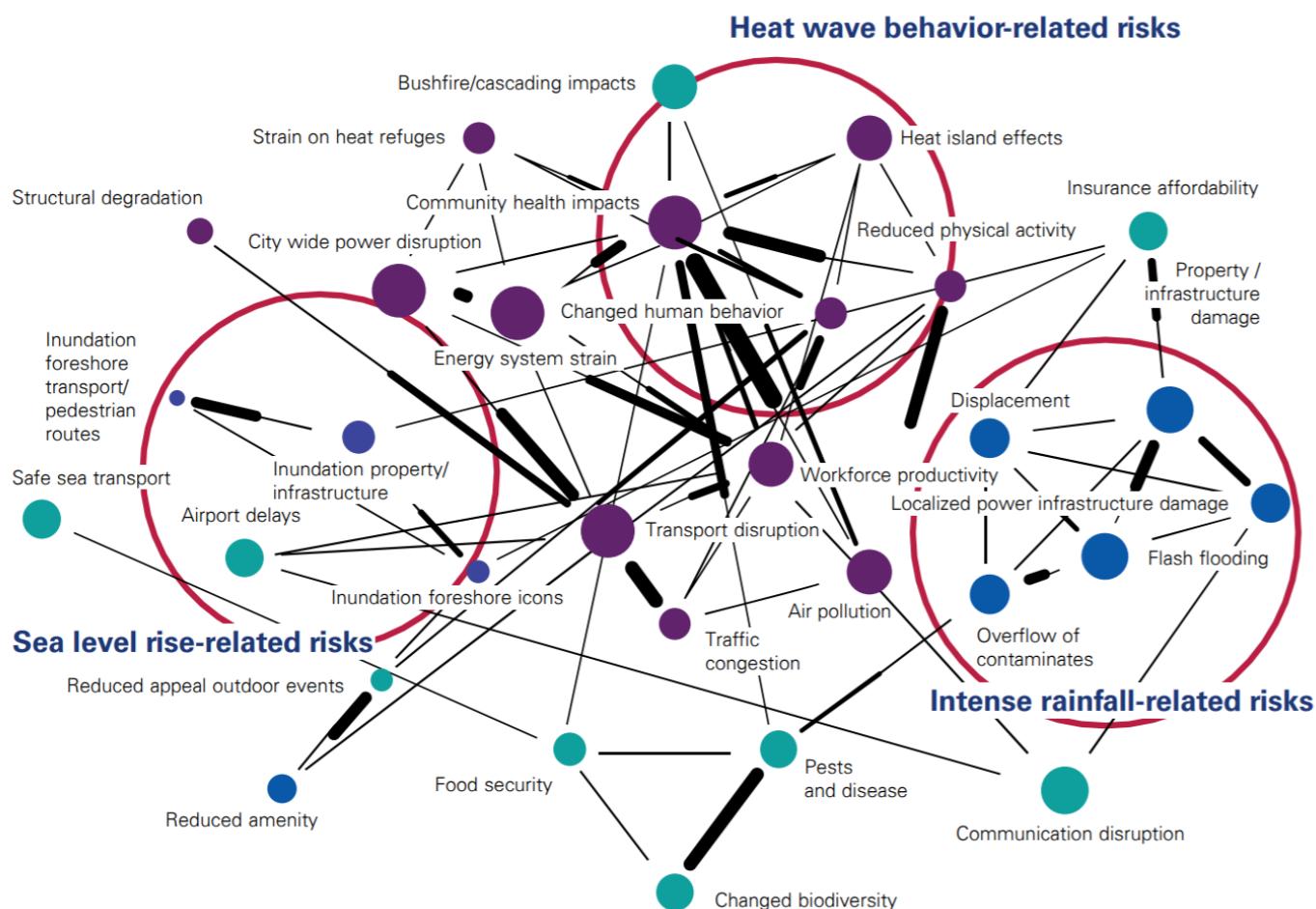
# Guidance

## Climate Change

### Risk and Audit Plan Considerations



An example of the KPMG Dynamic Risk Assessment. The colours, and size of the dots, demonstrate the likelihood and severity of the issue, whilst the thickness of the lines demonstrates the strength of the relationship between the various 'dots'. Such an exercise will help determine what should go on your annual plan.



**Image:** Dynamic Risk Map example prepared for the City of Sydney by KPMG.

**Source:** KPMG: Understanding Social and Environmental Risk

### 3

## Research

Your local regulations and laws.

This is not an easy area. Each country has a variety of rules, regulations, and some things which are in discussion / yet to be implemented. Generally, countries which have signed up to the Paris Agreement, are likely to have some form of legislation in place.

Currently, this appears to be regulated by the Financial Reporting Council (FRC) in the United Kingdom, as well as the Australian Securities and Investments Commission (ASIC) and Australian Prudential Regulation Authority (APRA) in Australia.

# Guidance

## Climate Change

### Risk and Audit Plan Considerations



It is recommended that you have an understanding of what laws are applicable to you as this will impact on our audit work to be performed.

#### 4

## Review

Your businesses preparedness and ability to respond.

Using the information gathered from **Step 2** and **Step 3**, we are able to understand the following about the business areas reviewed:

- Who is the most susceptible to climate change risks;
- Which are is most crucial to our customers;
- Which area is most under prepared; and
- Who is putting us at risk of not being compliant.

Rating the business areas, within consideration to our risk assessment performed also in **Step 2**, we can formulate an idea of who should be the focus of any detailed review.

It is important to look at the bigger picture. Where there is a general lack of preparedness, or large compliance risk, the auditor should take a step back and consider WHY. This could be because of the time from the top, where management has not seen this as an important factor, or it could be a lack of guidance being available or communicated to the business area. Regardless, we should be cautious to pass blame directly to the business area, as there could be multiple reasons as to why they are unprepared.

Where there is no organisation wide training, guidance, or poor management buy in, your initial review should focus on the high-level aspects of the business, and in particular, how to be compliant with any legislation.

If there is organisational guidance, or some level of preparedness, it is reasonable to begin a more granular and detailed review into the business areas.

The auditor, as part of their review, should consider:

- The realism of any plan;
- Awareness of the plan amongst staff and key team members;
- How the plan links / aligns to the risk assessment, any strategies, or business continuity plans;
- Ownership and maintenance of the plan; and
- Appropriateness of current disclosures within the Annual Report (where applicable).

A rolling review may be considered necessary for at risks areas. The risk assessment should be updated to continuously reflect the current risks to the business.

#### 5

## Report

What you have found.

The tone of the report is essential to ensure that we gain the right management buy in and participation. Where this is the first year of such a review being performed, it would be recommended to remove risk ratings from the report, and rather, provide 'Progressive Reporting'; a report which focuses on the actions and priority for completing them, with an explanation as to why; rather than the typical audit reporting approach of what was wrong, what's the implication, and what's the action.

'Progressive Reporting' will help remove any negative connotations associated with the review and focus more on the outcome and why its needed, rather that what the issue is and what they need to do.

# Guidance

## Climate Change

Risk and Audit Plan Considerations



More mature organisations with well embedded processes may see more benefit with standard audit reporting.

6

## Disclose

To shareholders and investors your position.

Depending on your location and reporting requirements, it is critical that you disclose your climate risks and associated implications in a clear, concise and accurate manner. Failure to do so may result in hefty penalties, or reputational risks for the business.

### Putting it on the audit plan

The above six steps will help you perform a baseline introduction review, or identify what areas are most at risks and should be considered for inclusion on the audit plan. Additionally, the information here can feed into an Audit Universe for future consideration.

Its important that these are constantly reviewed. Climate change was not previously considered to be an as substantial risk as it is today, and therefore, failure to frequently review these climate change risks may see your business fall behind.

## Conclusion

This is not a comprehensive guide, but rather a starter to help you and your business ensure that you are ready to face the varying climate change challenges which could directly impact your business.

My Audit Spot has a range of tools and templates which can assist with your review. Refer to our website to explore our range of tools and templates, blog posts, and resources.

If you have a question, email us at: [hello@myauditspot.com](mailto:hello@myauditspot.com).

# Subscribe

Click here to join our mailing list

