

IIGCC response to FCA Consultation Paper 22/20 on Sustainability Disclosure Requirements and investment labels

About us

The Institutional Investors Group on Climate Change (IIGCC) is the leading European membership body enabling the European and UK-based investment community in driving significant and real progress by 2030 towards a net zero and resilient future. IIGCC's 375+ members (over half of which are UK-based), representing £53 trillion assets under management, can catalyse real world change through their capital allocation decisions, stewardship and engagement with companies and the wider market, as well as through their policy advocacy.

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Executive Summary

IIGCC is pleased to respond to the FCA's CP22/20: Sustainability Disclosure Requirements and investment labels, a key milestone in the development of the UK's sustainable finance regulatory framework. The FCA's recognition of the materiality of climate and wider sustainability factors for investment decision-making and capital allocation is welcomed by the institutional investment community. By laying the foundations for informing investors and consumers on these factors, the proposals should help to accelerate progress towards the UK Government's objective to 'green the financial system'. Decision-useful information on climate and wider sustainability-related issues will provide a basis for investors to act on this information and ultimately shift financial flows in line with the UK's net zero commitment.

We are strongly supportive of the holistic approach the FCA has taken by establishing a fund labelling system alongside the broader sustainability disclosure regime – two distinct but related frameworks that will help to bring clarity to the market. Robust criteria for assessing the sustainability of investments, and the intended sustainability outcomes of these investments, will help to tackle greenwashing and underpin consistent approaches to fund categorisations. IIGCC is particularly pleased to see the inclusion of a dedicated 'Sustainable improvers' label in the regime, which will be critical for scaling and accelerating investment in the companies that will have the greatest impact on the UK's transition to a net zero economy. By bringing together a range of reporting requirements under one framework, including existing climate-related reporting obligations, the proposals will also help to establish a more coherent and holistic framework for sustainability disclosure. This represents an important step forward in terms of providing investors with the high-quality, standardised data they need to inform their decision-making processes and reorient capital in line with net zero and the UK's wider sustainability objectives.

While recognising these positive developments, IIGCC and its members have identified several areas which we encourage the FCA to consider in more detail. We acknowledge that many of the measures have been designed with retail investors in mind, but it will also be important to ensure that the needs of institutional investors are also accounted for. In particular, we ask the regulator to:

- provide clarity on the expansion of the scope of the regime to overseas and pension products as soon as possible;
- uphold interoperability between the proposals and regimes in other jurisdictions, including the EU's Sustainable Finance Disclosure Regulation (SFDR), recognising that many investors with exposure to the EU have already taken steps to meet the requirements of the EU regime;
- avoid sequencing issues in relation to the implementation of SDR, which will undermine the flow of information across the investment chain;
- reconsider the decision to make the three categories of labels mutually exclusive, in acknowledgement that many investors will pursue blended investment strategies when seeking to achieve sustainability objectives (including net zero alignment);
- clarify how funds pursuing these blended approaches (e.g. investing in climate solutions while also seeking to reduce the emissions profile of their portfolios) should navigate the labelling regime;
- clarify the concept of 'unexpected investments' and how this will apply in practice;
- clarify what is meant by a 'credible standard' of sustainability.

We would be happy to discuss further any aspect of our response and look forward to hearing from you.

Please note that we have not included in this document any questions which we have chosen not to respond to.

Q1. Do you agree with the proposed scope of firms, products and distributors under our regime? If not, what alternative scope would you prefer, and why?

IIGCC supports the proposed scope of firms, products and distributors under the regime. Many of IIGCC's members are either asset owners, EU-based, or both, and so we emphasise the need for the FCA to provide clarity on the expansion of the scope of the regime to overseas and pension products as soon as possible. To enable cross-border fund flows and comparability of sustainable investment products, the FCA must seek to ensure the UK regime is as interoperable and coherent with those established in other jurisdictions as possible, including the EU's Sustainable Finance Disclosure Regulation (SFDR).

We note that clarification on the application of the regime to overseas funds will also be important to create a level playing field between these funds and UK-domiciled ones. For example, so long as overseas funds are out of scope, then they could include sustainable terminology in their fund names and market sustainability features without complying with the stricter requirements established under the proposed naming and marketing rules. Although ESMA is consulting on guidelines on fund's names and the use of ESG terms, there is a risk that a lack of consistency between the two regimes could create confusion and risk misleading consumers and investors.

With regards to entity-level disclosure requirements, IIGCC supports the consistency between the proposed scope and the scope of firms captured by the FCA's TCFD disclosure requirements. This approach will help to support the overall coherency of the UK's sustainability disclosure framework. However, we note that smaller investors with under £5bn in AUM will not be covered by the proposed scope. To reorient capital towards net zero at the pace and scale needed to reach net zero by 2050, IIGCC believes it is essential for all investors to adequately identify, manage and disclose on

sustainability risks and opportunities in a manner proportionate to their resources and capabilities. Additionally, many of these firms will likely want to categorise existing products, or develop new products, that can qualify for the proposed labels to meet client demand for sustainable investments. In keeping with the FCA's TCFD disclosure regime for investors, IIGCC proposes that a review of the threshold for entity-level disclosures should be undertaken following the implementation of the rules (e.g. after 3 years of disclosures). In the interim, the FCA should encourage firms below the threshold to make entity-level disclosures on a voluntary basis, and provide guidance and resources to enable them to do this.

Q2: Do you agree with the proposed implementation timeline? If not, what alternative timeline would you prefer, and why?

While IIGCC is broadly supportive of the proposed implementation timeline, our main concern relates to the sequencing of the disclosure requirements in the context of the wider roll-out of SDR across the economy. To support the flow of information across the investment chain, it will be critical for corporate sustainability disclosures to come into force prior to those for investors, enabling the former to feed into the latter. At present, it remains unclear as to when SDR proposals for corporates will be issued, alongside associated implementation timelines, and whether a wider range of asset owners (e.g. occupational pension schemes) will be scoped into the regime. In addition, we still do not have clarity on the implementation of a UK 'green' Taxonomy, a vital cornerstone for the UK sustainable finance framework which will provide investors with transparency over the extent to which economic activities can align with the UK's climate objectives. This could create a situation similar to what we observed in the EU, where investors in scope of SFDR currently lack the data necessary to assess their holdings, undermining their ability to establish and monitor sustainability KPIs and metrics for their funds. IIGCC therefore emphasises the need for clarity on planned implementation timelines for these groups, and how these will relate to the roll-out of the proposals set out in this consultation. We strongly recommend that the FCA works closely and at pace with other regulatory bodies responsible for the rollout of SDR to expedite the development and agreement of corporate sustainability disclosure regimes.

Q4: Do you agree with our characterisation of what constitutes a sustainable investment, and our description of the channels by which positive sustainability outcomes may be pursued? If not, what alternatives do you suggest and why.

Overall, IIGCC is supportive of the FCA's characterisation of sustainable investments. In the interests of interoperability, we would encourage the FCA to consider how this definition relates to that established under SFDR Article 2.17, noting that many investors will have put in place processes for categorising funds in line with that definition. The FCA should engage with the European Commission and wider EU stakeholders (such as the European Supervisory Authorities) on this issue, noting that the Commission will seek to refine and clarify the definition this year.

While the importance of the enterprise contribution of underlying assets to sustainability outcomes are recognised in the consultation, we believe there should be a greater emphasis on the centrality of these contributions. Box 3 and the preceding paragraphs focus on the primacy of investor contributions to sustainability outcomes, but this is not necessarily in line with how the market perceives the hierarchy of contributions to sustainability outcomes. In the context of the net zero transition, while investors can provide an 'enabling' role by decarbonising their portfolios and scaling investment in climate solutions, the real-world impact (i.e. the decarbonisation of the real economy)

is driven by the investees themselves. Where enterprise contributions are negative, investors need to engage their holdings to encourage progress on their transition journeys. Conversely, where investees are generating positive impacts, investors should reorient capital allocations towards them. IIGCC suggests that the FCA draws the enterprise contributions out more strongly in the final text.

We agree that the channels for pursuing positive sustainability outcomes that have been identified by the FCA are relevant. We also agree that it is important to emphasise that these channels are not mutually exclusive, and investors seeking to drive positive, real-world outcomes will often seek to use a combination of all three mechanisms to do so. We have set out some high-level reflections on each of the proposed channels below:

- Active investor stewardship and engagement: IIGCC sees this as a critical channel for influencing outcomes across each of the three proposed labels, and could be broadened to account more clearly for advocacy with policymakers, regulators, standard-setters etc to drive systemic policy change (see below).
- Influencing asset prices and the cost of capital: we support this channel, but is likely to be more important for investment strategies that focus specifically on investing in climate solutions. Further detail on how asset allocation and portfolio construction can demonstrate intentionality would be helpful here (see below).
- Seeking a positive sustainability impact by allocating capital to underserved markets or addressing market failures: we have some reservations about the relevance of this channel in the context of the retail investment market. While this mechanism should be retained, it is more relevant for narrow, illiquid markets where investors play a more ‘catalytic’ role.

More broadly, IIGCC believes that there are other important mechanisms that investors leverage to achieve positive environmental and social outcomes which are not captured by the FCA in Box 3 of the Consultation Paper. For example, investors using the Paris Aligned Investment Initiative’s Net Zero Investment Framework (NZIF)¹ to align their holdings with net zero do so through a combination of portfolio construction, engagement and stewardship, and policy advocacy. Influencing asset prices and the cost of capital is relevant to portfolio construction, but as noted above, is particularly pertinent for investment strategies that focus on climate solutions. Additional actions to consider here include the use of tilted benchmarks and scaling investment in climate and wider sustainability ‘solutions’. Investors can play a critical role in shaping corporate capital allocation policies including, for example, in directing retained profits into capital expenditures that scale activity rather than paying profits out as dividends or through share buy-backs.

Top-down processes for allocating assets across different opportunities to achieve sustainability objectives (also known as ‘strategic asset allocation’) is also an important mechanism. Finally, investors should also be undertaking policy advocacy and industry engagement within financial services to help drive positive sustainability outcomes. Investors should ensure that direct and collective policy advocacy supports policy and regulation relevant for achieving ambitious sustainability objectives. They should also be engaging with market actors such as credit rating agencies, auditors, and data and service providers to ensure that their assessments, data and products are consistent with the achievement of these objectives.

¹ Net Zero Investment Framework, available [here](#).

While IIGCC acknowledges that the FCA cannot set out an exhaustive list of channels, we believe that the above mechanisms are critical tools for driving positive real-world sustainability outcomes, and would fit relatively neatly within the list of channels already identified by the FCA. IIGCC also stresses that there is an important distinction between achieving sustainability goals, such as emissions reductions, within a portfolio, and delivering emissions reductions in the real economy, which need to be considered in the context of these actions. Net zero portfolios are not the same as net zero economies, and if investors are to generate positive real-world outcomes, the focus must be on the latter. It is important that the regulatory framework for sustainable investment labels adequately reflects this.

Q5: Do you agree with the proposed approach to the labelling and classification of sustainable investment products, in particular the emphasis on intentionality? If not, what alternatives do you suggest and why?

IIGCC is supportive of an approach to classifying products based on intentionality, provided this intentionality is supported by robust, measurable criteria for assessing and reporting on how sustainability objectives are achieved.

The revisions to the sustainable labels are broadly sensible, and we welcome the decision to remove the 'responsible' and 'not promoted as sustainable' categories from the scope of the regime. We are particularly pleased to see that consideration has been given to the need for products investing in assets with the potential to transition towards sustainable levels of performance over time. In the context of climate change, IIGCC firmly believes that the primary objective of investors in relation to climate change should be to achieve the greatest real-world impact on emissions reductions possible by encouraging carbon-intensive companies to transition and by scaling investment in the climate solutions we need to reach net zero. As highlighted above, this will require an increased emphasis on the centrality of the enterprise contribution of underlying assets to climate and wider sustainability outcomes. In line with the alignment maturity scale established by NZIF, IIGCC would consider the 'Sustainable focus' label to primarily cover assets that are aligning or aligned with the Paris Agreement, 'Sustainable improvers' to primarily cover assets that are not presently aligned, but with whom investors are engaging, and 'Sustainable impact' to focus predominantly on climate solutions.

However, IIGCC has serious concerns with the proposal that the three categories of labels proposed by the FCA are intended to be mutually exclusive. Many investors pursuing sustainable objectives, including alignment of their portfolios with net zero, and across a range of asset classes, will in practice adopt a blended strategy for achieving this. Investors using NZIF set portfolio coverage goals to increase the percentage of their holdings that are i) achieving net zero or ii) 'aligned' with net zero, measured against current and forward-looking alignment criteria, and alongside stewardship and engagement actions. In addition, investors using NZIF also aim to increase investment in climate solutions (e.g. taxonomy-aligned activities) needed to reach net zero.

Given these nuances, it is not entirely clear which label a fund operating such a strategy would qualify for. While 'sustainable improvers' is perhaps the most obvious choice, would such a fund need to be re-labelled as 'sustainable focus' as the proportion of its 'aligned' holdings reaches a critical mass (e.g. 70%)? Would it need to sell assets that reach a 'credible' standard of sustainability (including any investments in climate solutions that are presently sustainable), or assets that are

assessed as ‘aligned’, and re-invest the capital in transitioning assets? If holdings in the fund are not demonstrating the necessary level of improvement over time, and key engagement objectives are not being met, would the fund lose its label? In our response to the FCA’s Discussion Paper,² IIGCC recommended that the FCA should not impose a binary distinction between ‘transitioning’ and ‘aligned’ products,³ but there is a danger that this is exactly what will happen under the proposed regime. Where investors are pursuing climate adaptation objectives, or investing in emerging markets, they may also incorporate elements of the criteria for ‘sustainable impact’ label as well.

IIGCC notes that NZIF is the most utilised methodology by investors for aligning their portfolios with net zero, with over 50 UK-based asset owners and managers having adopted the framework to date.⁴ We are concerned that the FCA’s proposals as they stand do not fully reflect how institutional investors are implementing blended climate investment strategies in practice, and would prevent those using frameworks like NZIF from being able to apply these labels. We would welcome further discussions with the FCA on this critical topic, including whether a ‘blended label’ approach could be considered (at least for institutional investors).

We acknowledge that one of the key aims of the FCA’s proposed labelling regime is to ensure that labels are sufficiently simple and accessible, which in turn will better enable clients and consumers to navigate the market for sustainable investment products. We support this objective fully, and understand that additional ‘sub-categories’ of labels are likely to add undue complexity to the regime. Nevertheless, IIGCC proposes that the FCA should issue guidance as to how investors pursuing these blended strategies, which could incorporate elements of two or three labels, should approach the categorisation of their products. As an example, this could include clarifying that a fund with a ‘sustainable improver’ label is also permitted to hold assets that are already sustainable as part of its strategy.

Q6: Do you agree with the proposed distinguishing features, and likely product profiles and strategies, for each category? If not, what alternatives do you suggest and why?

IIGCC broadly agrees with the proposed distinguishing features. However, we re-iterate our comments in our response to Q4 that investors will use a range of channels for achieving sustainability outcomes, some of which have not been adequately captured in the consultation. In relation to the three categories specifically:

a. Sustainable Focus: whether at least 70% of a ‘sustainable focus’ product’s assets must meet a credible standard of environmental and/or social sustainability, or align with a specified environmental and/or social sustainability theme?

- Sustainable Focus: setting a high minimum percentage of sustainable holdings within this category will help to ensure the credibility and integrity of funds using this label. However,

² IIGCC response to FCA Discussion Paper on Sustainability Disclosure Requirements and investment labels, available [here](#).

³ In line with NZIF, IIGCC would consider a transitioning asset to be ‘aligned’ if a credible plan is in place for the asset to reach net zero by 2050 or sooner. For listed assets, NZIF employs a number of forward-looking indicators to provide a more holistic view of alignment potential for assets in high impact sectors, including short- and medium-term emissions reduction targets, capital expenditure and whether a credible decarbonisation strategy is in place to achieve targets.

⁴ As of November 2022.

the current 70% threshold of sustainable investments will likely need to ratchet up over time to support the UK's climate targets, including its net zero by 2050 commitment. Such a threshold is unlikely to be an appropriate bar for ambition in 2030, for example, and even less so in 2040. Conversely, IIGCC notes that the investible universe of companies whose activities are already 'sustainable' or aligned with net zero is relatively small at present, which could create challenges for investors seeking to meet this threshold in practice. A degree of flexibility around how such funds are structured will therefore be important, alongside a continued focus on the need for robust real economy policies to increase the number of sustainable investment opportunities in the market.

- The FCA should clarify whether the threshold is intended to apply at entity-level (e.g. 70% of issuers/investees in the fund) or activity-level (70% of the activities undertaken by issuers/investees).
- We also believe there needs to be a stronger emphasis on how such funds should treat the remaining 30% of holdings. Without appropriate guardrails, this could create a risk of greenwashing (e.g. if the remainder of the fund assets included investments in companies whose activities were causing significant harm to the environment and/or society). IIGCC proposes that the FCA introduces requirements for funds using this label to describe the purpose of the remaining proportion of investments in the product, and explain how these investments will not harm the product's sustainability objective. Some form of Do No Significant Harm (DNSH) criteria could serve as a helpful guardrail in this context (noting that there will be a need to mitigate the usability issues we have seen in relation to the EU Taxonomy's criteria).
- The overarching focus of this label should be on products investing in assets that are already aligned, or aligning with, a credible standard of sustainability, such as the Paris Agreement. Strategies seeking to align with specific sustainability themes would be more suited to the proposed 'Sustainable impact' category.
- Additionally, while we acknowledge that the FCA wants to strike the right balance between principles and prescription, the concept of a 'reasonable investor' is very open to interpretation. The regime has clearly been designed with retail, rather than institutional investors in mind, reducing the scope for investors to pursue the type of blended strategies that clients of institutional investors would recognise and support. Related to this, the current definition of sustainable investments as those which meet a 'credible standard' of environmental and/or social sustainability is very broad, even if the expectation is for any such standard to be robust, independently assessed, evidence-based and transparent.
 - This approach provides a lot of flexibility for firms to self-determine what constitutes a 'reasonable investor', as well as the standard they assess the sustainability profile of their assets against. We believe it is important for the FCA to provide clarity on what would and wouldn't be considered a credible standard ahead of the regime coming into force, including the extent to which external and/or internal standards would suffice to meet the FCA's interpretation. We suggest that a degree of prescription could be introduced in relation to this requirement to help mitigate the risk of greenwashing, including clarity on whether such standards should be regulatory, market-driven, or proprietary in nature (or whether all these approaches are valid). The FCA could develop an indicative list of widely recognised and credible standards and initiatives here to help guide firms, such as the TCFD framework,

Climate Action 100+ Net Zero Benchmark,⁵ Transition Pathway Initiative, the NZIF, or Science Based Targets initiative (SBTi).

- Given the delay in the adoption of UK regulatory standards for assessing the sustainability of investments (such as the UK Taxonomy), and ongoing implementation and usability challenges with the EU's sustainable finance framework, a degree of flexibility in this area will be important. However, this must be balanced against the wide range of approaches investors are taking internally to determine the sustainability of their investments in the absence of further policy clarity. The FCA must therefore ensure that clear guardrails are in place to uphold a minimum baseline of ambition, consistency, and credibility where investors are using proprietary standards and frameworks to assess the sustainability of their holdings. Finally, we also note that the concept of a 'credible standard' will also likely need to be ratcheted upwards over time, and guidance should be provided on how to manage this, to continue to drive best practice for new products without the need to relabel existing older products.

b. Sustainable Improvers: the extent to which investor stewardship should be a key feature; and whether you consider the distinction between Sustainable Improvers and Sustainable Impact to be sufficiently clear?

- Sustainable Improvers: IIGCC agrees that stewardship should certainly be considered a key feature of funds seeking to achieve improvement in the sustainability performance of the underlying holdings over time. This recognises the critical role of investors in engaging with their holdings to encourage them to transition, including in line with net zero.
- The FCA should take care to ensure that criteria and metrics for engagement emphasise quality over quantity. For example reporting on the number of meetings/engagements held, or votes exercised, is not in and of itself helpful without disclosing the outcomes of these activities. We would encourage the FCA to engage with the Financial Reporting Council to ensure well-established and impactful metrics and criteria stewardship are developed, in line with the best practice established under the UK Stewardship Code.
- As highlighted in our response to Q2, it should be deployed alongside other levers such as direct management of assets, portfolio construction, asset allocation, policy advocacy and market engagement to maximise real-world impact. We also believe that the investor contribution should be considered a key feature for each of the proposed labels, and that the FCA should account for this in its final rules.
- In relation to the distinction between the 'sustainable improvers' category and 'sustainable impact' category, the incorporation of a clearly specified theory of change is a useful distinguishing feature. However, some aspects of the terminology used by the FCA could be revised to make the distinction between the two categories clearer. For example, the description of the latter as seeking to achieve 'measurable contribution to sustainable outcomes' could readily be applied to any of these labels. A 'sustainable improvers' fund may be seeking to achieve improvements in the sustainability profile of its assets over time to achieve real world emissions reductions in line with net zero. IIGCC proposes that the description of 'sustainable impact' could be amended to focus on '*an explicit intention to*

⁵ Climate Action 100+ Net Zero Company Benchmark, available [here](#).

generate positive, measurable *impact on sustainable outcomes*’ to make the distinction clearer.

c. Sustainable Impact: whether ‘impact’ is the right term for this category or whether should we consider others such as ‘solutions’; and the extent to which financial additionality should be a key feature?

- Sustainable Impact: IIGCC believes ‘impact’ is the appropriate term for this category, and the overarching focus should be investments in assets providing solutions to sustainability challenges (e.g. climate solutions). However, we reiterate that many investors are channelling capital into climate and wider sustainability ‘solutions’ across a range of strategies to achieve sustainability outcomes; investment in these solutions is not limited to funds pursuing sustainable impact objectives. Guidance on how investors should best navigate these blended approaches to investment strategies in the context of the proposed labelling regime is therefore critical. We also recommend that the FCA considers aligning its definition of impact investing more closely with that established by the Global Impact Investing Network (GIIN) in the interest of international consistency and best practice.
 - With regards to financial additionality being a key feature of such products, we note that this is very often difficult to measure (and existing definitions of impact investing, such as the GIIN definition, do not rely on this concept). This is particularly the case for equity investments, where demonstrating that investments have had an additional impact is open to debate, given that the capital will go towards general corporate purposes. Financial additionality is likely a more useful measure for other asset classes such as real estate, private equity/debt, infrastructure, and use-of-proceeds bonds such as green bonds.
 - IIGCC supports stewardship and engagement (the proposed secondary channel) as a key feature of these products. For example, NZIF recommends that investors engage in direct and collective stewardship and engagement actions in support of net zero objectives and report on the outcomes achieved. However, even in these cases, it can be difficult for investors to effectively demonstrate that it was their stewardship that constituted the ‘additional’ element in affecting change (particularly in the case of individual engagements), and it is also not clear that doing so would support the broad systemic engagement that is needed.

Q7: Do you agree with our proposal to only introduce labels for sustainable investment products (i.e. to not require a label for ‘non-sustainable’ investment products)? If not, what alternative do you suggest and why?

We agree with the FCA’s proposal to only introduce labels for sustainable investment products. As noted in the consultation, it is increasingly becoming the norm for investors to integrate ESG factors into their investment processes to manage financial risks and enhance financial returns. Including this baseline level of ESG integration within a sustainable labelling regime could muddy the waters, increasing the risk of greenwashing and undermining the FCA’s objective of helping consumers to identify and navigate the growing range of sustainable investment products. Only products with specified sustainability objectives, assessed against robust, measurable criteria, should qualify for these labels.

Beyond the proposed labelling regime, and given the materiality of sustainability risks to funds' financial performance, the FCA could consider the merits of introducing a baseline level of disclosure on ESG integration across the full range of products in-scope of the proposals. In line with Article 6 under EU SFDR, this could include reporting on whether and how sustainability risks have been integrated into investment decisions, and the potential impacts of these risks on returns, on a 'comply or explain' basis. This would help to increase transparency on how investors more broadly are considering ESG factors in their investment strategies and risk management processes. This would also be in keeping with the spirit of the current proposals, noting that the disclosure of factual and proportionate information on ESG integration policies is not prohibited for funds that don't pursue a sustainable investment label.

Q8: Do you agree with our proposed qualifying criteria? If not, what alternatives do you suggest and why? In your response, please consider:

- ***whether the criteria strike the right balance between principles and prescription***
- ***the different components to the criteria (including the implementing guidance in Appendix 2***
- ***whether they sufficiently delineate the different label categories, and;***
- ***whether terms such as 'assets' are understood in this context?***

Overall, IIGCC believes that the qualifying criteria proposed by the FCA strike an appropriate balance between principles and prescription, and we are broadly supportive of the different components to the criteria set out in the consultation. This approach should help to ensure that the UK regime avoids the implementation challenges investors have experienced in the context of the EU's SFDR, which does not, at present, set out clear qualifying criteria for determining what constitutes a sustainable investment.

We welcome the inclusion of a cross-cutting consideration under Principle 2 ('Investment Policy and Strategy') noting that firms must identify investments in a product that a reasonable investor may consider to be in conflict with the product's sustainability objective. IIGCC's view is that this consideration could be brought out more strongly in the category-specific criteria for the 'sustainable focus' label, to address concerns highlighted elsewhere in our response as to the treatment of the remaining proportion (e.g. 30%) of investments in these products. There are also several helpful references to this consideration in the implementing guidance that we feel could be highlighted more visibly in the qualifying criteria. This includes recommendations on disclosures setting out the circumstances in which 'non-sustainable' assets may be held, and the purposes for which they would be held.

This being said, issues we have raised previously (including our response to Q5) remain pertinent in the context of this question. The implementing guidance's section on investment policy and strategy cites an example of a product that invests in environmental solutions, noting that a 'reasonable investor' (which itself is defined very loosely) may reasonably expect such a product to avoid investments in carbon-intensive assets. Through the development of the NZIF, more than 100 IIGCC members representing over \$33trn in AUM fed into the design of an effective investment framework for achieving net zero emissions, measuring alignment, and transitioning portfolios. The two core pillars of this strategy are decarbonising portfolios consistent with net zero by 2050 and increasing investment in climate solutions. IIGCC remains concerned that an artificial, binary distinction between these two pillars could undermine the ability of investors to pursue a more holistic

approach to aligning their portfolios with net zero. While we note the importance of a simple and accessible regime for sustainable fund labels, additional guidance and flexibility from the FCA on this issue would be welcome.

IIGCC welcomes the strong emphasis placed on the need for credible, rigorous, and evidence-based KPIs aligned with a sustainable investment product's sustainability objective (Principle 3). However, as noted previously, in the absence of corporate SDR disclosures, investors will find it challenging to source robust and credible data for establishing these KPIs as a result of mismatched sequencing that undermines the flow of information across the investment chain. Robust criteria for the 'Sustainable Improvers' category are particularly important to avoid a situation in which funds invest in assets that are perpetually reported as 'improving' but which are in practice achieving little demonstrable progress. Investors will need to assess their holdings against credible frameworks to assess how they are progressing towards their stated goal or outcome (such as alignment with net zero). IIGCC views the five key components of a credible corporate climate transition plan as:

- Comprehensive, aligned emissions targets: short-, medium- and long-term targets, aligned with a 1.5°C scenario across Scope 1, 2 and 3 emissions (absolute and intensity);
- A credible strategy to deliver those targets: setting out quantified actions to deliver on targets, capital allocation consistent with a 1.5°C scenario, disclosure of neutralising measures, and appropriate governance and oversight;
- Demonstrable engagement to accelerate the transition: value chain and climate policy engagement consistent with a 1.5°C ambition, commitment to a Just Transition, and actions to deliver it;
- The contribution to "climate solutions": definition of low carbon production consistent with the objective of 1.5°C, investment in low carbon production consistent with a 1.5°C scenario, investment in nature-based solutions;
- Supporting emissions and accounting disclosure: disclosure of emissions and energy consumption, disclosure of impact of a 1.5°C scenario on balance sheet.

At present, the category-specific KPIs for a sustainable improvers label do not place sufficient focus on the short- and medium-term actions required to assess improvements in the sustainability profile of assets. While an increasing number of companies are committing to net zero by 2050, it is vital that these commitments are underpinned by concrete short- and medium-term steps that enable investors to assess the progress of their investees against these goals in the near-term. For example, NZIF assesses the alignment of assets against short- and medium-term emissions reduction targets, in line with the Climate Action 100+ Net Zero Climate Benchmark's alignment indicators. As noted in the consultation, outputs such as the Transition Plan Taskforce's sector-neutral and sector-specific disclosure frameworks will provide a helpful basis for formulating KPIs for the sustainable improvers category, and should be integrated into the requirements and guidance once finalised.

We note the FCA's observation that the standards in development by the ISSB could help to inform the KPIs specified for sustainable investment products. In the context of the sustainable improvers category, it will be vital to ensure that investors have access to data points that provide insights on how investees' activities impact sustainability factors, as well as the other way round (the 'double materiality' principle). IIGCC urges the FCA and Government to ensure that this double materiality lens is incorporated within the SDR regime to support investors in assessing the capability of their holdings to reduce any adverse impacts of their activities on the climate and environment, and improve their sustainability profile over time.

On Principle 5 (Stewardship), we'd encourage the FCA to consider the key steps for effective stewardship established under IIGCC's Net Zero Stewardship Toolkit (NZST).⁶ While the NZST provides guidelines to support investors with their net zero stewardship strategies, the general approach is likely to be useful for a wider range of sustainable investment strategies which focus on factors beyond climate. The NZST emphasises the need to focus on the quality rather than quantity of stewardship and engagement activities, using a systematic approach to both undertaking and disclosing on these activities, including through:

- Undertaking portfolio analysis and prioritising key engagements;
- Setting net zero alignment criteria, time-bound company-level objectives and portfolio goals;
- Developing an engagement strategy for priority companies;
- Developing a baseline (minimum-level) engagement and voting policy approach for all companies;
- Asset owner and manager alignment and engagement;
- Transparency and disclosure.

We would be happy to discuss the NZST with the FCA if of interest.

Lastly, there is a risk that the term 'assets' in this context will largely be associated with listed equity and corporate fixed income, for which there are more established methodologies and a considerably greater volume of data to enable the pursuit of sustainable investment objectives and development of KPIs. It will be critical to address data and disclosure gaps across a broader range of asset classes, such as private equity, debt, and infrastructure, and in different markets, as well as guidance on how to develop effective stewardship approaches across these asset classes and jurisdictions. The FCA should consider leveraging or showcasing existing frameworks and initiatives that are spearheading best practice in this area to help guide firms. For example, NZIF sets out recommended metrics and alignment actions across sovereign bonds and real estate, and is adding private equity and infrastructure to the asset classes covered by the Framework. This could provide useful insights for the FCA, and we would be happy to discuss our approach in more detail if of interest. With regards to sovereign debt, the Assessing Sovereign Climate-related Opportunities and Risks Project (ASCOR) is developing tools and indicators for investors to assess their sovereign debt holdings' exposure to climate-related risks and opportunities. IIGCC has also established a Bondholder Stewardship Working Group tasked with providing best practice guidance for investor engagement with corporate debt issuers, whether in developed or emerging markets. The working group will also develop guidance on new issuances in the labelled bonds market.

Q9: Do you agree with the category-specific criteria for:

- ***The 'Sustainable focus' category, including the 70% threshold?***
- ***The 'Sustainable improvers' category? Is the role of the firm in promoting positive change appropriately reflected in the criteria?***

⁶ Net Zero Stewardship Toolkit, available [here](#).

- ***The ‘Sustainable impact’ category, including expectations around the measurement of the product’s environmental or social impact? Please consider whether there any other important aspects that we should consider adding.***

See our response to Q8 for our views on the category-specific criteria, which addresses a number of these topics. As highlighted above, IIGCC notes that category-specific criteria for stewardship and engagement are only included for the ‘Sustainable improvers’ label. These activities are equally important for funds that seek to invest in assets that already align with a target sustainability profile, as well as funds pursuing a sustainable impact strategy. We encourage the FCA to consider requirements for firms to report on stewardship KPIs across each of the proposed fund labels to address this.

With regards to criteria to measure outcomes under the ‘Sustainable impact’ label, the focus should be on:

- intentionality and demonstrating that the intention of the investor is to enable positive sustainability outcomes (which can be delivered through a clear theory of change); and
- the measurement of the associated impact delivered through the enterprise contribution.

In addition, and of equal importance, these products should also demonstrate that they are delivering an investor contribution through the investor’s engagement and stewardship activities.

Q10: Does our approach to firm requirements around categorisation and displaying labels, including not requiring independent verification at this stage, seem appropriate? If not, what alternative do you suggest and why?

IIGCC agrees with the FCA’s approach at this stage, but we note that potential requirements for independent verification should be kept under review as the regime beds in.

Q11: Do you agree with our proposed approach to disclosures, including the tiered structure and the division of information to be disclosed in the consumer-facing and detailed disclosures as set out in Figure 7?

IIGCC broadly agrees with the proposed approach. We would like to reiterate some of our recommendations in our response to the FCA’s original Discussion Paper (DP),⁷ namely that consumers should be able to access the more detailed product- and entity-level information should they so choose. This could help them to make informed investment decisions, and would recognise the broad spectrum of understanding within the consumer marketplace for investment products.

Q12: Do you agree with our proposal to build from our TCFD-aligned disclosure rules in the first instance, evolving the disclosure requirements over time in line with the development of future ISSB standards?

IIGCC agrees with this approach, but we emphasise the need to ensure that investors can navigate the transition from TCFD disclosures to reporting against the ISSB standards once finalised. We also need clarity on how disclosures under ISSB relate to the wider sustainability disclosures that will

⁷ IIGCC response to FCA DP21/4, available [here](#).

need to be made under SDR. To this end, we urge the FCA to work with government departments to set out how the adoption of ISSB disclosures would be incorporated under the SDR regime, to address the risk of duplicative reporting requirements and support the flow of consistent, decision-useful information across the investment chain.

We reiterate the points we have made on sequencing in our response to the DP and elsewhere in this response. The proposed application dates for the SDR requirements go some way in addressing the concerns we highlighted in our DP response, namely that SDRs were being developed before the UK's economy-wide TCFD regime has had time to properly bed in. Nevertheless, we would still encourage the FCA to consider how best to manage the transition from TCFD reporting to reporting against the broader SDR framework, and mitigate complexity and costs for firms.

Appropriate sequencing is essential to facilitate the flow of information across the investment chain, from corporates to asset managers and then to clients (e.g. asset owners) and consumers. The UK has committed to learning lessons from the sequencing challenges that have arisen in the EU by requiring SDR disclosures for corporates before investors are required to report under the regime. We still do not have clarity from the FCA and the Government as to when the requirements for corporates will be rolled out, nor when a UK Taxonomy will be implemented. IIGCC urges the FCA and Government to manage this process carefully and ensure investors have the information they need from their investees to meet their broader sustainability reporting obligations under SDR.

While the development of further standards on additional sustainability topics by ISSB will help to increase the availability and quality of sustainability-related information, the 'financial materiality' lens employed by both TCFD and ISSB must be complemented with a focus on double materiality. Without such a focus, there is a risk that sustainability reporting is excessively focused on the impacts of sustainability factors on the entity or investment product, and not the impact of the entity or investment product on the climate, environment, and society. This is particularly important in the context of the proposed labelling regime, which is grounded in a double materiality approach. As highlighted in our response to Q8, IIGCC urges the FCA to ensure SDR includes disclosures and metrics that will allow investors to assess, and then report on, the impact of their investments on the climate, and their alignment with a 1.5-degree pathway in line with the objectives of the Paris Agreement.

Q13: Do you agree with our proposals for consumer-facing disclosures, including location, scope, content and frequency of disclosure and updates? If not, what alternatives do you suggest and why?

While IIGCC does not usually engage on retail and consumer-focused issues, we broadly agree with the proposals. We reiterate the points set out in our response to Q12 on enabling access to more detailed information where consumers wish to engage with it.

We also support the FCA's expectation that firms must use language that will be familiar and comprehensible to consumers while effectively and accurately describing the strategy in plain English. However, there is an educational dimension to consider here as well. Consumers may find it difficult to access terminology such as 'stewardship', but it's important that such critical terms are communicated effectively to a wider audience, especially given its role as a lever for encouraging companies to transition. This is also relevant in the context of 'unexpected investments'. IIGCC fully agrees that it is important to articulate why an 'unexpected investment' may be held in a portfolio,

but again, it's critical to ensure that disclosures are able to educate and inform consumers as to why that might be the case. For example, a carbon-intensive holding in a sustainable portfolio may appear 'unexpected', but if it has a credible plan to align its business model and strategy with net zero and it is essential for that industry to transition along with the wider economy, then such a holding could represent a considerable opportunity for outsize impact on real world emissions. Ensuring consumers are informed about such nuances, in simple and concise language, will help to increase understanding around the importance of real-world emissions reductions and the need to accelerate the transition of the real economy. In turn, this could increase capital flows towards funds that will have the greatest real-world impact and help to close the financing gap for net zero and wider sustainability objectives.

Q14: Do you agree with the proposal that we should not mandate use of a template at this stage, but that industry may develop one if useful? If not, what alternative do you suggest and why?

IIGCC agrees that the FCA's proposals strike the right balance between ensuring a core baseline of decision-useful information is required to be disclosed, while not stifling innovation by taking an overly prescriptive approach. This should help the UK disclosure regime to avoid some of the challenges we have seen in the context of the highly prescriptive templates established under the EU's SFDR, which have proven confusing for consumers to navigate. We agree that an industry-led approach to developing templates would work best at this stage, which could later form the basis of a standardised template developed by the regulator once consensus has been achieved as to the most decision-useful and accessible formats for disclosing sustainability-related information.

Q15: Do you agree with our proposals for pre-contractual disclosures? If not, what alternatives do you suggest and why. Please comment specifically on the scope, format, location, content and frequency of disclosure and updates.

IIGCC agrees with the FCA's proposals for pre-contractual disclosures. While we support the decision not to include requirements that mirror the SFDR's DNSH approach at present, it will be important for investors to disclose on the impacts of investments on the climate and wider sustainability factors, and how these impacts are mitigated over time (in keeping with the double materiality lens). We recommend that the FCA considers how DNSH criteria can be introduced into the UK disclosure framework, noting the usability issues that have created implementation barriers in the EU and ensuring that these issues are not replicated in the UK regime. The work being undertaken by the UK Green Technical Advisory Group to review and potentially streamline the DNSH criteria for the UK Taxonomy should be considered in the context of the proposed SDR and investment labels.

Q16: Do you agree with our proposals for ongoing sustainability-related performance disclosures in the sustainability product report? If not, what alternative do you suggest and why? In your response, please comment on our proposed scope, location, format, content and frequency of disclosure updates.

IIGCC broadly agrees with the proposals, but notes that the draft Handbook text would prevent a firm from disclosing metrics where there are gaps in underlying data or methodological challenges that cannot be addressed by using proxy data or assumptions. IIGCC's view is that while it is critical to avoid misleading metric disclosures, such gaps are likely to be transitional in nature (particularly if sequencing of disclosures is appropriate). They are also likely to be more pronounced for certain asset

classes, although the investment industry continues to make progress in refining methodologies for metrics across a range of sectors and asset classes that should help to address this over time.

Given the urgency of the climate crisis and the need to accelerate momentum on sustainability reporting more broadly, we would prefer the FCA to take a more pragmatic approach that doesn't 'throw the baby out with the bathwater'. Investors should be permitted to apply their own judgement as to whether they are able to report metrics, alongside disclosure of any gaps in the underlying data, and how the firm has addressed/ seeks to address these gaps. We propose that investors should report these metrics 'as far as they are able', while also being transparent as to where gaps and challenges are arising, and the actions being taken to address them. The FCA could add guidance on how firms can explain these gaps, for example by reporting how much of the product/portfolio is covered by reported, estimated, and verified data, and how much is missing. This is similar to the 'data quality' metric established under the Department for Work and Pensions' (DWP) TCFD regime. Such an approach has the benefit of ensuring that metrics disclosures can be made to the extent possible while also providing clients with transparency on transitional data challenges. Moreover, it will provide clients with actual data, rather than proxy data and assumptions, which can be subjective in nature and lack comparability.

Q17: Do you agree with our proposals for an 'on demand' regime, including the types of products that would be subject to this regime? If not, what alternative do you suggest and why?

IIGCC agrees with the proposals.

Q18: Do you agree with our proposals for sustainability entity report disclosures? If not, what alternatives do you suggest and why? In your response, please comment on our proposed scope, location, format, content, frequency of disclosures and updates.

IIGCC agrees with the proposals for entity-level disclosures and supports the consistency with the four TCFD pillars. As highlighted in previous responses, it will be important to consider sequencing with, and transition to, the wider SDR regime here, as investors will need relevant information from corporates to report on their own entity-level oversight and management of sustainability-related risks and opportunities.

Where firms are seeking to align their products with net zero, IIGCC recommends that they consider making appropriate entity-level commitments to accompany the product-level approach. This could include becoming a signatory to two of the investor net zero alliances under Race to Zero and GFANZ led by IIGCC and other investor networks globally. For asset owners this would be the Paris Aligned Asset Owners, and for asset managers the Net Zero Asset Managers Commitment.⁸ Together, these alliances contain over 350 investors globally that have committed to net zero.

As highlighted above, IIGCC has developed a NZST which sets out several recommendations and actions for aligning entity-level stewardship policies and activities with net zero commitments made by investors that apply to their portfolios. IIGCC would welcome the opportunity to discuss how NZIF and the NZST could be incorporated into entity-level disclosures.

⁸ Paris Aligned Asset Owner Commitment, available [here](#). NZAM Commitment, available [here](#).

Q19: Do you agree with how our proposals reflect the ISSB’s standards, including referencing UK-adopted IFRS S1 in our Handbook Guidance once finalised? If not, please explain why?

IIGCC supports the decision to reflect the ISSB’s standards in the proposals, which will help to promote international interoperability, a vital consideration for institutional investors given their global horizons. However, we expressed a number of concerns in relation to the draft climate-related disclosures under development by the ISSB, which we would like to see addressed before we can fully endorse the standards. Please refer to our consultation response for more information, which includes a high-level summary of the key issues identified by IIGCC and our proposed recommendations.⁹

Q20: Do you agree with our proposed general ‘anti-greenwashing’ rule? If not, what alternative do you suggest and why?

IIGCC is supportive of the rationale underpinning the FCA’s ‘anti-greenwashing’ rule, but given the breadth of its scope, it is not entirely clear how it will operate in practice, and how the FCA will carry out enforcement action under it. For example, what would constitute disproportionate or exaggerated naming and marketing of an investment product? We strongly recommend that the FCA provides more detail on the nature of this rule and publishes accompanying guidance and examples alongside it to help investors with their navigation of the proposed requirement in practice. For example, it would be helpful to provide clarity on how the proposed rule relates to the principles established in the FCA’s July 2021 ‘Dear Chair’ [letter](#), and whether the rule is intended to formalise and consolidate the letter’s principles.

While we acknowledge the principles-based approach the FCA is seeking to take, it will be important to ensure the anti-greenwashing avoids unintended and undesirable consequences, particularly in the absence of a ‘Responsible’ investment label. For example, there is a risk that the anti-greenwashing rule limits the scope for a broad range of funds to discuss their approaches to ESG integration or engagement, even though such approaches are increasingly seen as a ‘baseline’ form of risk management by the industry. Given that the labelling regime is intended to operate on a voluntary basis, we encourage the regulator to avoid an overly-restrictive approach that limits the ability to discuss ESG integration or engagement unless it relates to a labelled fund. We note this is not the FCA’s intention, and that funds would not be prohibited from disclosing their approach to ESG integration in a proportionate way. Nevertheless, it is important to clarify what this means in practice. See our response to Q7 for more information.

Q21: Do you agree with our proposed product naming rule and prohibited terms we have identified? If not, what alternative do you suggest and why?

IIGCC broadly agrees with the proposed product naming rule and prohibited terms identified. Given that these proposals are aimed at retail investors, we do not propose to comment in detail. However, we note that sustainability-related terminology continues to evolve rapidly, so the FCA will need to ensure it is able to accommodate for this consideration in the final rules.

Q22: Do you agree with the proposed marketing rule? If not, what alternative do you suggest and why?

⁹ IIGCC response to the International Sustainability Standards Board’s Exposure Draft IFRS S2 (Climate Exposure Draft), available [here](#).

See our response above.

Q23: Are there additional approaches to marketing not covered by our proposals that could lead to greenwashing if unaddressed?

IIGCC emphasises the need to ensure that the FCA’s regime is as interoperable as possible with the proliferation of mandatory and voluntary sustainability disclosure regimes emerging internationally. This has led to a fragmented reporting landscape, creating substantial challenges for investors with global investment horizons, who seek consistent approaches to sustainability disclosures that can facilitate cross-border investment and enable meaningful comparison between holdings.

In this context, we welcome the FCA’s efforts to map the proposals against SFDR requirements and SEC proposals. IIGCC suggests that the FCA should continue to build on and adapt this guidance as disclosure and labelling regimes evolve, while recognising that there are nuances that will need to be accounted for (e.g. SFDR operating solely as a disclosure regime). We also strongly advocate for close collaboration with other global regulators, policymakers, and standard setters to uphold internationally coherent approaches to sustainability disclosures to the extent possible. For more information, see IIGCC’s Investor Expectations of Corporate Sustainability Disclosures for Policymakers, which sets out key recommendations for disclosure regimes that are designed to support investors’ sustainability information needs, regardless of the jurisdiction in which they operate.¹⁰

Q25: What are your views on how labels should be applied to pension products? What would be an appropriate threshold for the overarching product to qualify for a label and why? How should we treat changes in the composition of the product over time?

IIGCC stresses the need to uphold consistency between the application of the regime for UK-domiciled funds, overseas funds, and pension products. In relation to pension products specifically, building on existing DWP climate disclosure requirements for occupational pension schemes would be helpful in this regard, alongside clarity as to when these firms will be brought into scope of the SDR framework.

Q27: Are there challenges or practical considerations that we should take into account in developing a coherent regime for pension products, irrespective of whether they are offered by providers subject to our or DWP’s requirements?

As noted above, to support the coherency of the overarching SDR framework for pensions, IIGCC urges the FCA and Government to elaborate on how the proposed roll-out of SDR will impact/apply to trustees of occupational pension schemes, as well as pension product providers. The sustainability-related labelling and disclosure requirements are intended to help meet institutional clients’ information needs, but there does not seem to be a complementary regime in train for how these clients identify and manage their own sustainability-related risks and opportunities. This is particularly important in the context of any streamlining and integration of existing economy-wide TCFD disclosures under the broader SDR regime.

¹⁰ IIGCC Expectations of Policymakers on Corporate Sustainability Disclosures, available [here](#).

While we note the FCA’s intention to consider the interaction between labels and disclosures by firms in scope of the proposed rules, and disclosures by firms in scope of DWP requirements, we need clarity on how this will happen in practice. Alongside other asset owners, pension schemes sit at the top of the investment chain, and their ability to meet any sustainability-related disclosure obligations they are subject to will depend heavily on information provided to them by their asset managers. It is therefore vital that a consistent approach is adopted between the FCA’s proposed requirements and any regime that pension schemes will need to adhere to (as well as ensuring these requirements are appropriately sequenced). This will help to ensure that SDR can inform trustees’ decision-making and capital allocation processes.

The Government’s Greening Finance Roadmap¹¹ appeared to confirm that trustees of occupational pension schemes would be in scope of the wider SDR regime. IIGCC would support this component of SDR being legislated for by DWP, consistent with the TCFD roadmap, and overseen/enforced by The Pensions Regulator. To avoid unnecessary duplication and costs, we suggest FCA-authorized occupational pension schemes are carved out of the scope of the FCA’s regime.

Overall, IIGCC feels that the FCA could provide more clarity on, and recognition of, the breadth and nuances across the range of pension products in existence, and how they will interact with the proposed regime. While the proposals clarify that the FCA will consider the interaction between its own label and disclosure regulations, and those to be taken forward by other regulatory bodies, it is unclear how these would work in practice, especially to avoid inefficient duplication of costs and requirements.

Q30: What other considerations or practical challenges should we take into account when expanding the labelling and disclosures regime to pension products?

See IIGCC’s response to Q27.

¹¹ Greening Finance: A Roadmap to Sustainable Investing, p.39, available [here](#).