

Fund Communication of Responsible Investment

Part 1: Incoming regulatory change and indication of next steps and timeline on best practice guidance

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Introduction

Fund Communication and Responsible Investment in the UK

Clearly, interest in sustainabilityⁱ and responsible investmentⁱⁱ is growing – from policy makers,ⁱⁱⁱ regulators^{iv} and clients.^v The number of sustainability-related funds and products^{vi} is also increasing, with a steady stream of new products being brought to market over the last two years.^{vii} The growth of responsible investment is an important development and one which the IA and its members are embracing.^{viii}

This increased focus on sustainable and responsible investment products comes at the same time as an increased focus on the clear communication of all products to retail investors more broadly. In February 2019, the FCA issued non-Handbook Guidance in [Policy Statement PS19/4](#) on the description of fund objectives (including non-financial objectives) and investment policies. A number of key messages come through the regulation that can help direct industry’s efforts to improve the communication of their products, including setting clear objectives so that customers know what to expect from their fund and key information disclosure aiding comparison between funds. These key messages, as set out in the [IA’s Fund Communication Guidance](#) published in February 2019, can also be applied to communicating the sustainable and responsible characteristics of funds.

At the IA, a dedicated working group on Responsible Investment Fund Language (“RI Fund Language Work Stream”) is tasked with taking forward best practice guidance on the communication of responsible investment characteristics at fund level. This best practice guidance will constitute Part 2 of the Fund Communication of Responsible Investment, and builds on the aforementioned Fund Communication Guidance as well as on the IA’s [Responsible Investment Framework](#).

When the IA began its dedicated policy work in sustainability at the start of 2018, there was no industry-agreed framework to articulate the broad range of approaches that are undertaken in responsible investment. A key priority of this work has, therefore, been to bring greater clarity and consistency to the use of language to describe different forms of responsible investment. As a result, in November 2019, the IA published its Responsible Investment Framework. This Framework categorises and defines different ways in which investment managers carry out responsible investment. Specifically, it splits responsible investment across “firm-level” and “fund-level” components. The Framework is used to explain to all

audiences (including policy makers, regulators and clients) how investment managers carry out responsible investment. It is also being used to gather and publish industry statistics. Moreover, it is available for IA members to use as they see fit, including mapping their product lines against and communicating with clients. More recently, it has also been adopted by other bodies to help bring consistency to the use of language across financial services. Notably, in January 2020, Hargreaves Lansdown [announced](#) it would be using the IA Framework in its communications with investors.

EU Sustainable Finance Regulation

In parallel to the development of funds' disclosure requirements more broadly is the implementation of a specific set of incoming rules from the EU, in particular, those relating to the disclosure of "sustainable investments" defined according to the [Regulation on sustainability-related disclosures in the financial services sector](#), also known as the Sustainable Finance Disclosure Regulation (SFDR). Under Article 2 (17) of SFDR, "sustainable investments" are defined as follows:

'sustainable investment' means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular, an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance;

There are also incoming requirements from the EU for products that have sustainable investments as their objective to disclose the extent to which they contribute to the six environmental objectives as set out in the [Regulation on the establishment of a framework to facilitate sustainable investment](#), also known as the Taxonomy Regulation. According to Article 9 of the Taxonomy Regulation, these objectives are as follows:

- a. climate change mitigation;
- b. climate change adaptation;
- c. the sustainable use and protection of water and marine resources;
- d. the transition to a circular economy;
- e. pollution prevention and control;
- f. the protection and restoration of biodiversity and ecosystems.

As you will see from the timeline graphic on page 6, there are additional disclosure obligations for funds being sold into the French market

stemming from the “AMF Doctrine”.

UK Adoption of EU Rules

In July 2019, the UK [set out its commitment](#) to match the EU in its level of ambition regarding sustainable finance. However, the UK will not automatically adopt EU regulation if the implementation date of that regulation is after the end of the transition period (31 December 2020). The UK will need to decide which pieces of regulation it wishes to remain consistent with – in part or in full. Irrespective of whether the UK remains consistent with the EU regulatory regime with respect to sustainable finance, some firms may still adopt the EU requirements. This may be to ensure their UK business remains consistent across clients in the UK and Europe or indeed because they are directly caught by the rules if they have operations in the EU. As such, the IA continues to support firms with the implementation of incoming EU sustainable finance requirements. We expect EU regulatory requirements on sustainable finance disclosure to impact future UK regulations to some degree whatever the outcomes of HM Government’s decisions.

On question of timing in the UK, we understand that, if and when the Government decides to introduce legislation in relation to SFDR, there will be a role for the FCA in implementing associated rules in its Handbook. This would in turn require full public consultation and Cost Benefit Analysis in accordance with FSMA and established practice. Given the FCA’s consultation timeframes, it would be highly unlikely this would be in place by March 2021. We have therefore been advised that industry will be given sufficient time to prepare to meet the necessary obligations.

Purpose of this Paper

This document – Part 1 of “Fund Communication of Responsible Investment” – is intended to provide an overview and summary of major incoming regulatory change in sustainable finance, in particular, from the EU. With a particular focus on SFDR and the Taxonomy, it is intended to help firms ascertain the extent to which their products are captured, what is expected of them, and by when.

Indication of Next Steps and Timeline on Best Practice Guidance

As you may know, on 23 April 2020, the European Supervisory Authorities (ESAs) published their [consultation](#) on ESG Disclosures. This provided remarkably detailed proposals including for pre-contractual disclosures regarding sustainability. Specifically, this consultation proposes further details for the implementation of SFDR, typically referred to as “Level 2 detail”. These changes are so extensive, that a large part of the focus of the RI Fund Language Work Stream was re-directed to unpacking these incoming regulatory changes – to better understand the nature of the changes themselves as well how these rules would impact the IA’s own proactive work, including the extent to which the rules are likely to be

adopted in the UK.

For months, it had not been clear how the proposed sustainability disclosures would fit into pre-contractual disclosures. It was thought they might be integrated into existing disclosures, i.e. used to update fund objectives and policies (in keeping with the PS 19/4 work and the approach taken by the AMF Doctrine). However, we have now seen [templates](#) from the ESAs which confirm this additional information is intended to sit separately in its own sustainability section.

Most recently, it has also been made clear that the Commission intends to delay the application of the level 2 requirements to some point after March 2021.

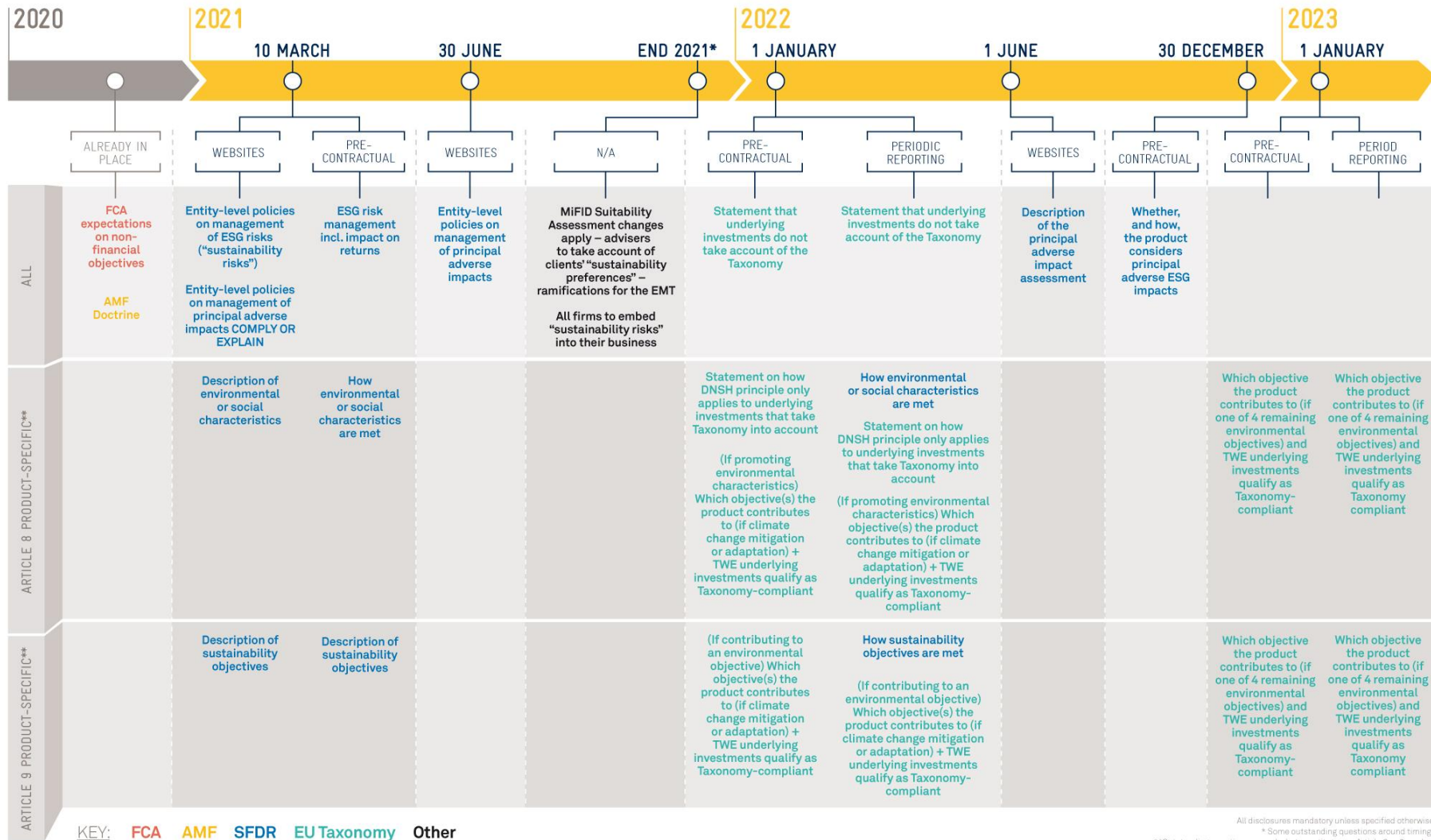
Clarity on how the incoming SFDR rules will or will not directly impact funds' objectives and policies is crucial for the scope of the IA's own best practice guidance. Having now received these templates, the IA is significantly better sighted on how best to take forward its own best practice guidance and provide the practical support for firms as they seek to improve the clarity and consistency of their sustainability disclosures through fund documentation.

It is also worth keeping in mind that we will be coordinating closely with FCA as their work develops on consumer access to sustainable products. They are aware of our work plans and timeline and we want to work closely to ensure we are moving in the same direction.

Summary of Next Steps for IA Work

Timeline	Output
Immediate	Publication of this document providing summary of regulatory requirements, what they are and how they fit together on a timeline
October/November	IA developing Implementation Q&A on practical issues around SFDR implementation
Q4 2020 / Q1 2021	Following clarity on the nature of the EU fund templates, IA to resume development of best practice guidance, coordinating closely with FCA.

Timeline for Incoming Regulatory Requirements



Overview of EU Incoming Rules on Sustainable Finance

Note that the detail included below is indicative and based on the detail that was proposed by the ESAs in their consultation on ESG Disclosures from 23 April 2020. The details themselves are subject to change pending the ESA's final report (expected January 2021) and the European Commission's final decision (expected mid-2021).

Most recently, we also understand that the European Commission will be delaying the implementation of the detail of the requirements (referred to as "level 2 requirements") to a date after March 2021 (possibly January 2022). Timeline for the high-level requirements (referred to as "Level 1") will stay as it is. We will keep members informed of any further development.

Which kinds of products are caught under SFDR and from when do the first obligations apply?

Obligations for all funds

From March 2021, firms will have additional sustainability-related disclosure requirements that apply to all funds. Specifically, firms will have to disclose the manner in which sustainability risks are integrated into their investment decisions as well as an assessment of the likely impacts of sustainability risks on the returns of funds. Where financial market participants deem such risks not to be relevant to investment decisions or returns, firms must explain why (Article 6, SFDR). This should appear in pre-contractual disclosures.

Obligations for sustainable products

Also, from March 2021, firms will have additional sustainability-related disclosure requirements to apply to their responsible and sustainable fund ranges. Specifically, these requirements are split across what are being referred to as "Article 8 products" and "Article 9 products".

An Article 9 product is defined as a financial product that "has sustainable investment as its objective". As mentioned above, "sustainable investment" is defined as follows under Article 2 (17) of SFDR.

'sustainable investment' means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular, an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially

disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance;

An Article 8 product is a financial product which “promotes, among other characteristics, environment or social characteristics of a combination of those characteristics, provided that the companies in which the investment are made follow good governance practices” (SFDR, Article 8(1)).

How do I go about categorising my products in practice?

Product categorisation according to Article 8 and 9 remains unclear and firms are working hard to interpret the rules based on available information to date. The industry is grateful to the ESAs for their efforts to bring clarity to the meaning of Article 8 products through the inclusion of Recitals 18-21. Below are additional suggestions from industry intended to bring greater clarity to these differences.

We can use the components of the IA [Responsible Investment Framework](#) to help bring additional clarity to the distinctions between Article 8 and 9 products. Below are the recommendations that the IA shared with the ESAs to further clarify the distinctions between Article 8 and 9 products in response to Question 16 of the ESAs consultation on ESG Disclosures.

Article 8 products	Article 9 products
Products that have any form of sustainability focus, including: <ul style="list-style-type: none"> - Sustainability-themed - Best in class - Positive tilt 	Environmental impact products, i.e. those that pursue an environmental objective and measure progress against this, alongside generation of a financial return
Products that apply exclusions that are specific to that fund could be brought into scope of Article 8 if these exclusions form a key feature of that fund.	Social impact products, i.e. those that pursue a social objective and measure progress against this, alongside generation of a financial return
Application of firm-wide exclusions policies should <i>not</i> result in all of a firm’s funds being caught by Article 8 requirements. Firm-wide exclusions are not used to help investors choose that particular fund.	
We agree that funds’ references to how they take account of sustainability risks under Article 6 of SFDR should <i>not</i> inadvertently bring them into scope of Article 8	

requirements.	
We support the ESAs clarification that only selection criteria for underlying assets that apply on a binding basis should bring funds into scope of Article 8 (or potentially 9).	

Additional Comments

Article 8 Products and “sustainable investments”

The IA has concerns around requiring Article 8 products to disclose the proportion of sustainable investments. Adopting such an approach increases the risk of conflating investment objectives for Article 8 products with those for Article 9 products as well as confusing investors who may not be seeking sustainable investments as per Article 9 products. The IA has asked that the ESAs consider this disclosure not being a requirement for Article 8 products. Instead, it should be dependent on whether this information is relevant to the investment strategy of the particular Article 8 fund.

By extension, the IA has also asked the ESAs to consider removing the warning proposed in Article 16 (1) of the draft RTS as, again, it is potentially misleading for investors who are not seeking Article 9 approaches.

Article 9 Products and Climate Benchmarks

The IA has voiced concerns over the proposed mandatory use of EU Climate benchmarks by Article 9 products that have as their objective to reduce carbon emissions. It is too prescriptive and takes away any possibility of innovation. Furthermore, it results in benchmark administrators using backward-looking data to determine how to achieve carbon emissions. By contrast, investment managers assess this on a forward-looking basis. This makes investment in transition companies impossible.

Overarching Comment

As an overarching comment, given SFDR is intended to avoid greenwashing, the predominant consideration in deciding whether a product falls under Article 8 requirements (or possibly Article 9 requirements) should be the extent to which their fund is described as having environmental or social characteristics in its documentation. The IA has urged the ESAs to consider this in their final recommendations.

What are the requirements for Article 8 products?

Given the likely delayed implementation of level 2 requirements, the detailed requirements outlined under this question are not expected to

apply from March 2021. More likely, detailed requirements – yet to be finalized by the European Commission – will be informed by ESAs’ draft proposals – from which the below is taken. This level of detail is likely to apply from January 2022.

According to Article 14 of the draft RTS proposed by the ESAs, for Article 8 products, firms would be expected to disclose the following:

- (a) Information on the ‘environmental or social characteristics promoted by the financial product’, which includes a description of this and a narrative and graphical representation of the different kinds of investments in the financial product, i.e. the extent to which that product has “sustainable investments”, investments that correspond to the product having environmental or social characteristics and any other investments.
- (b) The following statement: ‘This product does not have as its objective sustainable investment;
- (c) Description of ‘Investment strategy’ – including having to set out binding elements of the strategy
- (d) ‘Sustainability indicators’; - sustainability indicators used to attain the environmental or social characteristics promoted by the product
- (e) Its ‘Use of derivatives’;
- (f) ‘Website reference’ for further information and
- (g) if an index has been designated for the financial product as a reference benchmark, ‘Reference benchmark’.

Please refer to Articles 14-21 of [the proposed RTS](#) for full details.

What are the requirements for Article 9 products?

As above, the details outlined below are also unlikely to apply until January 2022 and subject to change based on the ESAs final proposals (expected Jan 2021) and the European Commission’s final decision (expected mid-2021).

For Article 9 products, firms would need to disclose the following:

- (a) ‘Sustainable investment objective of the financial product’ – Instead of a description of the characteristics as per Article 8 funds, firms have to disclose a description of the sustainable investment objective. The narrative and graphical representation of investments need to reflect the proportion of sustainable investment (as per Article 8) but in addition Article 9 products should provide subdivision of whether environmental or social objectives. Narrative explanation should distinguish between direct holdings in investee companies versus other kinds of disclosure to them.
- (b) Article 9 products must include an explanation of how their investments do ‘No significant harm to the sustainable investment objectives’;
- (c) As per Article 8 products, this should describe the ‘Investment strategy’, including binding elements of it
- (d) ‘Sustainability indicators’; - As per Article 8 product requirements
- (e) ‘Use of derivatives’; - as per Article 8 product requirements

(f) 'Website reference'; - as per Article 9 product requirements

(g) for a financial product referred to in Article 9(1) of Regulation (EU) 2019/2088, 'Sustainable investment objective attainment with a designated index'; and – Article 9 funds must explain how methodology of reference benchmark aligns with sustainable investment objective the product; how it differs from broad market index; explanation of how this alignment is ensured

(h) for a financial product referred to in Article 9(3) of Regulation (EU) 2019/2088, 'Objective of a reduction in carbon emissions' – it is currently proposed that, once available, such Article 9 product must follow a benchmark that qualifies as an EU Climate Transition Benchmark or an EU Paris-aligned Benchmark.

Please refer to Articles 23-31 of [the proposed RTS](#) for full details.

After March 2021, what are the next deadlines for product-level disclosure I need to be aware of?

After March 2021, the next obligation to comply with, at fund-level, is a disclosure requirement under the Taxonomy Regulation.

If you have Article 9 funds that are contributing to environmental objectives, from January 2022, you need to disclose whether they are contributing to climate change mitigation or climate change adaptation according to the Taxonomy. You also need to disclose the extent to which the funds' underlying investments qualify as Taxonomy-compliant. From the same date, these details will also need to be included in periodic disclosures.

From January 2022, under SFDR, you will need to include how your Article 9 funds have met their sustainability objectives in periodic reporting.

Also from January 2022, if you have Article 8 funds that are promoting environmental characteristics, you need to disclose whether they are contributing to climate change mitigation or climate change adaptation according to the Taxonomy as well as to what extent the funds' underlying investments qualify as Taxonomy-compliant. You will also have to disclose a statement on how the Do No Significant Harm Principles only applies to underlying investments that take account of the Taxonomy. From the same date, these details will also need to be included in periodic disclosures.

From January 2022, under SFDR, you would also need to include how your Article 8 funds have met their environmental or social characteristics in periodic disclosures.

For all funds that are neither Article 8 nor 9, you will need to disclose a statement saying that the fund's underlying investments do not take account of the Taxonomy. The specific wording for this is as follows (EU Taxonomy regulation, Article 7):

“The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.”

What is the next milestone for fund-level disclosures after January 2022?

From 30 December 2022, under SFDR, you will be required to disclose whether and, if so, how your products consider principal adverse sustainability impacts (SFDR, Article 7).

At a fund level, level 2 detail is not due to provide additional detail on what is meant by “principal adverse sustainability impacts”. It appears firms may need to draw conclusions from the firm-level descriptions.

And the next?

From January 2023, if you have Article 9 funds that are contributing to environmental objectives, from January 2022, you need to disclose whether these are contributing to any of the objectives according to the Taxonomy (i.e. including the remaining four objectives that hadn't been included from January 2022). You also need to disclose the extent to which the funds' underlying investments qualify as Taxonomy-compliant. From the same date, these details will also need to be included in periodic disclosures.

Also from January 2023, if you have Article 8 funds that are promoting environmental characteristics, you need to disclose whether they are contributing to any of the objectives according to the Taxonomy as well as to what extent the funds' underlying investments qualify as Taxonomy-compliant. From the same date, these details will also need to be included in periodic disclosures.

Are there any other immediate product-level considerations I should be aware of?

Firms marketing their funds into France are required to comply with the disclosures obligation under the “AMF Doctrine”. This new sets of rules from the French regulator is designed to prevent “greenwashing” by regulating the extent to which a fund can be promoted with regard to sustainable or responsible characteristics. The Doctrine introduces a categorisation framework based on the degree to which that fund is considered to be sustainable and establishes corresponding disclosure requirements.

The new rules apply immediately for UCITS launched and registered after 26 July 2020.

They apply from 30 September, for foreign UCITS launched, changed or established between 12 March 2020 and 27 July 2020.

They apply from 10 March 2021, for existing UCITS funds.

Appendix – Additional Detail on Regulatory Requirements

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AMF Doctrine, France

With the stated intention to prevent greenwashing, the French regulator – the AMF – has published requirements on how to disclose non-financial characteristics of products to retail investors.

The range of documents impacted includes:

- Regulatory documents,
- Any document available to investors and sent to the AMF for authorisation,
- Marketing Materials and
- The name of the fund.

The Doctrine revolves around the proportionality principle and distinguishes between three types of approach. Varying levels of disclosure pertaining to non-financial criteria are permitted for these three types of approach.

1. Approach based on a significantly engaging methodology (approche significativement engageante)

In such instances, non-financial characteristics are permitted to be included as a key aspect of communication. Key aspects of communication are defined as:

- The name of the collective investment product;
- Featuring prominently in the KIID; and
- Featuring prominently in marketing materials.

2. Non significantly engaging approach (approche non significativement engageante)

In such instances, non-financial characteristics cannot be disclosed as key aspects of communication but:

- can be disclosed within the KIID, so long as they feature in a concise and balanced manner and
- can be disclosed in marketing material also in a concise manner.

3. Approach not meeting central or limited communication standards (Approche n'atteignant pas les standards de la communication centrales ou réduites)

This category includes all funds that do not fall in either of the categories above. In such instances case, non-financial characteristics can only be disclosed in the prospectus.

Timeline for AMF Doctrine Application

The provisions apply to all funds established in France as well as foreign funds distributed in France as follows:

Deadline	Scope
Immediate application	UCITS launched and registered after 26/07/20
30/09/20	For foreign UCITS launched, changed or established 12/03/20-27/07/20
10/03/21	For existing UCITS funds (as at 11/03/20)*

*Note that amendments – in particular, the reduction of information disclosed – can be notified to investors in any way.

European MiFID Template (EMT), EU

The EMT (European MiFID Template), created and maintained by Findatex, a joint structure established by representatives of the European financial services, is designed to facilitate the exchange of data between distributors and manufacturers.

The template is a standardised tool to support the application of European Financial markets' legislations and is widely used by the Industry.

Considering the updated requirements on suitability introduced by the amended Mifid delegated act texts, manufacturers need to consider how best to communicate to distributors relevant information with respect to their products. The group has agreed that ESG considerations must be included in the EMT as soon as practicable as the last iteration of the EMT (version 3) contains only one field dedicated to ESG preferences limited as to whether or not the fund has an ESG dimension in the broader sense.

Further work is in progress to adapt the template in line with upcoming regulations. This includes considering how best to marry any additional fields in the EMT to the product categorisations as set out in the draft revisions to the MiFID Suitability Assessment on investors' sustainability preferences. At time of writing, the draft revisions define sustainability preferences as whether a client wishes to include products that pursue "sustainable investments" according to Article 2(17) of SFDR (Article 9 products) in their portfolio or products that promote, among other characteristics, environmental or social characteristics (Article 8 products) that also (i) pursue "sustainable investments"; or (ii) consider principal adverse impacts on sustainability factors (as referred to in article 7(1) (a) of SFDR).

Most recently, further criteria for "sustainability preferences" is being discussed whereby clients would dictate the proportion of a product that should be invested in "sustainable investments" as defined under Article 2(17) of SFDR.

Financial Conduct Authority (FCA) Non-Financial Objectives, UK

The FCA set out expectations on the Disclosure of non-Financial objectives through PS19/4 published in February 2019.^{ix} This guidance reiterates that non-financial objectives should be fair, clear and not misleading. In 2020, the FCA has been conducting a more thorough deep-dive into firms' practices and has focused on the nature of investment objectives, including how these are set and measured, as well as the investment processes behind such funds. This is being carried out with a view to assessing the extent to which additional guidance may be needed in the market.

MiFID II Delegated Acts, EU

On 8 June 2020, the Commission launched a 4-week consultation on proposed changes to the delegated acts under the UCITS, AIFMD, MiFID II (changes to organisational requirements/operating condition and suitability assessment and product governance requirements) as well as under the IDD and Solvency II frameworks. The Delegated Acts were drafted based on the recommendations prepared and publicly consulted on by ESMA and issued in April 2019. It also refers back to the Regulation (EU) 2019/2088.

The amendments encompass:

- The integration of sustainability risks within firms' processes
- The definition of "sustainability preferences" and clarification of requirements around the suitability assessment

- The consideration of principal adverse impacts of investment decisions on sustainability factors, within the due diligence process.

The drafting process is still underway, but the requirements are expected to apply from the end of 2021 at the earliest.

Non-Financial Reporting Directive, EU

In early 2020, the Commission launched its review of the Non-Financial Reporting Directive (NFRD). NFRD currently applies to large public interest entities with over 500 employees. NFRD requires these companies to report on information in relation to environmental protection; social responsibility and treatment of employees; respect for human rights; anti-corruption and bribery; and diversity on company boards, “to the extent necessary for an understanding of the development, performance, position and impact of [the company’s] activities”. This underpins the “dual-materiality perspective” – where companies are required to disclose not only how sustainability issues affect the company, and how the company affects society and the environment.

As a part of the NFRD review, the EU Commission is considering a significant expansion of the scope and content of the Non-financial reporting directive, which may result in other listed and unlisted companies to report on a much wider range of sustainability information.

NFRD and its review are particularly significant in the context of incoming requirements for firms, given that investment managers’ fulfilling their own disclosure obligations is reliant on the information they receive from companies. For this reason, the IA is asking that any review of NFRD supports financial market participants:

- With their financial decision making and investment processes; and
- With their own disclosure obligations, including under SFDR and the Taxonomy.

Specifically, the IA is asking that the Commission builds upon existing global standards, namely SASB and TCFD, to take this forward. The IA’s response to the NFRD Review can be found [here](#).

Sustainable Finance Action Plan, EU

In March 2018, the European Commission set out its Action Plan on sustainable finance as part of a strategy to integrate environmental, social and governance considerations into its financial policy framework and mobilise finance for sustainable growth.

In May 2018, the Commission released the first legislative package under the Action Plan. The four proposals included in the package were: (1) a unified EU classification system (“Taxonomy”), (2) investors' duties and disclosures, (3) low-carbon benchmarks, (4) better advice to clients on sustainability.

1. The first of the four proposals have since led to the development of the EU Taxonomy, requirements under which start to apply from January 2022.
2. The second proposal has led to the development of the Sustainability Finance Disclosure Regulation (SFDR), the requirements of which begin to apply from March 2021.
3. The third has led to the Sustainable Finance Benchmarks Regulation which has applied from April 2020 but for which No Action Relief has been adopted.
4. The fourth has led to the development of amendments to delegated acts under MiFID requiring financial advisers to gather the sustainability preferences of clients and offer products suitability to these preferences. The date of application has not yet been established but is likely to Q4 2021.

These regulatory interventions have significant consequences for disclosures, including at the product-level and for the distribution of such products, and are explored in further details below.

Sustainable Finance Disclosure Regulation, EU

On 22 March 2019, the European Council published the text of the political agreement on the proposed [Regulation on sustainability-related disclosures in the financial services sector](#) (SFDR). The Regulation was published in the Official Journal on 9 December 2019 and is directly applicable as from March 2021 to financial market participants and advisers. It also empowers the European Supervisory Authorities (ESAs) to develop technical standards on disclosure.

In effect, the SFDR requires market participants to provide entity-level and product-level disclosures on a firm's website, in its pre-contractual documents and also its periodic reports.

The SFDR also splits investment products into three categories for which different disclosure requirements apply:

- Products that manage their ESG risks (i.e. all investment funds that are subject to these EU rules, sometimes referred to as "Article 6 products")
- Products that promote environmental or social characteristics ("Article 8 products")
- Products that pursue a particular environmental objective (i.e. environmental impact products) ("Article 9 products")

These distinctions are significant as they determine whether a product is in scope of the various disclosure requirements as set out in the draft RTS of SFDR.

Sustainable Finance Disclosure Regulation RTS, EU

Pursuant to SFDR as amended by the Taxonomy Regulation, the European Supervisory Authorities (ESAs) published in April 2020 their [consultation](#) on regulatory technical standards ("RTS") for the SFDR. The draft RTS set out requirements on the content and presentation of entity-level and product-level disclosures.

As set out above, we now understand that the level 2 requirements on which the ESAs were consulting are expected to apply from a date later than March 2021 – most likely January 2022.

The final level 2 requirements are subject change pending the ESAs' final proposals and the European Commission's final decision expected mid-2021.

1. Entity-level disclosures on firms' website (Article 4 of SFDR)

Asset managers are required to provide, within a pre-defined template, details of their adverse sustainability impact assessment including mandatory quantitative disclosures and explanation. The mandatory quantitative disclosures require data on a range of indicators with accompanying metrics. While the rules are set to apply on a comply-or-explain basis, it is mandatory for financial market participants or groups with more than 500 employees. Entities that elect not to comply will have to disclose a prominent statement to highlight this.

2. Product-level disclosure in pre-contractual documents, website and periodic reports for products which promote environmental or social characteristics and for sustainable investment products (art 8, 9, 10, 11 of SFDR)

The proposed rules establish the obligation for asset managers to provide detailed disclosure for products with environmental or social characteristics (Article 8 of SFDR) and sustainable investment products (Art 9 of SFDR). It is worth noting that while the use a mandatory reporting template is alluded to, it has not yet been developed and does not appear within this draft RTS. It is understood the ESAs are developing the templates through a separate process.

Task Force on Climate-related Financial Disclosures (TCFD), global

In December 2015, the Financial Stability Board (FSB) established the industry-led Task Force on Climate-related Financial Disclosures (TCFD) to develop climate-related disclosures that "could promote more information on investment, credit and insurance underwriting decisions" and, in turn, "would enable stakeholders to understand better the concentrations of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks". The TCFD's [final report](#) was published in June 2017 and introduces a framework detailing four levels of disclosure at an entity-level as well as portfolio-level as follows:

- Governance

- Strategy
- Risk management
- Metrics and targets

The TCFD recommendations are not yet mandatory, but there are discussions underway on a possible mandatory application to listed companies and large asset owners.

In March 2020, the FCA put out its [consultation paper](#) on proposals to enhance climate-related disclosure by listed issuers and clarification of existing disclosure obligations. The IA responded in October, proposing mandatory reporting for premium listed companies and comply or explain for those with a standard listing. In August 2020, the DWP put out its [consultation](#) on improving governance and reporting by occupations pensions schemes. The IA responded in October highlighting the importance of consistent reporting across the investment chain; the importance of not inadvertently encouraging short termism through quarterly reporting of climate-related metrics; and calling for a narrower range of disclosures to encourage comparability and consistency. Most recently, The FCA [announced](#) that it will be consulting on Client-focused climate-related disclosures by investment managers and contract-based pension schemes in early 2021.

A cross-Whitehall/cross-regulator taskforce has been set up to coordinate the application of these requirements across the investment chain. A key consideration when bringing in these regulatory changes is to ensure that the requirements on investee company, investment manager, and asset owner are consistent.

Taxonomy, EU

The EU Taxonomy that is, the "[Regulation on the establishment of a framework to facilitate sustainable investment](#)" was published in the Official Journal in June 2020. It identifies economic activities that are deemed to be sustainable through a harmonised classification system and requires financial markets participants to make certain disclosures, primarily focusing on disclosing the level of alignment with activities that are considered as sustainable.

Particularly, the Regulation identifies six environmental objectives that an economic activity deemed to be environmentally sustainable must contribute toward:

1. Climate change mitigation;
2. Climate change adaptation;
3. Sustainable use and protection of water and marine resources;
4. Transition to a circular economy;
5. Pollution prevention and control; and

6. Protection and restoration of biodiversity and ecosystems.

In addition to substantially contributing to one or more of the six environmental objectives mentioned above, an activity is deemed environmentally sustainable if

- If it does no significant harm to any of the environmental objectives mentioned above;
- Is carried out in compliance with minimum safeguards; and
- Complies with the technical screening criteria that have been developed by the [Technical Expert Group \(TEG\)](#).

On 9 March 2020, the TEG published its [final report](#) on EU taxonomy. This has since been built upon by a technical [annex](#). The report contains recommendations relating to the overarching design of the EU taxonomy, as well as extensive implementation guidance on how companies and financial institutions can use and disclose against the taxonomy. The report is supplemented by a technical annex.

The requirements to disclose the alignment of an investment product with the first two objectives apply from January 2022.

Requirements to disclose alignment of an investment product with the remaining four objectives apply from January 2023.

ⁱ For the purposes of this paper, “sustainability” is understood as the ability to “meet the needs and aspirations of the present without compromising the ability to meet those of the future”. This is taken from the Brundtland Report’s definition of “sustainable development”.

ⁱⁱ For the purposes of this paper, “responsible investment” is used as the overarching term to refer to the broad range of investment approaches that encompass environmental, social and governance information. This may be used in relation to investment processes and/or in relation to investment outcomes.

ⁱⁱⁱ Demonstrated by the UK government’s [Green Finance Strategy](#) of 2 July 2019.

^{iv} Demonstrated by the [FCA’s Green Finance and Climate Change Policy Statement](#), October 2019 and [FCA Consultation Paper](#) CP20/3 March 2020. Bank of England [Stress Test Consultation](#), December 2019.

^v IA data show that from January 2019 to July 2020 retail savers put a net £8.1 billion into responsible investment funds, 40% of the total industry inflow over the same time period. A monthly breakdown of these figures is available [here](#).

^{vi} For the purposes of this paper, “sustainability-related funds” is intended to encompass the broad range of funds that either promote social and environmental characteristics or pursue sustainability objectives according to the EU Sustainable Finance Disclosure Regulation.

^{vii} According to Morningstar data, in 2019 European sustainable funds held €668 billion of assets, which was up 58% from 2018. According to the same report, 2019 saw the launch of 360 sustainable funds, which brought the total number across Europe to 2,405. The report goes on to say that approximately 50 of the sustainable funds launched in 2019 had a specific climate-oriented mandate. [Source](#).

^{viii} The IA identified sustainability and responsible investment at a dedicated policy area at the start of 2018. The committee leading this work is one of the IA’s largest.

^{ix} [FCA Policy Statement 19/4](#), Final non-Handbook Guidance, p. 9.