CONSULTATION RESPONSE

FCA SUSTAINABILITY DISCLOSURE REQUIREMENTS AND INVESTMENT LABLES

January 2022

ABOUT THE PRI

The Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI has over 4,500 signatories (pension funds, insurers, investment managers and service providers) to the PRI's six principles with approximately US $121 trillion in assets under management.

The PRI supports its international network of signatories in implementing the Principles. As long-term investors acting in the best interests of their beneficiaries and clients, our signatories work to understand the contribution that environmental, social and governance (ESG) factors make to investment performance, the role that investment plays in broader financial markets and the impact that those investments have on the environment and society as a whole.

The PRI works to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

ABOUT THIS CONSULTATION

This discussion paper for consultation seeks initial views on new sustainability disclosure requirements (SDR) for asset managers and FCA-regulated asset owners, as well as a new classification and labelling system for sustainable investment products. The FCA aims to consult in Q2 2022 on proposed rules to implement SDR disclosure requirements for asset managers and certain FCA-regulated asset owners and sustainable investment labels. This Discussion Paper (DP) aims to inform the FCA's work to develop these proposals, with a specific focus on: sustainable investment labels, consumer-facing disclosures for investment products, and client and consumer-facing entity and product-level disclosures by asset managers and FCA-regulated asset owners.

For more information, contact:

Olivia Mooney

Head of UK Policy

olivia.mooney@unpri.org

Freya Bannochie

UK Policy Analyst

freya.bannochie@unpri.org

PRI'S RESPONSE

The PRI welcomes this discussion paper from the FCA which forms an integral part of the UK government's Green Finance Roadmap as well as the FCA's intention to consult in Q2 2022 on proposed rules to implement SDR disclosure requirements for asset managers and certain FCA-regulated asset owners and sustainable investment labels within the FCA Handbook. The PRI is pleased to have the opportunity to input further technical advice via the development of the FCA's disclosures and Labels Advisory Group. Our overarching response and recommendations are formed on the basis of our work and insights as an organisation working with approximately 4,500 signatories globally, including 40 UK pensions fund signatories.

The PRI support the FCA's proposed approach on:

- **the design principles** – namely that labelling should have objective criteria and descriptive labels; with clear investment objectives, supported by further information on the activities used to deliver to the objectives
- **coherence and interoperability** and the FCA's recognition of the need to build on and align with existing international standards initiatives as far as possible
- **product labels and disclosure layers** – that there should be a standardised product and labelling system that is underpinned by more detailed product disclosures that are consumer facing, and further granular information beyond that aimed at institutional investors, noting that there will be challenges in translating complex jargon into consumer facing language
- **classification and labelling for a full range of investment products** and not only for products that make sustainability claims

The PRI recommend that FCA revise the potential categories of the classification and labelling system, and reconsider how best to draw on the EU Sustainable Finance Disclosure Regulation (SFDR).

On the potential categories, the FCA should clarify:

- that all funds, including those 'not promoted as sustainable', take ESG factors into consideration as part of their basic fiduciary duties and financial risk management. This is currently set out as criteria currently for 'Responsible' products.
- how it is proposed the distinction will be made between 'low' and 'high' taxonomy allocation in the proposed 'transitioning' and 'aligned' categories respectively, and that in addition to investment allocation, investor stewardship is also integral to transition.
- a goal which reflects the UK's commitment to net zero by 2050, against which products in the 'transitioning' and 'aligned' categories are being measured.
- how the product categories will apply across sustainability issues (i.e. not just climate change).

Regarding alignment with SFDR, the PRI supports taking the SFDR into account on possible disclosure requirements which will support interoperability (as above). However, the DP draws a comparison between SFDR and product classification. Whilst the SFDR has started to become (mis)used as de facto product labels by the market, the SFDR is a disclosure regime, and was not designed as means to label or classify funds.

The FCA's design of this regime should seek to avoid confusion between how funds are labelled, and their distinct but complementary disclosure requirements. In addition, the indicative mapping of categories against SFDR may risk confusion as to both the disclosure required by various articles in the SFDR and the intention for the classifications proposed in Figure 3. For example, in the DP:

- A proposed category of products "not promoted as sustainable" are stated as having no minimum criteria and where 'sustainability risks have not been integrated into investment decisions.' This is likened to Article 6 of the SFDR. However, Article 6 of the SFDR set out requirements on the 'transparency of the integration of sustainability risks' which can (and will) equally apply to all funds that integrate ESG risks whether promoted as sustainable or not. In addition, all funds - including those 'not promoted as sustainable' – will need to take ESG factors into consideration as part of their basic fiduciary duties and risk management.
- A proposed category of products "responsible" are stated as having no sustainability goal and are characterised by considering material sustainability factors and 'demonstrable stewardship'. This is linked to Article 8 of the SFDR. However, disclosure requirements under Article 8 are for products that 'promotes, among other characteristics, environmental or social characteristics' and makes no reference to stewardship.

The FCA should clarify the extent to which funds will align to the disclosure requirements of sustainable funds as set out in the SFDR[1].

The PRI has experience of public policy on sustainable finance policies and responsible investment across multiple markets and stands ready to further support the work of FCA in the development of disclosures and labelling regime. Question or comments related to this response can also be sent to policy@unpri.org.

[1] Sustainable investment (as defined in Article 2(17)): an investment in an economic activity that contributes to an environmental or social objective, provided that the investment does not significantly harm any environmental or social objective, and that the investee companies follow good governance practices.