WILLKIE FARR & GALLAGHER (UK) LLP

CLIENT ALERT

UK Sustainability Disclosure Requirements and Investment Labels Regime (SDR) and Anti-Greenwashing Rule

June 24, 2024

AUTHORS

Henrietta de Salis | Colin Fulton | Solomon Wifa | Rowan Khanna
Almahdi Coker

The UK Financial Conduct Authority's ("**FCA**") Sustainability Disclosure Requirements and Investment Labels Regime (collectively, the "**SDR**") is set out in the FCA's Policy Statement PS 23/16.[1] The package of measures introduced by the SDR includes an anti-greenwashing rule (the "**Anti-Greenwashing Rule**"), which came into effect for all UK-authorised firms on May 31, 2024.[2] The FCA published its Finalised Guidance on the Anti-Greenwashing Rule in April 2024.[3]

The SDR's investment labels are voluntary and only apply at this stage to UK asset managers in respect of UK funds such as UCITS, investment trusts and AIFs. The SDR's investment labels do not currently apply to non-UK firms or non-UK funds.

The FCA intends to expand the regime over time, for example, to portfolio management products, overseas funds, pension and other investment products.

1 Policy Statement PS 23/16 Sustainability Disclosure Requirements (SDR) and investment labels.

2 We discussed the October 2022 FCA Consultation on the SDR in a previous Client Alert.

3 FG24/3 Finalised non-handbook guidance on the Anti-Greenwashing Rule.

Comparison with EU Sustainable Finance Disclosures Regulation ("SFDR")[4]

The approach taken by the FCA is different from the EU's current approach under the SFDR in that it is focused on the naming and labelling of UK products marketed to retail investors rather than all investors, including professionals. Following recent consultations by the European Commission and market feedback, including from the European Supervisory Authorities[5], the EU may in time adapt the SFDR to adopt an approach based on product categories.

Key Obligations under the SDR

The Anti-Greenwashing Rule

The Anti-Greenwashing Rule builds upon the existing FCA Handbook requirements for firms. It requires firms to ensure that any claims they make about the sustainability characteristics of their products or services in communications are fair, clear and not misleading, and are consistent with the sustainability profile of the product or service.

Communications include, but are not limited to, statements, assertions, strategies, targets, policies, information, and images relating to a product or service. Where such communications may have been finalised pre-June 2024, if they are still being communicated to persons in the UK they will be within the scope of the Anti-Greenwashing Rule. The Anti-Greenwashing Rule applies to any communications by FCA-authorised firms to UK clients, both professional and retail, with respect to references to the sustainability characteristics (environmental and/or social characteristics) of a UK or non-UK product or service. This includes communications of financial promotions made to a person in the UK approved by authorised firms.

The FCA's Finalised Guidance on the Anti-Greenwashing Rule sets out, using examples, how sustainability references should:

- be correct and capable of being substantiated;
- be clear and presented in a way that can be understood;
- be complete – they should not omit or hide important information and should consider the full life cycle of the product or service; and
- ensure any comparisons to other products or services are fair and meaningful.

[4] Regulation (EU) 2019/2088.

[5] Joint ESAs Opinion: On the assessment of the SFDR.

Investment Labels

The SDR introduces four voluntary investment labels which UK asset managers may opt to use for qualifying products with sustainability objectives. The FCA hopes this will help consumers differentiate between distinct sustainability objectives and investment approaches to achieve those objectives.

The labels are: ‘Sustainability Focus’, ‘Sustainability Improvers’, ‘Sustainability Impact’ and ‘Sustainability Mixed Goals’. There is no hierarchy between the labels and they each have distinct key features as set out by the FCA:

Sustainability Focus	**Sustainability Improvers**	**Sustainability Impact**	**Sustainability Mixed Goals**
The sustainability objective must be consistent with the aim to invest in assets that **are environmentally and/or socially sustainable**, determined using a **robust, evidence-based standard** that is an absolute measure of sustainability.	The sustainability objective must be consistent with the aim to invest in assets that **have the potential to improve environmental and/or social sustainability over time** – determined by their potential to meet a **robust, evidence-based standard** that is an absolute measure of sustainability. Managers must identify the period of time by which the product and/or its assets are expected to meet the standard, including short- and medium-term targets. They must also obtain robust evidence to satisfy themselves that the assets have the potential to meet the standard.	The sustainability objective must be consistent with the aim to **achieve a pre-defined positive, measurable impact** in relation to an environmental and/or social outcome. Managers must specify a **theory of change** setting out how they expect their investment activities and the product’s assets to achieve a positive impact in accordance with a **robust, evidence-based standard** that is an absolute measure of sustainability. Managers must specify a robust method for measuring and demonstrating the positive impact of both the assets the product invests in and the managers’ investment activities.	Managers may only use this label where the sustainability product’s sustainability objective is to invest in accordance with **two or more of the other categories**. Managers must identify the **proportion of assets** which are invested in accordance with the two or more other categories. Managers must meet the specific requirements of the ‘Sustainability Improvers’ and ‘Sustainability Impact’ labels, as applicable (including the **robust, evidence-based standard** that is an absolute measure of sustainability).

UK managers opting to use an investment label in respect of a product must make associated disclosures and must meet the following five overarching principles: (i) the product must have a sustainability objective to improve or pursue positive environmental and/or social outcomes, (ii) at least 70% of the product's assets must be invested in accordance with its sustainability objective, (iii) the manager must identify key performance indicators to measure progress against the sustainability objective, (iv) the manager must ensure there are appropriate resources, governance and organisational arrangements to support delivery of the sustainability objective and (v) the manager must identify and disclose the stewardship strategy needed to support the delivery of the sustainability objective, including activities they expect to take and outcomes they expect to achieve.

UK managers must publish the label on their websites, if used, and must notify the FCA if they intend to use a sustainability label (or to revise or cease the use of that label). The FCA will not approve the use of a label, but may need to approve changes to pre-contractual disclosures as a result of a manager's decision to use a label.

The investment labels will be available for use from July 31, 2024, and consumer-facing and pre-contractual disclosures (see below) must be published at the same time the label is first used. The relevant naming and marketing rules must also be met from that date.

Naming and Marketing Rules

The new SDR naming and marketing rules apply to UK managers in respect of UK products for retail clients, unlike the Anti-Greenwashing Rule, which, as set out above, also applies to materials provided to professionals. Under the naming and marketing rules, "sustainability-related terms" can be used in product names and marketing materials only if such products:

- use a label, provided that, where the 'Sustainability Focus', 'Sustainability Improvers' or 'Sustainability Mixed Goals' labels are used, the word 'impact' is not used in the product's name; or
- do not use a label but comply with certain requirements in relation to naming and marketing materials, including not using the terms 'sustainable', 'sustainability' or 'impact' in their name to refer to the sustainability characteristics of the product, producing the same types of disclosures as required for a labelled product and providing a brief explanation as to why the product does not use a sustainability label.

The FCA has set out a non-exhaustive list of sustainability-related terms, which includes, for example, "ESG", "environment", "social", "climate", "sustainable" and "green", to which these rules apply.

These naming and marketing rules will come into force for UK managers using sustainability-related terms in their naming and/or marketing materials without product labels from December 2, 2024. For managers using labels, as set out above, these rules will apply from the date the label is first used.

Disclosures

The FCA is taking a tiered approach to the SDR disclosure regime, aiming to help provide accessible information to institutional investors and retail investors who may want more information in relation to labelled products or products using sustainability-related terms in their naming and/or marketing materials without a label. The regime consists of the following disclosures:

- consumer-facing disclosures for retail clients: summarising prescribed information and sustainability metrics;
- detailed product-level disclosures aimed at institutional investors, contained in:
  - **pre-contractual materials**, such as the prospectus; and
  - **a sustainability product report**; and
- entity-level disclosures in a **sustainability entity report**, which builds on the Task Force on Climate-related Financial Disclosures entity report.

UK managers must ensure consumer-facing disclosures are up-to-date in respect of the product's progress in achieving its sustainability objective and must ensure the consumer-facing disclosures, pre-contractual disclosures and sustainability product report remain accurate and consistent with any sustainability labels or sustainability-related terms used. Unlike the SFDR, there is no prescribed format for such disclosures or reports.

UK managers must make the above consumer-facing and pre-contractual disclosures from the date the label is first used or by December 2, 2024 for products using the sustainability-related terms without a label. The ongoing sustainability product report must be disclosed within 12 months following either the date the label or the sustainability-related terms are first used and annually thereafter. Managers must also, from December 2, 2025, provide within a reasonable period of time on-demand sustainability information, which includes certain information contained in the disclosures listed above, to an investor who requests it in order to satisfy sustainability-related disclosure obligations.

UK managers of UK funds with £5 billion or more of assets under management must publish a sustainability entity report annually, whether or not the manager uses an investment label or sustainability-related terms in relation to the funds it manages. Managers with less than £5 billion of assets under management may report on a voluntary basis. The first sustainability entity reports must be published by December 2, 2025 for the largest firms (asset managers with at least £50 billion in assets under management) and December 2, 2026 for smaller firms (with at least £5 billion in assets under management, calculated as a three-year rolling average on annual assessment).

Managers may change the reporting dates for subsequent reports following the first sustainability product and sustainability entity reports, but must ensure that there are no periods of time which are not covered and must issue an interim report if necessary.

Requirements for Distributors

Distributors must communicate the labels adopted by UK managers in respect of funds they distribute and provide access to consumer-facing disclosures to UK retail investors, either on a relevant digital medium for the product or using the channel they would ordinarily use to communicate information. Distributors must also include the following notice to UK retail investors for overseas products that use sustainability-related terms in their name or marketing materials to clarify that they are not subject to the SDR: 'This product is based overseas and is not subject to UK sustainable investment labelling and disclosure requirements'. Obligations on distributors apply from July 31, 2024 where managers are using investment labels and from December 2, 2024 for notices for overseas funds.

Next Steps

FCA-authorised firms should ensure they have established processes to comply with the Anti-Greenwashing Rule when making claims about the sustainability-related characteristics of their products and services, so that their sustainability claims are fair, clear and not misleading, and capable of being substantiated.

UK asset managers should familiarise themselves with the upcoming provisions of the SDR, including the requirements for using an investment label, the naming and marketing rules and the detailed disclosure requirements.

***

If you have any questions regarding this client alert, please contact the following attorneys or the Willkie attorney with whom you regularly work.

Henrietta de Salis
+44 203 580 4710
hdesalis@willkie.com

Colin Fulton
+44 203 580 4708
cfulton@willkie.com

Solomon Wifa
+44 203 580 4713
swifa@willkie.com

Rowan Khanna
+44 203 580 4987
rkhanna@willkie.com

Almahdi Coker
+44 203 580 4957
acoker@willkie.com