

Shared Assessments
FCA CP 25/34 Regulatory Response

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To: Financial Conduct Authority
From: Andrew Moyad, CEO, Shared Assessments LLC

Subject: FCA CP 25/34: ESG Ratings Regulatory Response

Shared Assessments appreciates the opportunity to submit comments in response to the U.K. Financial Conduct Authority's (FCA's) Consultation Paper 25/34: ESG Ratings. Shared Assessments is a member-driven, industry-standard body that defines best practices and develops tools to advance third-party risk management programs worldwide (see "About Shared Assessments" below). Our membership includes firms and agencies headquartered in or operating in the U.K. On behalf of the organisation and its diverse group of professional member firms, thank you for considering our response.

The consultation notes that CP 25/34 would be relevant to ESG providers, users of ESG ratings (specifically, asset managers, asset owners, and benchmark administrators), rated companies, trade associations, civic society organisations, academics, journalists, and other regulatory agencies and/or policy makers. Shared Assessments would like to stress that this proposal is also important to enterprise risk management (ERM) and third-party risk management (TPRM) programs. Our comments are provided specifically from the perspective of TPRM practitioners, for whom ESG ratings increasingly inform supplier due diligence, ongoing monitoring, and regulatory compliance obligations.

ESG Ratings: Proposed Approach to Regulation

We applaud the FCA's efforts to make the ESG ratings market more transparent, reliable, and comparable. We believe these efforts will benefit the increasing number of risk managers who rely on ESG ratings agencies in TPRM programs.

1. Benefits of the Proposed Framework for TPRM Programs

- 1.1. *Validation of third-party sustainability assessments.* Many of our member firms are incorporating ESG consideration into their third-party and supply chain due diligence assessments. This may occur at various points in the third-party lifecycle, most notably during procurement activities and ongoing due diligence assessments. Carbon emissions data or greenhouse gas emissions remain the most common ESG consideration requested during third-party due diligence assessments; however, some firms are incorporating a much broader array of assessment questions around additional issues such as waste management practices, renewable resource use, health and safety matters, modern day slavery and human trafficking, talent management, supplier diversity, community relations, product labeling, code of conduct, and board composition.

Shared Assessments has compiled more than 180 ESG-related due diligence questions for thousands of TPRM programs based on member input. As TPRM programs continue to mature and automate, we believe that risk managers will increasingly turn to ESG ratings agencies to help supplement and validate third-party responses to due diligence assessment questionnaires, so greater clarity about whether a rating establishes a defensible minimum standard of care (e.g., compliance with laws) versus a more expansive, visionary standard of care (e.g., best in class ESG excellence) are increasingly important for effective decision-making for business and risk leaders.

- 1.2. *Continuous monitoring of sustainability practices.* Greater transparency and consistency in ESG ratings methodology would materially increase adoption within the continuous monitoring frameworks now widely used by TPRM programs, including more clear, reliable indications that suppliers remain within measurable organizational risk tolerances, a key point for risk managers. To date, many TPRM programs have been slow to incorporate ESG rating agencies into their continuous monitoring efforts due to the wide variance in scores and methodologies across rating agencies. We believe that greater transparency on data collection and scoring methodologies would increase confidence and support broader integration of ESG ratings into ongoing monitoring of third-party sustainability performance.
- 1.3. *Due diligence assessments of ESG ratings agencies.* From a TPRM perspective, the ESG rating agencies may themselves be important suppliers to firms that rely on sustainability measures to help manage risk and allocate capital. This is particularly true for regulated firms such as institutional investors, asset managers, banks, insurance firms, and other diversified financial service firms. When determining the nature and scope of due diligence assessments, TPRM practitioners consider many factors, including the level of regulatory oversight of suppliers. Requiring ESG ratings agencies to meet baseline standards would materially enhance their credibility as third-party providers. (*Questions 2 & 3: We agree with the FCA's approach.*)

2. Support for Key Elements of the Proposal.

Shared Assessments believes the requirements outlined in the FCA's CP 25/34 consultation are both comprehensive and fully appropriate. We would like to highlight the following areas as particularly important for third-party risk practitioners:

- 2.1. *Minimum public disclosures.* The minimum public disclosures related to methodology are critically important to TPRM practitioners. In particular, the model disclosures (see items below that merit further clarity), a summary of data types, data policies, and the methodology review cycle are essential to those making even a high-level assessment of an ESG ratings provider's performance. (*Question 4: We agree with the proposed minimum public disclosures.*)
- 2.2. *Direct user disclosures.* Direct user disclosures at both product and individual rating levels are essential. Risk managers may receive ratings from multiple sources, or they may have to choose from among several sources. Therefore, not only must third-party risk managers evaluate individual ESG ratings, but they must also reconcile different scores for the same providers across rating agencies. (*Question 6: We agree with the proposed disclosures and feel the onward sharing is particularly important.*)
- 2.3. *Governance and outsourcing requirements.* We support the proposed governance requirements that require rating agencies to keep operational responsibility and influence over the entire ESG

rating process, including outsourced functions. The emphasis on oversight, accountability, and the ability to review and amend any part of the process is appropriate and aligned with established third-party risk management principles. (*Questions 10, 11, & 12: Section Four's emphasis on outsourcing and its requirement that authorized entities retain oversight and accountability for the entire ESG ratings process, including outsourced functions, is appropriate and welcomed.*)

- 2.4. *Methodology changes and quality assessments.* FCA's proposal requires that ratings providers conduct periodic quality assessments and notify users and rated entities of material changes before they come into effect. Third-party risk management practitioners must understand rating methodology changes as quickly as possible to properly interpret rating changes at individual entities within their supply chains. (*Question 16: We agree with the proposed approach.*)
- 2.5. *Market stability and operational resilience.* ESG ratings are increasingly used to inform supply chain due diligence and regulatory reporting. Concentrated reliance on a small number of providers could introduce model risk and operational resilience considerations across markets. In this context, clear transparency and governance requirements (such as those in CP 25/34) will further support market stability by reinforcing expectations around operational resilience, model validation frameworks, and conflict-of-interest controls.

3. Areas Where Further Clarification is Needed

- 3.1. *Transparency of models and the use of AI.* The consultation highlights recent transparency challenges for many users of outsourced models, including those used to develop ESG ratings for individual companies. Paragraph 3.21 highlights an important tradeoff between the requirement to support proportionate transparency and the need to protect commercially sensitive information. For example, disclosing the use of AI in ratings methodology (as the consultation suggests) is a helpful first step but not sufficient, as AI and the various techniques involved represent a material change from conventional model risk. Notably, AI models undergo ongoing training, commonly operate under either supervised or unsupervised learning modes (technically speaking), and may also involve agentic capabilities, so understanding these details will govern the form of model validation providers need to conduct and that users need to understand. Accordingly, as the use of opaque ("black box") model components increases, TPRM practitioners will require greater transparency to understand the internal drivers of ratings outcomes. Without this visibility, users may lack the information needed to interpret ratings or assess model risk effectively based on the nature of the technology(s) used. We encourage the FCA to clarify that model disclosures, including black-box components, are sufficient to ensure meaningful transparency.
- 3.2. *Scope exclusions for proprietary ESG ratings.* Paragraphs 2.32 – 2.34 exclude certain ESG ratings produced by asset managers, investment firms, and benchmark administrators from the proposed regulation. While we agree that any proprietary ratings resulting from internal research should remain outside the scope of regulation, additional clarification would be beneficial where such ratings are used in external or client-facing materials. (Notably, some of these potentially excluded organisations may partially or wholly own ESG providers that operate in the commercial marketplace, whether today or in the future.) At a minimum, high-level methodological disclosures from all commercially available ratings services would support informed use by investors and risk managers.

4. Conclusion.

We want to stress our support for the proposed approach to the regulation of ESG ratings providers. Shared Assessments believes the proposed regulation is straightforward and appropriate. The regulation will be especially important as regulatory approaches to ESG risk management continue to diverge across geopolitical boundaries. The proposed regulations will benefit a wide range of users, including those organisational risk managers charged with ensuring that their suppliers meet their enterprise and regulatory ESG-related outsourcing requirements.

About Shared Assessments

Since 2005, Shared Assessments has set the standard for third-party risk assessments. Shared Assessments is a member-driven, industry-standard body that defines best practices, develops tools, and conducts pace-setting research. Program members cut across the full range of compliance, legal, operations, procurement, and risk roles. Members work together in an interdisciplinary manner to build and disseminate best practices and develop related resources that give all third-party risk management stakeholders a faster, more rigorous, more efficient means of conducting security, privacy, and business resiliency control assessments. Additional information about Shared Assessments is available by visiting: <http://www.sharedassessments.org>.