

# Financial Reporting Council consultation on Assurance of the Sustainability Reporting Market Study Acas response

13 June 2024

This is the Acas Executive response to the [Financial Reporting Council's \(FRC\) Assurance of Sustainability Reporting Market Study consultation](#).

## Introduction

Acas (the Advisory, Conciliation and Arbitration Service) welcomes the opportunity to respond to the Financial Reporting Council's consultation on their proposal for a market study on sustainability reporting assurance.

Acas is an independent and impartial non-departmental public body with a statutory duty to promote the improvement of industrial relations in Great Britain. In carrying out this duty, Acas offers conciliation in both individual and collective disputes; good practice advisory services for employers, and a website and national helpline which assists millions of employers and employees each year.

Our work gives us unique insight into what is and is not conducive to good industrial relations and, in turn, what has potential to impact productivity and therefore the opportunity for value creation. It also makes Acas the evidential authority on the risks generated by poor workplace relations. We have been undertaking a study due to be published in Autumn 2024 to better define the element of social sustainability. From our work we believe there is a lack of clarity and understanding amongst stakeholders and assessors of the full scope of social responsibility and the contributing factors. Our work aims to provide further clarity on material 'Social' factors to better inform those reporting, those assessing and those making decisions based on sustainability reporting.

## Summary

We welcome the Financial Reporting Council's focus on assurance of the sustainability reporting market. We acknowledge and support the need to explore through a study whether 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.

Our insight suggests that a focus on the quality and quantity of assessment provision and associated impact on financial auditing, will be valuable in the drive to improve the robustness and reliability of corporate sustainability reporting going forward.

As regulations and standards increase nationally and internationally, it is important that parallel assessment processes are developed and implemented so reliance can be made by a range of stakeholders on the reports generated.

This will enable investors, supply chains, customers, employees, and material stakeholders to make informed reviews and decisions on the information provided in the reports. This is valuable as material non-financial information has the potential to support financial return – to companies, investors and to the wider UK economy – and that this is currently undermined by a lack of understanding of all aspects of sustainable performance of companies, especially in terms of 'Social' factors.

Whilst expectations continue to increase in terms of companies' sustainability reporting, the marketplace for companies to select competent, credible, and cost-effective assessors in both environment and governance. Social sustainability has not developed at the

same pace.

Our main message for this market assurance work is an ask to take a specific look at the 'Social' aspects of sustainability as a fundamental element of sustainability reporting and assessment.

Acas has been working with a range of partners to strengthen the definition and scope of the 'Social' aspects of sustainability - often referred to as the 'Social' in Environmental, Social and Governance (ESG) in stakeholder interviews we have not been provided with feedback pertaining to strong capability in social sustainability assessment.

## Comments on the consultation questions

### Question 1

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?

- We believe the current assurance market is too narrow. The Morgan Stanley Institute for Sustainable Investment (2024) identified that both environmental and 'Social' themes feature as top investment areas for retail and institutional investors, with financing climate change and the transition still at the forefront. This broadening focus has not yet been fully reflected in the UK sustainability assurance market.

### Question 2

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

- No specific comment
- There may need to be some further maturing in the scope of 'what' needs to be assured and audited around sustainability reporting and performance before the interplay on 'how' this is done can be understood and mapped.

### Question 3

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?

- We see choice linked with visibility, availability, and competence of service delivery. As the 'Social' elements of sustainable reporting have yet to be clearly and consistently defined the assessment process will suffer in a similar way. Our thinking is to ensure the definition of social sustainability is clear and documented. Followed by assessors building further capability in 'Social' factor skills to facilitate the robust assessment of 'Social' aspects of sustainability reports.

### Question 4

How does competition work in the UK sustainability assurance market? How might this change? Market capacity, opportunities, and barriers to entry or expansion

- No specific comment

### Question 5

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

- We have no specific comment on capacity, others would be better placed to comment on this. However, capacity can be affected by lack of clarity and consistency of processes. This is already a confused and unclear space. Our request is to avoid overcomplicating with more frameworks unless they are essential, and they replace or simplify existing ones.
- Lack of understanding in social sustainability is a particular barrier to capacity.

Lack of definition and knowledge gaps are exacerbated by wider factors:

- Investors described to us that they are grappling with challenges around data, regulation, disclosure, and performance. This is particularly true of 'Social' factors. The quality of Environmental, Social and Governance data remains the biggest concern with consistency and reliability of data hampering adoption.
- The interconnected nature of sustainability challenges means agencies can lack capacity to define and declare. Income inequality, for instance, is connected to poor education, poverty and food insecurity with the latter increasingly linked to climate change and biodiversity loss.
- A significant percentage of investors we interviewed were also concerned that climate only transitions are leaving behind 'Social' issues. Investors appear to be indicating that they want a just transition whereby the benefits of a greener economy are distributed more equitably and in a way that respects worker rights.
- From a long-term perspective, a reduction in inequality, improvements in labour standards and improvements in supply chain standards are probably more important in terms of risk reduction.

## Question 6

What are the opportunities for firms in the UK sustainability assurance market? To what extent are there any barriers to entry or expansion? (Regulatory framework and future developments)

- Current focus is on assessing operations and materiality against the UK, EU and International Standards coming into effect over 2025 to 2026. It would make sense to align assurance against one or more of the most widely recognised emerging standards.

## Question 7

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

- The UK sustainability assurance market should not be considered in isolation. Many companies operate across Europe and internationally and need to be able to provide a report on their overall sustainability performance. Different systems across countries add further complexity and force companies to choose between systems.
- We recommend focusing on the incoming European and International standards and associated frameworks. Through our stakeholder engagement and interviews we have heard stakeholders push back at the idea of 'another framework' unless it replaces a number of others and is seen as 'the' framework. Otherwise, there is a risk of it becoming another tick-list instead of a real measure of quality of performance reporting. This should also include some defining of competency requirements for assessors.

## Question 8

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

- There would be benefit in requiring standard setters to include an element of standardisation of assessment scope and methodology. For this to happen there need to be agreed definitions.
- Also, to implement consistently there needs to be competency requirements for those undertaking the assessments so companies, investors and other stakeholders can take reliance and confidence from the assessed sustainability reports.

- A good output of the market study would include specific examples from the work showing what the market for social sustainability assurance looks like and what the current gaps are including but not limited to: systems, practical tools, and names required competencies and skill gaps analysis tools for companies and assessors. Including recommendations to close the gaps.

## Suggested questions

As part of the market study, we suggest inclusion of the following themed questions on social sustainability:

1. How well is the UK sustainability assurance market currently functioning with regards to social sustainability?
2. How are assurance firms stepping into this space or focusing on the 'Environmental'?
3. Do they have sufficient clarity about the scope of the 'Social', if not what's missing?
4. What, if any, capacity issues exist in the UK sustainability assurance market with regards to social sustainability?
5. Are they able to add sufficient quality and rigour to assurance in social sustainability? If not, what are the barriers?

In summary: A lack of focus on the materiality of 'Social' and 'Environmental' factors and the overall quality of sustainability reporting provides a risk to those interpreting them in their business decisions and reputation.

More consistent assessment by competent assessors of the 'Social' as well as 'Environmental' aspects of sustainability reports would more reliably inform investors as they determine the risks and strategies to take with companies which have either good or poor social and environmental sustainability performance.