

Sustainability Disclosure Requirements (SDR) and investment labels

Consultation Paper

CP22/20***

October 2022

How to respond

We are asking for comments on this Consultation Paper (CP) by **25 January 2023**.

You can send them to us using the form on our website at: www.fca.org.uk/cp22-20-response-form

Or in writing to:

SDR and labels policy
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

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cp22-20@fca.org.uk



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1 Summary

Why we are consulting

- 1.1** Consumers must be able to trust sustainable investment products. Consumers reasonably expect these products to contribute to positive environmental or social outcomes.
- 1.2** There are growing concerns that firms may be making exaggerated, misleading or unsubstantiated sustainability-related claims about their products; claims that don't stand up to closer scrutiny (so-called 'greenwashing').
- 1.3** Already today, greenwashing may be eroding trust in the market for sustainable investment products. Trust and integrity in these products are important to the transition to a more sustainable future. So, we need to build guardrails against this to protect consumers from potential harms. If consumers can't trust the claims firms make about their products, they will shy away from this market, slowing the flow of much-needed capital to investments that can genuinely drive positive change.
- 1.4** Tackling greenwashing is a core regulatory priority for us. In November 2021, we published [A strategy for positive change: our ESG priorities](#). This set out the important role the financial services sector has to play in helping the UK economy adapt to the transition to net zero and a more sustainable future. One of the key themes of our strategy is the importance of building trust and integrity in sustainable instruments, products and the supporting ecosystem.
- 1.5** These outcomes align with the FCA's operational objectives to protect consumers, to protect and enhance market integrity, and to promote effective competition in the interests of consumers. They align with the Consumer Duty's requirement for firms to act in good faith and for consumers to be provided with information that enables them to make informed, effective decisions. They also support the expectations set out in the Chancellor's latest remit [letter](#) to us, in which he welcomed work we have done to date as we 'have regard to the Government's commitment to achieve a net-zero economy by 2050 when advancing our objectives'.
- 1.6** In this Consultation Paper (CP), we are proposing new rules to help consumers (also referred to in this CP as 'retail investors') navigate an increasingly complex investment product landscape, protect them from greenwashing, and rebuild trust.
- 1.7** Our proposals build from the early views set out in our Discussion Paper on Sustainability Disclosure Requirements (SDR) and investment labels (DP21/4), published last November. We received broadly positive feedback to our approach, along with more constructive, targeted feedback that we have taken into account in developing our proposals. We summarise this feedback in later chapters of this CP.
- 1.8** Through our proposals, we are playing our part in the delivery of the Government's [Roadmap to Sustainable Investing](#), published in October 2021. This Roadmap sets out plans to introduce SDR and investment labels, building from the UK's economy-wide

implementation of disclosure requirements aligned with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

- 1.9** The proposals in this CP are a starting point for a regime that we will expand and evolve over time. These proposals capture the core elements of the regime: sustainable investment labels; qualifying criteria that firms must meet to use a label; product- and entity-level disclosures; and naming and marketing rules.
- 1.10** The labels distinguish between different types of investment product based on their sustainability-related objectives and features. Together with the associated disclosures, they will give consumers the information they need to make informed choices about which products meet their needs and preferences. The package of measures that we are proposing aims to provide greater transparency, consistency, and in turn, trust, in the market for sustainable investment products.
- 1.11** The proposals in this CP focus on funds and portfolio management based in the UK, as set out in more detail in Chapter 3, Table 1. However, as we want retail investors to be able to trust all products offered in our market, overseas funds form an important part of the overall regime. We intend to follow with a separate consultation in due course on how the proposals in this CP may be applied in respect of overseas funds.
- 1.12** We also recognise that there is potential for similar consumer harm in relation to other investment products marketed to retail investors in the UK, such as pension products. We have included a short discussion on issues relating to these products in Chapter 8, with a view to expanding the regime in due course, working with other government departments to ensure a consistent and coherent approach.
- 1.13** Further, we recognise that the market for sustainable investment products is still evolving. Our proposals are designed to help consumers navigate the market as it is today, while allowing room for further development in future. Importantly, we intend to build on our proposed requirements in line with the development of international sustainability-related reporting standards by the International Sustainability Standards Board (ISSB).
- 1.14** In developing our proposals, a key aim has been to ensure the regime works both in the interests of consumers and for the firms that need to apply the rules in practice. So, we have engaged with industry throughout the process – including through our discussion paper and by taking advice from a dedicated Disclosures and Labels Advisory Group (DLAG).
- 1.15** Since the needs of consumers have been central to our policy design, we also carried out consumer research to inform our final proposals. The findings are summarised in Chapter 2 and outlined in full in an Occasional Paper published alongside this CP ([Occasional Paper 62](#)).
- 1.16** We sought to build on existing requirements and expectations for firms – outlined in our [Guiding Principles](#) for the design, delivery and disclosure of Environmental, Social and Governance (ESG) funds, published in July 2021 – emphasising that firms making sustainability-related claims must be able to evidence them. We have developed a set of qualifying criteria that will ensure firms are indeed able to substantiate the claims they are making. We are also proposing naming and marketing rules that restrict the use of certain sustainability-related terms for products that do not use a label.

- 1.17** While we need to move quickly to address potential harms in the market today, we recognise that firms will need time to apply the new rules: to assess their products against the qualifying criteria, and decide whether to label their products or amend their naming and marketing accordingly. They will also need to adjust to the new disclosure requirements.
- 1.18** So, we propose that the labelling, naming and marketing and initial disclosure requirements under this regime would not come into effect until at least 30 June 2024. This is one year after we intend to publish our final rules, subject to consultation feedback.
- 1.19** We are also proposing a general 'anti-greenwashing' rule reiterating requirements for all regulated firms that sustainability-related claims must be clear, fair and not misleading. Since this aims to clarify existing rules, this would come into effect immediately on publishing our Policy Statement (PS).
- 1.20** We want the UK to be a trusted centre for sustainable investment and place the UK at the forefront of sustainable investment internationally. Our proposals aim to do this by setting robust regulatory standards to protect consumers that raise the bar and build a strong foundation for sustainable investment products. However, as set out in DP 21/4, we recognise that many firms and products that may be in scope of our proposals operate internationally. We have sought, as far as possible, to achieve international coherence with other regimes – notably the Sustainable Finance Disclosure Regulation (SFDR) in the European Union (EU) and proposals by the Securities and Exchange Commission (SEC) in the United States (US).
- 1.21** The starting point for our proposals is, however, different as we are introducing a consumer-focussed labelling regime as well as disclosure requirements. So, although we have sought to complement the approaches taken in other jurisdictions our proposals differ in some areas, as discussed in Chapters 4 and 5, and Annex 1.

What we want to change

- 1.22** Our proposals cover the following main areas:
- **Sustainable investment labels** to help consumers navigate the investment product landscape and enhance consumer trust.
 - **Consumer-facing disclosures** to help consumers understand the key sustainability-related features of a product.
 - **Detailed disclosures** targeted at a wider audience (eg institutional investors and consumers seeking more information):
 - **pre-contractual disclosures** (eg in the fund prospectus), covering the sustainability-related features of investment products
 - **ongoing sustainability-related performance information** including key sustainability-related performance indicators and metrics, in a sustainability product report
 - **a sustainability entity report** covering how firms are managing sustainability-related risks and opportunities
 - **Naming and marketing rules** restricting the use of certain sustainability-related terms in product names and marketing materials unless the product uses a sustainable investment label.

- **Requirements for distributors** to ensure that product-level information (including the labels) is made available to consumers
- **A general 'anti-greenwashing' rule** applied to all regulated firms which reiterates existing rules to clarify that sustainability-related claims must be clear, fair and not misleading.

1.23 Taken together, our proposals aim to reduce greenwashing, address the associated harms and build trust in the market.

1.24 The labelling regime assesses products based on the sustainability objective they are seeking to achieve. The three labels – 'sustainable focus', 'sustainable improvers' and 'sustainable impact' – distinguish between different types of sustainable product, according to the nature of the objective and the primary channel by which each can plausibly achieve or encourage positive sustainability outcomes.

1.25 There is no hierarchy between the proposed labels: each is designed to deliver a different profile of assets and consumer preferences. We propose that firms can choose whether or not to label their products. Firms will however need to meet our proposed qualifying criteria to do so. The criteria will ensure firms are substantiating their sustainability-related claims – including by setting a clear, explicit sustainability-related objective and reporting on the sustainability performance on an ongoing basis. If firms are not able to meet these criteria to evidence their claims, we propose restrictions on the use sustainability-related terms in their product names and marketing. This is key to protecting consumers from greenwashing.

1.26 We note that considering the financial implications of ESG factors in investment decisions is increasingly seen as integral to a firm's meeting its fiduciary duty to clients and consumers. And some consumers' ESG preferences fall short of influencing positive environmental or social outcomes – for instance, they may seek certain exclusions to align with their individual ethics or values. It is important that consumers are able to identify and access such products.

1.27 But equally, it is important that they can distinguish them from products that do contribute to positive sustainability outcomes and meet our qualifying criteria. Our naming and marketing rules therefore allow for firms to describe the sustainability-related strategies of such products, but in a manner proportionate to the role that sustainability considerations play in their investment processes.

1.28 Further, our proposed product- and entity-level disclosure rules, and requirements for distributors, aim to provide consumers with the information they need to choose between different products and providers. We have sought to build from existing requirements to avoid placing a disproportionate burden on firms.

Outcomes we are seeking

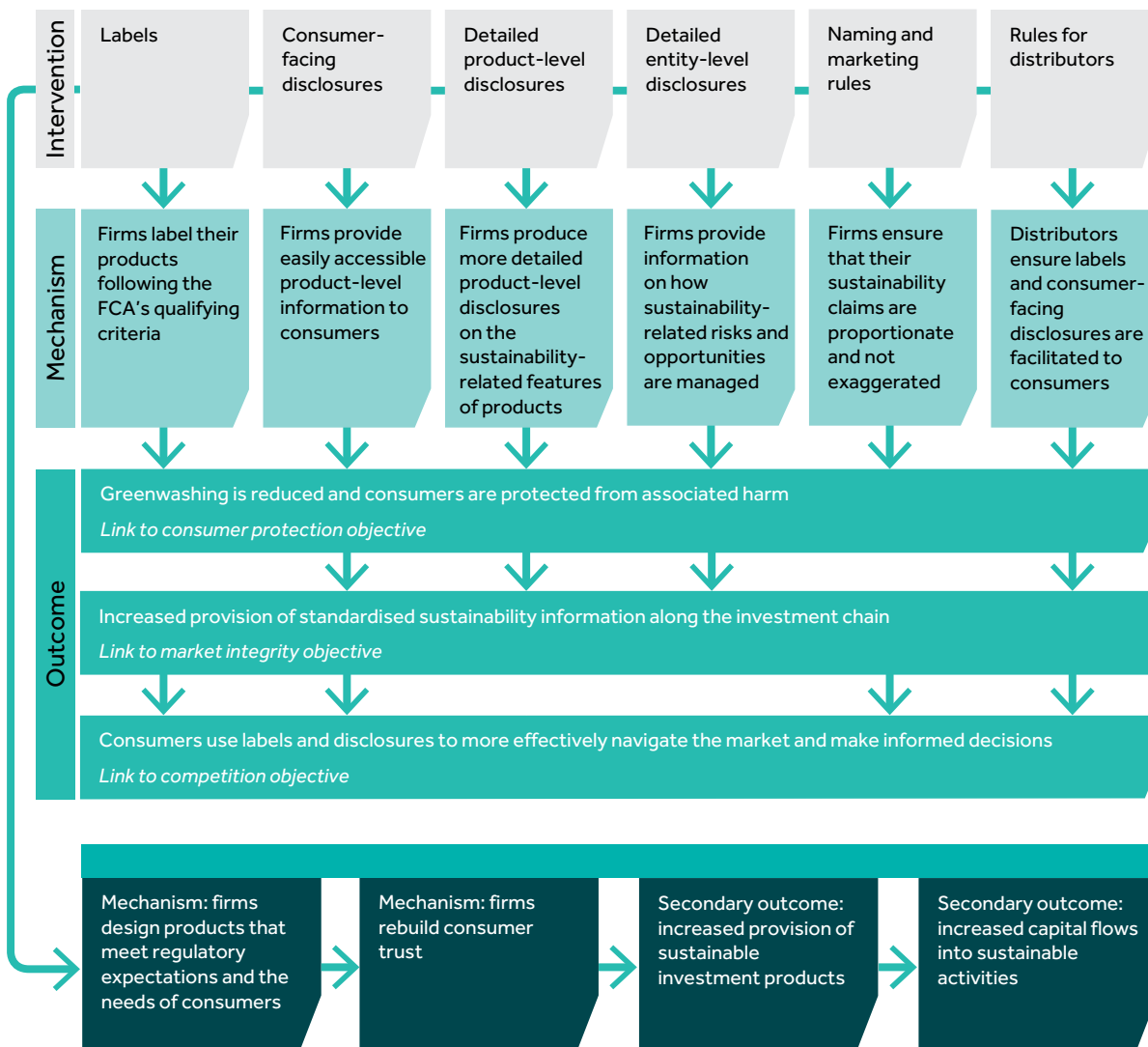
1.29 Our proposals are intended to advance the FCA's strategic objective to make markets function well, by increasing transparency on the sustainability profile of products and firms and reducing the risk of harm arising from greenwashing.

1.30 Our proposals are also intended to advance the FCA's operational objectives:

- The disclosure requirements will facilitate the flow of consistent information along the investment chain, increasing transparency in the market and furthering our objective to promote market integrity.
- Sustainable investment labels, consumer-facing disclosures, and rules for distributors will help to protect consumers by equipping them to navigate the market more effectively and identify products that meet their needs and preferences. The naming and marketing rules will similarly help to protect consumers by reducing the risk of greenwashing.
- The labels and consumer-facing disclosures will help consumers to compare products more effectively, and efficiently, potentially leading to greater competition among similar products (ie where consumers are comparing like-for-like), in line with our objective to promote competition in the interests of consumers.

1.31 **Figure 1** below sets out the proposed requirements, the actions that firms and other stakeholders will need to take, and how these will support our target outcomes.

Figure 1 – Causal chain



Measuring success

1.32 To assess the effectiveness of our policy, we will:

- monitor use of the sustainable investment labels by firms eg through a review of the characteristics of labelled products to assess whether they are meeting our criteria and how they are performing against their commitments
- assess the usefulness of the labels and product-level information to consumers eg through our Financial Lives Survey and by engaging with consumer groups such as Which?
- assess the provision of sustainability-related information through the FCA ESG Division's Market Intelligence and Engagement team's horizon-scanning activities and working with other regulators such as the Prudential Regulation Authority (PRA) and Financial Reporting Council (FRC)
- assess the incidence of greenwashing by firms through monitoring complaints made to the FCA's Supervision Hub and intelligence gathered on quality of applications made to Fund Authorisations. As set out in '[FCA outcomes and metrics](#)', we are working on metrics to monitor the incidence of misleading marketing for ESG products and the increase in trust of ESG-related products.
- carry out a post-implementation review after three years of the regime coming into force

Supervising and enforcing the regime

1.33 We will apply our usual supervisory and enforcement approaches and respond to compliance issues as they arise. We may also carry out periodic assessments. We may take enforcement action if a firm has ignored a requirement to make the necessary disclosures; made misleading disclosures or misused a label; or breached our naming and marketing rules.

1.34 If a firm chooses to label a product, the firm remains responsible for its classification and ensuring the label is appropriate. The Fund Authorisation team will review, and may challenge, the categorisation of any new fund submitted for authorisation. However, this will not be an approval of the label.

1.35 We will continue to support industry with the implementation of the regime through our stakeholder engagement (eg roundtables, webinars etc) and guidance (eg implementing guidance in Appendix 2 of this CP).

Who this applies to

1.36 This CP will be of interest to all FCA-regulated firms, as we are proposing to introduce a general 'anti-greenwashing' rule that will apply to all firms. The core elements of the regime – labelling and classification, disclosure and naming and marketing rules – will apply to asset managers initially. However, we are seeking views on expanding the regime to FCA-regulated asset owners in respect of their investment products. We are also proposing targeted rules for the distributors of investment products to retail investors in the UK.

1.37 Our proposals have been developed primarily in the interests of retail investors (also referred to in this CP as 'consumers') ie non-professional investors, as well as institutional investors (also referred to in this CP as 'clients'). We refer to clients more broadly in the draft instrument at Appendix 1 to cover both retail and institutional investors. We encourage feedback from these stakeholder groups.

1.38 We also welcome contributions from all parts of the financial sector, and other interested parties, including:

- industry groups and trade bodies
- consumer groups and individual consumers
- policymakers and other regulatory bodies
- industry experts and commentators
- academics and think tanks
- stakeholder advocacy groups

Equality and diversity considerations

1.39 We have considered the equality and diversity issues that may arise from the proposals in this CP. We do not consider that these proposals adversely impact any of the groups with protected characteristics ie age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment. We will keep this under review as we finalise the rules.

Next steps

1.40 We will review feedback received and intend to set out our final rules in a PS by the end of the first half of 2023. We also intend to build on the proposals in this paper and follow with further consultations in due course – including to expand the scope of the regime to overseas and pension products. See Chapter 8 for an overview of these actions.

2 Wider context and policy inputs

- 2.1** In this chapter, we provide some context for our proposals by describing the market for sustainable investment products and potential harms. We also set out the key policy inputs that have informed our proposals. This includes the feedback to DP 21/4, the recommendations of the DLAG, and consumer research carried out by the FCA's Behavioural Design Unit.

The market for sustainable investment products

- 2.2** As set out in DP21/4, the market for sustainable investment products – in the UK and worldwide – has grown rapidly and consumers can access an increasingly wide variety of product types. See **Box 1** below.

Box 1: Market for sustainable investment products

Sustainable investment products are structured around or pursue sustainability-related characteristics, themes or outcomes, while providing a financial return to investors.

Consumer demand for these products is growing rapidly. The FCA's latest Financial Lives Survey data shows that 81% of adults surveyed would like the way their money is invested to do some good as well as provide a financial return. Firms are responding to this demand: according to Investment Association (IA) data, the UK market for UK domiciled responsible investment funds grew 64% over 2021 to reach £79 billion, far outstripping the 11% growth in UK domiciled funds overall. In the longer term, [Broadridge Financial Solutions](#) has predicted the global market for sustainable investment products will reach \$30 trillion by 2030.

The market for sustainable investment products is diverse. This stems partly from the broad scope of terms such as 'ESG' and 'sustainable', which can accommodate a range of products from those seeking 'solutions to the global water challenge', to 'investing in demonstrable gender and/or ethnic diversity'.

- 2.3** There have already been attempts at categorising investment approaches. For example, bodies such as the IA and other groups have identified several distinct strategies:
- **ESG integration.** These products incorporate consideration of sustainability-related risks, opportunities and impacts into their investment processes, research and analysis to assess their implications for enterprise value creation and hence financial returns.
 - **Exclusion or negative screening.** These products exclude certain investments on the basis that they fail to meet certain sustainability-related criteria or norms or fail to align with the manager's or investors' values. Exclusionary strategies may vary in their intensity and breadth.

- **Thematic investing.** These products invest in assets with certain defined sustainability-related characteristics, or with a focus on certain sustainability challenges.
- **'Best in class' or positive screening.** These products invest in assets that meet defined sustainability-related criteria or are considered better positioned to manage sustainability risks or maximise opportunities from sustainability-related developments.
- **Impact investing.** These products aim to make a positive, measurable environmental or social impact, including by directing capital to underserved markets or addressing market failures.

No one strategy is 'better' than another. These different approaches offer welcome consumer choice. However, it is important that product disclosures provide sufficient, accessible information to enable consumers to easily distinguish between products and assess which meet their needs and preferences.

2.4 The FCA welcomes this growth and diversification, which can help consumers more effectively find products that meet their sustainability preferences. However, this will only be achieved if the market operates effectively. And we are concerned that this may not be the case, leading to potential consumer harm. Our main concerns are:

- **Some firms are making misleading sustainability-related claims about their investment products.** As noted in our [Dear Chair Letter](#) last year, we have identified instances of firms making sustainability-related claims about their investment products that do not stand up to scrutiny. Such instances of greenwashing increasingly damages consumer trust in the market for sustainable investment products and causes potential harm such as consumers buying unsuitable products. So, our aim is to protect consumers from such claims. Alongside the proposals in this CP, we will be carrying out a multi-firm review to assess how well the market has adjusted to the expectations in our Dear Chair Letter. We are prepared to take action if we see evidence of poor conduct.
- **The market is difficult for consumers to navigate.** There is a lack of standardised product-level reporting on sustainability objectives and strategies. This makes it difficult for consumers to determine what each product is seeking to achieve and which strategies are being pursued. So, it may be challenging for a consumer to determine whether a product is integrating ESG factors into financial risk/return considerations; whether it has a specific sustainability goal to achieve a real-world positive impact; or whether it is targeting a particular sustainability-related asset profile or theme. And periodic disclosures may fail to provide consumers with sufficient information to assess whether their expectations are being met. Firms also often use certain terms interchangeably to describe their products and strategies, which is confusing to consumers. These include 'ESG', 'responsible' or 'sustainable', and other complex terminology such as 'transition pathways' or 'scenario analysis'. Indeed, the acronym 'ESG' has no natural language meaning when taken out of context, and some consumers may be unaware of what it stands for.

Key policy inputs

2.5 Several policy inputs have helped to inform the proposals in this CP.

The Government's Roadmap to Sustainable Investing

- 2.6** In October 2021, the UK Government published Greening Finance: A Roadmap to Sustainable Investing ('Roadmap'). The Roadmap set out plans for the FCA to introduce SDR rules for asset managers, certain FCA-regulated asset owners, listed issuers and financial advisers, as well as a labelling and classification system for investment products.
- 2.7** These initiatives form part of the wider implementation of SDR – an integrated, economy-wide disclosure regime that will increase the provision of standardised sustainability-related information along the value chain. The Government signalled that it expects the ISSB's standards to 'form a core component of the SDR framework' in particular the 'backbone of its corporate reporting element'. It also committed to consulting on creating a mechanism to endorse and adopt the ISSB's standards in due course. The Roadmap also set out the Government's long-term ambition to green the financial system and align it with the UK's world-leading net-zero commitment.
- 2.8** This CP sets out our proposed sustainability labelling and classification system for funds and portfolio management arrangements as well as disclosure requirements for asset managers, initially, with a view to expand the regime to certain FCA-regulated asset owners and other investment products (eg pensions). Financial advisers may fall into scope in their capacity as distributors of product-level information. However, as set out in the Roadmap, we will explore how best to introduce rules on product suitability for financial advisers in due course.

TCFD recommendations and future ISSB standards

- 2.9** In line with the UK Government's commitment to introduce mandatory TCFD-aligned disclosure requirements across the economy by 2025, we introduced climate-related disclosure rules for listed issuers (PS20/17 and PS21/23) as well as regulated firms (asset managers and FCA-regulated asset owners) (PS21/24). In developing and finalising these rules, we clarified that we consider TCFD-aligned disclosure rules to be a starting point and that we would build on our requirements over time.
- 2.10** For listed issuers, we acknowledged that the ISSB's future standards would provide the additional specificity and detail to meet investors' information needs. As reiterated in our response to the ISSB's Exposure Drafts, we strongly support the ISSB's proposals. We remain committed to consulting on amending our TCFD-aligned disclosure rules for listed companies to reference the ISSB standards, once finalised and available for use in the UK. We intend to issue a separate CP, and cost-benefit analysis, with our proposals for listed issuers in due course.
- 2.11** For regulated firms, we signalled our intention to expand on our TCFD-aligned disclosure rules and guidance within the ESG Sourcebook, covering additional sustainability topics over time. Both our existing TCFD-aligned disclosure rules and the ISSB's draft general sustainability disclosure requirements have informed the proposed disclosure requirements in this CP.

Discussion Paper 21/4

- 2.12** As a first step towards our commitments in the Roadmap, we published DP21/4 in November 2021. We sought feedback on a potential approach to classifying and labelling investment products based on sustainability characteristics, to help consumers better navigate the market for sustainable investment products.

- 2.13** We invited views on a tiered structure to the regime whereby the labels would be supported by a consumer-facing layer of disclosure, and more detailed disclosures at both product and entity level. The more detailed disclosures would build on our TCFD-aligned disclosure rules for regulated firms.
- 2.14** We received 126 responses. Most respondents broadly supported our overall approach to introducing SDR and labels. For instance, there was good support for an approach to classifying products based on 'intentionality' (meaning the investor's deliberate intention to achieve the product's stated objective); for introducing disclosure requirements that build from TCFD and the future ISSB standards; and for aligning with SFDR where appropriate. Respondents also agreed with introducing requirements for distributors of investment products to retail investors. We did, however, receive constructive feedback in a number of areas, which has informed the proposals in this CP. We summarise the feedback in Chapters 4, 5, and 7.

Behavioural research

- 2.15** We conducted behavioural research to assess how well potential product classification, labelling and disclosures may help retail investors navigate the market for sustainable investment products. We summarise this research in **Box 2** below and full findings are set out in a separate [Occasional Paper](#) published alongside this CP. We encourage stakeholders to consider both the CP and behavioural research findings when responding to our proposals.

Box 2: Behavioural research – exploratory analysis, online experiments and qualitative research

As a first step, in July 2021 we carried out [exploratory analysis](#) to understand how different information about how sustainable a financial product is, affects consumers' investment decisions. This took the form of exploratory conjoint analysis – a technique that asks participants to view products that have different features and make a hypothetical choice between them, allowing us to infer how influential each feature is for their choice. Just over 1,500 participants took part.

We found that objective gradings, in the form of medals, influenced how consumers would hypothetically invest. Consumers more frequently chose products that were given bronze, silver, or gold medals stating that at least a small proportion of companies in the fund have a positive environmental, social, or governance impact, than products that indicated having 'no positive impact'. We also found that 'ESG' signifying fund images, descriptions and strategies had no statistically significant effect on how consumers said they would invest.

Second, we conducted an online experiment in December 2021 with almost 7,900 participants. This tested comprehension of the consumer-facing disclosures (referred to as 'sustainability factsheets' in the findings), based on labels from DP21/4 (reproduced in Figure 3 below). Key findings included:

- consumer comprehension of sustainability-related information improved when participants were provided with a dedicated consumer-facing disclosure, compared with when they were only provided with a Key Investor Information Document (KIID)

- having been provided with a sustainability factsheet, more participants hypothetically chose to invest in an 'impact' product; and fewer chose a 'no sustainable goals' product, when compared with those only provided with a KIID
- consumers overestimated some of the sustainable characteristics of the 'Transitioning' and 'Aligned' products
- the length of the document (either a 2.5 page or 1 page factsheet) did not have an impact on comprehension
- while we did not specifically test the consumer journey, we found that comprehension increased when participants opened all disclosures, suggesting that further consideration should be given as to how to encourage engagement with disclosures

Third, we carried out qualitative research in May 2022. The consultancy firm FutureSight conducted seven focus groups totalling around 35 consumers with investment experience ranging from 'novice' to 'experienced'. Participants were presented with consumer-facing disclosures for the three different 'sustainable' labels. While some members of the focus groups understood the labels once properly explained, other consumers did not expect products to vary significantly in terms of their sustainability credentials; and the terminology used in the disclosures (eg stewardship) was not always intuitively understood. In addition, when presented on a linear scale, some consumers viewed the labelling system as a hierarchy, without understanding the nuances of the different types of sustainable investments. However, featuring only one product in the consumer-facing disclosure appeared to generate fewer misconceptions about the presence of a hierarchy between the sustainability categories.

Finally, we conducted another online experiment with almost 6,750 participants in June 2022. This tested a version of the labels and disclosures broadly similar to those proposed in this CP. In line with the first online experiment, results showed that providing the redesigned sustainability factsheet significantly improved consumer comprehension, compared to only being provided with a KIID.

Importantly, including consumer-facing disclosures for products without a sustainable label, albeit with limited content reflecting the nature of the product, increased consumer comprehension of sustainability information compared to when disclosures were provided only for those products with a sustainable label. This increase in overall comprehension was driven by the increase in understanding of the product without a sustainable label. In addition, the revised label and disclosures for the 'Sustainable Improvers' product appeared to increase comprehension of sustainability characteristics that had not been well understood in the first experiment for the 'Transitioning' product.

International and domestic context

2.16 Our proposals take into account and are consistent with the International Organization of Securities Commissions' (IOSCO) Recommendations on Sustainability-Related Practices, Policies, Procedures and Disclosure in Asset Management. This includes introducing disclosures consistent with the TCFD's recommendations as well as disclosures to help investors better understand sustainability-related products; promoting consistency, comparability and reliability in disclosure; and helping to prevent greenwashing.

2.17 We have taken account of proposals or regimes in other jurisdictions to address similar issues to those observed in the UK market. In particular:

- The EU SFDR requires firms to report on their sustainability risks and impacts, at both product- and entity-level, with the intention of combatting greenwashing and improving transparency. SFDR also categorises investment products to determine disclosure requirements.
- The SEC also proposes requirements for sustainable investment funds, categorising products to determine disclosures and proposing changes to product naming rules, aimed at enabling investors to make better-informed decisions about these products.

2.18 In the UK, the Treasury Select Committee's report Net Zero and the Future of Green Finance notes the potential for labels to help consumers navigate the sustainable investment market. While the report only considered labels in the context of climate change, it recommended that the FCA consult on the merits of introducing labels to help consumers and encourage innovation.

2.19 We have also considered several market-led initiatives relating to the labelling, classification and/or disclosure of sustainable investment products. These include the IA's Responsible Investment Framework; the British Standards Institution's sustainable finance standards programme; the guidance and resources produced by the Impact Management Project, and the CFA Institute's voluntary ESG disclosure standards for investment products.

Disclosures and Labels Advisory Group (DLAG)

2.20 Another key policy input has been recommendations from the DLAG, which we established alongside DP21/4. The DLAG is an expert advisory group made up of key stakeholders, including industry experts and consumer representatives, to provide independent advice to us on the development and implementation of our regime. The full list of DLAG members is set out in Annex 2 of DP21/4.

2.21 The full DLAG met five times and also heard from external stakeholders on specific topics (including private equity and real estate). In addition, smaller sub-groups met to provide targeted feedback under three dedicated workstreams covering:

- the approach to classification and labelling of products, including label names
- qualifying criteria underpinning the labels
- the content and location of disclosures, including interaction with the labels

2.22 The DLAG made several recommendations which either reinforced or challenged the positions set out in DP21/4. This included encouragement to pursue the 'tiered' approach to disclosures and a classification and labelling regime based on 'intentionality'. Consensus was not always reached in DLAG discussions, but the advice and feedback has influenced our proposals. We set out a summary of feedback on labelling, disclosures and naming and marketing in Chapters 4-6.

2.23 We thank the DLAG for their time and contribution to this work.

Other stakeholder engagement

2.24 In addition to their contributions on the DLAG, we observed and/or were informed of the findings of consumer research carried out by The Investing and Saving Alliance (TISA) and the IA on disclosures and on terminology and labelling, respectively. This complemented findings from our own consumer research, as set out in Box 2.

2.25 Further to a TechSprint in October 2021, we held a targeted 'PolicySprint' to help inform the sustainable investment labels. Participants presented views on the approach to labelling, the criteria that could be met to use each label, and what their corresponding data points could be. We thank participants for their time and contribution to this work.

2.26 We also engaged with other key stakeholders such as regulatory authorities in other jurisdictions, regulated firms, non-governmental organisations (NGOs) and consumer groups to gather feedback on our developing proposals.

3 Overview, scope and timings

- 3.1** This chapter provides an overview of our proposed rules and guidance, including a summary of the proposed scope and implementation timeline.

Overview of our proposed requirements

- 3.2** Building on responses to DP21/4 and our wider stakeholder engagement, including with the DLAG, we propose to introduce rules in the following areas:
- **Sustainable investment labels.** Classification and labelling of products to help consumers navigate a complex product landscape and give them confidence in the integrity of the sustainable investment products they are offered. Classifying products based on 'intentionality', the proposed regime distinguishes between three different types of sustainable product according to the primary channel by which each can plausibly contribute to positive sustainability outcomes. In particular, the regime distinguishes between products according to whether they aim to invest:
 - i. in assets that are environmentally and/or socially sustainable ('sustainable focus')
 - ii. to improve the environmental and/or social sustainability of assets over time, including in response to the stewardship influence of the firm ('sustainable improvers')
 - iii. in solutions to environmental or social problems, to achieve positive, real-world impact ('sustainable impact')

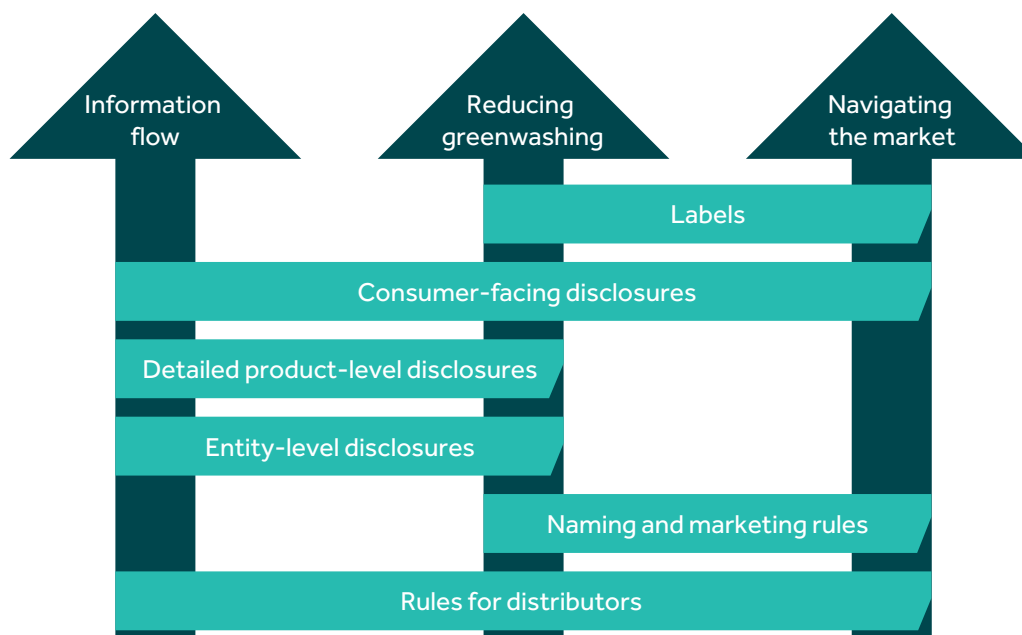
There is no hierarchy between the proposed categories: each type of product is designed to deliver a different profile of assets, and to meet different consumer preferences. The labels will be underpinned by a set of clear, objective criteria that set a high bar for quality and integrity. These criteria cover specification of an objective, investment policy and strategy, key performance indicators, firm-level attributes (resourcing and governance of ESG), and investor stewardship. Stewardship refers to 'the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society', as defined in the UK Stewardship Code 2020.

Firms will need to decide if they want to apply sustainable investment labels to their products, and assess whether the products meet our qualifying criteria. Any products that are not labelled must meet our naming and marketing rules set out below. While the labels are primarily aimed at helping consumers navigate the market and protecting them from greenwashing, firms may also choose to label products offered to institutional investors.

- **Consumer-facing product-level disclosures.** Consumer-friendly, accessible disclosures to help consumers understand the key sustainability-related features of an investment product. This includes its sustainability objective, investment approach, and performance against the objective. These must be produced for products with or without a sustainable investment label, although disclosures will inherently be more limited for products that do not have a label.
- **More detailed disclosures at product and entity level.** These additional, more granular disclosures are targeted at a broader range of stakeholders, including institutional investors or retail investors seeking more information:
 - Pre-contractual disclosures setting out the sustainability-related features of an investment product (eg its sustainability objective and investment policy and strategy). Sustainability-related information must be disclosed both for products which use a label and for products that do not use a label but which have sustainability-related features that are integral to their investment strategy (ie where the product has specific sustainability features and the firm has specific policies and procedures in place in relation to those features).
 - Ongoing sustainability-related performance information in a 'sustainability product-level report'. These disclosures must be produced for products that use a label.
 - Entity-level disclosures, in a 'sustainability entity report' on how firms are managing sustainability-related risks and opportunities. These disclosures must be made regardless of whether an in-scope firm uses a label.
- **Naming and marketing rules.** This includes a general 'anti-greenwashing' rule clarifying that sustainability-related claims must be clear, fair and not misleading. We are also proposing to restrict the use of sustainability-related terms in the naming and marketing of products offered to retail investors that do not use a sustainable investment label. This aims to ensure that product names and marketing align with, and are proportionate to, the product's sustainability-related objectives and strategy.
- **Requirements for distributors.** Requirements for distributors of in-scope investment products to retail investors in the UK to make the sustainable investment label and consumer-facing disclosures available to those investors.

3.3 **Figure 2** below sets out how our different proposals interact with each other to further our objectives of increasing transparency around sustainability-related information, supporting the flow of such information, protecting consumers from potential harm relating to greenwashing, and helping consumers navigate the market for sustainable investment products.

Figure 2 – Proposals and broad objectives



Overview of our proposed scope and implementation timelines

Scope

- 3.4** Our proposed general 'anti-greenwashing' rule will apply to all regulated firms (see Chapter 6).
- 3.5** The more targeted proposals in this CP – on labelling and classification, disclosure, naming and marketing and distribution – are directed at investment funds (primarily those marketed to retail investors in the UK) and the firms that manage or distribute those products. In this CP we use 'firms' to refer to asset managers of in-scope investment products and we refer to 'distributors' separately. Table 1 below sets out a summary of the scope, implementation timeline and relevant chapters setting out the proposals for each element of the regime.

Implementation timelines

- 3.6** Subject to feedback, we intend to finalise our rules and publish a PS by mid-2023. We propose to give firms sufficient time to prepare while balancing the need to address potential harm as early as possible. Our proposed implementation timeline recognises that some firms may find it more difficult to bring certain products (eg those already offered to retail investors) into compliance than others (eg new products). In summary, subject to the detail in Table 1 below, we propose that:
- the general anti-greenwashing requirement (ensuring that any references to the sustainability characteristics of a product are consistent with its sustainability profile and are clear, fair and not misleading) will become effective immediately on the publication of the PS (provisionally, from 30 June 2023)

- labelling, naming and marketing, consumer-facing and pre-contractual disclosure requirements – and rules for distributors – will become effective 12 months after publication of the PS (provisionally, from 30 June 2024)
- the first ongoing sustainability performance-related disclosures must be published 24 months after publication of the PS (provisionally, from 30 June 2025)
- entity-level disclosures in the sustainability entity report will have a staggered implementation, with the largest firms producing their first disclosures 24 months after publication of the PS (provisionally, from 30 June 2025)

Summary of scope and implementation timelines

3.7 Table 1 presents a summary of our proposed scope and implementation timelines for each part of the regime. This is a high-level summary and there may be some exceptions and further clarifications set out in the following chapters of the CP and draft Instrument at Appendix 1.

Table 1: Summary of scope and timelines

| Element of the regime | Firm | Product | Main location | Timelines | Chapter |
|---|--|---|---|---|--|
| Sustainable investment labels Labels can be used for products marketed to retail investors, and for those marketed to institutional investors, if the firm chooses to do so and meets our qualifying criteria. If not, firms marketing to retail investors must meet our naming and marketing rules | Firms carrying out portfolio management UK Undertakings for Collective Investment in Transferable Securities (UCITS) management company Investment company with variable capital (ICVC) that is a UCITS scheme without a separate management company Full-scope UK Alternative Investment Fund Manager (AIFM) Small authorised UK AIFM These are collectively referred to in this CP as 'in-scope firms' | Authorised funds (excluding feeder funds and funds in the process of winding up or termination) Unauthorised Alternative Investment Funds (AIFs), including investment trusts Portfolio management services can only use a label if 90% or more of the value of all constituent products in which they invest qualify for the same label These and the products in the row above are collectively referred to in this CP as 'in-scope products' | Relevant digital medium (website, mobile application) at which the product is offered | 12 months after the date of the PS (provisionally 30 June 2024) | CP – 4 Draft instrument – ESG 3.1 and 3.2 |
| | 18 months after the date of the PS (provisionally 30 December 2024) | | | | |

| Element of the regime | Firm | Product | Main location | Timelines | Chapter |
|------------------------------------|--|---|---|---|--------------------------------------|
| Consumer-facing disclosures | All in-scope firms marketing in-scope products to retail investors, regardless of whether they qualify for and choose to use a label, but excluding firms providing portfolio management services | All in-scope products, except portfolio management services | Relevant digital medium (website or mobile application) at which the product is offered | 12 months after the date of the PS (provisionally 30 June 2024) | CP – 5 Draft instrument – ESG 4.2 |
| | | Firms providing portfolio management services will not be required to produce consumer-facing disclosures, but will instead be required to provide an index of the underlying in-scope products, linking to their label and consumer-facing disclosure, as applicable | | 12 months after the date of the PS (provisionally 30 June 2024) | |
| Pre-contractual disclosures | All in-scope firms using a sustainable investment label, excluding firms providing portfolio management services Firms not using a label but where sustainability-related features are integral to the investment policy and strategy (excluding firms providing portfolio management services) | All in-scope products, excluding portfolio management services Firms providing portfolio management services will not be required to produce pre-contractual disclosures, but will instead be required to provide access to the pre-contractual disclosures for the underlying in-scope products (or under the 'on demand' regime below) | Fund prospectus Prior information document as required under FUND 3.2 Or otherwise Part A of the sustainability product report (including where the firm is only required to provide the contents of this report on-demand) | 12 months after the date of the PS (provisionally 30 June 2024) | CP – 5 Draft instrument – ESG 4.3 |

| Element of the regime | Firm | Product | Main location | Timelines | Chapter |
|---|---|---|---|--|--------------------------------------|
| Ongoing sustainability-related performance information | All in-scope firms using a sustainable investment label, except firms providing portfolio management services and UK AIFMs managing unauthorised AIFs not listed on a recognised exchange | All in-scope products, excluding portfolio management services and unauthorised AIFs not listed on a recognised exchange Firms providing portfolio management services will not be required to produce Part B of the sustainability product report but will instead be required to provide access to the relevant reports for the underlying in-scope products | Part B of the sustainability product report | 24 months after the date of the PS (provisionally 30 June 2025) | CP – 5 Draft instrument – ESG 4.5 |
| | Firms providing portfolio management services and Firms that are UK AIFMs managing unauthorised AIFs not listed on a recognised exchange using a label | Firms that are providing portfolio management services or are AIFMs managing unauthorised AIFs not listed on a recognised exchange will be required to provide information equivalent to the content of a Part A (pre-contractual disclosures) as applicable and Part B sustainability product report to clients on demand, where those clients require the information to meet their own legal obligations | 'On-demand' regime | 24 months after the date of the PS (provisionally, first requests from 1 July 2025) | CP – 5 Draft instrument – ESG 4.5 |
| Entity-level disclosures | All in-scope firms with assets under management (AUM) of £5 billion or more (on a 3-year rolling average) | Overall assets managed in relation to in-scope business | Sustainability entity report | Firms with £50 billion or more in AUM 24 months after the date of the PS (provisionally 30 June 2025) Firms with less than £50 billion but with £5 billion or more in AUM 36 months after the date of the PS (provisionally 30 June 2026) | CP – 5 Draft instrument – ESG 4.6 |

| Element of the regime | Firm | Product | Main location | Timelines | Chapter |
|-----------------------------------|---|---|--|---|--|
| Anti-greenwashing rule | All regulated firms | All firms' products and services | All marketing and communications | Immediately on publication of the PS (provisionally 30 June 2023) | CP – 6 Draft instrument – 3.3. (in particular ESG 3.3.1R) |
| Naming and marketing rules | All in-scope firms marketing in-scope products to retail investors, that do not use a label | All in-scope products | All in-scope product names, marketing and communications | 12 months after the date of the PS (provisionally 30 June 2024) | CP – 6 Draft instrument – 3.3 |
| | | Firms that are providing portfolio management arrangements will be exempt from the naming and marketing rules when 90% or more of the value of constituent products qualify for any label | | 18 months after the date of the PS (provisionally 30 December 2024) | |
| Distributors | Firms that are distributors of in-scope products to retail investors (including platforms and advisers) | All in-scope products distributed to retail investors | Relevant digital medium (eg website, mobile app) at which the product is offered | 12 months after the date of the PS (provisionally 30 June 2024) | CP – 7 Draft instrument – 3.1 |

3.8 As discussed in Chapter 1, overseas products are not included in scope of this CP. These are, however, an important part of the overall regime and we intend to follow with a further consultation on how proposals in this CP might be applied to those products. In Chapter 8 of this CP, we are also seeking views on how the regime could apply to other products, such as pension products. We intend to consult on proposals in due course.

3.9 Many of the proposals in this CP build on existing rules, and so we anticipate firms will already have systems and processes in place to implement them. We do, however, expect firms to incur costs in assessing and classifying their products against the criteria, labelling or renaming products and amending marketing materials as necessary, and putting systems, processes and resources in place to prepare additional disclosures. We discuss these costs in Annex 2 as well as the benefits.

Q1: Do you agree with the proposed scope of firms, products and distributors under our regime? If not, what alternative scope would you prefer, and why?

Q2: Do you agree with the proposed implementation timeline? If not, what alternative timeline would you prefer, and why?

Q3: Do you agree with the proposed cost-benefit analysis set out in Annex 2. If not, we welcome feedback in relation to the one-off and ongoing costs you expect to incur and the potential benefits you envisage.

4 Classification and labelling

Overview

- 4.1** Classification and labelling of sustainable investment products are fundamental components of our regime. Supported by our disclosure requirements, naming and marketing rules and rules for distributors, the labels are intended to help prevent greenwashing and allow consumers to navigate the market more easily.
- 4.2** In this chapter we introduce the conceptual inputs to our proposed classification and labelling regime, which emphasises the sustainability-related objectives that a product aims to achieve and the channels by which investors can help contribute to positive sustainability outcomes.
- 4.3** We summarise the key characteristics of our three proposed sustainable investment labels – 'sustainable focus', 'sustainable improvers' and 'sustainable impact' – and propose a set of qualifying criteria underpinning the labels. We also list the actions firms will need to take should they decide to use the labels.

Background and concepts

- 4.4** The fundamental aim of our classification and labelling regime is to:
- help consumers distinguish between products on the basis of their sustainability characteristics, themes and outcomes
 - help them distinguish between different types of sustainable investment product
- 4.5** In our view, one of the key attributes of a sustainable investment product is an explicit environmental and/or social objective ('sustainability objective'), that is part of the investment objectives (ie sitting alongside the product's financial return objective) and is expressed in specific and measurable terms.
- 4.6** A sustainability objective may target either:
- a particular sustainability profile for the product's assets, where it can be demonstrated that this profile has a plausible, purposeful and credible link to positive outcomes for the environment and/or society
 - directly positive outcomes for the environment and or society
- 4.7** Of course, the outcomes that any investment can achieve for the environment and/or society will reflect both:
- the **enterprise contribution** of underlying assets – ie the outcomes contributed by the issuer of the asset, independently of actions by the investor
 - the **investor's contribution** – ie the additional outcomes that can be attributed to the actions taken by the investor in respect of its assets

- 4.8** Both layers are critical. However, currently, relatively few firms attempt to describe a causal link between the firm's investment activities and the eventual positive real world sustainability outcomes of its products. More typically, firms emphasise the sustainability characteristics of the assets in which a product invests ie enterprise contribution.
- 4.9** To ensure proper accountability, we consider that the classification and labelling of sustainable investment products should emphasise the actions that the firm takes in the product's investment policy and strategy to contribute to positive outcomes for the environment and/or society. This would include the value that the firm adds through asset selection, portfolio construction and investor stewardship.
- 4.10** **Box 3** describes the various direct and indirect channels or mechanisms by which a firm may contribute to a positive sustainability outcome.

Box 3: Investor contribution mechanisms for positive sustainability outcomes

We consider that there are three main channels or mechanisms by which an investor may plausibly contribute to positive outcomes for the environment and/or society. These mechanisms are not mutually exclusive, and are often pursued together in a blended sustainable investment strategy.

In describing these channels, we have drawn on existing literature, such as a studies by Eugene F. Fama and Kenneth R. French: 'Disagreement, Tastes, and Asset Prices', and Paul Brest & Kelly Born: 'Unpacking the Impact in Impact Investing', and industry initiatives, including for example the Investor Contribution Strategies developed by the Impact Management Project:

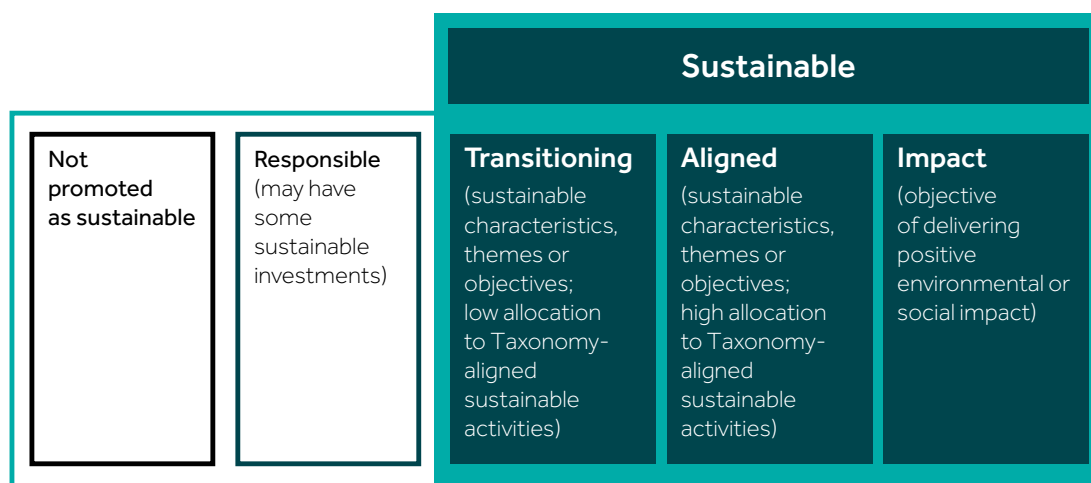
- 1. Active investor stewardship and engagement:** This channel involves asset managers' influencing the environmental or social performance of assets through active engagement, the exercise of voting and other rights, shareholder activism, or through participation in system-wide initiatives.
- 2. Influencing asset prices and the cost of capital:** The conceptual basis for this channel is that asset managers can influence asset prices and the cost of capital by 'screening in' assets that have strong sustainability credentials, and 'screening out' those that do not. If a sufficient weight of sustainability-focussed investors restricted their investments to assets that met certain sustainability characteristics, these assets would be rewarded by a lower relative cost of capital.
- 3. Seeking a positive sustainability impact by allocating capital to underserved markets or addressing market failures:** This channel involves investing in accordance with a stated theory of change, directing typically new capital to projects and activities that offer solutions to environmental or social problems, often in underserved markets, or to address observed market failures, with the explicit aim of achieving a positive, measurable sustainability impact. Under this channel an investor may allocate capital to underserved markets at non-concessionary prices, or may observe that a particular market is underserved precisely because it requires subsidy and therefore the pricing must be deliberately and explicitly concessionary.

- 4.11 Of course, identifying a 'plausible link' does not mean that any positive real-world outcome is certain. This underscores the importance of a classification and labelling approach based on 'intentionality', against which performance can be measured.
- 4.12 The potential magnitude of such outcomes will also depend on the particular facts and circumstances. For instance, the asset pricing/cost of capital mechanism may be stronger in less-liquid segments of the market. Further, robust methodologies to measure and attribute such outcomes are still being developed.

DP 21/4 feedback

- 4.13 In DP 21/4 we sought feedback on a classification and labelling system for investment products comprised of five labels, reflecting different sustainability characteristics and including a label for products not proactively making sustainability claims. The system was based around 'intentionality' – the investors' intention to achieve the product's objective. The labels are set out below.

Figure 3 – Product categories from DP 21/4



- 4.14 We asked for feedback on several aspects of the classification and labelling system, including fundamental issues such as the appropriate balance between principles and prescription in setting our criteria; interoperability with regimes in other jurisdictions; and whether the labels should apply only to products promoting themselves as sustainable, or to all investment products. We sought feedback on more granular issues relating to labels – such as the role of stewardship; key features of 'Impact' products; and interaction with the UK Green Taxonomy. And we also asked for views on more technical matters – such as how products tracking the Climate Transition and Paris-aligned benchmarks should be treated; and what stakeholders consider the roles of derivatives, short-selling and securities lending to be in sustainable investing.

We received detailed feedback, including:

Broad support for our direction of travel – Most respondents broadly welcomed our approach to classification and labelling. Respondents welcomed an objective (ie descriptive) approach to labelling rather than subjective comparisons (eg a traffic light system) that impose a value judgement as to whether the product is 'good' or 'bad', with some specifically warning against the latter.

Broad support for our design principles – Respondents also broadly supported the design principles set out in the DP, including structuring the regime around 'intentionality' and setting clear criteria. A small number called for the labels to be discrete and distinguishable from one another. While some suggested alternative approaches to labelling – such as a 'food label' style approach – most supported our approach.

Categories – Some respondents were concerned about the number of labels, which they considered could be too complex for consumers. Some also suggested that we simplify the label names and descriptions, to make them more accessible for consumers. Respondents also commented on the specific categories:

- Several – including asset managers, trade associations and banks – explicitly supported the '**Impact**' category and were largely comfortable with the high-level criteria referenced in the DP. Some respondents were divided over the potential inclusion of 'additionality' as a criterion (see **Box 4**), although most supported including a criterion on the measurability of impact.
- Respondents welcomed the '**Aligned**' category, although a small number felt that the framing of the category was too vague. Several also felt that the name of this category would be confusing to consumers.
- There was strong support for a '**Transitioning**' category. Respondents noted its importance in facilitating an economy-wide transition to a more sustainable future, but some felt that the term was more commonly associated with climate rather than sustainability more broadly. Some (including NGOs) argued for clear and measurable criteria underpinning the label.
- Of the respondents that commented on the '**Responsible**' category, a small majority were not supportive. Respondents questioned the description of this category – for example, noting that ESG integration and investor stewardship should not be enough to qualify a product as 'Responsible'. Some also argued that the name could be potentially misleading to consumers, and some noted the difficulty of delineating between certain 'responsible' and 'sustainable' investment strategies.
- While some respondents were in favour, a small number argued against including a '**Not Promoted as Sustainable**' category within the regime on the basis that this could unduly create a negative impression and disincentivise consumers from investing in these products (even if the products are not positioning themselves as being sustainable).

Box 4: Additionality

In DP21/4 we asked whether stakeholders agreed with our early views on the features of impact investing, which included additionality. This can be defined in terms of whether a proposed activity will produce some 'extra good' in the future relative to a specified baseline, typically the counter-factual in which the investment has not taken place.

Stakeholders generally fell into two groups: those who, broadly speaking, referenced the Global Impact Investing Network definition of impact investing (which does not include additionality) and those who considered financial additionality (as distinct from other forms of investor additionality) a necessary element of impact investing.

One respondent commented that additionality is important in distinguishing between impact products and the 'transitioning' category. Others argued that if impact was to be achieved through stewardship, additionality would be very challenging to evidence, especially when stewardship activities involved collaborative engagement.

Given the difficulties inherent in defining a baseline (or counter-factual) and measuring additionality, another respondent favoured a non-prescriptive approach in respect of both the consideration and evidencing of additionality.

4.15 Respondents also provided more granular feedback on other issues, for example:

- Respondents held mixed views on whether the regime should incorporate **entity-level** as well as product-level criteria for sustainable labels; the use of **ESG benchmarks** as a criterion (eg with some suggesting that they should be treated as any other product and others suggesting either a mapping to 'transitioning' or 'aligned' categories or a separate classification), and the roles of **securities lending, short-selling** and **derivatives** (see **Box 5**).
- Some respondents were concerned that the **UK Green Taxonomy** would be the primary tool to measure the 'sustainability' of investments and underpin the labels. They noted that this wouldn't be appropriate as the Taxonomy hasn't been developed, and that its scope, at least initially, will be limited to environmentally sustainable activities.

Box 5: Securities lending, short selling and derivatives strategies

Securities lending: We heard calls for the FCA to take a thoughtful, cautious approach that considers wider market implications. Looking at the intersection between securities lending and ESG, there seem to be four main areas of debate:

1. a concern that by engaging in securities lending an investor will be unable to exercise their voting rights and hence fulfil their stewardship objectives effectively
2. a concern that by lending an investor may facilitate the short selling of securities issued by companies that they consider have strong sustainability credentials

3. consideration of the identity of counterparties in back-to-back transactions given some lenders may not wish to enter into transactions with parties that do not share their values and standards
4. consideration of whether constraints on the sustainability profile of firms' investment portfolios should similarly be reflected in restrictions on the collateral they accept against securities loans.

Our response: Securities lending plays an important role in the market and provides investors with additional income. We do not consider securities lending as being incompatible with ESG as securities lending arrangements can be tailored to meet the ESG objectives of the lending and borrowing parties. So, we are not proposing any specific constraint to the ability of strategies that involve securities lending to qualify for one of the FCA sustainable investment labels. As part of our implementation guidance, we are proposing that, where applicable, a firm should clarify its securities-lending policy and the steps it takes to ensure this is coherent with its sustainable investment strategy.

Short-selling: A number of respondents noted the role that short-selling can play in contributing to positive sustainability outcomes, including by signalling a negative view of a company's sustainability risks or impacts and, with a sufficient weight of capital, increasing that company's cost of capital. This could incentivise behavioural and strategic changes. Other respondents focussed on the need for transparency around long and short positions and encouraged clarifications from regulators around disclosure methodologies.

Our response: At this stage, we do not propose to set specific parameters for the use of short-selling in the context of our sustainable investment labels. However, we propose guidance to clarify that, where relevant to its investment policy and strategy, a firm must explain how short selling aligns with or contributes to the sustainable investment product's stated sustainability objective.

Derivatives: We received mixed views on the use of derivatives in sustainable strategies and some respondents urged us to avoid making rules specifically relating to derivatives in the first instance, recommending instead that the FCA monitors developments in the market.

Our response: In line with feedback, we are proposing implementing guidance to increase transparency on the use of derivatives in sustainable investment products.

DLAG feedback

4.16 In addition to comments included in DP21/24 feedback above, the DLAG advised that:

- we consider introducing rules around the naming and marketing of products to complement and reinforce our labelling requirements (see Chapter 6)
- a classification approach on the lines of that set out in DP 21/4 would be preferable to other approaches, such as an approach akin to 'food labels'; in doing so, the DLAG strongly recommended that categories be mutually exclusive and not hierarchical

- the number of labels be reduced to avoid overloading or confusing consumers, and that the label names be as simple as possible
- the criteria underpinning the labels be clear and objective, and the distinction between all three categories must be clear
- stewardship should not be the sole defining feature of the Sustainable Improvers category, and carrying out stewardship should not alone be enough to qualify for the category
- some members proposed removing the 'Sustainable Improvers' category or alternative categorisation including a 'low', 'medium' and 'high' sustainability scale, or labels for 'sustainable focus: broad goal', 'sustainable focus: specific goal/theme' and 'impact'

Proposals

Label category descriptions and rationale

- 4.17** Consistent with the approach set out in DP21/4, we are proposing to introduce a classification and labelling regime to help consumers (ie retail investors) navigate the market for sustainable investment products.
- 4.18** Firms offering the investment products in our proposed scope (as set out in Chapter 3) will have the opportunity to use our sustainable investment labels if they choose to and if they meet our proposed qualifying criteria. Firms will also be required to make certain accompanying disclosures.
- 4.19** Where sustainability-related features are integral to an investment policy and strategy but the firm chooses not to use a label, or does not qualify to do so, they will need to ensure those features are communicated in a proportionate way to the sustainability profile of the product, in line with our naming and marketing rules in Chapter 6.
- 4.20** Building on the detailed feedback received, and the approach and contribution mechanisms set out earlier in this chapter, we propose to introduce three 'sustainable investment' labels. These aim to distinguish between products based on:
- **'intentionality'**, and in particular the sustainability objective it is seeking to achieve
 - the **primary channel and investor contribution mechanism** by which the product may plausibly achieve a positive outcome for environmental or social sustainability (see Box 3)
- 4.21** We recognise that many, if not most, products will generate outcomes via more than one of the channels described in Box 3. However, the qualifying criteria set out below are designed to ensure that the three categories in **Figure 4** are mutually exclusive.

Figure 4 – Sustainable investment labels



- 4.22** The three categories of sustainable investment label correspond broadly to those included under the 'sustainable' banner in DP 21/4. We do, however, agree with

feedback to simplify the regime and have done so by reducing the number of categories from five to three and removing the 'Responsible' and 'Not Promoted as Sustainable' categories.

4.23 We refined the descriptions of each category and sought to clarify how they are intended to function (see **Table 2**), based on the feedback received. We have also sought to simplify the label names to be more accessible to consumers, noting that these will be complemented by the consumer-facing disclosures. We tested the revised names with consumers (see Box 2) and found that revisions to the labels and disclosures helped to address the lack of understanding around previous versions.

Table 2: Proposed sustainable investment label descriptions and objectives

| Category Name | No sustainable label | Sustainable Focus | Sustainable Improvers | Sustainable Impact |
|------------------------------------|--|---|---|--|
| Description | Products that do not meet the criteria for a sustainable label | Products with an objective to maintain a high standard of sustainability in the profile of assets by investing to (i) meet a credible standard of environmental and/or social sustainability; or (ii) align with a specified environmental and/or social sustainability theme | Products with an objective to deliver measurable improvements in the sustainability profile of assets over time. These products are invested in assets that, while not currently environmentally or socially sustainable, are selected for their potential to become more environmentally and/or socially sustainable over time, including in response to the stewardship influence of the firm | Products with an explicit objective to achieve a positive, measurable contribution to sustainable outcomes. These are invested in assets that provide solutions to environmental or social problems, often in underserved markets or to address observed market failures |
| Consumer-facing description | | Invests mainly in assets that are sustainable for people and/or planet | Invests in assets that may not be sustainable now, with an aim to improve their sustainability for people and/or planet over time | Invests in solutions to problems affecting people or the planet to achieve real-world impact |

4.24 Note that products without a sustainability objective, but which may use strategies such as 'ESG integration', would not qualify for a sustainable investment label. As noted by respondents to DP 21/4, 'ESG integration' – that is, the consideration of ESG risks, opportunities and impacts that may be material to the future financial performance of the product's assets – is increasingly considered to be integral to a firm's acting in accordance with its fiduciary duty and risk management. ESG integration will often be central to investment strategies that pursue a financial return objective, but would not be regarded as a sustainable investment strategy in its own right.

4.25 Similarly, many products aim to meet consumers' needs and preferences by employing strategies such as 'exclusion/negative screening' or basic 'ESG tilts'. Where such strategies align with their objectives, it is important that consumers are able to identify, access and gather reliable information about these products. However, since such strategies, alone, would not plausibly contribute to positive sustainability outcomes,

it is also important that consumers can reliably distinguish them from genuinely sustainable investment products. They would therefore not qualify for a sustainable investment label. These approaches may, however, qualify for a sustainable investment label if combined with other strategies and if the full criteria were met – including that the product had a sustainability objective.

- 4.26** In the remainder of this section, we elaborate on the rationale for each product category. We have also considered the types of product that we might expect to see in each category, supported by selected examples of existing products that may meet some of the key criteria for each.
- 4.27** These existing products are described in anonymised form. We note that the examples provided are illustrative and in many cases would need to demonstrate that additional elements of the criteria have been met before being able to use a label. We elaborate in Box 9 some of the key areas that firms would need to consider in assessing whether existing products meet the qualifying criteria.

Sustainable focus ***Category description and rationale***

- 4.28** These products aim to invest in assets that a reasonable investor would regard as being environmentally and/or socially sustainable.
- 4.29** The key distinguishing features of this category of product are:
- **Sustainability objective.** Alongside its financial risk/return objective, a 'sustainable focus' product will have an objective to invest in assets that meet a credible standard of environmental and/or social sustainability, or that align with a specified environmental and/or social sustainability theme.
 - **Primary channel for sustainability outcomes.** This category of product would pursue its sustainability goals primarily via the market-led channel of influencing asset prices, and thereby reducing the relative cost of capital of sustainable economic activities/projects.
 - **Secondary channel for sustainability outcomes.** Products in this category will also typically pursue continuous improvements in the sustainability performance of assets through investor stewardship activities.
- 4.30** To meet consumers' expectations, the criteria for this category include that at least 70% of a 'sustainable focus' product's assets meet a credible standard of environmental and/or social sustainability, or align with a specified environmental and/or social sustainability theme. This means that it must be robust, independently assessed, evidence-based and transparent.
- 4.31** We note that a taxonomy – such as the UK Green Taxonomy, once developed – could be one way of demonstrating that assets meet a credible standard of sustainability. We are not, however, being prescriptive at this stage as to what the standard should be, provided that it meets the attributes set out above. These attributes should ensure there is greater transparency over how firms are determining 'sustainability' in relation to the products they offer, while recognising that this is an evolving space and that other standards may emerge. We will continue to monitor developments and assess how firms have implemented this criterion. We will consider updating our requirements over time as appropriate.

Box 6: Likely product profile and strategies

These products will typically be active and highly selective, applying extensive screens to allocate assets predominantly to investments that would reasonably be regarded as being environmentally or socially sustainable (or both), or supporting environmental or social sustainability (eg, by delivering sustainable solutions).

Some index-tracking strategies may meet the criteria, where they track selective benchmarks that reflect the objective standard for environmental or social sustainability specified in the fund objective.

This category of product will also meet the needs and preferences of those consumers who are seeking a highly 'screened' portfolio that invests predominantly in assets that display certain sustainability characteristics or are demonstrably aligned with a sustainability-related theme – and equally that avoids investments in assets that they do not associate with sustainability.

Examples

While these are examples of likely strategies that may meet the qualifying criteria, other aspects of the criteria set out below would need to be demonstrated; eg that at least 70% is invested in assets that meet a credible standard of environmental and/or social sustainability or meet a specified environmental and/or social theme.

Example 1:

Name: ABC Global Equity Educational Achievement Fund

Objective: To provide long-term capital growth and concentrate investments in companies with products and operations that are considered to be making a positive contribution to improving young people's educational achievement through technology and innovation while avoiding investment in companies with damaging or unsustainable business practices.

Investment Process: The product operates a three-step investment process. First, the investment team generates ideas, taking into consideration relevant long-term social themes. The team then excludes any companies with exposure to any business activities deemed to be socially or environmentally damaging, with particular tolerance thresholds. It then focuses on deploying capital to assets that are tightly aligned with its objective to invest in activities that foster, directly or indirectly, educational outcomes and support the goal of empowering all women and girls in line with Goal 5 of the UN Sustainable Development Goals (SDGs).

Example 2:

Name: ABC Sustainable Water and Waste Fund

Objective: The fund aims to achieve long-term capital growth from a portfolio primarily made up of equity securities issued by companies throughout the world and involved in the design, manufacture, or sale of products and services used for or in connection with the water and waste management sectors. The fund adopts a thematic strategy, under which a minimum of 70% of the fund's assets will be invested in securities of companies the economic activities of which are deemed to support the achievement of Goals 6 (Ensure access to water and

sanitation for all) and 14 (Conserve and sustainably use the oceans, seas and marine resources) of the UN Sustainable Development Goals.

Investment Process: The fund has a thematic approach which includes norm-based and negative screening of sectors, companies, practices based on specific industry as well as ESG criteria. The fund will consider a wide range of environmental characteristics, which include but are not limited to, water and waste management. The fund is actively managed, and seeks to promote these characteristics by adhering to the institution-wide sustainability framework, including frequent and targeted interaction with investee companies' boards and management teams.

Sustainable improvers ***Category description and rationale***

- 4.32** Products in this category aim to invest in assets that, while not objectively environmentally or socially sustainable at present, have the potential to deliver measurable improvements in their environmental and/or social sustainability over time, including in response to the stewardship influence of the firm.
- 4.33** We consider it critical that the proposed regime accommodates investment in assets in transition to becoming more sustainable. Products in the other two sustainable investment categories are likely to be highly selective and narrowly invested. Products in this category, by contrast, may be invested broadly across sectors, with the firm playing an important role in embedding and accelerating improvements in the sustainability profile of assets, including through its stewardship activities. Recognising such products as sustainable within the regime can support a whole-of-economy transition to a more sustainable future.
- 4.34** Given the broad scope of assets in which products in this category are likely to be invested, and the transitioning nature of their sustainability profiles, the proposed criteria for this category emphasise that the firm must disclose clearly where the product will and will not invest, and describe its asset selection and stewardship activities, including escalation triggers – and potential divestment – if its stewardship is not achieving the intended improvements.
- 4.35** Our proposed criteria also emphasise that a firm seeking to apply a sustainable improvers label to its product should also describe how it assesses the potential for the sustainability profile of assets to improve over time. A clear and measurable target for improvements in the sustainability profile of assets must also be reflected in Key Performance Indicators (KPIs), enabling a firm providing a sustainable improvers product to be held to account for performance over time. Once the outputs of the Government's Transition Plan Taskforce (TPT) have been finalised and implemented, metrics disclosed as part of transition plans could form part of the KPIs that firms use.
- 4.36** A clear and measurable target will also distinguish a sustainable improvers product from a traditional investment product that integrates ESG considerations in its investment process and stewardship activities solely to manage financial risk and maximise financial returns.

4.37 The key distinguishing features of this category of product are:

- **Sustainability objective.** Alongside its financial risk/return objective, a 'sustainable improvers' product will have an objective to deliver measurable improvements in the sustainability profile of its assets over time, including through investor stewardship.
- **Primary channel for sustainability outcomes.** This category of product would pursue its sustainability goals primarily via the channel of investor stewardship. The product's stewardship approach would be directed towards encouraging and accelerating improvements in the environmental or social sustainability profile of its assets, including through participation in system-wide initiatives, with flow-on positive implications for environmental and/or social sustainability.
- **Secondary channel for sustainability outcomes.** Portfolio construction and asset selection in 'sustainable improvers' products would be geared towards identifying those assets that are best-placed to improve their sustainability profile over time. So, a secondary channel would be the market-led channel of influencing asset prices and the relative cost of capital of more sustainable economic activities/projects.

Box 7: Likely product profile and strategies

These products will typically be invested across a broad range of sectors, with assets allocated according to objective criteria that emphasise their potential to become more environmentally or socially sustainable over time – including in response to active investor stewardship.

These criteria may include positive or negative screens that emphasise the relative sustainability characteristics of assets.

Some index-tracking strategies may meet the criteria, where they track tilted benchmarks that embed such criteria, and where the firm also engages proactively with the assets. In these cases, the firm must demonstrate that the index provider's methodology for index-construction aligns with the sustainable investment product's stated sustainability objective and its target environmental and/or social sustainability profile. Responsibility for ensuring that the index methodology reflects the stated sustainability objective and complies with all relevant requirements to qualify for a label rests with the firm, which needs to satisfy itself that this is the case on an ongoing basis.

Examples

While these are examples of likely strategies that may meet the qualifying criteria, other aspects of the criteria set out below would need to be demonstrated. For example, the objective would need to state an intention to improve the sustainability of the fund's assets over time.

Example 1:

Name: ABC Future World Global Equity Index Fund

Objective: The fund employs an index tracking strategy, aiming to provide broad and diversified exposure to developed and emerging equity markets with a view to significantly overweigh shares of companies that have clear decarbonisation

plans and a track-record of honouring their climate pledges and to ensure their management remain committed to highly ambitious climate targets relative to their peers.

Investment process: The fund has a best-in-class approach with a strong engagement and stewardship focus that leverages ABC's extensive outreach and collective engagement approach. The fund incorporates an institution-wide cross-cutting climate framework and a targeted engagement process. This commits the team running the fund to engage with companies to encourage them to adapt their business models and drive innovation in order to meet global climate change goals, and to divest from companies who fail to meet minimum standards. The team will prioritise engagement with larger companies with ESG scores that do not show meaningful improvement. These issuers are then more closely monitored and if there is no progress, divestment becomes a consideration according to the fund's escalation policy.

Example 2:

Name: ABC Emerging Markets Sustainable Finance Fund

Objective: To provide capital growth over the long-term (5-10 years) by investing at least 80% of the assets in financial institutions with significant exposure to emerging economies that have a strong commitment to and realistic prospects of meaningful improvements in their sustainability KPIs.

Investment Process: Following fundamental analysis, the investment team will select asset managers, banks and insurers that are particularly strong performers among peers on a variety of sustainability-related metrics. The fund manager will focus on engagement with companies, seeking to ensure their continued commitment to their sustainability strategies and pledges (eg, transition plans), influence positive change and support best practice eg through voting. The team will vote at all company meetings, in line with the firm's detailed proxy voting guidelines and will support collective engagement wherever feasible. Where companies fail to improve their performance to the standard required, they are monitored and if their performance improves, they may continue to be held. However, if not, action will be taken according to the fund's escalation policy.

Sustainable impact

Category description and rationale

- 4.38** These products aim to achieve a positive, measurable contribution to real world sustainability outcomes. While sustainable investment products in the other two categories would set objectives that target a particular sustainability profile for their assets, a firm seeking to use the sustainable impact label would commit to deliver and report on its (the investor's) contribution to a positive environmental and/or social sustainability outcome through financial as well as other types of investor additionality.
- 4.39** To achieve this, a sustainable impact product will invest in sustainability solutions to environmental and/or social problems, often in underserved markets or to address observed market failures. Products in this category would invest in line with a clearly articulated theory of change and show how they select assets that align with this – while also seeking to avoid unintended negative environmental or social impacts.

4.40 To evidence environmental or social outcomes in line with the product's stated objective, the manager of the product would be expected to apply industry standard approaches to performance measurement, reporting against rigorous, evidence-based KPIs that capture the investor contribution to positive sustainability outcomes.

4.41 To ensure the 'impact' label has meaning, we think it is important that a firm can stand behind any claims it makes regarding positive sustainability outcomes. A firm will typically be better able to demonstrate and measure the additionality of its contribution to real world outcomes if it is investing new capital – either via private or primary markets.

4.42 We expect continued innovation in vehicles that can support investment in sustainability solutions. For instance, we have seen examples of closed-ended exchange-traded products that could realistically qualify for this label if they wished to as well as plans to facilitate the launch of new products to fund voluntary carbon credits by the London Stock Exchange. We also note recent initiatives such as the Long-Term Asset Fund to provide a UK authorised open-ended fund structure that enables investment in long-term, illiquid assets.

4.43 The key distinguishing features of this category of product are therefore:

- **Sustainability objective.** Alongside its financial risk/return objective, a 'sustainable impact' product will have an objective to achieve a pre-defined, positive and measurable environmental and/or social impact.
- **Primary channel for sustainability outcomes.** This category of product would pursue its sustainability goals by directing typically new capital to projects and activities that offer solutions to environmental or social problems, often in underserved markets or to address observed market failures. Products would be expected to have a stated theory of change, and to pursue a highly selective asset selection strategy aligned with that theory of change.
- **Secondary channel for sustainability outcomes.** Driving continuous improvements in the sustainability performance of assets through investor stewardship activities would be a secondary channel.

Box 8: Likely product profile and strategies

These products will typically be highly selective, emphasising investment in assets that offer solutions to environmental or social problems and that align with a clearly specified theory of change.

The product provider will typically be highly engaged with the product's assets, directing such engagement towards embedding and accelerating progress towards real-world change.

Index-tracking strategies are unlikely to meet the criteria for this category of product.

Examples

While these are examples of likely strategies that may meet the qualifying criteria, other aspects of the criteria set out below would need to be demonstrated. For instance, among others, the firm would need to set out a clear theory of change for the product, as well as a robust methodology to demonstrate how its actions had impact, and an escalation plan should the real-world outcome no longer plausibly be achievable.

Example 1:

Name: ABC Investment Trust

Objective: The investment trust aims to have a positive environmental impact by investing in assets that support the transition to a low carbon, more efficient energy system and help the UK achieve Net Zero.

Investment process: The company invests across three thematic areas predominantly in the UK: energy storage and distribution, promoting efficient consumption and onsite generation, and distributed renewable energy generation. The investment thesis is underpinned by the idea that investments are needed which improve the efficiency of the whole UK energy system from generation to consumption. A key performance indicator is avoided emissions. While a considerable amount of additional capital has been observed entering the sector, the company considers that there remains a funding gap for new generation that needs to be closed if decarbonisation targets are to be achieved. As a consequence, the trust has modified its investment policy to allow for investments into developers and development stage assets to ensure that an investment in ABC Investment Trust can provide higher levels of additionality. The company has developed a rigorous impact measurement framework.

Example 2:

Name: ABC Clean Energy Impact Fund

Objective: To increase renewable energy use and access in emerging markets in Asia. Specifically, this investment will finance the construction of wind farms, which will increase access to and the share of renewable energy in Mongolia and reduce the country's carbon footprint.

Investment Process: The team identifies opportunities following an assessment of a country's policy framework, an investment's development impact and their role as financier. The team analyses potential risks and challenges and conducts thorough due diligence. It then categorises projects based on their potential impacts on environmental, social and human rights conditions. It meets regularly with the main stakeholders to properly assess, monitor and manage the investment's impacts. It also monitors performance of the investment and progress against its sustainability goals. In particular, it applies a proprietary scorecard to assess the non-financial performance of its investments, which takes into account a variety of factors. Environmental metrics tracked on this investment include the level of carbon emissions avoided and improvements in water management as well as pollutants' avoided emissions.

Q4: Do you agree with our characterisation of what constitutes a sustainable investment, and our description of the channels by which positive sustainability outcomes may be pursued? If not, what alternatives do you suggest and why?

- Q5:** Do you agree with the proposed approach to the labelling and classification of sustainable investment products, in particular the emphasis on intentionality? If not, what alternatives do you suggest and why?
- Q6:** Do you agree with the proposed distinguishing features, and likely product profiles and strategies, for each category? If not, what alternatives do you suggest and why? In particular, we welcome your views on:
- a.** Sustainable Focus: whether at least 70% of a 'sustainable focus' product's assets must meet a credible standard of environmental and/or social sustainability, or align with a specified environmental and/or social sustainability theme?
 - b.** Sustainable Improvers: the extent to which investor stewardship should be a key feature; and whether you consider the distinction between Sustainable Improvers and Sustainable Impact to be sufficiently clear?
 - c.** Sustainable Impact: whether 'impact' is the right term for this category or whether should we consider others such as 'solutions'; and the extent to which financial additionality should be a key feature?
- Q7:** Do you agree with our proposal to only introduce labels for sustainable investment products (ie, to not require a label for 'non-sustainable' investment products)? If not, what alternative do you suggest and why?

Proposed qualifying criteria for a sustainable investment label

- 4.44** Clear, objective criteria for sustainable investment labels are essential to upholding the integrity of the regime and building trust in sustainability investment products.
- 4.45** To set an appropriate quality standard for products to qualify for any one of the three sustainable investment labels, we have developed a set of threshold criteria that all firms must meet, as well as some implementation guidance. The criteria are objective, rigorous and aim to 'raise the bar'. At the same time, they provide flexibility to accommodate different sustainability objectives for continued evolution and innovation in the market within clear guardrails.
- 4.46** In developing these criteria, we have sought to build from and remain consistent with existing relevant expectations and requirements. These include those set out in the Guiding Principles, and the UK Stewardship Code 2020, published by the FRC.

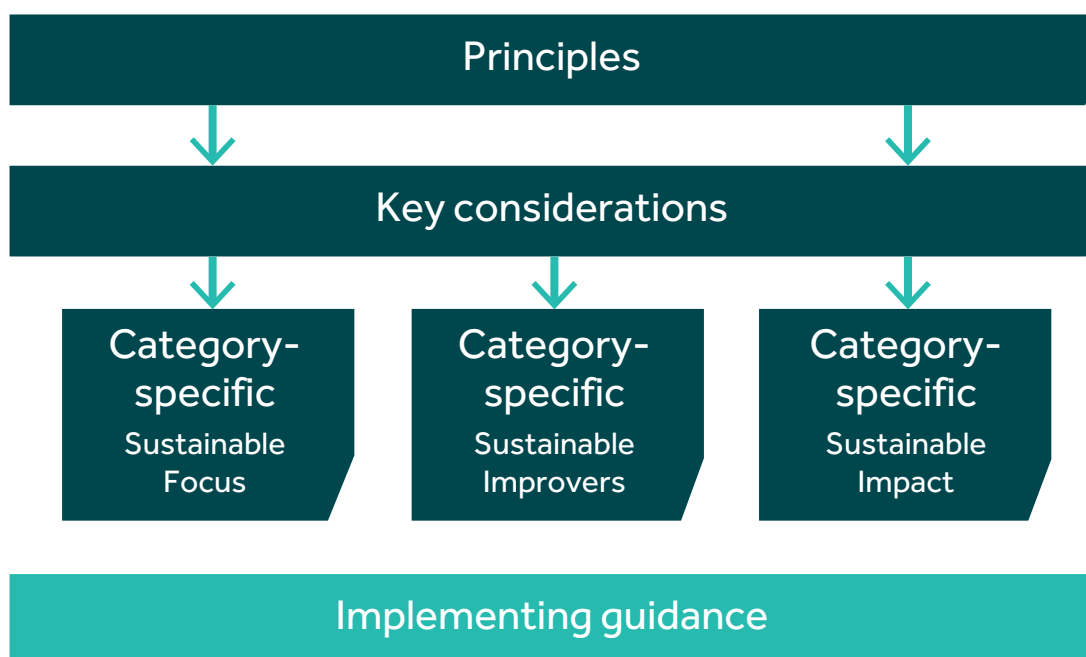
4.47 We propose that products qualifying for a sustainable investment label must meet:

- five overarching principles (referred to in the draft Instrument in Appendix 1 as 'general criteria'), covering (1) sustainability objective; (2) investment policy and strategy; (3) KPIs; (4) resources and governance; and (5) investor stewardship
- a number of key ('cross-cutting') considerations associated with each of the overarching principles. The requirements that cover what firms must 'do' are set out in this chapter, and requirements covering what firms must 'disclose' are set out in Chapter 5
- certain category-specific key considerations relevant to their particular label

4.48 As noted above, the three categories of labels are intended to be mutually exclusive. Products with a blended strategy could not qualify for more than one label according to our criteria, as the firm would be expected to set a clear objective that, together with the criteria that follow, determine which label is appropriate for the product.

4.49 The different elements of our criteria, including implementing guidance, are set out in **Figure 5** below.

Figure 5 – Criteria and implementing guidance



4.50 We set out below the overarching principles and associated key considerations covering **what firms must do** and the **sustainability-related features of the investment product**.

4.51 In Chapter 5 we set out the **disclosures associated** with the key considerations and where those disclosures must be made.

4.52 We have also developed some guidance to help firms implement the criteria. We are proposing to introduce this as non-Handbook guidance, as set out in Appendix 2. The criteria and associated disclosures are included in the draft instrument in Appendix 1.

- 4.53** The criteria for each label must be met in full and continue to be met on an ongoing basis in order to use that label.
- 4.54** To meet our first Principle, the firm must ensure that the product has an explicit environmental and/or social sustainability objective set out as part of its investment objectives. We consider such an objective to be a fundamental attribute of a sustainable investment product. While a product may have sustainability features that relate to environmental, social or governance factors, our criteria specify that a sustainability objective should specify either environmental or social themes, characteristics or outcomes. This is because we consider 'governance' to be an enabler of environmental or social outcomes, rather than an end in itself.
- 4.55** We are proposing that the sustainability objective must be expressed in specific and measurable terms, with a plausible, purposeful and credible link to positive outcomes for the environment and/or society. Firms may refer to Sustainability Accounting Standards Board (SASB) standards to help determine topics that a retail investor would reasonably associate with environmental and social sustainability.

Principle 1, Sustainability Objective. A sustainable investment product must have an explicit environmental and/or social sustainability objective.

Key considerations (cross-cutting)

1. A firm must determine the product's sustainability objective in clear, specific and measurable terms as part of its investment objectives.
2. A firm must ensure the product's sustainability objective has a plausible, purposeful, and credible link to an environmental and/or social outcome.
3. A firm must have adequate processes in place to
 - monitor the product's performance against its sustainability objective; and
 - provide ongoing performance reporting to investors (ie clients and consumers)

Category-specific criteria

| Sustainable Focus | Sustainable Improvers | Sustainable Impact |
|---|---|--|
| <p>The sustainability objective must align with requirements in the 'investment policy and strategy' section below ie to invest predominantly (at least 70%) in assets that meet a credible standard* for environmental and/or social sustainability; or that align with a specified environmental and/or social sustainability theme.</p> <p>*A credible standard is one that is robust, independently assessed, evidence-based and transparent.</p> | <p>The sustainability objective must align with requirements in the 'investment policy and strategy' section below ie to invest in assets that have the potential to become more environmentally and/or socially sustainable over time, including in response to active investor stewardship.</p> | <p>The sustainability objective must be to achieve a pre-defined, positive, measurable real-world environmental and/or social outcome.</p> |

See **Chapter 5** (pre-contractual disclosures) for the disclosures relating to Principle 1 and **Appendix 2** for the implementing guidance.

- 4.56** To meet our second Principle, the firm must also have an investment policy and strategy for the product aligned with its sustainability objective.

Principle 2, Investment Policy and Strategy. A firm's investment policy and strategy for the sustainable investment product must be aligned with its sustainability objective.

Key considerations (cross-cutting)

- 1.** A firm must develop and implement an investment policy and strategy aligned with the product's sustainability objective.
- 2.** A firm must ensure that the product is invested in accordance with its investment policy and strategy on an ongoing basis.
- 3.** A firm must determine its investible universe and the asset-level selection criteria it applies to meet a target environmental and/or social sustainability profile of assets, in specific and measurable terms, including
 - how the firm assesses the product's assets against the criteria
 - how the criteria relate to the target environmental and/or social profile of assets
 - how the target environmental and/or social profile of assets aligns with the product's sustainability objective
 - the conditions under which an asset ceases to meet its specified criteria for asset selection
- 4.** In the case of an index-tracking product, a firm must satisfy itself that the index provider's methodology for index-construction aligns with the product's sustainability objective and its target environmental and/or social sustainability profile. The firm must retain the responsibility for ensuring that the index methodology reflects the product's sustainability objective and complies with all relevant requirements to use a label on an ongoing basis.
- 5.** A firm must have appropriately designed policies and procedures in place to determine, measure, monitor, evaluate and report to investors (ie clients and consumers) on the environmental and/or social sustainability profile of assets on an ongoing basis.
- 6.** A firm must identify any investment made by a product that a reasonable investor (ie client or consumer) might consider to be in conflict with the sustainability objective, and the investment policy and strategy of the product.

See **Chapter 5** (pre-contractual disclosures and sustainability product report) for the disclosures relating to Principle 2 and **Appendix 2** for the implementing guidance.

Category-specific criteria

| Sustainable Focus | Sustainable Improvers | Sustainable Impact |
|--|--|--|
| <p>The firm must ensure that at least 70% of the product's assets either meet a credible standard of environmental and/or social sustainability; or align with a specified environmental and/or social sustainability theme.</p> <p>If reasons for beyond the firms' control, the assets cease to meet the requirements above, the firm must take action to restore compliance as soon as reasonably practicable, having regard to the interests of the firm's investors (ie clients and consumers).</p> | <p>The firm must ensure that the product is invested in assets that have the potential to become more environmentally and/or socially sustainable over time, including in response to active investor stewardship.</p> | <p>The firm must specify:</p> <ul style="list-style-type: none"> • a theory of change, in line with the product's sustainability objective, emphasising how its investment process aims to contribute to addressing either environmental and/or social problems • a robust method to measure and demonstrate that its investment activities have had a positive environmental and/or social sustainability impact • its escalation plan should the real-world outcome no longer plausibly be achievable, including potential divestment of assets |

See **Chapter 5** (pre-contractual disclosures and sustainability product report) for the disclosures relating to Principle 2 and **Appendix 2** for the implementing guidance.

- 4.57** To meet our third Principle, the firm must set credible, rigorous and evidence-based KPIs aligned with the sustainable investment product's sustainability objective, and monitor these on an ongoing basis. For the Sustainable Improvers category in particular we are proposing several criteria aimed at enabling firms to demonstrate how they are improving the environmental and/or social sustainability of the product over time. This will allow investors and other stakeholders to assess the product's ongoing performance against its sustainability objective.
- 4.58** As the corporate reporting standards in development by the ISSB are built out and implemented over time, disclosures under the metrics and targets pillar of the standards will be expected to inform the KPIs specified for sustainable investment products.
- 4.59** The International Capital Market Association's (ICMA) registry of illustrative KPIs could also be a useful reference, since it includes high-level recommendations and examples for the selection of KPIs. These KPIs have been devised for Sustainability-Linked Bonds but may also help to inform credible KPIs for investment products. ICMA also provides useful benchmarks for setting ambitions and benchmarks to measure progress.
- 4.60** The Climate Financial Risk Forum (CFRF) has also published industry guides that may provide useful references, including the Session 2 guide on Climate Data and Metrics. Further outputs on disclosures and metrics are expected to be published in due course.

Principle 3, Key Performance Indicators. A firm must specify credible, rigorous and evidence-based KPIs that measure a sustainable investment product’s ongoing performance towards achieving its sustainability objective.

Key considerations (cross-cutting)

1. A firm must have in place KPIs that are relevant to and aligned with the product’s sustainability objective.
2. A firm must monitor the product’s performance against its sustainability objective on an ongoing basis, with reference to its specified KPIs.

Category-specific criteria

| Sustainable Focus | Sustainable Improvers | Sustainable Impact |
|---|--|---|
| <p>In specifying KPIs to assess performance of the product, a firm must ensure that those KPIs include metrics that demonstrate the ongoing alignment of the product’s assets with a target environmental and/or social sustainability profile, and the product’s ongoing adherence to asset-level sustainability features in accordance with its investment policy and strategy.</p> | <p>In specifying KPIs to assess performance of the product, a firm must ensure that those KPIs include metrics that demonstrate:</p> <ul style="list-style-type: none"> • a clear and measurable target for improvements in the sustainability profile of the assets in which the product invests • the long-term sustainability profile of a product’s assets, as projected over a period of more than one year • the extent to which improvements in the sustainability of a product’s assets have been achieved over time, including through investor stewardship • how the firm’s stewardship strategy has been applied to support improvements in the environmental and/or social sustainability of assets, in accordance with the sustainability objective • the stewardship activities undertaken in relation to improving the sustainability profile of the product’s assets in accordance with its sustainability objective; the outcomes achieved (including any improvements in the sustainability profile of the product’s assets over time); and matters escalated (in accordance with the expectations under Principle 5, Stewardship, below) • how the product’s assets meet the asset-level selection criteria • the changes (if any) in the sustainability profile of the product’s assets over time, distinguishing between any improvement or deterioration in the sustainability profile of individual assets and changes arising from asset rotation | <p>In specifying KPIs to assess performance of the product, a firm must apply enhanced impact measurement and reporting based on industry best practices.</p> |

See **Chapter 5** (sustainability product report) for the disclosures relating to Principle 3 and **Appendix 2** for the implementing guidance.

4.61 To meet our fourth Principle, the firm must ensure that appropriate resourcing, governance and organisational arrangements are in place to support delivery in line with the product's sustainability objective.

4.62 The Key Considerations under Principle 4 are designed to ensure that a firm is able to stand behind its sustainability-related claims – for instance in the skills, experience, data and analytical tools it brings to the management of the product, and oversight by a governing body, where appropriate. As with Principle 2, this Principle will help support effective delivery of the product's sustainability objective.

Principle 4, Resources and Governance. A firm must apply and maintain appropriate resources, governance and organisational arrangements commensurate with the delivery of the sustainable investment product's sustainability objective.

Key considerations (cross-cutting)

- 1.** A firm must apply and maintain the following resources as appropriate for supporting and achieving the product's sustainability objective and the delivery of its investment policy and strategy:
 - investment professionals with appropriate skills and experience
 - technological inputs and research
 - data and analytical tools
 - where appropriate, oversight by any governing body in relation to the product; and
 - other resources as appropriate
- 2.** A firm must carry out due diligence on any data, research and analytical resources it relies upon (including when third-party ESG data service providers are used), ensuring that any gaps and shortcomings identified are documented and appropriately mitigated.
- 3.** A firm must maintain the arrangements and resources it has in place to oversee the sustainability research, data and analytical tools that it uses and ensure that these remain fit for purpose in supporting the product's sustainability objective on an ongoing basis.
- 4.** A firm must maintain governance and organisational arrangements that appropriately support and incentivise the high-quality delivery of its investment policy and strategy in line with the product's sustainability objective.

See **Chapter 5** (sustainability entity report) for the disclosures relating to Principle 4 and **Appendix 2** for the implementing guidance.

4.63 To meet our fifth Principle, the firm must ensure that its entity or product-level approach to stewardship is aligned with effective delivery of the product's sustainability objective. As set out in **Box 3**, we have identified active investor stewardship and engagement as an investor contribution mechanism for positive sustainability outcomes. The criteria below include reference to the FRC's Stewardship Code, consistent with requirements in COBS 2.2.3.

Principle 5, Stewardship. A firm must maintain its active investor stewardship strategy and resources (at firm-level or product-level) in a manner consistent with the sustainable investment product's sustainability objective.

Key considerations (cross-cutting)

1. A firm must apply its stewardship strategy and resources appropriate for achieving the product's sustainability objective.
2. Where stewardship plays a significant role in its investment policy and strategy for a sustainable investment product, the firm must specify credible, rigorous and evidence-based KPIs that relate to the contribution of stewardship activities and outcomes to the achievement of the product's sustainability objective [see also Principle 3, KPIs].
3. A firm must monitor its stewardship performance against any KPIs that are relevant to the delivery of the product in line with its sustainability objective.

See **Chapter 5** (pre-contractual disclosures and sustainability product report) for the disclosures relating to Principle 5 and **Appendix 2** for the implementing guidance.

Q8: Do you agree with our proposed qualifying criteria? If not, what alternatives do you suggest and why? In your response, please consider:

- whether the criteria strike the right balance between principles and prescription
- the different components to the criteria (including the implementing guidance in Appendix 2)
- whether they sufficiently delineate the different label categories, and;
- whether terms such as 'assets' are understood in this context?

Q9: Do you agree with the category-specific criteria for:

- The 'Sustainable focus' category, including the 70% threshold?
- The 'Sustainable improvers' category? Is the role of the firm in promoting positive change appropriately reflected in the criteria?
- The 'Sustainable impact' category, including expectations around the measurement of the product's environmental or social impact?

Please consider whether there any other important aspects that we should consider adding.

International coherence

- 4.64** We have committed publicly – in our ESG Strategy – to implementing rules that are coherent with international frameworks and standards as far possible. In developing our proposals, we recognise that the firms we regulate operate in global markets and are already subject to the EU SFDR, and will in future be subject to ESG disclosure rules proposed by the SEC. So, we are working to maintain coherence between our proposals, the SFDR requirements and the SEC's proposals. We will also consider regulations that develop in other markets as they become important for the UK market. However, our proposals must be appropriate for the UK market.
- 4.65** In Annex 1, we have provided a guide to help firms map product classifications in SFDR and the SEC's proposals to our own proposed classification and labelling regime. We have also incorporated some specific elements and language from the categories under those to regimes, as appropriate.
- 4.66** However, while our regime is compatible with those in the EU and the US, our starting point is different. As a result, there are differences in our approach. Our policy rationale for categorising products is to help consumers identify sustainable investment products and navigate the market. So, our criteria are designed to set a high bar for products that make sustainability claims, which is important to help clamp down on greenwashing against a backdrop of trust concerns. The starting point in the EU and US regimes, by contrast, has been to categorise products principally to determine disclosure requirements.
- 4.67** We will continue to engage closely with other securities regulators, both bilaterally and through IOSCO, to promote internationally coherent solutions wherever possible.

Implementation and operationalisation of product classification and labelling

- 4.68** In deciding whether to apply our sustainable labels to their products, in-scope firms will need to ensure that our criteria have been met in full (ie the overarching principles, key considerations and category-specific criteria) and make the associated disclosures. If firms do not meet the qualifying criteria for any of the sustainable label categories, our proposed rules prevent them from using a sustainable label for their in-scope products.
- 4.69** With respect to a portfolio management agreement or arrangement, 90% of the total value of the products in which it invests must meet the qualifying criteria for the same label in order for it to use the label. The firm must then make the disclosures for each of the underlying products available to consumers.
- 4.70** Firms that meet the criteria for their investment products and seek to use the label, must:
- use the relevant graphic when displaying the label; we will seek to trademark and set out the relevant graphics on our website once our rules are final
 - display the corresponding label prominently on the relevant digital medium at which the product is offered (ie main product webpage, page on a mobile application)
 - provide details as to where the associated consumer-facing disclosure can be found eg by adding a hyperlink on the relevant digital medium

- include the label in the consumer-facing disclosures, pre-contractual disclosures and sustainability product report
- notify the FCA that they are using the label within a month (we intend to provide a dedicated mailbox for this when finalising our rules)

4.71 We will seek to trademark the labels once finalised. We will also produce a dedicated webpage setting out further information on the labels, to which firms may also choose to hyperlink from the relevant digital medium.

4.72 We propose that firms must not use the sustainable investment label in a way that is misleading, or either claim or imply that the FCA has conferred or approved its use of the label, or that the use of the label means the product has been approved or endorsed by the FCA. Further, firms must not publish information in relation to the use of, or descriptors relating to, a label that contradicts information published by us.

4.73 If a firm chooses to use a label, we propose that it keeps a record as to the basis on which the label is being used, for as long as the label is being used (including updating it in line with any changes). We will expect firms to provide such a record to us should we request it.

4.74 We also propose that firms must review the categorisation and use of products with a sustainable investment label at least annually, as well prior to any proposed changes to a labelled product, and revise the use of a label as appropriate. Firms must retain a record of the review and decision as to whether the label remains appropriate.

4.75 Where a firm decides to change a product's categorisation and label (including if it decides to stop using a label), it must notify the retail investors and institutional clients invested in the product in writing as to the change and reasons for the change, publish the revised label and ensure relevant disclosures are updated. This must happen at least sixty days before the change comes into effect.

4.76 We also remind firms of obligations in COLL 4.3 as we expect a change to the use of a label to constitute at least a 'significant change' under the requirements.

4.77 In DP 21/4 we asked for feedback on whether firms should be required to seek independent verification on the categorisation of sustainable investment products before displaying the labels publicly. We received mixed feedback on this. Some respondents felt that mandatory verification could increase consumer trust in the labels and be key to the credibility of the regime. However, others noted that the requirement would significantly increase the costs and burden on firms, potentially disadvantaging smaller firms.

4.78 They also raised concerns over which types of firms would be best placed to perform this function (eg, data providers, rating agencies, or professional bodies). Some respondents also felt that independent verification shouldn't be needed if the labelling regime is underpinned by robust criteria.

4.79 After careful consideration of the feedback received, we have decided not to introduce a mandatory requirement for firms to seek independent verification of their labelling at this stage. However, we note that some firms may wish to seek verification and we encourage them to do so if they consider this would be helpful to their clients and consumers.

4.80 As set out in **Box 9** below, we have identified several areas where existing investment products with sustainability-related features do not currently meet our criteria, such as investment policy and strategy, KPI reporting and disclosures around governance and resourcing. It may be instructive for firms to consider these aspects in particular when preparing to use our labels.

Box 9: Mapping of existing funds to proposed qualifying criteria

We carried out a mapping exercise on a sample of existing funds with sustainability-related features to assess the extent to which they would meet our proposed qualifying criteria and where we anticipate most work may need to be done to meet our requirements.

Principle 1: Sustainability Objective

A number of funds had sustainability objectives although to meet our qualifying criteria, the objectives will need to be more specific and measurable. Firms will need to set out the sustainability-related outcomes the fund is seeking to achieve.

Principle 2: Investment Policy and Strategy

Disclosures on existing funds often included the target asset-level sustainability-related features in relation to the stated sustainability objectives. In some cases, this included information on how alignment of investment strategy with sustainability objectives was being measured. However, disclosures often fell short of this.

Principle 3: Key Performance Indicators

Few firms disclosed KPIs relating to the sustainability objectives (or other stated outcomes) of their products. However, the most common sustainability-related metrics disclosed were carbon footprint, board diversity, and other metrics relating to investments held over time.

Principle 4: Governance and Resourcing

There was little evidence of firms meeting the qualifying criteria for this principle. Some disclosures included the nature of expertise within the firm's sustainability research division, or a description of measures in place to ensure independence of sustainability teams within the wider company.

Principle 5: Stewardship

Some firms provided disclosures on their stewardship activity. For the funds likely to qualify for a 'Sustainable Focus' label, some disclosures contained sufficient information to meet the criteria. However, funds likely to fall under the 'Sustainable Improvers' category will need to monitor and disclose the impact of their stewardship on the profile of fund assets, which is rarely disclosed at present.

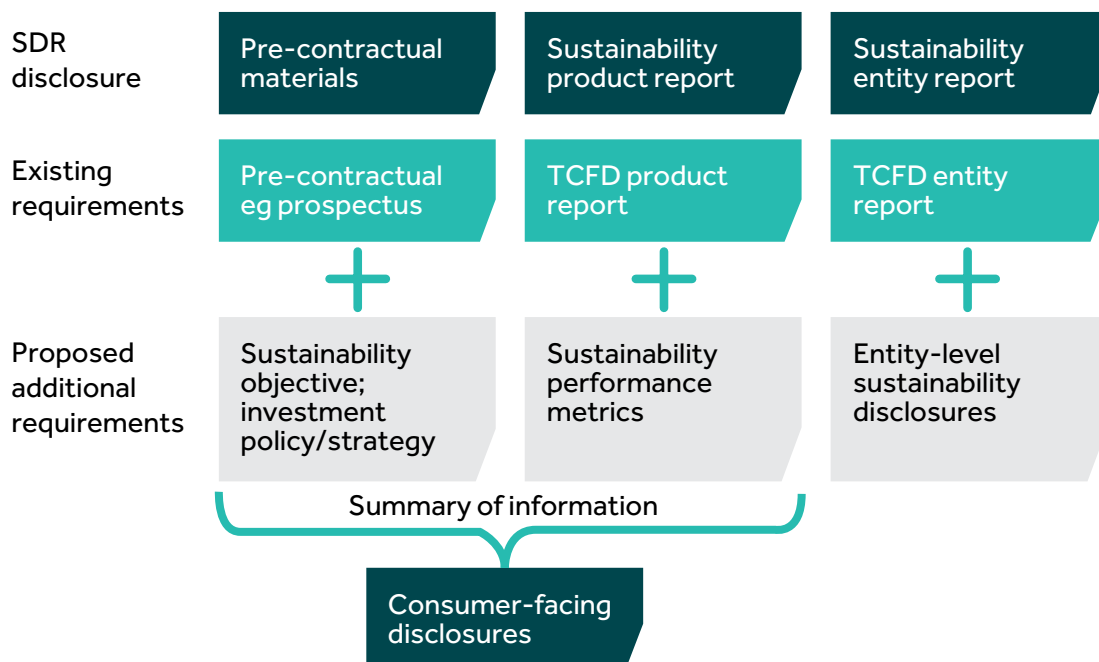
Q10: Does our approach to firm requirements around categorisation and displaying labels, including not requiring independent verification at this stage, seem appropriate? If not, what alternative do you suggest and why?

5 Disclosures

Overview

- 5.1** As set out in the Government’s Roadmap to Sustainable Investing, SDR will be introduced across the economy, building on the economy-wide climate-related disclosure requirements. This CP sets out proposals for disclosures by asset managers initially, with a view to extend them to certain FCA-regulated asset owners. Our proposals focus on delivering information on the sustainability-related features of investment products to retail investors in an accessible way, and providing more detailed information to those that want to know more.
- 5.2** The disclosure requirements set out in this CP are a starting point and we intend to develop our rules and guidance over time. For example, we propose to add more specificity to both product- and entity-level disclosure requirements as the ISSB develops its sustainability disclosure standards. In the meantime, since the Value Reporting Foundation completed its consolidation into the IFRS Foundation on 1 August, we encourage firms to consider the SASB metrics when making sustainability-related disclosures.
- 5.3** This chapter outlines the feedback to DP21/4 on disclosures and sets out our proposals to introduce consumer-facing disclosures, more detailed product-level disclosures in pre-contractual materials and a ‘sustainability product report’, and entity level disclosures in a ‘sustainability entity report’ (see **Figure 6**). Many of the disclosures relate to the qualifying criteria (in Chapter 4). The sustainability product and entity reports build from the TCFD product and entity reports (see PS21/24 paragraph 3.2).

Figure 6 – Overview of how SDR disclosures build from existing requirements



DP 21/4 feedback

5.4 We set out our early thinking on how the disclosures would form an integral part of the regime in DP21/4. We sought views on a tiered approach to disclosures while aiming to avoid duplication and costs, ensure clients and consumers receive consistent and coherent information, and take account of sustainability disclosure initiatives in other jurisdictions:

- consumer-facing disclosures: a subset of more detailed product-level information providing the most salient sustainability-related information to consumers in an accessible way
- detailed product-level disclosures: additional information eg on data, methodologies, limitations
- detailed entity-level disclosures: information on how the firm is managing sustainability risks and opportunities, building from our TCFD-aligned climate-related disclosure requirements to cover sustainability matters more broadly

5.5 Overall, we received strong support for our approach and both the structure and content of the three disclosure types.

Consumer-facing disclosures

5.6 Respondents welcomed this layer of disclosure, recognising the importance of making sustainability-related information accessible to a retail audience. They agreed that these disclosures should be kept simple and avoid jargon/technical language, and should avoid overloading consumers with information.

5.7 Comments on the content and format of the disclosures included that metrics be limited to those that are intuitive and likely to be decision-useful to consumers, and that taxonomy-related disclosures would be both challenging for firms to produce and for readers to interpret.

5.8 There were mixed views on the location of these disclosures. While some respondents were in favour of a dedicated 'ESG factsheet', others favoured incorporating disclosures into existing disclosure requirements. A small number recommended considering how sustainability-related information would be presented alongside financial information, noting that consumers need both.

5.9 Respondents also had mixed views on the level of prescription and standardisation. Several were in favour of specifying a template to standardise the required information, or at least to prescribe some elements to encourage consistency in disclosures. Others favoured more flexibility.

5.10 Other feedback included support for further consumer testing, and a small number of respondents encouraged some form of consumer education. Some also highlighted the need to remain consistent with the review of the UK retail disclosure regime, and to consider digital channels for accessibility.

5.11 We carried out more consumer research since the publication of our discussion paper and summarise the findings in Chapter 2, with the full results presented in the Occasional Paper published alongside this CP.

Detailed product-level disclosures

- 5.12** Respondents were supportive of aligning SDR requirements with existing TCFD-aligned product-level disclosure rules as well as SFDR, to the extent possible. Some noted that the disclosure of principal adverse impacts, as required under SFDR, would be neither decision-useful nor proportionate at product level. Respondents also encouraged us to leverage other initiatives across the investment chain when developing our requirements. These included the Guiding Principles set out in our [Dear Chair letter](#), forthcoming ISSB standards and UK Green Taxonomy disclosures.
- 5.13** Respondents generally agreed with the content of product-level disclosures (including data source, methodologies, etc). However, some recommended a flexible approach to disclosing metrics, noting in particular that social metrics are relatively underdeveloped. More generally, we were encouraged to phase-in the requirements and/or evolve them over time.

Detailed entity-level disclosures

- 5.14** Respondents were strongly supportive of building from our TCFD-aligned disclosure requirements at entity level, including the flexibility to cross refer to disclosures made in group or other relevant reports. However, a small number highlighted challenges such as applying scenario analysis to sustainability-related disclosures, or suggested that we follow SFDR without materially adding new requirements.
- 5.15** Some were also concerned about timing, noting that sustainability-related disclosure requirements would follow TCFD-aligned disclosure requirements too closely and emphasising the need for appropriate sequencing with requirements for corporates.
- 5.16** Many respondents echoed concerns regarding data availability and methodological challenges, as reflected in PS21/24. In particular, they were concerned that in some cases – particularly for asset classes such as asset-backed securities and currencies – data gaps and methodological challenges are so severe that using proxies and assumptions would result in misleading information.

DLAG feedback

- 5.17** In addition to comments reflected in the DP21/24 feedback, the DLAG advised that:
- disclosures should be embedded into existing disclosures (eg the fund prospectus, TCFD entity and product reports, KID and fund factsheets) to increase efficiency and reduce costs, rather than introducing new documents
 - consumer-facing disclosures should be simple and accessible, and limited to information that consumers 'need to know' to make an informed decision
 - disclosures should focus primarily on informing consumers as to 'what' the product is seeking to achieve and whether it is performing in line with its objectives; some may then seek more information on 'how' (ie, the strategy and approach)
 - the regime should not be prescriptive around KPIs, and we should ensure that the disclosures are helpful not only to consumers, but also their advisers

Proposals

- 5.18** Having considered stakeholder feedback and evidence from behavioural research (as set out in Box 2), we are proposing to introduce consumer-facing and detailed disclosure requirements in line with the tiered approach set out in DP21/4.
- Consumer-facing disclosures will provide a summary of the products' key sustainability-related features, helping consumers to better understand those features, compare similar products or the same product over time, and hold the provider to account for its sustainability claims.
 - Detailed disclosures will provide more granular information, which could be useful to institutional investors and a broader range of stakeholders. These will be located in pre-contractual disclosures, the sustainability product report and sustainability entity report.
- 5.19** The qualifying criteria that firms must meet to apply a sustainable investment label to their products (as in Chapter 4) has certain associated disclosures. These are set out in the following sections of this chapter according to where they must be made.
- 5.20** The rules we are proposing at this stage are a starting point for sustainability-related disclosures. We recognise that wider sustainability-related disclosures may be less familiar – and metrics less developed – than climate-related disclosures. As the ISSB develops further standards on additional sustainability topics, we intend to build on our requirements, adding sustainability metrics at product level and more specificity to disclosure requirements at entity level.
- 5.21** Our proposals also take into account other sustainability-related disclosure requirements (EU SFDR), or proposed requirements (US SEC), for asset managers and their investment products. We aim to support international coherence to the extent appropriate.
- 5.22** **Figure 7** shows a summary of the key disclosures and the main locations in which we are proposing that they are made. Cells are marked with an 'o' where all in-scope firms will need to make the disclosures (subject to certain exemptions as set out in Table 1), and marked with an 'x' where the disclosure only applies in respect of products that have a sustainable investment label.

Figure 7 – Summary of disclosure items

| Disclosure type | Product-level | | | Entity-level |
|---|-----------------|--|-----------------|------------------------------|
| | Detailed | | Summary | Detailed |
| | Pre-contractual | Sustainability product report (Part B) | Consumer-facing | Sustainability entity report |
| Sustainability objective | x | x | o | |
| Progress towards objective | | x | o | |
| Investment policy and strategy | x | | o | |
| Stewardship (approach) | x | | o | |
| Stewardship (KPIs), where applicable | | x | | |
| Unexpected investments (ie those a consumer may not typically associate with the sustainability objective) | x | | o | |

| Disclosure type | Product-level | | | Entity-level |
|--|-----------------|--|-----------------|------------------------------|
| | Detailed | | Summary | Detailed |
| | Pre-contractual | Sustainability product report (Part B) | Consumer-facing | Sustainability entity report |
| Ongoing reporting on sustainability metrics/KPIs | | x | o | |
| Resourcing/governance relating to delivery of sustainability objective | | | | x |
| Governance, Strategy, Risk Management, Metrics & Targets | | | | o |

Q11: Do you agree with our proposed approach to disclosures, including the tiered structure and the division of information to be disclosed in the consumer-facing and detailed disclosures as set out in Figure 7?

Q12: Do you agree with our proposal to build from our TCFD-aligned disclosure rules in the first instance, evolving the disclosure requirements over time in line with the development of future ISSB standards?

Proposed consumer-facing disclosure requirements

5.23 The consumer-facing disclosures that we are proposing in this section aim to complement the labels proposed in Chapter 4, by providing consumers with clear, targeted information to help them make considered choices about their investments.

5.24 The proposals aim to ensure that consumers have sufficient information, presented in an accessible way, on the sustainability-related features of investment products to assess whether they meet their needs and preferences.

Location

5.25 We propose that the consumer-facing disclosures be made available in a prominent place on the relevant digital medium for the firm (ie the main product webpage, page on a mobile application etc). For products that qualify for a label, the consumer-facing disclosure should be no more than 'one mouse click away' from where the label is presented. For example, this could be a hyperlink next to or underneath the label. In publishing the consumer-facing disclosure, it must be easy for consumers to identify the product it relates to as well as the label, where relevant, and access links to other relevant product-level disclosures.

5.26 We are proposing that firms produce the consumer-facing disclosure as a new, standalone document. However, we acknowledge feedback from DP21/4 and the DLAG on the importance of ensuring that consumers do not consider sustainability-related information in isolation, and that they read the disclosures with the context of other critical investment considerations, such as the product's financial risk/return profile and costs and charges.

5.27 So, we propose that firms provide the consumer-facing disclosure alongside documents that present other key investor information (eg the Packaged retail investment and insurance-based products (PRIIPs) Key Information Document (KID)).

This may be achieved by co-locating the documents on product pages and ensuring clear signposting from the consumer-facing disclosure to the relevant document.

5.28 We are not proposing to introduce any new rules that specifically require sustainability-related disclosures to be set out in the KID. Where sustainability-related features are integral to an investment product, we expect that firms will make relevant disclosures in the KID in line with their existing PRIIPs disclosure obligations. The supplementary consumer-facing disclosure is, however, an opportunity for the firm to provide more targeted information than it may be able to within the existing KID disclosure requirements.

5.29 We note that the Treasury intends to undertake a review of retail investor disclosures at some stage. This may have implications for sustainability-related disclosures in time. We will remain closely engaged with this work as it develops.

Scope

5.30 To build trust through transparency, it is important that consumers can access clear, consistent information about the sustainability attributes of investment products. Our behavioural research found consumers' comprehension of the sustainability-related features of products to be lower when consumers were only presented with consumer-facing disclosures for products that had a sustainable label, rather than for all products.

5.31 Accordingly, we propose that all in-scope firms must produce a consumer-facing disclosure for all in-scope products. For products that are not engaged in any sustainability-related strategies, the disclosure will be inherently more limited. However, the label field must be marked with 'no sustainable label' and other fields under the content section below marked with 'not applicable' or 'N/A'.

5.32 Where sustainability-related matters are integral to a product's investment policy and strategy, and included in the pre-contractual disclosure accordingly, a summary of the strategy should be included in the consumer-facing disclosure. Importantly, this must be proportionate to the sustainability profile of the product and the sustainability-related strategy, approaches or characteristics must not be overstated. This is in line with our proposed 'anti-greenwashing' rule as described in Chapter 6.

5.33 Firms providing portfolio management services will not be required to produce their own consumer-facing disclosures, but must instead provide an index of the underlying funds in which it invests, including the label and hyperlinking to the individual funds' consumer-facing disclosure, as applicable.

Format

5.34 We want to avoid being too restrictive and risk stifling product innovation in this developing market, while providing consumers with meaningful, consistent information to help them make informed decisions.

5.35 So, at this stage we are proposing to introduce some prescription around the format and content of the disclosures without introducing a template. We do, however, recognise the merits of a template eg to achieve better consistency and standardisation of information to help consumers compare products. We encourage industry to consider developing a market-led template based on the content and format used in our behavioural research and our rules, once finalised.

5.36 We propose that firms must ensure the disclosure is clear and concise, and format is suitable for consumers, taking into account matters such as accessibility and

comprehension (and requirements under the new Consumer Duty). The contents of the disclosure must not exceed 2 pages of A4 when printed, although must be accessible in digital format. Firms must also keep a copy of each version of the published disclosure and provide that copy to a consumer or us on request.

Content

5.37 Our proposed consumer-facing disclosure requirements are intended to be a summary of the information disclosed in the detailed product level disclosures. See **Figure 7** above for an overview of the proposed disclosures and location.

5.38 As noted in the 'format' section above, our intention is to promote consistency and comparability without being too prescriptive. Rather, we are proposing that firms must make the categories of disclosures as set out below:

- **Basic information:** Include the firm's name, product name, International Securities Identification Number (ISIN), or any other unique identifier, and date
- **Product Label:** Display this prominently towards the beginning of the disclosure and include a brief description of what the label means, consistent with the consumer-facing descriptors in Table 2.
- **Sustainability goal:** Clearly state the product's sustainability objective, signposted as 'sustainability goal', highlighting if there is an impact or expected impact on the financial return eg expected implications for the financial risk profile. In addition, describe progress towards the sustainability objective, eg examples of actions taken, and interim goals achieved.
- **Sustainability approach:** Provide a summary of key elements of the product's investment strategy to pursue the objective (eg investible universe, screening, themes), clearly signposted as 'sustainability approach'. This should include, as appropriate, key sustainability characteristics of assets in which the product will and will not invest and the firm's approach to stewardship. Our qualitative consumer research suggests that consumers may find it difficult to access terminology often used in the industry (eg 'best in class' and 'stewardship'). Firms must use language that will be familiar and comprehensible to consumers while effectively and accurately describing the strategy (eg 'themes', 'exclusions', 'engagement') in plain English.
- **Unexpected investments:** Provide a summary of the types of holdings that the firm would reasonably expect consumers of the product to find 'surprising' (ie inconsistent with the sustainability objective), considering factors such as the sector in which the product invests or trade-offs within the sustainability profile of a company. This must be clearly signposted as 'unexpected investments' and include the type of investment eg its sector and an explanation as to why it is held in the product. Where firms do not know this information, we encourage them to conduct consumer testing to better understand the types of holdings their consumers would or would not expect the product to invest in.
- **Sustainability metrics:** Disclose relevant metrics/KPIs linked to achieving the sustainability objective and, where relevant, any other metrics that would help consumers to further understand the approach that the firm has taken. This must be clearly signposted as 'sustainability metrics'. The metrics must be calculated using up-to-date data at the time of reporting and accompanied by contextual information explaining how the metrics should be interpreted.
- **Signposting to other disclosures:** Cross refer/hyperlink to further information in the detailed product-level disclosures (pre-contractual and ongoing performance disclosures), entity-level disclosures, and relevant documents that set out non-sustainability-related information for the product eg costs and charges. The latter may include the key investor information document or key information document.

5.39 The disclosure on 'unexpected investments' is important in helping to build trust as it provides greater transparency as to the types of holdings that might result in mismatched consumer expectations. By clarifying the profile of investments that a consumer may find 'surprising', the consumer will be able to determine whether the product still meets their preferences.

Frequency of disclosure and updates

5.40 To ensure that consumers have reliable information to support their decision-making, we propose that the first consumer-facing disclosures must be made available at the same time as the label (ie provisionally from 30 June 2024). The disclosures must be reviewed and updated at least annually thereafter – eg with at least an update on progress towards the sustainability objective and relevant metrics – and must remain consistent with the label, where applicable.

5.41 We also propose that the firm must review the disclosure prior to any proposed change to the product and revise the disclosure if needed to ensure it remains accurate. If the disclosure has been revised, the firm must notify investors in the product of the change and reasons for the change in writing at least sixty days before it takes effect. It must also publish an updated version of the disclosure with a new date and an explanation of why the change has been made within the same timeframe.

Box 10: New Consumer Duty

In July, the FCA published a new Consumer Duty aimed at ensuring a higher and more consistent standard of consumer protection. The rules aim to address harms such as firms presenting information in a way that exploits consumers' behavioural biases, among others. To achieve this, they require firms to focus on supporting and empowering customers to make good financial decisions, including by providing consumers with information they can understand.

Our SDR and labels are seeking similar outcomes, particularly with respect to consumer understanding. We want consumers to be given the information they need, at the right time, and presented in a way they can understand, to enable them to make informed decisions about financial products and services.

In complying with our consumer-facing disclosure rules, firms must also comply with the consumer understanding outcome under the new Consumer Duty. This means, for example, that firms will need to ensure their communications meet the information needs of retail customers, are likely to be understood, and equip retail customers to make decisions that are effective, timely and properly informed. The information must be communicated in a way that is fair, clear and not misleading, and provided on a timely basis.

We also draw attention to the requirements on 'testing, monitoring and adapting communications' to support understanding and good outcomes for retail customers. We have applied this approach in our own policy development by testing our proposed consumer-facing disclosures. Our experiments found that our specific content and format of disclosures increased consumers' comprehension of sustainability-related information, compared with the KIID.

The Duty's rules and guidance include a number of factors for firms to consider to determine whether testing of a communication is appropriate. This includes consideration of the purpose of the communication (eg impact on decision-

making); the context, timing and frequency of the communication; information needs of retail consumers; scope of harm to retail consumers etc (as set out in PRIN 2A.5.12 G).

We think it likely that firms will need to carry out their own testing on consumer facing disclosures under the SDR rules as the disclosures include information that many consumers may rely on to inform an important investment decision. There is a risk to consumers if they are making these decisions without being able to understand properly the information that is being presented to them. We expect any disclosures that firms produce to improve comprehension at least as much as the consumer-facing disclosure that we tested in our experiments (see full results published alongside this CP [here](#)).

Q13: Do you agree with our proposals for consumer-facing disclosures, including location, scope, content and frequency of disclosure and updates? If not, what alternatives do you suggest and why?

Q14: Do you agree with the proposal that we should not mandate use of a template at this stage, but that industry may develop one if useful? If not, what alternative do you suggest and why?

Proposals for detailed product-level disclosures

5.42 In addition to disclosures directed to retail investors, it is important that more detailed disclosures are available for institutional investors and other stakeholders – or retail investors that may be interested in receiving more information. These disclosures will provide greater transparency on the product’s sustainability objective, strategy, and progress towards meeting the objective, as well as ongoing performance metrics and contextual information.

5.43 We recognise that firms are already making product-level disclosures in different documents. So, to reduce the burden on firms while ensuring sustainability-related information reaches the intended audience, we are proposing that detailed product-level disclosures be made in two forms of existing documentation, depending on the information being disclosed:

- pre-contractual disclosures: fund prospectus, prior information document
- sustainability product report (building from the ‘TCFD product report’)

Pre-contractual disclosures

5.44 Before issuing an investment product, firms are required to produce a form of pre-contractual disclosure setting out key information. This is legally binding, static information that investors can use to inform their decisions about which products meet their needs and preferences. We consider these to be the appropriate location for disclosures about the key sustainability-related features of products.

5.45 At this stage, the 'fund prospectus' and prior disclosure document required under FUND 3.2 for full scope UK AIFMs are the only pre-contractual materials in scope of our proposals. As we consult on expanding the scope of products over time, we shall consider where it may be appropriate to expand the list of pre-contractual materials accordingly. However, for now, we propose that if the fund prospectus or prior information document are not the relevant pre-contractual material for an in-scope product (eg AIFs managed by small AIFMs), the firm must make the pre-contractual disclosures (as set out in the content section below) available in the sustainability product report ('Part A') and ensure that investors are made aware of the contents of the report before they invest in the product.

Scope

5.46 We propose that all products using a sustainable investment label must make pre-contractual disclosures associated with the qualifying criteria.

5.47 Where products do not qualify for a label but nevertheless adopt sustainability-related features that are integral to their investment policy and strategy, we also expect these to be disclosed in pre-contractual documents. We propose that firms set out those features (including a sustainability objective if any) and the investment policy and strategy in a proportionate manner to the sustainability profile of the product.

5.48 Firms providing portfolio management services will not be required to produce their own pre-contractual disclosures. However, they must provide retail investors with easy access (eg by hyperlinking) to the relevant disclosures.

5.49 Products that do not qualify for a label or adopt sustainability-related policies and strategies are not subject to our pre-contractual disclosure requirements.

Format, location and content

5.50 In accordance with the criteria in Chapter 4, we propose that firms display the sustainable investment label for the product and make the following pre-contractual disclosures:

Principle 1 – sustainability objective

- 1.** A firm must disclose the product's sustainability objective in specific and measurable terms as part of its investment objectives, including those with respect to achieving a financial return on that product.
- 2.** A firm must disclose details of the extent to which the sustainability objective has, or may have, impacted the financial return of the product.
- 3.** A firm must disclose details of the plausible, purposeful, and credible link between the product's sustainability objective's and environmental and/or social outcomes.

Principle 2 – investment policy and strategy

- 1.** A firm must disclose details of the product's investment policy and strategy and the way these align with the product's sustainability objective.
- 2.** A firm must describe the product's investible universe and the asset-level selection criteria it applies to meet a target environmental and/or social sustainability profile of assets (as referred to in Chapter 4), in specific and measurable terms, including:

- how the firm assesses the assets in which the product invests against the criteria
 - how the selection criteria relates to the target environmental and/or social profile of the product's assets
 - how the target environmental and/or social profile of the product's assets align with the product's sustainability objective; and
 - the conditions under which an asset in which the product has invested in may cease to meet its specified criteria for asset selection
3. A firm must provide details of its policies and procedures to determine, measure, monitor, evaluate and report to investors (ie clients and consumers) on the environmental and/or social sustainability profile of the product's assets over time.
 4. A firm must provide details of its target asset composition in respect of the product, including:
 - the different asset classes in which it will invest, its use of derivatives, its long-term and short-term exposures
 - the processes by which it complies with the requirement to have appropriately designed policies and procedures in place to determine, measure, monitor, evaluate, and report to investors (ie clients and consumers) on an ongoing basis; and a description of the environmental and social sustainability characteristics of assets (or asset types) in which the product will and will not invest
 5. A firm must disclose any investments made by the product that a reasonable investor (ie client and consumer) might consider to be in conflict with the sustainability objective, investment policy and strategy of the product.
 6. Where the product is an index-tracking product, a firm must describe how the index provider's methodology for index-construction aligns with the product's sustainability objective and its target environmental and/or social sustainability profile.

Principle 5 – stewardship

1. A firm must set out details, in a clear and accessible way, of its (firm-level and/or product-level) stewardship strategy and resources, including:
 - a. details as to any differences or conflicts between its firm-level and product-level stewardship strategy, in relation to the product, including any specific targets or constraints applied at the product-level (eg product-specific engagement or voting strategy)
 - b. details as to its commitment to the UK Stewardship Code 2020, published by the FRC
 - c. the specific methods it uses to influence sustainability outcomes across the product's assets
 - d. how it applies its strategy and resources in a manner consistent with the product's sustainability objective

| Category-specific criteria | | |
|----------------------------|---|--|
| Sustainable Focus | Sustainable Improvers | Sustainable Impact |
| | <p>The firm must describe (in relation to its asset-level selection criteria as required in Chapter 4) how it assesses potentially investible assets to determine the extent to which improvements in sustainability can be achieved over time, including through investor stewardship.</p> | <p>The firm must include the following information:</p> <ul style="list-style-type: none"> its theory of change, with clear examples that emphasise how its investment process aims to contribute to addressing environmental and/or social problems, in line with its sustainability objective a robust method to measure and demonstrate that its investment activities have had a positive environmental and/or social sustainability impact its escalation plan should the real-world outcome no longer plausibly be achievable, including potential divestment of assets in relation to specifying its asset-level selection criteria (as required in Chapter 4), how it assesses potentially investible assets to determine: <ul style="list-style-type: none"> whether those assets align with the product's theory of change, while also avoiding unintended negative consequences; and the extent to which a positive, measurable, environmental and/or social outcome can be achieved |

- 5.51** We are proposing that disclosures relating to the investment policy and strategy (ie Principle 2) be made in a dedicated section of the fund prospectus. This is to clearly identify these disclosures among what can in some cases be lengthy documents.
- 5.52** We also propose that Part A of a sustainability product report is published in a prominent place on a relevant digital medium for the firm (ie product webpage, page on a mobile app), where the product is offered.
- 5.53** We are not proposing to include requirements that mirror the EU SFDR's 'Do No Significant Harm' approach, ie disclosures on how a sustainable investment does not significantly harm the sustainability objective. We consider this approach may be too restrictive at this stage.
- 5.54** However, we have included some implementation guidance to our qualifying criteria that steers firms towards considering whether any trade-offs or adverse environmental or social impacts might arise in pursuing sustainability objectives. For 'Sustainable Impact' products, we also propose category-specific criteria requiring the firm to assess whether its potentially investible assets align with the product's theory of change, while also avoiding unintended negative consequences.

5.55 In addition, the disclosure of unexpected investments (as required in both the consumer-facing and pre-contractual disclosures) should provide greater transparency about holdings that consumers may not typically associate with product that has a sustainable investment label.

Frequency of disclosure and updates

5.56 We are proposing that the first pre-contractual disclosures must be made available at the same time as the label and consumer-facing disclosures (ie provisionally from 30 June 2024). This means firms preparing Part A of the sustainability product report will be required to publish that part one year earlier than Part B of the reports (see section below). Pre-contractual disclosures for existing products must be updated to reflect sustainability objectives and investment policies and strategies, accordingly.

5.57 If there is a material change to the product requiring a change to the pre-contractual disclosure, the same requirements for making such changes and notifying clients as set out under the section on consumer-facing disclosures must be followed.

Q15: Do you agree with our proposals for pre-contractual disclosures? If not, what alternatives do you suggest and why. Please comment specifically on the scope, format, location, content and frequency of disclosure and updates.

Sustainability product report – ‘Part B’

5.58 We are proposing that firms produce disclosures on the sustainability-related performance of their products on an ongoing basis, in a dedicated sustainability product report which builds from the TCFD product report.

Scope

5.59 In the first instance, we propose that a sustainability product report will only be required for products that qualify for a sustainable investment label.

5.60 As noted in the pre-contractual disclosures section above, the report may include the pre-contractual information set out above in cases where the in-scope product does not have a fund prospectus or prior information document (referred to as ‘Part A’ of the report).

5.61 All firms using a sustainable investment label will however be required to produce disclosures to help clients and consumers assess ongoing performance and progress towards meeting its stated objective. This is referred to as ‘Part B’ of the report.

5.62 In time, the sustainability product report will also include a baseline of sustainability-related metrics. building from the core climate-related metrics in the TCFD product report. Firms will be required to disclose these in respect of all in-scope products, regardless of whether the product uses a label. However, we are not proposing these at this stage. We will continue to monitor the development of ISSB standards on sustainability topics, and to assess risks and harms in the market, with a view to consulting on additional metrics as appropriate.

5.63 Firms providing portfolio management services will not be required to produce their own sustainability product reports. However, they must provide retail investors with

easy access (eg by hyperlinking) to relevant disclosures (Part A, where applicable, and Part B).

Location and format

5.64 In building from the TCFD product report, we are proposing that the sustainability product report is published in a prominent place on the main website for the business of the firm (eg with a link from the homepage). The report must include the information required under our TCFD rules (eg either by incorporating the contents or hyperlinking to the information), ensure the climate-related disclosures are easily identifiable and make it clear that the climate-related disclosures form part of the overall report. In addition, firms will need to include, or provide a hyperlink to, these disclosures in the appropriate form of client communication which follows most closely after the annual reporting deadline.

5.65 We are also proposing to retain the same flexibilities as for the TCFD product report, whereby a firm may cross-refer to relevant disclosures in a third-party's sustainability product report provided that those disclosures are clearly signposted and the firm sets out the rationale for doing so and any deviations between the third-party's and the firm's approach.

5.66 The firm may also choose to cross reference between its sustainability product report (Part B) and its sustainability entity report where relevant.

Content

5.67 In accordance with the qualifying criteria in Chapter 4, a firm must also make disclosures in Part B of its sustainability product report. We propose that the firm must display the sustainable investment label, and state the product's sustainability objective as well as progress towards meeting that objective. In addition, the firm must make the following disclosures associated with the criteria:

Principle 2 – investment policy and strategy

A firm must provide details as to how the product invests in accordance with its investment policy and strategy on an ongoing basis.

Principle 3 – KPIs

A firm must disclose details of the product's performance against the specified KPIs.

Principle 5 – stewardship

Where stewardship plays a significant role in the product's investment policy and strategy a firm must disclose:

- its specified (credible, rigorous and evidence-based) KPIs related to stewardship, including engagement and voting activity relevant to the delivery of the product (in line with its sustainability objective)
- outcomes of its stewardship activities, with reference to the product's sustainability objective; these disclosures can be made in existing stewardship-related reporting (eg reporting as a signatory of the UK Stewardship Code 2020) and cross-referenced in its sustainability product report

Category-specific criteria

| Sustainable Focus | Sustainable Improvers | Sustainable Impact |
|---|--|---|
| <p>The firm must disclose the KPIs specified in accordance with the requirements for this category under Chapter 4.</p> <p>In relation to its stewardship strategy, the firm must disclose how that strategy has been applied to achieve continuous improvement in environmental and/or social sustainability of the product's assets; and the outcomes achieved.</p> | <p>The firm must disclose details of the KPIs specified in accordance with the requirements for this category under Chapter 4.</p> | <p>The firm must disclose the KPIs specified in accordance with the requirements for this category under Chapter 4, also including:</p> <ul style="list-style-type: none"> its analysis as to how its actions have contributed to the impact achieved; or an explanation as to why its actions have not done so <p>The firm must also disclose details as to how its rights and influence (including through direct control as relevant) have been applied to pursue the pre-defined, positive, measurable real-world outcome specified in the product's sustainability objective, in line with its theory of change for the product.</p> |

5.68 In addition, we propose that Part B of the sustainability product report must include:

- any other metrics that a client or consumer might find useful in understanding the firm's approach to meeting the sustainability objective, or deciding whether to invest in a particular sustainability product eg common metrics within a certain sector. The firm should also explain the methodology used, and present KPIs relating to the sustainability objective at least as prominently as any other metrics.
- contextual information alongside KPIs/metrics disclosed including how KPIs/metrics should be interpreted, their limitations, and use of proxies/assumptions, to enable clients and consumers to interpret the data effectively and in a way that is not misleading
- historical annual calculations on KPIs/metrics after the first year of reporting, to enable clients and consumers to compare sustainability performance year-on-year in a way that is easy to understand and not misleading
- any disclosures where the firm's approach to a sustainability product materially deviates from the firm's overarching approach disclosed in the firm's sustainability entity report – in doing so the firm may cross-refer to disclosures in each report
- date of the report

5.69 We acknowledge that firms may face data and methodological challenges and therefore propose to retain the approach to disclosing metrics in our TCFD rules. This means that firms must use the most up to date information available within their reporting period when making disclosures.

5.70 However, firms must not disclose metrics where data gaps or methodological challenges are so severe that they cannot be addressed using proxy data or assumptions without the disclosure being misleading. If the firm has been able to address the gaps, they must nevertheless explain the gaps and how they've addressed them (including briefly setting out the methodologies and limitations of the approach).

If the firm has not been able to address the gaps, it must explain the gaps, why it has not been able to address them, and the steps it will take to address the gaps or challenges in future.

5.71 While these rules on data and methodological challenges apply in respect of metrics broadly, where a firm is using a label it must ensure that data relied upon to meet the criteria (ie for its KPIs) is sufficient to be disclosed (ie accurate and complete, including through use of proxies and assumptions where appropriate).

5.72 We also encourage firms to provide greater transparency on the quality of data by disclosing an explanation of the proportion of each sustainability product for which data are verified, reported, estimated or unavailable.

On demand reporting

5.73 As with our TCFD rules, we recognise that in some client relationships, public disclosures are not appropriate; eg firms that provide discretionary portfolio management services to individuals or institutional investors and UK AIFMs managing unauthorised AIFs that are not listed on a recognised investment exchange.

5.74 Where firms decide to use a label for these products, and their clients need the information to satisfy their own (or their clients' or customers') sustainability-related disclosure obligations, we are proposing that disclosures be made to the client upon request, once a year. The client cannot make such a request before 1 July 2025, specifying a calculation date no earlier than 30 June 2024 (ie 12 months after our rules enter into force). The calculation date can be the same as the reporting period for Part B of the sustainability product report, or an alternative date agreed by the client and firm. However, if a client relationship starts after 30 June 2024, the client cannot request data that precedes the start of the relationship. A firm must respond to an eligible client's request in a reasonable time and a reasonably acceptable format to meet their information needs.

5.75 Unauthorised AIFs managed by a UK AIFM that are not listed on a recognised investment exchange will need to provide the information in Part A (where applicable) and Part B of the sustainability product report. While firms providing portfolio management services will provide clients with access to Part A and Part B of the reports, as applicable, for each of the underlying products in which it invests, where these are not already publicly available.

5.76 We encourage firms to provide broadly equivalent disclosures to any client who requests them (ie regardless of their eligibility to request under our rules).

Frequency of disclosure and updates

5.77 We propose that the first disclosures under 'Part B' of the sustainability product report must be published no later than 24 months after our rules enter into force (ie provisionally from 30 June 2025). This aligns with the deadline for publishing the TCFD product report. TCFD rules relating to the reporting period also apply (ie ESG 2.1.1R(1) and ESG 2.1.2R(1)-(3)).

5.78 We also propose that disclosures are updated on an annual basis and in any case remain consistent with the sustainable investment label, including updating them in accordance with any changes to the label.

Q16: Do you agree with our proposals for ongoing sustainability-related performance disclosures in the sustainability product report? If not, what alternative do you suggest and why? In your response, please comment on our proposed scope, location, format, content and frequency of disclosure updates.

Q17: Do you agree with our proposals for an 'on demand' regime, including the types of products that would be subject to this regime? If not, what alternative do you suggest and why?

UK Green Taxonomy disclosures

- 5.79** In its Roadmap to Sustainable Investing, the UK Government set out plans for SDR to include disclosures against the UK Green Taxonomy. This included plans for disclosures on product-level Taxonomy alignment.
- 5.80** These disclosures are intended to help investors better understand and compare the environmental performance of investment products.
- 5.81** The Government established a Green Technical Advisory Group (GTAG) to advise on the development of the UK Green Taxonomy and will take a co-ordinated and consultative approach. The first tranche of this advice was published earlier this month. We are an observer on the GTAG and remain closely engaged with their work.
- 5.82** Once developed, our intention is to consider how we might update our rules to include disclosures relating to the Taxonomy, subject to the usual consultation and cost benefit analysis processes.

Proposals for detailed entity-level disclosures

- 5.83** In addition to information on the sustainability-related features of investment products, clients and consumers are increasingly interested in how firms offering these products are managing sustainability risks and opportunities.
- 5.84** This information enables clients and consumers to take sustainability matters into account when granting mandates or selecting firms. Producing these disclosures also benefits the disclosing firm, encouraging more structured dialogue on, and analysis of, sustainability-related matters across the organisation.
- 5.85** As envisaged in DP 21/4, we intend to build on our TCFD entity-level disclosure requirements. This will already be a familiar reporting framework for many in-scope firms and the four-pillar structure of the TCFD's recommendations have also formed the basis for the ISSB's proposed general sustainability-related disclosure requirements.

Scope

- 5.86** All in-scope asset managers (as set out in Table 1) will be required to produce a sustainability entity report.

5.87 We are proposing a phased implementation, similar to the proportionate approach we took in introducing TCFD-aligned disclosures. Larger firms (asset managers with above £50 billion in AUM) will be required to make their first disclosures by 30 June 2025, with smaller firms, excluding those with under £5 billion in AUM, required to make their first disclosures one year later. In [PS 21/24](#) we committed to reviewing the threshold after three years of climate-related disclosures. We will consider at that time whether to also amend the threshold for sustainability-related disclosures.

Location and format

5.88 Since we are proposing that the sustainability entity report builds from the TCFD entity report, we similarly propose that the report must be published in a prominent place on the main website for the business of the firm (eg with a link from the homepage).

5.89 We are proposing that the sustainability entity report may either incorporate disclosures required under the TCFD rules, or include a hyperlink to the TCFD entity report. Whether incorporating or hyperlinking, the TCFD-aligned disclosures must be clearly identifiable as part of the overall sustainability entity report.

5.90 We are also proposing to retain the flexible approach to the TCFD entity report, whereby firms are able to cross-refer to sustainability-related disclosures made in a group, affiliate or third-party's (eg a delegated asset manager's) sustainability report. This includes instances where the firm or member of its group produces a document other than the annual financial report for sustainability-related information. The disclosures must be relevant and cover the firm's in-scope products.

5.91 Where the firm chooses to cross-refer to disclosures in another report, the cross-referenced disclosures must be clear and easily navigable. So, we propose that the firm must set out in its sustainability entity report:

- clear signposting to where the group or other third-party disclosures can be found eg including relevant hyperlinks and cross references
- the rationale for cross referencing and why the disclosures are relevant
- any material deviations from the approaches set out in the cross-referenced report (ie where approaches taken under the cross-referenced firm's governance, strategy, risk management or metrics and targets differ to the in-scope firms' own approaches to any of those four pillars); these can be set out in the sustainability entity report or group/affiliate's report
- where relevant, how the firm's strategy has influenced the decision-making and process by which it delegates functions, selects delegates, and relies on services, strategies or products offered or employed by third parties

5.92 As with the TCFD entity report, the sustainability entity report must include a statement, signed by a member of senior management, confirming that the disclosures comply with Chapter 4 of the ESG Sourcebook. This would confirm that the disclosures accurately reflect the firm's own approach to managing sustainability risks and opportunities.

Content

5.93 As noted above, we propose to build on the TCFD framework, extending disclosure requirements under the four pillars – governance, strategy, risk management and metrics and targets – on climate-related financial disclosures to sustainability-related risks and opportunities.

- 5.94** Consistent with our climate-related disclosure rules, the entity-level disclosures would be made in respect of how the firm takes sustainability-related matters into account in managing investments on behalf of clients and consumers. The aim is to enable clients and consumers to understand the firm's approach to sustainability-related risks and opportunities.
- 5.95** We acknowledge that 'sustainability' covers a broad range of topics and firms may be taking different approaches for some of them. For example, firms may be prioritising the management of different sustainability-related risks and opportunities according to the profile of the assets they manage.
- 5.96** We also recognise that firms may need additional specificity on what to disclose in relation to different sustainability-related topics (other than climate change which is covered by our TCFD-aligned disclosure rules). The ISSB's proposed general sustainability-related disclosure requirements (IFRS S1) already build from the TCFD's four pillars, setting out requirements for disclosures on sustainability-related matters. Firms may therefore find it helpful to refer to those standards to consider the types of disclosures to be made in relation to sustainability-related risks and opportunities more broadly. Firms may also find it helpful to refer to SASB's sector-specific standards in developing their disclosures. However, we intend to build on the proposals in this CP over time, adding specific disclosure requirements on other sustainability-related topics in a manner consistent with future international reporting standards.
- 5.97** At this stage, we are only proposing to introduce core entity-level disclosure requirements based on the TCFD's four recommendations:
- the governance around sustainability-related risks and opportunities
 - the actual and potential impacts of sustainability-related risks and opportunities on their businesses, strategy and financial planning, where such information is material
 - how the firm identifies, assesses and manages sustainability-related risks
 - the metrics and targets used to assess and manage relevant sustainability-related risks, where such information is material
- 5.98** To help firms determine the content of disclosures that may be useful for clients and consumers, we propose to add the following Handbook guidance:
- Firms should consider disclosing the sustainability-related topics that they have prioritised in their governance, strategy and risk management, and the rationale for doing so. For example, a firm managing assets likely to be impacted by measures to protect biodiversity may set out how and why it has prioritised the management of biodiversity-related risks and opportunities.
 - Disclosures should be made under the four pillars in respect of both the firm's operations and how it manages assets on behalf of clients and consumers. For the latter, firms may refer to the TCFD's supplemental guidance for asset managers to help determine the types of disclosures to make. The guidance covers disclosures under the strategy, risk management and metrics and targets pillars.
- 5.99** We also consider the following may be relevant in helping firms to determine the content of disclosures that may be useful for clients and consumers, and propose to include a reference to these in Handbook guidance:

- The ISSB's general sustainability-related disclosure requirements: firms may find it helpful to refer to these standards as a guide to help determine the content of the governance, strategy, risk management, and metrics and targets disclosures. As the disclosure requirements are targeted at corporate entities, with a view to enabling investors assess enterprise value, we do not expect asset managers to disclose each line item set out in the standard. Rather asset managers should use the standard as a starting point when considering the types of sustainability-related information that would be decision-useful to clients and consumers. As noted above, we will add further specificity in time.

We note that the ISSB's standards have not yet been finalised or adopted for use in the UK. So, we are consulting on the basis that we would reference the final, UK-adopted IFRS S1 standards, provided that they are broadly consistent with those proposed.

- SASB Standards: firms may wish to refer to SASB standards to help determine sector-specific information to disclose.

5.100 The proposals for data considerations set out in paragraphs 5.69 – 5.72 also apply in respect of entity-level disclosures.

5.101 Since our proposals are based on the TCFD's four pillars, there are some key differences to the SFDR's entity level disclosure requirements. For example, we are not proposing to require disclosure of principle adverse impacts. Firms must however disclose the metrics used to assess and manage sustainability risks. Further similarities and differences are outlined in Annex 1.

5.102 In relation to the four pillars, where the approach at product level differs materially from the entity-level approach described, this should be disclosed in the entity-level report or in the relevant, cross-referenced sustainability product report.

5.103 Where a firm uses a sustainable investment label, it must make the following disclosures in relation to the qualifying criteria in its sustainability entity report:

Principle 4 – governance and resources

1. A firm must describe the arrangements and resources it has in place to oversee the sustainability research, data and analytical tools that it uses in supporting the product's sustainability objective.
2. A firm must describe the resources, governance and organisational arrangements that appropriately support and incentivise the high-quality delivery of its documented investment policy and strategy in line with the sustainable investment product's sustainability objective.

Frequency of disclosure and updates

5.104 As set out in Chapter 3, we propose a phased approach to implementation of the entity-level disclosure requirements, with the first disclosures to be published by the largest in-scope firms 24 months after the PS (ie provisionally by 30 June 2025) and smaller firms to publish their first disclosures one year later. These disclosures must be updated on an annual basis. This aligns with the deadline for publishing TCFD entity

reports. TCFD rules relating to the reporting period also apply (ESG 2.1.1R(1) and ESG 2.1.2R(1)-(3)).

Q18: Do you agree with our proposals for sustainability entity report disclosures? If not, what alternatives do you suggest and why? In your response, please comment on our proposed scope, location, format, content, frequency of disclosures and updates.

Q19: Do you agree with how our proposals reflect the ISSB's standards, including referencing UK-adopted IFRS S1 in our Handbook Guidance once finalised? If not, please explain why?

Transition plans

- 5.105** During COP26 last November, the Chancellor announced that the UK would be the first net zero-aligned financial centre. He set out plans to require listed companies, asset managers and asset owners to disclose transition plans that consider the Government's net zero commitment or explain why not.
- 5.106** Subsequently the Government set up a high-level Taskforce to develop a 'gold standard' for transition plans. We are pleased to be represented on both the Steering Group and Delivery Group of the UK Government's TPT. The TPT will develop a sector neutral transition plan framework, sector specific guidance and user and preparer guidance to support the development, disclosure and assessment of transition plans, with initial outputs to be published in Q4 2022.
- 5.107** We have already taken steps to introduce requirements for the disclosure of transition plans into our regulatory framework. In finalising our TCFD-aligned disclosure rules for listed issuers and regulated firms, we added a guidance provision (consistent with the TCFD's own guidance) to clarify that a firm headquartered in, or operating in, a country that has made a commitment to a net zero economy is encouraged to consider the extent to which it has considered that commitment in developing and disclosing its transition plan.
- 5.108** We are committed to drawing on the Taskforce's outputs to strengthen our disclosure expectations and encourage well-governed and credible transition plans by both listed companies and regulated firms. We will also encourage a globally coherent approach to transition plan disclosures, coordinating with bodies such as the Glasgow Financial Alliance for Net Zero and ISSB (both of which are also represented on the TPT Delivery and Steering Groups).
- Interaction with other sustainability disclosure initiatives***
- 5.109** We want our regime to be compatible with other initiatives internationally as far as possible, while remaining appropriate for the UK market. We recognise that many UK firms have been building capabilities to comply with SFDR in respect of their EU business and will be preparing to comply with the SEC's proposals. So, we have included a high-level mapping of the key disclosure items under our proposals to the SFDR and SEC's proposals in Annex 1.

- 5.110** Our rules seek to be flexible and enable firms to make disclosures at the level of consolidation that would be most decision-useful. So, we do not preclude firms from cross referencing to detailed entity-level disclosures produced in a group-level or affiliate report, provided that our requirements for cross-referencing are met.
- 5.111** However, in-scope firms must produce a separate consumer-facing disclosure as required under our rules. We acknowledge that there may be different types of disclosures for consumers based on requirements in different jurisdictions (eg the EU SFDR). As noted, our requirements have been informed by several rounds of behavioural research (see Box 2) and stakeholder feedback. We consider the parameters set out under our proposals will result in disclosures that meet the information needs of retail investors.
- 5.112** Our consumer-facing disclosures also accompany the sustainable investment label and so are tailored to provide key information that will help consumers better understand the sustainability-related features of the labelled product. This in turn will protect consumers by reducing scope for firms to greenwash their products.

6 Naming and marketing

Overview

- 6.1** The labels and disclosures proposed in this CP should help consumers more effectively navigate the market for ESG and sustainable investment products. The different categories of labels will help consumers distinguish between different types of sustainable investment products and find products that meet their preferences.
- 6.2** However, without further intervention, there remains a risk that products that do not qualify for a label will continue to name or market themselves in a way that may suggest they are sustainable. This may be confusing to consumers, could lead to greenwashing, and could compromise the effectiveness of the labels in helping consumers make choices.
- 6.3** For example, many products currently promote themselves as 'ESG-integrated' and many employ strategies such as 'exclusion/negative screening' or basic 'ESG tilts'. As set out in Chapter 4, we do not consider these attributes alone to be sufficient to meet the requirements for a sustainable label. If such products were to continue to name and market themselves as being 'ESG' or 'sustainable' in this way, despite not qualifying for a sustainable label, consumers could be misled.
- 6.4** To address these potential harms, this chapter sets out our proposals to introduce restrictions around names and marketing of investment products marketed to retail investors that do not qualify for a label. We also propose to introduce a general 'anti-greenwashing' rule applicable to all regulated firms, reaffirming that existing requirements around clear, fair and not misleading communications apply in the context of sustainability-related claims. Together these will advance our objectives to protect consumers and enhance market integrity.

DLAG feedback

- 6.5** As discussed in Chapter 4, DLAG members recommended reducing the number of labels to avoid overwhelming consumers, and also recommended removing the 'Not Promoted as Sustainable' product label.
- 6.6** Some also suggested mechanisms to ensure that products not qualifying for a sustainable label are effectively differentiated from those with labels. Specifically, one member recommended considering restrictions on the naming and marketing of products that do not meet the criteria for a sustainable label. These restrictions would ensure that products without a sustainable label could not promote themselves as being sustainable through their names or in marketing materials.
- 6.7** We have considered that feedback and agree both with the recommendation and the underlying rationale.

- 6.8** We are proposing new rules to help achieve this outcome: a general rule applying to all regulated firms, and requirements specifically addressing naming and marketing of in-scope investment products, respectively.

Proposals

A general 'anti-greenwashing' rule for all FCA-regulated firms

- 6.9** The first element of our proposed interventions is to introduce a general 'anti-greenwashing' rule. This would require all regulated firms to ensure that the naming and marketing of financial products and services in the UK is clear, fair and not misleading, and consistent with the sustainability profile of the product or service ie proportionate and not exaggerated. By applying this rule to all FCA-regulated firms, we would also be capturing firms that approve financial promotions for unauthorised persons, who will need to ensure that the promotions they approve for unauthorised persons comply with this rule as well as the financial promotions rules.
- 6.10** Firms should already be ensuring the information they communicate to clients is clear, fair and not misleading under PRIN 2.1, Principle 7, and COBS 4.2.1. However, we consider it necessary to add a specific rule to the ESG Sourcebook to link this directly to sustainability claims, and to ensure that firms understand that this applies when they are making sustainability claims. We further clarify that those claims must be proportionate to the sustainability profile of the product or services. This proposal will give us an explicit rule on which to challenge firms that we consider to be potentially greenwashing their products or services, and take enforcement action against them as appropriate. This will help to ensure better outcomes for consumers, in line with the new Consumer Duty and our objective to protect consumers.

Q20: Do you agree with our proposed general 'anti-greenwashing' rule? If not, what alternative do you suggest and why?

Product names and marketing materials

- 6.11** Product names may be one of the first things a retail investor reads or hears about a product, and marketing is key to their understanding of the product's features, so it is important that these are accurate and not misleading.
- 6.12** We are proposing to prohibit firms providing in-scope products to retail investors that do not qualify for and use one of the sustainable labels from using sustainability-related terms including (but not limited to) 'ESG' (or 'environmental', 'social' or 'governance'), 'climate', 'impact', 'sustainable' or 'sustainability', 'responsible', 'green', 'SDG' (sustainable development goals), 'Paris-aligned' or 'net zero' in their product names and marketing. We also propose that 'Sustainable Focus' or 'Sustainable Improvers' products be prohibited from using the term 'impact' in the naming and marketing of these products.
- 6.13** This proposal codifies the guidance set out in our [Guiding Principles](#) for the design, delivery and disclosure of sustainable investment funds, which in turn built upon our 'clear, fair and not misleading' rules for fund communications.

- 6.14** The rules will apply to in-scope products that are made available to retail investors in the UK. Products offered to institutional investors are not in scope of these requirements as we do not consider this to be proportionate at this stage.
- 6.15** However, as proposed in Chapter 5, where firms adopt sustainability-related investment policies and strategies that are integral to their investment policy and strategy, firms should describe these factually and in a proportionate way in their pre-contractual disclosures. So, the prohibition on including sustainability-related terminology does not apply for the purposes of disclosing factual information in the pre-contractual disclosures, the summary of information in consumer-facing disclosures, and any other disclosure requirements a firm may be subject to.
- 6.16** For example, a firm providing a tracker fund that does not qualify for a label but follows an ESG-tilted benchmark should disclose the use of this benchmark.
- 6.17** As set out in Chapter 3, we propose that specific rules will apply in relation to the use of sustainability-related terms in the naming and marketing of portfolio management agreements or arrangements to retail investors. In particular, firms will be able to use such terms, provided that 90% or more of the total value of the products in which the relevant portfolio invests qualify for a sustainability label and that the terms are not used in a misleading way.

Q21: Do you agree with our proposed product naming rule and prohibited terms we have identified? If not, what alternative do you suggest and why?

Q22: Do you agree with the proposed marketing rule? If not, what alternative do you suggest and why?

Q23: Are there additional approaches to marketing not covered by our proposals that could lead to greenwashing if unaddressed?

7 Distributors

Overview

- 7.1** In DP21/4 we noted the important role played by market participants such as distributors in communicating sustainability-related information – including the labels and disclosures – along the investment chain. Our regulatory intervention will be less effective if the sustainable investment labels and accompanying disclosures are not communicated to retail investors.
- 7.2** There are several important intermediaries involved in distributing investment products to consumers. We regard distributors as those that offer, sell, recommend, advise on, arrange, deal, propose or provide a product or service.
- 7.3** For example, we propose that financial advisers will be in scope of our rules as they relate to their roles as distributors of information to retail investors. As noted in Chapter 2, we are exploring how best to introduce further requirements for financial advisers focusing on product suitability, and we will consult on these in due course.
- 7.4** Other types of distributors include investment platforms, through which investors can compare and invest in multiple investment products and which are increasingly popular with UK retail investors. As with financial advisers, these platforms have an important role in ensuring regulatory information associated with products reach and are easily accessible to consumers.
- 7.5** This chapter sets out our proposals for distributors of in-scope products to retail investors in the UK. We propose that distributors must ensure the sustainable investment label and consumer-facing disclosures are made available to those investors.

DP 21/4 feedback

- 7.6** In DP 21/4 we asked for feedback from stakeholders on the role of other market participants in communicating information to investors.
- 7.7** Respondents were broadly supportive of increased communication of sustainability-related information along the investment chain, and of capturing distributors within scope of our rules to achieve this. Respondents also noted the importance of clarifying responsibilities over the production of this information, and of ensuring consistency with existing requirements.

Proposals

- 7.8** We are proposing that where in-scope products are offered to retail investors and have a sustainable investment label, distributors must display the label prominently on a relevant digital medium (eg product webpage, page on a mobile application or other medium) and provide access to the accompanying consumer-facing disclosures. The distributor must not use a sustainable investment label for a product other than the label that has been assigned by the firm. In addition, we propose that distributors must keep the relevant digital medium and marketing communications updated with any changes a firm makes to the label and disclosures.
- 7.9** For products that do not use a label, the distributor will nevertheless be required to provide retail investors with access to the consumer-facing disclosure.
- 7.10** These proposals are consistent with current expectations on distributors in making information available to investors. So, we remind distributors that they must comply with existing requirements for the distribution of financial products in the PROD Sourcebook and under the new Consumer Duty.
- 7.11** As set out in Chapter 1, we want to protect retail investors from potential greenwashing in all investment products offered to them in the UK, including overseas products. We intend to follow with a separate consultation on how our proposals may apply to overseas products in due course. However, in the meantime, we need to help retail investors understand that some products with sustainability-related terms in their names and marketing may not have an associated sustainable investment label.
- 7.12** We are proposing that where prohibited sustainability-related terms (as set out in Chapter 6) are used in relation to the naming and marketing of overseas products that are recognised schemes, including exchange-traded funds, distributors of those products to retail investors must place a notice on that product, alerting retail investors that: "This product is based overseas and is not subject to FCA sustainable investment labelling and disclosure requirements". The notice must be placed in a prominent place on the relevant digital medium (eg product webpage or page on a mobile application), and be accompanied by a hyperlink to the FCA webpage which will set out what the labelling and disclosure requirements are for retail investors that wish to know more.
- 7.13** This is intended to be a temporary approach in the event that rules for UK funds come into effect before those for overseas products. We intend, however, to follow with a consultation on the approach to overseas products in due course to address this issue.

Q24: Do you agree with our proposals for distributors? If not, what alternatives do you suggest and why?

8 Next steps

- 8.1** As noted throughout this consultation paper, we consider the proposals set out at this stage to be a starting point aimed at addressing immediate harms and helping firms to build their capabilities around sustainability-related disclosures, primarily in the interests of retail investors.
- 8.2** Subject to the outcome of the consultation, we aim to finalise our rules and publish a policy statement by the end of H1 2023.
- 8.3** We intend to build on these proposals and evolve our scope and requirements over time eg in response to domestic, international and market developments. We set out below the areas on which we intend to build on initially, subject to further progress in those areas and the usual consultation processes.
- 8.4** As noted in Chapter 1, this includes expanding the scope of our requirements to overseas products. It also includes expanding requirements to pension products and other investment products marketed to retail investors such as insurance-based investment products (IBIPs). This chapter includes a discussion on considerations which we would particularly welcome stakeholders' views on in respect of pension and other investment products.

Discussion on pension and other investment products

- 8.5** We recognise that the potential harms that we are seeking to address with the proposals in this CP may arise with respect to pension products and other investment products offered to retail investors, such as IBIPs. So, we are considering how we might bring these products into scope of the regime in the future. Our aim is to ensure retail investors have greater transparency on sustainability-related matters with respect to both their direct investments (eg those covered by the proposals in this CP) and their savings (eg pension products).

Pension products

- 8.6** As pension products often have long investment horizons, consumers may want those products to have specific sustainability-related features, and/or may want to know how the firm is managing sustainability-related risks and opportunities.
- 8.7** We introduced climate-related disclosure rules for pension providers and their products in PS21/24, signalling the importance of greater transparency for clients and consumers to help them make informed decisions. The Department for Work and Pensions (DWP) also introduced TCFD-aligned governance and disclosure requirements for larger trustees of occupational pension schemes.
- 8.8** However, there are some important considerations to further explore before applying a labelling and classification regime, as well as accompanying disclosure requirements and naming and marketing rules, to these products.

8.9 Our early view on labelling is that it would be most decision-useful to apply a sustainable investment label to pension products at the level at which the consumer invests, rather than at the pension scheme level. This is consistent with our approach in our TCFD-aligned disclosure. This would, for example, be the level of pre-set strategies such as default pensions arrangements. So, in respect of these rules, the label and accompanying product-level disclosures would apply at the level of the constituent funds.

8.10 If we were to apply the approach for portfolio management arrangements set out in Chapter 3, an overall pension product eg default arrangement would be able to use a sustainable investment label if 90% of the total value of the constituent funds qualified for the same label. However, we recognise that this may not be appropriate for pension products. For example, default arrangements change over time to reflect the change in consumers' retirement journey and risk appetite. So, we are seeking views on what would be a feasible approach for these products.

Q25: What are your views on how labels should be applied to pension products? What would be an appropriate threshold for the overarching product to qualify for a label and why? How should we treat changes in the composition of the product over time?

8.11 We recognise that the approach to labelling will affect how pension providers are able to name and market their products. Our aim is for pension providers to communicate these features in a proportionate manner, to help inform consumers' decisions. We welcome views on whether our proposed naming and marketing rules in Chapter 6 would be sufficient to achieve this outcome for pension products, subject to a potentially lower threshold of constituent funds qualifying for a label for the naming and marketing exemption to apply.

Q26: Do you consider the proposed naming and marketing rules set out in Chapter 6 to be appropriate for pension products (subject to a potentially lower threshold of constituent funds qualifying for a label). If not, why? What would be an appropriate threshold for the naming and marketing exemption to apply?

8.12 We will consider the interaction between labels and disclosures by firms in scope of our rules and disclosures by firms in scope of DWP requirements; eg where trustees of defined benefit schemes delegate investment management to asset managers or life insurers. We welcome views on any challenges or practical considerations that we should take into account.

Q27: Are there challenges or practical considerations that we should take into account in developing a coherent regime for pension products, irrespective of whether they are offered by providers subject to our rules or DWP's requirements?

8.13 With respect to disclosures specifically, our aim is to ensure greater transparency on both sustainability-related features of products and how providers are managing sustainability-related risks and opportunities at entity level. We recognise that providers are already making disclosures in different documents. So, similarly to the proposals in this

paper, we want to reduce the burden on providers while ensuring clients and consumers can easily access sustainability-related information. We welcome views on the extent to which the disclosures outlined in Chapter 5 (ie consumer-facing, pre-contractual, Part B sustainability product report and sustainability entity report (with flexibility to cross refer to group, affiliate or third-party disclosures)) would be appropriate for pension providers.

Q28: To what extent would the disclosures outlined in Chapter 5 be appropriate for pension providers ie do you foresee any challenges or concerns in making consumer-facing disclosures, pre-contractual disclosures and building from the TCFD product and entity-level reports?

8.14 In introducing our TCFD-aligned product-level disclosure rules we took a proportionate approach that excludes the smallest and least popular default strategies from scope (ie those with less than 10% of overall amounts in defaults, or with less than £100 million in assets under management and administration in the default).

8.15 In addition, if the default pension arrangements use life-styling or a number of target date funds for different age profiles, pension providers can calculate metrics and targets based on the most representative profile (provided that they identify and provide a narrative around the risks and opportunities which affect particular cohorts more strongly).

8.16 As these provisions relate specifically to the calculation of product-level metrics, we do not consider them to be necessary in respect of products qualifying for a sustainable investment label and the accompanying disclosures. However, we may consider a similar approach when expanding the regime to introduce a baseline of sustainability-related metrics that firms would be required to disclose for all products, irrespective of whether or not they have a label.

Q29: Do you agree that the approach under our TCFD-aligned product-level disclosure rules should not apply to products qualifying for a sustainable investment label and accompanying disclosures? Would it be appropriate to introduce this approach for disclosure of a baseline of sustainability-related metrics for all products in time?

8.17 We welcome views on any further considerations or practical challenges that we should take into account when expanding our labelling and disclosure regime to pension products. These may be associated with the nature of the products or investments in the product – such as practicalities around products that change over time to reflect consumers' risk appetite – requirements on providers and interaction with existing rules, and distribution channels.

Q30: What other considerations or practical challenges should we take into account when expanding the labelling and disclosures regime to pension products?

8.18 As noted above, we also intend to bring other investment products marketed to retail investors into scope. These include IBIPs and exchange-traded products (ETPs). We are seeking views on whether there would be any challenges in implementing the proposals set out in Chapters 4-7 of this CP to those products. For example, would a threshold of 90% of the total value of constituent funds qualifying for a label be appropriate?

Q31: Would the proposals set out in Chapters 4-7 of this CP be appropriate for other investment products marketed to retail investors such as IBIPs and ETPs. In your response, please include the type of product, challenges with the proposals, and suggest an alternative approach.

Next steps

8.19 In addition to developing proposals to expand the scope of investment products captured under this regime, we will look to expand the regime in the following areas:

- **Overseas products:** We will continue to work with the Treasury to consider options for how to treat overseas products. We intend to follow with a separate consultation on how proposals in this CP might apply in respect of those products.
- **Financial advisers:** We are exploring how to introduce rules for financial advisers aimed at confirming that they should take sustainability matters into account in their investment advice and understand investors' preferences on sustainability to ensure their advice is suitable. We intend to follow with a separate consultation in due course.
- **Listed issuers:** As reiterated in our response to the ISSB's Exposure Drafts, we intend to consult on adapting our TCFD-aligned disclosure rules for listed issuers to reference the ISSB's standards, once finalised and made available for use in the UK. This is consistent with the Government's expectation that the ISSB standards will form the 'backbone' of the corporate reporting element of SDR.
- **Disclosure of transition plans:** We intend to build on our TCFD-aligned disclosure rules, which reference the TCFD's guidance on transition plans. In doing so we intend to draw on the outputs of the Government's TPT.
- **Taxonomy-related disclosure requirements:** We will consider how to update our product-level disclosure requirements to include relevant disclosures once the UK Green Taxonomy is developed.
- **Sustainability-related metrics:** We intend to build on our product-level disclosure requirements, adding a baseline of core sustainability-related metrics for firms to disclose in respect of all products, as further ISSB sustainability disclosure standards are developed.
- **Entity-level disclosures:** We also intend to build on our entity-level disclosure requirements, adding more specificity and granularity to disclosure requirements for different sustainability topics in line with the development of future ISSB standards.

8.20 We acknowledge this is a new regime and we want to work with industry to ensure it is implemented effectively. We will continue to engage via roundtables, webinars etc, considering where we may need to provide further guidance where we can. We also intend to carry out a review to explore how firms have implemented the final rules and will carry out a post-implementation review after three years of the regime coming into force. We welcome views on any additional ways in which we can help industry adapt to the new requirements, to ensure we introduce an effective regime for both consumers and the firms we regulate.

Annex 1

Mapping to SFDR requirements and SEC proposals

Classification and labels

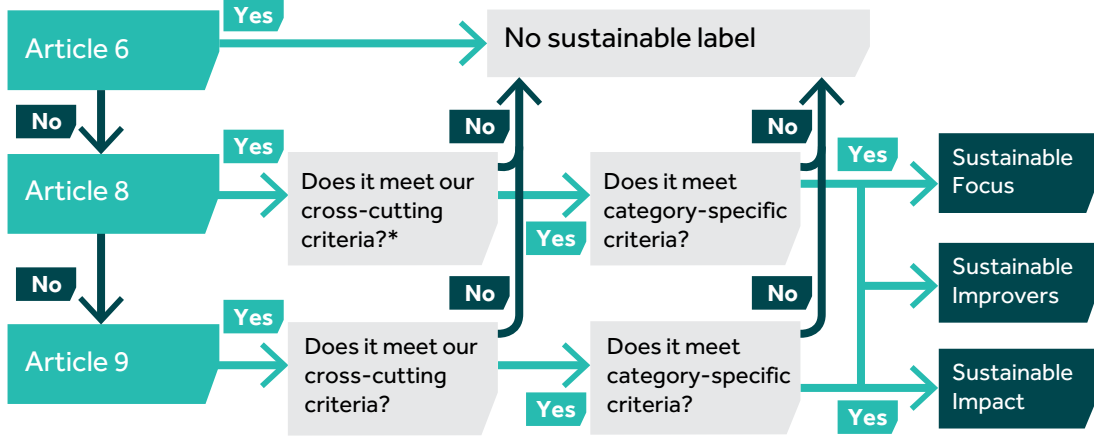
1. We recognise that many UK firms are already subject to the EU SFDR in respect of their EU business and have already invested in systems and processes to classify products according to the SFDR provisions. To help firms leverage the systems investments they have made, respondents to DP 21/4 noted that a mapping of UK product categories to those in the SFDR would be helpful. The SEC has since issued proposals that, similar to the SFDR, categorise products to determine the disclosures that firms are required to make.
2. Since the UK framework is designed as a labelling regime, with detailed criteria to determine eligibility, its starting point is different to both the SFDR and the SEC's proposals. Products that do not meet the qualifying criteria under our proposals will not be able to use any of the sustainable investment labels under our proposed regime. So, there are steps firms will need to consider when determining how a product categorised under the SFDR or SEC's proposals would be treated under our proposals. We set out these steps below.

SFDR

3. The SFDR introduced the following three categories of products with respective disclosure requirements – these have become a de facto classification and labelling system.
 - Article 6 – funds that do not integrate sustainability into the investment process
 - Article 8 – funds that promote, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices
 - Article 9 – funds that have sustainable investment as their objective

4. In considering how to treat a product categorised under SFDR in our proposed regime, firms should follow the steps below:

Is your product?



* Note that Article 8 funds will need to 'level up' to meet our criteria by specifying a sustainability objective. It is unlikely that an Article 8 fund would meet the criteria for Sustainable Impact.

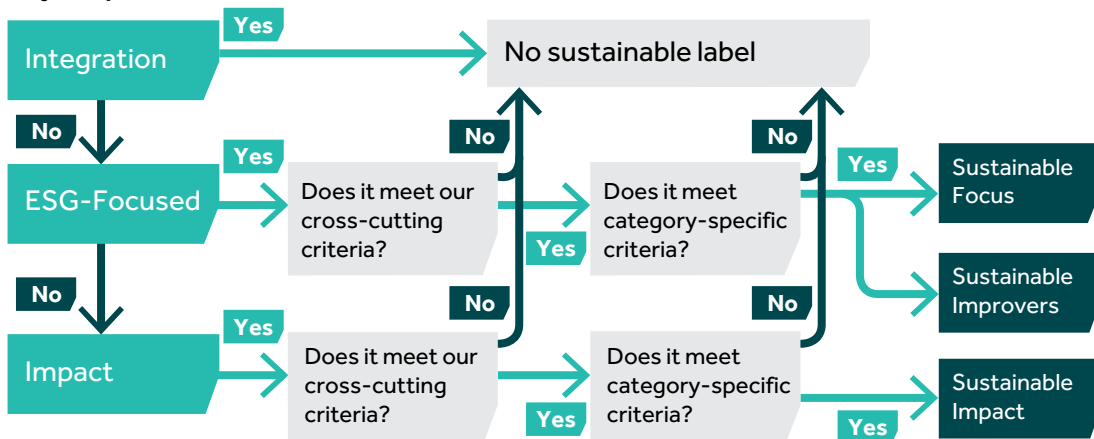
SEC's proposals

5. The US SEC is proposing the following categories of funds with respective disclosure requirements:

- Integration – integrate ESG factors alongside non-ESG factors in investment
- ESG-Focused – ESG factors are a significant or main consideration
- Impact – a subset of ESG-Focused Funds that seek to achieve a particular ESG impact

6. In considering how to treat a product categorised under the SEC's proposals in our regime, firms should follow the steps below:

Is your product?

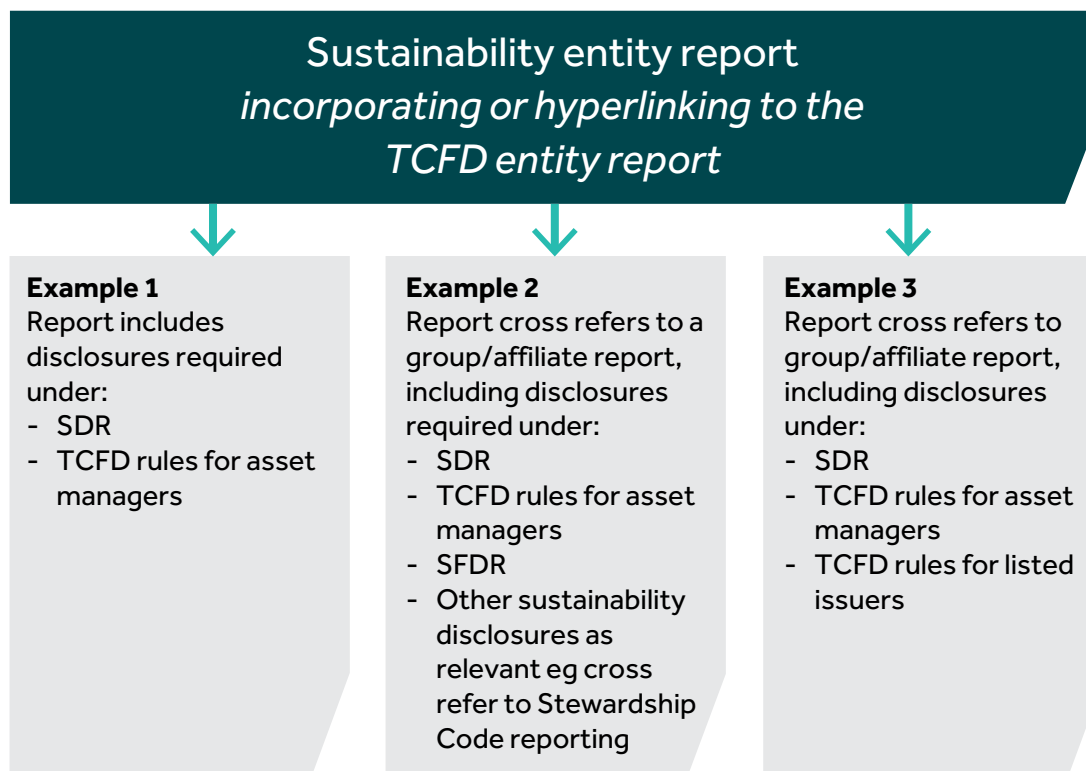


Disclosures

7. As noted above, we recognise that many in-scope firms will need to make disclosures under other regimes internationally. So, we have taken existing and proposed disclosure requirements in other jurisdictions into account in developing our own requirements, as well as wider international developments such as the development of ISSB standards, with a view to remain as coherent as possible while meeting the needs of the UK market. This section focuses on the key similarities and differences between our proposals and the EU SFDR requirements and proposed US SEC requirements. We have focused on these jurisdictions given that they cover a broadly similar scope of firms and products to those proposed in this CP.

Entity-level

8. Our proposed entity-level disclosure requirements build from the TCFD's four pillars. This is consistent with our early views and feedback to our discussion paper (DP21/4). By taking this approach we aim to remain coherent with international standards developed by the ISSB, which also build from the TCFD's framework. Once the ISSB's standards are finalised and adopted in the UK and globally, this approach will support the flow of consistent, comparable and reliable information along the investment chain internationally.
9. This approach does, however, mean that our entity-level disclosure requirements are not fully aligned with the EU SFDR requirements or US requirements for fund advisers. While some overarching disclosure items are in some cases consistent, such as how sustainability factors are integrated into investment decisions, there will be differences in the overall structure and content of our proposals. For example, the key difference is that we are not requiring disclosure of principal adverse impacts. Rather, we intend to update our disclosure requirements as appropriate in line with the development of more specific ISSB standards.
10. Nevertheless, we want to reduce the burden on firms producing disclosures while ensuring clients and consumers receive decision-useful information at the level of consolidation that is most relevant, given the global nature of firms' business and some sustainability-related topics. So, we are proposing that firms can make the entity-level disclosures (in respect of how the firm takes sustainability-related matters into account in managing investments on behalf of clients and consumers) in a group or affiliate report that includes other sustainability-related disclosures, provided that the cross referencing and other requirements in Chapter 5 are met. Sustainability entity reports may therefore include information as presented in the (non-exhaustive list of) examples below with appropriate cross referencing, but must include a compliance statement confirming that the disclosures comply with our requirements:



Product-level

SFDR

11. As noted in the section above the starting point for our regime is different to SFDR, SFDR was intended to be a disclosure regime only, while our regime introduces a labelling regime to help protect consumers. Accordingly, our disclosure requirements are associated with the qualifying criteria that firms are required to meet to use a label.
12. Both our proposals and the SFDR require disclosures to be made in similar types of document: pre-contractual, website disclosures and periodic disclosures. However, while the SFDR has introduced templates for many of the disclosures, we are not proposing to mandate a template this early stage, and instead encourage industry to do so if considered helpful to firms.
13. As set out in the table below, firms making product-level disclosures under SFDR will need to make disclosures under many of the same disclosure items as required under our proposals. In some cases, however, our proposals require more granular information eg particularly under investment policy and strategy to provide greater transparency on the firm's asset selection processes and criteria.
14. There are also some disclosure items required under the SFDR disclosures that we are not proposing in this CP. These include: 'do no significant harm' (DNSH), which we consider may be too restrictive at this stage; Taxonomy-alignment, which we will consider once developed in the UK; and principal adverse impacts, as we will consider introducing a baseline of sustainability metrics that all products will be required to disclose in line with the development of ISSB standards.

| Firms making SFDR product-level disclosures will be considering... | Is this required under SDR proposals? |
|--|---|
| Sustainable investment objective; E or S characteristics of the product | Yes – Principle 1: sustainability objective |
| Monitoring sustainability objective; E or S characteristics (sustainability indicators) | Yes – Principle 3: KPIs |
| DNSH | No – see Chapter 5 |
| Principal adverse impacts | No – see Chapter 5 |
| Investment strategy | Yes – Principle 2: investment policy and strategy |
| Asset allocation/proportion of investments that promote E or S characteristics (including use of derivatives) | Yes – Principle 2: investment policy and strategy |
| Taxonomy-alignment | No – see Chapter 5 |
| Methodologies, data sources and processing, limitations to methodologies and data | Yes – Part B sustainability product report |
| Due diligence | Yes – Principle 4: governance and resources |
| Engagement policies (where part of strategy) | Yes – Principle 5: stewardship |
| Reference benchmarks | Yes – Principle 2: investment policy and strategy |
| Extent to which E or S characteristics/sustainable investment objective were met (performance of sustainability indicators) | Yes – Principle 3: KPIs |
| Proportions of investments (eg top investments; those that attained E or S characteristics/met the objective; those in different economic sectors and sub-sectors; Taxonomy-aligned) | No |
| Performance against designated reference benchmark | Yes – Principle 3: KPIs (eg where a benchmark has been designated as a performance indicator) |
| Historical comparison | Yes – Part B sustainability product report |
| Information on underlying investment options | No |

SEC proposals

15. The SEC's proposed regime is also focused on categorisation of products to determine disclosure requirements. However, we have sought to remain consistent with the disclosures and approach to the extent appropriate. For example, some key similarities in our approach include 'tiering', whereby firms would be required to set out a summary of information, followed by more detailed disclosures. Both regimes also require disclosures to be made in pre-contractual disclosures (ie the prospectus) as well as periodically.
16. Firms making disclosures under the SEC proposals will broadly need to make disclosures under the same disclosure items as required under our proposals, as set out in the table below.
17. However, while the SEC is proposing that disclosures on ESG strategy be set out in a table, we are not proposing to introduce a table or template for any of our disclosure requirements at this stage. Rather we are proposing to set parameters around the

format of disclosures and require disclosures under certain categories of information to ensure consistency, while giving firms some flexibility.

- 18.** The other key difference is that we are not requiring XBRL tagging for machine readability at this stage, based on stakeholder feedback to our discussion paper that while considered useful, it may be premature to do so for this regime.

| Firms making SEC fund-level disclosures will be considering... | Is this required under SDR proposals? |
|---|--|
| Integration Funds: disclosures on how ESG factors are incorporated into investment processes | No specific disclosures (see Chapter 4) |
| ESG strategy (eg tracks an index, applies an inclusionary/exclusionary screen, seeks to achieve a specific impact, proxy voting, engagement, other) | Yes – Principle 2: investment policy and strategy |
| How ESG factors are incorporated into investment decisions | Yes – Principle 2: investment policy and strategy |
| How the Fund votes proxies and/or engages with companies about ESG issues | Yes – Principle 5: stewardship |
| GHG emissions (where relevant) – data sources, estimated data, methodologies | Yes – Principle 3: KPIs TCFD product report disclosures |
| Impact Funds: impact intention within investment objective, relationship between impact and financial return | Yes – Principle 1: sustainability objective |
| Impact Funds: progress towards achieving impact | Yes – Principle 3: KPIs |
| Periodic reporting on proxy voting/engagement (where significant) | Yes – Principle 3: KPIs |

Consumer-facing disclosures

- 19.** As set out in Chapter 5, we acknowledge that there may be different types of disclosures for consumers based on requirements in different jurisdictions (eg the EU SFDR). Our requirements have been informed by several rounds of behavioural research and stakeholder feedback, and we consider parameters set out under proposals will result in disclosures that meet the needs of retail investors. Our consumer-facing disclosures also accompany the sustainability investment label and so are tailored to provide key information that will help consumers better understand the sustainability-related features of a labelled product, where a label is used.
- 20.** So, we consider it appropriate to require firms to produce a separate consumer-facing disclosure for in-scope products. We encourage firms to consider the Occasional Paper on Sustainability Disclosure Requirements when producing these disclosures.

Annex 2

Cost benefit analysis

Introduction

1. FSMA, as amended by the Financial Services Act 2012, requires us to publish a cost benefit analysis (CBA) of our proposed rules. Specifically, section 138I requires us to publish a CBA of proposed rules, defined as 'an analysis of the costs, together with an analysis of the benefits that should arise if the proposed rules are made'.
2. This analysis presents estimates of the significant impacts of our proposal. We provide monetary values for the impacts where it is reasonably practicable to do so. Where it isn't reasonably practicable, we provide estimates of outcomes in other dimensions. Our proposals are based on carefully weighing up these multiple dimensions and reaching a judgement about the appropriate level of consumer protection, taking into account all the other impacts we foresee.

Our analytical approach

3. To understand the impact of the proposed rule changes set out in Chapters 3-7, this CBA considers:
 - the likely benefits to asset managers, clients and consumers of their products, distributors and the wider market
 - the likely compliance costs to asset managers, distributors and other regulated firms in scope
4. As a regulator, we will also incur costs from supervising against the new rules. We will assess the resource implications as part of our annual business planning.
5. The analysis presented below has been produced using assumptions and averages set out in "Baseline and key assumptions" section. We also used evidence from the following sources:
 - Morningstar fund data: We estimate the number of UK-based funds affected by the labelling and naming and marketing rules to be approximately 450. This figure was found by (i) filtering Morningstar fund data for key sustainability-related terms in their name or objectives (eg 'sustainable', 'ESG') and (ii) limiting the sample to funds that are actively marketed in the UK.
 - FCA data on asset managers, including wealth managers, and distributors carrying out activities in scope of our proposals as at the time of writing the CP
 - Information gathered from a small sample of large and medium sized firms that will be affected by our rules. We asked for feedback on the likely actions they will need to take to comply with our proposed rules, the business areas that are likely

to be affected and the costs they are likely to incur. Firms were able to provide an overview of the likely impact on their business and either estimates of the costs or resources they would need to implement the proposals.

Problem and rationale for intervention

6. We describe the problem and rationale for intervention in Chapters 1 and 2. As noted, we are concerned that the market for sustainable investment products is difficult for consumers to navigate, there is a lack of trust, and potential harm to consumers due to greenwashing. The market for sustainable investment products is diverse, offering welcome consumer choice. There is a risk, however, that consumers' sustainability-related needs and preferences are not being met. We consider that these harms arise from market failures, including:
 - *Lack of standardisation in product information.* There is a lack of standardised reporting on sustainability objectives and strategies. This makes it difficult for consumers to determine what each product is seeking to achieve, and which strategies are being pursued. Firms also frequently use certain terms interchangeably to describe their products and strategies – eg, 'ESG', 'responsible' or 'sustainable' – making it difficult for consumers to understand or compare products.
 - *Asymmetric information.* Clients and consumers may not receive clear information on how the firm is managing sustainability-related risks and opportunities, or the sustainability-related features of investment products. Firms may voluntarily disclose less information than clients and consumers might prefer, due to the coordination failures mentioned below, and the cost of making extensive disclosures.
 - *Coordination failure among firms.* A firm may be disincentivised to be a 'first-mover' in making sustainability-related disclosures voluntarily. They may fear reputational damage or an adverse market response if they are perceived not to have considered sustainability-related risks and opportunities appropriately in managing their investments, or not to have invested in line with clients' and consumers' sustainability-related expectations.
 - *Coordination failure among clients and consumers.* Clients and consumers may have insufficient bargaining power, and may be unable to coordinate effectively to encourage a market-led improvement in sustainability-related disclosures and labels across firms. Disclosures and labels will then be determined by the firms' own private incentives.
7. The causal chain set out in Chapter 1 (Figure 1) shows that introducing new sustainability-aligned disclosure and labelling rules should advance our objectives and lead to better outcomes for consumers.
8. Intervention to address the harms flows directly from our strategic objective to ensure that the relevant markets function well, as well as advancing our operational objectives:
 - The disclosure requirements should facilitate the flow of information along the investment chain, increasing transparency in the market and furthering our objective to promote market integrity.

- Sustainable investment labels, the consumer-facing disclosures, and rules for distributors should help to protect consumers by equipping them to identify products that meet their needs and preferences and navigate the market more effectively. The naming and marketing rules should similarly help to protect consumers by reducing the risk of greenwashing.
- The labels and consumer-facing disclosures should help consumers to compare products more effectively, potentially leading to greater competition in the market, in line with our objective to promote competition in the interests of consumers.

9. Our proposals are designed to address the market failures specified above. In particular, the sustainable investment labels along with product-level disclosures will provide a framework for greater standardisation of product information. The product and entity disclosure requirements will facilitate narrowing the information gap between clients and consumers and their providers, whilst the expectations on distributors should further enhance this process by ensuring consumers can access the relevant product-level information. Overall, our intervention should also facilitate coordination both among firms and their clients and consumers as it requires firms to shift towards a more transparent landscape of investment products and sustainability risks and opportunities.

10. Our proposals also support the expectations set out in our remit letter from the Chancellor, for the FCA to 'have regard to the Government's commitment to achieve a net-zero economy by 2050 under the Climate Change Act 2008 (Order 2019) when considering how to advance its objectives and discharge its functions'.

Summary of proposals

11. Our proposals are set out in Chapters 3-7 along with feedback to our discussion paper DP21/4.

12. We propose to consult on the following main areas:

- **Sustainable investment labels** to help consumers navigate the investment product landscape and enhance consumer trust.
- **Consumer-facing product-level disclosures** to help consumers understand the key sustainability-related features of a product.
- **Detailed disclosures at both product and entity level** targeted at a wider audience (eg institutional investors or retail investors seeking more information):
 - **pre-contractual disclosures** (eg fund prospectus), covering the sustainability-related features of investment products
 - **ongoing sustainability-related performance information**, in a sustainability product report
 - **a sustainability entity report** covering how firms are managing sustainability-related risks and opportunities at entity-level
- **Naming and marketing rules** restricting the use of certain sustainability-related terms in product names and marketing materials for products that do not use a label.
- **Requirements for distributors** to ensure that product-level information (including the labels) is made available to consumers.
- **A general 'anti-greenwashing' rule** applied to all regulated firms which reiterates existing rules to clarify that sustainability-related communications must be clear, fair and not misleading.

13. We are proposing that the anti-greenwashing rule comes into effect immediately on publication of the PS (ie provisionally 30 June 2023), and that rules for labelling, consumer-facing disclosures, pre-contractual disclosures and naming and marketing rules apply one year later (ie from 30 June 2024). Ongoing performance-related information in the sustainability product report must be published a further year later (30 June 2025). We propose to phase-in the entity-level requirements, initially requiring disclosures by the largest firms (asset managers with over £50 billion in AUM) from 30 June 2025 and smaller firms (with over £5 billion in AUM) one year later.

Firms in scope of the requirements and key assumptions

14. A breakdown of in-scope firms and products is included in Chapter 3. For the purposes of this CBA, we have grouped them according to which areas of our rules (as listed in the summary section above) apply. Table 1 presents a summary of affected firms and their estimated population and size.

Table 1

| Firm type | Policy components and firm features | Firm population | Firm size | Sub-population label |
|-----------------------|---|-----------------|-----------|----------------------|
| Asset managers | Firms affected by: <ul style="list-style-type: none"> Sustainable investment labels Consumer-facing disclosures Detailed product-level disclosures (pre-contractual and ongoing sustainability-related performance ie Part B of the sustainability product report) | 25 | medium | A |
| | Firms affected by: <ul style="list-style-type: none"> Naming and marketing rules Consumer-facing disclosures whose funds: <ul style="list-style-type: none"> do not use labels use prohibited terms | 49 | medium | B |
| | Firms affected by: <ul style="list-style-type: none"> Naming and marketing rules Consumer-facing disclosures whose funds: <ul style="list-style-type: none"> do not use labels do not use prohibited terms | 87 | large | C |
| | Firms in scope of portfolio management rules | 1,471 | medium | D |
| Asset managers | Entity-level disclosures – sustainability entity report | 37 | large | E |
| | | 135 | medium | F |
| Advisors | Expectations on distributors | 250 | large | G |
| | | 5,523 | medium | H |
| Platforms | | 34 | large | I |
| Other regulated firms | General 'anti-greenwashing' rule | 100 | medium | J |
| | | 42,148 | small | K |

15. Whilst our requirements for labels and product-level disclosures will be applied on a fund-by-fund basis, we estimate costs on a firm-by-firm basis to reflect that asset managers who manage multiple funds are likely to be able to benefit from economies of scale, ie applying our rules to one fund should facilitate applying them to other funds and thus lower the per-fund costs of compliance. We calculated costs based on an average firm size (ie medium) and an average number of managed funds per firm in our data (ie the 450 funds with sustainability-related terms in their names, resulting in 74 firms managing around six funds each).
16. Please also note that some of the subpopulations listed in the table overlap, specifically: *C* and *D* comprise all firms carrying out in-scope asset management activities (see Chapter 3). *A* and *B*, and *E* and *F* are a subset of these firms. This has implications for how we calculated some of the costs.
17. Subpopulations *J* and *K* from Table 1 includes all firms in scope of the general 'anti-greenwashing rule' outside the scope of our other rules proposed in this paper. We expect the vast majority of large and medium firms regulated by the FCA to be captured by the latter. As we also expect the rule to impose a minimal burden on the firms, we treat all the firms in subpopulation *K* as small for the cost estimations.
18. The asset managers in-scope of the proposals represent £10.6 trillion in total assets under management in the UK.

Baseline and key assumptions

19. Our CBA is subject to several uncertainties and assumptions:
20. **Calculating costs:** The incremental costs of meeting our proposed requirements were calculated using the Standardised Cost Model. The assumptions we used for the model reflected both the feedback we received from several firms which responded to our request for information and other internal FCA data.
21. **Firms choosing to use the label:** Of the firms that currently use sustainability-related terms in their names and marketing, we do not know how many will choose to use the sustainable investment labels for their in-scope products and how many will instead choose to no longer use sustainability-related terms. While we expect firms will be incentivised to use the labels so as to be able to continue using sustainability-related names and marketing, we expect some may not. This may be due to not being able to meet the qualifying criteria, the impact on costs and resources, not wanting to be a first-mover etc. So, for the purposes of this CBA we assumed that a third of the products (and corresponding firms) that currently have sustainability-related terms in their names and marketing will use the sustainable investment labels under our rules, and two thirds will amend their naming and marketing accordingly.
22. **Incremental costs from building from TCFD:** The sustainability product and entity reports under our proposals build from the TCFD product and entity reports introduced in our TCFD-aligned disclosure rules, and apply to a broadly similar scope of asset managers. (As noted in Chapter 8, we intend to expand the regime to FCA-regulated asset owners, in due course). Therefore, we expect firms will already have some capabilities and structures (eg IT structures) in place to help produce these reports. The main difference is that all firms that use a sustainable investment label will

be required to produce a sustainability product report (as well as pre-contractual and consumer-facing disclosures), and this may include firms with under £5 billion in AUM.

- 23. Sourcing data:** We recognise that data availability remains a major challenge. So, we are not proposing to impose sustainability-related metrics on firms at this stage. Where firms are disclosing metrics/KPIs to demonstrate performance against a stated sustainability objective, or provide consumers with additional information on their approach, we expect the firm to have access to the relevant data – or to use proxies or assumptions, provided that the methodologies and limitations are explained. Some firms may use third party data sources and incur costs in doing so. We do not, however, consider these to be considerable incremental costs resulting from our proposed requirements. We expect firms to already have sight of how a product named or marketed using sustainability-related terms is performing against those claims.
- 24. Resourcing:** We recognise that there are a number of different approaches that firms may wish to take to comply with our proposed rules. For instance, depending on their existing resources and capabilities, some firms may rely on hiring new staff or reallocating existing staff and resources, while others may seek third party advice eg external consultants. The resourcing costs are captured in our estimates as training, project change, and IT change costs.

Summary of costs and benefits

- 25.** In the sections below, we present the potential benefits and costs that arise from our proposals. First, we describe the benefits. This is a summary of the outcomes and benefits discussed in Chapters 1 and 2 of the CP. We also present the estimated one-off and ongoing (annual) compliance costs arising from each of the elements of the proposed framework. They reflect the incremental changes that firms would not have undertaken had we not introduced our proposals.

Benefits

- 26.** As described in our causal chain analysis, many of the benefits, by their nature, will be indirect, accruing from better market functioning over the long term. We do not consider that it is reasonably practicable to quantify the benefits of our proposals at this stage, prior to introduction. We will however measure the benefits and success of our intervention as set out under the 'measuring success' section of Chapter 1. The benefits we expect are as follows:
- 27. Reduced greenwashing and increased consumer protection.** Together the labelling, disclosure, naming and marketing rules should help protect consumers from greenwashing. Restricting the use of sustainability-related terms in product names and marketing unless the product qualifies for and uses a label will require firms to reflect on the sustainability-related features of the product, the objective (if any) it may be seeking to achieve and the primary channel by which it can plausibly achieve or encourage positive sustainability outcomes. This should result in naming, marketing and disclosures that better reflect the sustainability-related features of the investment product. In addition, our anti-greenwashing rule reiterates that sustainability-related claims in all communications – by all regulated firms in respect of their products and services – must be proportionate to the sustainability profile of the product or service.

- 28. Increased provision of standardised sustainability-related information.** Our labelling regime requires firms to use clear and objective criteria to determine whether a product qualifies for a sustainable investment label. This should help firms to take a consistent approach to categorising their products. It should also give consumers better confidence that a sustainable-labelled product is meeting certain criteria, and enable consumers and other stakeholders (eg NGOs) to hold firms to account for their sustainability-related claims. Further, the product and entity-level disclosure requirements are designed to provide greater consistency in the information disclosed to clients and consumers.
- 29. Consumers better navigate the market and make more informed decisions.** The labels and consumer-facing disclosures should also help consumers better navigate the market for sustainable investment products, identify products that meet their needs and preferences, and in turn build trust in the market. Distributors play a key role in ensuring this information is made available to consumers. Some respondents to our CBA questionnaire also consider the labels and consumer-facing disclosures will help to provide useful clarity to advisers. In addition, the entity-level disclosures should provide greater transparency about how firms are managing sustainability-related risks and opportunities in their investment decisions and are likely to help both clients and consumers take those factors into account when granting investment mandates and selecting products. Given the global reach of firms operating in the UK and flexibilities we are providing in our proposals, better transparency is likely to benefit clients' and consumers' decision-making internationally.
- 30. Better informed capital allocation and asset pricing.** Both the labelling regime and disclosures framework should promote a more structured approach to the consideration of sustainability-related features of investment products, and how sustainability-related risks and opportunities are managed at entity level. This should encourage an ecosystem of service providers to emerge, driving innovation and thought leadership to support high-quality sustainability-related disclosures. It should also support a coordinated flow of information along the investment chain, resulting in better assessment of sustainability-related risks and opportunities across the market. Better transparency should therefore help markets price assets more accurately and allocate capital more effectively.
- 31. Better labelling and transparency can help facilitate an orderly transition to a more sustainable future.** More informed pricing of assets and allocation of capital should lead to a smoother transition to a lower-carbon, more sustainable economy with less exposure to abrupt market corrections. In addition, clients and consumers should be better able to hold firms to account for their sustainability-related claims. This should encourage them to label and disclose the sustainability-related features of investment products accurately, manage sustainability-related risks and opportunities effectively, and direct capital towards projects and activities that better support the transition to a more sustainable future.

Costs

- 32.** All the per firm costs reported in the following sections have been rounded to the nearest hundreds, whilst the industry costs to the nearest hundreds or tens of thousands. Due to rounding differences, some of the aggregate figures might not be the exact sum of the individual components.

Table 2: Estimated compliance costs to firms in scope

| Firm type | Policy components and firm features | One-off costs | | Ongoing costs | |
|-----------------------|--|-----------------------------|-----------------------|-----------------------|-----------------------|
| | | Present Value for industry* | Average cost per firm | Annually for industry | Average cost per firm |
| Asset managers | Firms affected by: <ul style="list-style-type: none"> Sustainable investment labels Consumer-facing disclosures Detailed product-level disclosures (pre-contractual and ongoing sustainability-related performance ie Part B of the sustainability product report) | £8.4m | £338,000 | £5.4m | £216,100 |
| | Firms affected by: <ul style="list-style-type: none"> Naming and marketing rules Consumer-facing disclosures whose funds: <ul style="list-style-type: none"> do not use labels use prohibited terms | £11.3m | £230,600 | £0.3m | £6,800 |
| | Firms affected by: <ul style="list-style-type: none"> Naming and marketing rules Consumer-facing disclosures whose funds: <ul style="list-style-type: none"> do not use labels do not use prohibited terms Firms in scope of portfolio management rules | £31.5m | £20,200 | £11.5m | £7,400 |
| Asset managers | Entity-level disclosures – sustainability entity report | £2.6m | £15,200 | £1.6m | £9,300 |
| Advisers | Expectations on distributors | £63.4m | £11,000 | £7.2m | £1,200 |
| Platforms | | £14.8m | £435,900 | £0.6m | £18,400 |
| Other regulated firms | General 'anti-greenwashing' rule | £14.7m | £300 | - | - |
| Total | | £146.7m | | £26.7m | |

* As the medium-sized asset managers come into scope of entity-level disclosure requirements in year 2 after introduction, this is the only discounted one-off cost.

33. To get a perspective on the size of the costs, we can compare them to the total assets under management of the in-scope firms. The estimated total one-off costs of compliance are equivalent to 0.0014% of the total assets under management (AUM) of all asset managers in scope (as listed in subpopulations C and D), whilst the estimated total ongoing costs of compliance are equivalent to 0.0003% of AUM of the same group of firms. Note that these firms are manufacturers of products distributed by advisers and platforms. In this context, we consider the expected benefits and improvements to the market functioning as a result of our proposals are likely to exceed the compliance costs over the medium and long time period.

34. The remainder of this section describes in more detail the approach we have taken to calculating costs and the assumptions that we have made.

Summary of one-off and ongoing compliance costs

35. Table 3 shows a summary of the one-off and ongoing compliance costs:

| Estimated costs | Totals |
|--|---------------|
| Familiarisation and gap analysis | |
| Asset managers and distributors: <ul style="list-style-type: none"> • Small: £800 • Medium: £4,500 • Large: £13,700 | |
| Other regulated firms (in respect of the anti-greenwashing rule): <ul style="list-style-type: none"> • Small: £300 • Medium: £1,300 | £28.7m |
| Training | |
| Asset managers and distributors: <ul style="list-style-type: none"> • Small: £700 • Medium: £3,800 • Large: £7,400 | £11.5m |
| IT changes | |
| Asset managers using a label: <ul style="list-style-type: none"> • Medium: £118,000 | £2.95m |
| Asset managers not using a label but amending product naming and marketing: <ul style="list-style-type: none"> • Medium: £118,000 | £5.8m |
| Other firms producing consumer-facing disclosures and firms in scope of portfolio management rules: <ul style="list-style-type: none"> • Medium: £3,000 • Large: £17,800 | £5.9m |
| Asset managers in scope of entity level disclosures: <ul style="list-style-type: none"> • Medium: £3,000 • Large: £17,800 | £1m |
| Distributors: <ul style="list-style-type: none"> • Platforms: £213,900 • Advisers: £59,000 | £22m |
| | £37.7m |
| Change and governance | |
| Asset managers using a label: <ul style="list-style-type: none"> • Medium: £216,100 | £5.4m |
| Asset managers not using a label but amending product naming and marketing: <ul style="list-style-type: none"> • Medium: £108,800 | £5.3m |
| Other firms producing consumer-facing disclosures and in scope of portfolio management rules: <ul style="list-style-type: none"> • Medium: £6,800 • Large: £18,400 | £11.5m |

| Estimated costs | Totals |
|--|---------------|
| Asset managers in scope of entity level disclosures: <ul style="list-style-type: none"> • Medium: £6,800 • Large: £18,400 | £1.5m |
| Advisers: <ul style="list-style-type: none"> • Medium: £108,800 • Small: £2,000 | £38.2m |
| Platforms: £200,800 | £6.8m |
| | £68.8m |
| Ongoing costs | |
| Asset managers using a label: <ul style="list-style-type: none"> • Medium: £216,100 | £5.4m |
| Other firms by firm size: <ul style="list-style-type: none"> • Large: £18,400 • Medium: £6,800 • Small: £1,000 | |
| Firms producing consumer-facing disclosures (including those that amended sustainability-related terms in naming and marketing in year one) and firms in scope of portfolio management rules | £11.9m |
| Asset managers in scope of entity level disclosures | £1.6m |
| Distributors | £7.8m |

One-off compliance costs: details

36. In developing our proposals, we have taken into account existing requirements on firms. While the regime introduces several new requirements – eg labelling, classification and disclosures – many of these are grounded in existing rules and expectations. For example:

- **General 'anti-greenwashing' rule.** This clarifies the principle on clear, fair and not misleading communications (PRIN 2.1, Principle 7, and COBS 4.2.1) with respect to sustainability-related claims.
- **Qualifying criteria for labels.** These are broadly based on the Guiding Principles set out in our Dear Chair letter to authorised fund managers in July 2021. The Guiding Principles themselves set out how existing rules in COLL and SYSC apply in the context of sustainable investment funds, including on investment objectives and policy, disclosure and resourcing.
- **Disclosures.** The sustainability product report and sustainability entity reports broadly build from TCFD product and entity reports, for which in-scope firms will already be building processes to produce. In response to our questionnaire, some firms based costs for our proposed disclosures on costs to produce disclosures required under SFDR. We note that the SFDR requires firms to disclose several sustainability-related metrics, which we expect will drive up data costs. We are not requiring any sustainability-related metrics at this stage (beyond those associated with firms' stated sustainability objective) and therefore expect costs to be lower. However, all firms will incur costs to produce consumer-facing disclosures, which are a new standalone disclosure.

- **Rules for distributors.** These are similar to existing expectations on distributors to make product-level information available to retail investors.

We recognise that firms may nevertheless incur costs to familiarise themselves with our proposals, classify and label their products if they choose to do so, amend naming and marketing for non-labelled products, and make relevant disclosures. We list below the main drivers of costs and our estimates which are based on the Standardised Cost Model.

Familiarisation and gap analysis

37. We expect firms will incur costs to familiarise themselves with our proposed rules and to perform a legal review along with a gap analysis. We estimate that large, medium, and small firms will need to respectively assign 20, 5, and 2 compliance staff to reading the consultation paper, as well as 4, 2, and 1 legal team member to perform a gap analysis, for which we further assume that they will require 4, 3, and 1 day per team member to review 50 pages of legal text. Based on our standardised assumptions, we calculate costs for all of the estimated in-scope 1,558 asset managers, 34 platforms, and 5,773 advisers, ie the following subpopulations defined in Table 1: C, D, G-I. The average cost of familiarisation and gap analysis per firm is estimated at £800 for small, £4,500 for medium, and £13,700 for large entities.
38. We also expect that all remaining FCA-regulated firms (subpopulations J and K) will need to broadly familiarise themselves with our new anti-greenwashing rule. We assume that medium and small firms will need to respectively assign 4 and 1.5 full time equivalent compliance staff to reading the consultation paper. We estimate the familiarisation cost in this group per medium firm at £1,300 and per small firm at £300.
39. Taking into account the length of this CP and the legal instrument, we estimate these costs to be around £28.7m in total to all firms in scope.

Training

40. To comply with our proposals on labelling, disclosures, naming and marketing we expect firms to incur costs to train their staff. We estimate that large, medium, and small firms will need to provide bespoke training to 10, 5, and 1 staff member respectively. We expect asset management firms to provide separate training for staff teams that manage products in scope of our requirements. Respondents to our questionnaire noted that training may be needed across other teams such as compliance, marketing, data and legal teams. Some confirmed that they will not need to hire any new permanent staff. They may, however, seek external (third-party) advice. We also expect distributors to train their staff on the new expectations.
41. So, we expect the following subpopulations defined in Table 1 to undertake this training: A-D, G-I.
42. Using our standardised assumptions, we estimate training costs of £11.5m across the affected population. The average cost per firm is estimated at £700 for small, £3,800 for medium, and £7,400 for large entities.

IT Changes

43. If firms choose to label their investment products as sustainable, they may incur some discretionary costs in updating their IT systems to implement changes eg for

both the detailed and consumer-facing disclosures. We note that some – particularly smaller and some medium – firms may use third party/external tools and systems to do so. We expect these costs to be moderate and, using our standard assumptions, estimate them to be £2.95m (subpopulation A). We estimate the average per firm cost at £118,000.

44. Similarly, we expect firms that use sustainability-related terms in their product names and marketing but decide not to pursue labelling will need to update their IT systems to remove the prohibited terms. We expect these costs to be moderate, using our standard assumptions, and estimate them to be £5.8m (subpopulation B). The average cost per firm is estimated again at £118,000.
45. We expect firms that do not use sustainability-related terms in their names and marketing, but which will nevertheless be required to produce consumer-facing disclosures, to incur a small cost to enable them to do so. We also expect portfolio managers that will need to make disclosures of underlying in-scope products available to consumers to incur a small cost. We estimate these costs using our standard assumptions to be £5.9m (in total for subpopulations C and D). The average cost per firm is estimated at £17,800 for large entities and £3,000 for medium entities.
46. In addition, we expect small updates to IT systems will be needed to make entity-level disclosures. We estimate the net present value of these costs for the large and medium asset managers (in total for subpopulations E and F) to be £1m. Please note that this cost is discounted at a standard government green book rate of 3.5% for medium-sized asset managers that come into scope of our rules from year 2 after their introduction. The average cost per firm is estimated at £17,800 for large entities and £3,000 for medium entities.
47. Distributors in scope of our requirements will also need to implement relatively minor changes to their IT systems to make the label and consumer-facing disclosures available to retail investors, as we expect them to already have processes and systems in place to provide information to clients and consumers. Specifically, we expect that large platforms will need to devote to implementation 546 person-days and medium-sized advisers 156 person-days. We expect that this work is usually carried out across a team of people in large firms, and for most of the costs to come from programmers' work. We estimate these overall costs to be £22m (for subpopulations G-I; note however that we expect small advisers' IT costs to be negligibly small). The average cost per firm is estimated at £213,900 for platforms and £59,000 for medium-sized advisers.
48. So, we estimate the total cost for IT changes for all firms in scope to be £37.7m.

Change and governance

49. Firms that decide to use sustainable investment labels (subpopulation A) will need to translate and operationalise our qualifying criteria into concrete actions and ensure there is appropriate governance to ensure compliance. Our qualifying criteria are based on the Guiding Principles set out in our Dear Chair letter which reiterates existing requirements, so should be broadly familiar to firms and many of them may already be met. However, firms will need to review whether and how those criteria are met in respect of each product that uses a label, and in some cases take additional steps to meet them. In addition, they will need to prepare consumer-facing and detailed product-level disclosures for each labelled product. Firms that responded to this part of

our questionnaire clarified that they are likely to use existing governance structures to oversee these changes. However, costs may be incurred due to increased management oversight or establishing project teams. We assume a moderate size of the project and estimate the cost using the Standardised Cost Model. We estimate the total cost of the changes and governance to be £5.4m and the average per firm cost at £216,100.

50. Firms that use sustainability-related terms in their product names and marketing materials, but choose not to label those products (subpopulation *B*), will need to remove those prohibited terms and produce consumer-facing disclosures. We estimate these changes to be minor at a total cost to the firms in scope at £5.3m and the average per firm cost at £108,800.
51. While firms that choose to withdraw sustainability-related claims from the naming and marketing materials for their products might expect to lose some of their customers, we assume that these customers will switch to products manufactured by the same firm or other firms that comply with our proposed requirements. Therefore, the switching will not affect the overall cost of the proposals.
52. For firms managing funds without sustainability-related terms in their names and marketing ie those that only need to prepare consumer-facing disclosures and comply with our naming and marketing rules going forward, as well as those in scope of portfolio management rules, we estimate small costs amounting to £11.5m (subpopulations *C* and *D*). The average cost per firm is estimated at £18,400 for large firms and £6,800 for medium firms.
53. In addition, we consider that firms in scope of entity-level disclosure requirements will incur small governance-related costs. We estimate the costs at £1.5m (subpopulations *E* and *F*) with an average cost of £18,400 per large firm and £6,800 per medium firm.
54. Finally, distributors may also incur some governance-related costs to meet our requirements. Advisers and platforms are likely to already have processes in place to make product-level information available to retail investors. These will need to be adjusted and tailored to convey the sustainability-related information clearly to consumers. Further, we expect distributors (particularly those which are not execution-only platforms) may need to be ready to respond to consumer queries about the sustainability-related features of the products that they offer. Using standard assumptions we estimate the overall cost to advisers (subpopulations *G* and *H*) at £38.2m with an average per firm cost of £108,800 per medium and £2,000 per small entity; and the overall cost to platforms (subpopulation *I*) at £6.8m with an average per firm cost of £200,800.
55. We estimate the overall cost of managing change and governance in respect of our proposals for all firms in scope at £68.8m.

Ongoing costs: details

56. Our proposed SDR and investment label rules are also likely to create ongoing annual costs for in-scope firms eg to ensure continued compliance and appropriate product reviews. We classified these ongoing costs as the 'change and governance' category. The relevant aggregate costs to the industry along with average per firm costs are presented in table 2.

- 57.** These costs are likely to be most significant for firms using sustainable investment labels (subpopulation *A*). Using our standard assumptions, we estimate these to be moderate at: £216,100 per firm on average, £5.4m in total across the affected firms.
- 58.** We also expect that small ongoing costs estimated at £18,400 per large, £6,800 per medium, and £1,000 per small firm will be incurred by entities in scope that are:
- currently using sustainability-related terms in their product names and that amended their naming and marketing in the first year (subpopulation *B*), and those not currently using sustainability-related terms in their product names or marketing materials, as these firms will nevertheless need to produce consumer facing disclosures on an ongoing basis; and firms in scope of portfolio management rules (subpopulations *C* and *D*) (at a total estimated cost of £11.9m)
 - required to produce the entity-level disclosures (subpopulations *E* and *F*); these will also require governance changes for the asset managers in scope (at a total estimated cost of £1.6m)
 - covered by our expectations on distributors (subpopulations *G-I*); the latter will also create a need for an ongoing compliance (at a total estimated cost of £7.8m)

Annex 3

Questions in this paper

- Q1:** Do you agree with the proposed scope of firms, products and distributors under our regime? If not, what alternative scope would you prefer, and why?
- Q2:** Do you agree with the proposed implementation timeline? If not, what alternative timeline would you prefer, and why?
- Q3:** Do you agree with the proposed cost-benefit analysis set out in Annex 2. If not, we welcome feedback in relation to the one-off and ongoing costs you expect to incur and the potential benefits you envisage.
- Q4:** Do you agree with our characterisation of what constitutes a sustainable investment, and our description of the channels by which positive sustainability outcomes may be pursued? If not, what alternatives do you suggest and why.
- Q5:** Do you agree with the proposed approach to the labelling and classification of sustainable investment products, in particular the emphasis on intentionality? If not, what alternatives do you suggest and why?
- Q6:** Do you agree with the proposed distinguishing features, and likely product profiles and strategies, for each category? If not, what alternatives do you suggest and why? In particular, we welcome your views on:
- a.** Sustainable Focus: whether at least 70% of a 'sustainable focus' product's assets must meet a credible standard of environmental and/or social sustainability, or align with a specified environmental and/or social sustainability theme?
 - b.** Sustainable Improvers: the extent to which investor stewardship should be a key feature; and whether you consider the distinction between Sustainable Improvers and Sustainable Impact to be sufficiently clear?
 - c.** Sustainable Impact: whether 'impact' is the right term for this category or whether should we consider others such as 'solutions'; and the extent to which financial additionality should be a key feature?

- Q7:** Do you agree with our proposal to only introduce labels for sustainable investment products (ie to not require a label for 'non-sustainable' investment products)? If not, what alternative do you suggest and why?
- Q8:** Do you agree with our proposed qualifying criteria? If not, what alternatives do you suggest and why? In your response, please consider:
- whether the criteria strike the right balance between principles and prescription
 - the different components to the criteria (including the implementing guidance in Appendix 2)
 - whether they sufficiently delineate the different label categories, and;
 - whether terms such as 'assets' are understood in this context?
- Q9:** Do you agree with the category-specific criteria for:
- The 'Sustainable focus' category, including the 70% threshold?
 - The 'Sustainable improvers' category? Is the role of the firm in promoting positive change appropriately reflected in the criteria?
 - The 'Sustainable impact' category, including expectations around the measurement of the product's environmental or social impact?
- Please consider whether there any other important aspects that we should consider adding.
- Q10:** Does our approach to firm requirements around categorisation and displaying labels, including not requiring independent verification at this stage, seem appropriate? If not, what alternative do you suggest and why?
- Q11:** Do you agree with our proposed approach to disclosures, including the tiered structure and the division of information to be disclosed in the consumer-facing and detailed disclosures as set out in Figure 7?
- Q12:** Do you agree with our proposal to build from our TCFD-aligned disclosure rules in the first instance, evolving the disclosure requirements over time in line with the development of future ISSB standards?

- Q13:** Do you agree with our proposals for consumer-facing disclosures, including location, scope, content and frequency of disclosure and updates? If not, what alternatives do you suggest and why?
- Q14:** Do you agree with the proposal that we should not mandate use of a template at this stage, but that industry may develop one if useful? If not, what alternative do you suggest and why?
- Q15:** Do you agree with our proposals for pre-contractual disclosures? If not, what alternatives do you suggest and why. Please comment specifically on the scope, format, location, content and frequency of disclosure and updates.
- Q16:** Do you agree with our proposals for ongoing sustainability-related performance disclosures in the sustainability product report? If not, what alternative do you suggest and why? In your response, please comment on our proposed scope, location, format, content and frequency of disclosure updates.
- Q17:** Do you agree with our proposals for an 'on demand' regime, including the types of products that would be subject to this regime? If not, what alternative do you suggest and why?
- Q18:** Do you agree with our proposals for sustainability entity report disclosures? If not, what alternatives do you suggest and why? In your response, please comment on our proposed scope, location, format, content, frequency of disclosures and updates.
- Q19:** Do you agree with how our proposals reflect the ISSB's standards, including referencing UK-adopted IFRS S1 in our Handbook Guidance once finalised? If not, please explain why?
- Q20:** Do you agree with our proposed general 'anti-greenwashing' rule? If not, what alternative do you suggest and why?
- Q21:** Do you agree with our proposed product naming rule and prohibited terms we have identified? If not, what alternative do you suggest and why?
- Q22:** Do you agree with the proposed marketing rule? If not, what alternative do you suggest and why?
- Q23:** Are there additional approaches to marketing not covered by our proposals that could lead to greenwashing if unaddressed?

- Q24:** Do you agree with our proposals for distributors? If not, what alternatives do you suggest and why?
- Q25:** What are your views on how labels should be applied to pension products? What would be an appropriate threshold for the overarching product to qualify for a label and why? How should we treat changes in the composition of the product over time?
- Q26:** Do you consider the proposed naming and marketing rules set out in Chapter 6 to be appropriate for pension products (subject to a potentially lower threshold of constituent funds qualifying for a label). If not, why? What would be an appropriate threshold for the naming and marketing exemption to apply?
- Q27:** Are there challenges or practical considerations that we should take into account in developing a coherent regime for pension products, irrespective of whether they are offered by providers subject to our or DWP's requirements?
- Q28:** To what extent would the disclosures outlined in Chapter 5 be appropriate for pension providers ie do you foresee any challenges or concerns in making consumer-facing disclosures, pre-contractual disclosures and building from the TCFD product and entity-level reports?
- Q29:** Do you agree that the approach under our TCFD-aligned product-level disclosure rules should not apply to products qualifying for a sustainable investment label and accompanying disclosures? Would it be appropriate to introduce this approach for disclosure of a baseline of sustainability-related metrics for all products in time?
- Q30:** What other considerations or practical challenges should we take into account when expanding the labelling and disclosures regime to pension products?
- Q31:** Would the proposals set out in Chapters 4-7 of this CP be appropriate for other investment products marketed to retail investors such as IBIPs and ETPs. In your response, please include the type of product, challenges with the proposals, and suggest an alternative approach.

Annex 4

Compatibility statement

Compliance with legal requirements

1. This Annex records the FCA's compliance with a number of legal requirements applicable to the proposals in this consultation, including an explanation of the FCA's reasons for concluding that our proposals in this consultation are compatible with certain requirements under the Financial Services and Markets Act 2000 (FSMA).
2. When consulting on new rules, the FCA is required by section 138I(2)(d) FSMA to include an explanation of why it believes making the proposed rules is (a) compatible with its general duty, under s. 1B(1) FSMA, so far as reasonably possible, to act in a way which is compatible with its strategic objective and advances one or more of its operational objectives; and (b) its general duty under s. 1B(5)(a) FSMA to have regard to the regulatory principles in s. 3B FSMA. The FCA is also required by s. 138K(2) FSMA to state its opinion on whether the proposed rules will have a significantly different impact on mutual societies as opposed to other authorised persons.
3. This Annex also sets out the FCA's view of how the proposed rules are compatible with the duty on the FCA to discharge its general functions (which include rule-making) in a way which promotes effective competition in the interests of consumers (s. 1B(4)). This duty applies in so far as promoting competition is compatible with advancing the FCA's consumer protection and/or integrity objectives.
4. In addition, this Annex explains how we have considered the recommendations made by the Treasury under s. 1JA FSMA about aspects of the economic policy of Her Majesty's Government to which we should have regard in connection with our general duties.
5. This Annex includes our assessment of the equality and diversity implications of these proposals.
6. Under the Legislative and Regulatory Reform Act 2006 (LRRRA) the FCA is subject to requirements to have regard to a number of high-level 'Principles' in the exercise of some of our regulatory functions and to have regard to a 'Regulators' Code' when determining general policies and principles and giving general guidance (but not when exercising other legislative functions like making rules). This Annex sets out how we have complied with requirements under the LRRRA.

The FCA's objectives and regulatory principles: Compatibility statement

- 7.** Our proposals are intended to advance the FCA's strategic objective to make markets function well. Following introduction of our requirements, markets should become more transparent, more accessible to consumers and less at risk from harms such as greenwashing.
- 8.** We consider our proposals advance our operational objective to protect consumers. In developing our proposals we have had regard to the differing degrees of risk involved in investments, differing degrees of consumer expertise, consumers' need for timely and accurate information, the general principle that consumers should take responsibility for their decisions, the general principle that those providing regulated financial services should be expected to provide consumers with a level of care that is appropriate and the different expectations that consumers may have about their investments.
- 9.** We consider that the sustainable investment labels should help consumers more easily navigate the market for ESG investment products, understand the different approaches taken to sustainability by different firms and products, and find products meeting their sustainability preferences. Our consumer research shows that consumers find labels useful and help consumers understand the sustainability characteristics of funds.
- 10.** The disclosure rules should increase transparency on sustainability-related matters in a timely manner and ensure that the information provided by firms is accurate, clear, fair and not misleading. This should enable consumers to better understand the sustainability characteristics of products and better assess how well firms manage sustainability-related risks and opportunities. Consumers should therefore be better able to interrogate firms' offerings, enabling them to make more informed decisions when selecting products and providers. This should enable consumers to better protect themselves against unsuitable or mis-sold products and may in turn encourage firms to offer higher-quality products that better meet consumer needs and preferences.
- 11.** The naming and marketing rules prevent firms from exaggerating sustainability claims, which mitigate the risk of greenwashing and allow consumers to make informed choices without being misled.
- 12.** These proposals also align with the new Consumer Duty requirement for firms to act in good faith and for consumers to be provided with information that enables them to make informed, effective decisions.
- 13.** We also expect our proposals to advance our operational objective to enhance and promote market integrity. The labels should bring helpful structure to the complex market for sustainable investment products, in which complicated terminology is often used interchangeably and some consumers find it difficult to find products meeting their needs and preferences. Greater transparency is also likely to support the flow of information along the investment chain, and may also lead to better-informed asset pricing and capital allocation decisions.
- 14.** In considering how our proposals may also deliver a market integrity benefit, we have had regard to the soundness stability and resilience of financial markets, the orderly operation of financial markets, and transparency of the price formation process in those markets.

15. Further, we consider a strengthened regulatory framework for sustainable investment products may increase opportunities and competition in the market and help foster demand and supply of products that better suit the needs and preferences of clients and consumers. For example, firms may offer new products that qualify for a sustainable investment label. With greater transparency on how asset managers are managing sustainability-related risks and opportunities in delivering their products and services, clients and consumers should also be better enabled to select suitable providers.
16. In considering how our proposals enhance competition in the interests of consumers, we have had regard to the needs of different consumers who use or may use those services, the ease with which consumers who obtain those services can change the person from whom they obtain them, the ease with which new entrants can enter the market, and how far competition is encouraging innovation.
17. In addition, we also consider our proposals to support the expectations in the Chancellor's latest remit letter to the FCA, that we have regard to the UK Government's target of net zero by 2050, in carrying out our duties. The Chancellor also asked us to have regard to the Government's energy security strategy. Our proposals are intended to help consumers better understand which firms and investment products are aligned with the transition to a more sustainable economy. Further, our proposals should not disincentivise consumers from investing in energy companies. The 'Sustainable improvers' label reflects that consumers may wish to invest in energy companies that are transitioning to becoming more sustainable over time.
18. In preparing the proposals set out in this consultation, the FCA has had regard to the regulatory principles set out in s. 3B FSMA.

The need to use our resources in the most efficient and economic way

19. In building from existing requirements to the extent possible (eg our Guiding Principles and TCFD requirements) we have been able to introduce new measures in a complex and novel area of policy in the most efficient manner. We also engaged extensively with stakeholders in developing our proposals to incorporate expertise and feedback throughout the process.

The principle that a burden or restriction should be proportionate to the benefits

20. The cost benefit analysis in Annex 2 sets out the costs and benefits for the proposals in this CP. While we recognise there will be a cost for firms in implementing these proposals, we consider that the benefits, such as reducing greenwashing and rebuilding trust in the market, outweigh the costs.

The desirability of sustainable growth in the economy of the United Kingdom in the medium or long term

21. Greater transparency on sustainability-related matters should enable clients and consumers to make better-informed decisions about their investments and providers. This may lead to better allocation of capital throughout the economy, facilitating a smoother transition to a more sustainable economy.

The general principle that consumers should take responsibility for their decisions

22. Labels should enable consumers to better navigate the market for sustainable investment products, and disclosures should increase transparency of the sustainability-related features of products and on how firms are managing sustainability-related risks and opportunities. Together, these proposals should enable consumers to make better-informed decisions when selecting their products and providers.

The responsibilities of senior management

23. We consider that our proposals are likely to enhance the ability of senior asset managers of in-scope products to take responsibility for their decisions by providing a framework that will encourage them to think about the classification and features of sustainable investment products, as well as the governance, risk management and strategy for managing investments in a systematic and considered way.

The desirability of recognising differences in the nature of, and objectives of, businesses carried on by different persons including mutual societies and other kinds of business organisation

24. Our proposals will apply to asset managers initially in respect of in-scope products as well as distributors of those products to retail investors. However, we intend to expand the scope of the regime over time to include other investment products offered to retail investors. In recognising the differences in the nature of and objective of businesses carried on by different persons offering these products, we are seeking feedback on how the proposals in this CP would apply to a broader range of products.

The desirability of publishing information relating to persons subject to requirements imposed under FSMA, or requiring them to publish information

25. Our proposals require firms to make disclosures largely in the public domain, or in some cases provide disclosures to clients upon request. We do not propose that the information be reported to the FCA. However, we do propose that firms notify us if they decide to use a sustainable investment label.

The principle that we should exercise of our functions as transparently as possible

26. In developing our proposals, we have acted as transparently as possible. We signalled our intention to introduce SDR and labels in the Government's Roadmap to Sustainable Investing in October 2021. We then published a Discussion Paper (DP21/4) in November seeking early views on a labelling and disclosure regime. We have since engaged with stakeholders via a Disclosures and Labels Advisory Group (comprised of industry experts and consumer representatives) as well as through roundtables, panel discussions, webinars etc. We will continue to engage closely with stakeholders as we finalise our rules.
27. In formulating these proposals, the FCA has had regard to the importance of taking action intended to minimise the extent to which it is possible for a business carried on (i) by an authorised person or a recognised investment exchange; or (ii) in contravention of the general prohibition, to be used for a purpose connected with financial crime (as required by s. 1B(5)(b) FSMA).

Expected effect on mutual societies

- 28.** The FCA does not expect the proposals in this paper to have a significantly different impact on mutual societies. Mutual societies are not within scope of our proposed rules.

Equality and diversity

- 29.** We are required under the Equality Act 2010 in exercising our functions to 'have due regard' to the need to eliminate discrimination, harassment, victimisation and any other conduct prohibited by or under the Act, advance equality of opportunity between persons who share a relevant protected characteristic and those who do not, to and foster good relations between people who share a protected characteristic and those who do not.
- 30.** As part of this, we ensure the equality and diversity implications of any new policy proposals are considered. We do not consider that these proposals adversely impact any of the groups with protected characteristics ie, age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment. We welcome your comments if you have any concerns.

Legislative and Regulatory Reform Act 2006 (LRRRA)

- 31.** We have had regard to the principles in the LRRRA for the parts of the proposals that consist of general policies, principles or guidance. We consider that our proposals are consistent with LRRRA principles – that regulatory activities should be carried out in a way which is transparent, accountable, proportionate, consistent and targeted only at cases in which action is needed.
- 32.** We have followed a consistent regulatory approach in developing our proposals. We have clearly set out our proposed rules in a transparent way. We consider our proposals to be proportionate. For example, our proposed product-level disclosure requirements balance the need to provide greater transparency on sustainability-related features of products with the costs for firms in producing those disclosures ie there will be fewer and less detailed disclosures for products that do not use a sustainable investment label. We are also proposing to phase in our requirements for firms to make entity-level disclosures, and exclude the very smallest firms from scope of those disclosures.
- 33.** We have had regard to the Regulators' Code for the parts of the proposals that consist of general policies, principles or guidance, particularly the requirement for regulatory activity to be proportionate and targeted.

Annex 5

List of non-confidential respondents to DP21/4

2 Degrees Investing

abrdrn

Allianz GI

Alternative Investment Management Association (AIMA) and the Alternative Credit Council (ACC)

ARC Ratings (UK) Limited

Association of British Insurers (ABI)

Association of Investment Companies (AIC)

Association of Real Estate Funds (AREF)

Baillie Gifford

Bloomberg

Border to Coast Pensions Partnership

Brewin Dolphin

British Private Equity & Venture Capital Association (BVCA)

Brunel Pension Partnership

Cardano

CDP

CFA UK

Charles Stanley

ClientEarth

CMS Cameron McKenna Nabarro Olswang LLP

Connected Asset Management

CQS LLP

DATA

Devlin Mambo

Dimensional

E2 Management

E3G

EdenTree

EIRIS foundation

ESG Accord

ESGi

Ethical Futures

European Association for Investors in Non-Listed Real Estate Vehicles (INREV)

Eversheds Sutherland

EY

FCA Financial Services Consumer Panel

FCA Practitioner Panel

FCA Smaller Business Practitioner Panel

FE fundinfo

FIA EPTA

Financial Inclusion Centre

Green Llama

Hargreaves Lansdown

Impact Cubed

Impax Asset Management

Innovate Finance

Insight Investment

Institute and Faculty of Actuaries (IFoA)

Institutional Investors Group on Climate Change (IIGCC)

Interactive Investor

Intercontinental Exchange (ICE)

International Business of Federated Hermes

International Securities Lending Association (ISLA)

International Swaps and Derivatives Association (ISDA)

Invesco

Investment and Life Assurance Group (ILAG)

Investment Association

Investment Property Forum (IPF)

Isio

JP Morgan AM

Jupiter Asset Management

M&G

Make My Money Matter (MMMM)

MSCI

Nationwide

Nest

Ninety One

Nucleus Financial Services

Openwork Limited

Parmenion Capital Partners

Personal Investment Management & Financial Advice Association (PIMFA)

Prequin

Principles for Responsible Investment (PRI)

Red Ribbon Fund Management

Royal London

Schroders

Securities Industry and Financial Markets Association (SIFMA)

ShareAction

Square Mile Investment Services

SRI Services

St James's Place

Standards Board for Alternative Investments (SBAI)

State Street Global Advisors (SSGA)

T Bailey Asset Management

The Good Economy

The Investing and Saving Alliance (TISA)

The Law Society

Triodos Investment Management

TrustDFM

UK Sustainable Investment and Finance Association (UKSIF)

Vanguard Asset Management

WHEB Asset Management

World Federation of Exchanges (WFE)

World Wide Fund for Nature (WWF)

XPS Pensions Group

22 respondents requested their answers to be treated as confidential. We have also decided to treat 9 responses from individuals as confidential.

Annex 6

Abbreviations used in this paper

| Abbreviation | Description |
|---------------------|--|
| AIF | Alternative Investment Fund |
| AIFM | Alternative Investment Fund Manager |
| AUM | Assets Under Management |
| CFRF | Climate Financial Risk Forum |
| CP | Consultation Paper |
| DLAG | Disclosures and Labels Advisory Group |
| DP | Discussion Paper |
| DWP | Department for Work and Pensions |
| ESG | Environmental, Social and Governance |
| ETP | Exchange-traded Product |
| EU | European Union |
| FRC | Financial Reporting Council |
| GTAG | Green Technical Advisory Group |
| IA | Investment Association |
| IBIPs | Insurance-based investment products |
| ICMA | International Capital Market Association |
| ICVC | Investment company with variable capital |
| IOSCO | International Organization of Securities Commissions |
| ISIN | International Securities Identification Number |
| ISSB | International Sustainability Standards Board |
| KID | Key Information Document |
| KIID | Key Investor Information Document |
| KPI | Key Performance Indicator |
| PRA | Prudential Regulation Authority |

| Abbreviation | Description |
|---------------|---|
| PRIIPs | Packaged Retail Investment and Insurance-Based Products |
| PS | Policy Statement |
| SASB | Sustainability Accounting Standards Board |
| SDGs | Sustainable Development Goals |
| SDR | Sustainability Disclosure Requirements |
| SEC | Securities and Exchange Commission |
| SFDR | Sustainable Finance Disclosure Regulation |
| TCFD | Task Force on Climate-related Financial Disclosures |
| TISA | The Investing and Saving Alliance |
| TPT | Transition Plan Taskforce |
| UCITS | Undertakings for Collective Investment in Transferable Securities |
| US | United States |

We make all responses to formal consultation available for public inspection unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.

Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

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Appendix 1

Draft Handbook text

**SUSTAINABILITY LABELLING AND DISCLOSURE OF
SUSTAINABILITY-RELATED FINANCIAL INFORMATION INSTRUMENT 202X**

Powers exercised

- A. The Financial Conduct Authority (“the FCA”) makes this instrument in the exercise of the following powers and related provisions in or under:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
 - (a) section 137A (The FCA’s general rules);
 - (b) section 137R (Financial Promotion Rules);
 - (c) section 137T (General supplementary powers);
 - (d) section 139A (Power of the FCA to give guidance);
 - (e) section 247 (Trust scheme rules);
 - (f) section 248 (Scheme particulars rules);
 - (g) section 261I (Contractual scheme rules); and
 - (h) section 261J (Contractual scheme particulars rules);
 - (2) regulation 6(1) of the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228); and
 - (3) the other rule and guidance making powers listed in Schedule 4 (Powers exercised) to the General Provisions of the FCA’s Handbook.
- B. The rule-making provisions listed above are specified for the purposes of section 138G(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on [*date*].

Amendments to the Handbook

- D. The modules of the FCA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below.

| (1) | (2) |
|---|---------|
| Glossary of definitions | Annex A |
| Conduct of Business sourcebook (COBS) | Annex B |
| Product Intervention and Product Governance sourcebook (PROD) | Annex C |
| Environmental, Social and Governance sourcebook (ESG) | Annex D |
| Collective Investment Schemes sourcebook (COLL) | Annex E |
| Investment Funds sourcebook (FUND) | Annex F |

Notes

- E. In the Annexes to this instrument, the “notes” (indicated by “**Note:**” or “*Editor’s note:*”) are included for the convenience of readers but do not form part of the legislative text.

Citation

- F. This instrument may be cited as the Sustainability Labelling and Disclosure of Sustainability-Related Financial Information Instrument 202X.

By order of the Board
[*date*]

Annex A

Amendments to the Glossary of definitions

Insert the following new definitions in the appropriate alphabetical position. All the text is new and is not underlined.

| | |
|--|--|
| <i>consumer-facing disclosure</i> | a disclosure produced in accordance with <i>ESG 4.2</i> in respect of a <i>sustainability product</i> . |
| <i>IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information</i> | [<i>Editor's note</i> : This standard is yet to be finalised. Link to publication by the International Sustainability Standards Board is to follow] the International Financial Reporting Standard (IFRS) S1 General Requirements for Disclosure of Sustainability-related Financial Information. |
| <i>on-demand sustainability information</i> | information produced in accordance with <i>ESG 4.5.14R</i> to <i>ESG 4.5.16G</i> for a <i>person</i> who is entitled to such information under <i>ESG 4.5.14R(1)</i> in respect of: <ol style="list-style-type: none"> (1) the <i>investments</i>, including rights to or interests in <i>investments</i>, in respect of which the <i>firm</i> provides <i>portfolio management</i> to that <i>person</i>; or (2) assets under management in an <i>unauthorised AIF</i> in which the <i>person</i> is an investor, but only in respect of an <i>unauthorised AIF</i> managed by a <i>UK AIFM</i> which is not listed on a <i>recognised investment exchange</i>. |
| <i>pre-contractual disclosure</i> | a disclosure of the information set out at <i>ESG 4.3.1R</i> to <i>ESG 4.3.5G</i> . |
| <i>pre-contractual materials</i> | (in relation to <i>ESG</i>) a <i>prospectus</i> or, in relation to a <i>full-scope UK AIFM</i> , the prior disclosure information document required by <i>FUND 3.2.2R</i> . |
| <i>public product-level sustainability report</i> | a report comprising Part A (where applicable) and Part B, produced in accordance with <i>ESG 4.5.1R</i> to <i>ESG 4.5.13R</i> in respect of the following insofar as it is a <i>sustainability product</i> : <ol style="list-style-type: none"> (1) an <i>authorised fund</i>; and (2) an <i>unauthorised AIF</i> managed by a <i>UK AIFM</i> that is listed on a <i>recognised investment exchange</i>; this includes an <i>investment trust</i>. |
| <i>relevant digital medium</i> | (in relation to <i>ESG</i>) a <i>firm's</i> website and any mobile application or other digital medium that the <i>firm</i> may be using in relation to a <i>sustainability product</i> . |

| | |
|---|---|
| <i>sustainability characteristics</i> | environmental, social or governance characteristics. |
| <i>sustainability entity report</i> | a public report regarding the overall assets managed by the <i>firm</i> in relation to its <i>sustainability in-scope business</i> as per the requirements in <i>ESG 4.6</i> . |
| <i>sustainability in-scope business</i> | the following activities, as set out in more detail in <i>ESG 1.2.1R</i> : <ol style="list-style-type: none"> (1) <i>portfolio management</i>, to the extent that <i>ESG 1.2.4R</i> applies; (2) <i>managing a UK UCITS</i>; and (3) <i>managing an AIF</i>. |
| <i>sustainability label</i> | any of the labels that are listed at <i>ESG 3.1.1R(1)</i> . |
| <i>sustainability objective</i> | a statement of intention to undertake activities with the aim of pursuing, promoting or improving environmental and/or social <i>sustainability characteristics</i> . |
| <i>sustainability product</i> | a <i>TCFD product</i> but excluding: <ol style="list-style-type: none"> (1) an agreement or arrangement under which a <i>firm</i> provides a <i>client</i> with <i>portfolio management</i>, except to the extent that <i>ESG 1.2.4R</i> applies; (2) a <i>personal pension scheme</i>, a <i>stakeholder pension scheme</i> or a <i>SIPP</i>; and (3) an <i>insurance-based investment product</i>. |
| <i>theory of change</i> | (in relation to <i>ESG</i>) a comprehensive description and illustration of how and why a desired change is expected to occur in a particular context. |

Amend the following definitions as shown.

| | |
|---------------|---|
| <i>client</i> | ... |
| | (B) in the <i>FCA Handbook</i> : |
| | (1) (except in <i>PROF</i> , in <i>MIFIDPRU 5</i> , in relation to a <i>credit-related regulated activity</i> , in relation to <i>regulated funeral plan activity</i> , in relation to a <i>home finance transaction</i> and , in relation to <i>insurance risk transformation</i> and activities directly arising from <i>insurance risk transformation</i> , and in relation to <u>undertaking <i>sustainability in-scope business</i> in relation to <i>sustainability products</i></u>) has the meaning given in <i>COBS 3.2</i> , that is (in summary and without prejudice to the detailed effect of <i>COBS 3.2</i>) a <i>person</i> to whom a <i>firm</i> provides, intends to provide or has provided a service in the course of carrying |

on a *regulated activity*, or in the case of *MiFID* or *equivalent third country business*, an *ancillary service*:

...

...

(12) (in *ESG*) includes:

- (i) a unitholder or potential unitholder in a scheme; and
- (ii) to the extent not within (i), an investor or potential investor in an AIF.

distribute ...

(5) (in relation to *ESG*) in relation to a *client*, offering, selling, recommending, advising on, arranging, dealing, proposing or providing a *sustainability product* or a *recognised scheme* (including an *ETF* that is a *recognised scheme*).

distributor ...

(4) (in relation to *ESG*) a *firm* which offers, sells, recommends, advises on, arranges, deals, proposes or provides a *sustainability product* or a *recognised scheme* (including an *ETF* that is a *recognised scheme*).

on-demand TCFD information an *on-demand TCFD product report* or *underlying asset data*.

TCFD product any of the following:

...

(5) an *unauthorised AIF* managed by a *UK AIFM*, unless it is a ~~closed-ended AIF that makes no additional investments after 22 July 2013 (see regulation 74(1) of the *AIFMD UK Regulation*).~~:

- (a) a closed-ended AIF that makes no additional investments after 22 July 2013 (see regulation 74(1) of the *AIFMD UK Regulation*);
- (b) a *SEF*; or
- (c) an *RVECA*.

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

4 Communicating with clients, including financial promotions

4.1 Application

Who? What?

...

4.1.1A R *COBS 4.4.3 R applies to a firm with respect to the activity of issuing electronic money.*

4.1.1B G A firm is reminded of its obligations under the naming and marketing rules in ESG 3.3 (in particular, ESG 3.3.1R) when it:

- (1) *communicates or approves a financial promotion that references the sustainability characteristics of a product or service;*
- (2) *undertakes sustainability in-scope business in relation to a sustainability product.*

...

4.10 Systems and controls and approving and communicating financial promotions

...

Approving financial promotions

4.10.2 R ...

- (3) *When approving a financial promotion, the firm must confirm compliance with the financial promotion rules that would have applied if the financial promotion had been communicated by a firm other than in relation to MiFID or equivalent third country business.*

- (4) When communicating or approving a financial promotion, a firm must ensure that that promotion complies with ESG 3.3.1R.

...

18.5 Residual CIS operators and small authorised UK AIFMs

...

Format and content of fund documents

...

18.5.9 G *A small authorised UK AIFM of an unauthorised AIF or a residual CIS operator will still have to comply with other COBS provisions as a result of the reclassification of an investor as a retail client. For example, the firm must provide periodic statements to investors who are retail clients in an unauthorised fund (see the rule on periodic statements for an unauthorised fund (COBS 18.5.11R)).*

18.5.9A G *A small authorised UK AIFM that uses a sustainability label in relation to an AIF is reminded of its obligations in ESG 4.3 to ESG 4.5 relating to the preparation of Part A of a public product-level sustainability report.*

...

Annex C

Amendments to the Product Intervention and Product Governance sourcebook (PROD)

In this Annex, underlining indicates new text and striking through indicates deleted text.

3 Product governance: MiFID

...

3.3 Distribution of products and investment services

General

...

3.3.2 G A *distributor* should consider what impact the selection of a given *manufacturer* could have on the *end client* in terms of charges or the financial strength of the *manufacturer*, or possibly, where information is available to the *distributor*, how efficiently and reliably the *manufacturer* will deal with the *distributor* or *end client* at the point of sale (or subsequently, such as when queries/complaints arise, claims are made, or a *financial instrument* reaches maturity).

3.3.2A G A *distributor* is reminded of its obligations under ESG 3.1.13R to ESG 3.1.15R in meeting its obligations under PROD 3.3.1R(1).

...

Annex D

Amendments to the Environmental, Social and Governance sourcebook (ESG)

In this part of the Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

1 Purpose and application

1.1 Purpose and application

Purpose

...

1.1.3 G ...

1.1.3A G ESG 3 contains rules and guidance which restrict the use of sustainability labels in relation to sustainability products by prohibiting the use of such labels except where certain criteria are met, together with further rules and guidance on naming and marketing restrictions with respect to sustainability products.

1.1.3B G ESG 4 contains rules and guidance regarding the consumer-facing disclosures, pre-contractual disclosures, public product-level sustainability reports and (where applicable) on-demand sustainability information that firms must produce in relation to sustainability products, together with rules and guidance requiring firms to produce entity-level reports.

1.1.4 G The TCFD-related disclosures are intended to help meet the information needs of market participants, including a *firm's* institutional *clients* (e.g. pension trustees, employers and corporate investors) and *consumers* of their products (e.g. pension scheme members and retail investors), in relation to the climate-related impact and risks of a *firm's TCFD in-scope business*.

1.1.4A G The sustainability-related labelling and disclosures are also intended to help meet the information needs of market participants, including a *firm's retail clients* and institutional *clients* in relation to the *sustainability characteristics of sustainability products* and the sustainability-related risks and opportunities in relation to a *firm's sustainability in-scope business*.

...

1.2 General application

1.2.1 R (1) The *rules* in this sourcebook apply to a *firm* of a type listed in column 1 of the table at ESG 1.2.1 R(2) in relation to the *TCFD in-scope business* and the *sustainability in-scope business* carried out from an establishment maintained by it in the *United Kingdom* as described in column 2.

(1A) The rules in ESG 2 will apply to all firms in the table at ESG 1.2.1R(2), while (subject to ESG 1.2.3R) the rules in ESG 3 and ESG 4 will only apply to firms in Part A of that table.

(2) This table belongs to ESG 1.2.1R(1).

| Column 1: Type of firm | Column 2: TCFD in-scope business <u>and sustainability in-scope business</u> |
|---|--|
| Part A: Asset managers | |
| Any firm | <i>Portfolio management</i> , subject to ESG 1.2.4R |
| ... | |
| Part B: Asset owners (<i>TCFD in-scope business only</i>) | |
| ... | |

1.2.2 R A firm is exempt from the disclosure requirements under ESG 2 and ESG 4.6 if and for as long as the assets under administration or management in relation to its *TCFD in-scope business or sustainability in-scope business* amount to less than £5bn calculated as a 3-year rolling average on an annual assessment.

1.2.3 R ESG 3.3.1R(1) will apply to all firms and ESG 3.1.13R to ESG 3.1.15R will apply to firms that are distributors.

1.2.4 R A firm that is undertaking sustainability in-scope business in relation to a sustainability product that is an agreement or arrangement under which a firm provides a client with portfolio management will be undertaking sustainability in-scope business only insofar as the following rules and guidance apply:

(1) ESG 3.1.1R(2)(b);

(2) ESG 3.3.3R;

(3) ESG 4.1.1R(2);

(4) ESG 4.4.1R(2);

(5) ESG 4.5.14R to ESG 4.5.16G; and

(6) ESG 4.6

...

2 Disclosure of climate related financial information

2.1 Preparation of climate-related reports

Application

- 2.1.1 R (1) ...
- (2) If a *firm* (including an *OPS firm*) receives a request for *on-demand TCFD information* from a *person* who is entitled to make such request under *ESG 2.3.5R*, it must prepare and provide the *on-demand TCFD information* to the *person* within a reasonable period of time and in a format which the *firm*, acting reasonably, considers appropriate to meet the information needs of that *person*.

...

2.3 Product-level reporting

...

On-demand TCFD product reports and underlying data

- 2.3.5 R (1) A *client* who requires *on-demand TCFD information* in order to satisfy climate-related financial disclosure obligations, whether under this chapter or as a result of other legal or regulatory requirements, is entitled to request such information from, and be provided with it by, the *firm* and to receive a response to that request in accordance with *ESG 2.1.1R(2)*.
- (2) On receipt of a request from a *client* under (1), a *firm* must provide *on-demand TCFD information* as at a calculation date determined in accordance with *ESG 2.1.9R* or at an alternative calculation date where this has been agreed between the *client* and the *firm*.

...

...

Insert the following new sections, ESG 3 (Sustainability labelling, naming and marketing) and ESG 4 (Disclosure of sustainability-related information), directly before ESG TP 1 (Transitional provisions). The text is all new and is not underlined.

3 Sustainability labelling, naming and marketing

3.1 Sustainability labels

- 3.1.1 R (1) Subject to *ESG 3.1.1R(2)*, a *firm* must not make use of the following *sustainability labels*:
- (a) ‘Sustainable focus’;

- (b) ‘Sustainable improvers’; or
 - (c) ‘Sustainable impact’.
- (2) A *firm* may only make use of a *sustainability label* in ESG 3.1.1R(1) in circumstances where it is undertaking *sustainability in-scope business* in relation to a *sustainability product* and the following conditions are met:
- (a) the *firm* meets the criteria pertaining to the particular *sustainability label*, as set out in ESG 3.2; and
 - (b) in relation to an agreement or arrangement under which a *firm* provides the *client* with *portfolio management*, 90% of the total value of the products in which that *sustainability product* invests (whether or not those products are *sustainability products*) meet the criteria with respect to using the same *sustainability label*.
- (3) A *firm* must, where it makes use of a *sustainability label* in accordance with ESG 3.1.1R(2), use the relevant graphic prescribed by the *FCA*:
- (a) when displaying that label in relation to a *sustainability product* on the *relevant digital medium* for the business of the firm; and
 - (b) in a *consumer-facing disclosure*, a *pre-contractual disclosure* and Part B of a *public product-level sustainability report*.
- 3.1.2 G For the purposes of ESG 3.1.1R(3), the relevant graphic can be found on the *FCA* website. [*Editor’s note*: link to follow]
- 3.1.3 R A *firm* that uses a *sustainability label* must not:
- (1) use a *sustainability label* in a way that is misleading;
 - (2) claim in a public statement or to a *client*, either expressly or by implication, that:
 - (a) the *FCA* has conferred or approved the use of a *sustainability label* in relation to a particular *sustainability product*; or
 - (b) the *firm’s* use of a *sustainability label* indicates that a *sustainability product* has been approved or endorsed by the *FCA*.
 - (3) publish information in relation to the use of, or descriptors pertaining to, a *sustainability label* which contradicts the information that has been published by the *FCA*.

Record keeping

- 3.1.4 R A *firm* that uses a *sustainability label* must:

- (1) prepare and retain a record as to the basis on which the *sustainability label* has been used; and
- (2) maintain that record for the duration of the *sustainability label's* use (including updating that record should the use of the *sustainability label* change).

Notifying the FCA

- 3.1.5 R A *firm* that uses a *sustainability label* in relation to a *sustainability product* must, within one *month* of the date on which the *firm* starts to use that label, notify the *FCA* at [*Editor's note: link to follow*] that it is using the label in relation to a particular *sustainability product*.

Publication of sustainability labels

- 3.1.6 R (1) Where a *firm* uses a *sustainability label* in relation to a *sustainability product*, it must publish on the *relevant digital medium* for the business of the *firm*:
- (a) the *sustainability label* that has been applied to that *sustainability product*; and
 - (b) details as to where the *consumer-facing* disclosure pertaining to that *sustainability product* can be easily accessed.
- (2) A *firm* must locate the information at *ESG 3.1.6R(1)* in a prominent location on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered.
- 3.1.7 G In addition to the information required under *ESG 3.1.6R*, a *firm* may choose to provide further information in relation to the *sustainability label* by including on the *relevant digital medium* for the business of the *firm*, locating it at a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered, a hyperlink to the relevant webpage of the *FCA's* website.
- 3.1.8 G For the purposes of these *rules* and *guidance*, a 'prominent place' should take account of the content, size and orientation of the information pertaining to the *sustainability product* (or, in the case of *ESG 3.1.15R(3)*, a *recognised scheme*, including an *ETF* that is a *recognised scheme*) on the relevant webpage or page of the mobile application or other digital medium as a whole.

Reviewing sustainability labels

- 3.1.9 R A *firm* that uses a *sustainability label* in relation to a *sustainability product* must:
- (1) keep under review the use of that label – in particular:

- (a) a *firm* must review its use of a *sustainability label* at least every 12 months; and
 - (b) a *firm* must review its use of a *sustainability label* prior to any proposed change to a *sustainability product*, where those changes have not been subject to a review under *ESG 3.1.9R(1)(a)*.
- (2) following a review under *ESG 3.1.9R(1)*, revise the use of the *sustainability label* as appropriate.
- 3.1.10 R A *firm* must prepare and retain a record of the fact that it has undertaken a review under *ESG 3.1.9R* and the decision it has reached as a result of that review regarding whether the *sustainability label* it has used remains appropriate.
- 3.1.11 R A *firm* must, where it has either revised the *sustainability label* that it uses in relation to a *sustainability product*, or ceased to use that label:
- (1) give prior written notice to its *clients* who have invested in that product that the *sustainability label* has been revised and the reasons for that revision, at least 60 *days* before that change takes effect;
 - (2) publish the revised *sustainability label* (or the fact that the *firm* has ceased to use a label) and the reasons for the revision on the *relevant digital medium* for the business of the *firm*, locating it at a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered, at least 60 *days* before that change takes effect; and
 - (3) ensure that the *pre-contractual disclosures*, *consumer-facing disclosures* and reports prepared under *ESG 4.4* and *ESG 4.5* in relation to the *sustainability product* are updated to coincide with the publication of the revised *sustainability label*.
- 3.1.12 G For the purposes of *ESG 3.1.11R(1)*, *firms* are reminded of their obligations under *COLL 4.3* – in particular *COLL 4.3.6R(2)* – as a change in the use of a *sustainability label* will constitute at least a significant change and may, depending on the circumstances, constitute a fundamental change.

Distributors

- 3.1.13 R (1) Where a *firm* distributes to retail clients a *sustainability product* which uses a *sustainability label*, that distributor must:
- (a) display the *sustainability label* that the *firm* that is undertaking *sustainability in-scope business* uses in relation to a *sustainability product* on the *relevant digital medium* for the business of the *firm*, locating it at a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered;

- (b) not use a *sustainability label* in relation to a *sustainability product* other than the label that the *firm* that is undertaking *sustainability in-scope business* uses in relation to that *sustainability product*; and
 - (c) ensure that *retail clients* are provided with access to a *consumer-facing disclosure* in relation to that *sustainability product*.
 - (2) Where a *firm* does not use a *sustainability label*, a *firm* that *distributes sustainability products* must ensure that *retail clients* are provided with access to the *consumer-facing disclosure* in relation to the *sustainability product*.
- 3.1.14 R A *firm* that *distributes a sustainability product* to *retail clients* must ensure that its *relevant digital medium* and marketing communications in relation to that *sustainability product* are kept updated in accordance with any changes that are made to the relevant *sustainability label* or to the disclosures under *ESG 3* or reports under *ESG 4*.
- 3.1.15 R A *firm* that *distributes recognised schemes*, including *ETFs* that are *recognised schemes*, to *retail clients* must comply with the following *rules*:
- (1) A *firm* must, where the terms set out in *ESG 3.3.2R* are used in either the name or marketing communications in relation to *recognised schemes*, include a notice as set out in *ESG 3.1.15R(2)*.
 - (2) A *firm* must include the following text in the notice specified at *ESG 3.1.15R(1)*, and publish it in accordance with *ESG 3.1.15R(3)(a)*: ‘This product is based overseas and is not subject to FCA sustainable investment labelling and disclosure requirements.’
 - (3) A *firm* must, in relation to the *relevant digital medium* for the business of the *firm*:
 - (a) display the notice at *ESG 3.1.15R(2)*, locating it in a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered; and
 - (b) include a hyperlink to the relevant webpage of the *FCA* website which sets out for *retail clients* further information in relation to the sustainability labelling and disclosure requirements under these *rules*.

Meaning of assets

- 3.1.16 G In *ESG 3* and the related disclosure requirements in *ESG 4*, unless the context otherwise requires, reference to the term ‘assets’ means:
- (1) the *scheme property*, in relation to an *authorised fund*; or

- (2) in relation to a *sustainability product* other than an *authorised fund*, the *investments* that a *sustainability product* makes.

3.2 Criteria for applying sustainability labels

- 3.2.1 R A *firm* must, in order to use a *sustainability label* in relation to a *sustainability product* in accordance with ESG 3.1.1R(2), ensure that both the general criteria and the specific criteria which relate to that particular *sustainability label* have been met and continue to be met on an ongoing basis.
- 3.2.2 G ESG 3.2 sets out the relevant general and specific criteria, and ESG 4 sets out the locations at which information associated with those criteria must be included, either in a *consumer-facing disclosure*, a *pre-contractual disclosure*, Part B of a *public product-level sustainability report* or in an *entity sustainability report*.

General criteria

- 3.2.3 R The general criteria are set out as follows:
- (1) A *firm* must ensure that a *sustainability product* has an explicit *sustainability objective*, in relation to an environmental and/or a social *sustainability characteristic*, that aligns with one of the specific *sustainability labels* in ESG 3.2.5R to ESG 3.2.8R and that:
- (a) a *sustainability product's sustainability objective* is stated in clear, specific and measurable terms, as part of its investment objectives;
 - (b) the *sustainability product's sustainability objective* has a plausible, purposeful and credible link to an environmental and/or a social outcome;
 - (c) the *firm* has adequate processes in place to:
 - (i) monitor the *sustainability product's* performance against its *sustainability objective*; and
 - (ii) provide ongoing reporting to *clients*.
- (2) A *firm* must ensure that a *sustainability product's* investment policy and strategy are aligned with its *sustainability objective* – in particular:
- (a) a *firm* must develop and implement an investment policy and strategy aligned with the *sustainability product's sustainability objective*;
 - (b) a *firm* must ensure that a *sustainability product* is invested in accordance with its investment policy and strategy on an ongoing basis;
 - (c) a *firm* must determine its investible universe and the asset-level selection criteria it applies to meet the environmental and/or social

target sustainability profile of assets in specific and measurable terms, including:

- (i) how the *firm* assesses the *sustainability product's* assets against the criteria;
 - (ii) how the criteria relate to the target environmental and/or social profile of assets;
 - (iii) how the target environmental and/or social profile of assets aligns with the *sustainability product's sustainability objective*; and
 - (iv) the conditions under which an asset ceases to meet its specified criteria for asset selection.
- (d) a *firm* must, with respect to a determination made in accordance with *ESG 3.2.3R(2)(c)* which relates to an index-tracking product:
- (i) satisfy itself that the index provider's methodology for index-construction aligns with the *sustainability product's sustainability objective* and its target environmental and/or social sustainability profile; and
 - (ii) retain the responsibility for ensuring that the index methodology reflects the *sustainability product's sustainability objective* and that it complies with the relevant criteria under *ESG 3.2* for the purposes of using a *sustainability label* on an ongoing basis.
- (e) a *firm* must have appropriately designed policies and procedures in place to determine, measure, monitor, evaluate and report to *clients* as to the environmental and/or the social sustainability profile of a *sustainability product's* assets on an ongoing basis.
- (f) the *firm* must identify any investment made by a *sustainability product* that a reasonable *client* might consider to be in conflict with the *sustainability objective*, investment policy and strategy of the *sustainability product*.
- (3) A *firm* must:
- (a) have in place key performance indicators (KPIs) for the purposes of measuring a *sustainability product's* ongoing performance towards achieving its *sustainability objective*, which are:
 - (i) credible, rigorous and evidence based;
 - (ii) relevant to, and aligned with, the *sustainability product's sustainability objective*;

- (b) monitor that *sustainability product's* performance against its *sustainability objective* on an ongoing basis with reference to the KPIs referred to at *ESG 3.2.3R(3)(a)*.
- (4) A *firm* must apply and maintain appropriate resources, governance and organisational arrangements commensurate with the delivery of the *sustainability product's sustainability objective* – in particular:
- (a) a *firm* must apply and maintain the following resources as appropriate for supporting and achieving the product's *sustainability objective* and the delivery of its investment policy and strategy:
 - (i) investment professionals with appropriate skills and experience);
 - (ii) technological inputs and research;
 - (iii) data and analytical tools;
 - (iv) where appropriate, oversight by any governing body in relation to a *sustainability product*; and
 - (v) any other resources as appropriate for supporting and achieving the *sustainability product's sustainability objective*;
 - (b) a *firm* must carry out due diligence on any data, research and analytical resources it relies upon (including when third-party ESG data service providers are used), ensuring that any gaps or shortcomings in that data, research or analytical resources are documented and appropriately mitigated;
 - (c) a *firm* must maintain the arrangements and resources it has in place to oversee the sustainability research, data and analytical tools that it uses, and ensure that those things remain fit for purpose in supporting the achievement of the *sustainability product's sustainability objective* on an ongoing basis; and
 - (d) a *firm* must maintain governance and organisational arrangements that appropriately support and incentivise the high-quality delivery of its investment policy and strategy in line with the *sustainability product's sustainability objective*.
- (5) A *firm* must:
- (a) maintain an active investor stewardship strategy and resources (at firm-level or product-level), in a manner consistent with the *sustainability product's sustainability objective*;
 - (b) apply its active investor stewardship strategy and resources appropriate for achieving the *sustainability product's sustainability objective*;

- (c) where stewardship plays a significant role in its investment policy and strategy for a *sustainability product*, specify credible, rigorous and evidence-based KPIs that relate to the contribution of stewardship activities and outcomes to the achievement of the *sustainability product's sustainability objective*; and
- (d) monitor its stewardship performance against any KPIs that are relevant to the delivery of the *sustainability product* in line with its *sustainability objective*.

3.2.4 G A *firm* may, in determining its *sustainability objective* in relation to a *sustainability product*, refer to the standards produced by the Sustainability Accounting Standards Board in order to help determine the topics that a *retail client* would reasonably associate with environmental and social *sustainability characteristics*.

Specific criteria

3.2.5 R A *firm* must, in addition to the general criteria, meet the specific criteria in relation to a particular *sustainability label* referred to in *ESG 3.1.1R(1)* before it can apply that label to a *sustainability product*.

Sustainable focus

3.2.6 R The specific criteria for the *sustainability label* 'sustainable focus' are as follows:

- (1) A *firm* must ensure that at least 70% of the *sustainability product's* assets either:
 - (a) meet a credible standard of environmental and/or social sustainability, in accordance with *ESG 3.2.6R(2)*; or
 - (b) align with a specified environmental and/or social sustainability theme.
- (2) A credible standard for the purposes of *ESG 3.2.6R(1)(a)* means that the standard must be robust, independently assessed, evidence-based and transparent.
- (3) If, for reasons beyond a *firm's* control, the *sustainability product's* assets cease to meet the requirements of *ESG 3.2.6R(1)*, the *firm* must take action to restore compliance as soon as reasonably practicable, having regard to the interests of the *firm's clients*.
- (4) A *firm* must ensure that, in specifying KPIs to assess the performance of a *sustainability product* under *ESG 3.2.3R(3)*, those KPIs include metrics that demonstrate:
 - (a) the ongoing alignment of the *sustainability product's* assets with a target environmental and/or social sustainability profile; and

- (b) the *sustainability product's* ongoing adherence to asset-level environmental and social *sustainability characteristics*, in accordance with its investment policy and strategy.

Sustainable improvers

3.2.7 R The specific criteria for the *sustainability label* 'sustainable improvers' are as follows:

- (1) A *firm* must ensure that a *sustainability product* is invested in assets that have the potential to become more sustainable over time, either environmentally and/or socially, including in response to investor stewardship.
- (2) A *firm* must ensure that, in specifying KPIs to assess the performance of a *sustainability product* under ESG 3.2.3R(3), those KPIs include metrics that demonstrate:
 - (a) a clear and measurable target for improvements in the sustainability profile of the assets in which the *sustainability product* invests;
 - (b) the long-term sustainability profile of a *sustainability product's* assets, as projected over a period of more than one year;
 - (c) the extent to which improvements in the sustainability of a *sustainability product's* assets have been achieved over time, including through investor stewardship;
 - (d) in relation to the *firm's* stewardship:
 - (i) how the *firm's* stewardship strategy has been applied to support improvements in the environmental and/or social sustainability of assets, in accordance with the *sustainability product's sustainability objective*;
 - (ii) the stewardship activities undertaken in relation to improving the sustainability profile of the *sustainability product's* assets in accordance with the product's *sustainability objective*;
 - (iii) the outcomes achieved (including any improvements in the sustainability profile of the *sustainability product's* assets over time); and
 - (iv) matters escalated in accordance with the requirements in ESG 3.2.3R(5);
 - (e) how the *sustainability product's* assets meet the asset-level selection criteria as set out in ESG 3.2.3R(2)(c)-(d); and

- (f) the changes (if any) in the sustainability profile of the *sustainability product's* assets over time, distinguishing between any improvement or deterioration in the sustainability profile of individual assets and changes arising from asset rotation.

Sustainable impact

- 3.2.8 R The specific criteria for the *sustainability label* ‘sustainable impact’ are as follows:
- (1) A *firm* must ensure that a *sustainability product's sustainability objective* aims to achieve a pre-defined, positive, measurable real-world outcome, in relation to an environmental and/or a social outcome.
 - (2) A *firm* must develop:
 - (a) a *theory of change*, in line with the *sustainability product's sustainability objective*, emphasising how its *investment* process aims to contribute to addressing environmental and/or social problems;
 - (b) a robust method to measure and demonstrate that its *investment* activities have had a positive real-world impact, environmentally and/or socially;
 - (c) an escalation plan, should the anticipated real-world impact no longer be plausibly achievable, including the potential divestment of assets.
 - (3) A *firm* must, in specifying KPIs, apply enhanced impact measurement, and reporting based on industry best practices.

3.3 Naming and marketing

- 3.3.1 R A *firm* (whether it is undertaking *sustainability in-scope business* or not, including *firms* that *approve financial promotions* for *unauthorised persons*) must ensure that any reference to the *sustainability characteristics* of a product or service is:
- (1) consistent with the sustainability profile of the product or service; and
 - (2) clear, fair and not misleading.
- 3.3.2 R (1) Subject to *ESG 3.3.3R*, *ESG 4.3.4R* and any other *rules* or legal requirements to which a *firm* is subject in relation to disclosing certain information, a *firm* must comply with the restrictions in *ESG 3.3.2R(2)* and *ESG 3.2.3R(3)* in circumstances where the *firm*:
- (a) is undertaking *sustainability in-scope business* in relation to *retail clients* in respect of *sustainability products*; and

- (b) does not use a *sustainability label* in relation to that *sustainability product*.
- (2) A *firm* must not use the following terms in relation to the naming or marketing of a *sustainability product*:
- (a) ‘ESG’ (or ‘environmental’, ‘social’ or ‘governance’);
 - (b) ‘climate’;
 - (c) ‘sustainable’ or ‘sustainability’;
 - (d) ‘green’;
 - (e) ‘transition’;
 - (f) ‘net zero’;
 - (g) ‘impact’;
 - (h) ‘responsible’;
 - (i) ‘sustainable development goals’ or ‘SDG’;
 - (j) ‘Paris-aligned’; and
 - (h) any other term which implies that a *sustainability product* has *sustainability characteristics*.
- (3) A *firm* that is using the *sustainability label*, ‘sustainable focus’ or ‘sustainable improvers’ in relation to a *sustainability product* must not use the word ‘impact’ in the name of that product.
- 3.3.3 R A *firm* that is undertaking *sustainability in-scope business* in relation to a *sustainability product* that is an agreement or arrangement to provide a *retail client* with *portfolio management* and does not use a *sustainability label* under *ESG 3.1.1R(2)(b)* may, in the name, *pre-contractual materials* or other marketing communications relating to that *sustainability product*, use the terms set out in *ESG 3.3.2R(2)*, providing that:
- (1) 90% of the total value of the products in which the relevant *portfolio* invests use a *sustainability label*; and
 - (2) the terms set out at *ESG 3.3.2R(2)* are not used in a way that is misleading.

4 Disclosure of sustainability-related information

4.1 Preparation of sustainability disclosures

- 4.1.1 R (1) Subject to *ESG 4.1.1R(2)*, a *firm* that is undertaking *sustainability in-scope business* must prepare the following disclosures in accordance with this chapter, as follows:
- (a) a *consumer-facing disclosure*; and
 - (b) where a *firm* uses a *sustainability label* in relation to a *sustainability product*, a *pre-contractual disclosure* in relation to that product.
- (2) A *firm* that is undertaking *sustainability in-scope business* in relation to a *sustainability product* that is an agreement or arrangement to provide a *client* with *portfolio management* is subject to the following *rules*:
- (a) a *firm* is exempt from the requirements of *ESG 4.2* and *ESG 4.3* in relation to that *sustainability product*;
 - (b) a *firm* must, for *retail clients*, publish in accordance with *ESG 4.1.1R(3)* an index of all the *sustainability products* in which the relevant *portfolio* invests, with details as to:
 - (i) the *sustainability label* (if any) that each of those individual *sustainability products* is using; and
 - (ii) the *consumer-facing disclosure* that relates to that *sustainability product* (including providing hyperlinks to that information).
- (3) A *firm* must, for the purposes of *ESG 4.1.1R(1)* and *ESG 4.1.1R(2)(b)*, publish the required information on the *relevant digital medium* for the business of the *firm*, locating it in a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered.

Reviewing consumer-facing disclosures and pre-contractual disclosures

- 4.1.2 R (1) A *firm* must ensure that a *consumer-facing disclosure* and *pre-contractual disclosure* remain consistent with the *sustainability label* (if any) that is used in relation to a *sustainability product*.
- (2) A *firm* must, in relation to a *consumer-facing disclosure* and *pre-contractual disclosure* pertaining to a *sustainability product*:
- (a) keep under review that disclosure – in particular:
 - (i) a *firm* must, at least every 12 *months*, review the disclosure and provide an update on the progress of the *sustainability product* in meeting its *sustainability objective*, ensuring that up-to-date metrics and information is used; and

- (ii) a *firm* must review the disclosure prior to any proposed change to a *sustainability product* with respect to the continued accuracy of that disclosure in relation to the *sustainability product*.
 - (b) following a review under ESG 4.1.2R(2)(a), revise the disclosure as appropriate to ensure that it continues to reflect the *sustainability product* accurately.
- 4.1.3 R A *firm* must, where it has revised a *consumer-facing disclosure* or a *pre-contractual disclosure* in relation to a *sustainability product*:
- (1) give prior written notice to *clients* who have invested in that product that the *consumer-facing disclosure* or the *pre-contractual disclosure* has been revised and the reasons for that revision as soon as practicable and in any event, at least 60 *days* before that change takes effect:
 - (2) publish, within 60 *days* of the change having occurred, the following information on the *relevant digital medium* for the business of the *firm*, locating it in a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered:
 - (a) the revised *consumer-facing disclosure* or *pre-contractual disclosure*;
 - (b) the reasons for the revision; and
 - (c) in the case of a *consumer facing disclosure*, the date of the revised disclosure.

4.2 Consumer-facing disclosures

- 4.2.1 R A *firm* that is undertaking *sustainability in-scope business* must prepare and publish *consumer-facing disclosures* for *retail clients* in relation to each of its *sustainability products*.
- 4.2.2 R A *firm* must include the following information in the *consumer-facing disclosure* which relates to a *sustainability product*:
- (1) the *firm's* name;
 - (2) the name of the *sustainability product* to which the *consumer-facing disclosure* relates;
 - (3) the *International Securities Identification Number (ISIN)* or other unique identifier (if any) for that *sustainability product*;

- (4) the *sustainability product's sustainability objective*, clearly signposted as the *firm's* 'sustainability goal' for that product, including a summary of:
- (a) the extent to which the product's *sustainability objective* may have impacted, or may be expected to impact, on the financial return of that particular *sustainability product*; and
 - (b) the *firm's* progress in meeting the *sustainability objective* in relation to that product;
- (5) the *sustainability label* which the *firm* uses in relation to that *sustainability product*, together with the relevant descriptor for that label, as follows:
- (a) for the *sustainability label* 'sustainable focus', the relevant descriptor is: 'invests mainly in assets that are sustainable for people or the planet';
 - (b) for the *sustainability label*, 'sustainable improvers', the relevant descriptor is: 'invests in assets that may not be sustainable now, with an aim to improve the sustainability of those assets for people or the planet over time';
 - (c) for the *sustainability label* 'sustainable impact', the relevant descriptor is: 'invests in solutions to problems affecting people or the planet to achieve a real-world impact';
- (6) a summary of the key elements of the *firm's investment strategy* in pursuing the *sustainability product's sustainability objective* which is clearly signposted as the *firm's* 'sustainability approach' and:
- (a) sets out the key *sustainability characteristics* of assets in which that *sustainability product* will and will not invest;
 - (b) ensures that the *firm* uses language that is familiar and comprehensible to *retail clients* by effectively and accurately describing the strategy in plain English; and
 - (c) sums up the *firm's* approach to stewardship.
- (7) a summary of any of the *sustainability product's investments* which are inconsistent with (or may be reasonably perceived as being inconsistent with) the *sustainability objective* of that particular *sustainability product* which is clearly signposted as the *firm's* 'unexpected investments' and sets out:
- (a) the type of *investment* concerned and the particular industry in which it arises; and
 - (b) why the *firm* is holding that *investment*.

- (8) a summary of the relevant metrics, for example, KPIs, in relation to that *sustainability product* which is clearly signposted as the *firm's* 'sustainability metrics' and sets out:
- (a) the *firm's* KPIs, calculated using the most up-to-date data as at the time of preparing the *consumer-facing disclosure*, in relation to achieving the *sustainability product's sustainability objective*;
 - (b) any relevant contextual information, such as explaining how the metrics, for example, the KPIs should be interpreted; and
 - (c) any other metrics that a *retail client* might reasonably find useful in understanding the *firm's* approach in meeting the *sustainability product's sustainability objective* and the progress that the *firm* has made in achieving that objective;
- (9) details (including, as appropriate, hyperlinks) as to where a *retail client* can easily access the following information:
- (a) the relevant *pre-contractual disclosures* in relation to the *sustainability product* including, where applicable, Part A of the *public product-level sustainability report* in relation to that *sustainability product*;
 - (b) Part B of the *public product-level sustainability report* in relation to the relevant *sustainability product*;
 - (c) the *firm's sustainability entity report*;
 - (d) other non-sustainability related information in relation to a *sustainability product*, such as (for example) costs and charges that are associated with that product; and
- (10) the date of the disclosure.
- 4.2.3 R A *firm* must ensure that the information at ESG 4.2.2R(4) is located in a prominent place at the front of the *consumer-facing disclosure*.
- 4.2.4 G A *firm* may, in considering the types of *investment* that may be reasonably perceived to be inconsistent with a *sustainability product's sustainability objective* under ESG 4.2.2R(7), consider disclosing the particular sector where appropriate, or trade-offs within the sustainability profile of a company, or any other factors that the *firm* would reasonably expect its *retail clients* to perceive as inconsistent.
- 4.2.5 G A *firm* may, for the purposes of ESG 4.2.2R(9)(d) choose to refer to documents such as the *key information document* or the *key investor information document* in relation to the particular *sustainability product*.
- 4.2.6 R A *firm* must ensure that a *consumer-facing disclosure* is clear, concise and can be easily understood by *retail clients* and that:

- (1) it does not exceed 2 pages of printed A4 paper in length;
- (2) it is accessible in digital format; and
- (3) it complies with *PRIN 2A.5.8R* to *PRIN 2A.5.12R* in tailoring a *consumer disclosure* appropriately to the needs of its *retail clients*;

4.2.7 R A *firm* that does not use a *sustainability label* in relation to a *sustainability product* must, in meeting the requirements in *ESG 4.2.1R* and *ESG 4.2.6R*, include in a *consumer-facing disclosure* an entry for each aspect of *ESG 4.2.2R* against which it is required to report, with ‘no sustainable label’ in the label field and using the words ‘not applicable’ or the acronym, ‘N/A’ in other fields.

4.2.8 R A *firm* must ensure it keeps a copy of each version of its published *consumer-facing disclosure* and provide a copy on request from a *retail client* or the *FCA*.

Publication of a consumer-facing disclosure

4.2.9 R (1) A *firm* must publish a *consumer-facing disclosure* on the *relevant digital medium* for the business of the *firm*, locating it in a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered.

(2) A *firm* must ensure that, in publishing a *consumer-facing disclosure*, it is easy for *retail clients* (including prospective *retail clients*) to:

- (a) identify the particular *sustainability product* to which the *consumer-facing disclosure* relates;
- (b) identify the relevant *sustainability label* (if any); and
- (c) access the information set out at *ESG 4.2.2R(9)*.

4.2.10 G If a *firm* chooses to use a hyperlink in order to comply with *ESG 4.2.9R(2)*, it should ensure that the *consumer-facing disclosure* is available at no more than one mouse click away from the specific webpage at which the relevant *sustainability label* (if any) is located.

4.3 Pre-contractual disclosures

4.3.1 R Where a *firm* uses a *sustainability label* in relation to a *sustainability product* it must include the following information in a clear and accessible way in either the *pre-contractual materials* for that particular *sustainability product* or, where that product does not have *pre-contractual materials*, Part A of the *public-product-level sustainability report* relating to that product, in accordance with *ESG 4.5.2R* to *ESG 4.5.5R*:

- (1) the *sustainability label* that the *firm* is using in relation to the *sustainability product*;

- (2) the *sustainability product's sustainability objective*, as part of its *investment objectives*, including with respect to achieving a financial return on that product, set out in specific and measurable terms;
- (3) details of the extent to which the *sustainability objective* has, or may have, impacted on the financial return of that particular *sustainability product*;
- (4) details of the plausible, purposeful and credible link between the *sustainability product's sustainability objective* and an environmental and/or a social outcome, as set out in *ESG 3.2.3R(1)(b)*;
- (5) details of the *sustainability product's investment policy and strategy* and the way that these align with the product's *sustainability objective*;
- (6) a description of the *sustainability product's investible universe* and its asset-level selection criteria referred to in *ESG 3.2.3R(2)(c)-(d)* above in specific and measurable terms, including:
 - (a) how the *firm* assesses the assets in which the *sustainability product* invests against the selection criteria;
 - (b) how the selection criteria relate to the target environmental and social profile of the *sustainability product's assets*;
 - (c) how the target environmental and/or the social profile of the *sustainability product's assets* align with the product's *sustainability objective*; and
 - (d) the conditions under which an asset in which a *sustainability product* has invested may cease to meet the specified criteria for asset selection.
- (7) details of the *firm's policies and procedures* to determine, measure, monitor, evaluate and report to *clients* on the environmental and social sustainability profile of the *sustainability product's assets* over time;
- (8) details of the *firm's target asset composition* in respect of the *sustainability product*, including:
 - (a) the different asset classes in which the product will invest, its use of derivatives, and its long-term and short-term exposures; and
 - (b) the processes by which it complies with *ESG 3.2.3R(2)(e)* and a description of the environmental and social *sustainability characteristics* of assets (or asset types) in which that *sustainability product* will and will not invest;
- (9) details of any *sustainability product's assets* identified in *ESG 3.2.3R(2)(f)*;

- (10) where the *sustainability product* is an index-tracking product, how the index provider's methodology for index-construction aligns with the *sustainability product's sustainability objective* and its target environmental and/or social sustainability profile; and
- (11) details, set out in a clear and accessible way, of the *firm's* stewardship strategy and resources (at firm-level or product-level), including:
 - (a) details as to any differences or conflicts between the *firm's* firm-level stewardship strategy and its product-level stewardship strategy in relation to a *sustainability product*, including any specific targets or constraints applied at the product level (for example, product-specific engagement or voting strategy);
 - (b) details as to the *firm's* commitment to the UK Stewardship Code 2020, published by the Financial Reporting Council;
 - (c) the specific methods the *firm* uses to influence sustainability outcomes across the *sustainability product's* assets; and
 - (d) how the *firm* applies its strategy and resources in a manner consistent with the *sustainability product's sustainability objective*.

4.3.2 R In addition to the information set out in *ESG 4.3.1R*, a *firm* must also include the following information in the *pre-contractual disclosures* for a *sustainability product* in either the product's *pre-contractual materials* or, where the product does not have *pre-contractual materials*, Part A of the relevant *public product-level sustainability report* in accordance with *ESG 4.5.2R* to *ESG 4.5.5R*:

- (1) a *firm* must, where it uses the *sustainability label* 'sustainable improvers', describe in relation to its asset-level selection criteria at *ESG 3.2.3R(2)(c)-(d)*, how the *firm* assesses potentially investible assets to determine the extent to which improvements in sustainability can be achieved over time, including through investor stewardship;
- (2) a *firm* must, where it uses the *sustainability label* 'sustainable impact', include the following information:
 - (a) the *firm's theory of change*, with clear examples that emphasise how its *investment* process aims to contribute to addressing environmental and/or social problems, in line with its *sustainability objective*;
 - (b) a robust method to measure and demonstrate that its *investment* activities have had a positive environmental and/or social sustainability impact;
 - (c) the *firm's* escalation plan should the real-world outcome no longer plausibly be achievable, including potential divestment of assets;

- (d) in relation to specifying its asset-level selection criteria at *ESG 3.2.3R(2)(c)-(d)*, a firm must set out how it assesses potentially investible assets to determine:
 - (i) whether those assets align with the *sustainability product's theory of change*, while also avoiding unintended negative consequences; and
 - (ii) the extent to which a positive, measurable outcome can be achieved, environmentally and/or socially.
- 4.3.3 R A firm must, in order to meet the requirements of *ESG 4.3.1R(5)* to *ESG 4.3.1R(11)*, set out the required information in a dedicated section of the *pre-contractual materials* relating to the particular *sustainability product* (unless that information is otherwise being included in Part A of the relevant *public product-level sustainability report* for that *sustainability product* in accordance with *ESG 4.5.2R* to *ESG 4.5.5R*).
- 4.3.4 R A firm must, where a *sustainability product* has *sustainability characteristics* as an integral part of its *investment policy* or strategy but does not meet the criteria under *ESG 3.2* to use a *sustainability label*, set out in the *pre-contractual materials* for that *sustainability product* or, where the product does not have *pre-contractual materials*, Part A of the relevant *public product-level sustainability report* in accordance with *ESG 4.5.2R* to *ESG 4.5.5R*:
 - (1) the specific *sustainability characteristics* of that product;
 - (2) the firm's *sustainability objective* (if any) in relation to that product; and
 - (3) the firm's *investment policy* and strategy in relation to that product.
- 4.3.5 G In meeting the requirements of *ESG 4.3.4R*:
 - (1) a firm is reminded of the requirements of *ESG 3.3.1R*; and
 - (2) the reference to 'integral' in the context of this rule means that a firm's *sustainability product* has specific *sustainability characteristics* and that the firm has specific policies and strategies in place with respect to those characteristics.

4.4 Preparation of sustainability reports

- 4.4.1 R (1) Subject to *ESG 4.4.1R(2)* and *ESG 4.4.1R(3)*, a firm that is undertaking *sustainability in-scope business* in relation to a *sustainability product* must prepare and publish for *clients* the following reports in accordance with this chapter:
 - (a) A firm that uses a *sustainability label* in relation to a *sustainability product* must prepare:

- (i) Part A of a *public product-level sustainability report*, in circumstances where *ESG 4.5.2R to ESG 4.5.5R* apply;
 - (ii) Part B of a *public product-level sustainability report*.
 - (b) A *firm* must, subject to *ESG 1.2.2R*, prepare a *sustainability entity report*, regardless of whether it uses a *sustainability label* in relation to a *sustainability product*.
 - (2) A *firm* that is undertaking *sustainability in-scope business* in relation to a *sustainability product* that is agreement or arrangement under which a *firm* provides a *client* with *portfolio management* is exempt from the requirements of *ESG 4.5*, except with respect to *ESG 4.5.14.R to ESG 4.5.16R*.
 - (3) A *firm* that is undertaking *sustainability in-scope business* in relation to a *sustainability product* that is an agreement or arrangement to provide a *client* with *portfolio management* must provide *retail clients* with easy access (for example, by providing hyperlinks) to the following information in relation to each *sustainability product* in which the relevant *portfolio* invests:
 - (a) the *pre-contractual disclosures* in relation to the *sustainability product* (if any) including, where the product does not have *pre-contractual materials*, Part A of the relevant *public product-level sustainability report*, in accordance with *ESG 4.5.2R to ESG 4.5.5R*; and
 - (b) Part B of the *public product-level sustainability report* (if any) for the relevant *sustainability product*.
- 4.4.2 R (1) Subject to *ESG 4.4.2R(2)*, the following provisions of *ESG 2* apply for the purposes of this chapter, where the references to ‘*TCFD entity report*’ and ‘*public TCFD product reports*’ are substituted for the references ‘*sustainability entity report*’ and ‘*public product-level sustainability report*’, respectively:
- (a) *ESG 2.1.1R(1)*;
 - (b) *ESG 2.1.2R(1)*;
 - (c) *ESG 2.1.2R(2)*;
 - (d) *ESG 2.1.2R(3)*;
 - (e) *ESG 2.1.3R*; and
 - (f) *ESG 2.1.4G*.

(2) *ESG 4.4.2R(1)* does not apply in relation to the preparation and publication of Part A of a *public product-level sustainability report* under *ESG 4.5.2R* to *ESG 4.5.5R*.

4.4.3 R A *firm* must, where it is required to prepare a *public TCFD product report*, include the contents of that report (or a hyperlink to it) in Part B of a *public product-level sustainability report*, making clear that the *public TCFD product report* forms part of the *firm's* overall Part B of a *public product-level sustainability report* with respect to climate-related disclosures.

4.4.4 R A *firm* must, where it is required to prepare a *TCFD entity report*, include the contents of that report (or a hyperlink to it) in its *sustainability entity report*, making clear that the *TCFD entity report* forms part of the *firm's* overall *sustainability entity report* with respect to climate-related disclosures.

Data considerations when preparing sustainability reports

4.4.5 R A *firm* must comply with *ESG 4.4.6R* to *ESG 4.4.11R* in relation to preparing Part B of a *public product-level sustainability report* or a *sustainability entity report*.

4.4.6 R In satisfying its reporting and disclosure obligations under this chapter 4.4, a *firm* must, insofar as is reasonably practicable, use the most up to date information available.

4.4.7 R In preparing Part B of a *public product-level sustainability report*, a *firm* must select, from within the 12-month reporting period, the most recent calculation date for which up-to-date information is available.

4.4.8 R A *firm* must not disclose metrics where:

- (1) there are gaps in underlying data or methodological challenges; and
- (2) these data gaps or methodological challenges cannot be addressed using proxy data or assumptions without the resulting disclosure, in the reasonable opinion of the *firm*, being misleading.

4.4.9 R A *firm* must ensure that Part B of a *public product-level sustainability report* and a *sustainability entity report* include an adequate explanation of:

- (1) any gaps in the underlying data relied upon to make sustainability-related disclosures;
- (2) how the *firm* has addressed these gaps, for example, by using proxy data or assumptions and briefly setting out any methodologies used in doing so, providing relevant contextual information and explaining any limitations of the approach;
- (3) any metrics that the *firm* has not been able to disclose, on the basis that *ESG 4.4.8R* applies; and

- (4) in respect of *ESG 4.4.9R(2)*:
- (a) the gaps in underlying data or methodological challenges that have resulted in the *firm* being unable to make the relevant disclosure;
 - (b) why the *firm* has not been able to address those gaps or challenges using proxy data or assumptions; and
 - (c) what steps the *firm* will take to address those gaps or challenges in the future.

4.4.10 G In addition, a *firm* may include in its *sustainability report* an explanation of the proportion of each *sustainability product* for which data are verified, reported, estimated or unavailable.

4.4.11 R Where a *firm* uses a *sustainability label* in relation to a *sustainability product*, it must ensure that the data it is relying upon in order to meet the criteria at *ESG 3.2* is accurate and complete (including using proxies and assumptions where appropriate).

Cross-referencing third-party sustainability-related disclosures

4.4.12 R A *firm* must comply with *ESG 4.4.13R* to *ESG 4.4.15R* in relation to preparing Part B of a *public product-level sustainability report* or a *sustainability entity report*.

4.4.13 R A *firm* may include hyperlinks and cross-references to relevant sustainability-related disclosures contained in a third party's sustainability reporting, where such information enables the firm to prepare a Part B of a *public product-level sustainability report* or a *sustainability entity report*.

4.4.14 R The *firm* must set out the rationale for relying on any third-party sustainability disclosures, and any deviations between the third party's approach and that of the *firm*.

4.4.15 R Where relevant, a *firm* may also draw links and refer to Part B of its *public product-level sustainability report* from its *sustainability entity report* and vice versa.

4.5 Sustainability product-level reporting

Public product-level sustainability disclosures

4.5.1 R A *firm* that uses a *sustainability label* in relation to a *sustainability product* must prepare for *clients* a *public product-level sustainability report* in relation to that *sustainability product*, as follows:

- (1) In circumstances where *ESG 4.5.2R* applies, a *firm* must prepare Part A of a *public product-level sustainability report* in accordance with *ESG 4.5.3R* to *ESG 4.5.5R*.

- (2) A *firm* must prepare Part B of a *public product-level sustainability report* in accordance with *ESG 4.5.6R* to *ESG 4.5.13R*.

Form and content of Part A of a public product-level sustainability report

- 4.5.2 R A *firm* must prepare Part A of a *public product-level sustainability report* in circumstances where a *sustainability product* does not have *pre-contractual materials* that relate to it.
- 4.5.3 R A *firm* must ensure that Part A of a *public product-level sustainability report*:
- (1) contains the information set out in *ESG 4.3.1R* and *ESG 4.3.2R* and *ESG 4.3.4R* and *ESG 4.3.5G*; and
 - (2) is made available to *clients* before they invest in a *sustainability product*.
- 4.5.4 R A *firm* must publish Part A of a *public product-level sustainability report* on the *relevant digital medium* for the business of the *firm*, locating it at a prominent place on the specific webpage or page on a mobile application or other digital medium at which the *sustainability product* is offered.
- 4.5.5 R A *firm* must ensure that it keeps the information set out in Part A of a *public product-level sustainability report* under review in accordance with *ESG 4.1.2R* and *ESG 4.1.3R*.

Form and content of Part B of a public product-level sustainability report

- 4.5.6 R *ESG 2.3.1R* to *ESG 2.3.4R* apply for the purposes of a *firm* preparing Part B of a *public product-level sustainability report*, where the reference to '*public TCFD product report*' is substituted with the reference to '*public product-level sustainability report*'.
- 4.5.7 R In addition to the requirements at *ESG 4.4.3R*, a *firm* must also include the following information in Part B of a *public product-level sustainability report* in relation to a *sustainability product*:
- (1) the *sustainability label* that the *firm* is using in relation to the *sustainability product*;
 - (2) details of the *sustainability product's sustainability objective*;
 - (3) details as to the *firm's* progress in meeting the *sustainability objective* in relation to a *sustainability product*;
 - (4) details as to how a *sustainability product* invests in accordance with its *investment* policy and strategy on an ongoing basis;
 - (5) details of the *sustainability product's* performance against the KPIs specified at *ESG 3.2.3R(3)*;

- (6) in circumstances where stewardship plays a significant role in its *investment* policy and strategy in relation to a *sustainability product*, details as to:
 - (a) the *firm's* stated KPIs related to stewardship as set out at *ESG 3.2.3(5)(c)*, including engagement and voting activity relevant to the delivery of the *sustainability product*; and
 - (b) the outcome of the *firm's* active stewardship activities, with reference to the *sustainability product's sustainability objective*;
- (7) details of the relevant metrics, for example KPIs (other than those set out in *ESG 4.5.7R(5)* and *ESG 4.5.7R(6)*) that a *retail client* might reasonably find useful in understanding the *firm's* approach in:
 - (a) meeting the *sustainability product's sustainability objective* and the progress that the *firm* has made in achieving that objective; or
 - (b) deciding whether to select a particular *sustainability product*;
- (8) details of the following information, where this is relevant to a *retail client's* understanding of the metrics set out at *ESG 4.5.7R(5)* to *ESG 4.5.7R(7)*:
 - (a) relevant contextual information such as explaining how the metrics should be interpreted and their associated limitations, for example, if particular assumptions or proxies have been used; and
 - (b) historical annual calculations of the metrics in *ESG 4.5.7R(5)* to *ESG 4.5.7R(7)* after the first year of preparing Part B of a *public product-level sustainability report* in relation to the *sustainability product* that enables *clients* to compare the *sustainability product's* sustainability performance year-on-year in a way that is easy to understand and is not misleading;
- (9) details (if any) where the *firm's* approach in relation to a *sustainability product* deviates materially from the *firm's* overarching approach disclosed in the *firm's sustainability entity report*; and
- (10) the date of the report.

4.5.8 R In addition to the information set out in *ESG 4.5.7R*, a *firm* must also include the following information in relation to Part B of a *public product-level sustainability report* relating to a *sustainability product*:

- (1) A *firm* must, where it uses the *sustainability label* 'sustainable focus' in relation to a *sustainability product*, include:
 - (a) the KPIs set out in *ESG 3.2.6R(4)(a)* and (b);

- (b) in relation to the *firm's* stewardship strategy for the *sustainability product*:
 - (i) how that strategy aims have been applied to achieve continuous improvement in the environmental and/or the social sustainability of the product's assets; and
 - (ii) the outcomes achieved in relation to meeting that strategy.
 - (2) A *firm* must, where it uses the sustainability label, 'sustainability improvers' in relation to a *sustainability product*, include the matters set out in ESG 3.2.7R(2).
 - (3) A *firm* must, where it uses the sustainability label, 'sustainable impact' in relation to a *sustainability product*, include:
 - (a) the *firm's* KPIs in accordance with ESG 3.2.8R(3), including:
 - (i) the *firm's* analysis as to how its actions have contributed to the impact achieved; or
 - (ii) the *firm's* explanation as to why its actions have not done so;
 - (b) details as to how the *firm's* rights and influence (including through direct control as relevant) have been applied to pursue the pre-defined, positive, measurable real-world outcome specified in the *sustainability product's sustainability objective*, in line with its *theory of change* for that *sustainability product*.
- 4.5.9 G A *firm* may, for the purposes of ESG 4.5.7R(6)(b), choose to cross-reference and include a hyperlink in its *public product-level sustainability report* to a report that it has published for the purposes of demonstrating its compliance with the UK Stewardship Code 2020, published by the Financial Reporting Council.
- 4.5.10 G To the extent that a *firm* discloses the metrics referred to at ESG 4.5.7R(7), it should clearly explain the methodology used in providing each relevant metric and ensure that the metrics calculated under ESG 4.5.7R(5) and ESG 4.5.7R(6) are at least as prominently presented.
- 4.5.11 G The metrics *referred to* in ESG 4.5.7R(7) may include (for example) KPIs that are not linked specifically to the *sustainability objective* of the *sustainability product*, but which may be common metrics within a particular certain sector.
- 4.5.12 G If a *firm* discloses material deviations under ESG 4.5.7R(9), it may refer to the relevant sections of its *sustainability entity report*, and similarly its *sustainability entity report* may refer to these disclosures in Part B of its *public product-level sustainability report*.

Reviewing Part B of a public product-level sustainability report

- 4.5.13 R (1) A *firm* must ensure that Part B of a *public product-level sustainability report* remains consistent with the *sustainability label* that is used in relation to a *sustainability product*, as well as the disclosures required under *ESG 4.2* and *ESG 4.3* in relation to that *sustainability product*.
- (2) Where a *firm* has revised a *sustainability label*, it must update Part B of a *public product-level sustainability report* as appropriate to coincide with the publication of the revised label and disclosure.

On-demand product-level sustainability information

- 4.5.14 R (1) A *client* who requires *on-demand sustainability information* in order to satisfy sustainability-related disclosure obligations, whether under this chapter or as a result of other legal or regulatory requirements, is entitled to request such information from, and be provided with it by, the *firm* and to receive a response to that request.
- (2) On receipt of a request from a *client* under *ESG 4.5.14R(1)*, a *firm* must provide *on-demand sustainability information* as at a calculation date determined in accordance with *ESG 4.4.7R* or at an alternative calculation date where this has been agreed between the *client* and the *firm*.
- (3) The request by a *client* in *ESG 4.5.14R(1)* may be made no earlier than 1 July 2025 in respect of any reporting period of the *firm* under *ESG 4.4.2R(1)(b)* which starts after 30 June 2024 or, if later, with effect from the reporting period in which the *client's* arrangements with the *firm* concerning the *sustainability product* commenced.
- (4) If a *firm* receives a request for an *on-demand sustainability report* from a *person* who is entitled to make such request, it must prepare and provide the *on-demand sustainability information* for the *person*:
- (a) within a reasonable period of time;
 - (b) subject to *ESG 4.5.14(4)(c)*, in a format which the *firm*, acting reasonably, considers appropriate to meet the information needs of that *person*;
 - (c) ensuring that, where the *firm* receiving the request for *on-demand information* is:
 - (i) an *unauthorised AIF* managed by a *UK AIFM* which is not listed on a *recognised investment exchange*, that *firm* includes the information set out in *ESG 4.4.3*, *ESG 4.5.2R* to *ESG 4.5.5* (as applicable) and *ESG 4.5.7R* and *ESG 4.5.8R*; or
 - (ii) a *firm* that is undertaking *portfolio management* in relation to the relevant *person*, that *firm* provides the information set out at *ESG 4.4.1R(3)(b)*.

- 4.5.15 R The entitlement in *ESG 4.5.14R(1)* is limited to one request for *on-demand product-level sustainability information* in respect of each *sustainability product* in each of the *firm's* reporting periods under *ESG 4.4.2R(1)(b)*.
- 4.5.16 G A *firm* is encouraged to consider, where practicable, making available to a *client*, disclosures broadly equivalent to Part A and Part B of a *public product-level sustainability report* irrespective of the *client's* eligibility to request such information under *ESG 4.5.14R(1)*.

4.6 Sustainability entity report

Content of a sustainability entity report

- 4.6.1 R In addition to the requirements at *ESG 4.4.4R*, a firm must include in its *sustainability entity report* the following information relating to the overall assets managed by the *firm* within its *sustainability in-scope business*:
- (1) a *firm* must set out in its *sustainability entity report*:
 - (a) the *firm's* approach to governance, with respect to managing sustainability risks and opportunities;
 - (b) the actual and potential impacts of any material sustainability-related risks and opportunities on the *firm's* businesses, strategy and financial planning;
 - (c) how the *firm* identifies, assesses and manages sustainability-related risks; and
 - (d) the metrics and targets used by the *firm* to assess and manage relevant material sustainability-related risks.
 - (2) A *firm* must explain, either in its *sustainability entity report* or in a cross-referenced *public product-level sustainability report*, where its approach to a particular *investment* strategy, asset class or product is materially different to its overall entity level approach to governance, strategy, risk management or targets and metrics.
 - (3) A *firm* must, where relevant, briefly explain in its *sustainability entity report* how the *firm's* strategy has influenced the decision making and process by which it delegates functions, selects delegates, and relies on services, strategies or products offered or employed by third parties, including delegates.
- 4.6.2 G The *FCA* considers the following documents relevant in relation to a *firm* determining the content of disclosures under *ESG 4.6.1R(1)*:
- (1) the *IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information*, with respect to the *firm's* disclosures on governance, strategy, risk management and metrics and targets; and

- (2) the Sustainability Accounting Standards Board standards with respect to relevant sector-specific matters.

4.6.3 G A *firm* should, in meeting the requirements of ESG 4.6.1R(1):

- (1) consider disclosing sustainability-related topics that it has prioritised in its governance, strategy and risk management, and the rationale for doing so; and
- (2) refer to part 4, section D of the *TCFD Annex*, entitled ‘Asset managers’ in determining how to make disclosures required under ESG 4.6.1R(1) with respect to assets managed on behalf of *clients*.

4.6.4 R Where a *firm* uses a *sustainability label* in relation to a *sustainability product* it must include the following information in a clear and accessible way in a *sustainability entity report*:

- (1) a *firm* must describe the arrangements and resources it has in place to oversee the sustainability research, data and analytical tools that it uses to support the achievement of the *sustainability product’s sustainability objective*, as set out in ESG 3.2.3R(4)(c); and
- (2) a *firm* must describe the resources, governance and organisational arrangements that appropriately support and incentivise the high-quality delivery of its *investment policy* and strategy in line with a *sustainability product’s sustainability objective*, as set out in ESG 3.2.3R(4)(d).

Approach to relevant sustainability-related disclosures contained in other reports at an entity-level

- 4.6.5 R
- (1) If a *firm* is a member of a group, it may rely on disclosures consistent with those of the group or a member of its group when producing its *sustainability entity report*, but only to the extent that those group disclosures are relevant to the *firm* and cover the assets the *firm* manages as part of its *sustainability in-scope business*.
 - (2) If a *firm* does rely on such group disclosures, it must ensure that its *sustainability entity report*:
 - (a) includes cross-references, including hyperlinks, to any disclosures contained within the group or group member’s report that relate to assets managed by the *firm* in relation to its *sustainability in-scope business* on which the *firm* is relying to meet its disclosure obligations under this section; and
 - (b) sets out the rationale for relying on the disclosure made by its group or a member of its group and why the disclosure is relevant to the assets managed by the *firm* in relation to its sustainability in-scope business.

- 4.6.6 R A *firm* must also ensure that any material deviations between its approach to governance, strategy, risk management or targets and metrics as disclosed under *ESG 4.6.1R* and that the disclosures contained within the group report are clearly explained, either in its *sustainability entity report* or in the report made by its group or a member of its group.
- 4.6.7 R (1) If a *firm* or a member of its group produces a document, other than its annual financial report, which includes *sustainability characteristics*, the *firm* may cross-refer to these disclosures in its *sustainability entity report* where this information is relevant to *clients* or a person who is an investor in an unauthorised *AIF* managed by a UK *AIFM*, including hyperlinks to where the relevant disclosures are available.
- (2) Where a *firm* so refers, it must explain in its *sustainability entity report* the rationale for relying on the disclosures in the supplementary document and how such disclosures are relevant to the *clients* or a person who is an investor in an unauthorised *AIF* managed by a UK *AIFM* of the *firm's sustainability in-scope business*.

Compliance statement

- 4.6.8 R *ESG 2.2.7R* applies in relation to the preparation of a compliance statement for the purposes of a *sustainability entity report* as if the reference to a *firm's TCFD entity report* has been substituted by the reference to a *firm's sustainability entity report*.

Amend the following as shown.

TP 1 Transitional provisions

| (1) | (2) Material to which the transitional provision applies | (3) | (4) Transitional provision | (5) Transitional provision: dates in force | (6) Handbook provision: coming into force |
|-----|---|-----|---|---|--|
| 1.1 | ... | | | | |
| 1.5 | <i>ESG 2.3.5R(3)</i> | R | For a <i>firm</i> to whom the disapplication in <i>ESG TP 1.1</i> or <i>ESG TP 1.2</i> is available, (a) the earliest reporting period for which a <i>person</i> | From 1 January 2022 | Effective date of instrument |

| | | | | | | |
|------------|--|----------|-----|---|---|-------------------------------------|
| | | | | can request <i>on-demand TCFD information</i> is to commence from 1 January 2023, and | | |
| | | | (b) | the earliest a <i>person</i> can request <i>on-demand TCFD information</i> is 1 July 2024. | | |
| 1.6 | <i>ESG 2.3.9R(1)(b)</i> | R | | The first reporting deadline for scope 3 greenhouse gas emissions is 30 June 2024. | From 1 January 2022 | Effective date of instrument |
| <u>1.7</u> | <u><i>ESG 3.3.1R</i></u> | <u>R</u> | | | From [TBC, provisionally the same date as publication of any FCA decision to make the proposed rules] | <u>Effective date of instrument</u> |
| <u>1.8</u> | <u><i>ESG 3 (excluding ESG 3.3.1R)</i></u> | <u>R</u> | (a) | For a <i>firm undertaking sustainability in-scope business, excluding portfolio management.</i> | From [TBC, provisionally 12 months from the date of publication of any FCA decision to make the proposed rules] | <u>Effective date of instrument</u> |
| | | | (b) | For a <i>firm undertaking portfolio management.</i> | From [TBC, provisionally 18 months from the date of publication of any FCA decision to make the proposed rules] | |

| | | | | | | |
|-------------|---|----------|-----|--|--|-------------------------------------|
| <u>1.9</u> | <u>ESG 4.1 to ESG 4.3</u> | <u>R</u> | | | <u>From [TBC, provisionally 12 months from the date of publication of any FCA decision to make the proposed rules]</u> | <u>Effective date of instrument</u> |
| <u>1.10</u> | <u>ESG 4.4 insofar as it relates to the preparation of Part A of a <i>public product-level sustainability report</i> and <i>ESG 4.5.2R to ESG 4.5.5R</i></u> | <u>R</u> | | | <u>From [TBC, provisionally 12 months from the date of publication of any FCA decision to make the proposed rules]</u> | <u>Effective date of instrument</u> |
| <u>1.11</u> | <u>ESG 4.4 insofar as it relates to the preparation of Part B of a <i>public product-level sustainability report</i> and <i>ESG 4.5, (excluding ESG 4.5.2R to ESG 4.5.5R)</i></u> | <u>R</u> | | | <u>From [TBC, provisionally 24 months from the date of publication of any FCA decision to make the proposed rules]</u> | <u>Effective date of instrument</u> |
| <u>1.12</u> | <u>ESG 4.4 insofar as it relates to the preparation of <i>entity sustainability reports</i> and <i>ESG 4.6</i></u> | <u>R</u> | (1) | <u>For a <i>firm</i> that meets the requirements of an <i>enhanced SMCR firm</i> pursuant to <i>SYSC 23 Annex 1 8.2R</i> paragraph 1 in relation to <i>sustainability in-scope business</i>.</u> | <u>From [TBC, provisionally 24 months from the date of publication of any FCA decision to make the proposed rules]</u> | <u>Effective date of instrument</u> |
| | | | (2) | <u>For a <i>firm</i> that does not meet the requirements of an <i>enhanced SMCR firm</i></u> | <u>From [TBC, provisionally 36 months from the date of publication of any FCA</u> | |

| | | | | | |
|--|--|--|---|--|--|
| | | | <p><u>pursuant to SYSC 23 Annex 1 8.2R paragraph 1 but has assets under management in relation to sustainability in-scope business of £5bn or more calculated as a 3-year rolling average on annual assessment.</u></p> | <p><u>decision to make the proposed rules]</u></p> | |
|--|--|--|---|--|--|

Annex E

Amendments to the Collective Investment Schemes sourcebook (COLL)

In this Annex, underlining indicates new text and striking through indicates deleted text.

4 Investor Relations

...

4.2 Pre-sale notifications

...

Table: contents of the prospectus

4.2.5 R This table belongs to *COLL* 4.2.2R (Publishing the prospectus).

| | |
|--|--|
| Document status | |
| ... | |
| Investment objectives and policy | |
| 3 | The following particulars of the investment objectives and policy of the <i>authorised fund</i> : |
| | (a) ... |
| | (aa) <u>the sustainability objective of the authorised fund (if any);</u> |
| | ... |
| ... | |
| Investment in overseas property through an intermediate holding vehicle | |
| 26A | If investment in an overseas immovable is to be made through an <i>intermediate holding vehicle</i> or a series of <i>intermediate holding vehicles</i> , a statement disclosing the existence of that <i>intermediate holding vehicle</i> or series of <i>intermediate holding vehicles</i> and confirming that the purpose of that <i>intermediate holding vehicle</i> or series of <i>intermediate holding vehicle</i> is to enable the holding of overseas immovables by the <i>scheme</i> . |
| <u>Sustainability information</u> | |
| <u>26B</u> | <u>The following information, as applicable:</u> |
| | (a) <u>where a sustainability label is used in relation to a scheme, the information set out at ESG 4.3.1R and ESG 4.3.2R, in the form prescribed at ESG 4.3.3R;</u> |

| | | |
|-----|-----|--|
| | (b) | <u>where a <i>sustainability label</i> is not used in relation to a <i>scheme</i>, but that <i>scheme</i> has <i>sustainability characteristics</i> as an integral part of its <i>investment policy</i> or strategy, the information set out at <i>ESG 4.3.4R</i>.</u> |
| ... | | |

4.5 Reports and accounts

...

Contents of the annual long report

- 4.5.7 R (1) An annual long report on an *authorised fund*, other than a *scheme* which is an *umbrella*, must contain:
- ...
- (e) the report of the auditor in accordance with *COLL 4.5.12R* (Report of the auditor); ~~and~~
- (f) subject to *COLL 4.5.7R(1)(g)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*; and
- (g) where a *sustainability label* is used in relation to a *scheme*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 4.5.6R*.
- (2) An annual long report on a *scheme* which is an *umbrella* must be prepared for the *umbrella* as a whole and must contain:
- (a) for each *sub-fund*:
- ...
- (iii) comparative information in accordance with *COLL 4.5.10R*; ~~and~~
- (iv) subject to *COLL 4.5.7R(2)(a)(v)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*; and
- (v) where a *sustainability label* is used in relation to a *sub-fund*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent

cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with ESG 4.5.6R;

...

...

...

Contents of the half-yearly long report

- 4.5.8 R (1) A half-yearly long report on an *authorised fund*, other than for a *scheme* which is an *umbrella*, must contain:
- ...
- (b) the report of the *authorised fund manager* in accordance with COLL 4.5.9R (Authorised fund manager's report); ~~and~~
- (c) subject to COLL 4.5.8R(1)(d), its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website in accordance with ESG 2.3.1R, where the half-yearly long report most closely follows the reporting deadline of 30 June, under ESG 2.1.1R(1); and
- (d) where a *sustainability label* is used in relation to a *scheme*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website in accordance with ESG 4.5.6R, where the half-yearly long report most closely follows the reporting deadline of 30 June, under ESG 4.4.2R(1)(a).
- (2) A half-yearly long report on a *scheme* which is an *umbrella*, must be prepared for the *umbrella* as a whole and must contain:
- (a) for each *sub-fund*:
- ...
- (ii) the report of the *authorised fund manager* in accordance with COLL 4.5.9R; ~~and~~
- (iii) subject to COLL 4.5.8R(2)(iv), its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with ESG 2.3.1R, where the half-yearly long report most closely follows the reporting deadline of 30 June, under ESG 2.1.1R(1); and

(iv) where a *sustainability* label is used in relation to a *sub-fund*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report’s location on the *firm’s* website, in accordance with *ESG 4.5.6R*, where the half-yearly long report most closely follows the reporting deadline of 30 June, under *ESG 4.4.2R(1)(a)*.

...

...

6 Operating duties and responsibilities

...

6.9 Independence, names and UCITS business restrictions

...

Use of the term ‘long-term asset fund’ or ‘LTAF’

...

6.9.8D G ...

ESG naming restrictions

6.9.8E G Further requirements related to the naming and marketing of *authorised funds* are found in *ESG 3.3*.

...

8 Qualified investor schemes

...

8.3 Investor relations

...

Table: contents of qualified investor scheme prospectus

8.3.4 R This table belongs to *COLL 8.3.2R*.

| | |
|----------|---|
| 1 | Document status |
| ... | |
| 3 | Investment objectives and policy |

| | | | |
|------------|--|--|--|
| | (1) | Sufficient information to enable a <i>unitholder</i> to ascertain: | |
| | | (a) | ... |
| | | (aa) | <u>the sustainability objective of the authorised fund (if any);</u> |
| | | ... | |
| ... | | | |
| 18B | Information on authorised contractual schemes | | |
| | A statement that: | | |
| | ... | | |
| | (4) | the <i>scheme property</i> of a <i>co-ownership scheme</i> is beneficially owned by the <i>participants</i> as tenants in common (or, in Scotland, is the common property of the <i>participants</i>). | |
| 18C | <u>Sustainability information</u> | | |
| | The following information, as applicable: | | |
| | (1) | <u>where a sustainability label is used in relation to a scheme, the information set out at ESG 4.3.1R and ESG 4.3.2R, in the form prescribed at ESG 4.3.3R;</u> | |
| | (2) | <u>where a sustainability label is not used in relation to a scheme, but that scheme has sustainability characteristics as an integral part of its investment policy or strategy, the information set out at ESG 4.3.4R.</u> | |
| | ... | | |
| ... | | | |

Contents of the annual report

- 8.3.5A R (1) An annual report, other than for a *scheme* which is an *umbrella*, must contain:
- ...
- (d) the report of the auditor in accordance with *COLL* 4.5.12R (Report of the auditor); ~~and~~
- (e) subject to *COLL* 8.3.5AR(1)(d), its public TCFD product report or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the firm's website, in accordance with *ESG* 2.3.1R; and

- (d) where a *sustainability label* is used in relation to a *scheme*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 4.5.6R*.
- (2) An annual report on a *scheme* which is an *umbrella* must be prepared for the *umbrella* as a whole and must contain:
- (a) for each *sub-fund*:
- ...
- (iii) comparative information in accordance with *COLL 4.5.10R (1A) and (2A)*; ~~and~~
- (iv) subject to *COLL 8.3.5AR(2)(v)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*; and
- (v) where a *sustainability label* in relation to a *sub-fund*, its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 4.5.6R*;
- ...
- ...
- ...

Contents of the half-yearly report

- 8.3.5B R (1) A half-yearly report on an *authorised fund* or *sub-fund* must contain:
- ...
- (b) the report of the *authorised fund manager* in accordance with *COLL 8.3.5CR*; ~~and~~
- (c) subject to *COLL 8.3.5AR(1)(d)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to ~~where~~ the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*, where the half-yearly report most closely follows the reporting deadline of 30 June, under *ESG 2.1.1R(1)*; and
- (d) where a *sustainability label* is used, Part B of its *public product-level sustainability report* or an adequately

contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 4.5.6R*, where the half-yearly report most closely follows the reporting deadline of 30 June, under *ESG 4.4.2R(1)(a)*.

...

...

15 Long-term asset funds

...

15.4 Prospectus and other pre-sale notifications

...

Table: contents of a long-term asset fund prospectus

15.4.5 This table belongs to *COLL 15.4.2R*.

| | | | |
|-------------------|---|---|--|
| 1 | Document status | | |
| | ... | | |
| 3 | Investment objectives, policy and strategy | | |
| | The following particulars, which must be set out fairly, clearly and in plain language: | | |
| | (1) | Information to enable a <i>unitholder</i> to ascertain: | |
| | | (a) | ... |
| | | (aa) | <u>the sustainability objective of the authorised fund</u> (if any); |
| | | ... | |
| ... | | | |
| 28 | Information on authorised contractual schemes | | |
| | ... | | |
| | (4) | the <i>scheme property</i> of a <i>co-ownership scheme</i> is beneficially owned by the <i>participants</i> as tenants in common (or, in Scotland, is the common property of the <i>participants</i>). | |
| <u>28A</u> | <u>Sustainability information</u> | | |
| | <u>The following information, as appropriate:</u> | | |

| | | |
|-----|-----|---|
| | (1) | <u>where a <i>sustainability label</i> is used in relation to a <i>scheme</i>, the information set out at <i>ESG 4.3.1R</i> and <i>ESG 4.3.2R</i>, in the form prescribed at <i>ESG 4.3.3R</i>; and</u> |
| | (2) | <u>where a <i>sustainability label</i> is not used in relation to a <i>scheme</i>, but that <i>scheme</i> has <i>sustainability characteristics</i> as an integral part of its <i>investment policy</i> or <i>strategy</i>, the information set out at <i>ESG 4.3.4R</i>.</u> |
| ... | | |

15.5 Annual report and investor relations

...

Contents of the annual report

- 15.5.3 R (1) An annual report, other than for a *scheme* which is an *umbrella*, must contain:
- ...
- (e) the report of the auditor in accordance with *COLL 4.5.12R* (Report of the auditor); ~~and~~
 - (f) subject to *COLL 15.5.3R(1)(g)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to ~~where~~ the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*; and
 - (g) where a *sustainability label* is used in relation to a *scheme*, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and to the report's location on the *firm's* website, in accordance with *ESG 4.5.6R*.
- (2) An annual report on a *scheme* which is an *umbrella* must be prepared for the *umbrella* as a whole and must contain:
- (a) for each *sub-fund*:

...

 - (iii) comparative information in accordance with *COLL 4.5.10R(1A)* and (2A); ~~and~~
 - (iv) subject to *COLL 15.5.3R(2)(g)*, its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG 2.3.1R*; and
 - (v) where a *sustainability label* is used in relation to a *sub-fund*, Part B of its *public product-level sustainability report* or an

adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG* 4.5.6R;

...

...

...

Contents of the half-yearly report

15.5.5 R (1) A half-yearly report on an *authorised fund* or *sub-fund* must contain:

...

- (b) the report of the *authorised fund manager* in accordance with *COLL* 15.5.6R; ~~and~~
- (c) subject to *COLL* 15.5.5R(1)(d) its *public TCFD product report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG* 2.3.1R, where the half-yearly report most closely follows the reporting deadline of 30 June, under *ESG* 2.1.1R(1); and
- (d) where a *sustainability label* is used, Part B of its *public product-level sustainability report* or an adequately contextualised and prominent cross-reference and hyperlink to the report's location on the *firm's* website, in accordance with *ESG* 4.5.6R, where the half-yearly report most closely follows the reporting deadline of 30 June, under *ESG* 4.4.2R(1)(a).

...

...

Annex F

Amendments to the Investment Funds sourcebook (FUND)

In this Annex, underlining indicates new text and striking through indicates deleted text.

3 Requirements for alternative investment fund managers

...

3.2 Investor information

...

Prior disclosure of information to investors

3.2.2 R An *AIFM* must, for each UK *AIF* that it manages, and for each *AIF* it *markets* in the *UK*, make available to *AIF* investors before they invest, in line with the *instrument constituting the fund*, the following information and any material changes to it:

...

(16) (a) the identity of the *prime brokerage firm*;

...

(d) information about any transfer of liability to the *prime brokerage firm* that may exist; ~~and~~

(17) a description of how and when the information required under *FUND* 3.2.5R and *FUND* 3.2.6R will be disclosed; and

(18) (a) where a *sustainability label* is used in relation to an *AIF*, the information set out at *ESG* 4.3.1R and *ESG* 4.3.2R, in the form prescribed at *ESG* 4.3.3R;

(b) where a *sustainability label* is not used in relation to an *AIF* but that *AIF* has *sustainability characteristics* as an integral part of its *investment* policy or strategy, the information set out at *ESG* 4.3.4R.

...

Appendix 2

Non-Handbook Guidance: implementing guidance

1. As discussed in Chapters 4 and 5, we are proposing to introduce a set of criteria that firms must meet to qualify for a sustainable investment label. This aims to set a quality standard and support our outcome to build trust by raising the bar, and by taking an objective, rigorous approach.
2. We are proposing that all firms must meet five overarching principles and a set of cross-cutting criteria covering what the firm must do as well as category-specific criteria for each label, and make associated disclosures. We have also produced some additional guidance setting out further considerations to help firms implement the criteria.
3. The implementing guidance will be presented as non-Handbook guidance to the criteria and disclosures included in Chapters 4 and 5, and in the draft instrument in Appendix 1. The implementing guidance is nevertheless a key part of the overall qualifying criteria and we seek feedback on the full package in Chapter 4.

Implementing guidance to the general criteria

The following implementing criteria relate to the general criteria set out in ESG 3.2.3R.

Sustainability objective

1. In accordance with ESG 3.2.3R(1)(b) and ESG 4.3.1R(4), in specifying and disclosing details of the plausible, purposeful and credible link between the *sustainability product's sustainability objective* and an environmental and/or social outcome, a firm should clearly state:
 - a. the nature of the positive environmental and/or social outcome to which it expects the *sustainability product* to contribute, including any link to third-party sustainable development goals, such as the UN Sustainable Development Goals
 - b. whether the *sustainability product's sustainability objective*
 - i. directly targets a positive environmental and/or social outcome
 - ii. contributes indirectly to environmental and/or social outcomes by operating instead as a 'constraint' on i) the sustainability profile of assets, ii) the strategy and iii) the stewardship approach adopted by the *firm*
 - c. whether pursuit of the *sustainability objective* could result in any trade-offs or adverse environmental or social impacts, including a clear articulation of any financial trade-offs that may arise
2. The firm must also cite evidence of the plausibility and credibility of the mechanisms described under 3 below.

3. In accordance with ESG 3.2.3R(1)(a) and ESG 4.3.1R(2), in determining and disclosing its *sustainability objective* in specific and measurable terms, a firm should describe:
 - a. the mechanism(s) by which the *sustainability objective* is expected to be attained
 - b. the time horizon over which the *sustainability objective* is expected to be attained
 - c. potential barriers or risks to the attainment of the *sustainability objective*
4. In ensuring the firm has adequate processes in place in accordance with ESG 3.2.3R(1)(c), the firm should describe in its pre-contractual disclosures:
 - a. how it will monitor, measure and evaluate progress toward, or attainment of, the *sustainability product's sustainability objective* and set out how it will report to investors
 - b. how it will monitor, assess, manage or address and any negative social and environmental impacts that may arise in pursuit of the *sustainability objective*

Investment policy and strategy

5. In accordance with ESG 3.2.3R(2)(a) and ESG 4.3.1R(5), in describing its investment policy and strategy in the *sustainability product's pre-contractual disclosures*, a firm should provide sufficient information for the client to be able to distinguish between offerings that pursue their *sustainability objectives* in different ways – drawing out, for example, its use of screening strategies, thematic investing approaches and the role of investor stewardship
6. In accordance with ESG 3.2.3R(2)(b), a firm should put in place appropriately designed systems and controls for the *sustainability product*, including data inputs and monitoring tools, to ensure that
 - it invests in accordance with its investment policy and strategy on an ongoing basis
 - it is able to demonstrate ongoing adherence to its investment policy and strategy in its annual reporting to *clients*
7. In accordance with ESG 3.2.3R(2)(c) – (f) and ESG 4.3.1R(6) – (10) the following implementing guidance apply:
 - a. A firm should describe the data inputs it relies on to monitor that its holdings in the sustainable investment product align with the target environmental and/or social sustainability profile of assets
 - b. Where a firm relies exclusively or largely on ESG data services provided by a third-party (including ESG data that determine the asset composition of an index that it is either tracking or uses as a benchmark) to make judgements about ESG matters for the *sustainability product*, it should disclose this as part of the additional information required to be included in the *pre-contractual materials*
 - c. Where a firm applies either positive or negative screens as part of its asset selection for the *sustainability product*, it should describe, in the product's *pre-contractual materials*: (i) the factors the screen applies, and how these align with the *sustainability product's sustainability objective*; (ii) the percentage

of the portfolio to which it applies, and why it applies to less than 100% where applicable (excluding for cash management purposes)

- d. In disclosing the *sustainability characteristics* of assets in which it will invest, a firm should consider the expectations of a reasonable client; for example, if a *sustainability product's sustainability objective* targets investment in assets issued by companies that develop environmental solutions, a client might reasonably expect the product to avoid investments in assets issued by companies in sectors of the economy with high carbon emissions
- e. Where a firm may hold assets, potentially at a reduced weighting vis a vis a benchmark, that a reasonable client might not expect, given the *sustainability product's sustainability objective*, this should be made clear in the product's *pre-contractual materials*, including the circumstances in which such assets may be held and the purposes for which they would be held
- f. Where relevant to its investment policy and strategy, a firm should explain how its use of derivatives aligns or contributes to achieving the *sustainability product's sustainability objective*
- g. Where relevant to its investment policy and strategy, a firm should explain how short selling aligns with or contributes to the *sustainability product's sustainability objective*
- h. Where applicable, a firm should clarify its securities-lending policy and the steps it takes to ensure this is aligned with its sustainable strategy and the target environmental and/or social sustainability profile of assets for the *sustainability product*; for example, it may explain how it ensures that voting rights are exercised in line with the stewardship policy of the *sustainability product*, including as regards the recalling of shares for voting purposes

KPIs

8. In accordance with ESG 3.2.3R(3), there should be a clear link between a *sustainability product's* specified KPIs and its *sustainability objective*; for example, a *sustainability product* that is committed to investing in assets that meet a target profile for environmental sustainability – eg, with reference to *sustainability characteristics* such as carbon emissions profile, or 'green revenues' – should, among others, specify KPIs on these characteristics in its ongoing performance reporting (ie in its *public product-level sustainability report (Part B)* or as part of *on-demand sustainability information*, as applicable)
9. In accordance with ESG 4.5.7R(5), in disclosing performance against the specified KPIs on an ongoing basis, these should be decision-useful to *clients* in holding the *sustainability product* to account for performance against its *sustainability objective*
10. In accordance with ESG 4.5.7R(8)(b), in providing historical annual calculations of the KPIs after the first year of disclosures, a firm should:
 - a. evidence and evaluate performance of the *sustainability product*, with examples of actions taken in pursuit of the *sustainability objective*; for example, where stewardship forms an integral part of a *sustainability product's* strategy, it should articulate clearly how the execution of its stewardship strategy has supported the achievement of its *sustainability objective*
 - b. describe any factors that have materially impeded its ability to achieve the *sustainability product's sustainability objective*

11. Where relying on either proprietary or third-party data and analytical tools to support disclosures in accordance with ESG 4.5.7R(5), a firm should:
 - a. provide (subject to intellectual property considerations) interpretative information
 - b. describe relevant methodologies used
 - c. highlight any material data considerations/limitations

Resourcing and Governance

12. In accordance with ESG 3.2.3R(4), in applying and maintaining resources to deliver the *sustainability product* in line with its *sustainability objective* and its associated investment policy and strategy, a firm should
 - a. include in its *pre-contractual materials* details of the skills and expertise of its investment team, and other internal and third-party expertise engaged in the *sustainability product's* delivery
 - b. specify, as appropriate, the primary data and analytical tools that support delivery of the *sustainability product* and the degree of reliance on these tools, clarifying where these are sourced internally or from third-party providers
13. In accordance with ESG 3.2.3R(4)(b) in carrying out due diligence on data, research and analytical resources (including when third-party ESG data service providers are used), a firm should:
 - a. assure the quality and fitness for purpose of data, research and analytical inputs by conducting appropriate model validation and data governance
 - b. understand how data and research inputs are sourced and derived (including relevant methodologies) and consider carefully how any gaps and limitations in such inputs may hinder achievement of the product's stated objectives
14. In accordance with ESG 3.2.3R(4)(c), in overseeing sustainability research, data and analytical tools (including when third-party ESG data services are used), a firm should
 - a. monitor the ongoing quality and fitness for purpose of research, data and analytical tools used to support the delivery of the sustainable investment product
 - b. ensure that clear processes are in place to challenge internal and third-party providers of such resources and address on a timely basis any issues identified
15. In accordance with ESG 3.2.3R(4)(d), in maintaining governance and organisational arrangements that appropriately support and incentivise high-quality delivery of its investment policy and strategy in line with the *sustainability product's sustainability objective*; this should include ensuring that such arrangements support and incentivise:
 - a. the creation of an organisational culture and purpose aligned with the effective delivery of the *sustainability product*
 - b. the maintenance of adequate resources, including appropriate skills, experience, research, data and analytical tools, to deliver in accordance with *client's* expectations

- c. as appropriate, adherence to relevant industry codes and standards (eg. relevant codes and standards set by Principles for Responsible Investment, Chartered Financial Analyst, British Standards Institution etc), and active participation in multilateral groups and initiatives, where these may be pertinent to the *sustainability product's sustainability objective*
- d. careful oversight of any interactions between organisational arrangements and the delivery of the *sustainability product* to avoid any potential conflicts, and to manage any potential trade-offs that could hinder attainment of the *sustainability product's sustainability objective*

Stewardship

- 16. In accordance with ESG 3.2.3R(5)(b), in applying its active investor strategy and resources appropriate for achieving the *sustainability product's sustainability objective*, this should include stewardship across asset classes as well as an engagement strategy to promote good sustainability outcomes across the wider system (as set out in Principle 4 of the UK Stewardship Code 2020)
- 17. In accordance with ESG 4.3.1R(11), in setting out the nature of its commitment to the UK Stewardship Code 2020, a firm should clarify whether it is a signatory, or whether it has applied – or intends to apply – to become a signatory; if it has not applied to be a signatory or does not intend to do so, it should explain why and describe its alternative approach
- 18. Where stewardship plays a significant role in the firm's investment policy and strategy for the *sustainability product*, this should be reflected in the detail and specificity of its *pre-contractual materials*; as appropriate, a firm should describe
 - a. the proportion of assets (across asset classes) with which it aims to engage on matters related to environmental and/or social sustainability matters, aligned with its *sustainability objective*
 - b. the nature and intensity of such engagement, including the role it expects to play in collaborative engagement activities
 - c. how it aims to use its voting rights and other accountability mechanisms to influence outcomes
 - d. how it expects to escalate its stewardship activities, should the desired outcomes not be observed, including potential divestment
 - e. how it expects to engage with governments, policymakers, NGOs and cross-industry initiatives relevant to the *sustainability product's sustainability objective*
- 19. In accordance with ESG 3.2.3R(3), ESG 3.2.3R(5)(c) and ESG 4.5.7R(6), where stewardship plays a significant role in the *sustainability product's* investment policy and strategy, this should be reflected in the KPIs that the firm specifies, its ongoing monitoring of performance against these KPIs, and annual performance disclosures in its *public product-level sustainability report (Part B)*
- 20. In accordance with ESG 3.2.3R(3), ESG 3.2.3R(5)(c) and ESG 4.5.7R(6), where a firm's stewardship strategy for the *sustainability product* targets ongoing improvement in the environmental and/or social sustainability profile of assets over time, it should report performance against KPIs that track how the firm's stewardship strategy has been applied to support such improvements and the outcomes achieved; these may include, among others, relevant metrics for

- a. the number and types of engagements relevant to the *sustainability product's sustainability objective*
- b. the proportion of engagements (across asset classes) that led to a material positive change in the environmental or social sustainability of assets
- c. metrics on voting outcomes, as appropriate, relevant to the *sustainability product's sustainability objective* (including any material exceptions from the firm-level voting policy)
- d. collaborative engagement activities, including details of the role played and the outcomes achieved
- e. stewardship escalation activities (eg, divestment reviews, restrictions or exclusions on portfolio companies, refusal to rollover maturing debt instruments)
- f. the number and types of engagement activities with governments, policymakers and NGOs and details of participation in industry or policy initiatives relevant to the *sustainability product's sustainability objective*, including the role played and the outcomes achieved

Implementing guidance for the specific criteria

The implementing guidance for the sustainability label "Sustainable Focus" are as follows:

1. In accordance with ESG 3.2.6R(1), in ensuring that at least 70% of the *sustainability product's* assets meet a credible standard of environmental and/or social sustainability, a firm should:
 - describe the credible standard that it applies in the *sustainability product's pre-contractual materials* (this should be articulated in terms of positive sustainability attributes, rather than negative attributes, and be absolute as opposed to relative)
 - demonstrate that the standard selected in – whether a third-party or proprietary source – is credible, consistent, rigorous and evidence-based
 - explain why the standard selected is fit for purpose given the *sustainability objective* and the mechanism and transmission channels by which it expects either directly or indirectly to contribute to positive environmental and/or social outcomes
2. The firm should, as far as reasonably practicable, avoid investment in assets that a reasonable *client* would consider to be in conflict with the credible standard of environmental and/or social sustainability

The implementing guidance for the sustainability label "Sustainable Improvers" are as follows:

1. In accordance with ESG 3.2.7R(1), a firm should:
 - describe the standard/framework/logic that it applies as a reference for the target environmental and/or social sustainability profile of assets that it aims to achieve over time
 - demonstrate that the standard selected – whether a third-party or proprietary source – is credible, consistent, rigorous and evidence-based
 - explain why the standard selected is fit for purpose given the *sustainability objective* and the mechanism and transmission channels by which it expects

either directly or indirectly to achieve positive environmental and/or social outcomes over time

2. Where, as part of its asset-level selection criteria, a firm applies a positive screen (eg, a 'best in class' approach) to assess the relative environmental and/or social sustainability of assets and the extent to which improvements in sustainability may be achieved over time, it should:
 - describe the methodology that it applies to measure and assess relative environmental and/or social sustainability, including where it relies upon ESG data services provided by a third-party
 - describe the link to expected future improvements in sustainability
3. In specifying its asset-level selection criteria in respect of a *sustainability product*, a firm must describe in the *sustainability product's pre-contractual materials*:
 - how it determines whether individual assets' longer term environmental or social sustainability profiles align with the *sustainability product's sustainability objective*, and
 - how it assesses potentially investible assets to determine the extent to which improvements in sustainability can be achieved over time, including through active investor stewardship

The implementing guidance for the sustainability label "Sustainable Impact" are as follows:

1. In accordance with ESG 3.2.8R(1) and ESG 4.5.8R(3), a firm should describe, in both qualitative and quantitative terms, its progress towards achieving its target real-world environmental and/or social outcome
2. In applying enhanced impact measurement and reporting based on industry best practices in accordance with ESG 3.2.8R(3), a firm could include:
 - an articulation of the ambition and ex-ante assessment of expected results
 - an explanation of the investor contribution, (eg, through signalling, engagement, value additionality or by providing flexibility around financial returns or catering for undersupplied capital markets etc)
 - monitoring of progress throughout the lifecycle of the investment
 - where investment is realised or at predefined point in time, ex-post evaluation and assessment
 - independent verification of results

