

Business, Energy and Industrial Strategy Committee

Oral evidence: Environmental, social and corporate governance: reporting and investment, HC 703

Tuesday 11 October 2022

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Members present: Darren Jones (Chair); Andy McDonald; Charlotte Nichols; Mark Pawsey.

Questions 44 - 76

Witnesses

II: Richard Spencer, Director of Sustainability, Institute for Chartered Accountants of England and Wales; Kate O'Neill, Director of Stakeholder Engagement and Corporate Affairs, Financial Reporting Council; Ingrid Holmes, Executive Director, GFI, and Chair, Green Technical Advisory Group.

Examination of witnesses

Witnesses: Richard Spencer, Kate O'Neill and Ingrid Holmes.

Q44 **Chair:** Welcome to Richard Spencer, who is the director of sustainability at the Institute of Chartered Accountants for England and Wales, Kate O'Neill, who is the director for stakeholder engagement and corporate affairs at the regulatory body the Financial Reporting Council, and Ingrid Holmes, who is the executive director of the Green Finance Institute and chair of the Green Technical Advisory Group. Good morning to all of you. Thank you for joining us this morning.

I just want to kick off with the last question, which hopefully you all heard. I think I got an answer to my question, but in my head in this whole ESG debate there is a problem somewhere that I am trying to understand properly. I wonder whether you might agree or disagree with the previous answer that we had from Emma Wall from Hargreaves Lansdown. Kate O'Neill, do you want to come in first on that?

Kate O'Neill: As a regulator in this space, though not the only regulator in this space, I listened to her answer with great interest. We set standards and expectations not just about the reporting but the stewardship code, which the FRC sets, as well as the UK corporate governance code.

If you want to become a signatory to the stewardship code—we are delighted that fund managers all over the world see that as a high bar, and rightly so—you have to prove you are doing the things you say. Whether you call it woke-washing, greenwashing or whatever the phrase, it has been incredibly helpful at raising the bar for fund managers to prove that engagement. You cannot just put out a glossy brochure saying, "Invest it in our funds. We are ESG. Aren't we wonderful?" It forces you to prove what engagement you undertake. It will not solve all of the problems, but it has certainly gone a long way to saying to fund managers, "You cannot say certain things about how you do things unless you can prove in your applications that you are actually doing it".

Becoming a signatory of the stewardship code is not "one and done". You have to reapply every year, which we think is a very healthy way to keep it current and to reflect the fact that fund managers cannot fall back to default positions. We believe the stewardship code can be part of this.

When it comes to the UK corporate governance code, which is a principles-based code, i.e. comply or explain, we are very clear with the corporates and preparers that we engage with that it is okay not to be perfect on everything. You might say, "We are not looking at that issue from an ESG perspective because it is not part of our business operations or part of our strategy". That is fine. You might say, "It is taking us five years instead of three years, as we thought it would, to become carbon neutral". That is fine. It is about having healthy discussions about the art



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of the possible while setting out what we would say are well articulated standards and expectations.

It also goes back to consumers, though. You have to be very open and honest about what you want from the companies you engage with, you are employed by and you supply through to who you are investing in. Hargreaves Lansdown has an important role, given the number of retail investors they look after on their platform.

Q45 Chair: Dr Raghunandan said that there are all these policies and people may write about how they comply with the policies, but no one really checks or enforces them. What is your answer to that?

Kate O'Neill: As a regulator, we would disagree a bit with that. I would agree that there are a lot of standards and a lot of different approaches globally on this, which is why the FRC is very much behind the creation of the International Sustainability Standards Board, which we think will not totally codify but give a really good starting point for international standards.

I am not criticising this—it is just what has happened—but the more consistency we have across this important reporting spectrum, the more we will be able to see consistency. This also goes to the point about data. There are a lot of data providers and a lot of taxonomies, which makes it a confusing landscape. We have just put out quite a lot of guidance helping preparers and investors understand what the data is, what it means and what is meaningful reporting. Our mantra is, “Report once; use often”. We would like to see people not thinking that better reporting or regulation means having more.

Q46 Chair: Richard Spencer, the answer we got before was that there is not some big conspiracy theory or political debate worrying investment firms and banks; it is that they have not really formalised their internal processes, reporting and assurances in such a way that they feel confident speaking about. Is that your experience?

Richard Spencer: Yes, that is true. There is no conspiracy. What you have is businesses that are starting on a journey. When any of us start on a journey, we are reluctant to say where we are. The narrative has very much been in the past one of saints and sinners. If you are not perfect, you are beyond redemption. That stops businesses being open and honest about where they are.

We are also asking businesses to make a massive change. I do not know whether in the previous discussion you drew the distinction between ESG and sustainability, but ESG is very much about the risks that planet and people pose to the enterprise value of an organisation. It is risk-based. Sustainability is much more about the impact you are having on the planet.

I recognise there is a spectrum of impact, but that is a massive thing to now ask businesses to do. I would imagine that a lot of organisations



have looked at their processes. One of the benefits of this is in looking at your processes and seeing what is there. The enormity of what is being asked of them is probably quite frightening. They are on that journey and they are coming to terms with that.

There are also the data issues and the public scepticism. There is also a knowledge gap. We have seen sustainability and ESG mushroom as issues in the last two or three years, and now suddenly everybody needs to be an expert. If you think about the number of experts needed and the number of people available, it just does not add up, does it? All of those factors are in the mix here. That is driving what you are seeing as a problem.

Q47 Chair: It is an interesting point, is it not? If you are the CEO of an SME, you are running your business, dealing with inflationary pressures, wanting to pay your staff well, trying to get customers to buy things and then you have all this other stuff to deal with. If you decide that it is good for your staff and your customers to be an ESG champion, you will think, "Where am I going to go to get help with the data collection, the assurance and the reporting?"

For the modern slavery example, everyone went to their lawyers and saw it as a compliance issue. The lawyer would write a little statement up based on some feedback from procurement. They would put it on the website, and the box would be ticked. It actually does not really work very well in practice. For this type of work, do people just go to their local accountant? Does their local accountant say, "We know what we need to do" or do they say, "I just do the numbers; I do not know how to do the ESG stuff"?

Richard Spencer: We are certainly, along with most of our sibling professional bodies in the accountancy world, driving our members down the education route so they can do exactly that. Particularly during Covid, we saw that in practice our members were almost economic first responders, in the sense of helping businesses through their troubles.

We learned a lesson there, which is that our members could help guide those smaller and medium-sized businesses through this. We are engaging in a lot of education and help there. At the moment, I would not say that your practitioner on the Clapham omnibus is going to say, "Yes, I can help you through that", but that is certainly where we need to go.

For SMEs, particularly small businesses, a lot of that is not necessarily going to come through reporting; it is going to come through supply-chain requirements. If you are a very large business that has made a net zero commitment, for example, and you are doing that under science-based targets, you will have to report on your scope 3 emissions—in other words, those in your value chain.

Those SMEs are going to get all sorts of requests for that information. One of the things we hear very much from our members who are either



advising or who are small and medium-sized businesses is the need for standardised requirements. They do not want to get seven different requests for the same information in seven different shapes. Standardisation is not just about public disclosures; the standardisation needs to be there in the supply chain. That is really where the majority of the economy is going to find the prudential regulations: through the Bank of England, the FCA or through other reporting requirements imposed on businesses. The majority of the economy will get those through the supply chain.

Kate O'Neill: If I could just add to that, SMEs, like large companies, have to set out their stall. Do not report on stuff that is not relevant to the operations of your business. Do not feel that FOMO: "The person down the road did 10 pages; I had better do 50 pages". It is about proportionality; it is about materiality; it is about talking about what is relevant to what you have said to the world you do. You also have to consider whether you are part of someone else's supply chain. If you are bidding for some Government contracts, you may have to talk about some things that you did not talk about five years ago.

Certainly, it is about being confident about what you do, what your strategy is and also what your timing is. It may not be that you are net zero-compliant tomorrow and it will take longer. Say that. The clearer you are and the more transparent you are about the journey, to use Richard's phrase, the more you will be heard and the more people will be fine with that.

Q48 Chair: Ingrid Holmes, from a green finance perspective, you must be delighted with all this money being redirected into ESG investments.

Ingrid Holmes: That is true. The biggest benefit to this is that we are starting to see the mainstreaming of the understanding that some of these environmental and social factors that people thought were non-financial can become financial. That is the point.

That is why we are seeing a slowness in the uptake to your invitation to the market. It is about hiring people in; it is about changing systems; it is about getting heads around new data sets. It is also really important to remember that the disclosures are just a means to an end.

On your SME example, I would be a bit disappointed if your first port of call was your accountant. What you are looking at are operational changes within the business. That is where you go first, and then you can think secondly about how you report that information to the market.

Q49 Chair: Where do you go for operational changes if you do not have a COO or somebody else?

Ingrid Holmes: If it is on a social issue, you might consult a social enterprise on how you get your diversity numbers up. If it is an environmental issue, there are lots of consultants out there who can help you with your engineering questions and your supply chain questions.



That is the change that these disclosure regimes are seeking to drive. The disclosure is just a means to an end.

Kate O'Neill: Yes, absolutely.

Q50 **Mark Pawsey:** Kate O'Neill, you referred to taxonomy. Tell us a bit more about that. What is a green taxonomy?

Kate O'Neill: I will leave my friend to talk about green taxonomies. Taxonomies are really just the way in which you are collecting, codifying and consolidating data. One of the challenges I heard in the last part of the session is this whole idea of where you get the data to talk about what you are doing and how it is aggregated.

If you look at fund managers, quite often they might say their benchmark is the FTSE green index; other people might use the MSCI for good; other people might use Bloomberg. There are all of these data providers that have to sell their product. I have to say that the proliferation of them means that the taxonomies are difficult to compare and contrast. It is difficult to say, "Is that one better? Does that one tell me more? Is that going to bring about the outcomes that we expect?"

We are part of the discussion across the regulatory spectrum. We believe there needs to be consolidation and clearer taxonomies to help preparers use forms of data that are going to be recognised by users across the spectrum and not create more confusion. I will leave the green one to you.

Q51 **Mark Pawsey:** You are really talking about standardisation in the same way we heard from our witnesses in the previous session.

Kate O'Neill: Yes, this is about standardisation, but your point was excellent. It is not just about disclosure fixing the problem; it is about the data that goes into those taxonomies. For some firms, finding the data is challenging as their—I will overuse the word—journey continues.

Q52 **Mark Pawsey:** Ingrid, where does the data for a green taxonomy come from? How can we make sure it is consistent?

Ingrid Holmes: It is a new data set. We need to differentiate here between taxonomy with a small T, which is the sets of information and the more generic ESG reporting landscape, and the green taxonomy that we are looking to introduce in the UK.

It is a completely different way of reporting. I will just give you a quick sense-check, but it is basically a set of definitions of environmentally sustainable economic activities made up of two bits. One is making a significant positive contribution to the six criteria that the taxonomy covers, such as climate change mitigation and adaptation and, in due course, biodiversity, pollution prevention and control and so on.

You also have to do no harm to those other elements, which is a key facet of sustainability. As an example, a wind farm would make a positive



contribution to climate change mitigation. If you put it in a site of special scientific interest, it is harming biodiversity. That would not be taxonomy-aligned. The other important thing about the green taxonomy is how it is reported. It is reported as financial metrics. You need to report your capital expenditure, your investment or your revenues from sales of goods and services that are taxonomy-aligned.

It is really objective and it is focused on directing capital to where we need it most. Because it is objective, it helps us deal with this greenwashing issue. It is very different to the kinds of climate data you get from ESG reporting, which will be things like greenhouse gas emissions, water resource use and whether there is board leadership on climate management. It is a new addition to the space.

There are going to need to be some areas for improvement. One of the things we have spotted in our work as GTAG is that the “do no significant harm” criteria mainly rely on you complying with the law, which you would hope companies do anyway.

Q53 Mark Pawsey: When you say “areas for improvement”, do you mean improvement by companies or improvement in reporting?

Ingrid Holmes: This is an emergent instrument in the UK. It is live in the EU currently. We have the benefit of being a fast follower. Something like 2,000 UK companies already have to report against the EU taxonomy. What we are finding around this “do no significant harm” piece is you just cannot report. To give you an example, one of the requirements is when you are investing in adaptation measures that you do not harm others’ ability to adapt. You cannot prove a negative. There are some areas that we in the UK can improve on as part of our contribution to international taxonomy development.

On this point about standardisation—it is really important; it is the theme of the entire discussion today—there are going to be core elements of taxonomies across the globe on which there will be agreement, on which they will all say, “Yes, that is environmentally sustainable”. That will be electric vehicles, wind farms and so on. You are always going to see variations in different jurisdictions because there will be different views on transition—

Q54 Mark Pawsey: Are there circumstances in which adopting green taxonomy principles would prevent an investment from taking place? Could you give us an example of where that might occur?

Ingrid Holmes: Again, it is back to the nature of disclosures. This is just a transparency instrument. It is one of a smorgasbord of tools that are being developed in the UK and internationally to support—

Q55 Mark Pawsey: If people were using these tools and identifying that the outcome would be less desirable than it might otherwise be, might that then cause an investment not to take place when it would otherwise take place?



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Ingrid Holmes: Again, it is back to the point about this being a transparency tool. This is not a rule about what you can or cannot invest in. It is an indicator for people who are interested in looking at—

Q56 **Mark Pawsey:** If it is providing an outcome, that will be something that decision-makers will refer to, will it not?

Ingrid Holmes: If you are running a fund that only wants to invest in taxonomy-aligned businesses, that will exclude some businesses that do not fit within the spectrum of what is deemed green.

Q57 **Mark Pawsey:** Richard, I wondered whether I might come back to you. I am interested in where this journey towards greater ESG reporting is going to take us. You did speak about the supply chain. A prime manufacturer might be looking for data down the supply chain down to what will often be SMEs, which might have some challenges in providing this information. What are the downsides? Is that one of the downsides to this move?

Richard Spencer: I would not describe it as a downside because it is all part of—

Q58 **Mark Pawsey:** Is it not a distraction for a small business that really just wants to get on with providing whatever it provides upwards to the prime?

Richard Spencer: You could say that, but that would be a bit like saying we should not report on modern slavery because it is a bit of a distraction and it would push your wage bill up. These are outcomes that the public and society want. It would be much more onerous to require SMEs to make public reports. It would be much more helpful for SMEs if the information those businesses are collecting was standardised, like a reading from a smart meter, for instance. That should also help improve their business.

Q59 **Mark Pawsey:** You are not concerned that there may be small SMEs that are really bothered about the amount of time and effort they are going to have to put in to gathering information to pass up to the prime manufacturer, which will act as a distraction to the core activity within their business.

Richard Spencer: There is always a chance. It is about being proportionate.

Q60 **Mark Pawsey:** Kate, can you see that danger?

Kate O'Neill: I can see a danger if you are looking for information that is not relevant or necessary to prove to the person—

Q61 **Mark Pawsey:** If there is a smaller company in a supply chain, and a big company is demanding all sorts of information from the smaller company, the smaller company is hardly going to say, "I am sorry. I am not going to do that".



Kate O'Neill: You have to look at the big picture. You also have to look at your business strategy. You might not want to do business with that big company. It might be the cost of business that you will have to become better at providing the information they require.

Q62 **Mark Pawsey:** The point I am making is that the big company may be demanding more information from the smaller company than is actually necessary.

Kate O'Neill: It comes back to setting out your stall and saying, "I have given you the information that is relevant to our business strategy and to the risks of us delivering what you have asked us to do". You have to look at this as risk management as well. What are the risks to a company being able to supply to—

Q63 **Mark Pawsey:** I can tell you that most SMEs faced with a demand from a big and important customer will put lots of resources into doing what the big company is asking them to do.

Kate O'Neill: Yes, but as ever it is about capital investment and demand. Your bank might say, "I need you to prove that you have mitigated the risk of your carbon emissions in the type of work you do". That will just be a part of what you have to do to deliver what you—

Q64 **Mark Pawsey:** Why should the bank need that information?

Kate O'Neill: I have no idea. They may want to know that your risks are being mitigated before they lend you money. Like anybody providing capital or debt, they might want to know you have a risk framework in place.

Ingrid Holmes: It is important to bring it back up to the big picture. We do face environmental and social deficit, and we do need to start seeing the opportunities and risks factored into the cost of capital to send the right price signals to the market.

To Kate's point, it is about asking the supply chains of big companies to report on the material risks. What is important to their bottom line and to their business strategy? If you think about a company like L'Occitane, which relies on natural plant products, if we have droughts and extreme temperatures and that is not being factored in to how you are thinking about your land stewardship, you have a non-financial risk that is going to become financial. It then makes sense to think about more regenerative forms of agriculture and diversifying where you source your goods. It has to be material. The point of these disclosures is not for disclosure's sake. It is to address these bigger issues.

Q65 **Mark Pawsey:** The point I am making is that the small company, faced with that demand for information from the big company, is unlikely to be able to say, "I am sorry. I am not going to do that". That is the relationship between big company customers and small company suppliers. I am bothered that there may be too much of a burden being



passed down to SMEs, which are going to struggle to provide everything that is being asked of them.

Ingrid Holmes: It is prudent to ask the supply chain company that question so they can think about the risks and report back, "It is not relevant", "It is managed" or, "It is unmanaged and we are doing something about it".

Kate O'Neill: It is about setting out exactly those points: "It is relevant to us", "It is not relevant" or "We are on it". It does not have to be onerous if you are confident that you have actually thought about using that company or supplier.

Richard Spencer: You are right in highlighting the danger of unbearable amounts of information being required. That is part of the need that we see in understanding what these issues truly are. For businesses at the top of the supply chain, it is about asking for information that is material to their decision rather than blanket asking for all the information.

Q66 **Mark Pawsey:** The danger is that they will just have a blanket ask of everybody—

Richard Spencer: As capacity and understanding of the issues goes up, I would not see that as a danger.

Q67 **Andy McDonald:** It is an absolutely fascinating discussion. At the outset, we talked about the stewardship code and the International Sustainability Standards Board and these being transparency instruments. It is a fascinating area, but I still do not have a handle on what auditors are required to do in terms of disclosure and verification. It seems to be a journey that people are on.

We have the EU taxonomy. That is out of the window now. We are going to copy and paste it and put a Union flag on it, apparently. What is actually required?

Richard Spencer: Currently, assurance of ESG information is voluntary. Insofar as an auditor will conduct a regulatory audit of a financial statement, that auditor then provides a consistency view of the other information in the annual report. That sounds very basic, but most auditors do a great deal of work with the narrative and non-financial information to assess consistency with the audit. You have a statutory audit piece here.

What is coming up in the future with the International Sustainability Standards Board? We do not know yet, but there could well be a requirement to assure that information. The IAASB, the International Auditing and Assurance Standards Board, is producing a framework that will be published in 2023 for consultation.

Q68 **Andy McDonald:** Things are going to look very different in a few short years.



Richard Spencer: Yes. That comes back to my point about the knowledge gap. Auditors have the skills and experience currently to look at historic financial information and to make a consistency assessment. They do have those skills.

When it comes to forward-looking or prospective information or non-financial information, I would say there is a knowledge gap that we and other professional bodies are addressing, which is simply to do with understanding the new subject matter. There is a knowledge gap, but I would say there is no skill gap and there is no experience gap.

Q69 **Andy McDonald:** There is an appetite for this information.

Richard Spencer: Yes. That is part of the challenge. It is growing exponentially. The new ISSB will, in all probability, have an assurance requirement coming alongside it. At the moment it is voluntary in the UK.

Kate O'Neill: You have to look at the link between non-financial information and financial information. We do hear people find that non-financial information is all so burdensome. That is why we say, "Report once; use often".

The linkages are becoming more acute for the right reasons. You should not be saying things in the front of a report that has an impact on your financial outcomes and vice versa. There is also a demand for the information that is not always measured in financial outputs, such as the way you treat your employees or the way you treat your supply chains. There is much more demand for assurance that what you are saying about those things is true.

I completely agree that the skill sets are there. Ten or 15 years ago people were not asked to look at things like cyber risk. They have developed those skills and continue to develop skills in areas that are evolving. The non-financial link to financial reporting is becoming much more important. That has to be relevant, rather than the marketing of, "We are a wonderful company. We are great".

The introduction of double materiality has helped a bit with that, dare I say, woke-washing or greenwashing.

Q70 **Andy McDonald:** What does that mean?

Kate O'Neill: Double materiality is when you talk about the way in which you are impacted by ESG factors in your business model. You also have to talk about how you then, either the products you produce or the things that you do, talk about your materiality and impact on the environment, supply chains, et cetera.

That has meant that investors have said, "Yes, we have read the glossy bit, but none of your products do what you say they do. None of your interactions actually support that". That has been used as a tool more



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and more to make sure people are doing what they say they are. I do not know whether you have a view on materiality, Ingrid.

Ingrid Holmes: It is horses for courses in terms of reporting frameworks. One of the challenges with the ISSB is to get the double materiality view in. It is purely, as I understand it, looking at the impact environmental, social and governance factors have on your financial performance, which is one lens.

There is not necessarily scope within that to report on your impact as a company on the world and what you are doing to manage some of these deficits we talked about. That will probably sit more in some kind of corporate strategy report. It is something that will need to be implemented through our Companies Act in the UK. You cannot load everything on to these metrics; we need a suite of tools.

Kate O'Neill: It is quite a good lens to start getting those types of views coming through.

Ingrid Holmes: It is the purpose discussion, is it not?

Kate O'Neill: Yes, that is right. I could have brought in the auditing standards in a small vehicle. We can always provide those to the Committee. They should be evolving and they should be updated, where appropriate, to meet the changing requirements of users of corporate reporting and the people who depend on it.

Q71 **Charlotte Nichols:** I am interested in hearing from the panel about the expectation gap between what auditors are required to do to verify ESG disclosures and what stakeholders expect auditors to be able to do. Does this expectation gap exist? If it does, how can it be addressed? Kate, I will probably start with you, if that is okay.

Kate O'Neill: Auditors have a role in this. It is not the only role. The board and management absolutely have to assure the financial information they produce and the non-financial information. It cannot just be the auditors being told, "It is all on you". It has to involve resilient statements, the role of an audit committee in the board structure and the board's own sign-off. That means education for boards and management teams on the ever-evolving requirements around ESG and its relevancy to their operations and strategy.

Auditors are one part of the outcomes, not the only people we should be pointing the finger at and saying, "It is up to you". Boards and management committees, the internal auditors and any other part of the assurance network all become very important in this.

Q72 **Charlotte Nichols:** The other parts of that that you mentioned would all be internal within the company. What about in terms of external verification?



Kate O'Neill: You might be getting help with your assurance from external bodies, who may have the expertise that you do not want to have in-house. This is the huge linkage between the corporate governance code and all of the remit of the FRC. Nothing is seen in isolation. There is a huge ecosystem that is all interlinked.

Richard Spencer: There is a huge expectation gap. There is often a misunderstanding about what audit covers. Audit is a statutory process that covers the financial statements. There is an assumption that the auditor is auditing the whole of the annual report; they are not. They are auditing the financial statements and then talking about consistency with the rest of it.

That is compounded by the growing interest and expectations of so-called ESG reporting. It is also about understanding how an audit happens. People often think that the auditor looks at everything rather than sampling and testing. There is a big gap about what is happening.

Ingrid Holmes: There is the audit of the accounts and a need to skill up to understand how key environmental and social factors might affect revenues in future. A really specific example would be for an auditor to look at oil price forecasts and carbon budgets and say, "Is this a reasonable set of assumptions to put into your profit forecasts?"

There is also a separate piece around the ESG data itself, but getting those financial metrics and valuations right is key. From the conversations I was involved in maybe five years ago, that capability was not there. It is now slowly being built.

Q73 **Charlotte Nichols:** Just to dig down a bit deeper into that, all of you have alluded to the idea that auditors are not necessarily the right people to be making these determinations. I am thinking of big cases such as the collapse of Carillion, for example. KPMG ended up getting sued for that because of the fact they had not even fulfilled their financial requirements as auditors, let alone these other responsibilities that we might be asking them to go into.

Do accountants and auditors have the skills, expertise and capacity to report on and audit ESG factors? Would putting the onus on audits and accountants further consolidate, for that reason, the auditing sector into the Big Four auditors that we see? People might say that perhaps only these bigger auditors would have the necessary skills and people to be undertaking audits at that level. That is probably not a very concise question. Hopefully you have made some sense of it.

Richard Spencer: Certainly, auditors do have the skills and experience and, when it comes to historic information and financial information, the expertise and capacity. As I was saying, they also have the skills to make that consistency assessment under the requirements.

ESG assurance itself requires specialist knowledge. Audit firms frequently and regularly bring in experts on ESG. As ESG assurance matures, it



would not be surprising to see two models. In one model, you would have auditors who are within a regulatory environment that enforces high standards and a boutique consultancy that has expertise.

Equally, many of the audit firms are building their expertise in this area at the same time. We fully recognise that and we are participating with others in building that capacity amongst our members.

Kate O'Neill: When the happy day comes when primary legislation is passed to create ARGAs—I am just putting a little plug in there—the FRC will be on a statutory footing and its remit will be expanded. The competition issues that have, dare I say it, plagued the industry for a long time will be able to be examined through things like the proposed managed share audit, which might, as we have just said, result in specialist boutique firms being brought in. We do see that the larger firms are employing people for ESG auditing at some pace to develop the skill sets there.

Again, it is about the assurance that can be given by management and boards. We have to factor that in. It cannot just be on the auditors. They can only audit what is being produced for them to review, challenge and sign off on.

Q74 **Charlotte Nichols:** Within wider society, are there sufficient consultants and things that boards, as you said, can go to for advice and information?

Kate O'Neill: I would say there are too many on some issues. Some of the FOMO and anxiety that some boards and reporting entities feel is probably to do with having too much information. They said, “No, we should not do it that way. I heard you have to do 100 pages here and there”.

At the FRC, we sometimes scratch our heads. We put out a bit of fairly straightforward guidance, and suddenly it erupts, with people saying, “We have to go and report on this now”. We never asked for that; we really did not. That is why we put out so many pieces—we hope they are very useful—of best practice, guidance and examples, et cetera, and have very extensive stakeholder engagement. We use other regulated bodies in our remit such as the ICAEW to reach those preparers and auditors.

Ingrid Holmes: I am not an audit expert, so I am going to pass on that one.

Richard Spencer: I was just going to say that, as standards like the International Sustainability Standards Board’s standards come in, the wraparound not only of what I need to do but how I need to do it is going to be so important. We need to be ready to help build that capacity across the professions.

Chair: It sounds like we should all go and work in ESG.

Richard Spencer: It is a booming market.



Q75 **Chair:** There is just one last question from me. All of this seems to rely on the fact that the vast majority of companies, directors and boards want to do the right thing, comply with the regulations and the guidance and go about doing their business in line with their obligations.

Of course, there are always examples where people do not. We have had the CEOs of big companies before this Committee telling us that they broke the law; they knew they broke the law; they would do it again; and they got away with it. Should there be some hard enforcement on this? Is it okay for directors to flagrantly break the law and be able to get away with it?

Kate O'Neill: I cannot comment on our fellow regulators that look after some of that. We have said publicly that we think dropping the introduction of Sarbanes-Oxley from the BEIS White Paper was a missed opportunity. You win some; you lose some.

This has to be about holding people to account. At the moment, the FRC's powers are limited, until we become ARGA, to a certain subset of part of the assurance and governance process. Given the comply-or-explain principles of our corporate governance code, it is pleasing to see that, as you say, most people want to do the right things. If they are not doing it now, they are talking about how they intend to change that.

We also are very interested in how the Wates principles that apply to private companies mirror some of the same behaviours of the corporate governance code. There is no code or requirement that they should comply, but they want to because they want to be able to say to their stakeholders that they are doing their best to deliver what they said they were going to do in the right way. That might sound a bit fluffy, but there is hope. I am hoping that the people you refer to, Chair, are in the minority rather than otherwise.

Q76 **Chair:** They are, but you would like to see the director liability provisions brought back into the Bill when it finally reaches—

Kate O'Neill: I am not sure that is actually going to be possible.

Chair: You would like to see it.

Kate O'Neill: We think it is a missed opportunity. If you look at the fact that a fairly libertarian state like the United States of America could put it in place, that shows the art of the possible there.

Chair: Thank you to all three of you for your contributions. That brings the session today to an end.