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FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

On 28 November 2023, the UK's Financial Conduct Authority (FCA) unveiled its Policy Statement PS 23/16 (Policy Statement), which sets out the final rules for sustainability disclosure and investment labels (SDR Rules). The market has been anticipating this development since the FCA released its consultation paper on the draft SDR Rules in October 2022 (SDR Consultation). See our 1 March 2023 client alert "UK Labeling Rules for 'Sustainable' Investment Products Will Soon Be Finalised".

Recognising the growing global market in ESG-oriented assets, now estimated to total \$18.4 trillion, the FCA emphasises the critical need for a UK sustainable labelling, marketing and disclosure regime, similar to the European Union's influential Sustainable Finance Disclosure Regulation (EU SFDR). The finalisation of the SDR Rules is a significant step towards that goal.

The SDR Rules represent a comprehensive suite of regulations and measures designed to help investors navigate the UK market for sustainable investment products. They include:

- Anti-greenwashing rules.
- Financial products labelling regulations.
- Product naming and marketing requirements.
- Product-level and entity-level disclosure requirements.
- Rules for distributors that market these products to retail investors.

In this article, we discuss the key features of the new rules, along with the detailed takeaways for each rule within the package. Additionally, we will examine the global compatibility with other regulatory developments and look into the FCA's future regulatory ambition.

1. Key Features of the Suite: Limited Scope and Staggered Implementation

Although the SDR Rules have been keenly awaited by the market and offer a degree of regulatory certainty, their scope is fairly narrow, thus limiting their practical impact on the UK's institutional alternative investment market. However, these rules lay a foundation for the FCA's future regulatory steps. In the meantime, the staggered implementation is designed to guide the market smoothly through the evolving regulatory expectations.

Aside from the anti-greenwashing rule which is set to become effective on 31 May 2024 and will apply to all FCA-authorized firms (Anti-Greenwashing Rule), the majority of the SDR Rules — ranging from product labelling, naming and marketing to disclosure rules — are applicable primarily to UK asset managers, which, most commonly, include

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

UK undertakings for collective investment in transferable securities (UCITS) and both full-scope and small UK alternative investment funds (AIFs).

In contrast, overseas funds and portfolio management services currently fall outside the scope of these rules. Limiting the regulations to UK asset managers contrasts with the approach of the EU SFDR, which applies to both EU funds and non-EU funds marketed within the EU.

While some SDR Rules are aimed at both institutional and retail investors, many are specifically designed for the retail market. This includes the naming and marketing rules for unlabelled products, the consumer-facing product disclosure rules and the specific requirements for retail distributors. As the FCA has

stated, the primary aim of the SDR Rules is to “inform and protect consumers and improve trust in the market for sustainable investment”, so the FCA’s rules are tailored to assist consumers in navigating the market for sustainable products and to ensure they have access to consistent information to make informed choices.

In contrast, the EU SFDR encompasses both the institutional and retail investor markets, with a notable impact on the institutional sector.

To facilitate easier comprehension, we have summarised each of the key SDR Rules in the table below, detailing what types of firms come within their scope, target investor types and the timelines for implementation. The specifics of each rule will be discussed in their respective sections in Section 2 below.

SDR Rules (with links to details below)	In-Scope Firms	Target Investor / Implementation Timeline
Anti-Greenwashing Rule (Section 2.1)	All FCA-authorized firms	All investors: From 31 May 2024
Labelled Product: Labelling and Naming Rules (Section 2.2)	UK asset managers (incl. managers for UK AIFs and UK UCITS)	All investors: From 31 July 2024
Unlabelled Product: Naming and Marketing Rules (Section 2.3)		Retail investors: From 2 December 2024
Product-Level and Entity-Level Disclosure Rules (Section 2.4)		All investors:* Various dates from 2024 to 2026 (detailed below)
Rules for Distributors (Section 2.5)	Distributors	Retail investors: 31 July 2024 or 2 December 2024 (detailed below)

* Certain consumer-facing disclosures for retail investors only.

2. Takeaways

2.1 Anti-Greenwashing Rule and Guidance Consultation

Tackling “greenwashing” is a regulatory priority for the FCA. The Anti-Greenwashing Rule applies to all FCA-authorized firms, which number 45,608 across the UK, according to the Policy Statement. These rules mandate that any references or descriptions made to the sustainability product or service must be both (a) consistent with the sustainability characteristics of that product or service and (b) fair, clear and not misleading.

The Anti-Greenwashing Rule is broad, encompassing all communications and financial promotions, written or verbal, that make sustainability-related claims about the environmental or social characteristics of a product or a service. It covers references to aspects such as the environment, climate, biodiversity, nature, social issues and corporate social responsibility. The rule also applies to the use of specific terms like “green” or “sustainable”, to ensure that such claims are aligned with the true nature of the products or services they describe.

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

To facilitate a smoother adoption, the FCA is currently [consulting on further guidance](#) for the Anti-Greenwashing Rule, which is set to conclude on 26 January 2024. As outlined in the consultation paper, the FCA expects firms to ensure that any sustainability-related claims are:

- Factually correct and capable of being substantiated.
- Clear, transparent and straightforward, avoiding any technical jargon or vague, broad and general terms.
- Representative and complete, and consider the full life cycle of the product or service.
- Fair and meaningful in relation to any comparisons to other products or services, thereby aiding consumers in making informed choices.

2.2 Labelled Products: Labelling and Naming Rules

The Policy Statement incorporates and advances the labelling principles previously outlined in the SDR Consultation, creating defined product categories.

There have been a few modifications: The three labels proposed in the SDR Consultation, “*Sustainable Focus*”, “*Sustainable Improvers*” and “*Sustainable Impact*”, have now been renamed as “*Sustainability Focus*”, “*Sustainability Improvers*” and “*Sustainability Impact*”, respectively. Additionally, the Policy Statement introduces a new, fourth label not included in the SDR Consultation: “*Sustainability Mixed Goals*”, which is designed for products that invest in a mix of assets.

Although the use of labels is entirely optional for UK firms, any product using one of the four labels must meet the qualifying criteria on an ongoing basis. These criteria include five general criteria applicable to all labels, alongside some specific criteria unique to each label. Appendix A outlines the four labels, their respective descriptors, and the general and specific criteria that must be satisfied for each.

2.3 Unlabelled Products: Naming and Marketing Rules

The naming and marketing rules are specifically designed for products offered to retail investors that do not bear one of the four approved labels.

The FCA has made it clear that sustainability-related terms, like “green”, “environmental”, “social” or “responsible,” are only permissible in a product’s name if either (a) the product carries one of the four labels (except that the term “impact” is exclusively reserved for the Sustainability Impact label) and meets the criteria for the label, or (b) the product does not use a label but adheres to certain prescribed naming and marketing criteria:

Naming criteria: Product names must provide an accurate representation of the sustainability characteristics (except that “sustainable”, “sustainability”, “impact” and their variations must be used for labelled products only). These unlabelled products must make the same types of disclosures required for labelled products. Firms are also obligated to publish a statement clarifying the absence of a label and providing an explanation why.

Marketing criteria: Firms must produce the same disclosures, set out in Section 2.4 below, as products using sustainability-related terms in their names.

2.4 Product-Level and Entity-Level Disclosure Rules

Like the EU SFDR, the SDR Rules create disclosure obligations in two main categories: product-level and entity-level. In contrast to the EU SFDR, which mandates in its Regulatory Technical Standards the distinct disclosure content for various product categories, the SDR Rules adopt a more uniform approach for both labelled and unlabelled products, albeit with certain distinctions based on their sustainability attributes.

The product-level disclosure framework includes four key types of disclosures: (1) consumer-facing disclosures, (2) pre-contractual disclosures, (3) periodic disclosures and (4) on-demand disclosures. A comprehensive breakdown of these disclosure types and their respective implementation timeline is presented in Appendix B.

It should be noted that, for UK AIFs that are not FCA-authorized and not listed on a recognised exchange, there is a requirement to furnish on-demand disclosures to “eligible clients”, *i.e.*, clients who require the information for their own sustainability-related disclosure obligations, whether under the SDR Rules or as a result of other legal or regulatory requirements. While the FCA has not provided explicit clarification, “other legal or regulatory requirements” may be interpreted to encompass foreign regulatory frameworks, too. This could potentially place additional pressure on UK asset managers, as they are obliged to act reasonably and provide on-demand disclosures that they consider appropriate to meet the information needs of their eligible clients.

At the entity level, in alignment with the four pillars outlined by the Task Force on Climate-related Financial Disclosures (TCFD), the SDR Rules also require that firms provide information about their (1) governance, (2) strategy, (3) risk management and (4) metrics and targets, concerning the management of those sustainability-related risks and opportunities. Additionally, when firms use labels or use sustainability-related terms in the names and marketing of their unlabelled products, they must also include details on their resources, governance and organisational arrangements in relation to those products.

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

The FCA has listed some global standards that may be relevant in helping firms to determine what they should disclose:

- The TCFD's supplementary guidance for asset managers.
- The International Financial Reporting Standards sustainability disclosure standard.
- The Sustainability Accounting Standards Board's standards.
- The Global Reporting Initiative's standards.

The implementation date for firms of over £50 billion in assets under management is 2 December 2025 and for all other firms is 2 December 2026.

2.5 Rules for Distributors

The SDR Rules also govern the distribution of funds to UK retail investors, including both UK labelled funds and UK and overseas unlabelled funds that use ESG terms in their marketing materials. The term "distributor" refers to UK firms that "distribute" a product by offering, selling, advising or making arrangement for such products. That includes financial advisers and platforms targeting retail investors.

In-scope distributors are required to (a) communicate the labelling information and the consumer-facing, product-level disclosures to retail investors, and (b) when distributing overseas products that use sustainability terms in naming or marketing, include a clarification note that the product is not subject to the SDR regime. The compliance date for (a) is 31 July 2024 and for (b) is 2 December 2024.

3. Global Compatibility and Future Regulatory Plans

The FCA has recognised that many UK firms are already subject to the EU SFDR. Accordingly, the Policy Statement evaluates the SDR Rules' compatibility with other regulatory regimes, including not only the EU SFDR but also various other proposals and policy plans put forth by regulators in the US, Australia, Singapore, Switzerland, the Netherlands and other jurisdictions.

With regards to labels and criteria, the SDR Rules notionally align with the EU SFDR. For example, the use of key performance indicators (KPIs) under both regimes is intended to measure the attainment of environmental and/or social characteristics and sustainable objectives. However, there is a significant distinction in that the EU SFDR mandates "sustainable objectives" only for Article 9 products (funds that have sustainable investment as their objective), whereas the SDR Rules extend the requirement to have

a "sustainability objective" as part of their investment objectives to all labelled products, making it a general criterion applicable to all labels regardless how "green" the product is.

For product-level and entity-level disclosures, both the SDR Rules and the EU SFDR have similar coverage areas, such as the disclosure of adverse impacts, the proportion of sustainable investment, the investment strategy and any engagement policies. However, the SDR Rules have gone a step further by requiring additional details that in-scope firms must provide. For example, the SDR Rules mandate that firms should outline their resources, governance and organisational arrangements that align with the delivery of sustainability objectives. Additionally, the stewardship strategy, which encompasses expected activities and outcomes, requires further work such as the escalation plan, which goes beyond the engagement policy disclosure under the EU SFDR.

Looking ahead, the FCA has outlined plans to explore the possibility of extending the SDR regime or similar rules to the following sectors:

Portfolio management: The FCA has recognised that the SDR Rules are not yet applicable to portfolio management because most portfolio managers have diversified portfolios and are unlikely to only invest in labelled UK funds. To address this gap, the FCA plans to initiate a consultation in early 2024 on proposals concerning portfolio management, with a focus on those targeting UK retail clients, including managed portfolios and discretionary wealth management services.

Overseas funds: While overseas funds are not currently in scope (except for the requirement that the distributors of overseas funds add a notice to retail investors that the funds are not subject to the SDR regime), the FCA intends that all firms marketing their products in the UK should preferably be subject to the same broad requirement, so it plans to continue working with the HM Treasury to extend the SDR Rules to overseas funds.

Miscellaneous: The FCA plans to develop proposals for other products and financial services providers in the future. For instance, the FCA seeks to develop proposals for pension and insurance-based investment products in the medium term by engaging the relevant pension regulators. It intends to explore further supervision of financial advisers advising on sustainability, by setting up independent working groups for the advice industry. It also plans to consider updating the product-level and entity-level disclosure requirements once the UK Green Taxonomy, which is intended to specify certain environmental objectives for economic activities, is in use.

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

Appendix A: Investment Labels

The SDR Rules establish five basic principles governing the labelling of sustainability products:

Sustainability objective: The product must have a clear, specific and measurable sustainability objective to improve or pursue positive environmental and/or social outcomes as part of their investment objectives, and firms must identify and disclose whether that pursuit may result in any material negative outcomes.

70% asset rule: 70% of the gross value of the assets must be invested in accordance with its sustainability objective and firms must also identify and disclose other assets held for other reasons (e.g., cash, derivatives).

Key performance indicators (KPI): While the FCA has not prescribed which KPI shall be used, it requires firms to identify KPIs to measure performance and progress against their sustainability objective.

Resources and governance: Firms must have appropriate resources, governance and organisational arrangements in place to support the delivery of their sustainability objective.

Stewardship: While the FCA has not prescribed the form of stewardship strategy, it requires firms to identify and disclose the investor stewardship strategy and resources to achieve sustainability objectives, and to adopt an escalation plan when their assets do not demonstrate sufficient progress towards the 70% threshold.

Four product labels are established under the rules, with definitions and label-specific requirements:

Label	Descriptor	Label-Specific Criteria
Sustainability Impact	Invests mainly in solutions to sustainability problems, with an aim to achieve a positive impact for people or the planet.	<p>The sustainability objective must be consistent with an aim to achieve a pre-defined positive measurable impact in relation to an environmental and/or social outcome.</p> <p>Firms must specify a theory of change setting out how they expect their investment activities and the product's assets to contribute to positive impact.</p> <p>Firms must also specify a robust method for measuring and demonstrating the positive impact of both their investment activities and the assets invested.</p>
Sustainability Focus	Invests mainly in assets that focus on sustainability for people or the planet.	<p>The sustainability objective must be consistent with an 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.</p> <p>Other assets out of the 70% scope must not be in conflict with the sustainability objective.</p>
Sustainability Improvers	Invests mainly in assets that may not be sustainable now, with an aim to improve their sustainability for people or the planet over time.	<p>The sustainability objective must be consistent with an 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 environmental and/or social sustainability.</p> <p>Firms must identify the period of time in which the product and/or its assets are expected to meet the standard, including short and medium-term targets for improvements.</p> <p>Firms must also obtain robust evidence that the selected assets have the potential to meet the standard.</p> <p>Firms' investor stewardship strategy should support the delivery of the objective and help to accelerate improvements over time.</p>

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

Label	Descriptor	Label-Specific Criteria
Sustainability Mixed Goals	Invests mainly in a mix of assets with a mix of sustainability objectives.	<p>The sustainability objective should be a combination of the sustainability objectives for the other labels.</p> <p>Firms must identify and disclose the proportion of assets invested in accordance with any combination of the other labels.</p> <p>The specific criteria for each of the constituting labels in the “mix” must be met.</p>

Appendix B: Disclosure Requirements

Disclosure Type / Requirements	Disclosure Items	Implementation
Consumer-Facing Disclosure		
<p>Required when marketing to retail investors.</p> <p>Provided in a standalone document (no specific template).</p> <p>Reviewed and updated annually.</p>	<p>For labelled products, description of its label and sustainability objective. For unlabelled products, a statement to clarify that it does not have a label and explain why.</p> <p>Investment policy and strategy, and relevant metrics.</p> <p>Details of where a consumer can access other relevant sustainability disclosures.</p>	2 December 2024
Pre-Contractual Disclosure		
<p>Made in a fund prospectus, prior information document or Part A of a Sustainability Product Report (based on the TCFD product report), as applicable.</p> <p>Do not need to be updated annually but as soon as a label is revised or ceased to use.</p>	<p>For labelled products, the disclosure should be broadly associated with the qualifying criteria for the labels, including the general criteria and label-specific criteria.</p> <p>For unlabelled products, the disclosure should include a statement that the product does not have a label and explain why. The disclosure should also at a minimum include information relating to the investment policy and strategy, and relevant metrics.</p>	<p>Labelled products: 31 July 2024</p> <p>Unlabelled products: 2 December 2024</p>
Periodic Disclosure		
<p>Published annually.</p> <p>Required for both UK authorised funds and unauthorised UK AIFs listed on a recognised investment exchange.</p> <p>Must be made in Part B of a Sustainability Product Report.</p>	In general, similar to pre-contractual disclosure.	<p>Labelled products: 31 July 2025</p> <p>Unlabelled products: 12 months after the sustainability term is first used</p>

FCA Finalises UK Sustainable Investment Rules, With More To Follow After Further Consultation

Disclosure Type / Requirements	Disclosure Items	Implementation
On-Demand Disclosure		
<p>For UK AIFs not authorised in the UK or listed on a recognised exchange, on-demand disclosures must be provided to eligible clients. Discussed in detail in Section 2.4.</p> <p>Must be provided within a reasonable timeframe of client request.</p> <p>Must be provided in a form that the UK asset manager, acting reasonably, considers appropriate to meet the information needs of that client.</p>	<p>In general, similar to pre-contractual disclosure.</p>	<p>2 December 2025</p>