



Financial Reporting Council

# Assurance of Sustainability Reporting Market Study

Invitation to comment

March 2024

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# 1. Introduction

1. The market for the assurance of sustainability reporting by UK companies appears to be growing fast.<sup>1</sup> In 2022, 84% of FTSE 100 companies reporting sustainability information received assurance compared to 68% in 2020.<sup>2</sup>
2. Growing demand for sustainability assurance may have implications for the supply of statutory audit in the UK. Audit firms may provide sustainability assurance as well as statutory audit. In recent years, audit firms have reported facing capacity constraints. This is of interest to the FRC given our strategic objective to create a more resilient audit market through greater competition and choice. Audit firms are only one type of supplier of sustainability assurance; if they supplied less, this might enhance supply of audit.
3. Given some audit firms supply sustainability assurance, we conducted an initial review of this market in 2023, which showed potential for issues to emerge. Some stakeholders raised concerns about the extent of choice and diversity of supplier (audit and non-audit firms), and how this might change. We heard concerns about whether there is sufficient capacity to meet current, and future, demand for sustainability assurance. Queries have been raised about how changing regulatory requirements internationally could affect the market. Suppliers of sustainability assurance in the UK may need to pivot and respond to a developing regulatory framework.
4. We now want to explore these issues further through a market study. We want to ensure the UK's sustainability assurance market is working effectively, producing high quality assurance to support the production of useful, reliable reporting for investors, without creating undue burdens and costs on business. We want to understand if, and how, any developments in this market could affect the UK's statutory audit market. We want to ensure there is effective competition to help drive economic growth.
5. Market studies are a useful regulatory tool for exploring issues in a market. They can lead to a range of outcomes including richer insights about issues and proposals to improve how a market functions. In our draft plan and budget 2024/5<sup>3</sup>, we set out our intention to build our capability to deliver market studies under existing FRC powers. This will be the FRC's first market study.
6. We are keen to hear from any organisation or individual who may wish to respond to this invitation to comment on the UK's sustainability assurance market. The remainder of the document provides further information to help inform responses. Some specific consultation questions and details of how to respond are set out on page 6.

<sup>1</sup> A study on sustainability reporting and assurance across 21 jurisdictions found that the UK had the fastest rate of growth in sustainability assurance between 2019 and 2021, rising from 55% to 82%. Source: IFAC, State of Play in Sustainability Assurance: 2019-2021 Trends & Analysis, February 2023.

<sup>2</sup> Source: IFAC, State of Play in Sustainability Assurance: 2019-2022 Trends & Analysis, February 2024.

<sup>3</sup> Please see FRC draft plan and budget 2024/5 at <https://www.frc.org.uk/about-us/reports-plans-and-budgets/plan-and-budget/>

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## 2. Scope and approach to the market study

### Overview of sustainability information and assurance

1. Many UK companies disclose sustainability information<sup>4</sup>, often in their annual reports or dedicated annual sustainability reports. To provide additional confidence in the information being reported, these companies may choose to have that information 'assured'. Assurance is the service in which third parties review the underlying evidence and form a conclusion over their degree of confidence in the information being disclosed.
2. Sustainability is a broad term that can be interpreted widely, and sustainability assurance varies (both in the subject matter being assured and the level and nature of assurance being provided). In the UK listed companies, FCA regulated entities, and other specified companies are required to provide climate-related financial disclosures alongside other sustainability related disclosures.<sup>5</sup> Assurance of this information is not subject to any mandatory requirements in the UK.
3. Sustainability assurance for UK companies is currently supplied by a variety of audit and non-audit firms. Non-audit firms include engineering firms, sustainability consultancies and industry-specific inspection and certification bodies. In 2022, 42% of assurance obtained by FTSE 100 companies was provided by audit firms.<sup>6</sup>
4. Some suppliers of sustainability assurance choose to use internationally recognised standards, such as ISAE3000, AA1000 or ISO14064<sup>7</sup>, but other suppliers may not follow any recognised standards. Some suppliers may provide different levels of assurance. For example, a 'limited' or a 'reasonable' assurance engagement.
5. Recent regulatory developments internationally could impact the UK's sustainability assurance market. Some of the key developments include:
  - The International Auditing and Assurance Board has developed a new assurance standard specifically tailored for the assurance of sustainability information, ISSA5000. This may have an impact on the standards being used in the market.

<sup>4</sup> This includes: (i) any information about the opportunities, risks or impacts of economic, environmental, social, governance or other sustainability factors on an entity's activities; or (ii) the entity's own impact on the economy, the environment, or the public.

<sup>5</sup> Climate reporting in the UK is aligned to the Taskforce on Climate Related Financial Disclosures (TCFD) recommendations and operates on a comply or explain basis for listed and FCA regulated entities. For those companies reporting under The Companies Act regulations mandatory climate related financial disclosures are reported in the Non Financial and Sustainability Information Statement (NFSIS). Other mandatory sustainability reporting requirements include SECR (Streamlined Energy and Carbon Reporting) and reporting of the company's impact on the environment, as well as information on environmental matters, employees, social, community and human rights issues in Companies Act s414C and s414CB (NFSIS). There are also other pieces of sustainability reporting in mandatory areas such as Companies Act s172 disclosures.

<sup>6</sup> IFAC, State of Play in Sustainability Assurance: 2019-2022 Trends & Analysis, February 2024.

<sup>7</sup> The most prevalent of these is ISAE3000, which was found to be used in 68% of the sustainability assurance opinions published by the FTSE100 in 2022. Source: IFAC, State of Play in Sustainability Assurance: 2019-2022 Trends & Analysis, February 2024.

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- The European Commission passed the Corporate Sustainability Reporting Directive (CSRD) in January 2023. CSRD requires '*large undertakings*'<sup>8</sup> to publish specified sustainability information and obtain limited assurance over this information. Certain companies are subject to these requirements (from 1 January 2024), which will impact their corporate reporting from 2025 onwards. These requirements are likely to affect a number of UK-based companies and assurance providers.
  - The International Ethics Standards Board for Accountants (IESBA) is currently consulting on proposed frameworks for expected behaviours and ethical provisions for all sustainability assurance providers. These frameworks are currently subject to consultation and, once finalised, are likely to have an impact on the market.

## Proposed focus and themes for the market study

6. Drawing on our initial review in 2023, we will focus on how well the UK sustainability assurance market is functioning. We want to know if this market is delivering desirable outcomes including high quality assurance with minimal burdens and costs on business, and how the market could change. We expect to focus on three key themes.

### Choice and competition

7. We want to understand if UK companies have sufficient choice of sustainability assurance provider, what drives their choices, and if they have the information needed to make informed choices and receive high-quality assurance. We want to explore how their selection of provider affects competition, and how competition works in this market.

### Market capacity, opportunities and barriers to entry / expansion

8. We want to identify if there is sufficient capacity amongst suppliers to meet demand for sustainability assurance. Given the skilled staff required to deliver sustainability assurance we will explore whether there are any labour market issues. We are interested in whether firms see opportunities in this market and any barriers to entry and expansion they face.

### Regulatory framework

9. We want to understand how changing regulatory requirements internationally could affect the UK's sustainability assurance market. We will be interested in stakeholders' views on what, if any, developments they would like to see in the UK market.

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<sup>8</sup> '*Large undertakings*' are companies which meet or exceed at least two of the three criteria: (a) €50 million in net turnover, (b) €25 million in assets, and (c) 250 or more employees. Article 3(4), Directive 2013/34/EU.

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## How the FRC will carry out the market study

10. We want to engage closely with stakeholders throughout the market study. In addition to seeking written responses to this document, we intend to gather views and information through meetings and roundtables. We will also gather data about the market.
11. We will be flexible in our approach and timings to take account of our stakeholders and any relevant, wider developments. We will aim to provide further opportunities for comment, for example on our emerging findings and any proposals for action. We anticipate the market study will conclude by early 2025.

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## 3. Consultation process and next steps

1. We want to hear from any interested parties. We particularly welcome responses, supported with data and evidence where available, to the following questions.

### Consultation questions

Q1. How well is the UK sustainability assurance market currently functioning? To what extent does it help support economic growth or create burdens and costs on business?

Q2. What, if any, interplays exist between the UK sustainability assurance and UK audit markets?

### Choice and competition

Q3. To what extent do UK companies have sufficient choice of sustainability assurance provider? What factors, such as quality, influence their choice? How might this change?

Q4. How does competition work in the UK sustainability assurance market? How might this change?

### Market capacity, opportunities and barriers to entry / expansion

Q5. What, if any, capacity issues exist in the UK sustainability assurance market? How might these change?

Q6. What are the opportunities for firms in the UK sustainability assurance market? To what extent are there any barriers to entry/expansion?

### Regulatory framework and future developments

Q7. How might international regulatory developments affect the UK sustainability assurance market?

Q8. What, if anything, would you like to see change in the UK market? (For example, any regulatory /policy changes and/or any specific actions taken by FRC, Government, firms, companies or others).

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2. Please email your responses by 13 June 2024 to [competition@frc.org.uk](mailto:competition@frc.org.uk)
  3. All responses will be acknowledged. We expect to make responses publicly available on the [FRC website](#) unless respondents specifically request otherwise. If you send an email response which includes an automatically generated notice stating that the content is to be treated as confidential, you should make it clear in the body of your message whether you wish your comments to be treated as confidential. We will process personal data in accordance with UK data protection legislation.<sup>9</sup>

## **Financial Reporting Council, March 2024**

<sup>9</sup> Please see FRC privacy policy at <https://www.frc.org.uk/about-the-frc/procedures-and-policies/privacy-the-frc>



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