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The FCA's Sustainability Disclosure Regime: A Practical Implementation Guide

F: Disclosure and Fund Naming Rules

This is the sixth briefing in a series of alerts focused on the Sustainability Disclosure Requirements (SDR) regime. Two key aspects of the SDR include the disclosure rules (at both the product and entity level) and the fund naming rules. This briefing provides a detailed overview of these rules and focuses in particular on how the regime applies to retail managers.

1. Fund-level Disclosures

This briefing considers the fund-level disclosures required under the SDR (i.e. pre-contractual and ongoing product disclosures), which will typically be aimed at professional clients or those retail clients looking to understand their products in further detail. This alert covers fund and entity-level disclosures as well as aspects of the regime that are particularly relevant to retail managers.

The key points are as follows:

- UK funds which adopt an SDR label or include sustainability-related terms in the fund's name and marketing materials will be required to provide SDR-compliant product level disclosures (see below).

- Disclosures must be kept up to date and will likely need to be amended in circumstances where firms are changing (or removing) SDR labels.

- Pre-contractual disclosures:
  - these disclosures must be made in a fund prospectus, prior disclosure document or Part A of the fund's sustainability product report (where required to be published under the FCA's Task Force on Climate-Related Financial Disclosures (**TCFD**) disclosure requirements);
  - the FCA notes that the disclosures "must be clearly identifiable" and that this can be "achieved by including the information in a dedicated section"; however, any disclosures that are specific to the product's SDR label or sustainability objective (including statements noting that the product has no label) must be located in a prominent place in the pre-contractual materials;
  - the FCA has also noted that it does "not expect firms to make changes to the [pre-contractual] disclosures… other than when first using a label, or revising or ceasing to use a label, as relevant";
  - a full list of the information required in the pre-contractual disclosures is set out at Annex A to this briefing.

- Ongoing disclosures:
  - these disclosures must be made on an annual basis from the point at which a firm begins using an SDR label;
  - helpfully, the SDR permits firms to cross-reference other information sources (e.g. TCFD or SFDR reporting) in their ongoing product disclosures, provided that the information is relevant and clearly signposted;
  - these disclosures must either:
    - be made in Part B of the fund's sustainability product report (where required under the FCA's TCFD disclosure requirements); or
    - provided on demand to eligible clients, in circumstances where public disclosures are not appropriate (e.g. for unauthorised AIFs not listed on a recognised investment exchange). Note that:

- on-demand disclosures are only required from 2 December 2025 onwards;
- where ongoing disclosures are provided on demand:
  - the firm must respond to a single request for the information in each 12-month period "at a calculation date agreed with the client or at the most recent date the up-to-date information is available within the 12-month reporting period";
  - the firm must also respond to eligible clients' requests within a reasonable timeframe and in a format that "meets the information needs of the client";
- a full list of the information required in the ongoing product disclosures is set out at Annex B.

- Firms should bear in mind that products using the Sustainability Mixed Goals label must: (i) disclose the proportion of assets invested in accordance with each of the relevant labels; and (ii) more generally, meet all of the criteria and associated disclosures for each relevant label as required under ESG 4.2.19.
  - For example, a UK fund investing 40% of its assets in accordance with the sustainability improver label and 60% of its assets in accordance with the sustainability impact label will need to disclose those percentages and comply with the label-specific disclosure requirements under ESG 4.2.15 (in respect of its sustainability improver assets) and ESG 4.2.17 (in respect of its exposure to sustainability impact assets).
- Lastly, the FCA notes that "[w]here the strategy to pursue the sustainability objective is likely to have a material impact on the financial return, firms must disclose the extent to which the strategy may have affected, or be expected to affect, the financial return".
  - It is not clear at this stage whether the impact on return should be disclosed only in circumstances where the impact is negative, or whether disclosure should also cover positive impacts.

Timing considerations

Firms may use labels from 31 July 2024 onwards and will need to make the associated disclosures (i.e. pre-contractual and consumer-facing) and comply with the marketing rules from the date they first use a label. Managers that elect not to apply an SDR label to products during this initial period (i.e. from 31st July 2024) will need to ensure that they are not automatically drawn within scope of the SDR disclosure rules (for example by inserting sustainability-related references in marketing documentation).

2. Entity-level Disclosures

In addition to product-level disclosures, the SDR requires all UK managers with more than £5 billion in assets under management to make annual, entity-level disclosures as part of a "sustainability entity report". The FCA is also encouraging small firms to produce voluntary disclosures, and will consider whether to amend the £5 billion threshold going forward. The sustainability entity report is defined as "a public report regarding the overall assets managed by a manager in relation to its sustainability in-scope business" (i.e. the activities of managing a UK UCITS and/or a UK alternative investment fund).

The SDR's entity-level disclosure regime builds on the FCA's pre-existing regime, which already requires larger asset managers to make climate-related disclosures against the TCFD. In summary, UK managers that are required to make entity-level disclosures will need to disclose the following under ESG 5.6.1, which are broadly consistent with the TCFD and ISSB's four pillar approach:

1. the manager’s approach to governance, with respect to managing sustainability risks and opportunities;
2. the actual and potential impacts of any material sustainability-related risks and opportunities on the manager’s businesses, strategy and financial planning;
3. how the manager identifies, assesses and manages sustainability-related risks;
4. the metrics and targets used by the manager to assess and manage relevant material sustainability-related risks;
5. in addition to the above, the manager will also need to:
    a. explain 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;
    b. briefly explain in its sustainability entity report how the manager’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; and
6. lastly, where the manager is required to prepare a TCFD entity report, it must include the contents of that report or hyperlink it within its sustainability entity report.

In terms of scope, the requirement to produce entity-level disclosures will apply as follows:

- UK managers above the threshold that are not currently using SDR labels will need to make a baseline entity disclosure; and
- UK managers that use SDR labels or sustainability-related terms in their product names will be required to include additional details in their disclosures on their "resources, governance and organisational arrangements in relation to those products".

Note also that these disclosure rules apply to UK fund managers – they would not, for example, apply to MiFID investment firms in respect of their portfolio management business.

Helpfully, as with ongoing product-level disclosures, firms can cross-refer to disclosures made in other documentation such as group level reporting, provided the information is clearly signposted.

The FCA recommends that managers seeking guidance on disclosures consult the "TCFD's supplementary guidance for asset managers, IFRS sustainability disclosure standard (IFRS S1), the SASB Standards and GRI Standards".

It is not immediately clear that the new SDR entity-level reporting rules will significantly add to existing TCFD disclosure requirements; however, the new SDR requirements suggest a move away from a core focus on climate and towards a wider "sustainability" reporting regime.

3. Product Names and Marketing

Key features of the naming and marketing rules

A core component of the SDR regime is a set of new requirements on fund names. In practice, managers may only use sustainability-related terms in fund names where:

(i) the product uses a sustainability label; *or*

(ii) the product does not use a sustainability label, but the manager markets the product as sustainable and is therefore required to opt in to compliance with the SDR naming and marketing rules. A product will be marketed as sustainable where the manager uses sustainability-related terms in the product's name or in a financial promotion that details the sustainability characteristics of that product. "Short, factual, non-promotional statements" will not, however, rise to the level of marketing on the basis of sustainability.

UK managers should note that there is some debate around whether certain of the naming and marketing rules apply to all funds, or solely to funds made available to retail investors. For example, the FCA notes in its Policy Statement that certain of the naming and marketing rules apply to UK fund managers that make their products "available to retail investors", and the trigger for the application of certain rules (set out in ESG 4.3) references UK managers undertaking in-scope business "for retail clients". However, it is not immediately clear from either the FCA's Policy Statement or the rules in its ESG Sourcebook whether UK fund managers which: (i) do not have retail investors; and (ii) are marketing UK funds that are not open to retail investment, are intended to be drawn within scope of the SDR naming and marketing rules. It remains to be seen whether the FCA offers clarification on this point.

Marketing Disclosure Requirements

Managers of UK funds that use either a sustainability label or sustainability-related terms in either the product's name or in a financial promotion relating to the sustainability characteristics of that product are required to provide: (i) the same product-level disclosures as set out in section 1 of this alert; and (ii) the statement referenced below, for both types of fund.

Product naming requirements

The SDR imposes a number of requirements around the use of product names for funds which use sustainability-related terms in their names and marketing. The key requirements are as follows:

- no UK fund may include the word "sustainable", "sustainability" or "impact" (or any variation thereof) in its name if it does not use an SDR label;
- in addition, an SDR-labelled fund may not use the term "impact" in its name unless the fund in question uses the Sustainability Impact label;
- UK managers may use a specified list of sustainability-related terms (as set out in ESG 4.3.2) if they apply an SDR label to the fund;
- UK managers that do not adopt an SDR label may use the terms set out in ESG 4.3.2 provided that:

- the product's name reflects the product's sustainability characteristics, and those sustainability characteristics are material to the product. The FCA's guidance on the latter requirement notes that at least 70% of the product's assets must have sustainability characteristics;
- the manager complies with the general rule above that no fund may include the word "sustainable", "sustainability" or "impact" (or any variation thereof) in its name if it does not use a label;
- the manager produces a consumer-facing disclosure (where relevant), pre-contractual disclosure and ongoing product disclosures (ESG 4.3.5(2));
- the manager publishes the following information on a relevant digital medium in a prominent place where the sustainability product is offered (ESG 4.3.5(3)):
    - an explanation as to the purpose of a sustainability label, using either the standard text – 'Sustainable investment labels help investors find products that have a specific sustainability goal' – or alternative text which reflects the substance of the standard text;
    - a statement noting that the product does not use a sustainability label, using the text: "This product does not have a UK sustainable investment label"; and
    - a brief explanation as to why the product does not use a sustainability label.

4. Considerations Specific to Retail Managers

a. Consumer duty

When considering compliance with SDR disclosure requirements, retail managers will need to take into account the interaction between the SDR regime and the FCA's Consumer Duty requirements. The FCA's Policy Statement on the SDR noted a number of instances in which the two regimes overlap, and whilst not all firms to whom the SDR applies are required to apply the Consumer Duty, the FCA "expect[s] them to apply our rules and guidance keeping the aim of the [consumer] duty in mind".

In practice, this means that firms which are in scope of both the SDR and the Consumer Duty should:

> - act in good faith to deliver sustainability-related products and services, taking into account the reasonable expectations of retail investors;
> - avoid causing foreseeable harm, including through greenwashing or the sale of unsuitable products; and
> - consider how best to support retail customers in pursuing their investment objectives, including where sustainability-related needs and preferences form part of these objectives.

The fact that significant aspects of the SDR regime (such as labelling and the consumer-facing product disclosures) have been designed with consumers in mind underlines the FCA's continued focus on the Consumer Duty. UK retail managers should therefore focus on monitoring the effectiveness of their SDR implementation programme with respect to its ultimate impact on consumers, in order to demonstrate how they are meeting the principles and outcomes of the Consumer Duty.

b. Consumer-facing disclosures

Where in-scope funds are distributed to retail investors, UK managers will need to provide consumer-facing product-level disclosures. This consumer-facing disclosure must be produced for both labelled products and unlabelled products using sustainability-related terms (in either the product's name or in a financial promotion relating to the sustainability characteristics of that product). The key requirements for consumer-facing disclosures as follows:

- The disclosure must include:

> - either the product's sustainability objective and label, or a statement to clarify that the product does not have a label;
> - the investment policy and strategy (including what the product will and will not invest in);
> - relevant metrics;
> - details of where a consumer can access other relevant sustainability and non-sustainability information; and
> - for the 'Sustainability Mixed Goals' label only, the proportion of assets invested in accordance with each of the other relevant labels.

- The disclosure should be located in a prominent place on the digital medium through which the product is offered (e.g. website or mobile application). Hard copies must also be made available on request.
- Finally, the disclosure must be updated on an annual basis, and disclosures for labelled products must, at a minimum, track how the product is reaching the sustainability objective.
- As was the case with the PRIIPs rules, UK managers who are not specifically intending to target retail investors will need to take care to limit the circumstances in which their funds could end up in the hands of a retail investor in order to reduce the risk of being inadvertently drawn within scope of the consumer disclosure requirements.

What will the consumer-facing disclosure look like?

The rules require the consumer-facing disclosure to be no more than two pages in length and set out in a standalone document which is "presented in a prominent place on the product webpage, app or other digital medium, alongside other key investor information". The FCA has not mandated a template for the consumer-facing disclosure, perhaps with a view to avoiding the type of issues that arose with respect to PRIIPs-compliant Key Information Documents. However, the FCA notes that it encourages development of an industry-led template.

Automatic application of consumer-facing disclosures

As set out above, consumer-facing disclosures are only required for labelled products and products that use sustainability-related terms in their names and marketing materials. This scope of application is somewhat similar to the circumstances in which SFDR disclosure obligations will be triggered – for example, the European Commission's guidance on the scope of the SFDR made clear that marketing a product by reference to its ESG credentials will draw that product within scope of Article 8 or 9 and their associated disclosure requirements. However, one crucial difference is that the SDR consumer-facing disclosure requirements appear to be limited to retail funds being distributed to a sub-set of investors.

Annex A - Pre-contractual Product Disclosures

L	Label	The label used for the product
NL	Statement	Statement clarifying that the product does not have a label and why
L	Sustainability objective	The sustainability objective; where the investment strategy to pursue the objective may result in a material effect (including expected effect) on the financial risk and return; the link between the objective and positive environmental and/or social outcome; and where pursuing that objective may result in material negative environmental and/or social outcomes.
L NL	Investment policy and strategy	Details of the investment policy and strategy for the product, including how the manager determines the assets the product invests in (eg, the criteria it applies to determine sustainability characteristics)
L		The robust, evidence-based standard of sustainability, including the basis on which the standard is considered appropriate and the function or third party that carried out the independent assessment (without naming individuals)
L		The proportion of assets invested in accordance with the sustainability objective and the types of assets that are held for other reasons, and why.
L		How the index providers' methodology aligns with the product's sustainability objective (where relevant)
L	Sustainability metrics	Details of the policies and procedures, and the KPIs, that the firm will use to monitor and demonstrate performance towards the sustainability objective
NL		Details of any other metrics a consumer may find useful in understanding the investment policy and strategy for the product
L	Investor Stewardship	Details of the investor stewardship strategy and resources to support achievement of the sustainability objective, including how that strategy will be applied and, where relevant, whether the firm is a signatory to the UK Stewardship Code
L	Escalation plan	Any actions the firm will take in accordance with its escalation plan
L	Category-specific disclosures	Specific disclosures associated with the relevant labels: ▪ Sustainability Improvers (eg, expected timescales for improvement and the types of evidence relied on), ▪ Sustainability Impact (eg, the theory of change and method to measure and demonstrate impact) and ▪ Sustainability Mixed Goals (eg, the proportion of assets invested in accordance with each sustainable investment category and the specific disclosures associated with each category)

Annex B - Ongoing Product Disclosures

L NL	Basic information	Date of the report
L	Label	The label used for the product
NL	Statement	Statement clarifying that the product does not have a label and why
L	Sustainability objective	Details of the sustainability objective, progress towards achieving the objective, the proportion of assets invested in accordance with the sustainability objective and the types of assets held for other reasons (and why)
L NL	Investment policy and strategy	Details of how the product is invested in accordance with its investment policy and strategy on an ongoing basis
L	Sustainability metrics	Details of the product's performance against KPIs
L NL		Details of any other relevant metrics that a consumer might find useful in understanding the investment policy and strategy for the product
L NL		Contextual information and historical annual calculations for the KPIs and/or metrics (as relevant)
L NL	Material deviations	Details as to how the firm's approach to the product materially deviates from its entity-level approach (where relevant)
L	Investor stewardship	Details as to how investor stewardship has been applied, including activities undertaken and outcomes achieved (or expected to be achieved). These may include cross-references to Stewardship Code reporting, provided that information relevant to the product is clearly signposted.
L	Escalation plan	Details of matters escalated
L	Category-specific disclosures	Specific disclosures associated with the relevant labels: ▪ Sustainability Impact (eg, progress that the product is making towards achieving a positive impact)

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