



LATHAM & WATKINS

6 December 2023

Financial Regulation Monthly Breakfast Seminar

Overview



The information, documents (electronic, printed or otherwise) and other materials provided to support this presentation are for general information and training purposes only. The aforementioned, or any other information provided in support of this presentation are not intended to constitute legal advice and should not be relied on or treated as a substitute for legal advice from an appropriately qualified lawyer. While we have made every effort to ensure the accuracy of the information contained in this presentation, we do not accept any responsibility for any reliance on information, documents and materials used in this presentation. This presentation does not establish an attorney-client relationship between you and our firm. All materials used in this presentation, unless otherwise stated, are copyright works of Latham & Watkins. Please see our website for further information regarding our regulatory disclosures.



LATHAM & WATKINS

ESG Update
Nicola Higgs and Nell Perks

PS23/16: Sustainability Disclosure Requirements (SDR)

28 November 2023: FCA published final rules on its Sustainability Disclosure Requirements (SDR) and investment labelling regime

The FCA is introducing the following key measures:

1. An **anti-greenwashing rule** for all UK authorised firms to make sure sustainability-related claims are fair, clear and not misleading
2. An **investment labelling regime** for UK asset managers, comprising four investment labels that may be used for products seeking to achieve positive sustainability criteria
3. New rules and guidance for UK asset managers marketing investment funds on the basis of their sustainability characteristics, but which do not use a label

PS23/16: Sustainability Disclosure Requirements (SDR)

Anti-greenwashing rule

- Applies to all UK-authorized firms who make sustainability-related claims about their products and services
- Comes into force: 31 May 2024
- Applies to all communications about financial products/services which refer to the environmental and/or social characteristics of those products/services
- Includes: statements, assertions, strategies, targets, policies, information, images

PS23/16: Sustainability Disclosure Requirements (SDR)

Anti-greenwashing rule

A firm must ensure that any reference to the sustainability characteristics of a product or service is:

- (a) consistent with the sustainability characteristics of the product or service; and
- (b) fair, clear and not misleading.

- Guidance – to provide clarity on expectations
- Interaction with naming and marketing rules – forms the foundation
- Implementation – extended, allowing for consultation on the guidance

PS23/16: Sustainability Disclosure Requirements (SDR)

Consultation: Guidance on the Anti-Greenwashing rule - GC23/3

Sustainability references should be:

Correct and capable of being substantiated

- No exaggeration/overstatement
- Supported by robust and credible evidence

Clear and presented in a way that can be understood

- Technical terms should be explained
- Overall impression is relevant – visual presentation
- Interaction with Consumer Duty

Complete – should not omit/hide important information; should consider full life cycle of product/service

- Conditions/caveats to be clearly and prominently stated
- Balanced presentation
- Consider whole life cycle of product/service

Fair and meaningful in relation to any comparisons to other products/services

- Enable audience to make informed decisions
- Evidence to substantiate comparative claims

PS23/16: Sustainability Disclosure Requirements (SDR)

Consultation: Guidance on the Anti-Greenwashing rule - GC23/3

Questions:

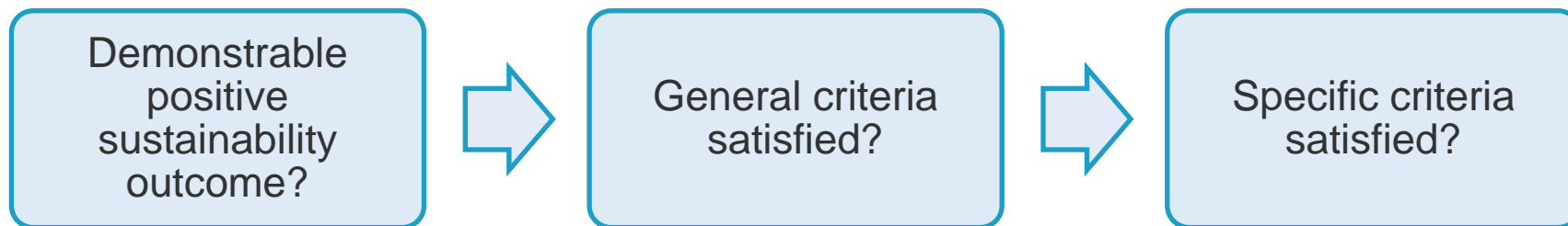
1. Does the proposed guidance clarify the anti-greenwashing rule? If not, what more could we do to provide clarity?
2. Do you have any comments on the proposed guidance including the examples given?
3. Do you agree that the guidance should come into force on 31 May 2024?

Responses due: 26 January 2024

PS23/16: Sustainability Disclosure Requirements (SDR)

Investment labelling regime

- In order to use one of the four labels, a product must meet both general and specific criteria relating to that label on an ongoing basis
- FCA emphasises that the labels have not been designed as a hierarchy; rather, they reflect different investment objectives and approaches
- FCA has now set a percentage (70%) across all labels for the minimum proportion of assets that must be invested in accordance with the sustainability objective for the product to qualify



Investment strategies such as exclusions, negative screening, ESG integration or basic ESG tilts alone are not enough to qualify for a label

PS23/16: Sustainability Disclosure Requirements (SDR)

General criteria

1. **Sustainability objective.** All products using a label must have a sustainability objective to improve or pursue positive environmental and/or social outcomes as part of their investment objectives
2. **Investment policy and strategy.** At least 70% of the product's assets must be invested in accordance with its sustainability objective. These assets must be chosen with reference to a robust, evidence-based standard that is an absolute measure of environmental and/or social sustainability
3. **KPIs.** Asset managers must use KPIs to measure progress against the sustainability objective. These can measure the progress of the whole product or individual assets

PS23/16: Sustainability Disclosure Requirements (SDR)

General criteria (cont.)

4. **Resources and governance.** Asset managers must ensure there are appropriate resources, governance, and organisational arrangements to support delivery of the sustainability objective
5. **Stewardship.** Asset managers must identify and disclose the stewardship strategy needed to support the delivery of the sustainability objective, including activities they expect to take and outcomes they expect to achieve

PS23/16: Sustainability Disclosure Requirements (SDR)

Specific criteria

Sustainability Labels

1. Focus

- 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

2. Improvers

- 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 sustainability
- Asset managers will need to identify the period of time by which the product and/or its assets are expected to meet the standard, including short and medium-term targets. They must also obtain robust evidence to satisfy themselves that the assets have the potential to meet the standard
- Asset managers should note that stewardship should support delivery of the sustainability objective

PS23/16: Sustainability Disclosure Requirements (SDR)

Specific criteria (cont.)

Sustainability Labels

3. Impact

- 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, determined by the potential of those assets to meet a robust, evidence-based standard that is an absolute measure of sustainability
- Asset managers must specify a theory of change setting out how they expect their investment activities and the product's assets to achieve a positive impact
- Asset managers must specify a robust method for measuring and demonstrating the positive impact of both the assets the product invests in and the asset manager's investment activities

4. Mixed Goals

- Products with a sustainability objective to invest in accordance with a combination of the sustainability objectives for the other labels
- Asset managers must identify (and disclose) the proportion of assets invested in accordance with any combination of the other labels

PS23/16: Sustainability Disclosure Requirements (SDR)

Naming and Marketing Rules

- UK asset managers that make products available to retail investors which:
 - do not use one of the four sustainability investment labels, but
 - use sustainability-related terms
- Can still use sustainability-related terms (such as “green”, “climate”, “social”) in product names and marketing if they meet the FCA’s product name, disclosure, and statement conditions:
 - The product must have sustainability characteristics and the product’s name must accurately reflect those characteristics
 - The sustainability characteristics of a product should be material to that product, meaning, for example, that at least 70% of its assets have sustainability characteristics

PS23/16: Sustainability Disclosure Requirements (SDR)

Naming and Marketing Rules (cont.)

- The terms “sustainable”, “sustainability”, “impact” and any variation of those terms must not be used
- Asset managers must produce the same types of disclosures as required for a labelled product (consumer-facing, pre-contractual, and ongoing product-level disclosures)
- Asset managers must also produce and prominently publish a statement to clarify that the product does not have a label and the reasons why

PS23/16: Sustainability Disclosure Requirements (SDR)

Disclosures

Consumer-facing disclosures	Detailed product-level disclosures	Entity-level disclosures
<p>Scope: Products using a label and products using sustainability-related terms in their naming and marketing.</p>		<p>Scope: UK asset managers with AUM above £5 billion (regardless of whether they use labels or sustainability-related terms)</p>
<p>Format: Standalone document. No more than 2 pages long. No set FCA template (anticipated industry led standard form).</p> <p>Presented in a prominent place on the product webpage, app or other digital medium, alongside other key investor information.</p>	<p>Format:</p> <ol style="list-style-type: none"> 1. Pre-contractual 2. Ongoing 	<p>Format: Disclose the relevant information annually in a “Sustainability Entity Report”, which builds from the TCFD Entity Report.</p> <p>Managers that use labels or sustainability-related terms in their naming and marketing must also include details of their resources, governance, and organisational arrangements in relation to those products.</p>
<p>When: Label: from the date the label is first used. No Label: By 2 December 2024</p>	<p>When: Pre-contractual - Label: from the date the label is first used. No Label: By 2 December 2024. Ongoing - (i) published 12 months after the label is first used and annually thereafter; and (ii) provided to eligible clients on demand from 2 December 2025.</p>	<p>When: Asset managers with AUM above £50 billion from 2 December 2025. Asset managers with AUM above £5 billion from 2 December 2026.</p>

FCA Findings on Review of Green Funds

16 November 2023:

- FCA reviewed authorised fund managers' (AFMs') compliance with existing regulatory requirements, including the Guiding Principles set out in the Dear Chair letter issued in July 2021 and the Consumer Duty
- The FCA expects boards to take the lead in monitoring this area and ensuring AFMs make any required changes

FCA Findings on Review of Green Funds (cont.)

- FCA has issued guidance on:
 - **Design** – When using ESG / sustainability terms in fund names – consider whether there is an *explicit* ESG objective (rather than ESG outcomes reflected in the investment policy / strategy)
 - Identify clear examples of progress resulting from AFMs' engagement with investee companies
 - Embed stewardship activity within investment teams, having active engagement policies, and recording outcomes of stewardship activities

FCA Findings on Review of Green Funds (cont.)

- FCA has issued guidance on (cont.):
 - **Delivery** – Be prepared to explain instances in which fund holdings appear inconsistent with a fund’s ESG or sustainability objectives:
 - Maintain a credible, defined, and documented approach to the treatment of holdings that appear inconsistent with a fund’s objectives
 - Embed a strong focus on due diligence for asset selection, carrying out appropriate due diligence on third party data providers, and maintaining appropriate systems and controls to assess the ongoing appropriateness of ESG data

FCA Findings on Review of Green Funds (cont.)

- FCA has issued guidance on (cont.):
 - **Disclosure** – Key ESG and sustainability information was often not explained or put into context in disclosures. For example, some AFMs did not explain that they excluded Scope 3 emissions from their disclosures. The FCA reiterates that it expects AFMs to explain any material data limitations or considerations in fund disclosures:
 - Firm-level disclosures were not easily reconcilable with fund-level disclosures
 - Be mindful of using supplementary ESG reports and cross-referring when considering accessibility to investors
 - Test how investors understand information about the fund

FCA Findings on Review of Green Funds (cont.)

- FCA has issued guidance on (cont.):
 - **Governance** – Strategies and intent must be matched with appropriate oversight and control frameworks, including:
 - Maintaining a strong product governance structure
 - Monitoring adherence to funds' investment objectives and policy
 - Appropriately monitoring relevant management information
 - Ensuring that suitable investment policies and processes are embedded within the AFM

TPT's Sectoral Guidance for Climate Transition Plans

October 2023: Publication of the UK TPT framework

November 2023: The TPT has now published, for consultation, **draft guidance for the financial sectors** (in addition to certain non-financial sectors):

- Banks
- Asset owners
- Asset managers

The Guidance is open for consultation until 29 Dec 2023. With final guidance due in February 2024.



LATHAM & WATKINS

HM Treasury's amendments to the financial
promotion exemptions
Jonathan Ritson-Candler

Refresher on the Review

- HM Treasury consulted on changes to the financial promotions exemptions for high net worth individuals (“**HNWIs**”) and self-certified sophisticated investors (“**SCSIs**”) in December 2021
- FCA had previously called for these exemptions to be reviewed in light of:
 - The fact they were last updated in 2005. Since then, there has been considerable social, economic and technological change; and
 - Their ongoing misuse by bad actors to promote high-risk investments to vulnerable retail customers, particularly via online scams
- Consultation closed March 2022
- HM Treasury published its consultation response in November 2023

Outcome of the Review

- Draft Statutory Instrument, The Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) (No. 2) Order 2023, due to enter into force on 31 January 2024 and makes the following changes to the HNWI and SCSi exemptions
- These exemptions are applicable to financial promotions relating to **unlisted** companies

Type of change	Current position	Position from 31 Jan 2024
Increasing financial thresholds for HNWI exemption	<ul style="list-style-type: none">• Income of at least £100,000 in the last financial year• Net assets of at least £250,000 throughout the last financial (excluding primary residence or pension)	<ul style="list-style-type: none">• To reflect inflation:<ul style="list-style-type: none">• Increased to income of £170,000 in the last financial year• Net assets of at least £430,000 throughout the last financial year (excluding primary residence or pension)

Outcome of the Review (cont.)

Type of change	Current position	Position from 31 Jan 2024
Amending the criteria for SCSIs	<ul style="list-style-type: none"> One of the four criteria to be classified as a SCSi is to have made more than one investment in an unlisted company in the previous 2 years Another criterion is to have been a director of a company with an annual turnover of at least £1m 	<ul style="list-style-type: none"> Now much easier to invest in unlisted companies No longer an indicator of sophistication Criterion removed To reflect inflation: <ul style="list-style-type: none"> Have been a director of a company with an annual turnover of at least £1.6m
Businesses to provide information about themselves in any communications made using exemptions	<ul style="list-style-type: none"> N/A 	<ul style="list-style-type: none"> Businesses must now provide: <ul style="list-style-type: none"> Full name of the person making the communication Postal / electronic address The jurisdiction of incorporation Company registration number

Outcome of the Review (cont.)

Type of change	Current position	Position from 31 Jan 2024
Updating HNWI and SCSi investor statements	<ul style="list-style-type: none">• Concern is that the current format of the statements means some investors do not understand or engage with the information presented to them, including the statement that they need to sign• Meaning some investors may incorrectly certify themselves and/or not understand regulatory protections lost	<ul style="list-style-type: none">• Updating format: conditions for certification moved from bottom to top of statement + clearer that promotions will not follow FCA rules or have FSCS or FOS protections• Simplifying the language: statements remove cross references to legislation and provide a more consumer-friendly explanation of which assets are out of scope for the net assets calculation• Requiring greater investor engagement: investors are required to select specific criteria that qualify them as either HNWI or SCSIs. For example, they must declare income / net assets to the nearest £10,000 / £100,000 respectively

Proposals not taken forward

- HM Treasury has decided not to take forward the proposal in the CP that would have placed a greater degree of responsibility on firms seeking to rely on the HNWI and SCSi exemptions to ensure that individuals meet the relevant criteria
- Proposal was that firms must have a “reasonable belief” that the individuals meet the criteria, beyond signing the relevant investor statement



LATHAM & WATKINS

An update on the Edinburgh Reforms
Nicola Higgs

UK Retail Disclosure Framework: Consumer Composite Investments (CCI)

November 2023:

1. HM Treasury published Policy Note on UK Retail Disclosure Framework = “a fundamental overhaul of the UK’s retail disclosure framework”
2. HM Treasury has published a near final SI: Consumer Composite Investments (Designated Activities) Regulations 2024:
 - Introduces new designated activities into FSMA (section 71K)
 - Manufacturing a UK retail CCI
 - Advising on a UK retail CCI
 - Offering a UK retail CCI

UK Retail Disclosure Framework: Consumer Composite Investments (CCI) (cont.)

- Firms engaged in any of these activities, regardless of their authorisation status, will be in scope of FCA rules in respect of retail disclosure
- Maintains the transition period for funds currently providing the UCITS KIID (31 December 2026)
- HM Treasury welcomes technical comments on the draft SI by **10 January 2024**
- FCA will follow with detailed rule-making on the content of retail disclosures:
 - Replaces the UK PRIIPs KID Regulation (and certain MiFID II costs & charges rules)

Latest on Edinburgh timings

- UK Listing Regime: FCA consultation expected by the end of 2023, with final rules due late H1 2024
- UK Prospectus Regime: legislation to be made by the end of 2023, with the FCA to consult on its rules in summer 2024
- Intermittent Trading Venue: this will be delivered through the FMI Sandbox powers, and will be up and running by the end of 2024
- Investment research: Consultation expected Q1 2024, with final rules made in H1 2024
- Wholesale Markets Review: FCA Policy Statement on the consolidated tape for bonds, and Consultation Paper on the transparency regime for bonds and derivatives, due by the end of 2023

Latest on Edinburgh timings (cont.)

- Securitisation: main legislation to be made by the end of 2023, with PRA/FCA rules expected to take effect Q2/Q3 2024
- SMCR Review: Consultation on potential improvements and reforms expected Q2 2024
- Ring-Fencing: Legislation to implement short-term reforms expected to be made Q1 2024; policy response on the long-term future of the regime expected H2 2024
- Bank capital requirements: consultations on repeal and replacement of CRR expected in 2024, with rules to be finalised H1 2025 and implemented H1 2026

Latest on Edinburgh timings (cont.)

- Consumer credit: Detailed second-stage consultation expected H2 2024
- UK funds regime: Consultations on reforming the regime expected in 2024
- Advice/guidance boundary review: Policy paper due by the end of 2023
- Insurance Distribution Directive: FCA's final rules for moving remaining legislative provisions into the Handbook expected December 2024, and expected to take effect end March 2024

Other updates from the Regulatory Initiatives Grid

- HM Treasury has ended its review of the Overseas Persons Exclusion
- New section added to show timings for review and repeal of Retained EU Legislation, but no timings or priorities set out for Tranche 3 as yet



LATHAM & WATKINS

The FCA's final report on IFPR implementation
observations
Rob Moulton

Background

- FCA interested in investment firm failures
 - Market impact
 - Complex administrations
 - Take up FCA's supervisory time
- February 2023 “observations on IFPR”
 - ICARA process harmonised
 - Focus on wind-down planning
 - New November 2023 multi-firm review feedback (“no change to existing policy”)

Liquid Asset requirements

- MiFIDPRU 7 requires a “reasonable estimate of the amount of liquid assets” for ongoing operations in “severe but plausible” stresses
- Severity and breadth of stresses often inadequate
- Not regularly reviewed and updated (since February?)
- Use intra-day funding needs, even if positions are flat daily
- Understand difference between liquid assets and own funds

Early Warning Indicators

- Early Warning Indicator now required (FCA notification)
- Need to include assets to support wind-down in the EWI calculation
- Use stress testing to help to calculate this buffer
- Note interaction with Threshold Conditions

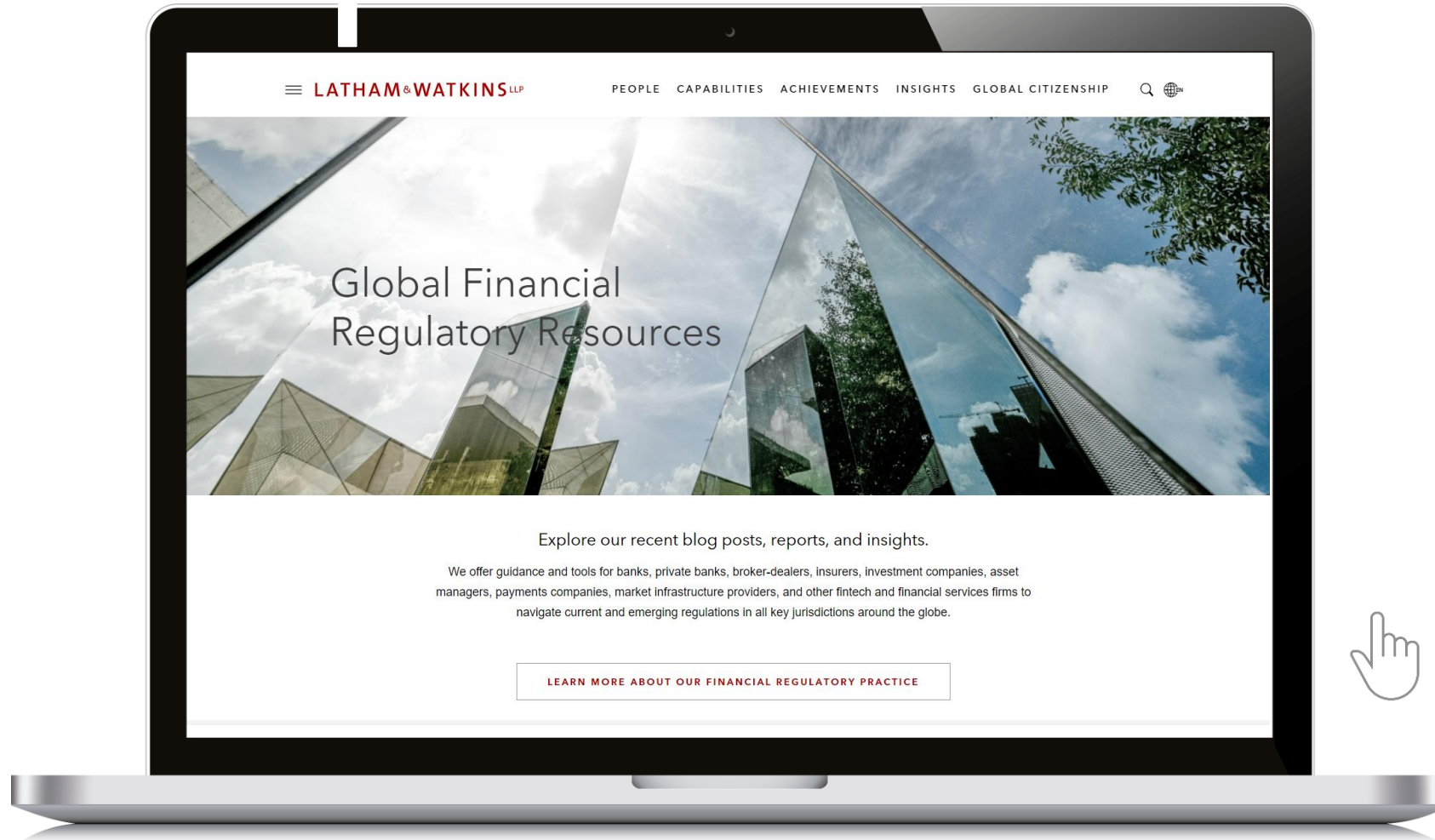
Wind-Down Plans

- Impact of group membership – governance, risk appetite, availability of resources (e.g. people)
- Inter-relationship between entity-level ICARA with group-wide resolution planning

Operational Risk

- Firms should identify OpRisk and build it into scenario analysis and stress considerations
- Subject matter experts were asked to assess once in a lifetime (40 year) scenarios
- Mathematical models were used to extrapolate to less frequent scenarios (200+ years)

Our Global Financial Regulatory Resources Page



Click to Access
Latham's Global
Financial Regulatory
Resources

Recent Thought Leadership



Monthly London Webcast Materials

Each month the UK and European Financial Regulatory lawyers at Latham & Watkins host a presentation and discussion covering recent changes to financial services regulation.

[VIEW](#)



- [FCA Publishes Final Rules on Sustainability Disclosures and Investment Labelling](#)
- [FCA Finds Further Improvement Needed on Design, Delivery, and Disclosure of ESG Funds](#)
- [HM Treasury Confirms Changes to Financial Promotion Exemptions](#)
- [EU Revamps Consumer Credit Rules](#)