



Internal Control over Sustainability Reporting **ICSR**



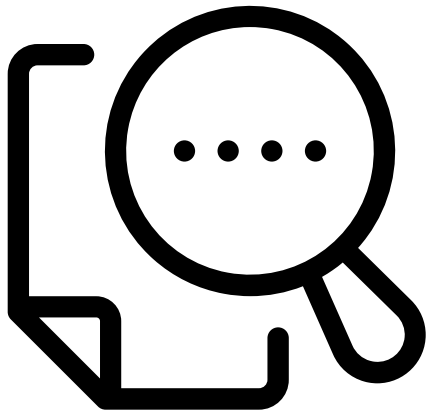
The INSTITUTO DE AUDITORES INTERNOS DE ESPAÑA (the Institute of Internal Auditors Spain) is a professional association founded in 1983, whose mission is to contribute to the success of organizations by promoting internal auditing as a key function of good governance. It has 4,100 members in Spain, who are internal auditors in the main organizations and institutions within all economic sectors in the country.

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Internal Control over Sustainability Reporting **ICSR**

 **ESSENTIAL GUIDES**
IAA SPAIN

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Instituto de
Audidores Internos
de España

Presentation.

At the Institute of Internal Auditors Spain, we understand that enhancing internal control not only enhances the reporting of information for financial markets, but also the management of organizations, since internal control provides structure and organizes complex processes, which increases the confidence of the different stakeholders.

This guide, promoted by the Institute of Internal Auditors Spain (IAI Spain), provides a solution to the need for organizations to respond to the accountability requirements for sustainability information in accordance with the principles and criteria established in the European regulations and standards, as well as in the local regulations that transpose them.

For the information reported to the markets to accurately reflect the impact of organizations on society and the environment, as well as the effects of ESG (Environmental, Social, and Governance) factors on the condition, performance, and evolution of the entity, organizations must implement an effective internal control system. This system should cover the entire process of preparing, validating, and publishing this information and ensure its quality.

The guide addresses the key elements that define an effective control system: the related regulations, the inherent characteristics of sustainability information, the roles of the different participants involved in its governance and oversight, the design and implementation of an ICSR (Internal Control over Sustainability Reporting) framework, as well as the key aspects and intervening parties, both internal and external, for its assessment.

For the development of this guide, the IAI Spain has brought together a group of experts from different sectors and professional backgrounds: Chief Audit Executives; Sustainability Directors; Risk Managers; internal audit and external verification professionals; internal control and reporting experts, as well as independent board members and supervisory body professionals (in the case of Public Interest Entities), who have shared their knowledge and experience to prepare this document, so that the Institute of Internal Auditors Spain can make it available to the interested public. Our thanks to all of them.

As of the date of issuance of this document, not specific methodological references for establishing an ICSR framework are available, so this Guide is presented as an innovative reference in this field that we hope will serve as orientation for the different professionals who have responsibility for Sustainability Reporting.

Institute of Internal Auditors Spain

Composition of the Working Group.

This Guide has been approved by the Institute of Internal Auditors Spain based on the work of a group of experts. Consequently, its contents do not necessarily reflect the individual opinions of the professionals who have contributed to its preparation, nor the position of the organizations for which they work. The experts who have been members of the Working Group come from different sectors and have a wide range of experience and expertise. This diversity has allowed multiple perspectives and approaches to be incorporated into the development of the document.

The members of the Working Group have collaborated selflessly, dedicating their time and effort to the common goal of enhancing the quality and effectiveness of Internal Control over Sustainability Reporting (ICSR). Their work has been instrumental in providing recommendations and guidelines to aid organizations and practitioners in implementing rigorous and sound assurance practices in this field.

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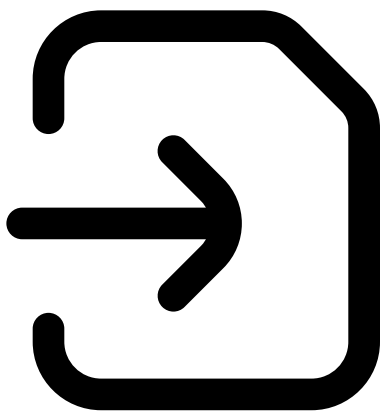
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Executive Summary



Executive Summary.

Objective and Scope of this Guide.

Sustainability reporting obligations require an internal control system that ensures the quality and reliability of the information, providing confidence to the Board of Directors (or other governing body), specialized committees and stakeholders, such as regulatory supervisors, analysts, and society as a whole, whereby the impact of organizations on the environment and society is accurately reflected.

The European sustainable finance disclosure regulation establishes specific requirements on internal control processes for the management of information on environmental, social and governance (ESG) aspects. Organizations should design and implement a system for Internal Control Over Sustainability Reporting (ICSR), taking advantage of synergies with other existing assurance models and promoting integrated controls. Internal auditors play a key role in the design, oversight, and continuous improvement of this system, providing objectivity and expertise to ensure its effectiveness.

In the absence of a specific guide, the Institute of Internal Auditors Spain has coordinated the development of this document with the contribution of experts from various sectors, providing guidance for the implementation of ICSR. The guide details key elements of the system, as well as roles and methodologies, addressing the responsibilities of the Boards of Directors, management, control functions and internal auditors. Maintaining this system updated will be essential as regulations evolve and experience is gained in its effective application.

Regulatory Framework.

The European Union's CSRD Directive, in force since 2023, regulates the disclosure of Sustainability Information for large companies and establishes a progressive implementation schedule according to the size and type of entity with the objective of harmonizing the presentation and assurance of information on ESG factors, requiring companies to disclose characteristics of their internal risk management and control systems related to this process.

In addition to CSRD, the European Sustainability Reporting Standards (ESRS) introduce specific standards, such as Disclosure Requirement GOV-5, detailing the related requirements and the integration of risk management into organizational functions. Additionally, regulatory bodies such as ESMA, the European Securities and Markets Authority, highlight the connection between financial and non-financial information as a priority for oversight.

In Spain, the transposition of CSRD is still pending, although the Bill for this purpose proposes amendments to the Commercial Code, the Corporate Enterprises Act (*Ley de Sociedades de Capital*) and the Statutory Auditing Law. It is necessary to highlight the importance of the Audit Committee oversight of internal control systems and the integration of good sustainability practices, supported by technical guides, such as that of the CNMV, which emphasize assurance and oversight of such systems.

The assurance of Sustainability Reports, introduced by CSRD, requires an accredited auditor or independent assurance provider to issue limited assurance reports. In Spain, this practice was already contemplated in Law 11/2018.

Sustainability Information: Definition and Characteristics.

According to the different European regulations, sustainability reporting covers environmental, social and governance (ESG) aspects. In the environmental section, it includes factors such as climate change, biodiversity, and use of natural resources, among others. In the social area, it focuses on labor relations, human rights, and transparency with consumers. For governance, it addresses business ethics, anti-corruption, and supplier relations. This information is cross-cutting and should be analyzed under the double materiality approach, considering both financial and social impacts.

To be useful, Sustainability Information must meet fundamental (relevance and faithful representation) and improvement (comparability, verifiability, and understandability) characteristics, which implies accurate, neutral, and traceable data, as well as clear time references. However, the constant development of standards and control tools represents an additional challenge to ensure their quality and reliability.

The main challenges include integrating sustainability at all levels of the organization, responding to the diverse demands of stakeholders and managing the complexity of reporting throughout the value chain. It is also necessary to address the topical diversity, the heterogeneity of indicators, the lack of specialized personnel and the regulatory differences between countries. To overcome these challenges, there must be a clear governance model, robust processes, and unification of criteria through specific manuals.

Scope Boundaries for Sustainability Reporting.

To set the scope boundaries for Sustainability Reporting, the following aspects are considered:

- Determination of the group of companies included in the financial statements to identify those that generate relevant data on ESG aspects, using a methodology that organizes indicators by topic, to ensure the inclusion of all relevant entities within the scope of the sustainability report, with an annual updating process to reflect structural changes.
- Extension of the assessment to encompass the organization's entire value chain, covering upstream and downstream phases of the business model. This analysis identifies key activities, agents and geographies involved in each stage, ensuring a comprehensive view of the associated impacts and risks. It also establishes the importance of periodically updating the value chain to reflect operational changes and improve data accuracy. In complex cases, justified estimates can be used to ensure proper representation.
- Double materiality assessment to identify impacts, risks, and opportunities (IROs) in sustainability issues: considering how business activities affect the environment and how these issues impact the organization financially. It includes the identification of relevant issues, their evaluation, the definition of materiality thresholds and their validation by senior management. This process ensures that the data disclosed is comprehensive and aligned with corporate strategy, fostering the integration of sustainability into risk management and strategic decision making.

Key roles in ICSR Governance and Oversight.

Three key roles can be identified for establishing the system for ICSR:

1. Management Functions

- Responsible for the collection, preparation, and control of sustainability information, considering double materiality and legal requirements.
- Multiple areas are involved (Sustainability, Risk, Finance, Human Resources, etc.), in charge of activities, such as defining reporting criteria, compiling information, and designing controls.
- A coordinating area oversees the consistency and comparability of the process, ensuring compliance with regulations and integration between financial and sustainability information.

2. Control Functions

- Ensure that controls are in place to mitigate risks associated with Sustainability Reporting.
- Tasks include ensuring the integrity of ICSR, assessing risks and controls, overseeing the execution of controls, and promoting process automation.
- They act as critical support for management, ensuring that controls are sufficient and effective.

3. Evaluation Function (Internal Audit)

- Performs an independent review of the design and effectiveness of the system for ICSR.
- Assesses risks and the model for governance and controls, issuing recommendations to improve the system.
- Provides confidence to the Board of Directors (or governing body) and stakeholders through periodic reviews and advisory activities, thereby strengthening risk management and internal control.

Role of Governing Bodies in Sustainability.

The integrity of Sustainability Reporting requires a sound governance structure that includes the Board of Directors, the Audit Committee and, where appropriate, the Sustainability Committee.

The Board has the ultimate responsibility for ensuring an effective ICSR, in promoting the internal control culture and overseeing sustainability reporting.

Specialized committees, such as the Audit Committee, oversee the effectiveness of internal controls and associated risks, while the Sustainability Committee, if in place, may propose ESG strategies and policies for approval. Collaboration between these committees is key to addressing financial and non-financial risks in an integrated manner. Mechanisms, such as joint meetings and coordinated risk management, are recommended to strengthen the effectiveness of the Board. In addition, its composition requires diverse profiles with knowledge and experience in sustainability, among other areas, as well as training and capabilities to address emerging issues, which are essential due to the constant evolution of standards and regulations.

Senior management plays a crucial role in allocating resources, developing policies, and ensuring transparency in accountability. Management's commitment is reflected in processes such as data certification and the linking of variable incentives to the quality of the information reported. This ensures that Sustainability Information is consistent, relevant and complies with regulatory standards, thus reinforcing stakeholder confidence in the organization.

The following additional aspects are also considered to ensure adequate governance and supervision of ICSR:

- **Formalization of the Governance Model:** Enables the establishment of segregated roles and responsibilities within the organizations, adapting them to their operational needs and regulatory requirements. Each entity must guarantee the independence and objectivity of its functions through mechanisms such as external assurance. To this end, it is crucial to document the Sustainability Reporting Governance Model, specifying areas, roles, and responsibilities for clear and efficient management.
- **Integration and synergies between existing control systems:** Allows for greater efficiency of the organizations' control system when the existing parallels between the Internal Control over Financial Reporting System (ICFR) and that for ICSR are considered, taking advantage of methodologies, controls, and tools. Likewise, other control models, such as compliance models, can complement the ICSR processes.

Conceptual framework for the design and implementation of ICSR.

The conceptual framework of the COSO ICSR model highlights the importance of having an effective ICSR, which ensures that the information reported is useful, faithful, and verifiable by third parties, and characterized by aspects such as accuracy, clarity, and neutrality. It integrates the following key elements:

- **Control environment:** in emphasizing the organization's commitment to ethics, through policies such as the Code of Ethics and the whistleblower channel. Senior management monitors compliance with sustainability objectives and promotes staff competence and training.
- **Risk assessment:** by applying double materiality criteria (impact and financial) to identify relevant risks, and considering internal, external, and technological changes, as well as specific risks such as errors, fraud or inconsistencies in the information provided.
- **Control activities:** by addressing identified risks through controls at entity, process, and technology levels, ensuring data quality and availability.
- **Information and communication:** This is fundamental for managing and communicating sustainability data in a transparent manner and adapting to the demands of the environment.
- **Oversight:** reinforces confidence in the information through periodic evaluations, ensuring that internal controls evolve along with the requirements, strengthening the reliability and quality of the reports.

ICSR encompasses various channels and formats for the disclosure of Sustainability Information, such as financial reports, corporate websites, and rating agency questionnaires, among others.

These disclosures can be based on regulatory frameworks (ESRS, ISSB, TCFD, SEC and GRI) to ensure that the data disclosed is relevant and useful to users, focusing on the material impacts, risks, and opportunities of organizations.

The use of prioritization criteria is suggested, given that it is not always possible to cover all the Sustainability Information, to implement ICSR efficiently. European standards include approximately one hundred disclosure requirements, encompassing some one thousand data points in sustainability reports, including narrative, semi-narrative, and numerical data, each with different inherent risks, though quantitative data is generally of higher risk. Although sustainability information is predominantly qualitative, its disclosure requires a detailed focus on the context of business activities, including strategy, risks and impacts in the short, medium, and long term. Furthermore, integrating value chain information presents additional challenges due to the reliance on third-party data.

The regulations require the inclusion of material disclosures not covered in the ESRS when they are relevant from a financial, environmental, or social perspective. To ensure the quality of this data, it is crucial that they are clearly defined or conform to accepted frameworks such as GRI or ISSB for ICSR to ensure the reasonableness and reliability of the additional information reported, thereby strengthening its usefulness for strategic decision making.

ICSR Risk Scoping.

Risks associated with the reporting of sustainability information arise from lack of internal controls and defined processes, which can result in information that is not aligned with regulations. Risk identification requires first defining and communicating the company's sustainability strategy, along with clear principles for measurement and reporting. Additionally, ICSR must ensure fundamental characteristics, such as information that is relevant, faithfully represented, comparable and verifiable.

Among the main risk factors, the following are identified:

- Failure to identify material issues, such as lack of clear objectives, allocation of resources and accepted methodologies for assessing impacts, risks, and opportunities.
- Reporting errors due to incorrect calculations, omission of data or lack of appropriate disclosures. The inclusion of value chain data and consistency with financial information represent additional challenges, especially in large organizations with international operations and uneven levels of maturity in their internal controls and risk management.
- Fraud, such as “greenwashing” or “social washing”.
- Cybersecurity, due to high digital dependency and exposure to threats such as ransomware.
- Regulatory changes.
- Disclosure of confidential information.
- Cultural change mandated by regulations.

ICSR Control Activities.

The specific control activities in an entity seek to mitigate risks of errors or irregularities in the Sustainability Reporting and are organized in three levels: entity, process, and IT controls.

- Entity Level Controls (ELCs): these are documented in risk and control matrices like those used in the ICFR, including ICSR policies and whistleblower channels, with annual reviews to ensure they are updated and traceable.
- Process-level controls: these are defined based on the double materiality assessment, and of the businesses or companies relevant to sustainability issues, thereby ensuring that identified risks are effectively addressed.
- IT controls: it is crucial to have an inventory of key applications and to establish general controls (e.g., access control management, backups, or segregation of duties), as well as application-specific (e.g., automatic reconciliations or parameter restrictions). Given the diverse nature of Sustainability Reporting, it is necessary to manage a larger number of applications than in ICFR, covering data of distinct types, such as CO₂ emissions or employee information, as well as applying an adapted methodology that facilitates data capture, processing and reliable reporting.

Documentation of ICSR processes and controls.

The following elements are considered for documenting ICSR:

- Procedure for calculating double materiality, aligned with the EFRAG Materiality assessment implementation guidance Materiality Analysis Implementation Guide issued jointly by EFRAG and the *Instituto de Contabilidad y Auditoría de Cuentas* (ICAC).
- Identification of relevant business processes that affect Sustainability Reporting, based on a double materiality assessment.
- ICSR manual with the Sustainability Reporting procedure, describing the activities to be conducted by the areas involved to ensure the correct reporting of information.
- Reporting instructions on disclosure requirements for Sustainability Information, in the style of the guidelines and procedures governing the preparation of financial information.
- Risk and control matrices.
- Roles and responsibilities matrices.
- Detailed ICSR policy and manual that incorporates the procedure for internal control and oversight of Sustainability Reporting.
- Flow charts or narratives describing the process for calculating and reporting the main quantitative and qualitative indicators.
- Systems map and risk matrix, as well as IT General Controls (ITGCs) linked to Sustainability Reporting.

Maintenance, updating and oversight of ICSR.

The effectiveness and efficiency of ICSR requires regular maintenance, updating, and oversight of its operation and its adaptation to changes in the environment through an annual internal control plan:

- Maintenance and Updating: involves periodic updating of ICSR coverage (scoping); annually or in the event of significant changes, assessing risks for the required scope and determining whether the model is still valid for the company's situation, whereby documentation is updated. Accurate and updated records are maintained of processes, procedures, and policies, updating manuals and guides, as necessary.
- Oversight: regardless of the activities performed by Internal Audit within its plan, it is typically assigned the function responsible for the maintenance of ICSR considering aspects such as: periodic review of controls, periodic oversight of certain elements that are beyond normal controls (e.g.: key activities and transactions to identify irregularities and deviations with automated monitoring tools), and a diagnosis of ICSR, integrating a theoretical analysis of the model with respect to best practices or methodological frameworks.
- Report to governing, management and supervisory bodies on the assessment of the design and effectiveness of ICSR, including material weaknesses, relevant changes, and performance (performance indicators linked to ICSR).
- Communication and training plan for the areas involved in ICSR.
- Supporting technologies for information processing and internal control.

Assessment of ICSR.

During the ICSR assessment, risks and internal control deficiencies that could affect the fulfillment of its objectives are identified. Inspiration for implementation of this can be drawn from the set of recommendations on internal control over financial reporting (ICFR) by The Internal Control Working Group (ICWG) that was set up at the instance of the CNMV, as well as the guides issued by COSO. The ICSR assessment should consider the status of implementation and degree of development of ICFR. It is expected that the level of maturity of ICSR will progressively increase to the point that it can be subject to verification with reasonable assurance, as contemplated by CSRD.

To carry out the assessment, the following elements are proposed:

- Evaluation of the design of existing internal control structures: This begins with an understanding of the organization's strategy, governance model, risks, and specific factors in this area. An analysis of the ICSR implementation approach is essential, considering criteria such as double materiality, complexity of information, and associated risks, including IT and value chain controls, focusing on their adequacy and effectiveness.
- Assessment of the functioning of controls to verify whether they operate as expected, considering factors such as their design, type (manual or automatic), periodicity and effectiveness. This is done through review techniques (interviews, observations, inspections) and assessment of documentary evidence.

- Evaluation of weaknesses: where failures are discovered, their impact on the integrity and reliability of the data is assessed, classifying the severity of the findings and proposing improvements.

Additionally, the training and awareness of those who supervise and execute the controls is promoted.

- Frequency and scope of evaluations: This will vary depending on the nature of the organization, its regulatory environment, and inherent risks. Annual, quarterly, or continuous assessments are recommended, as well as specific reviews in the event of significant changes, prioritizing critical indicators, relevant processes and regulatory or strategic factors, or requirements based on the Board of Directors' judgement.
- Certification of Sustainability Reporting: a formal certification process or structure can be implemented in ICSR on an annual basis, coinciding with the preparation of the Sustainability Report, which must provide a series of assurances determined by the responsibility of the person signing the certification.

Internal Audit Function.

Internal Audit plays a key role in supporting the Board of Directors in the oversight of ICSR, through a model of periodic assessment of the system to ensure its correct design and operation, involving the identification of deficiencies and areas for improvement, and reviewing the information preparation process to ensure its integrity and transparency, in coordination with external assurance providers.

The review by Internal Audit, which must always maintain its independence and objectivity, may cover the following aspects:

- Governance.
- Policies and recognized frameworks.
- Consistency and comparability of data.
- Risk management and the information preparation processes.
- Availability and certification of relevant data, ensuring the correct boundaries of reporting and compliance with defined methodologies.

In the initial stages of ICSR implementation, the review will be adapted to the degree of maturity of the system, prioritizing aspects of greater criticality, such as the double materiality assessment or data capture processes.

External Assurance.

The external assessor can play two main roles in relation to Sustainability Reporting:

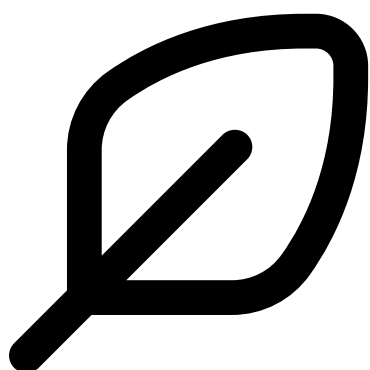
- Verification of Sustainability Reporting: CSRD requires an independent external verification of the report to ensure that it complies with current reporting standards. This process begins with a limited level of assurance and will evolve to reasonable assurance from 2028 onwards, thereby

providing greater confidence in the information reported. While the external assessor does not issue a specific conclusion as to the effectiveness of ICSR, significant weaknesses may be identified during the review, which will encourage the continuous strengthening of the internal control systems.

- ICSR evaluation: Governing bodies may voluntarily commission an ICSR assessment to reinforce the reliability and effectiveness of the internal control system. This engagement, which may include limited or reasonable assurance, seeks to strengthen stakeholder confidence, ensure regulatory compliance, validate the integrity of documentation, and prioritize risks. Furthermore, the report's findings and recommendations contribute to the continuous improvement of ICSR, thus increasing the credibility of internal processes and facilitating the implementation of robust controls.



Introduction



Objective and scope.

The reporting obligations in relation to Sustainability Information of organizations and their governing bodies, which derive from European Union legislation and its transposition into the regulations of the Member States, require that internal control be in place over the information generated.

This system must be robust and capable of providing confidence to the main stakeholders involved: the Board of Directors (or governing bodies) of the organizations, specialized committees, if they exist (mainly the Audit and Sustainability Committees, although the latter is not common in all entities) and other stakeholders potentially using this type of information, such as supervisors, analysts or society as a whole.

Sustainability reporting is an essential element for the accountability of organizations to their stakeholders, as well as for decision making based on environmental, social and governance (ESG) criteria. The European Union has established a regulatory framework for sustainability reporting to harmonize requirements, improve data comparability and increase the confidence of users of this type of information.

Specifically, the Corporate Sustainability Reporting Directive (CSRD), in the Disclosure Requirement GOV-5 of the European Sustainability Reporting Standard #2, expressly addresses the internal control processes related to the generation and publication of Sustainability Information. This implies that organizations should describe how they internally manage and monitor the Sustainability Information they disclose, ensuring the accuracy and completeness of this data.

Organizations must prepare and publish a Sustainability Report periodically, following the principles and criteria established in European regulations and directives, as well as in the local regulations that transpose them. This information must faithfully and transparently reflect the impact of organizations on society and the environment and, therefore, their contribution to sustainable development, as well as the effects of ESG matters on the situation, performance, and evolution of the entity.

To ensure the quality, relevance, reliability and transparency of Sustainability Reporting, organizations must have an effective internal control system that covers the entire process of preparation, validation, and publication of the aforementioned information. This internal control system must be aligned with the principles and criteria established in international regulations and standards and adapted to the specific characteristics and risks of each organization.

Moreover, the design and implementation of an ICSR system should consider the existing synergies between the methodologies of other assurance models within the organization (Internal Control System for Financial Information, compliance models, etc.), in addition to leveraging controls contemplated in these models.

In relation to this system, internal auditors play a key role from a two points of view: first, in an advisory capacity for the design and implementation, and second, regarding oversight, since their experience, independence and comprehensive vision of the organization can provide great value in assessing the adequacy and effectiveness of this internal control system, identifying areas for improvement and recommendations for its optimization and continuous improvement. In this regard, it is essential to ensure that internal auditors maintain their objectivity and independence, as contemplated in the Global Internal Audit Standards.

Although there are control frameworks and methodologies that may be partially applicable, a comprehensive Guide does not exist for professionals in this field and other users of this information to help develop and implement, in a specific manner, a system of internal control for these characteristics.

Considering the challenges associated with the implementation of an Internal Control System for Sustainability Reporting, the Institute of Internal Auditors Spain has brought together a group of experts from different sectors and professional fields to respond to this need and advise the Institute in the preparation of this Guide. Chief Audit Executives; Sustainability Managers; Risk Managers; specialized internal audit and external assurance professionals in this type of information; internal control and reporting experts, as well as independent board members and professionals from the supervisory body (in the case of public interest entities) have all shared their knowledge and experience to produce this document and for the Institute of Internal Auditors Spain to make it available to the interested public.

The main purpose of this Guide is to provide orientation to assist organizations in developing and implementing ICSR, as well as to internal auditors and the governing bodies that have responsibility for overseeing Sustainability Reporting and the related internal control system.

Starting from the regulatory framework for sustainability reporting in the European Union, with special attention to the Corporate Sustainability Reporting Directive (CSRD¹), the European Sustainability Reporting Standards (ESRS²) and the Environmental Taxonomy regulation, this Guide describes the different key elements of ICSR, as well as the participants that influence its design and implementation, taking the COSO framework as a reference.

Additionally, it describes the role and functions of the participants, including those of internal auditors, in relation to Sustainability Reporting and the associated internal control system, as well as the most important methodologies and tools that may be used so that the Internal Audit Function and external independent assurance providers of Sustainability Reporting have a reference for carrying out their work in this area.

Finally, it describes the role and responsibilities of the Board of Directors (or other governing body) and, if applicable, of its specialized committees (e.g., the Audit and/or Sustainability Committees, if in place), involved in the process of overseeing Sustainability Reporting and its internal control system.

There are few specific methodologies for establishing an ICSR system as of this document's issuance date. Therefore, this Guide is presented as an innovative reference in this field. However, it will be important to update its content as new regulatory developments emerge or as experience is gained in relation to its application in the future.

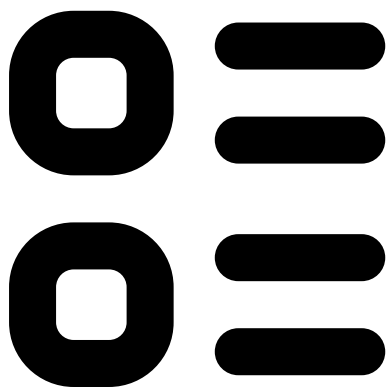
¹ Corporate Sustainability Reporting Directive (CSRD).

² European Sustainability Reporting Standards (ESRS).

Part I

Sustainability

Information Basics and
Legislation



1. Regulatory Framework.

1.1. European Union regulations.

1.1.a) Corporate Sustainability Reporting Directive (CSRD).

Directive (EU) 2022/2464 EU of 14 December 2022 on Corporate Sustainability Reporting (CSRD³), which came into force on 5 January 2023, is the applicable European standard at the time of this Guide's issuance with regard to the disclosure of Sustainability Reporting for large public interest companies with more than 500 employees. For the remainder of the entities bound by CSRD, the national regulations implementing Directive 2014/95/EU (NFRD⁴), regarding the disclosure of non-financial information, shall remain in force on a transitional basis, where applicable.

When?	Who?
In 2025 for fiscal year 2024 employees.	Large public-interest companies with more than 500
In 2026 for fiscal year 2025	Remainder of large companies (+250 employees and/or turnover of €50 million and/or total assets of €25 million)*
In 2027 for fiscal year 2026	Listed small and medium-sized enterprises (SMEs)** (except micro-enterprises), small and non-complex credit institutions (public and private), and captive insurance and reinsurance undertakings.
In 2029 for fiscal year 2028	Non-European companies generating a turnover of €150 million in the EU which have a subsidiary or branch in the EU above certain thresholds.

* Thresholds set after the amendment of Directive 2013/34/EU in December 2023.

** Each SME may choose to defer the obligation and not prepare it until fiscal year 2028 (publication in 2029).

According to CSRD, which aims to improve the framework for the presentation and assurance of Sustainability Disclosures, the content of Sustainability Disclosures should be based on the European Sustainability Reporting Standards. CSRD refers to the fact that these standards should specify the information that companies should disclose on governance factors, which should include information on the organization's internal control and risk management systems in relation to the Sustainability Reporting process.

1.1.b) European Sustainability Reporting Standards (ESRS).

The Commission Delegated Regulation (EU) 2023/2772⁵ of 31 July supplemented the Directive 2013/34/EU by adopting the first set of disclosure rules for Information on Sustainability.

³ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32022L2464>

⁴ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014L0095>

⁵ https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202302772

The ESRS, developed by EFRAG⁶, consists of twelve general standards, including two that are cross applicable to all sustainability issues.

ESRS 2, General Information, includes a section on Governance, which aims to establish disclosure requirements for understanding the governance processes, controls, and procedures in place to control, manage and oversee sustainability issues. This section includes five disclosure requirements.

Disclosure Requirement GOV-5 establishes that the organization shall disclose the key features of its risk management and internal control system in relation to the Sustainability Information disclosure process and, in particular, the following information:

- The scope, key features, and components of risk management and internal control processes and systems related to Sustainability Disclosures.
- The approach used for risk assessment, including the methodology for risk prioritization.
- The main risks identified and the strategies to mitigate them, including related controls.
- A description of how the company integrates the findings of its risk assessment and internal controls regarding the Sustainability Disclosure process into relevant internal functions and processes.
- A description of the periodic reporting of the findings mentioned in the previous point to the governing, management, and supervisory bodies.

1.1.c) EFRAG⁷ guidelines for the Implementation of ESRS.

In May 2024, EFRAG published three companion guides to assist in the implementation of the ESRS:

- EFRAG IG 1 on Materiality Assessment.
- EFRAG IG 2 on the Value Chain.
- EFRAG IG 3 on ESRS Data Points⁸.

1.1.d) European Environmental Taxonomy.

Regulation (EU) 2020/852⁹, and subsequent delegated regulations developing and supplementing it, establish progressive disclosure obligations on how and to what extent the activities of required organizations qualify as environmentally sustainable. Such information must form part of the Sustainability Report and is therefore affected by Disclosure Requirement GOV-5 of ESRS 2.

⁶ European Financial Reporting Advisory Group.

⁷ <https://www.efrag.org/en/projects/esrs-implementation-guidance-documents>

⁸ Data points are a list of specific units of information created by EFRAG, which must be reported according to ESRS, defined to meet the reporting requirements of CSRD.

⁹ <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852>

1.2. Current Regulations in Spain and other standards.

1.2.a) National transposition of European standards CSRD-ESRS.

At the date of publication of this document, CSRD has not yet been transposed into Spanish law. According to the current draft law¹⁰ (bill) to transpose this Directive, there will be modifications in relation to Sustainability Information in the Commercial Code, the revised text of the Corporate Enterprises Act (TRLSC), and Law 22/2015 regarding Statutory Auditing.

1.2.b) ESMA: Priorities and guidelines.

In the last quarter of each year, the European Securities and Market Authority (ESMA)¹¹ publishes the common supervisory priorities for the following year regarding implementation of European regulations in annual financial reports.

In its document for the Non-Financial Reporting Statements (NFRS) 2023¹², it highlighted the role that governing bodies and Audit Committees should play in ensuring that there are internal control and due diligence procedures on the data used. The quality of non-financial reporting data and transparency regarding such quality was one of the supervisory priorities for 2022 Non-Financial Information Statements¹³. Similarly, the document: *European common enforcement priorities for 2024 corporate reporting*¹⁴ of October 24, 2024, highlights the importance of the connection between financial and non-financial information since it is essential to provide a complete and consistent view of the situation and performance of organizations.

In July 2024, the ESMA also published its guidelines for national authorities on the supervision of Sustainability Information¹⁵ (GLESI), in accordance with the obligation introduced by CSRD. Such supervision consists of examining whether the aforementioned information is prepared in accordance with the applicable regulatory framework, taking appropriate action when non-compliances are identified in the supervision process.

1.3. Other references.

1.3.a) Annual Corporate Governance Report (ACGR).

Article 540 of the revised text of the Corporate Enterprises Act, approved by Royal Decree 1/2010, of July 2, 2010, requires listed companies to annually publish a corporate governance report providing a detailed explanation of the structure of the company's governance system and how it operates in practice.

¹⁰ Bill pending since 11/15/2024.

¹¹ Regulatory and supervisory body for financial markets in the European Union.

¹² https://www.esma.europa.eu/sites/default/files/2023-10/ESMA32-193237008-1793_2023_ECEP_Statement.pdf

¹³ https://www.esma.europa.eu/sites/default/files/library/esma32-63-1320_esma_statement_on_european_common_enforcement_priorities_for_2022_annual_reports.pdf

¹⁴ ESMA32-193237008-8369 European common enforcement priorities for 2024 corporate reporting

¹⁵ https://www.esma.europa.eu/sites/default/files/2024-07/ESMA32-992851010-1600_Final_Report_on_Guidelines_on_Enforcement_of_Sustainability_Information_GLESI.pdf

National Securities Market Commission (CNMV) Circular 5/2013, as amended 3/2021¹⁶, establishes the models to be used in the report, which specifically include:

- 1) In section E, a description of the financial and non-financial risk control and management systems.
- 2) In section G, the degree of compliance with the recommendations of the Good Governance Code of Listed Companies¹⁷, under the “comply or explain” principle, including recommendations on sustainability.

1.3.b) Board of Directors and Audit Committee.

According to Article 253 of the revised text of the Corporate Enterprises Act, directors must prepare the annual accounts and management report, including the Statement of Non-Financial Information where appropriate.

Regarding listed companies, Article 529 *ter* includes, among the non-delegable powers of the Board of Directors, the supervision of the process of preparation and presentation of the aforementioned information. This article also states the requirement for establishing an Audit Committee.

Similarly, in accordance with the Draft Bill for the transposition of the CSRD, the revised text of the Corporate Enterprises Act will be amended to include references to Sustainability Information. In particular, in Article 529 *quaterdecies*, it is mentioned that the following minimum functions of the Audit Committee will be included:

- Oversight of the effectiveness of internal control, internal audit, and risk management systems, as well as discussions with the statutory auditor and the Sustainability information independent assurance provider regarding significant weaknesses of the internal control system detected during the audit and assessment.
- Supervision of the process of preparation and presentation of the mandatory financial and sustainability information.

Regarding internal control and information systems, the Code of Good Governance of Listed Companies recommends that the Audit Committee oversee: (i) the preparation and integrity of both financial and non-financial information¹⁸; and (ii) the systems for managing and controlling financial and non-financial risks¹⁹.

Finally, the CNMV Technical Guide 1/2024 on Audit Committees of Public Interest Entities²⁰, published on July 1, 2024, defines a set of recommendations and best practices. It updates the first version from 2017 and incorporates the role of the Audit Committee in relation to Sustainability

¹⁶ https://www.boe.es/diario_boe/txt.php?lang=es&id=BOE-A-2021-16391

¹⁷ https://www.cnmv.es/DocPortal/Publicaciones/CodigoGov/CBG_2020_ENen.PDF

¹⁸ In accordance with the CNMV's GT 1/2024, non-financial information is defined generically as any periodic corporate information published by the public-interest entities (PIEs) other than financial statements, such as the report and the various reports contained therein. Non-financial information includes information on Sustainability.

¹⁹ According to the CNMV's GT 1/2024, non-financial risks refer to risks that are not directly financial in nature, though they may have a financial impact. These include political, strategic, legal, reputational, and cybersecurity risks, among others. risks, also including sustainability risks.

²⁰ https://www.cnmv.es/DocPortal/Legislacion/Guias-Tecnicas/GT_ComisionesAuditorias_en.pdf

Information. Section 3 deals with the oversight of financial and non-financial information and specifically refers to:

- Understanding of the internal control system for financial and non-financial information and assessment of its effectiveness.
- Reviewing, analyzing, and discussing the financial statements and other relevant non-financial information with management, internal auditors, external auditors, and the Sustainability Reporting assessor.
- Promoting and supervising a system that allows for reporting irregularities to the Audit Committee, especially those of financial, accounting or sustainability-related significance.

In this regard, one should be reminded that the main objective of this Guide is to offer a set of best practices for developing and implementing ICSR and, therefore, when speaking of non-financial information, it focuses on sustainability information.

It should be noted that Article 22.3 and 4 of Law 6/2023 of March 17 on Securities Markets and Investment Services²¹ states that the CNMV may require explanations from supervised entities and groups that deviate from the criteria, practices, methodologies or procedures indicated in their technical guides, or in those others endorsed and approved by other international bodies or committees that are involved in the regulation and supervision of the securities market.

1.3.c) Sustainability reporting verification.

CSRD introduces, at a European level, the requirement for verification of Sustainability Reporting by statutory auditors and/or other accredited assurance services providers. This aspect was already incorporated into Spanish Law 11/2018. In this sense, the *Instituto de Censores Jurados de Cuentas* and the *Registro de Economistas Auditores* issued guidelines for this purpose, most of which are used by independent assurance providers to issue their limited assurance reports under ISAE 3000²².

The European Commission will expand CSRD to establish limited assurance standards and will assess the practicality of issuing reasonable assurance standards through delegated acts no later than 1 October 2026 and 2028, respectively. Prior to this, Member States may issue rules for national implementation.

In this regard, the Spanish Accounting and Auditing Institute, *Instituto de Contabilidad y Auditoría de Cuentas (ICAC)*²³ created a working group with the aim of preparing the first standard regarding limited assurance, whose objective is to provide a response in the first years of implementation of the CSRD to the expected requirements for assurance. A notice regarding this standard was published on 18 December 2024, and it will be approved once the law transposing the CSRD enters into force.

The assurance provider's responsibility includes incorporating acknowledgement of the control system for Sustainability Information, given that, and in accordance with the Draft Bill, one of the amendments to Law 22/2015 on Statutory Auditing will affect its Article 7^{ter} regarding the assurance report for Sustainability Information, by indicating that the independent assurance provider will include "an opinion on whether the Sustainability Information complies with the presentation standards adopted by the European Union, and the entity's process for identifying the Sustainability Information to be included in the Management Report".

²¹ <https://www.boe.es/buscar/act.php?id=BOE-A-2023-7053>

²² International Standard on Assurance Engagements 3000.

²³ <https://www.icac.gob.es/>; Assurance of sustainability information | ICAC

2. Sustainability Information.

2.1. Definition.

In accordance with Directive (EU) 2013/34, of June 26, on financial statements, as amended by Directive (EU) 2022/2464, of December 14 (CSRD), and the related regulations for implementation in Spain²⁴, Sustainability Information is understood as information on environmental, social and governance aspects. Further details on these three areas are provided below:

- **Environmental (A):** covers issues related to climate change, the circular economy, water and marine resources, pollution, biodiversity, and natural resource usage.
- **Social (S):** this refers to information on the management and relations established with the company's own workforce, value chain workers, customers and affected communities, covering issues such as working conditions (diversity and inclusion, training, compensation, management, health and safety, etc.), human rights, and commitment and transparency with consumers.
- **Governance (G):** covers corporate culture, ethics, anti-corruption, bribery, governance bodies, compliance, competitive behavior, and supplier relations, including payment practices.

Sustainability information is broad and transversal, thereby reporting should be based on a double materiality assessment²⁵, which makes it possible to identify and prioritize the impacts, risks and opportunities related to environmental, social and governance issues, according to their relevance for each organization.

2.2. Qualitative characteristics.

In accordance with ESRS provisions, as mentioned in section 1.1. b) above, the Sustainability Information must comply with five qualitative characteristics, classified into two categories:

a) Fundamental:

- *Relevance:* the information must be useful for decision making, as it can make a difference in users' decisions, applying a double materiality approach.
- *Fair representation:* the information should be (i) complete, i.e., include all material information necessary for it to be understood by users), (ii) neutral, i.e., unbiased in its selection or disclosure, and (iii) accurate, i.e., free from material misstatement, with accurate descriptions, estimates, clearly indicated approximations and forecasts, reasonable assertions, and based on sufficient and quality information.

²⁴ https://www.cnmv.es/DocPortal/Legislacion/Guias-Tecnicas/GT_ComisionesAuditorias_en.pdf

²⁵ Although the term used in the ESRS is "double relative importance", the Working Group involved in the preparation of this document has decided to use the term "double materiality", as it is considered widely known by the public. The concept of "double materiality" is discussed in detail in Section 2.4 Scope of Sustainability Reporting of this document.

b) Enhancing Information:

- *Comparable*: with information that can be referred to from previous periods, either from the organization itself or provided by other organizations or the sector in which it operates.
- *Verifiable*: traceable and can be reviewed/corroborated, which implies that several well-informed and independent observers could reach a consensus regarding its faithful representation.
- *Understandable*: clear and concise so that it can be understood by different users.

To comply with all these characteristics, it is essential to implement adequate internal processes and controls. Currently, this represents an additional challenge for Sustainability Reporting, as it is in a constant phase of development and evolution.

2.3. Primary challenges of Sustainability Information.

The following is an overview of the primary challenges faced by Sustainability Reporting to meet the qualitative characteristics mentioned above:

- **The need to strengthen corporate culture and awareness**: it is necessary to continue enhancing so that all levels of the organization, including Senior Management, recognize the importance of measurable, reliable, and quality Sustainability Information. Implementing and monitoring sustainability objectives tied to variable compensation, along with training and certifications at all levels, from the operational level up to the person who is ultimately responsible, ensures that each area is a guarantor of the veracity of the information it provides, gradually integrating this responsibility across all company layers.
- **Content conditioned by the requirements of stakeholders and information users**: the Sustainability Report must respond to the requirements and expectations of the different stakeholders and information users to whom it is addressed (investors, analysts, clients, regulators, NGOs, activists, employees, suppliers, the community, etc.). This may give rise to the risk that the reports are overloaded with content when trying to satisfy the information needs of all these stakeholders, since such reports are also used as communication tools by organizations.
- **Lack of maturity of reporting and control standards**: regulatory sustainability standards are still very recent since they arose for the first time in Directive 2014/95/EU (transposed in Spain by Law 11/18 on non-financial information and diversity) and later replaced by CSRD in 2022. Regarding internal control, COSO published the first specific control standard for Sustainability Reporting in 2023²⁶.
- **Broad scope of reporting**: sustainability requires reporting not only on the company's own operations (controlled companies), but also along its value chain, including upstream and downstream.

²⁶ Achieve effective internal control over Sustainability Reporting:
www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

- **Information based on different time horizons:** the Sustainability Report contemplates several time horizons: short term (reference period in the financial statements); medium term (five years from the end of the short term reference period) and long term (more than five years), which adds complexity to the report, as it must include future projections and value judgments, as well as analysis over time.
- **A broad spectrum of issues:** sustainability covers a range of quite different issues, and each organization must identify and prioritize those that are relevant to ensure effective reporting. For example, it makes sense for an energy company to give higher priority to reporting on climate change management, while a beverage company may focus more on water management.
- **Indicators with heterogeneous units of measurement:** Sustainability Reporting includes quantitative indicators with various units of measurement, from data points expressed, for example, in tons of waste, euros, kWh or cubic meters of water in environmental matters, to data points with regard to social matters that are measured in people or number of complaints. Furthermore, CSRD introduces data points that combine financial and sustainability sources, such as the expected financial effects of physical and transitional material risks. Moreover, Sustainability Reporting is notable for including a high degree of qualitative in addition to quantitative requirements.
- **New responsibilities within the organization:** Currently, many reporting units (companies or locations) do not have specific departments responsible for preparing certain Sustainability Information, such as information related to waste or climate change.
- It is crucial to establish a **clear governance model** (see point 3 *Governance and Oversight of Sustainability Reporting* in this Guide) and to designate those who will be responsible for reporting and control, in alignment with those who manage the information and set its objectives and monitoring.
- **The need for specialized and qualified personnel:** CSRD requires detailed and accurate reporting on ESG issues, which requires trained professionals with a prominent level of technical knowledge, advanced data analysis skills and a solid understanding of the regulatory framework.
- **Sustainability materiality:** This involves two perspectives as outlined in Section 2.4 *Scope of Sustainability Information* of this Guide. It considers how sustainability factors affect the company's financial position (financial materiality) and how the company's operations impact the environment and society (impact materiality).
- **Decentralized information sources and manual processes:** Currently, Sustainability Information is collected from various sources and primarily through manual processes, which are supported by limited and inconsistent tools across different reporting units.

In addition to these challenges, companies operating in different countries may be subject to local regulations or standards different from the global ones. Thus, it is essential to develop a "Sustainability Reporting Manual" that minimizes variation and provides a documented method when differences are unavoidable.

2.4. Scope of Sustainability Reporting.

The scope of Sustainability Reporting will be determined through an integrated process considering three interconnected elements, conducted in tandem and in parallel:

2.4.1. Review of all companies included in the reporting organization's financial statements.

The group of companies in the consolidated financial statements (parent company and all subsidiaries) must be reviewed and clarified for the Sustainability Reporting to identify which specific companies generate information for the different ESG issues.

The following process can be followed:

- a) **Obtain the corporate scope of the financial statements:** the financial area will have a list that reflects each of the companies that make up the consolidated Group, as well as the associated entities and those under joint control. It is recommended to include each company's consolidation method, ownership percentage, and the country in which it operates.
- b) **Review the data points required by the CSRD:** in parallel, and using the double materiality assessment as a reference, obtain the detailed EFRAG data points required by the European Sustainability Reporting Standards, which include approximately one hundred disclosure requirements affecting the organization. Given that EFRAG proposes approximately one thousand data points²⁷, the process can be made more efficient by taking quantitative indicators as a reference (although for a complete and exhaustive analysis it is recommended that qualitative indicators also be analyzed), which are mandatory and material for the company.
- c) **Create topics according to the nature of the data points:** the data points will be grouped into different sustainability topics, depending on the criteria to be met by each set of companies. This may involve adjusting the corporate scope of the financial statements according to the CSRD data requirements. For example, all the indicators on Own Workforce (ESRS S1) may meet a corporate criterion of "all group companies controlled by the organization with employees" and may be grouped under the same reporting topic, whose name could be "Own Workforce". This ensures the consolidated data points for the "Own Workforce" topic (workforce and diversity, salaries, training, health, and safety, etc.) include aggregated data from all controlled companies with employees.

Another example could be the indicators related to Scope 1 and 2 energy consumption and emissions (ESRS E1). The corporate criterion could be "all companies controlled by the Group with assets or employees," grouped under a different category called "Scope 1 and 2 energy and emissions."
- d) **Identify those responsible for each topic:** including those responsible for reporting or owners of the information for each topic and validate with them whether the established criteria (which determine whether to include or exclude a company) are consistent.

²⁷ At the date of preparation of this Guide, the sectoral disclosure requirements under the European Sustainability Reporting Standards are pending publication.

Based on the established topics and their criteria, the corporate scope of the financial statements may be adapted to the sustainability report, ensuring the disclosure of information relating to the entire consolidated Group.

Although it can take different formats, it is proposed to use a matrix format with the first column listing the Group's companies in detail, and the first row identifying various sustainability topics (e.g., Own Workforce, Energy and Scope 1 and 2 emissions or suppliers, among others). This matrix must indicate each of the companies that generate data for the different ESG topics.

Given the diversity of situations that may arise, the main aspects to be considered when determining one's own operations are listed below:

- Some companies may be irrelevant for sustainability purposes, while others present key material impacts, risks, and opportunities on specific ESG issues.
- It is necessary to update corporate group information at least annually, usually by the financial area, to reflect on any changes (new companies, deregistration of companies and other structural changes) and to distribute this update periodically to those responsible for each sustainability topic. For reporting and assurance of the information, it is recommended to perform the update at year-end, so that the data reported refers to the companies that have formed part of the scope during the year; if there is pre-verification in the third quarter, it can also be performed at this time.
- A review should be conducted at least annually to determine whether companies previously excluded from a topic have begun to meet the established criteria. For example, for the topic "Own Workforce", verify if an excluded company has hired employees between fiscal years to determine if it should be included.
- There will be indicators that refer to the "value at year-end" (e.g., total headcount at year-end) and others that refer to the "sum of values during the year" (e.g., occupational illnesses). For the latter, it is important to include the data of companies that were part of the consolidated Group during the year, but which have ceased to do so prior to the end of the year.
- The criteria established for each topical area must guarantee the integrity and completeness of the information, covering all the companies that generate data related to the topical area in question. In situations where information is widely distributed among companies, parameters for representativeness or materiality can be established, provided they are documented. These parameters can be based on either quantifiable coverage or, in some cases, qualitative criteria to justify the exclusion of certain less significant companies²⁸. Thus, provided that it is documented, a representativeness parameter can be established to ensure that it reflects a true and fair view of the Group.

²⁸ In consolidated groups that manage a large volume of controlled companies (e.g. 300-400), collecting data may require a very significant effort. In these cases, a representativeness/materiality analysis could be performed and the dispersion of the data assessed. For example, if 99% of the data is concentrated in one hundred companies, while the remaining 1% is distributed among another 100 companies, it is advisable to establish documented thresholds to exclude less significant companies, provided that this is justified and ensures an accurate representation of the Group's actual situation.

2.4.2. Extension of the analysis to the entire value chain.

The value chain comprises all the activities, resources and relationships that are part of an organization's business model, as well as the external environment in which it operates. It is a fundamental framework for ensuring that sustainability issues are integrated into all the stages on which it relies to create its products and services, from conception to delivery, consumption and end-of- life. A clear understanding of the value chain is crucial to conducting an effective double materiality assessment and identifying the impacts, risks and opportunities that may arise along the value chain.

In this value chain analysis, it is important to assess whether associated companies and joint ventures are part of the value chain as suppliers or customers. If so, they will be considered as agents within it, integrating their exposure to impacts, risks, and opportunities in the consolidated analysis of the entity.

By contrast, if they are not part of the value chain, they can be treated as investments, whereby their impacts are assessed and those that are material are reported.

In both cases, indicators related to the Company's Scope 3 will be disclosed, when significant, given the nature of the indicator. There are three phases of the value chain:

- *Upstream*: includes the activities, resources, and relationships that the organization uses to create its products or services. This includes raw materials, direct and indirect suppliers, and any business relationships necessary for producing products or services.
- *Own operations*: comprises the activities, resources, and relationships conducted by the organization to develop its business and its products and services.
- *Downstream*: encompasses the activities, resources, and relationships necessary for the commercialization, use and completion of the life cycle of the organization's products and services. This phase includes both direct and indirect commercial relationships and/or customers who use the company's products and services or other downstream stages identified by the entity, though excludes the end user.

The process for defining the value chain is described below:

- a)** Identify the various stages of the value chain: recognize and define the various stages that make up each of the phases (upstream, own operations and downstream) of the value chain of the company. For example, the downstream phase could be the marketing, use or after-sales stages.
- b)** Establish the key activities in each of the defined stages: Following the example above for the downstream phase, in the after-sales stage, activities identified may include service, technical support or customer waste management.
- c)** Identify the actors involved in the different activities: Determine all the actors directly or indirectly involved in the activities at each stage of the value chain. This can range from raw material suppliers to distributors and other distribution channels (such as franchises), customers, business partners and other key agents that contribute to the success of operations at each stage.
- d)** Identify the main geographic locations where the different activities of the value chain are carried out.

Considering the potential complexity due to transitional options, estimates, or unavailable data for the initial adoption of the European Sustainability Reporting Standards as per EFRAG's guidelines, key factors in determining the value chain are outlined below:

- Identify all critical areas of the company that can contribute to the definition of the value chain and actively involve them in the process, which will ensure that the value chain accurately reflects the operational reality. Likewise, it allows the experience and knowledge from the different areas to be leveraged, thus promoting a comprehensive and accurate perspective.
- Considering the sustainability scope is essential to reflecting all the activities of the various companies. It also serves as a guide for the identification of activities, actors, and geographic locations at each stage of the value chain, ensuring a consistent and complete view of Sustainability Reporting.
- Periodically reviewing and updating the value chain is essential to ensure changes in operations, such as the inclusion of new suppliers or expansion into new markets are reflected. This allows the value chain to remain aligned with operational reality, identifying impacts, risks, and opportunities accurately at all stages.
- Adequately and clearly identifying the main activities within the value chain is an essential element. In complex companies, where value chain activities are dispersed and varied, it is advisable to simplify the value chain by incorporating representative information to improve data traceability and ensure that the information provided is reliable and consistent. If it is not possible to obtain information from a significant company in the value chain, duly calculated and justified estimates may be used.

2.4.3. Conduct double materiality assessment: Impacts, Risks and Opportunities (IROs).

Double materiality is a key approach to ensure that the Sustainability Information reported reflects how the company's activities and value chain impact the environment and society as a whole (by identifying both positive and negative impacts) and, in turn, what financial impact sustainability issues may have on the company (by identifying risks and opportunities).

In this way, it is possible to identify relevant sustainability issues for each company and determine which information to report to allow an accurate and integrated view.

The typical process for implementing double materiality assessment (DMA) is as follows:

- a)** Identify potentially material sustainability issues: CSRD provides a generic list of sustainability issues to be considered in the double materiality assessment. This list serves as a basis; for complete identification it is necessary to:
 - a.1) Include specific topics: consider those issues which, according to the company's business model and value chain, may be material, and for which impacts, risks and opportunities should therefore be analyzed. As detailed in CSRD, in the absence of specific sectoral standards, it is recommended to use available sustainability frameworks and standards, such as the International Financial Reporting Standards (IFRS)' sectoral guides, Sustainability Accounting Standards Board (SASB), and industry standards such as the Global Reporting Initiative (GRI).

- a.2) Discard non-applicable issues: identify those sustainability issues that are not relevant to the organization, due to its business model and value chain, disregarding them in the first instance.
- b)** Identify and assess impacts, risks, and opportunities (IROs): with the final list of potentially material topics, subtopics, and sub-subtopics, proceed to identify their IROs (at the most disaggregated level, usually sub-subtopics). It is essential to involve all relevant areas of organization, considering the entire value chain, as well as all the specific requirements detailed in the standard. An analysis of the impacts, both positive and negative, should be conducted initially, to then identify the risks and opportunities derived from them.
- c)** Define material topics: after identifying and assessing all IROs, the results will be consolidated and the materiality threshold will be determined, i.e., the point at which an impact, risk and opportunity is considered material. This process results in a list of material topics and subtopics for the organization and the significant IROs to be disclosed. Since the standard does not establish a standard format for the disclosure of this information, it can be presented in the manner that best facilitates its understanding (for example, in the form of a list).
- d)** Validation: the result of the analysis must be validated, ensuring the commitment and approval of Senior Management for the implementation and reporting of the sustainability issues identified.

Given that this process can be quite complex, as there is no methodology that indicates how to assess the scope, scale and irremediable character, organizations should develop their own models. The main aspects to be considered can be summarized as follows:

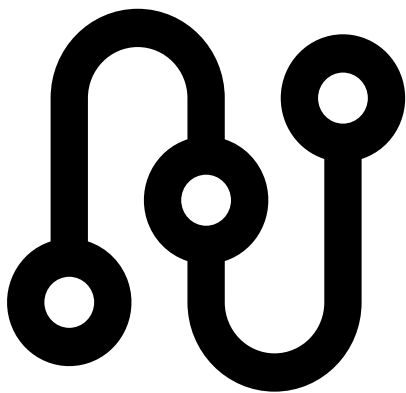
- The double materiality assessment is critical for determining the Sustainability Information to be disclosed. It should be comprehensive, involve all relevant areas in the management of sustainability topics of the organization and be based on reliable sources, both internal and external.
- Understanding the value chain will promote the correct identification of impacts, risks, and opportunities at each stage.
- Leveraging existing information is useful for identifying impacts, risks, and opportunities. For example, an organization with a due diligence report should use it to identify negative impacts and thereby improve the consistency of Sustainability Reporting.
- Integrating the risks identified during the double materiality assessment into the corporate risk management model is essential for ensuring a comprehensive and consistent risk review. This approach allows all sustainability aspects to be considered in the company's overall strategy and aligns with corporate risk management and internal control practices. Conversely, it is also necessary to consider the information derived from the organization's risk management (e.g., Risk Map) to achieve alignment and consistency in reporting.
- Balancing the financial and sustainability perspectives ensures that both aspects are considered in a fair and balanced manner in the double materiality assessment and thus in strategic decision making.
- When assessing financial impact (as part of double materiality), the thresholds set should be in line with the materiality thresholds of the organization's financial statements. In other words, it is recommended that when assessing risks and opportunities, the potential impact of financial

effects, both current and anticipated, is considered and their materiality is determined based on established corporate financial thresholds.

- Identifying stakeholders is essential for evaluating communication channels and promoting participation and engagement, from all parties (from shareholders up to local communities), in the preparation of the double materiality assessment.
- Periodically reviewing and updating the double materiality assessment ensures that the organization keeps up with changes in its operating environment and promotes continuous improvement in sustainability management. It is important to align this analysis with any changes in the scope of sustainability and value chain.

Part II

Control over Sustainability Reporting



3. Governance and Oversight of Sustainability Reporting.

The ICSR Governance Model should establish the system's objectives, roles and responsibilities, and the corresponding regulatory framework. This allows organizational units to interact effectively and in a coordinated manner, to ensure that published Sustainability Information is transparent, traceable, and comparable, and thereby reliable, and of high quality.

3.1. Roles in ICSR.

3.1.a) Management Functions - Responsibility for processes involved in preparation of Sustainability Reporting.

In the process of preparing Sustainability Reporting, the area that manages each business point linked to the sustainability data to be published (data owner) is responsible for the preparation and control of this information, in accordance with the double materiality assessment and the legislative/regulatory requirements in force.

Many areas are usually involved in the process of generating Sustainability Information due to its specific characteristics (which have already been addressed in previous parts of this Guide). Their number and functions may vary from one organization to another, but it is common for areas such as Risk Management, Sustainability, Human Resources, Communications, Finance, Legal, Technology, Purchasing, among others, to participate to a greater or lesser extent. Their participation may consist of producing one or more indicators, compiling auxiliary information, and providing it to another department, defining reporting criteria, coordinating and ensuring comparability and consistency of indicators, or several of these functions at the same time.

Key tasks to be performed by these functions include the following:

- Participate in the double materiality assessment and identify the indicators and metrics to be reported, according to the result of this analysis.
- Define the criteria for the development of indicators and metrics. Document the end-to-end processes for generating indicators, either in narratives or flowcharts, and update them when necessary.
- Compile the necessary information to prepare the metrics and indicators, as well as the remaining qualitative information published.
- Identify risks, opportunities and impacts associated with Sustainability Reporting.
- Develop and update ICSR supporting documentation.
- Design, establish and implement controls to ensure data quality.
- Participate in training and awareness programs on risks and controls.
- Ensure that consolidated data integrates information from the full scope of sustainability reporting.

The details of the documentation associated with these processes are detailed in Section 4.2.e *Supervisory Activities* of this document.

Due to the involvement of several areas or departments preparing indicators, together with the specific characteristics of Sustainability Reporting (detailed in point 2.2 *Qualitative Characteristics* of this Guide), it is advisable to have an area within the organization in charge of coordinating the process of preparing Sustainability Reporting.

A coordinating area can facilitate the implementation of mechanisms designed to ensure the consistency and comparability of information prepared and reported by companies. Its responsibilities include the following:

- Supervise the criteria for the preparation of the information and ensure that they meet the requirements established by applicable regulations.
- Define and update the scope (including the perimeter as well as value chain activities).
- Coordinate the double materiality assessment.
- Oversee the process for identifying impacts, risks and opportunities associated with Sustainability Reporting.
- Evaluate the consistency of reporting.
- Establish delivery dates for all areas.

This coordinating area may be part of the Sustainability or Financial area, or it may be independent of the aforementioned. In any case, from the identification of risks to their materialization, there are related financial and sustainability impacts, and the connection and coherence between financial and sustainability reporting is important and required by regulators. Therefore, it is important to involve the financial area in the processes for preparing the Sustainability Report.

3.1.b) Control Functions - Responsibility for the control and supervision of Sustainability Reporting.

In all organizations there should be a function that ensures that controls are in place to mitigate the risks associated with Sustainability Reporting, as well as to facilitate their effective functioning. This function must understand the Sustainability Reporting risks and ensure that the control system in place covers the identified risks.

Depending on the organization, this function may be integrated into the area that performs the management/preparation role (data owners), or it may be separate from it.

The main functions performed within the organization are:

- Ensure the integrity and consistency of ICSR.
- Advise on the identification and assessment of risks to provide an objective perspective regarding exposure.
- Evaluate the presence and adequacy of controls and their design to ensure the reliability of Sustainability Reporting, considering its materiality (according to the result of the double materiality assessment) and complexity.

- Monitor compliance and execution of controls in accordance with the definition foreseen in the risk and control matrices, through inspection of the evidence provided, as well as consultation with those who performed them.
- Monitor the internal certification process of the control activities established in the ICSR system, if such a process exists.
- Collaborate in the implementation of the corrective actions identified in reviews of ICSR.
- Promote the efficiency and robustness of the model through advisory activities and promotion of implementation of automated controls, as well as in the general controls of the key applications that support the processes linked to the generation of Sustainability Reporting. This will require the involvement of technology specialists.
- Assess and evaluate supporting ICSR documentation, confirming that all risks and controls have been documented, along with their characteristics (periodicity, assertions covered, etc.) and relevant evidence.

As previously mentioned, while the data owners must identify risks and establish controls over Sustainability Reporting, a supervisory function is essential to oversee ICSR effectiveness, aiding in the identification of risks and providing assurance that the controls identified are sufficient and effective to mitigate existing risks.

3.1.c) Evaluation function - Internal Audit.

The Internal Audit Function provides an independent review of the design and effectiveness of defined controls to provide greater confidence in the quality and reliability of Sustainability Reporting. This role performs objective and systematic evaluations of the processes and controls implemented. Its importance lies in its independent and objective nature, enabling an unbiased evaluation of the internal control system's integrity and effectiveness.

In an environment where i) companies are increasingly committed to strategic objectives linked to social and environmental sustainability; ii) there are relevant regulatory changes; iii) there is, in many cases, a limited level of maturity of the control systems for Sustainability Reporting and iv) the level of assurance provided by the external independent assurance providers is limited, the role of the internal auditor is essential for providing confidence to the organization, the Board of Directors and the Audit Committee (if applicable). Therefore, internal auditors must include projects related to Sustainability Reporting and assurance of ICSR in their Internal Audit Plan, considering the above considerations.

The Internal Audit Function identifies areas for improvement and ensures that recommendations for strengthening risk management, internal control, and governance systems for the sustainability report are implemented. This provides an additional layer of assurance to stakeholders that the Sustainability Reporting is accurate and reliable, and that risks are being properly managed. Its functions are as follows:

- Conducting periodic reviews of ICSR and issuing the corresponding reports, in accordance with the provisions of the entity's Annual Audit Plan.
- For those areas and indicators that are included in the entity's Annual Audit Plan, designing and executing a test plan for: i) the governance model; ii) the risks identified; and iii) the control model. This plan will consider any self-assessments conducted by control personnel, if applicable.

- Verifying the correct implementation of ICSR action plans by management and control areas, based on the recommendations raised during the audits carried out.
- Periodically informing the Board of Directors or the Audit Committee and, where applicable, the Sustainability Committee of the results of the evaluations performed, including weaknesses identified, as well as monitoring the recommendations and defined action plans.

In addition to assurance work, Internal Audit may perform advisory work, without compromising its independence and objectivity, with the aim of helping organizations to improve the level of maturity of their risk management and internal control systems related to ICSR. Thanks to its holistic vision, the Internal Audit Function can promote the strengthening of the governance system, advise on the organizations' risk identification process, and assist in understanding the relationship between these aspects and other existing risks.

3.2. Other Governing Bodies involved in Sustainability Reporting and ICSR system.

The integrity and reliability of Sustainability Reporting are fundamental pillars for any entity committed to responsible and transparent business practices. In this context, ICSR must be supported by a robust governance structure, where various stakeholders play decisive roles.

An adequate internal control system for Sustainability Reporting includes key Governance Bodies such as the Board of Directors and, where appropriate, the Audit Committee and the Sustainability Committee²⁹. This structure ensures transparent disclosure of environmental, social, and corporate governance data while also promoting principles and best practices that ensure consistent and reliable Sustainability Information.

3.2.a) Governing body or the Board of Directors.

The Consolidated Text of the Corporate Enterprises Act (Ley de Sociedades de Capital) describes those powers that may not be delegated by the Board of Directors, defined as the highest decision-making, oversight and control body, which include responsibility for an adequate and effective ICSR. The supervision of this process is delegated to the audit committee, where this exists, with senior management in charge of its design and implementation.

Among the principles and best practices aimed at achieving this objective within the framework of ICSR are the following responsibilities:

- Approval of policies related to internal control, sustainability risks and management of sustainability information.
- Ultimate responsibility for the existence and maintenance of an adequate and effective ICSR.
- Ensuring that the control culture is disseminated from the upper layers so that it permeates into the lower strata of the organization.
- Preparing any Sustainability Report required from the Board of directors by law.

²⁹ The Audit Committee is mandatory for listed companies, while the Sustainability Committee is voluntary.

- Encouraging an open discussion by the Board itself of any relevant matter regarding Sustainability Reporting for the entity and its Group.

3.2.b) Functions of Specialized committees³⁰.

CNMV Technical Guide 1/2024 on Audit Committees of public interest entities introduces the treatment of Sustainability Reporting and its risks, establishing principles for their functions, criteria for their composition and guidelines for complying with regulatory requirements. It highlights the oversight of Sustainability Reporting and financial and non-financial risks, with special mention of sustainability risks.

The CNMV Technical Guide and the Corporate Enterprises Act (when considering the changes in the Draft Law), establish that the Audit Committee must oversee the effectiveness of the risk control and management systems, covering both financial and non-financial risks. Nevertheless, the power to approve the risk strategy and policy shall correspond to the Board of Directors, at the proposal, if applicable, of the Risk Committee, or of the Sustainability Committee (if any); the latter case referring specifically to the sustainability risks within its purview.

In relation to the assurance provider for Sustainability Reporting, it is also recommended that the Audit Committee be responsible for the selection process, to ensure professional competence and independence, as well as for the adequacy of the quality of such assurance. In this process, it is also recommended that the Audit Committee consult or involve, in some manner, the Sustainability Committee where it exists.

In this regard, considering the novelty of the functions of the Audit Committee on Sustainability Reporting and its associated risks as introduced by the CSRD, it should be noted that, notwithstanding the responsibilities of the Audit Committee for the oversight of sustainability reporting, and the effectiveness of the related risk control and management systems, it seems reasonable that the establishment of ESG or sustainability strategies, plans, policies and objectives by the Board of Directors should be carried out at the proposal of the Sustainability Committee, in the event that such committee has been constituted and has the corresponding powers.

3.2.b.1) Recommendations for coordination between the Specialized Committees.

The establishment of clear responsibilities between the specialized Committees (mainly the Audit Committee and the Sustainability Committee, where applicable) is an issue that requires attention. Although these committees have different approaches, effective collaboration between them is key to strengthening the organizations' ability to address both financial and sustainability challenges in a coherent and effective manner, through coordination strategies such as the following³¹:

- **Clarification by the Board of Directors:** the Board of Directors should take an active role in clarifying responsibilities and promoting awareness among all board members and members of the management team.

³⁰ Depending on the characteristics, nature and sector of the organization in question, there may be, where appropriate, other committees that take part in the process of supervising sustainability and/or its associated information, such as the Nominating, Risk or Sustainability Committees.

³¹ In addition to those indicated above, the coordination mechanisms contemplated in paragraph 50 of Technical Guide 1/2024 on Audit Committees of Public Interest Entities of the CNMV may be considered: https://www.cnmv.es/DocPortal/Legislacion/Guias-Tecnicas/GT_ComisionesAuditorias_en.pdf

- **Reviewing and updating the Committee charters** to clearly assign responsibilities and authority. This will provide a clear basis for the efficient functioning of the Committees.
- **Specifying coordination mechanisms:** to improve interaction between the Committees. These mechanisms may include:
 - The cross-inclusion of members between Committees.
 - Meetings of Committee Chairpersons.
 - Joint meetings between specialized committees (e.g., the Audit Committee and other committees).
- **Integrated risk management:** develop an integrated approach to risk management that considers both financial and non-financial risks, including environmental, social and governance risks, thus reducing duplication of efforts and confusion in the identification and management of interrelated risks.

Finally, and if there are other Committees in the organization that deal with matters related to sustainability and/or the related information (such as risks, compensation, etc.), it is important that they are also coordinated.

3.2.b.2) Resources and experience for the composition of the Committees.

The composition of the Sustainability Committee, where applicable, requires a diversity of skills ranging from environmental science to management of community relations. This also extends to the Audit Committee, since, to adequately exercise its responsibilities regarding the organization's Sustainability Reporting, it is necessary that its members, as a whole, have a solid knowledge of sustainability reporting.

The main difficulties in the composition of the specialized Commissions include the following:

- **Adaptability and flexibility:** the ability to adapt to new requirements is critical to the success of the Committees. This not only includes understanding regulatory changes, but also the ability to apply this knowledge in the formulation of effective strategies and decision making.
- **Relationship and stakeholder management:** sustainability is not only about environmental policies; it also involves managing relationships with stakeholders such as local communities, NGOs and shareholders committed to ESG issues. Therefore, committee members must be able to understand and manage these complex dynamics.
- **Sustainability expertise:** Sustainability issues cover a wide range of topics, including climate change, environmental management, human rights, diversity, and inclusion, among others. It is essential that the members of the specialized Committees for sustainability matters have practical experience in these areas to effectively evaluate the proposed policies and strategies.
- **Continuous training on emerging issues:** Sustainability regulations and expectations are constantly evolving, requiring committee members to keep up to date with the latest trends and regulations. In addition, they must be prepared to address emerging and complex issues such as the carbon footprint, circular economy, and social inclusion, which require a continuous commitment to training.

- **Shortage of sustainability professionals:** The rising commitment to sustainability by organizations has increased demand for professionals experienced in this field, making it challenging to find suitable talent for specialized Committees with the knowledge to make informed decisions.

3.2.c) Senior Management.

Senior Management's commitment to transparency and accountability is fundamental to the credibility of Sustainability Reporting, and this includes its support to facilitate the implementation of internal control systems and external assurances of such information, since Senior Management can allocate the necessary resources to implement and maintain such initiatives as a priority for the organization.

Its commitment can be demonstrated in several ways. First, by developing and approving sustainability policies that define the organization's objectives and principles; then integrating these objectives into corporate strategy and in the day-to-day operations, establishing governance structures to oversee the achievement of the company's sustainability objectives; and finally, by promoting transparent communication on sustainability achievements and challenges, both internally and externally.

The following are two of the main mechanisms implemented in some organizations to ensure the accuracy, consistency and alignment of the information reported with recognized sustainability regulations and standards, such as CSRD, GRI³², or SASB, or with the organization's internal standards. This alignment ensures that information is not only accurate, but also comparable and relevant in the context of stakeholder expectations and current regulations on Sustainability Reporting:

- **Waterfall approach in the data certification process:** Senior Management confirms the reliability and integrity of the Sustainability Reporting presented, emphasizing the responsibility of managers.
- **Senior Management's variable compensation:** may be tied to better quality information (e.g., no significant errors are identified), to increase the accuracy of the Sustainability Reporting.

3.3. Other relevant aspects.

3.3.a) Formalization of the Governance Model.

A Governance Model helps to establish responsibilities and roles within organizations.

As mentioned above, organizations must define their governance model and adapt it to their operating circumstances. In some heavily regulated sectors, there are requirements for the separation of functions into clearly differentiated areas. It is the prerogative of each organization to consider which model is appropriate, and to ensure that it incorporates sufficient independence. In the event of a conflict, the necessary safeguards should be established between the areas that share responsibilities to ensure independence and objectivity of the related functions. For example, by obtaining assurance from independent third parties.

³² Global Reporting Initiative - International non-profit organization.

It is recommended that the Sustainability Reporting Governance Model be documented³³, distinguishing the areas involved and their respective roles and responsibilities.

3.3.b) Other control models.

Despite the differences and distinctions between Sustainability Reporting and financial reporting, there are also parallels between the systems for Internal Control over Financial Reporting (ICFR) and ICSR, whereby organizations can benefit from the lessons learned from implementing ICFR and take advantage of the methodology developed, the specialized teams, the controls already implemented that are applicable to ICSR and the tools used. There may be other control models implemented in the organization (such as, for example, compliance models) whose controls may partially cover ICSR processes. A comprehensive overview of these control models, along with the effective use of synergies between them, can enhance the efficiency of ICSR.

³³ See Section 4.2.e of this Guide, *Documentation of information definition processes and associated controls*.

4. Design and implementation of the Internal Control over Sustainability Reporting System.

4.1. COSO ICSR Conceptual Framework (2023).

As has been addressed in previous parts of this Guide, for Sustainability Reporting to be useful to its different stakeholders, it must be relevant and faithfully represent the organization's material sustainability issues (relative importance).

To achieve this reliability, Sustainability Reporting must be complete, neutral, and accurate. To be verifiable by a third party (either through limited or reasonable assurance), it must possess the qualitative characteristics indicated above in point 2.2 of this document: *Qualitative Characteristics*. For Sustainability Reporting to be effective, it must be clear and concise to ensure it is easily understandable by its users.

When ICSR has been designed and is properly functioning, it can be considered as effective and thereby provides reasonable assurance that Sustainability Reporting is prepared in accordance with the characteristics outlined above. The main components that ICSR must have to achieve this are provided below. To this end, this Guide has taken the model proposed by COSO as a fundamental reference in the document titled: *"Achieving Effective Internal Control over Sustainability Reporting (ICSR): Building Trust and Confidence through the COSO Internal Control-Integrated Framework"*, 2023. The approach from this is a widely accepted framework considers the CNMV document *"Internal Control over Financial Reporting in Listed Companies"*, 2010, as well as certain key aspects contemplated in the European Sustainability Reporting Standards.

4.1.a) Control environment³⁴.

The organization demonstrates its commitment to integrity and ethical values through the leadership and commitment of the Board of Directors and Senior Management to contribute towards the company's sustainability. To this effect, it establishes standards of conduct (Code of Ethics) and a Sustainability Policy that allows it to assess compliance within the organization and its value chain, if necessary. Likewise, Senior Management addresses the deviations identified, following up on them to correct them.

It will also have an internal whistleblower channel for irregularities in the preparation process for Sustainability reporting with specific measures to protect whistleblowers.

The Board of Directors, either directly or through its specialized committees, exercises its independent oversight role over ICSR, ensuring that members responsible for this oversight (or the oversight body as a whole) have the necessary knowledge and experience in sustainability matters, as mentioned in Section 3.2 *Other Governance Bodies involved in Sustainability and ICSR* of this Guide.

The roles of the participants in the preparation, approval and oversight of Sustainability Reporting will be defined through an ICSR Policy approved by the Board of Directors, considering all the functions of the organization and establishing appropriate reporting lines.

³⁴ Achieving effective internal control over Sustainability Reporting:
www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

The entity will employ competent human resources for the preparation of Sustainability Information, with an adequate description of the functions of the personnel involved in the process, ensuring that their knowledge is maintained up to date. It will assess their competencies, establishing training plans where deficiencies are identified. Additionally, it will attract and develop talent for these positions and define a succession plan for key employees involved in the Sustainability Reporting process.

Finally, it will establish a system of accountability and responsibilities for the Sustainability Reporting process. Performance measures and incentives related to sustainability objectives will be implemented, with periodic assessments to ensure their alignment with the organization's evolution and objectives (adaptation to change). This also considers whether there are excessive pressures for the achievement of objectives and analyzes the performance of the people involved with reward or disciplinary systems.

4.1.b) Risk assessment³⁵.

The organization clearly establishes its objectives related to sustainability. This allows risks to their achievement to be identified and analyzed throughout the organization, as well as determining how they should be managed.

In setting these sustainability objectives, the organization considers the interests and opinions of its stakeholders (shareholders, members of the organization itself, customers, suppliers, business partners, regulators, business associations, the society where it operates, etc.³⁶).

This risk identification and assessment process must be maintained over time, as it is necessary to consider significant changes, both internal and external, as well as emerging trends.

As mentioned earlier in this Guide (point 2.4 *Scope of Sustainability Reporting*), the outcome of the risk analysis will depend on the organization's activity, the geographical dispersion of its business model and value chain, stakeholder expectations, existing information systems, complexity of data collection and estimation, formalization of internal procedures and controls, and the training and knowledge of the personnel involved in Sustainability Reporting.

The risk assessment will consider the concept of double materiality (impact and financial), assessing whether the impacts caused are positive or negative, and whether they are real or potential.

For positive impacts, materiality will consider the magnitude and scope (for actual impacts), adding the probability of occurrence (for expected or potential impacts).

For negative impacts, materiality assesses the magnitude, extent, and irremediable nature of actual impacts, as well as the likelihood of occurrence for potential impacts.

Financial materiality refers to financial effects that have a material influence or could reasonably be expected to have a material influence, on the development, financial position, financial performance, cash flows, access to finance or the short, medium or long-term cost of capital of the organization. It refers not only to matters within the entity's control, but also to

³⁵ Achieve effective internal control over Sustainability Reporting:
https://www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

³⁶ Additionally, and in compliance with the ESRS, companies must identify the impacts, risks and opportunities related to sustainability aspects that are material, as mentioned in section 2.4. *Conduct double materiality assessment: Impacts, Risks and Opportunities (IROs)* of this document.

material risks and opportunities in business relationships. Along with the identification of risks related to meeting the sustainability objectives set by the organization, ICSR should identify the risks related to the information itself, such as errors in the selection of the relevant aspects to be reported identified in the double materiality assessment process, or the lack of integrity of the information reported.

In addition, consideration should be given to the possibility of fraud in the Sustainability Reporting process (lack of information on material issues, unreliable or erroneous or intentionally biased reporting, greenwashing, social washing, etc.).

It is also necessary to highlight the risk related to the information technologies involved in the process of obtaining Sustainability Reporting in terms of security, availability, and confidentiality.

Another aspect to consider is that Sustainability Information reported may be both quantitative and qualitative, affecting the required information's characteristics differently (such as faithful representation, neutrality, accuracy, understandability, etc.³⁷) and consequently the risks associated with failing to meet these characteristics. Furthermore, the coherence and consistency of the quantitative sustainability data with the financial information should be considered.

It will also be necessary to address the risks related to information provided by third parties within the value chain, applying due diligence and paying special attention to the estimates they may contain.

For the deployment of control activities, it is necessary to evaluate the scope of ICSR³⁸, which considers, among other aspects, the risks identified in the double materiality assessment; significant entities, subsidiaries, divisions, operating and/or functional units; the risks associated with the characteristics of the Sustainability Information mentioned earlier in this document, as well as the risks related to the quality and availability of the data.

Based on this scope assessment and the determination of the sustainability aspects selected following the double materiality assessment (and the corresponding data points, in accordance with the ESRS), the controls to be implemented to mitigate the associated ICSR risks must be determined. With this data, the Sustainability Information risk and control matrix can be drawn up, which will form part of the entity's risk management system and the related risk map.

4.1.c) Control activities³⁹.

This refers to specific control activities that the entity has implemented to mitigate the risks of error (including those related to the scope) or irregularities in the Sustainability Reporting.

To identify control activities in a practical manner, the following considerations must be considered. As in ICFR, control activities should be identified at three levels: entity-level controls, process-level controls, and information technology controls.

- 1) Entity level controls (ELCs) align with the details in the control environment component. These should be documented in an ELC risk and control matrix, like that used for ICFR (ICSR policy, whistleblower channel, etc.). It is recommended that it be reviewed annually, maintaining evidence and traceability of its review.

³⁷ For more details, see section 2.2 of this document: *Qualitative Characteristics*.

³⁸ It may be in the form of a table/matrix or in any other format.

³⁹ Achieving effective internal control over Sustainability Reporting:
https://www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

- 2) The scope of process-level control activities depends on the prior risk assessment, which identifies (i) relevant Sustainability Information topics/subtopics based on double materiality assessment and (ii) significant businesses/companies for each of these.
- 3) For IT controls, it is necessary to maintain an inventory of applications for processes involving key matters and identify general IT controls (access, backup, segregation of duties, system operation and changes, etc.), as well as at the level of the application itself (automatic reconciliation, parameter restrictions, etc.). The methodology is like that used for ICFR, with the particularity that, for Sustainability Reporting, a larger number of applications is normally used to capture, process and report truly diverse information (tons of CO₂, employee data, etc.).

4.1.d) Information and communication⁴⁰.

Information systems are essential for managing sustainability activities, making strategic decisions, and facilitating both internal and external communication. These systems should be key tools for organizations to not only meet their environmental and social requirements, but also to communicate their efforts and results effectively.

This implies a meticulous approach to identifying relevant and necessary data for communication that supports sustainability objectives, and considers the availability of this information in time, form and with the necessary quality, as well as a commitment to clear and effective internal communication within the organization, with the objective that all employees are informed and engaged.

Likewise, transparency towards the outside world is important, where accurate and timely information on sustainability practices must be shared with stakeholders. These systems must be developed with the capacity to adapt and respond to the changing expectations of the market and society.

In this sense, the principles, and best practices to achieve this objective are detailed below:

- The identification of relevant information requirements to support internal operations and external communication is essential. This information will be both qualitative and quantitative and should allow the integration of relevant data not only to comply with legal requirements and stakeholder expectations and to serve as a basis for sustainability projections, but also to strengthen transparency and corporate responsibility. In this sense, the European Sustainability Reporting Standards outline the scope and mode of operation.
- Sustainability Information identified as relevant should be made available based on realistic and achievable goals, based on a cost-benefit analysis that considers and assesses different alternatives, as well as allowing them to be obtained in the most agile manner possible.
- In addition to being robust, the Information System must be flexible and adaptable, as well as capable of incorporating new data and trends, and of responding to the changing demands of the environment. Investment in information and communication systems not only improves sustainability management but also makes a decisive contribution to establishing a robust Internal Control System. Developing a Sustainability Reporting System involves identifying the relevant information needs for the organization based on its materiality assessment, in collaboration with both internal and external stakeholders, to determine its availability. Such information will be

⁴⁰ Achieve effective internal control over Sustainability Reporting:
https://www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

collected, verifying its homogeneity and the quality of the data to be included; existing information systems are adapted to process and present sustainable data.

- A well-structured internal communication system ensures that all members of the organization, from the Board of Directors and Senior Management to relevant function heads (management, control, and internal audit), have the necessary information to efficiently fulfill their roles in an informed manner and within deadlines. Similarly, internal communication must extend to value chain members to ensure information integrity, availability, and consistency.
- Collaboration between the Sustainability, Finance, IT Systems, and Internal Audit Departments is essential, considering the previous experience and skills developed in the management and control of financial information, as an essential starting point to ensure the integrity and relevance of the data.
- In relation to external communication, the information systems must be capable of generating sustainability reports that accurately reflect the activities, identifying the related impacts, risks, and opportunities. These reports must be understandable and accessible to stakeholders, allowing for an open and constructive dialogue.
- Proactive transparency in external communication is essential to mitigate the risk of greenwashing, especially in the absence of specific regulation or accepted homogeneous procedures.

4.1.e) Monitoring activities⁴¹.

The monitoring and evaluation of internal control systems are key components for building confidence in Sustainability Reporting. These processes not only detect and correct errors but also strengthen stakeholder confidence in the information presented.

As with financial information, the Audit Committee or, in its absence, the Board of Directors (or governing body), must apply an equivalent level of supervision to Sustainability Information. Generally, the guidance provided by the working group set up at the proposal of the CNMV on Internal Control over Financial Reporting (ICFR) is applicable with regard to the adequacy of policies and procedures, integrity of the preparation process, correct delimitation of the scope of consolidation, and the application of sustainability regulations.

Applying reasonable assurance to Sustainability Reporting is inherently complex, as it involves subjective qualitative data and forward-looking projections. Key aspects for oversight of Sustainability Information include:

- Continuous monitoring of internal controls to maintain their effectiveness in a changing Sustainability Reporting environment. This involves periodic review to ensure that controls evolve along with new requirements, stakeholder demands and emerging risks.
- Financial and impact materiality are key components in the identification of significant aspects to be reported, as well as impacts, risks and opportunities and the composition of the value chain. Ongoing monitoring and periodic evaluation of these elements based on the entity's judgments and estimates, promotes confidence among investors, regulators, and society in general, ensuring that the information disclosed is complete and relevant. While the standards do not require specific documentation on materiality, entities should document their assessment process so that double materiality and its results can be included in independent verification processes.

⁴¹ Achieving effective Internal Control over Sustainability Reporting:
https://www.coso.org/_files/ugd/719ba0_0b33989b84454d1682399ab5c71e49cb.pdf

- Sustainability reporting often includes estimates, value judgments and long-term objectives, which can be difficult to verify due to the variety and lack of standardization in sustainability practices. This poses a significant challenge for oversight and verification. In this respect, it is essential to develop robust methodologies and frameworks with clear reference points, both for the estimation and projection processes, as well as for their oversight, which enables review of the information in a consistent and comparable manner.
- Timely and effective communication of deficiencies identified during assessments is vital for informed decision making. This enables senior management to fulfill its oversight role, and function managers to act accordingly to correct issues and improve existing controls.
- Effective oversight at all relevant stages of the value chain ensures that an adequate level of security is maintained in Sustainability Reporting, protecting against errors, omissions, or fraud. This is achieved through the implementation of preventive and detective controls, as well as mitigation and remediation mechanisms. Although the level of maturity of the control and reporting processes implemented by the company and with its supply chain will evolve and improve, it is important to establish common standards and procedures for the components of the value chain, both in the measurement and monitoring processes. Specifically, oversight procedures can be adapted to those already in place for the reporting of financial information of subsidiaries, as well as extended to new procedures (such as self-assessment questionnaires, approval of suppliers, or periodic reporting with limited assurance by an external party, among others).
- Moving from limited to reasonable assurance for Sustainability Information reports enhances confidence in the data. This level of assurance implies a more rigorous and complete evaluation, which increases the reliability of the information presented and, therefore, improves its level of quality. In this sense, it would be advisable to adopt a progressive approach that allows advancing to reasonable assurance of specific and relevant aspects, and towards a complete assessment, thus proceeding in the standardization of the data collection processes, the establishment of controls over the process and in evaluating its operation and effectiveness, as stated in Section 5.7.a of this document.

4.2. Specific elements of ICSR.

4.2.a) Scope of application of ICSR.

As we have seen above, Sustainability Information can be defined in many different ways and presented through various channels and formats, such as notes to the financial statements regarding the financial impact of climate change, the Annual Report, rating agency questionnaires, presentation of information to stakeholders or investors, and the website, among others, as well as under different regulatory or voluntary frameworks, including the ESRS, ISSB⁴², TCFD, SEC⁴³ and GRI.

⁴² International Sustainability Standards Board founded by the IFRS Foundation (International Finance Reporting Standards).

⁴³ U.S. Securities and Exchange Commission climate-related disclosure rules - Disclosure requirements on the financial impact of climate change published by the U.S. Securities and Exchange Commission in March 2024.

4.2.b) Scope of breakdown requirements.

ICSR disclosures must encompass information that could influence the users of Sustainability Information. In other words, ideally, all qualitative and quantitative data in the scope of ICSR should be that which is disclosed in the Sustainability Report associated with material (or materially important) impacts, risks, and opportunities. In the understanding that it may not be possible to cover all Sustainability Information, it is suggested that prioritization criteria be established when approaching the implementation of an internal control system for Sustainability Reporting.

The European Sustainability Reporting Standards include approximately one hundred disclosure requirements (around one thousand data points) that must be disclosed in the Sustainability Report (in accordance with the double materiality assessment) included in the Management Report of companies in the scope of application of CSRD.

Sustainability Reporting includes several types of data: narrative, semi-narrative and numerical (including, for example, energy, volume, percentages, tables or monetary units). The nature of these types of data implies a different approach in terms of the inherent risk they may represent (as an example, quantitative data could be considered to represent higher inherent risk than qualitative data). In general, Sustainability Reporting is predominantly qualitative in nature because the standards require descriptions of the context of companies' activities, including their strategy and their risks, opportunities and impacts in the short, medium, and long term.

In relation to the inclusion of the value chain within the scope of the report, it is necessary to mention that this implies the integration of information provided by third parties, which can create a difficulty for the scope of ICSR.

Moreover, European regulations require the disclosure of material information not covered ESRS⁴⁴ if it concerns significant financial, environmental, or social issues within the ICSR scope.

In the event of including additional material disclosures to those covered by ESRS, it is fundamental to clearly define the information included in such disclosures (or defined in accordance with a generally accepted framework, such as GRI, ISSB, etc.) in order for ICSR to effectively ensure the reasonableness of these data.

4.2.c) Risk Scoping.

Risks in Sustainability Reporting include inadequate application of internal control criteria and unstable or undefined processes, which can result in information that does not align with the characteristics. The internal control model for Sustainability Reporting will be based on a top-down analysis of risks and will be implemented at entity, subsidiary, division, operating unit, and functional levels, when applicable.

A necessary and important condition for the identification of risks is the prior definition and communication of the company's strategy and sustainable business objectives⁴⁵, as well as

⁴⁴ ESRS1-§30.b "...shall...disclose additional entity-specific information...and report thereon when the material sustainability issue is not covered by an ESRS or is covered at insufficient granularity."

⁴⁵ According to the COSO ICSR Framework, when defining these objectives, regulatory requirements, industry practices and the stakeholders that use the information must be considered, establishing the need to define objectives at the level of operations, external financial reporting, external sustainability reporting, internal reporting and those related to compliance.

establishing clear measurement and reporting principles so that they can be adequately applied in the organization and considered in the double materiality assessment, in the identification of IROs, and subsequently in the reporting for compliance with European Sustainability Reporting Standards.

As with financial information, it is necessary for ICSR to ensure a series of assertions or statements regarding Sustainability Information, for the purpose of representing the fundamental characteristics of the information, i.e. relevance and faithful representation of a company's activities, as well as the other qualitative characteristics for enhancing information (comparability, verifiability, and understandability) in accordance with ESRS 1. There is no universally accepted list of applicable assertions, and different approaches can be identified. For instance, these methods are outlined in UNE0081⁴⁶ for data quality assessment, in the International Standards on Auditing (ISA)⁴⁷, or within the auditing standards issued by the U.S. Public Company Accounting Oversight Board⁴⁸ (PCAOB). As stated in the latter standard, assertions should adequately identify the types of potential errors and provide an appropriate response to the risk of error in each required disclosure. This includes considering a reasonable possibility of containing a material error, whether individually or in combination with other errors.

The following assertions are proposed for ICSR, based on the ICFR guide:

- 1.** The transactions, facts and other events covered by the Sustainability Information exist and have been recorded at the appropriate time (existence and occurrence).
- 2.** The information reflects all transactions, facts, and other events that affect the entity or impact on people, the environment, and the government (completeness).
- 3.** Transactions, facts, and other events are recorded and valued in accordance with applicable standards (accuracy and valuation).
- 4.** Transactions, facts, and other events are classified, presented, and disclosed in the Sustainability Information in accordance with applicable standards (presentation, disclosure, and comparability).
- 5.** The Sustainability Information contained in the analysis of risks and opportunities reflects the rights and obligations to which the company is subject (rights and obligations).

Additionally, and as included in Appendix B of ESRS 1, it is necessary to consider the consistency that certain sustainability information should have with financial information (for example, breakdowns by Sustainable Taxonomy or others for revenue by type of activity, sector, etc.), in order to ensure the understandability of the Sustainability Report. The source of this data might be governed by ICFR, which may initially lower the inherent risk associated with these figures. However, it is important to note that consistency between financial reporting and sustainability reporting remains a crucial factor.

⁴⁶ UNE (*Asociación Española de Normalización*, or Spanish Association for Standardization): A guide that proposes a series of data quality characteristics: Accuracy, Completeness, Consistency, Credibility, Currency, Accessibility, Conformity, Efficiency, Accuracy, Traceability, Understandability, Portability and Retrieval. UNE 0081 Specification - Data Quality Assessment Guide | datos.gob.es

⁴⁷ International Standard on Auditing 315 - ISA-315-Full-Standard-and-Conforming-Amendments-2019 ([ifac.org](https://www.ifac.org)): Existence; Rights and Obligations; Completeness; Accuracy, Valuation and Allocation; Classification; Presentation.

⁴⁸ Public Company Accounting Oversight Board - Auditing Standard No. 15 | PCAOB (pcaobus.org): Existence or occurrence; Completeness; Valuation and allocation; Rights and obligations; Presentation and disclosure.

In line with what was mentioned above regarding the consistency between financial information and Sustainability Information, it is also necessary to consider other differences such as the definition of the scope⁴⁹ including companies under operational control and the value chain (vs. financial control criteria), forward-looking and longer-term views (vs. Historical data and 5-year projections⁵⁰) and use of Alternative Performance Measures (APM⁵¹) when disclosing financial information in the Sustainability Report.

Considering all the above, among the main sources of risk sources for Sustainability Reporting, the following can be mentioned:

4.2.c) 1. Failures in the identification of material issues.

The double materiality assessment is key to identifying the importance (materiality) of sustainability aspects in the company's value chain, forming the basis for all Sustainability Reporting. Although point 2.3 of this Guide highlights the primary challenges faced by Sustainability Information, the main risk factors associated with the identification of material issues are listed below:

- Failure to identify or specify sustainability objectives.
- Failure to determine risk appetite or to define tolerance limits.
- The lack of inclusion of financial and performance objectives related to sustainability objectives.
- Lack of allocation of resources for the fulfillment of objectives.
- The absence of a level of functional knowledge and training on behalf of those responsible and participating in key aspects, such as, for example, in the double materiality assessment.
- Inadequately analyzing the outcome of the identification of impacts, risks and opportunities and material issues in the company's framework, strategy, and financial information.
- An insufficient level of enterprise risk management maturity.
- The lack of coordination of the area responsible for the double materiality assessment with key business areas and assurance functions that provide a holistic view in terms of strategy, risks, impacts and opportunities.
- The lack of application of an identification methodology based on accepted frameworks.

⁴⁹ Although reference is made in several ESRS to the reporting scope aligned with that of financial reporting (e.g. "In preparing information regarding its business model and value chain, an enterprise shall take into account... c) the cost structure and revenues of its business segments, consistent with the disclosure requirements set out in IFRS 8 for the financial statement, where applicable..." SBM-1 -§AR.14), in the section on requirement related to the general value chain related information states that "The information on the reporting company provided in the sustainability statement shall be expanded to include information on...the company through its direct and indirect business relationships upstream or downstream in the value chain" ESRS-1 §63 and in the assessment occurrences, risks and opportunities refer to "...the entire consolidated group, regardless of the legal structure of the group" ESRS-1 §102

⁵⁰ Basis for estimating future cash flows: "Projections based on these budgets or forecasts shall cover a period of not more than five years, unless a longer period can be justified" International Accounting Standards (IAS) 36-§33.b

⁵¹ Alternative Performance Measures. For more information see the European Securities and Markets Authority (ESMA) guidelines on Alternative Performance Measures: ESMA publishes final guidelines on Alternative Performance Measures (europa.eu).

Moreover, regulatory changes require ongoing adaptation. Without a comprehensive approach, it may be challenging to identify material issues and impacts, risks, and opportunities.

Finally, it is fundamentally important that the area responsible for Sustainability Reporting coordinates with the risk/internal control and sustainability (where the reporting area is not part of the sustainability area) areas, to ensure the traceability of the assessment of material issues, impacts and risks in the general framework of the company's risk management.

4.2.c) 2. Errors or incompleteness in the presentation of the information.

The nature and reporting maturity of Sustainability Information are major risk factors. Among these we can highlight the lack of consideration of the qualitative characteristics of Sustainability Information (for example, lack of sufficient granularity, lack of forward-looking information, lack of value chain information, omission of negative data, or excessive emphasis on positive data that could cause bias or, in any other manner, present a misleading or unfaithful image of the sustainability profile of the entity, of a certain product or service or of an activity carried out by it, etc.); errors in the calculations implemented in the systems or failures in the supporting processes; human failures in the absence of systems; the level of formalization (procedures, instructions, controls) of the calculations and aggregations of the information reported.

Similarly, previously discussed aspects such as the organization's size; international presence; centralized or decentralized model; management function maturity (clear, defined and implemented roles and responsibilities), which directly affects the maturity level of the internal control function; or the level of sustainability-related knowledge of the supervising and reporting areas are all aspects that can increase the likelihood of errors in Sustainability reporting.

One aspect to remember is the fact that Sustainability Reporting covers the upstream and downstream stages of the value chain. In this regard, as seen in the previous Section 2.4 *Scope of Sustainability Reporting*, the entity's ability to obtain certain information will depend on factors such as its level of control over operations outside the scope of consolidation of the Sustainability Report or its contractual agreements, among others. Particular attention should be paid to information that is subject to judgments or estimates. In relation to the completeness of the information, we can mention, as risk factors, its level of quality and availability (considering its diverse origins), as well as the lack of a holistic view of sustainability objectives, internal control and risk management, impacts or opportunities, which would limit the ability to assess whether the information reported by the different areas includes all aspects implemented in the company. A final aspect to consider is consistency with the company's other public information, mainly financial information in line with EFRAG, CNMV and ESMA recommendations.

4.2.c) 3. Fraud.

The main risk factors for fraud in Sustainability Reporting are the definition of ambitious objectives, the subjective component of estimations in Sustainability Reporting, difficulty in determining forward-looking information, appropriate identification of the value chain, and the conflicts of interest due to bonuses or variable compensation linked to performance in sustainability matters, assigned to the areas that have responsibilities in the reporting of information, its approval or oversight (management or the Board of Directors). Companies usually have controls at the entity level related to fraud, depending, in each case, on their business, as well as other general controls, such as the code of ethics or a whistleblowing channel. However, consideration should be given to determining whether there is a need to develop internal control by implementing new specific controls related to these aspects (process controls).

Key risks to consider when managing Sustainability Reporting include greenwashing and social washing. These involve companies falsely claiming to be more environmentally or socially sustainable by giving stakeholders inaccurate or misleading information. This risk may arise intentionally or unintentionally.

Special attention should also be given to detailing the due diligence process, as further outlined and enhanced in the Corporate Sustainability Due Diligence Directive (CSDDD)⁵². This process involves the organization identifying, assessing, preventing, mitigating, and reporting on how it manages the negative impacts of its activities on both the environment and people. Due diligence must be integrated into the governance, strategy, and business model.

Finally, it should be noted that the risk of fraud in Sustainability Reporting is higher than for financial information reporting due to the high number of indicators subject to estimates and to criteria that may be subjective.

4.2.c) 4. Cybersecurity.

In addition to IT-related risks, the following risk factors are particularly relevant from a cybersecurity point of view: high digital dependency that this report requires, which leads to centralizing highly sensitive information necessary for reporting within a tool, including both sustainability and financial data; the growing trend of cloud-based tools, which increases the information security risk and requires control over data transfer mechanisms or; among others, the increase in ransomware that could compromise data, tools and systems. In general, this is a systemic risk for which organizations usually have specific controls, as well as measures for mitigation and transfer.

4.2.c) 5. Control environment-related risks.

In addition to the above the quantity of disclosure requirements, as well as their novelty, could increase the level of risk at a corporate level. The main situations are highlighted below:

- **Disclosure of confidential information.** Sustainability reporting involves disclosing information on strategy, plans, and actions. The risk that the required disclosures do not jeopardize information that has commercial value and is secret must be assessed. In this sense, regulations contemplate that organizations may omit classified and sensitive information related to intellectual property, innovation or related to strategies that may be confidential.
- **Uniformity in reporting.** The continuous evolution of sustainability reporting regulations (CSRD, climate change, due diligence) could lead to inconsistencies in reporting at distinct levels, agencies or administrations. Alignment with financial information should also be considered.
- **Regulatory changes.** Adaptation to regulatory changes could increase the associated costs, both derived from adapting to systems, and from having the necessary knowledge and/or support to be able to undertake them.

⁵² Directive (EU) 2024/1760 of the European Parliament and of the Council of 13 June 2024 on corporate sustainability due diligence and amending Directive (EU) 2019/1937 and Regulation (EU) 2023/2859.

- **Cultural and systems transformation.** The level of detail of CSRD requires a change in the management of risks, opportunities and impacts of material sustainability issues, which involves all levels and areas of the company throughout its operations. The implementation of internal control measures, policies, and measurements, among others, as well as the systems and processes that support them, must follow a sustainability management maturity strategy.
- **Management of Stakeholders' expectations.** The previous reporting of non-financial information (Law 11/2018 - Directive 2014/95/EU) has functioned as a mechanism for communication and management of expectations of the main stakeholders of the organization, apart from regulators, among which we can mention banking entities or providers of sustainability stock market indexes, among others. The absence of regulation on reporting information allows for responses tailored to stakeholders' expectations, since the trend in recent years has been for information to be shared directly on corporate websites for public consumption. In a framework of Sustainability reporting (CSRD) with more requirements, where the data to be reported is more precisely defined, it is key to maintain communication with stakeholders, and to align the business, communication and reporting strategy in order to continue providing information of value to stakeholders through the data point requirements.

4.2.d) Control Activities

As mentioned above, the development of risk matrices and controls over Sustainability Reporting is a key element in the implementation of ICSR. Additional information on this principal element of the internal control system is provided below.

As discussed in point 4.1.c of this document *Control Activities*, there are three types of controls:

- 1) General controls over ICSR, at the entity levels which may be shared with other systems/regulations such as ICFR.
- 2) Specific controls on ICSR (process level controls), related to the CSRD and involving controls on quantitative and qualitative information. Controls are essential for mitigating risks and therefore must always be associated with them.

In this regard, it is necessary to distinguish between two types of processes:

- 'Cross' processes: those that affect Sustainability Information as a whole, such as the Sustainability Report preparation process itself, the scoping, and the double materiality assessment process.
- 'Specific' processes: these refer to specific items equivalent to each of the topics/subtopics and their related ESRS (climate change, own personnel, etc.). An end-to-end review will be conducted for each process and within every significant business or company included in the reporting scope, commencing from data capture up to consolidation and reporting, whereby the necessary controls are determined to provide reasonable assurance as to the reliability of the information generated in each phase. The controls aimed at ensuring the reliability of the information will focus on the quality of the source data, with comparisons to the previous year or budget, among other aspects; review of estimates and hypotheses such as climate scenarios; evidence of secondary reviews and approvals (segregation of functions); controls over third-party data; roles or functions involved in the preparation of the information; and homogeneity of processes in different units (indicator sheets, policies and procedures that ensure uniformity), as well as the definitions and metrics of indicators.

In addition, and based on practical experience, the critical aspects on which to focus the control framework would be the following:

- Controls for the double materiality assessment process, focusing on risks, opportunities, and the calculation and estimation of environmental and social impacts on the business model.
 - The controls related to the establishment of objectives related to sustainability issues and their subsequent follow-up in terms of calculating those measurement indicators, how information is extracted, how it is processed and how deviations or alignments are reviewed, as well as the associated communication and reporting process.
 - Controls aimed at ensuring the integrity of forward and backward looking information and the scope of the entire value chain, through self-assessment questionnaires, variance analysis, awareness, and training campaigns, etc.
 - Controls aimed at guaranteeing the quality and availability of the data that make up the Sustainability Information (data validation, accessibility and security, continuous monitoring, etc.).
 - Controls to ensure the correct and full applicability of the European Sustainability Reporting Standards (process controls to ensure the integrity of qualitative and quantitative information).
 - Reconciliation controls of the information reported under different reporting frameworks, such as the European Union Taxonomy or the TFC⁵³ recommendations, as well as the consistency of the structure of the new Sustainability Report that brings together all this Sustainability Information.
 - Controls related to the reconciliation of monetary amounts included in the Sustainability Information and the corresponding information disclosed in the financial statements.
 - Controls related to scenarios and plans that ensure companies' business models and strategies are aligned with the transition to a sustainable economy, including limiting global warming to 1.5°C and achieving climate neutrality by 2050.
- 3)** Controls related to applications and information technologies (access, integrity, change management, confidentiality, physical security) involved in the key processes for generating, obtaining, and processing sustainability information.

⁵³ Task Force on Climate-related Financial Disclosures. This is an initiative created in 2015 by the Financial Stability Board (FSB) at the request of the G-20 leaders. Its main objective is to improve and increase the disclosure of climate-related financial information. This includes the risks and opportunities that climate change presents to companies and financial markets.

In line with the Sustainability Reporting risks detailed above, the following is a non-exhaustive list of risks and related control activities, which can be found in most ICSR models⁵⁴:

Risks	Control activities
Failure to identify material issues.	• A strategic plan, defined at the highest level, which includes sustainability objectives in a clear and precise manner, including, if applicable, appetite, tolerance levels and target metrics. • Approval of the aforementioned plan by the Board of Directors or delegated body. • A follow-up process for the implementation of the sustainability plan. • A documented process for calculating and approving double materiality, based on recognized methodologies, such as: consultation with managers responsible for risks related to the environment, governance, and social aspects; internal and external experts; and benchmark analysis with the sector. • Identify the value chain definition process and its validation process through internal and external experts, benchmarks, etc. • Verify alignment of the results of the double materiality assessment with the results of the organization's enterprise risk identification. • Approval of the double materiality assessment by the Board of Directors. • Internal and external audits on the process for identifying double materiality.

⁵⁴ To help the reader understand the relationship between risk and control, the following list is proposed. This list was drawn up by the Working Group that prepared this document. However, for some ICSR the wording and detail may be different from the example developed here.

Risks

Control activities

Errors or incompleteness in the presentation of information

- Identification of the relevant processes for the preparation of Sustainability Reporting. The processes should be formalized and documented.
- Clear reporting instructions issued by the coordinating area.
- Review policies and procedures to ensure that they are still in force, covering all relevant aspects and in a spirit of continuous improvement.
- Conduct reviews to ensure consistency between financial and sustainability information.
- A procedure for identifying and updating the scope of Sustainability Reporting.
- A procedure in place that clearly defines the information to be included in those material disclosures that are additional to those contemplated by the ESRS, based on a framework.
- A procedure in place to identify greenwashing or social washing practices.
- Identify the necessary competencies and verify that the professionals with responsibility for Sustainability Reporting possess such competencies.
- Supporting documentation on the criteria followed for the calculation of quantitative and qualitative data, as well as consistency with the previous year. In the case of divergences between periods, this should be explained.
- Automation of the process ideally through a specialized tool.
- Ensure the integrity, security, quality, and availability of information when using Excel files or data from multiple sources.
- Expert support in particularly complex calculations.
- Segregation of duties between the person performing the calculation and the person responsible for it. Supervisory controls.
- Consider including independent experts during the first years of adaptation to accompany the process.
- Training and updating programs in place on ICSR and sustainability issues in general.

Risks	Control activities
Errors or incompleteness in the presentation of information	• Preparation of risk and control matrices by process. Evaluate the use of GRC tools to automate the process.. • Identification of specific controls over third-party information providers for Sustainability Reporting: – Selection criteria for third parties should include the evaluation of their internal control practices. – Evaluate third parties' compliance with the organization's policies and procedures. – Test the information (recalculations, reconciliations, etc.). – Third party certification (SOC report or similar). – Perform internal audits. – Follow up on the deficiencies detected. • Implement self-assessment techniques for the design and effectiveness of controls. • Identification of roles and responsibilities in Sustainability Reporting. • Communication to employees of their responsibilities regarding Sustainability Reporting. • Evaluate sources of information through questioning, process documentation, document review, inspection, recalculations, and reconciliations. • Analyze the independent reviewer's recommendations regarding Sustainability Reporting.
Risks	Control activities
With respect to the control environment	• Policies on confidentiality and disclosure of sensitive information. • Segregation and assignment of duties for the reporting process. Procedure/Manual for the generation of Sustainability Reporting and alignment with financial information. • Monitoring and follow-up of regulatory changes. • Verification of compliance with sustainability maturity strategies. • Assessment of the degree of alignment with business strategies, communication and reporting on sustainability.

Risks	Control activities
Fraud	• General controls (control environment) should encompass the principle of reliability of information, both financial and non-financial, within the code of ethics. • Recalculations, double validations. • Segregation of duties and supervisory controls. • Approvals by management and the Board of Directors. • Clarity and documentation of indicator calculation. • Review of the whistleblowing channel to identify sustainability-related issues. • Fraud risk reviews of data provided by value chain managers (based on alternative formulas such as sample analysis, internal audits, third-party validations, certifications, verification reports, etc.).

Risks	Control activities
Cybersecurity ⁵⁵	• General controls over information systems that guarantee, among other aspects, security of access to data and programs, control over changes, correct operation of these aspects, continuity, and the adequate segregation of functions. • Sustainability reporting often uses spreadsheets and specifically developed programs. In these cases, the information must be protected, preserved, and periodically reviewed to ensure its integrity. • When commercial platforms are used to assist in Sustainability Reporting, SOC⁵⁶ type certificates should be requested as part of the control process for such platforms.

⁵⁵ In this case, it details controls related to cybersecurity, as a key aspect of risks associated with Information Technology.

⁵⁶ Refers to reports and certifications related to the security of a company's systems and processes, issued according to SOC (System and Organization Controls) standards. These reports are mainly used to evaluate internal controls in terms of data security, confidentiality and privacy

4.2.e) Documentation of information definition processes and associated controls.

The following are suggested elements necessary to document the Internal Control System for Sustainability Reporting:

- 1) A procedure for calculating double materiality, in accordance with EFRAG's Materiality Assessment Implementation Guide and that of the *Instituto de Contabilidad y Auditoría de Cuentas (ICAC)*⁵⁷.
- 2) Identification of relevant business processes that affect Sustainability Reporting based on a double materiality assessment. By way of example, some process-owner areas that may be relevant to Sustainability Reporting are listed, although they may not be present in all companies.

Scope of Disclosure	ESRS	Affected areas
General Requirements	1 General Requirements	Strategy
	2 General Disclosures	Business risks Strategy Institutional Relations
Environmental Issues	E1 Climate change	Environment Operations General Services
	E2 Pollution	Environment Operations General Services
	E3 Water and Marine Resources	Environment Operations General Services
	E4 Biodiversity and Ecosystems	Environment Operations General Services
	E5 Circular Economy	Purchasing Production
Social Issues	S1 Workforce	Human Resources Personnel Administration
	S2 Value chain workers	Purchasing Operations Production
	S3 Affected groups	Social Action Compliance
	S4 Consumers and end users	Quality Customer Management
Governance	G1 Business conduct	Corporate Governance Compliance

⁵⁷ Implementation Guide - EFRAG IG 1: available on the ICAC website: <https://www.icac.gob.es/sostenibilidad/normativa>

In addition to the processes related to reporting standards, the general requirements of the European Sustainability Reporting Standards call for organizations to provide additional entity-specific information if a standard does not sufficiently cover a relevant impact, risk, or opportunity. This helps users understand the sustainability impacts, risks, or opportunities related to the organization. For this reason, the areas or processes not expressly mentioned in the regulations, but which could be relevant, should be included; for example, matters relating to Taxes, Information Security, Regulatory Compliance or R&D&I Management, among others, in line with Section 51.a. of CMNV Technical Guide 1/2024 on Audit Committees of Public Interest Entities.

- 3) An ICSR Manual containing the Sustainability Reporting procedure should be in place, describing the activities to be conducted by all the areas involved to ensure the correct reporting of the company's Sustainability Information. These procedures may include, among others, the following points:
 - A matrix of roles and responsibilities.
 - Process for defining and communicating the reporting scope.
 - Criteria used to calculate/report the information included.
 - Communication process, based on a double materiality assessment, including material issues, their impacts, associated risks and opportunities and the breakdown requirements (data points) that must be disclosed to the areas responsible for the information.
 - The reporting timetable depends on the type of information since there is qualitative or narrative information that can be reported before the end of the year. However, most quantitative, or numerical information must be reported as at year-end.
 - Information reporting tools, such as the use of reporting templates or market report fulfillment tools.
- 4) There must be reporting instructions for each of the Sustainability Reporting disclosure requirements, aligned with the guidelines and procedures that govern financial information. In this sense, the development of a "Sustainability Reporting Manual", covering the method for defining the reporting scope, the calculation methodology for indicators, how estimates should be calculated, or which external sources should be used (e.g. for emissions calculation), helps those responsible for reporting understand exactly how they should report the data to be disclosed
- 5) Development of risk and control matrices that include, for example, the following elements:
 - **Associated ESRS** standards: the alphanumeric code included in ESRS.
 - **Description of the associated ESRS indicator:** narrative description of the response to each breakdown requirement.
 - **Data typology:** narrative, semi-narrative and numerical.
 - **Data origin:** sources from which data are obtained, information systems, policies, procedures, other sources.
 - **Section of the Sustainability Report** where the data is reported, based on the established index.
 - **The material issue** is associated with control.

- **Risk description and risk level:** see previous Section 4.2.c) *Risk Scoping*.
- **Control code:** internal control identifier.
- **Control Description:** Include the input (the information needed to execute the control), the characteristics of the control (detective or preventive, manual or automatic, periodicity of the control, etc.), what the control consists of (description of how the control is carried out) and the expected output (evidence arising from the execution of the control). In the case of quantitative indicators, the method of calculation of the indicator shall be included.
- **Assertions:** see previous Section 4.2.c) *Risk Scoping*.
- **Formalization of the control/evidence:** this field indicates where the control, procedure, policy, etc. is formalized.
- **Importance:** "Key" or "Non-Key", depending on the degree of mitigation of the risk associated with the control.
- **Process.**
- **Procedure.**
- **Organization.**
- **Person(s) responsible for executing control:** see next step 6) Development of matrices for roles and responsibilities.
- **Person(s) responsible for supervisory control:** see next step 6) Development of matrices for roles and responsibilities.

6) Development of role and responsibility matrices. For example:

- **Person(s) responsible for executing control:**
 - Execute control tasks.
 - Communicate any deviations that may occur.
 - Assess the design and effectiveness of the control.
 - Report to those responsible for control.
 - Custody of the evidence generated by control activities.
 - Implement improvements to existing controls.
- **Person(s) responsible for the control:**
 - Monitor ICSR within the area of responsibility.
 - Report to the ICSR manager.
 - Propose improvement actions.
 - Propose and implement new controls.

- **Person(s) responsible for ICSR:**

- Receive, compile, and analyze the information reported by each of the areas.
- Participate in the identification of new risks and the implementation of controls within the process.
- Collaborate in the proposal of improvement actions and resolution of incidents.
- Alerts on changes in regulatory scenarios.

- **Internal Audit:**

- Assess ICSR. In many organizations, Internal Audit also promotes change and collaborates actively in the design of the model as an expert in internal control, risk management and governance, in addition to providing business knowledge and a global perspective. In this regard, we are reminded that any advisory role, which is additional to its assurance role, must be conducted without affecting its independence and objectivity.
- Preparation of the annual Internal Audit Plan, establishing review and update activities.
- Communicating the results to the Audit Committee.
- Follow-up of recommendations.

- **Business risks:**

- Ensure integration of double materiality assessment into the ERM model.
- Update the elements of the ERM system (policy, risk catalog, scales, consolidation model, etc.).
- Advise the sustainability area as an expert in ERM methodologies.

- **Audit Committee:**

- Plan the internal audit of ICSR.
- Oversee the effectiveness and proper functioning of ICSR, proposing recommendations for improvement.
- Communicate the results to the Board of Directors.
- Follow-up of recommendations.
- Maintain the relationship with the independent assurance provider of Sustainability Reporting, analogous to the relationship with that with external auditors.

- **Sustainability Committee (if any):**

- Guide, monitor and evaluate the degree of compliance with policies, best practices, and specific action plans in the area of sustainability.
- Determine the general principles and criteria that should govern the content of the Sustainability Report in accordance with applicable regulations.

- **Board of Directors:**

- Ultimately responsible for ensuring that all information is adequate and effective regarding Sustainability reporting.

- 7) Development of a detailed ICSR Policy and Manual that includes the procedure for internal control and oversight of Sustainability Reporting including, for example, the procedure for identifying processes, risks, and controls relevant to Sustainability Reporting, procedures for calculating indicators, roles and responsibilities, and internal and external assessments of Sustainability Information.
- 8) Preparation of flow charts or narratives showing the process for calculating and reporting the main quantitative and qualitative indicators.
- 9) Preparation of a systems map and a risk and control matrix of the general controls over information systems (ITGCs) linked to Sustainability reporting.

4.2.f) Maintenance, updating and monitoring ICSR activities.

To ensure the effectiveness and efficiency of ICSR, it is crucial to conduct regular maintenance, updates, and monitoring of its operations. These activities ensure that the overall ICSR and control activities continue to be adequate amid changes in the operating, regulatory, and technological environment.

Normally there are various activities that are essential for the Internal Control System and should be included in the “annual internal control plan”. This plan normally revolves around the following objectives:

- Clarity in the assignment of responsibilities for each activity or process to be executed.
- Elimination of unnecessary redundancies.
- Management of peak or excessive workloads at certain times of the year.

The following are the main activities to be conducted as part of this plan:

4.2.f) 1. Maintenance and updates.

For ICSR to fulfill its main objective relative to the reliability of Sustainability Reporting, it is essential that it be able to respond to changes that may occur at various levels, among which the following can be highlighted:

- Structure: either external (new regulations, new stakeholder requirements) or internal (new corporate scope, new activities, new countries of operation, etc.).
- Operation: in terms of the performance of its main elements.
- Allocated resources: particularly regarding their adequacy and suitability.
- Software tools used.

Therefore, the following activities are usually conducted:

- a) ICSR coverage update - Scoping: Conduct a risk analysis periodically, usually annually, or when significant changes occur to ensure the ICSR model remains valid and relevant to the company's needs (see Section 4.2.c).

b) Documentation update, particularly for two main elements:

- i. Maintain accurate and up-to-date records of all internal control processes, procedures, and policies (see Section 4.2.e of this document).
- ii. Update internal control manuals and guidelines, as necessary.

4.2.f) 2. Monitoring:

The responsibility for monitoring ICSR, regardless of what the Internal Audit function considers appropriate to include within its own plan, should be assigned within the organization, typically to the function responsible for its maintenance. This monitoring, as is the case with other internal control models, usually consists of the following main activities:

- a) Periodic Review of Controls:** by means of different monitoring activities that are adapted to the nature of each of the controls, with the objective of verifying whether they are functioning properly:
 - i. They continue to cover the risks as planned (Test of Design, or “ToD”).
 - ii. They are being executed as described in the risk and control matrix and are operating effectively, in such a way that they cover the risks for which they were designed (ToE or Test of Effectiveness).

The planning of these activities throughout the year (or years) will respond to each company's needs and available resources. Detected incidents should be monitored to ensure they are being addressed.

These activities may be conducted internally or by a third party, which may provide diverse levels of assurance on the controls or ICSR in general.

- b) Periodic monitoring:** in addition to the above, it is also advisable to periodically monitor, to the extent possible, certain elements beyond the controls of the model, such as key activities and transactions, to identify irregularities and deviations through the use of automated monitoring tools that allow detection and reporting of anomalies in real time, or of companies or subsidiaries that systematically report failures in the execution of controls, etc.
- c) ICSR Diagnosis:** in line with other control models, some companies conduct an analysis of their model from a theoretical point of view with respect to best practices or a methodological framework, to check whether all the necessary elements are being covered.

4.2.f) 3. Reporting to the governance, management, and supervisory bodies.

To respond to the demands of stakeholders and the regulations of the markets in which they operate, as well as to ensure the early detection of events that have an impact on ICSR, organizations must have, as discussed in the section above, formalized information and communication mechanisms.

Such mechanisms seek to facilitate continuous improvement through ordinary and extraordinary reporting to achieve the following objectives:

- Report on the evaluation of the design and effectiveness of ICSR and communicate material weaknesses.

- Report relevant changes in the company that may have an impact on ICSR.
- Report on the day-to-day performance of ICSR through performance indicators linked to it.

The circumstances in which these communications must take place depend on the particularities of each organization. However, in general, the elements that make up the reporting model are as follows:

- 1) Responsibility** (who reports).
- 2) Time of occurrence** (when reporting takes place).
- 3) Content** (what is reported).

By combining these elements, the different alternatives described below are illustratively configured:

<i>Practical example</i>	Responsibility	Time of occurrence	Content
Ordinary Report	• ICSR control area or areas responsible for this function	Semiannual	• Follow-up of incidents and action plans at key control level.
	• ICSR control area or areas responsible for this function • Sustainability area	Annual (quarter following the end of the corresponding fiscal year)	• Diagnosis vs. COSO and this Guide, as a level of compliance with the principles of effectiveness and the corresponding action plans, if applicable. • Proposed ICSR description update for the Sustainability Report. • Definition of ICSR scoping and proposal of a work plan for the following fiscal year, including the resources to be used and the deadlines to be met.
Extraordinary Report	Depending on the type of change / incident	When significant changes or incidents occur	In the event of a change or significant incident in ICSR, this shall be immediately communicated to the ICSR Control Area or areas responsible for this function and, where appropriate, to Internal Audit, regardless of the established reporting schedule. These areas will review the reported item and jointly assess the relevance of the change, incident or issue and the appropriateness of reporting to the sustainability area.

4.2.f) 4. Communication and training plan for all the areas involved.

In addition to the above activities, ICSR must, in turn, have other cross-cutting mechanisms aimed at strengthening its functioning. It must have communication and training activities, which have the following objectives:

- Inform and make all employees aware of the importance and benefits of ICSR.
- Ensure understanding of policies, procedures, and internal controls.
- Promote a culture of transparency and compliance.

However, activities should be tailored to distinct groups within companies, identifying the different stakeholders within the organization (senior management, middle management, operational staff, etc.), whereby messages and the form of communication are adapted according to the level and functions of each group. These messages must respect the following:

- Define clear and consistent messages on the importance of internal controls over Sustainability Reporting.
- Explain the roles and responsibilities of each employee in maintaining an effective control system.
- Communicate compliance expectations and the consequences of not following internal controls.

In general terms, the main objective is that all those involved in ICSR know what their role is and, therefore, what is expected of them for the proper functioning of the System. In fact, the appropriate training to be provided to those involved in the Sustainability Reporting process should be covered within the entity-level controls (ELCs). In turn, this objective is usually achieved through the following initiatives:

- a)** Notify staff of any changes in applicable regulations, both external and internal, i.e., policies and procedures related to Sustainability Reporting in general or ICSR in particular.
- b)** Provide regular training to employees regarding the organization's internal controls and procedures.
- c)** Establish activities to monitor the effectiveness of training measures.

A communication and training plan for ICSR is essential to ensure that all participants comprehend their roles and responsibilities concerning internal controls, and that information flows effectively within the organization.

4.2.f) 5. Supporting technologies for the preparation of information and internal control.

The use of different technologies is a key factor for an effective and efficient reporting and control model, given the complexity and volume of information to be managed. It is necessary to distinguish between the technologies used for the reporting model and those used to support the internal control system.

Specifically, these technologies are grouped into three broad categories:

- 1)** Specific supporting technologies for the preparation of Sustainability Reporting, which reinforce and bring efficiency to all activities within the Sustainability reporting process from source to final recipient. Nevertheless, given today's rapidly changing environment and the important level of manual intervention associated with Sustainability Reporting, tools must continue to evolve to ensure the appropriateness and completeness of this type of information.

- 2)** Internal control technologies allow the recording and traceability of all control activities and their monitoring, including the maintenance, updating and supervision of ICSR.
- 3)** In common with the two previous groups, we can highlight technologies for process automation, data analytics, OCR⁵⁸, machine learning, artificial intelligence, etc. These technologies allow, on the one hand, for an increase in the effectiveness and efficiency of processes and controls and, on the other, improvement in the scope, efficiency, and ease of use for monitoring and reporting of controls.

Finally, the technologies that can be used depend on different parameters, among which the following can be highlighted:

- Volume and complexity of the Sustainability Information managed, including the details of its sources.
- Available resources, both for the initial investment and parameterization to be conducted, as well as for subsequent maintenance.
- Knowledge and experience of the team involved in the preparation of the information and the internal control system.
- Maturity of processes and controls supporting reporting.
- Degree of integration with different assurance systems used by other control models (for example, compliance models or ICFR).

⁵⁸ Optical Character Recognition.

5. Assessment of the Internal Control over Sustainability Reporting System.

The ICSR evaluation process identifies risks and internal control deficiencies that may impact compliance with its objectives. For this assessment, companies can draw inspiration from the Guide issued by the working group established by the CNMV regarding internal control over financial reporting. They may also consider the guides issued by COSO⁵⁹.

However, in the preliminary stages of the ICSR evaluation, the state of implementation and the degree of development with respect to the ICFR should be considered. The maturity level of ICSR should evolve in the coming years to reach the objective of being verifiable with reasonable assurance, as required by the CSRD regulations, and to provide a response to the supervisory requirements of the Board of Directors.

5.1. Evaluation of the design of existing internal control structures.

To begin with, it is important to understand the organization's strategy, governance model, associated risks, and specific sustainability factors and how these elements are integrated into and impact its operations and decision-making processes.

Additionally, the approach adopted for the implementation of ICSR must be understood, considering the degree of maturity and the process followed. The implementation may be conducted in phases according to a development roadmap, given the volume and diversity of the information to be published. Therefore, it is important to understand the criteria and factors forming the basis for prioritizing information to be used for building ICSR (result of the double materiality assessment, company strategy, information identified as Sustainability-related, risks, complexity of the information to be prepared or reported, quantitative or qualitative data, etc.).

Additionally, to conduct a proper evaluation of the ICSR design, as previously mentioned, it is essential to have comprehensive documentation prepared during the implementation process. This documentation should facilitate an understanding of the existing processes and clearly identify the objectives, risks, and the controls implemented to mitigate those risks.

Specifically, the following should be considered:

5.1.a) Evaluation of the risk identification process: completeness and relevance.

To respond to this objective, the systematic process of risk identification must be understood, obtaining and analyzing existing documentation (risk and control matrices, descriptive documents of the processes, etc.) and holding fact-finding meetings with those responsible. Additionally, to reinforce this understanding, other sources should be considered, such as flow charts and recommendations made by external reviewers and internal auditors, among others.

⁵⁹ <https://www.coso.org/guidance-on-ic>

The risk identification evaluation will determine existing risks and any overlooked present or future risks that could significantly impact the organization's reputation, profitability, and long-term sustainability. When applicable, the inclusion of unidentified risks should be evaluated. These risks may be linked to existing control or necessitate the development of a new control to address them. Emerging risks must be systematically considered in each evaluation process as this is not static over time.

5.1.b) Identification of controls that mitigate risks: sufficiency and design.

Control design testing seeks to evaluate whether all the necessary controls have been identified to cover the identified risks, and whether the existing controls are adequately designed to prevent or detect errors in Sustainability information. Consideration should be given to redesigning current controls or adding new ones, linking them to emerging or existing risks, whenever deficiencies in their design are detected, to ensure the reliability of the Sustainability Reporting. As with ICFR, the identification of key controls⁶⁰ during the design evaluation process is particularly relevant.

The proposal for redesigning a control may be related to its constituent elements: scope, description, existing evidence, incorporation of new evidence, frequency and those responsible for executing and supervising the control.

5.1.c) Information technology controls (IT).

Sustainability Information is very heterogeneous and comes from records included in multiple IT systems across the organization. As with ICFR, to develop engagements aimed at verifying the proper functioning of systems that support Sustainability Reporting, it is essential to define the corresponding information technology controls across the various technological layers, i.e., IT application layer and technological infrastructure layers (operating systems and databases, or analogous components). To this end, it is necessary to draw up an inventory of the applications used in the capture and processing of data used for Sustainability Reporting, prioritizing the definition of controls over those applications involved in the processes related to the most relevant information.

If the identified applications are the same as those covered by the ICFR, consideration should be given to potential synergies and existing IT controls.

5.1.d) Controls related to the Value Chain.

The CSRD contemplates the inclusion of the organization's entire value chain in the report. This implies the incorporation of controls focused on covering the risk of material error in the data related to the value chain, as well as control activities related to the inclusion of activities beyond the organization within the reported scope, and to the monitoring of variations.

⁶⁰ A key control is one that is designed for the prevention of material errors.

5.2. Evaluation regarding operation and effectiveness.

To ensure that ICSR is operating as expected and that the planned objectives are being achieved, the design evaluation process should be completed with an assessment as to how those controls rated as effective are functioning, following a twofold approach for design and implementation.

To assess whether controls are operating effectively, certain characteristics will be taken into account, such as the type of control (manual or automatic); nature (preventive or detective); periodicity (annual, half-yearly, quarterly, etc.), and the level of risk associated with the control, among other factors. Based on the above, the most appropriate review technique will be applied (interview, observation, inspection, etc.) or a combination of these techniques to obtain greater audit evidence.

Evidence can be obtained directly by reviewing the control and supporting documentation available for its execution, by requesting additional information, or through monitoring other procedures. Depending on the type of information to be assessed, several types of evidence will be requested. It is important to bear in mind that Sustainability information includes many estimates and scenarios on short, medium, and long-term objectives that should be adequately supported for review.

Deficiencies in the execution of controls can occur for several reasons, such as their initial design, incorrect execution, or failure to carry out the control, among others. If key controls are not functioning or are not fully effective, consideration should be given as to the existence of compensating controls and assessed in terms of the effectiveness of their operation.

The assessment of control operations should include an evaluation to determine if they are conducted and overseen by individuals with adequate authority and competence to perform the control effectively. In this regard, given the lower maturity in the implementation of ICSR compared to that of the ICFR, awareness and training in the reporting culture of the operators and supervisors of the controls is particularly relevant.

5.3. Evaluation of internal control weaknesses.

An internal control weakness in Sustainability Reporting is any deficiency in processes and systems that ensure its reliability and compliance with the characteristics discussed in Section 2.2 *Qualitative Characteristics* of this document.

The evaluation of a control system involves identifying cases in which the defined controls do not mitigate the identified risks. Assessing the relevance of this situation involves determining the potential impact on the accuracy, completeness, and reliability of the data of such weakness, and classifying the severity of the finding based on its current relevance and potential impact.

The identification of weaknesses may lead to the conclusion that controls do not exist or that controls are incorrectly designed or incorrectly executed, which may affect the integrity of the information, resulting in incomplete or inaccurate data. Lack of consistency and coherence may lead to discrepancies in the information reported, as well as in the accuracy of estimates and forecasts.

The evaluation of weaknesses in controls is based on several key criteria that affect the quality of Sustainability Reporting. In this regard, the steps for assessing the severity of the finding

involves: identifying the weakness and documenting it, including the nature of the problem and the supporting evidence; assessing the impact on the accuracy of the data, concluding whether the finding affects the accuracy of the reported data; understand the origin of such incidence (data source, calculation errors or non-application of policies and criteria, among others); assess its impact on the completeness, consistency and comparability of the information and, finally, classify the severity of the finding (high-medium-low), based on its potential impact.

In this context, a valuable tool for determining the level of impact is the double materiality assessment⁶¹, which assists in identifying and prioritizing the most significant sustainability aspects for the organization and its stakeholders. It is advisable to utilize this tool to establish the relevance of the identified weakness.

It is also best practice to identify a tolerable level of error in the evaluation of Sustainability Information, understood as the minimum threshold below which it is not necessary to conduct review work. However, it is important to establish procedures to avoid the accumulation of minor errors that, combined, may be significant. In any case, it will be necessary to carry out an internal analysis to adapt this threshold to the nature and characteristics of each organization.

As the external independent assurance provider's review progresses towards reasonable assurance, it is important to understand materiality levels when conducting an engagement on Sustainability Reporting. This understanding helps avoid inconsistencies in assessing weaknesses which, if identified, could result in exceptions in the engagement report.

5.4. Periodicity and scope of the evaluation.

The process of monitoring an entity's internal control system may vary depending on factors such as the nature of the entity, its regulatory environment, or inherent risks. Given this situation, the following are general recommendations that could be applied in relation to the periodicity and scope of the evaluation:

- a) Annual evaluations:** A complete evaluation of the internal control system should be conducted at least once a year. This allows any significant deficiencies to be identified and addressed before they affect the reliability of the information. An annual evaluation of the double materiality process is recommended, since it will determine the breakdowns to be reported in the Sustainability Report.
- b) Quarterly or semi-annual assessments:** In larger organizations, or in highly regulated industries, more frequent assessments, such as quarterly or semi-annual, may be beneficial.
- c) Ongoing evaluations:** In addition to periodic evaluations, it is advisable to implement an ongoing monitoring process. This involves the regular review of certain key controls throughout the year to ensure that they are operating effectively.
- d) Ad-hoc evaluations:** These evaluations may be necessary in response to specific events, such as changes in organizational structure, changes in the double materiality assessment, new breakdowns to be reported, changes in the value chain or in the corporate scope, implementation of new technologies, significant changes in information gathering processes, or in response to incidents of fraud or errors.

⁶¹ Addressed in Section 2.4 *Scope of Sustainability Reporting* of this document.

e) Pre-implementation or initial design evaluations: In the ICSR design processes, reviews will be carried out on its correct design in accordance with the COSO Internal Control Integrated Framework and, subsequently, initial implementation reviews of the control activities to verify that they have actually been established in accordance with their conceptual design.

f) Post-implementation evaluations: After implementing new controls, processes, or systems, it is important to perform an evaluation to ensure that they are working as expected and to make the necessary adjustments, if necessary.

In short, the entity must define and specify the type or types of evaluation it will carry out for its internal control of Sustainability Reporting.

However, the scope of the evaluation of ICSR, in each period, shall be subject to the judgment of the Board of Directors responsible for the management of the model, and should be based on the objectives and risks of Sustainability Reporting and the means available to the organization. An evaluation covering the entire ICSR may be conducted for each fiscal year, or over several fiscal years, whereby the following may be carried out:

- 1) Establish policies for rotating Sustainability Report indicators or sections for periods not exceeding two or three years, based on factors such as: (i) results of previous evaluations; (ii) existence, or not, of changes in the control process; (iii) existence, or not, of changes in the information gathering process; (iv) existence, or not, of changes in the scope of the entity's business model or strategy; (v) existence, or not, of regulatory changes; and (vi) risk of errors, taking into account their probability, nature and impact.
- 2) Consider particularly critical processes in the preparation of Sustainability Information: process for assessing materiality, determining the value chain, critical indicators, general entity controls, general IT controls, etc.
- 3) Consider changes in the business model, in the markets in which the entity operates or in its value chain (e.g., substitution of suppliers), as well as changes in applicable regulations or significant organizational changes.

If the assessment is conducted with the objective of determining its effectiveness as of a specific date, the scope of testing should focus on the risks and controls in place as of that date.

5.5. Certification of Sustainability Information.

A formal certification process or structure can be implemented in ICSR on an annual basis, coinciding with the preparation of the Sustainability Report. This process should provide a series of assurances based on the responsibility of the individual or firm signing the certification.

This certification process, whose system and level of granularity can be adapted to the characteristics and degree of maturity of ICSR in the organization, seeks to provide confidence, both to the different agencies and to the main executives of the organization, regarding the process for preparing Sustainability Information, prior to its formulation by the Board of Directors.

This process reflects the way the information is generated, both in the organization and, where appropriate, in the subsidiaries that make up a group. In this structure, company leaders certify the reliability of the Sustainability Information, and the effectiveness of the internal control system established to guarantee this reliability within their areas of responsibility. This certification process is

supervised by the corresponding body (Audit Committee, Sustainability Committee, if any, etc.), and the conclusions obtained in the sessions in which the Sustainability Report is formally formulated are communicated to the Board of Directors.

5.6. The internal auditor.

The Internal Audit Function plays a significant role in the evaluation and monitoring of Sustainability Reporting. As an independent function, Internal Audit supports the Board of Directors in its responsibility to supervise ICSR, evaluating the actions of the management units and control units, to mitigate the risks linked to both compliance with disclosure regulations and the accurate presentation of information.

The Internal Audit Function can take on two fundamental activities in the evaluation of Sustainability Reporting, while always maintaining, where appropriate, its independence and objectivity.

- 1) Implementation of a model for periodic evaluation of ICSR, to obtain sufficient evidence of its proper design and operation, identify areas for improvement and escalate control deficiencies and relevant opportunities for improvement to the organization's governing bodies. It is also advisable to carry out initial design evaluations, given that control deficiencies for this aspect are highly relevant for implementing a robust ICSR from the outset.
- 2) Review of the Sustainability Reporting process, ensuring its integrity and transparency. Additionally, there is coordination with external independent assurance providers to ensure comprehensive and effective audit activities, with access to their findings and following up on recommendations.

To this end, Internal Audit must ensure that its Audit Plan encompasses evaluations of both ICSR and the establishment of procedures for reviewing Sustainability Information, thereby providing adequate coverage of the significant risks identified by Internal Audit in relation to Sustainability Reporting, while considering the internally established periodicity and rotation criteria.

Internal Audit's review of ICSR evaluates the design and effectiveness of preventive and detective controls over risks related to Sustainability Reporting. This review process should cover, among others, the following aspects:

- **Governance:** This involves assessing the various levels of oversight performed by the Board of Directors, existing specialized Committees, and Senior Management in ensuring alignment with the sustainability strategy. This includes the adequacy of the allocation of resources, verifying the correct segregation of functions among them, their training in sustainability, as well as the internal and external communication process.
- **Sustainability reporting policies, methodologies, and frameworks:** evaluate the sustainability reporting strategy, which should incorporate clearly defined methodologies and frameworks covering the completeness of material information. The absence of methodologies and clear frameworks may result in inconsistencies and lack of comparability of Sustainability Information, limiting Internal Audit's ability to validate it.
- **Consistency and comparability of data:** It is recommended to adopt internationally recognized standards. When recognized standards are insufficient, internally develop and document clear

methodologies for generating relevant sustainability information. In this context, it is essential for internal auditors to have an overall view of the relevant reporting requirements, upon having reviewed the double materiality assessment developed by the organization.

- **Risk assessment and management processes:** review the sustainability risk identification, assessment, and management processes implemented by the entity's management, focusing on the key aspects identified during the materiality assessment, with particular attention to potential omissions or risks that could include elements of greenwashing and/or social washing in Sustainability Reporting.
- **Internal Processes for the Preparation of Sustainability Information:** This involves overseeing the internal processes for collecting and preparing sustainability information, ensuring the accurate delineation of the reporting scope, and applying appropriate policies and procedures. Emphasis is placed on the processes for obtaining data and relevant sustainability information, whether through newly defined ad-hoc processes or by integrating with existing organizational processes.
- **Availability of the necessary data for sustainability reporting:** conduct an assessment of the availability of information, for which it is essential to identify the relevant information management systems, evaluate the processes for data collection (from internal or third-party sources) and validate compliance with the defined methodologies.
- **Certification processes** for Sustainability Reporting and ICSR controls.

The Audit Plan should be reassessed periodically to ensure that the review processes cover the evolution of procedures and internal controls due to, among other things, regulatory developments, changes in risk assessment or stakeholder expectations.

In the absence of effective internal control structures, and during the process of building and strengthening ICSR, Internal Audit's focus can be on substantive testing for coverage of associated risks until remediation.

In the initial stages of implementation of CSRD and operation of ICSR, Internal Audit may adopt a progressive approach for evaluation linked to the degree ICSR maturity. As part of this progressive implementation, it is recommended to initially include reviews focused on the most critical aspects in the Annual Internal Audit Plan, considering those control components that provide greater coverage for the processes for double materiality assessment, data capture and preparation of the Sustainability Information (general controls and systems). Where applicable, the more mature processes that are already in place for ICFR can be considered.

Internal Audit's communication of control weaknesses and follow-up on recommendations to address them is a key component in enhancing the ICSR's effectiveness. This process adds substantial value to the entity's risk management and aids the Board in overseeing operations by facilitating the implementation of corrective actions to strengthen internal processes.

Furthermore, Internal Audit can also play a key role in supporting senior management by providing advisory services and making recommendations to improve internal control processes and collaborating with other departments to strengthen ICSR, as well as using its knowledge of the entity and the control environment to identify internal control processes or controls already implemented that may be applicable to Sustainability Reporting, thus optimizing the effectiveness and efficiency of the processes. In this context, as highlighted throughout this guide, it is crucial to remember that these advisory tasks must be performed while maintaining independence and objectivity.

5.7. The roles of the independent assurance provider for Sustainability Information.

The external independent assurance provider has two main roles:

5.7.a) Independent assurance provider's review of the Sustainability Report in compliance with regulations.

The CSRD establishes that the Sustainability Report shall be subject to an independent external verification, to check the conformity of the Sustainability Information reported with applicable presentation requirements.

To perform this assurance, the independent assurance provider shall comply with the technical standards applicable at any given time and obtain sufficient knowledge and understanding of the entity's internal controls to identify and assess the risk of material misstatement of Sustainability Information, although this is not for the purpose of expressing a conclusion on the effectiveness of the entity's internal control.

With regard to the level of assurance of the verification, the European legislator has opted for a progressive approach, whereby at an early stage there is an obligation to issue a conclusion based on a limited assurance review, and, in a second stage from 2028, when the European Commission has adopted standards at European level for a full audit, moving on to issue an opinion based on reasonable assurance.

In a limited assurance engagement, the objective is, in general terms, to reduce the risk of the engagement to an acceptable level depending on the circumstances. It involves a higher risk than the reasonable assurance engagement, given that the nature and scope of the procedures and tests performed are less extensive, especially as they relate to applicable systems, though they must provide a level of security that enhances user confidence in the verified information.

In a reasonable assurance engagement, detailed tests are performed to obtain greater confidence and assurance on the information reported, with the same degree of assurance as is provided in the auditor's report on the financial information, especially as it relates to internal control systems. The independent assurance provider draws a positive conclusion as to whether the information has been prepared in all respects as required by the European Sustainability Reporting Standards.

The independent assurance provider may limit the scope of the engagement on the internal control system based on professional judgment and the level of assurance required by the entity (limited or reasonable). However, the independent assurance provider will not issue a specific conclusion on ICSR in either case.

In any case, the independent assurance provider, in communicating significant issues to the entity's management and its governing bodies, may consider it appropriate to report on significant weaknesses in the internal control system identified in the course of the verification performed, though without expressing an opinion on the effectiveness of internal control in the verification report.

The overall maturity level of ICSR should increase at an accelerated rate in the coming years to align with more comprehensive reviews of internal control systems by external independent assurance providers, derived from reasonable assurance work.

5.7.b) ICSR Verification voluntarily requested by the organization's Board of Directors.

In this case, the assignment aims to provide assurance on ICSR to the organization's Board of Directors through an agreed-upon engagement conducting procedures to obtain limited or reasonable assurance.

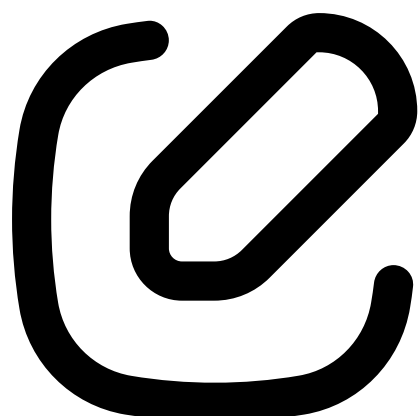
The independent assurance provider could be the same entity that verifies the Sustainability Report, or it could be an independent third party.

In this context, a report from an external independent assurance provider on ICSR can contribute in several ways to:

- Reinforce stakeholder confidence in the effectiveness of the entity's internal control system, including shareholders, investors, suppliers, customers, and regulators, in addition to the Board.
- Strengthen the internal evaluation conducted, increasing the credibility of the findings identified and recommendations made.
- Ensure the organization adheres to applicable regulations and that control procedures are established and operational.
- Ensure the completeness and accuracy of the documentation supporting the information reported.
- Provide an independent assessment of risks, helping the entity to identify and prioritize them. The report's findings and recommendations can serve as a basis for continuous improvement initiatives in the internal control system.



Appendix



Appendix: Glossary of terms and acronyms.

- **ACGR:** Annual Corporate Governance Report.
- **CNMV:** *Comisión Nacional de Mercado de Valores* or (Spanish) National Securities Market Commission.
- **CO₂:** Carbon dioxide.
- **COSO:** The Committee of Sponsoring Organizations of the Treadway Commission.
- **CSDDD:** Corporate Sustainability Due Diligence Directive.
- **CSRD:** Corporate Sustainability Reporting Directive.
- **Disclosure Requirement:** ESRS Disclosure Requirement.
- **DMA:** Double Materiality Assessment
- **EFRAG:** European Financial Reporting Advisory Group.
- **ELC:** Entity-Level Control.
- **ERM:** Enterprise Risk Management.
- **ESG:** Environmental, Social and Governance, or ESG for its acronym in English.
- **ESMA:** European Securities and Markets Authority.
- **ESRS:** European Sustainability Reporting Standards.
- **EU:** European Union.
- **GLESI:** Guidelines on the Enforcement of Sustainability Information.
- **Governing Body:** The group of people responsible for the leadership and management of an organization. This body has the authority to make strategic and operational decisions, and its structure may vary depending on the type and nature of the organization in question.
- **GRC:** Governance, Risk (Management), and Compliance.
- **GRI:** Global Reporting Initiative.
- **ICAC:** *Instituto de Contabilidad y Auditoría de Cuentas*, or (Spanish) Accounting and Auditing Institute).
- **ICFRS:** Internal Control over Financial Reporting System.
- **ICSRS:** Internal Control over Sustainability Reporting System⁶².
- **ICSR:** Internal Control over Sustainability Reporting.
- **IFRS:** International Financial Reporting Standards.
- **IROS:** Impacts, Risks and Opportunities.
- **ISAE:** International Standard on Assurance Engagements.
- **ISSB:** International Sustainability Standards Board.
- **IT:** Information Technology.
- **NFRD:** Non-Financial Reporting Directive.
- **NFRS:** Non-Financial Reporting Statement.

⁶² https://internet.cnmv.es/DocPortal/Publicaciones/Grupo/Control_interno_sciifenen.pdf

- **OCR:** Optical Character Recognition.
- **PCAOB:** Public Company Accounting Oversight Board.
- **PL:** In Spain: *proyecto o proposición de ley* (a Bill or proposal for a new law or for altering an existing law).
- **RD:** Royal Decree.
- **SASB:** Sustainability Accounting Standards Board.
- **SEC:** U.S. Securities and Exchange Commission. U.S. federal agency whose mission is to protect investors and maintain fair and efficient capital markets.
- **Senior Management:** The executives who report directly to the Board of Directors or to the chief executive of the company.
- **Specialized committees:** A formal internal group within the management body of an organization that deals with specific issues. The main specialized committees are the Audit, Nominations (and Appointments), and Compensation Committees. Depending on the type of organization, there may be other committees, such as Risk or Sustainability Committees, or they may be integrated into one of those mentioned above.
- **TCFD:** Task Force on Climate-related Financial Disclosures.
- **TRLSC:** *Texto Refundido de la Ley de Sociedades de Capital*. (Spanish Royal Legislative Decree Approving the Consolidated Text of the Corporate Enterprises Act).

