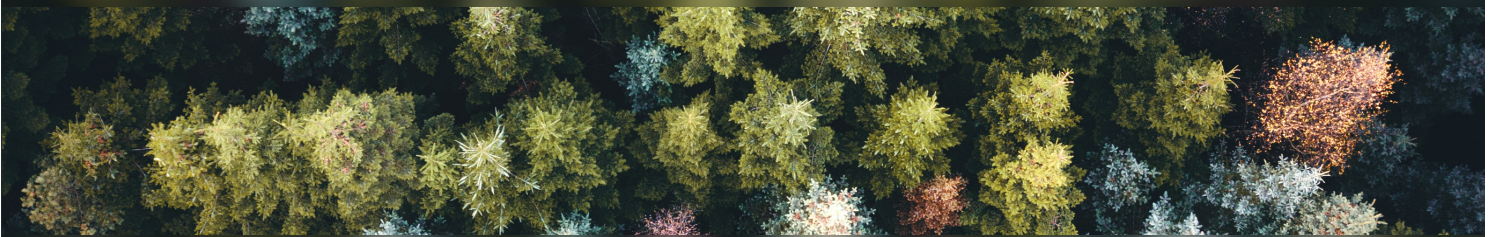


C L I F F O R D

C H A N C E



**THE UK'S SUSTAINABILITY DISCLOSURE
REQUIREMENTS REGIME**

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THE UK'S SUSTAINABILITY DISCLOSURE REQUIREMENTS REGIME

Speed read...

In November 2023, the UK's Financial Conduct Authority (FCA) published the [final rules](#) for its new Sustainability Disclosure Requirements regime (SDR). Firms are now preparing to comply with the regime, which will be phased in from 31 May 2024. Here are our key takeaways:

- The SDR is a package of measures. It has five key elements:
 1. An **anti-greenwashing rule**, requiring firms to ensure that references to the sustainability characteristics of products or services in client communications and financial promotions are: (i) consistent with the sustainability characteristics of the product or service; and (ii) fair, clear and not misleading.
 2. The introduction of **four sustainability labels**, designed to help consumers to navigate the market for sustainable investment products. Firms within the scope of the regime will be able to use the labels for their products on a voluntary basis. If a product does use a label, it must satisfy certain qualifying criteria set by the FCA.
 3. **Restrictions on the use of sustainability-related terms in the name and marketing materials** of certain products for retail clients. For these products, sustainability-related terms may only be used if: (i) the product also uses one of the four voluntary sustainability labels; or (ii) certain criteria are satisfied, which include the production of sustainability-related disclosures.
 4. The introduction of four types of **sustainability-related disclosures**: (i) consumer-facing disclosures; (ii) pre-contractual product-level disclosures; (iii) periodic product-level disclosures; and (iv) entity-level disclosures.
 5. **Requirements for distributors** to communicate labels (where used) and provide consumer-facing disclosures to retail investors. Distributors must also include a notice on overseas products to state that those products are not subject to the SDR.
- The application of the regime varies depending on the nature of the firm. The anti-greenwashing rule will apply to all FCA- and PRA-authorized firms. The remaining elements of the regime will apply, broadly, to UK AIFMs and UK UCITS managers in respect of UK AIFs and UK UCITS.
- The regime will be phased in, starting with the anti-greenwashing rule on 31 May 2024. Firms will be able to use the labels (with associated disclosures) from 31 July 2024 and the remaining requirements will be phased in from December 2024 to December 2026.
- Future developments are likely. The FCA has confirmed that it will consult in early 2024 on the introduction of a tailored version of the regime for portfolio managers. The FCA has also stated that it intends to build on its sustainability disclosure requirements over time.

In more detail...

Why has the SDR been introduced?

The SDR has been introduced to help consumers to navigate sustainability-related information and products and to help to prevent greenwashing. Although similar to the EU's Sustainable Finance Disclosure Regulation (SFDR) in that both require sustainability disclosures, the SDR is a broader package of measures that also includes an anti-greenwashing rule, product labels, naming and marketing requirements and requirements for distributors.

To which firms and products will the SDR apply?

One of the more complex aspects of the regime is its application, which varies depending on the specific measure in question.

The anti-greenwashing rule will apply to all FCA- and PRA-authorized firms when they: (i) communicate with a UK client in relation to a product or service; or (ii) when they communicate a financial promotion to a person in the UK.

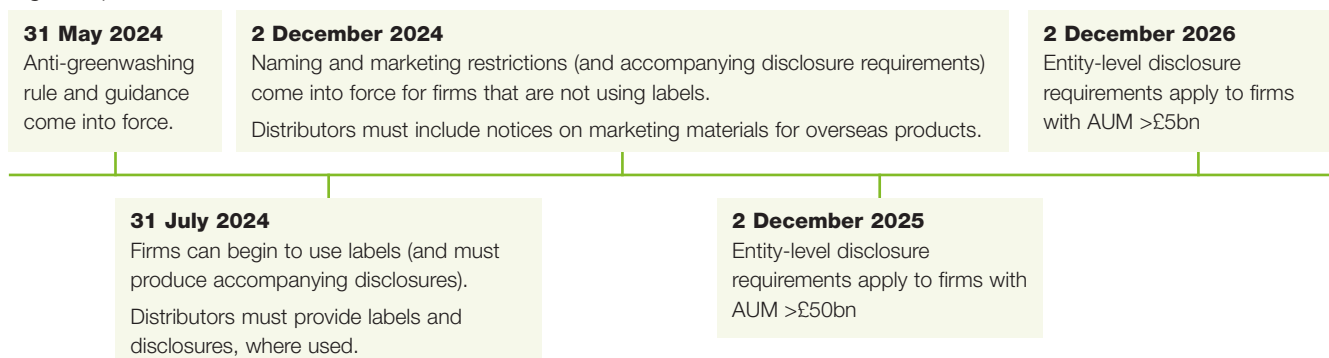
The four sustainability labels, restrictions on the use of sustainability-related terms in products' names and marketing materials and the sustainability-disclosure requirements will apply only to UK UCITS management companies when managing a UK UCITS and full-scope and small authorised UK AIFMs when managing UK AIFs. Importantly:

- these aspects of the regime do not apply in respect of non-UK products (although it would be possible for HM Treasury to consult on expanding the regime to cover non-UK products in the future).
- while the FCA originally intended to apply some of these aspects to firms carrying on portfolio management, it has decided not to do so at this stage. The FCA will instead issue a further consultation paper in H1 2024 on creating tailored requirements for portfolio managers.

Finally, the requirements for distributors will apply to FCA- and PRA-authorized distributors when distributing certain products to retail clients.

When will the rules begin to apply?

The FCA has opted to phase in requirements, commencing with the anti-greenwashing rule on 31 May 2024. The following diagram provides a high-level summary of the regime's phase-in:



What are the key elements of the regime?

1. The anti-greenwashing rule

The new anti-greenwashing rule will require firms to ensure that references to the sustainability characteristics of products or services in client communications and financial promotions are: (i) consistent with the sustainability characteristics of the product or service; and (ii) fair, clear and not misleading.

The FCA has issued a consultation on proposed guidance that will sit underneath the anti-greenwashing rule. The draft guidance contains principles with which firms' communications should comply and examples of how the rules and principles should be applied in practice. The finalised guidance is expected to be published before the anti-greenwashing rule comes into force on 31 May 2024.

2. Product labels

The SDR will introduce four voluntary product labels:

Sustainability Impact	Sustainability Focus	Sustainability Improvers	Sustainability mixed goals
For products that invest in assets that are environmentally or socially sustainable, determined by a robust, evidence-based standard of sustainability.	For products that invest in assets that have the potential to become more sustainable over time, determined by their potential to meet a robust, evidence-based standard of sustainability over time.	For products that aim to achieve a predefined, positive, measurable environmental or social impact.	For products that aim to invest in assets that meet or have the potential to meet a robust, evidence-based standard for sustainability and/or invest with an aim to achieve positive impact.

If a firm would like to use a label for a particular product, the product must meet relevant qualifying criteria. These include a requirement for the product to have a sustainability objective that aligns with the relevant label and a requirement for at least 70% of the product's assets to be invested in accordance with that sustainability objective.

3. Naming and marketing restrictions

The SDR will prohibit asset managers that conduct in-scope business for retail clients from using certain sustainability-related terms in the name or marketing materials of the relevant product. Terms that will be prohibited include 'ESG', 'environment', 'social', 'impact', 'responsible' and 'sustainable'.

Firms will only be allowed to use these terms in the product's name or marketing materials if: (i) the firm uses one of the four sustainability labels for the product; or (ii) the firm satisfies certain criteria, including producing sustainability disclosures under the SDR for that product.

4. Disclosure requirements

The SDR will introduce four disclosure requirements:

- **Consumer-facing disclosures:** These will be mandatory for products that use a label or that use sustainability-related terms without a label. They should be clear summaries of the key sustainability features of a product, targeted towards retail investors, and no more than two A4 sides in length. They will be provided when the product is offered.
- **Pre-contractual product-level disclosures:** These will be mandatory for products that use a label or that use sustainability-related terms without a label. They will provide more detailed pre-contractual sustainability information than the consumer-facing disclosure.
- **Ongoing product-level disclosures:** These will be annual disclosures for products that use a label or that use sustainability-related terms without a label. They will provide updates on the progress of the product towards meeting its sustainability objective. They will be publicly-available or, where this is not appropriate, provided to eligible clients on demand.
- **Entity-level disclosures:** These will be mandatory for all asset managers with AUM above £5 billion, irrespective of whether they use product labels or sustainability terms. These disclosures will provide information on how the firm manages sustainability-related risks and opportunities at an entity-level.

The FCA has not created templates for these disclosures (although has left it open to the industry to do so).

5. Requirements for distributors

The SDR will require distributors to:

- communicate labels and consumer-facing disclosures to retail investors;
- ensure the labels and disclosures are kept up-to-date; and
- provide a notice on overseas products to clarify that those products are not subject to the SDR.

How does the SDR relate to other sustainability disclosure regimes?

The SDR sits in an increasingly complex and multi-layered environment of sustainability disclosures both within the UK and internationally. A point of focus for the FCA has been interoperability between the SDR and SFDR. The FCA has produced a map to indicate how features of the SDR map to features of the SFDR. Of particular interest are the FCA's comments regarding the relationship between Articles 8 and 9 of the SFDR and the product labels under the SDR – the FCA indicates that it would be possible for Article 8 or 9 products to use any of the four SDR labels, although Article 8 products would need to 'level up' to qualify for the labels.

Within the UK, the SDR's sustainability disclosure requirements will build on requirements that the FCA has already introduced for asset managers to produce Task Force on Climate-Related Financial Disclosures (TCFD) -aligned disclosures.

What are the next steps?

Firms will need to conduct an initial scoping exercise to determine which entities and products are within scope of the SDR. Care will need to be taken to ensure that this is sufficiently granular, as different elements of the regime have different scopes of application. Firms will then be in a position to move into their implementation phase, preparing to comply with the anti-greenwashing rule, determining whether to use labels, and ensuring that naming, marketing and disclosure requirements will be complied with as applicable.

Firms will also need to monitor for further developments in the regime, including the publication of the FCA's finalised anti-greenwashing guidance and potential extensions of the regime for portfolio managers and non-UK funds.

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