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By email: dp-21-04@fca.org.uk

Dear Sir / Madam,

Financial Services Consumer Panel response to DP21/4 Sustainability Disclosure Requirements (SDR) and investment labels.

The Financial Services Consumer Panel (the Panel) is an independent statutory body. We represent the interests of individual and small business consumers in the development of policy and regulation of financial services in the UK.

We welcome the opportunity to respond to this consultation on sustainability disclosure requirements and investment labels. The Panel is very supportive of the initiative to introduce an effective regime underpinning sustainability disclosures for all products. We consider that it aligns well with our Vision for the retail investment market,¹ which is that firms should have a duty to act in the best interests of their customers and the aim should be to create a market where:

- products are better designed, labelled and described to enable consumers to better understand fully the opportunities, risks and costs involved and easily compare these across options;
- the information disclosed to potential investors is designed in a way that will allow them to make effective decisions, and to compare the risks and rewards not only of different options for a given product type, but also of different products;
- it is not possible to use regulatory arbitrage to circumvent rules designed to protect consumers;
- information, education, guidance and advice is readily available and tailored to the consumer to ensure they are supported in taking decisions both pre-investment and on an ongoing basis. This will require the re-engineering of current thinking to better integrate these aspects together and blend them throughout the customer's investment life-cycle. Only in this way will trust be established and consumers supported through what is an inherently complex set of decisions;
- more of the population with investible assets, and where the decision is right for them, make an active and informed choice to invest, so maximising their own returns and supporting the real economy; and
- when harm does occur, there must be easily accessible and efficient redress and compensation solutions.

In relation to the specific points raised in this consultation, the Panel considers that the key issues are that it would be helpful if:

- the design of disclosure documentation should be tested on consumers to determine what helps them make effective decisions, not just what do they like.

¹ See our [response to the FCA's call for input on consumer investments](#).

- the approach used is applied to all investment products, not just a subset. Where individual product options are not being promoted as sustainable, then this should also be clearly labelled;
- the resulting classification system was designed in a way to ensure that it will be applied consistently, to avoid different providers applying different labels to what are inherently the same product;
- the measurement system used to underpin the classification and labelling takes account of outcome measures, not simply activity measures;
- the “Responsible” classification should be dropped, as this is likely to confuse consumers when used in conjunction with “sustainable” classifications; and
- consideration was given to how to combine climate change reporting with reporting on other sustainability criteria such as pollution and social responsibility. As these goals may potentially be in conflict, and people may prefer to prioritise different aspects, the aim should be to develop an integrated set of disclosures that work as a group, rather than a single disclosure measure.

Our responses to the questions posed in the consultation are included at Annex 1 below.

Yours sincerely,

Wanda Goldwag

Chair, Financial Services Consumer Panel

Annex 1

Q1: What are your views on the tiered approach set out in Figure 2? We welcome views on any concerns and/or practical challenges.

The Panel recognises the challenges of creating an effective disclosure regime that will allow consumers to understand the sustainability characteristics associated with investment products. Providing too much information will potentially confuse consumers, or lead them to switch off. Providing too little information, however, will potentially make it impossible for consumers to compare options. This is particularly true as for many consumers the term sustainability will cover a range of different aspects including: climate change; pollution; and social sustainability considerations, such as human rights. These different aspects of sustainability will not always be fully aligned.

The Panel recognises that providing two layers of disclosure documentation (one aimed at consumers and one aimed at institutional investors and other stakeholders such as NGOs) may help. This would allow for high level information to be available for everyone, with more detail information available for those who want to investigate in more depth.

For a regime involving two layers of disclosure documentation to be effective, however, it will need to embody several characteristics:

- The two layers of information will need to be fully aligned, so that the summary information provided to everyone is an effective summary of the more detailed information. If, for example, a consumer label is used that the detailed information suggests is inaccurate, this will undermine trust.
- Secondly, the more detailed information should be available for consumers, so that those who are particularly engaged in sustainability issues can access it if they require.
- Finally, even though the main audience of the more detailed information will be institutional investors, the language and presentation of any information in this second layer should be accessible and prepared using plain English. This will facilitate everyone's understanding and will help ensure that where consumers would like to investigate further they are able to do so.

Q2: Which firms and products should be in scope of requirements for labels and disclosures? We particularly welcome views on whether labels would be more appropriate for certain types of product than for others, please provide examples.

The Panel considers that the scope of requirements for labels and disclosures should be as broad as possible. This will help ensure that different product groups do not end up producing slightly different disclosure requirements, which would make it impossible to compare options across investment types.

The Panel also considers that the labelling requirements should extend to all products, not just those that are aimed at investors wanting sustainable options. In other words, if, for example, the relevant label would be "not promoted as sustainable", then this should be clearly shown.

However, the Panel does not necessarily consider that labels would be needed for individual shares.

Q3: Which aspects of these initiatives, or any others, would be particularly useful to consider (for example in defining terms such as responsible, sustainable and impact) and how best should we engage with them?

The Panel does not have specific views about the relative merits of the different sustainability disclosure and classification initiatives produced by different bodies.

However, for the sake of consumers, the Panel considers that it would be helpful for a consistent approach, involving agreed definitions, to be used across all classification initiatives. This will help to avoid a situation where seemingly similar labels are applied in different ways by different organisations. Without consistency it will be harder for the use of labels to help drive change, and would potentially undermine faith in the system. In addition, the Panel considers that labels should be both easy to understand and align with the current customer usage, as it would be very unhelpful if any labels were to redefine terms already in common usage.

The Panel also considers that would be helpful to ensure that once an agreed naming convention has been decided upon, products will not be able to use those terms, unless they qualify. For example, funds should not be able to use the term "impact" (if that is an agreed label) unless they meet the relevant criteria.

The Panel also considers that the eventual agreed classification system should also encompass broader concepts of sustainability, not purely climate change.

Q4: Do you agree with the labelling and classification system set out in Figure 3, including the design principles we have considered and mapping to SFDR? We welcome views on further considerations and/or challenges.

The Panel is concerned about the inclusion of "Responsible" in the classification system outlined in Figure 3. As set out, "Responsible" involves a lower bar in terms of sustainability credentials than "Transitioning", but linguistically would imply more stringent sustainability credentials.

The Panel considers that the "Responsible" category is potentially superfluous, and that the classification system could be simplified to: not promoted as sustainable; transitioning; aligned; and impact. If the "Responsible" label is retained, then the Panel considers it should be included under the sustainable classifications, with agreed criteria associated with it for any product to qualify. In addition, consumer testing would be needed to determine where in the classification system it should sit, in terms of consumer understanding of the relative stringency of different labels.

Some thought could also be given to whether the labels used properly describe what each classification is designed to achieve. For example, changing "transitioning" to "facilitating transition", might give a clear view of what this products classified under this section are aiming to achieve.

Q5: What are your views on 'entry-level' criteria, set at the relevant entity level, before products can be considered 'Responsible' or 'Sustainable'? We welcome views on what the potential criteria could be and whether a higher entity-level standard should be applied for 'Sustainable' products. We also welcome feedback on potential challenges with this approach.

For the reasons set out above, the Panel is concerned about the inclusion of "Responsible" in the classification system.

The Panel considers that the use of "entry-level" criteria before a product can be considered "sustainable" would be helpful, to ensure that a consistent approach is applied.

The Panel also considers that there could be merit in applying an "Entity-level" standard for sustainable products. For example, this could help avoid situations where the goals of the fund and the fund manufacturer are not aligned.

Q6: What do you consider to be the appropriate balance between principles and prescription in defining the criteria for sustainable product classification? We welcome examples of quantifiable, measurable thresholds and criteria.

The Panel considers that it will be important that any potential classification system is applied consistently. This suggests that a degree of prescription may be necessary.

Q7: Do you agree with these high-level features of impact investing? If not, why not? Please explain, with reference to the following characteristics:

- **intentionality**
- **return expectations**
- **impact measurement**
- **additionality**
- **other characteristics that an impact product should have**

The Panel has no specific comment on the characteristics features identified for impact investing, beyond noting that there should be a consistent approach to how they are used. However, as there may be trade-offs between the features, there needs to be a credible means of measurement, reporting and comparison.

Q8: What are your views on our treatment of transitioning assets for:

a: the inclusion of a sub-category of 'Transitioning' funds under the 'Sustainable' label?

There appears to be a certain degree of confusion within this discussion paper as to what the purpose of the "transitioning" category would be. In paragraph 3.33 it is stated that "*Transitioning products would at the time of assessment have a low allocation to sustainable activities*". This suggests that the difference between the transitioning and aligned categories rests in the share of the allocation given to sustainable activities. However, in Box 3 the transitioning category is described as "*These products pursue strategies that aim to influence underlying assets towards meeting sustainability criteria over time, for instance through active and targeted investor stewardship. The expectation, therefore, is that this proportion will rise over time*". In other words, it is not simply about the share, but instead about the level of activity aimed at transforming the approach taken by the underlying assets, and it is this latter aspect that is most important.

The Panel therefore considers that it would be helpful if the definition of "transitioning" was clearer. From a sustainability perspective, the Panel considers that it would potentially be helpful if more emphasis was placed on the active influencing role in this category. However, in order for this to be properly aligned to sustainability goals, there should also be an aim to measure not just the influencing activity, but also the outcome, and for there to be a requirement that the investment approach will be adjusted where the influencing activities have had no impact.

For example, if the only criteria were the attempt to influence, a product provider could claim that the product they were offering was a "transitioning" sustainability option even if the underlying asset had very poor sustainability credentials, providing they were actively engaging to ask for change. However, if there was never any prospect of change, or even after a reasonable time period no change resulted, then the product provider will have failed to achieve any "transition". In those circumstances, to continue to call the product "transitioning" would be misleading, even if the active engagement to call for change was on-going.

In addition, the Panel considers that thought needs to be given to whether there should be a time limit on how long a product can be classified as transitioning, or if an investment could permanently remain under this classification.

b: possible minimum criteria, including minimum allocation thresholds, for 'Sustainable' funds in either sub-category?

No comment.

Q9: What are your views on potential criteria for 'Responsible' investment products?

For the reasons set out above, unless it is part of the formal classification system for sustainable funds, the Panel considers that the use of the "Responsible" category is likely to be confusing for consumers, and hence undesirable.

Q10: Do you agree that there are types of products for which sustainability factors, objectives and characteristics may not be relevant or considered? If not, why not? How would you describe or label such products?

The Panel agrees that there may be types of product that do not take sustainability considerations into account. In such cases the Panel considers that these should be clearly labelled. The Panel considers that the label "Not promoted as sustainable" is a helpful label.

Q11: How do you consider products tracking Climate Transition and Paris-aligned benchmarks should be classified?

No comment.

Q12: What do you consider the role of derivatives, shortselling and securities lending to be in sustainable investing? Please explain your views.

The Panel considers that there is no specific reason not to allow these types of activities, providing it can be shown that they are not designed to influence a point in time measurement of which sustainability classification a product belongs to.

Q13: What are your views on streamlining disclosure requirements under TCFD and SDR, and are there any jurisdictional or other limitations we should consider?

The Panel considers that streamlining disclosure requirements would be helpful, in order to promote consistency and reduce confusion.

Q14: What are your views on consumer-facing disclosures, including the content and any considerations on location, format (eg an 'ESG factsheet') and scope?

The Panel considers that it is very important that the design of any approach to disclosure is tested with consumers. The aim of this testing should be to determine whether the disclosure improves decision-making, not simply whether consumers "like" an option. The aim should be to produce an approach to disclosure that is jargon free and easily comprehended.

The Panel also considers that it would also be helpful to include broader aspects of sustainability (such as pollution, and social responsibility), not simply those related to climate change, as part of any new approach. How this can be best achieved should also be tested on consumers, in order to determine the impact on decision-making.

The Panel considers that it would also be helpful to give some thought about how the criteria underpinning classifications and labelling will evolve over time, and to incorporate

this into any consumer testing. For example, will the criteria associated with each classification be developed on a "once and done" basis, or is the FCA intending to gradually tighten criteria over time, as the market evolves? If the intended approach is the latter, then considering how consumers might react to changing rules might be helpful.

Q15: What are your views on product-level disclosures, including structure, content, alignment with SFDR and degree of prescription?

The Panel does not have specific views on how product-level disclosures should be structured. However, the Panel does consider that a consistent approach to disclosure would be helpful.

In addition, for the reasons set out above, for any regime involving two layers of disclosure documentation to be effective, the Panel considers that:

- The two layers of information need to be fully aligned, so that the summary information provided to everyone is an effective summary of the more detailed information. If, for example, a consumer label is used that the detailed information suggests is inaccurate, this will undermine trust.
- The more detailed information should also be available for consumers, so that those who are particularly engaged in sustainability issues can access it, if they require.
- Even though the main audience of the more detailed information will be institutional investors, the language and presentation of any information in this second layer should be accessible and prepared using plain English. This will facilitate everyone's understanding and will help ensure that where consumers would like to investigate further they are able to do so.

Q16: What are your views on building on TCFD entity-level disclosures, including any practical challenges you may face in broadening to sustainability-related disclosures?

The Panel is supportive of the introduction of entity-level disclosure, as this will allow consumers to understand not just whether the product itself is aligned to their goals, but also whether the provider itself is.

How this information is presented to consumers as part of any disclosure process should be informed by consumer testing, as part of a test of the whole disclosure regime, to determine which approach best facilitates effective decision-making.

Q17: How can we best ensure alignment with requirements in the EU and other jurisdictions, as well as with the forthcoming ISSB standard? Please explain any practical or other considerations.

The Panel has no specific recommendations on how to achieve alignment. However, the Panel does consider that alignment is helpful and supports the intention to do so.

Q18: What are your views on the roles of other market participants in communicating sustainability-related information along the investment chain?

The Panel would support the UK adopting the same approach as the EU, by confirming that advisers should consider sustainability matters in their investment advice and ensure their advice is suitable and reflects consumer sustainability-related needs and preferences. Similar consideration should be given to the role that guidance should take.

The Panel considers that the availability of appropriate advice and guidance is important for the functioning of the investment market.

Q19: Do you consider that there is a role for third-party verification of the proposed approach to disclosures, product classification and labelling and organisational arrangements of product providers? Do you consider that the role may be clearer for certain types of products than others?

The Panel considers that it is important that any classification system that is introduced should be robust, applied consistently and credible. The Panel does not have a preference on whether this function should be performed by third party providers, providing it can be shown that the chosen approach meets these criteria to ensure that consumers can be confident in any disclosure provided.

Q20: What approaches would you consider to be most effective in measuring the impact of our measures, including both regulatory and market-led approaches, and should disclosures be provided in a machinereadable format to better enable data collection and analysis?

The Panel would support the provision of disclosures in a machinereadable format to better enable data collection and analysis, and it will be easier to mandate this from the start as that will ensure any systems are properly aligned.