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Developing an oversight regime for assurance of sustainability-related financial disclosures

Response from ICAS

DBT - Developing an oversight regime for assurance of sustainability-related financial disclosures

Comments on Consultation questions

Q1. Do you agree or disagree with the government's core proposal to create a voluntary registration regime for sustainability assurance? Provide justification.

We agree with the Government's conclusion following the Financial Reporting Council (FRC)'s market study which found that the sustainability assurance market would benefit from regulatory oversight.

We are supportive of ARGA, when established, being given the powers to register and oversee sustainability assurance providers in a way that is consistent with its intended powers over statutory auditors. This would mean that under this proposal, ARGA would have responsibility for:

- determining the qualifications and criteria that such assurance providers must meet to be registered; and
- regulating such providers, including appropriate and proportionate monitoring and oversight, thereof.

However, we question why are we waiting for ARGA to be established? In the interim period given the importance of this matter we believe that it should be taken forward by the FRC building on the work that has already been done to date by the ICAEW, supported by input from ICAS, in developing a register for sustainability assurance practitioners.

Scope of Recognition

We note: "The regime would recognise assurance providers as being capable of assuring information disclosed against UK SRS, European Sustainability Reporting Standards (ESRS) and any jurisdictional standards that are aligned to the International Sustainability Standards Board (ISSB) standards." (para 1.15)

We welcome that the proposed objective of the regime is intended to also cover assurance over disclosures prepared under ESRS as we are supportive of the concept of double materiality believing that this results in better decision-making information being available to stakeholders, including investors. This is a sustainability policy position that ICAS publicly advocates, see #1 here: [sustainability-policy-positions_post-jeb.pdf](#)

Given that ESRS is specifically highlighted we recommend that the regime should also specifically recognise assurance providers as being capable of assuring information against the Global Reporting Initiative (GRI) standards, the global standards on which the impact disclosures in ESRS are based. This proposed approach would also be in line with ISSA 5000. According to IFAC research, disclosures prepared under GRI standards most commonly have assurance provided against them.

We do, however, question whether the European Commission (EC) would necessarily recognise UK assurance providers who are generally performing engagements in relation to information that has been prepared solely from a financial materiality perspective, given that the EU has introduced a regime based on "double materiality". In that regard, we also query the appropriateness of the definition of the term "sustainability assurance provider" in the context of the proposed regulatory regime as it is being used to refer to the assurance of only sustainability-related financial disclosures and does not cover impacts or anything to do with sustainable development. We also flag an apparent contradiction whereby, paraphrased from para 1.5 bullet 3 of the consultation paper, "registration [as a sustainability assurance provider] would recognise an assurance provider as being capable of conducting high-quality assurance of disclosures against UK SRS, TCFD, ESRS and any other domestic standards that are based on ISSB disclosures" these being disclosures that apply both double and financial materiality. We recommend that sustainability assurance providers should be capable of providing assurance over sustainability disclosures as well as sustainability-related disclosures and this definition is clearly defined and consistently applied.

We are not convinced that operating the proposed registration regime on a voluntary basis is the best approach in the public interest as assurance providers will not necessarily opt in to the voluntary regime that is proposed. Therefore, given the importance of the subject matter we would prefer for the scheme to be mandatory, and this has to be the aim within a reasonable time period. This would provide greater confidence for stakeholders. However, we can understand the logic of the Government pursuing a voluntary registration regime for sustainability assurance at the outset given the immature stage of this developing market.

Ultimately, regardless of the approach adopted, the establishment of appropriate registration criteria, and adherence thereto, will be key to creating a register that has value for stakeholders. We believe that it should be a legal requirement for those providing services to UK companies where there is strong public and investor interest to be on the register.

We would also recommend referring to sustainability as well as sustainability-related disclosure frameworks to ensure that a wider range of engagements are scoped in to meet market demands.

Detailed elements of regime

We note: “ARGA would consult on detailed elements of the regime, once established. We also expect that the regime’s requirements will evolve over time as market practice develops, and in response to future developments in sustainability disclosure frameworks both in the UK or overseas.” (para 1.17)

We agree and welcome this proposed approach, subject to our comments on the delay in establishing ARGA requiring a solution in the interim period which we believe could be solved by FRC involvement.

Registration and oversight

We believe that for PIEs there is merit in registration and oversight being provided by ARGA. However, for entities which do not fall into this category then sustainability assurance, like financial statement audit, could be regulated by the respective professional bodies and others deemed of equivalence in terms of applicable performance, quality management and regulatory standards.

Given the large proportion of companies that have external assurance against GRI Standards (currently by far the largest instance of external assurance against sustainability and sustainability-related frameworks according to IFAC research) we recommend explicitly including GRI Standards. Not including GRI Standards could signal that assurance engagements by registered providers were of a lower quality. If the intention is to include all types of assurance engagements then assurance of impacts eng under GRI should be included.

As noted above, we also question whether the EC will deem sustainability assurance practitioners qualified under the proposed regime to be equivalent to those providing assurance under the CSRD in the EU.

We also believe that there would be merit in companies publishing audit and assurance policy statements. The introduction of an audit and assurance policy statement would help to create greater transparency as to where a board of directors obtains the necessary assurance on key areas of the business and its reporting, including on sustainability-related matters. This of course needs to be proportionate and therefore we would highlight our 2015 publication ‘Towards Transparency’ in this regard. Whilst the focus of this publication is on assurance on Key Performance Indicators (KPIs), the approach can be extended to other areas over which assurance is desired. This also highlights the importance of increased dialogue and engagement with users which will enable audit committees/boards to determine whether the source of assurance obtained meets user expectations.

Q2. In your view, what are the advantages and disadvantages of the opt-in approach?

The disadvantages include:

- It may allow providers (depending on the applicable criteria and checks applied), being individuals and entities, to promote their ability to provide assurance services without any checks on their credentials. Such an approach therefore increases the risk of such services being inappropriately provided and a risk to the quality of the assurance provided.

- Users will not be able to easily differentiate between the quality of those providers on the register and those who are not. Mandating registration would provide greater clarity and certainty.

The advantages include:

- Potentially lower costs for those providing such assurance services and hence lower cost for those procuring such services.
- Opt in by providers will be tantamount to a mark of quality of assurance opinion from that particular firm/individual.

Q3. Do you agree or disagree with the government taking a profession-agnostic approach to sustainability assurance? Provide justification.

We are supportive of this proposed approach to seek to ensure appropriate competition and choice. However, this needs to be supported by set criteria that all sustainability assurance practitioners should have to comply with, as we cannot have regulatory asymmetry that offers stricter requirements for certain sustainability assurance providers.

As a minimum these criteria should cover experience, expertise, performance standards, quality management standards and ethics/independence standards. We recommend that sustainability assurance providers should provide assurance over sustainability disclosures as well as sustainability-related disclosures and the definitions are clearly defined and consistently applied.

We also note that in the consultation paper it states: "A profession-agnostic approach to sustainability assurance has been promoted internationally, including by the International Organization of Securities Commissions (IOSCO). This approach recognises that a broad range of skills will likely be needed to perform effective assurance of sustainability-related financial disclosures and aims to provide opportunity for the emergence of new sustainability assurance providers, including but not limited to statutory auditors." (para 1.15)

Whilst this is true, in the EU various member states have elected that sustainability assurance provided under the requirements of the Corporate Sustainability Reporting Directive should be restricted to financial statement auditors. This is because of their expertise in undertaking assurance engagements and proven track record in doing so. They can engage experts as necessary to assist them in performing sustainability assurance engagements.

We would also highlight that adoption of a profession agnostic approach would appear at odds with the scope of the sustainability oversight regime covering assurance over any reporting under S1, S2, TCFD and CSRD that could potentially have a "material financial impact". If solely related to material financial disclosures then this should not be called "sustainability assurance". Therefore, we believe there is a need to clarify the scope of what is being proposed - is it just assurance engagements over "material financial disclosures" or a fuller range of sustainability assurance engagements eg specific engagements about GHG emissions etc, external reviews/second party opinions/verifications that are part of the International Capital Market Association's green/social/sustainability/sustainability-linked bond principles etc. We believe there is a need for the scope of the engagements to be covered to be much wider i.e. to be reporting framework neutral which the ISSA 5000 standard is designed to deal with. This would ensure that engagements under TCFD, GRI etc are covered.

Q4. Do you agree or disagree that both individuals and firms should be able to be registered as sustainability assurance providers? Provide justification and explain whether any specific requirements are needed to ensure appropriate accountability.

We agree with this proposal. The firm or individual who will be signing off the assurance report should be accountable. Many financial statement audits currently require the use of various experts as part of the engagement. Therefore, this dynamic is not new and will continue to exist on sustainability assurance engagements.

We are aware of other jurisdictions that have not solved this issue which has resulted in significant confusion in the market (eg signatory is "a" registered auditor or "the" company's auditor) therefore this should be resolved as soon as possible.

Q5. In broad terms, what are the main principles that ARGA should consider when developing a registration regime for sustainability assurance providers?

These should include:

- Competence
- Fairness
- Transparency
- Experience
- Proportionality
- Accountability
- Promotion of quality.
- Scope.

Q6. How should ARGA work with other organisations when developing a future registration regime?

ARGA should work with organisations, including professional accountancy bodies which have members who are experts in providing assurance, including on sustainability-related information. Such bodies also have experience in establishing similar, efficient and effective registers of firms and individuals.

Q7. Do you agree or disagree that the UK's registration regime should recognise 'sustainability assurance providers' as being capable of providing high-quality assurance over multiple reporting standards (that is, TCFD, UK SRS, ESRS)? Provide justification.

We agree and recommend that sustainability assurance providers should provide assurance over sustainability disclosures as well as sustainability-related disclosures and that definitions are clearly defined and consistently applied.

However, given the diversity of these reporting standards there may be a need to have some form of categorisation. Of course, this could be left to the relevant individuals and firms undertaking such engagements to ensure that they are professionally competent to undertake the assurance engagement in question. For this to work, all such individuals/firms would need to be subject to high-quality ethical requirements that would include appropriate provisions on professional competence.

Q8. Do you agree or disagree that sustainability assurance providers must follow UK-equivalent standards to ISSA 5000? Provide justification and, if you disagree, indicate whether any other standards are considered appropriate.

We agree with this proposal. ISSA 5000 is a high-quality assurance standard that is framework agnostic and we would expect the FRC to adopt this standard for use in the UK following its current consultation. We note however (see above) the proposal scope is much narrower as it relates to only financially-material reporting and we believe this needs to be widened.

Q9. How should ARGA exercise its proposed functions in respect of sustainability assurance standard setting in the future?

We would envisage that this would follow a similar approach to that currently adopted by the FRC for setting auditing standards in the UK. This entails the international standards on auditing produced by the International Auditing and Assurance Standards Board (IAASB), being subject to appropriate due process, including consultation, forming the basis of UK auditing standards, subject to any UK specific requirements that are deemed necessary.

Q10. What factors should ARGA consider when developing its approach to enforcement. Provide justification.

This needs to be well defined, fair, transparent, feature appropriate checks and balances and be proportionate. ARGA/FRC will very much need to play the role of an improvement regulator and

recognise the mindset shift broadly required to accept restatements where they result in disclosure of better information.

Q11. Do you agree or disagree that assurance of UK SRS disclosures is desirable in the long term? Explain your view and also indicate whether there are any implementation approaches (for example, timelines for phasing-in requirements) or alternative measures to regulation that the government should consider.

As sustainability assurance is a developing area, we believe that for the moment it should continue to operate on a voluntary basis. The long-term goal, however, has to be mandated assurance for all in scope entities but this will need to be achieved over time and in separate phases.

We would favour starting this process, at a future date to be determined, with a mandate for assurance of certain categories of companies' disclosures against UK SRS. Such an approach would allow companies to focus on improving the quality of their data, processes and controls in the early years of reporting under UK SRS. This process could draw upon existing definitions like public interest entity (PIE) or a subset thereof, or lever upcoming terms like economically significant entities (ESE), as long as they can be well defined, and consistently applied. However, we would question the focus on a future regulatory regime that is limited to those "economically significant entities" where there is likely to be strong public and investor interest. We are not convinced that this is necessarily the relevant scope for such a regime although it could be used as a starting point. There needs to be some account taken of the impact of entities and their externalities, regardless of their economic significance.

In the absence of a clear definition of ESEs we would suggest that consideration should be given towards mandating assurance of UK SRS disclosures for certain public interest entities in the medium term, and as the market matures increasing the scope of companies subject to assurance in line with those subject to mandatory sustainability reporting.

Such assurance provides confidence to stakeholders, including investors, in the veracity of the information reported and will also help put sustainability disclosures on an equal footing to financial statement disclosures, which is desirable. We would envisage that as has been the case in the EU, such assurance would be limited in nature, at least in the early years.

Q12. Provide evidence where assurance providers have been excluded from or where you anticipate future barriers to competing for CSRD assurance engagements, due to a lack of UK registration regime or other reasons. Where possible, include quantitative estimates of the scale of impact on UK companies.

We are aware that UK firms have not generally been in a position to provide assurance engagements under the CSRD. We are not in a position to provide any supporting evidence.

Q13. Provide evidence where the non-audit services cap has been a barrier to accessing or providing high-quality sustainability assurance. Where possible, include quantitative estimates of the scale of impact.

We are not in a position to provide direct evidence. We do, however, believe that there is a risk that the cap may act as a barrier to certain companies being able to use their financial statement auditor to undertake a sustainability assurance engagement and we are aware that many businesses would prefer to be able to do so. It is hard to assess the impact of the cap in relation to the fees associated with sustainability assurance services provided to date, as the scope of such engagements might well be less than those that will be required to assure information in accordance with IFRS (UK) S1 and S2 and other reporting frameworks.



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