

Grant Thornton's framework for ESG risk management

Risk Advisory – Quantitative Risk Services

July 2025

Introduction

In January 2025, the European Banking Authority (EBA) released [final guidelines on managing environmental, social, and governance \(ESG\) risks](#).

- ❖ **Purpose:** These guidelines specify the minimum standards for financial institutions to identify, measure, and manage ESG risks over short-, medium-, and long-term horizons including a time horizon of at least 10 years.
- ❖ **Support for EU Goals:** The guidelines support the EU's goal of achieving net-zero emissions by 2050, as outlined in Regulation (EU) 2021/1119.
- ❖ **International Alignment:** The guidelines also align with third-country legal and regulatory requirements for internationally active institutions, in accordance with Article 87a(5)(b) of that Directive.

How should institutions assess and manage ESG risks?

Institutions should conduct regular assessments and use methods like exposure- and scenario-based approaches to identify and manage ESG risks, integrating them into their overall risk management framework.

How should ESG risks be embedded in institutional processes?

ESG risks should be integrated into processes such as risk appetite, internal controls, ICAAP, and monitored through effective reporting and ESG metrics.



How do environmental risks impact institutions, and what processes should be in place to manage them?

- ❖ Environmental risks, including transition and physical risks, can significantly impact the stability of institutions by affecting all traditional financial risks, such as credit, market, and operational risks.
- ❖ To ensure long-term resilience, the guidelines require institutions to implement robust internal processes and ESG risk management arrangements.

What should institutions do to address transition risks and how should the EBA guidelines be applied according to EU laws?

- ❖ Institutions should create plans to manage risks related to the transition to ESG regulations, ensuring alignment with EU requirements and relevant legislation.
- ❖ The EBA guidelines related to ESG risks must be followed by competent authorities and financial institutions, in accordance with specific EU rules, including Article 109 of Directive 2013/36/EU, Regulation (EU) No 1093/2010, and Regulation (EU) No 575/2013.



When will the EBA's ESG risk guidelines take effect?

The guidelines take effect on January 11, 2026, for all institutions except small and non-complex ones, which must comply by January 11, 2027.

Background

Why ESG risk guidelines matter: Legal mandate, Objectives, and Proportionate application

Institutions should systematically identify, assess, and manage ESG risks, driven by legal mandates, financial materiality, and climate goals, through a proportionate, scalable, and supervisory-aligned framework.

EU Legal Mandate

The [guidelines published by EBA](#) strengthen ESG risk management by integrating definitions, capital strategies, and governance into the CRR and CRD. They require institutions to establish ESG frameworks, conduct resilience testing, and comply with EBA standards for financial stability and sustainability.

Plans to monitor and address ESG risks

Implementation of structured ESG risk management **plans across short-, medium-, and long-term horizons**. These should be integrated into business strategies, stress testing, and scenario analysis, with supervisory oversight ensuring adequate risk controls.

Alignment with International Standards

The EBA guidelines on the management of ESG risks align with EU and international ESG standards, including BCBS principles, and reference EBA guidelines on loan origination, governance, and ESG disclosures. They are part of the EBA's mandate on sustainable finance and ESG risk management.

Impact of ESG risks

ESG risks, particularly climate-related risks, **impact financial stability, business models, and risk profiles**. Physical and transition risks affect asset values, creditworthiness, and capital adequacy, while social and governance risks **influence financial and reputational exposures**.

Proportionality

A proportionality approach needs to be applied as part of the assessment of the ESG risks **based on institution size, complexity, and risk exposure**. Smaller institutions may adopt simplified approaches, while larger institutions must implement advanced ESG risk management practices.

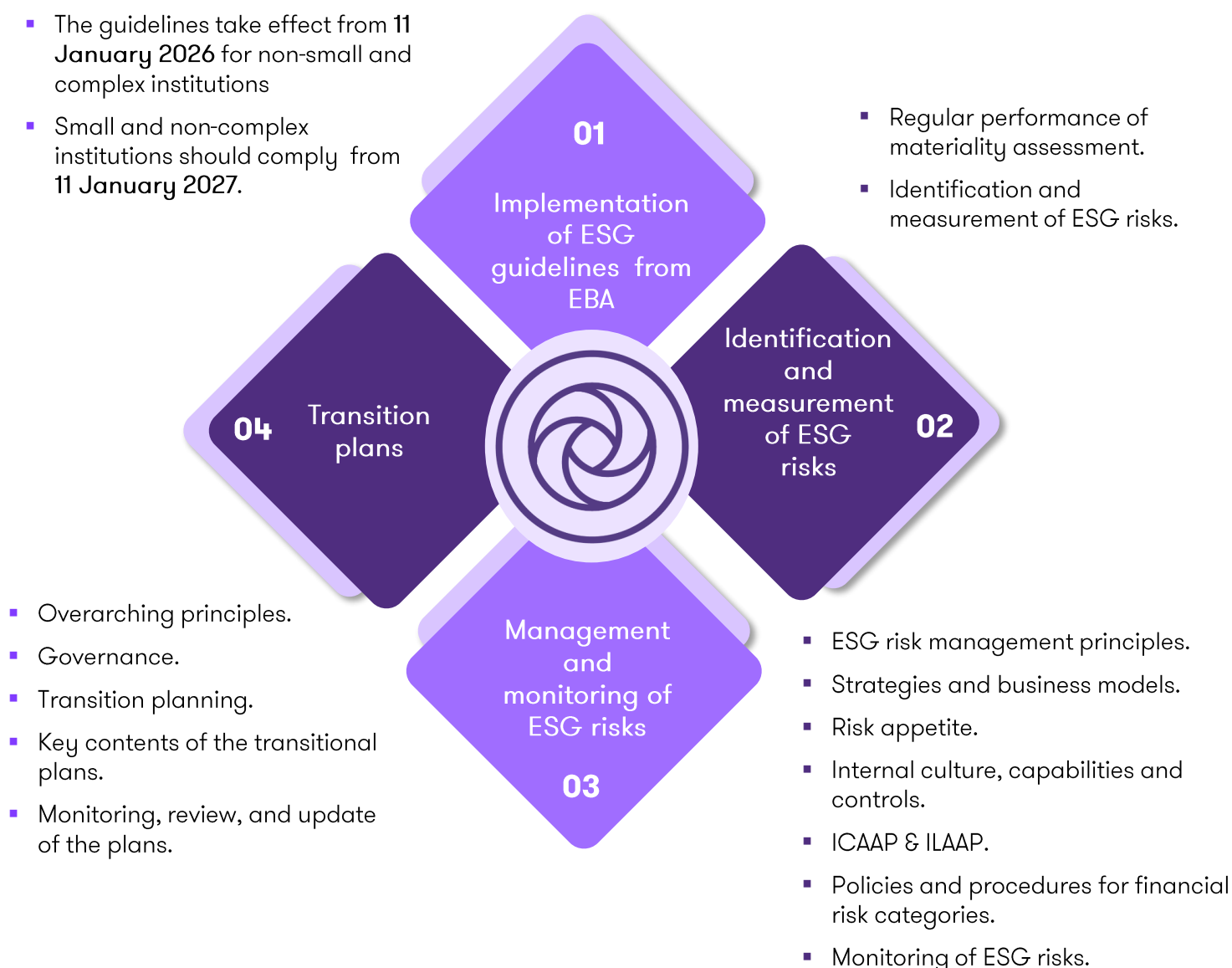
Environmental risks and ESG risks

Assessment of a broad range of ESG factors, including biodiversity loss and ecosystem degradation. Institutions must consider both how ESG risks affect their financial performance and how their activities impact environmental and social factors.

Areas of focus

Key areas of focus related to the management of ESG risks

The graphic below presents the key areas of focus related to identification, measurement, management, and monitoring of ESG risks based on EBA guidelines



Important note:

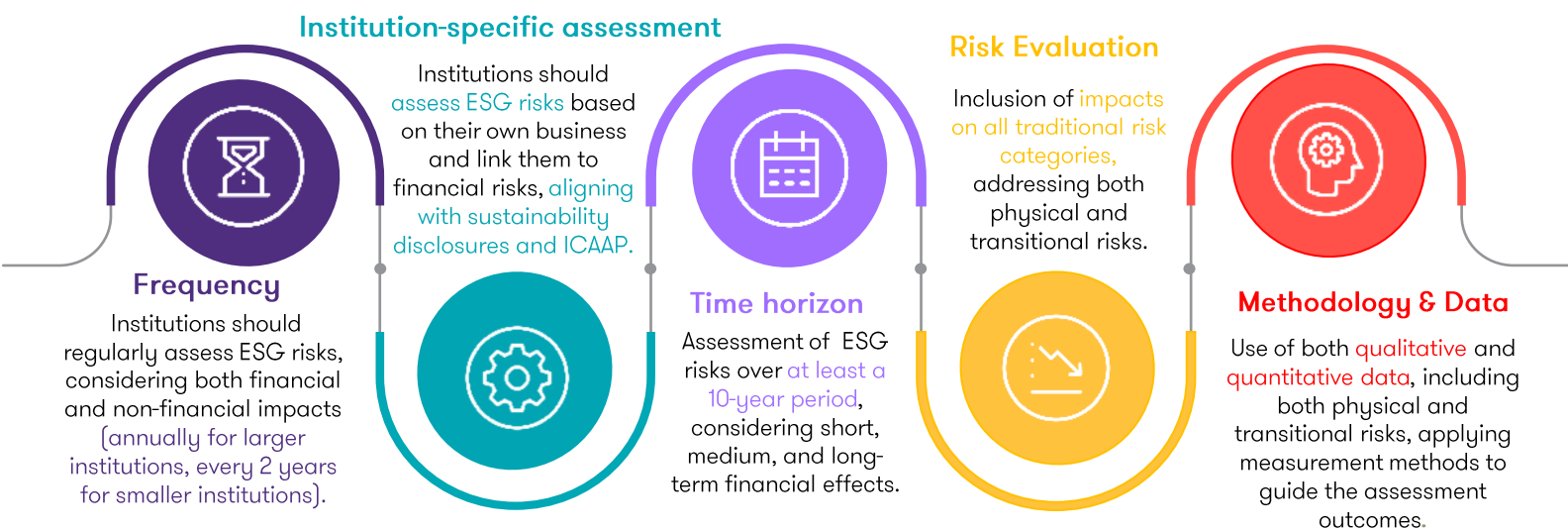
Issued under Article 16 of Regulation (EU) No 1093/2010, the EBA Guidelines on ESG risks set out the EBA's supervisory expectations, requiring competent authorities and financial institutions to make every effort to comply and to report their compliance status to the EBA by a specified deadline.

Identification and Measurement of ESG risks

This section outlines methodologies for integrating ESG risks into existing frameworks, ensuring alignment with regulatory expectations and industry standards. Through robust data governance and proportional risk assessment, institutions can enhance resilience and informed decision-making.

Materiality Assessment

Below are the key expectations for ESG materiality assessments as outlined by the European Banking Authority (EBA):



Identification and Measurement of ESG risks

General Principles

- **Assessment Tools:** Use of tools to assess ESG risks and their financial impact, with a forward-looking perspective.
- **Time Horizon:** Evaluation of the risks in the short, medium, and long term, focusing on more accurate data in the short-to-medium term.
- **Environmental Risks:** Quantification of the climate-related risks and environmental factors (e.g., biodiversity loss) and establishment of key risk indicators (KRIs).
- **Social & Governance Risks:** Initial qualitative evaluation, progressively adding quantitative measures.
- **Risk Interconnections:** Assessment of each ESG risk independently before considering interconnections.

Data Processes

- **Information management:** Implementation of robust systems for the identification, collection, structuring, and analysis of ESG data, integrated into data governance and IT infrastructure.
- **Granular Data Collection:** Assessment of client- and asset-level data to support ESG risk management and monitoring.
- **Use of Internal & External Data:** Use of internal and external ESG data; regular review of counterparty sustainability disclosures; alignment with European Sustainability Reporting Standards (Directive 2013/34/EU) and voluntary SME guidelines (COM(2023) 535 – SME relief package).
- **Supplementary Data:** Assessment and monitoring of ESG risks through supplementary data sources, including third-party data and data obtained through client engagement, with a clear understanding of data sources, methodologies, and limitations.
- **Addressing Data Gaps:** Identification of gaps, use of estimates or proxies when necessary, and progressive improvement of data quality.
- **Large Corporates:** Collection of ESG risk data, including location, emissions, energy use, and transition plans, alignment with international standards and impacts on workers and communities.
- **Non – Large Corporates:** Determination of relevant data points like for large corporates and use expert judgment or proxies to fill gaps.

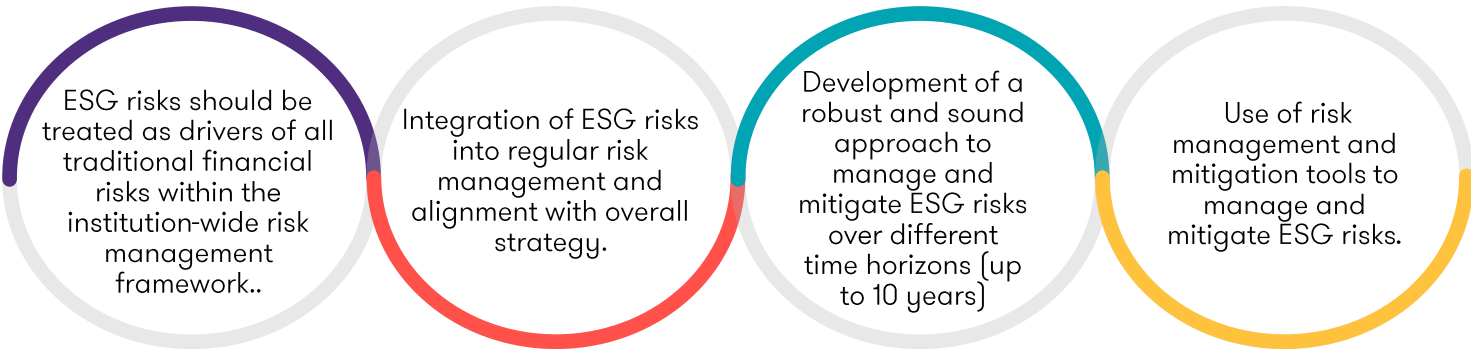
Scenario-Based Assessment Methods

- **Exposure-Based Methods:** Assessment of the counterparties' exposure to ESG factors, integrating them into risk classification and credit assessments. This includes evaluating physical and transition risks, regulatory impacts, business model vulnerabilities, and risk mitigation measures. Social and governance risks should also be considered through due diligence.
- **Sector-Based & Portfolio-Based Methods:** Application of heat maps and portfolio mapping to identify ESG risk concentrations and assess sector-specific vulnerabilities. Methodological choices, including scenario selection and exposure sampling, should be documented.
- **Scenario-Based Methods:** Conduct of scenario analyses to evaluate resilience to ESG risks, with a focus on climate-related risks. Portfolio alignment with climate targets and regulatory pathways should be assessed using science-based scenarios from recognised national and international sources. Large institutions should develop tools to measure the financial impact of nature degradation and sustainability goal alignment.

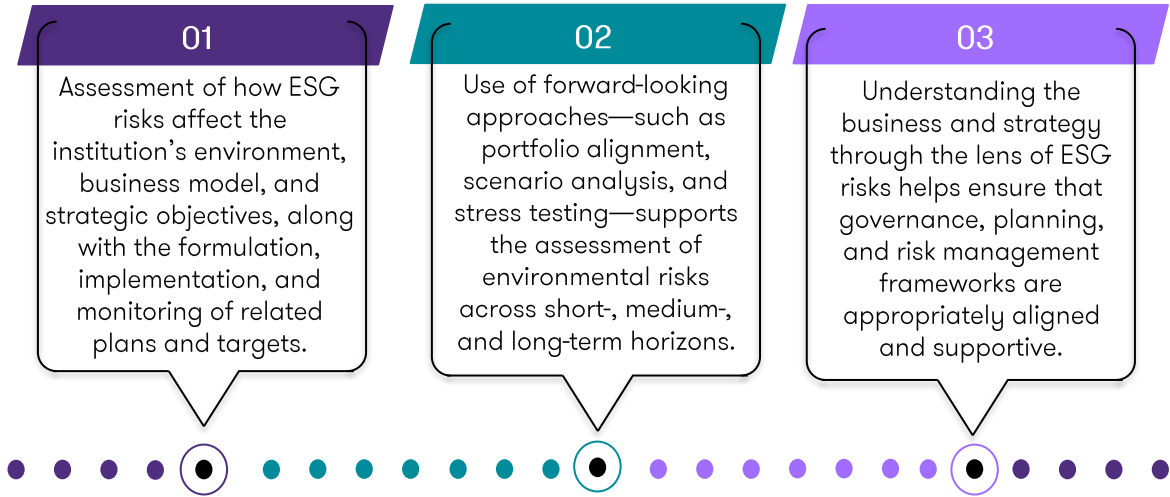
Management and monitoring of ESG risks

Institutions should integrate ESG risks into their risk management frameworks, strategies, and risk appetite, by embedding them across all risk categories, employing various mitigation tools, assessing long-term impacts, and ensuring consistent governance, monitoring, and alignment with strategic objectives over at least a 10-year horizon.

ESG risk management principles



Strategies and business models



C. Risk Appetite

- Definition of ESG risk limits within the risk appetite framework reflects alignment with the institution's materiality assessment, portfolio objectives, overall strategy, and ESG-related plans and targets.
- Use of ESG-related key risk indicators (KRIs), tailored to the institution's materiality assessment and business context, can support the risk appetite framework. This includes consideration of relevant metrics outlined in section 5.7 of the EBA guidelines (e.g., Share and amount of exposures and income from clients in sectors with high climate impact).
- Application of ESG risk appetite across all parts of the group ensures a consistent understanding and implementation of ESG risk limits at all levels, which is particularly important for larger institutions.
- Monitoring of ESG risk appetite and related key risk indicators (KRIs) should be supported by clear escalation processes, in line with the expectations set out in paragraph 80 of the EBA guidelines.

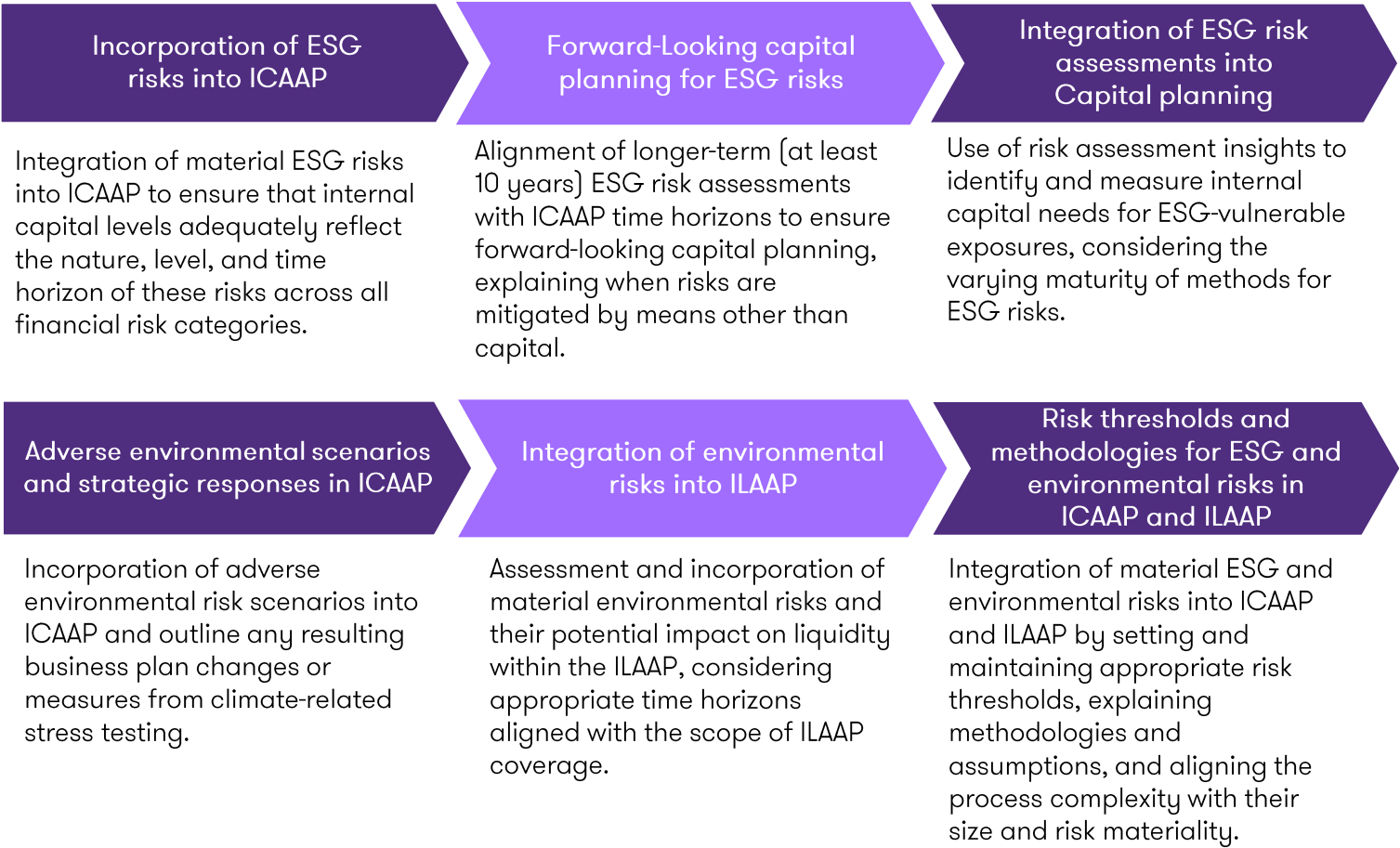
Management and monitoring of ESG risks

Institutions should continuously develop internal capabilities, governance, and control frameworks, including training, risk culture, and the three lines of defence, to effectively identify, assess, and manage ESG risks, and integrate these risks into their internal capital (ICAAP) and liquidity (ILAAP) adequacy assessments using forward-looking and proportionate methodologies.

Internal Culture, Capabilities, and Controls



ICAAP & ILAAP

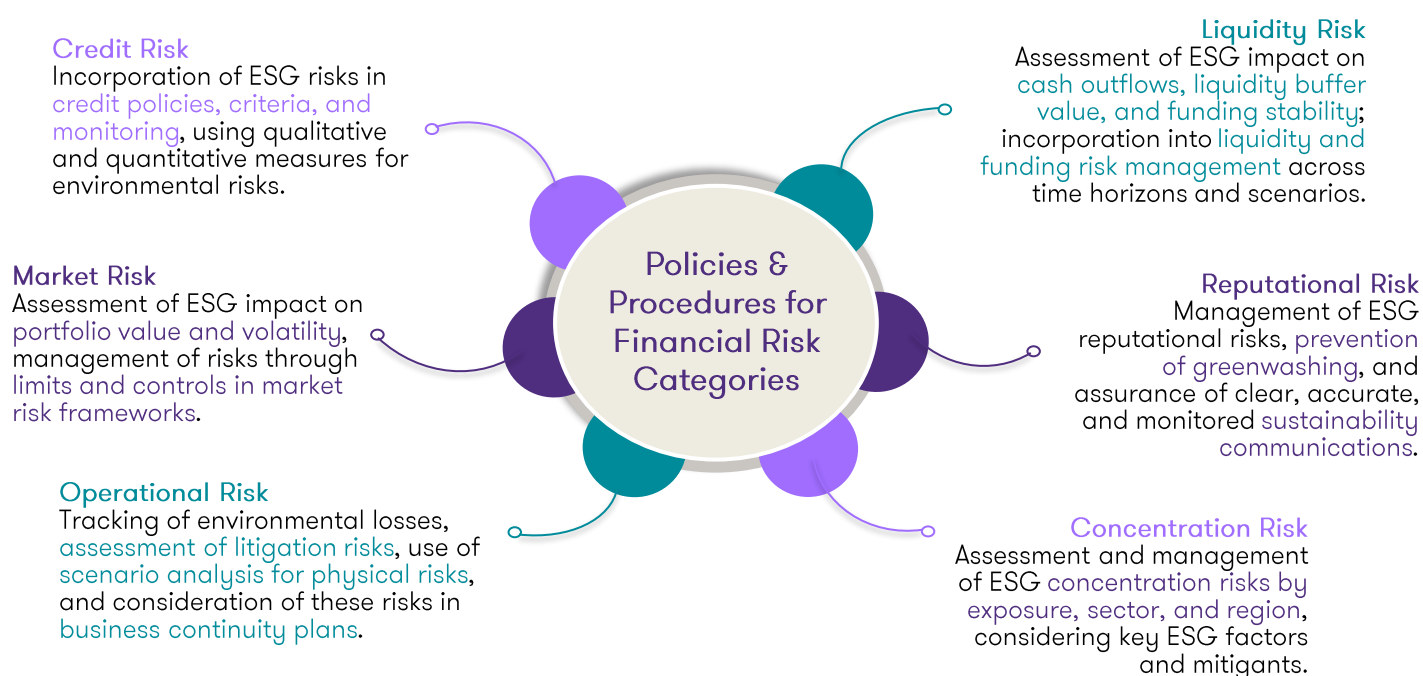


Management and monitoring of ESG risks

Institutions should integrate ESG risks into all relevant financial risk management policies and procedures by using both qualitative and quantitative methods, setting clear metrics, continuously monitoring exposures, and ensuring effective governance and reporting to manage the current and future impact of ESG risks across their operations.

Policies and procedures for financial risk categories

Institutions should manage ESG risks' impact on credit, market, liquidity, operational, and reputational risks using forward-looking analysis.



G. Monitoring

- ✓ **Reporting Frameworks:** Use of internal reporting systems and dashboards to inform management of ESG risks.
- ✓ **Monitoring & review:** Maintenance of continuous, granular ESG monitoring at both institutional and portfolio levels.
- ✓ **Early warning indicators:** Early warning indicators and escalation procedures for ESG risk breaches to be set.
- ✓ **ESG metrics:** Monitoring of a wide range backward- and forward looking ESG risk indicators, especially for the large institutions.
- ✓ **ESG indicators for SNIs and other non-large institutions:** Selection and expansion of ESG indicators based on materiality assessments.
- ✓ **Methodology documentation:** Establishment and documentation of clear methodologies for calculating ESG metrics and indicators.

Requirements for transition plans

This section outlines key principles and requirements for developing, governing, and implementing credible transition plans that integrate ESG risks into institutions' strategy, risk management, scenario analysis, and target setting to support a shift toward a sustainable economy.

01

OVERARCHING PRINCIPLES

ESG risk management, alignment with sustainability goals and EU regulations, integration with business and risk strategies, proportionality to size and risk, and inclusion of non-EU subsidiaries under local ESG laws.

02

GOVERNANCE

Role definition, management oversight, cross-functional engagement, capacity and expertise, gap remediation, data governance, and monitoring.

03

TRANSITION PLANNING

Assessment of ESG risks using science-based scenarios and materiality, with defined time horizons, aligned milestones, proportional forward-looking metrics, and tailored target-setting supported by consistent documentation.

04

MONITORING, REVIEW, AND UPDATE OF THE PLANS

Monitoring processes of plans, metric tracking, progress and impact assessment, management oversight, and periodic plan updates reflecting strategic shifts, revised risk assessments, scenario developments, and regulatory changes.

05

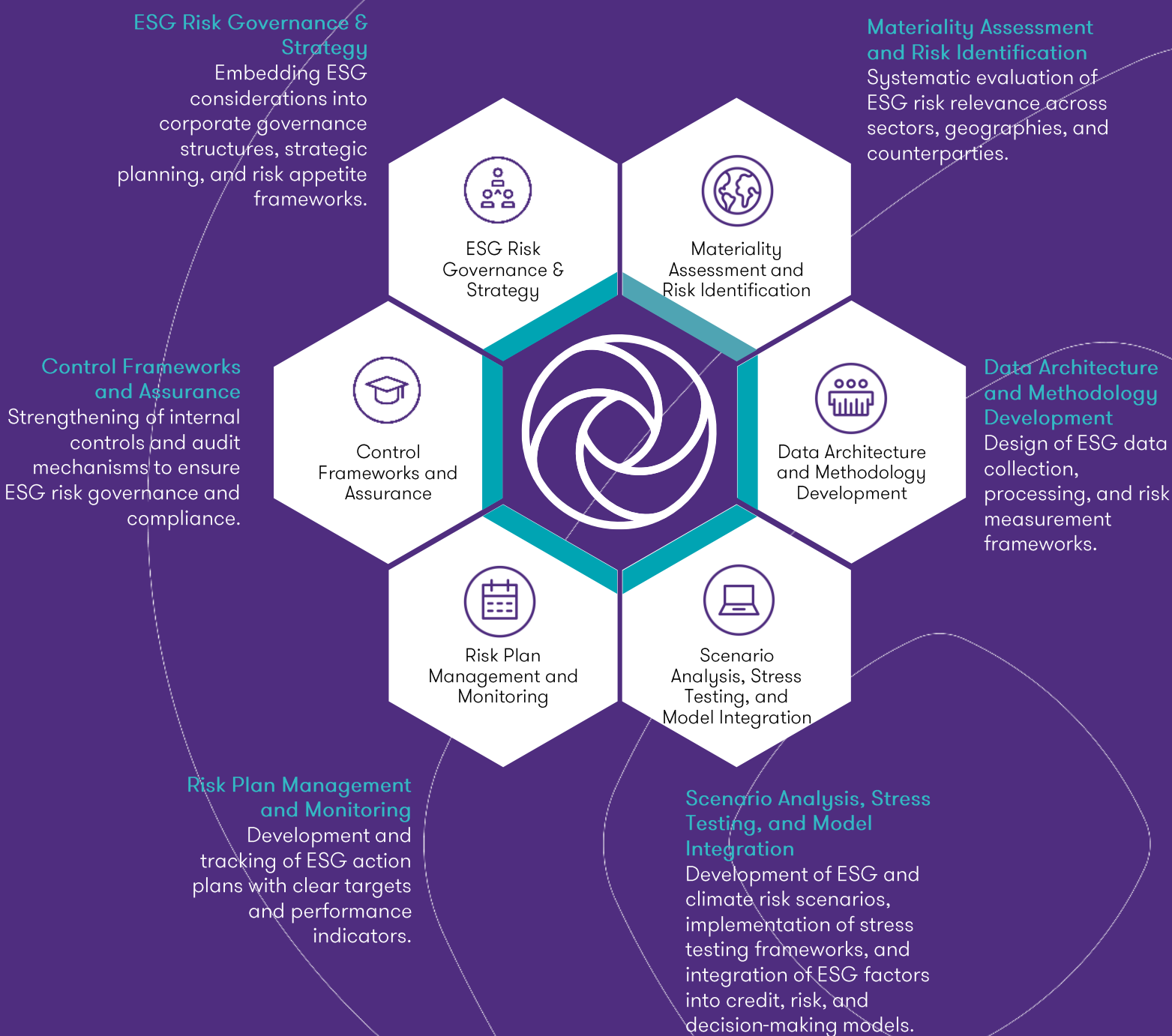
KEY CONTENTS OF THE PLANS

Documentation of ESG transition plans covering methodologies, targets, actions, and risk scope, covering at least environmental risks:

- Large institutions must include detailed strategic, governance, implementation, and engagement elements
- SNCIs and other non-large institutions may apply simplified requirements, and all are encouraged to use the Annex as guidance.

How can Grant Thornton support you?

We provide end-to-end ESG risk management advisory services, helping institutions align with supervisory expectations through governance integration, materiality assessment, data and methodology development, scenario analysis and stress testing, model integration, risk plan implementation, and internal control assurance.



Contact

Our team specialises in implementing effective ESG risk management practices aligned with supervisory expectations. From governance design and materiality assessment to data methodologies, scenario analysis, and control integration, our flexible services support the full ESG risk lifecycle. Let's enhance your ESG risk framework together. Contact us today for tailored support.

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