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FCA PUBLISHES CP22/20 ON SUSTAINABILITY DISCLOSURE REQUIREMENTS AND INVESTMENT LABELS: RAISING THE BAR TO BUILD TRUST

As envisaged in the Government's roadmap to greening finance and following its discussion paper DP 21/4 published late last year, the FCA has now published its long-awaited consultation on sustainability disclosure requirements and investment labels for investment products (CP22/20). With the exponential growth in investment products marketed as having ESG characteristics, the FCA has been concerned with greenwashing for some time and the impact this could have on shifting capital to investments which genuinely support transition. As evidenced in the publication of its Guiding Principles for the design, delivery and distribution of ESG funds, the FCA has been clear that any sustainability-related claims must be substantiated. In the FCA's own words, it is deliberately seeking to set a "high bar for quality and integrity" when developing the proposed regime. In this briefing, we provide an overview of the proposals and discuss some of the issues arising from the requirements.

Overview

The consultation seeks to introduce a comprehensive regime covering sustainable investment labels with corresponding eligibility criteria; consumer facing as well as product and entity-level disclosures; naming and marketing rules; and rules for distributors. At the heart of the FCA's proposals is a consumer-focused labelling regime for investment products that seeks to help consumers (the FCA's term for retail investors) navigate the increasingly complex landscape of sustainable investments and to protect them from greenwashing harms. To this end, the FCA is proposing a labelling system based on three categories (see summary box alongside) underpinned by a stringent and objective qualifying criteria. Strict rules restricting the use of certain terms by asset managers when naming or marketing products that do not qualify for, or use, the proposed labels would also apply.

The FCA is also proposing the introduction of consumer-facing product disclosures, supplemented by a more detailed entity and product-level disclosure regime that builds on existing requirements for asset managers and asset owners to make TCFD-aligned disclosures. As an indication of its seriousness of intent in clamping down on greenwashing more generally, one somewhat unexpected development is the proposed introduction of a general "anti-greenwashing" rule that applies to all

Summary of the proposals

- ***sustainable investment labels*** *- to help consumers navigate the investment product landscape and enhance consumer trust. There will be three categories: (i) 'sustainable focus' - for products investing in assets that are environmentally or socially sustainable; (ii) 'sustainable improvers' - for products investing in assets to improve environmental or social sustainability over time, including in response to the stewardship influence of the firm; and (iii) 'sustainable impact' - for products investing in solutions to environmental or social problems to achieve positive, measurable real-world impacts.*
- ***a general 'anti-greenwashing' rule*** *- applying to all regulated firms requiring that sustainability-related claims in relation to a product or service must be consistent with the sustainability profile of that product or service and clear, fair and not misleading.*
- ***naming and marketing rules*** *- restricting the use of certain sustainability-related terms in product names and marketing materials where products do not qualify for the sustainable investment labels.*
- ***consumer-facing disclosures*** *- to help consumers understand the key sustainability-related features of a product.*
- ***detailed disclosures targeted at a wider audience*** *- comprising: (i) pre-contractual disclosures, covering the sustainability-related features of investment products; (ii) ongoing sustainability-related performance information, including key sustainability-related performance indicators and metrics, in a sustainability product report; and (iii) a sustainability entity report covering how firms are managing sustainability-related risks and opportunities.*
- ***requirements for distributors*** *- to ensure that product-level information (including the labels) is made available to consumers.*

regulated firms, not just asset managers of in-scope investment products.

A few initial comments on the overall regime: The FCA is unashamedly consumer-focussed. Although it is very aware that the rules need to be sufficiently practicable for firms to implement, it is clear that "*the needs of consumers have been central to [their] policy design*". To this end, it has commissioned behavioural research to inform its policy design, the findings of which are set out in Occasional Paper OP62. The concern is that greenwashing may erode the integrity of, and trust in, the market for such products, particularly among retail investors, possibly slowing the flow of capital into sustainable investments - something that is much needed if the Government's stated ambition to become a leading centre for sustainable finance and its net zero target are to be met. The FCA is also clear that these proposals simply represent a starting point - and expects the regime to evolve and expand over time, particularly given the market for sustainable investment itself is still evolving rapidly.

Scope

Most of the detailed proposals apply to investment products (funds), primarily those marketed to UK retail investors, with obligations being placed on the managers, and separately distributors, of in-scope products. Some rules apply only to products which use the proposed sustainable labels; others to all in-scope products. However, the general anti-greenwashing rule applies to all regulated firms and their products and services.

Who do the proposals apply to?

- *portfolio managers (see below on application of proposed rules to portfolio management services)*
- *UK UCITS management companies*
- *full-scope UK AIFMs*
- *small authorised UK AIFMs*

What products are in scope?

- *An authorised fund (including an ICVC, authorised unit trust or authorised contractual scheme)*
- *An unauthorised Alternative Investment Fund (AIF) (any non-UCITS fund which are not authorised funds, including investment trusts) managed by a UK AIFM*
- *Portfolio management agreements or arrangements (only some aspects of the regime apply)*

Pension products (personal pension schemes, stakeholder pension schemes or SIPPs) and IBIPs (insurance-based investment products) are, for the moment, outside scope, although the intention is to bring them within scope in due course.

Timeline

The FCA intends to publish its policy statement and finalise its rules by the **first half of 2023 (provisionally by 30 June 2023)**. The general anti-greenwashing rule will come into force immediately on publication of the final rules, while the labelling regime and naming and marketing rules will apply 12 months later. The disclosure requirements will be implemented in phased stages. Appendix 2 sets out the FCA's provisional timeline for the implementation of the proposals.

Labelling

The FCA is introducing a classification and labelling regime which allows firms offering in-scope investment products to use the FCA's "sustainable investment" labels for their products if they meet the proposed qualifying criteria. The approach taken is based on intentionality" - that is, in relation to that product, there must be a deliberate intention to achieve the product's stated objective. In the FCA's view, only products that have a sustainability objective and contribute to a positive sustainability outcome should qualify to use the proposed sustainable investment labels. As stated in the consultation, "*one of the key attributes of a sustainable investment product is an explicit environmental and/or social objective that is part of the investment objective…*" Simply considering the financial risks, opportunities and impact of ESG factors in investment decisions should be seen as merely part of an asset manager's existing fiduciary duty to clients and part of its usual risk management practice. This will be insufficient, in and of itself, to make a particular product qualify for one of the proposed labels.

Following feedback on the more complex scheme set out in DP21/4, a simpler scheme comprising three labels has been proposed: (i) "**Sustainable focus**", (ii) "**Sustainable improvers**" and (iii) "**Sustainable impact**". A description of the features of each category is set out in Appendix 1 (Part A).

The "responsible" category contemplated in DP21/4 has been removed entirely on the basis it is potentially confusing, while the "not promoted as sustainable" category was thought to unduly convey too negative a perception on products that do not qualify for any of the labels (but which may nonetheless contain certain sustainable-related features that may be of interest to investors).

The labels are meant to be mutually exclusive and *not* hierarchical. In other words, they do not serve to inform consumers the degree to which a particular product is "sustainable" (that is, the application of a "Sustainable focus" label does not mean that the product is somehow more "sustainable" than a product applying a "Sustainable improvers" label). Rather, they are completely separate categories meant to help investors distinguish one product from the other.

Qualifying criteria

To qualify for one of the three sustainable labels, the product must meet criteria comprising five overarching principles (general criteria), a number of key 'cross-cutting' considerations and category-specific considerations that sit underneath each Principle (specific criteria). The FCA has also developed implementing guidance to supplement the criteria.

- **Principles (general criteria)**: This covers: sustainability objective, investment policy and strategy, Key Performance Indicators (KPIs), resources and governance, and investor stewardship.

Principle 1	*A sustainable investment product must have an explicit environment and/or social sustainability objective.*
Principle 2	*A firm's investment policy and strategy for the sustainable investment product must be aligned with its sustainability objective.*
Principle 3	*A firm must specify credible, rigorous and evidence-based KPIs that measure a sustainable investment product's ongoing performance towards achieving its sustainability objective.*
Principle 4	*A firm must apply and maintain appropriate resources, governance and organisational arrangements commensurate with the delivery of the sustainable investment product's sustainability objective.*
Principle 5	*A firm must maintain its investor stewardship strategy and resources (at firm-level or product-level) in a manner consistent with the sustainable investment product's sustainability investment objective.*

- **Key considerations**: These set out what "firms must do" (in relation to any sustainable investment product) to demonstrate adherence to the relevant principle. For example, in relation to Principle 1, the key considerations require, among other things, that firms determine the sustainability objective "in clear, specific and measurable terms as part of its investment objectives".
- **Category-specific criteria**: This refers to the more granular sustainability-related criteria that the product must satisfy in relation to each principle in order to qualify for a particular label. Again by way of illustration, in relation to Principle 1, to qualify as a "Sustainable impact" product, the category-specific criteria requires that the objective must be "to achieve a pre-defined, positive, measurable real-word environmental and/or social outcome". The category-specific criteria for each label is set out in Appendix 1 (Part B).

Some points to note with respect to the FCA's proposals on labelling. The FCA is clear that firms must ensure that the criteria have been met in full when determining whether it can apply a label to any product and must continue to be met *on an ongoing basis*. The proposed rules will not allow the use of the relevant label if the qualifying criteria for each of the categories are not, and do not continue to be, met. With respect to the provision of services relating to portfolio management, 90% of the total value of products invested under the agreement or arrangement must meet the criteria for the relevant label before that label can be applied. However, in its current form, the rules do not require independent verification of a firm's application of a label although firms are encouraged to voluntarily seek verification if they consider it helpful to their end-users.

Disclosure requirements

Disclosure requirements will focus on ensuring retail investors have accessible information on the sustainability-related features of the product (in new consumer-facing disclosures) and on the provision of more detailed entity and product-level disclosures particularly to institutional investors but also to retail investors who are interested in knowing more. The FCA is proposing:

- **Consumer-facing disclosures** - which will take the form of a new *standalone* document providing a summary of key sustainability-related features of a product. This requirement applies to all in-scope products (including those that are not engaged in any sustainability-related strategies), and not just those that apply a label. Firms providing portfolio management services are not required to produce their own consumer-facing disclosure. Instead, they must provide an index of the underlying funds in which it invests, including links to the underlying funds' consumer-facing disclosure, as applicable.
- **Detailed disclosures** - required in pre-contractual disclosures (i.e., the prospectus, information memorandum or KIID) and in periodic reports, which builds on FCA's existing TCFD –aligned climate-related disclosure requirements (requiring firms to produce a TCFD entity report and TCFD product reports - see our previous client briefing):

  At the product level, firms must make pre-contractual disclosures associated with the qualifying criteria with respect to their products that apply a sustainable investment label. For those products which do not qualify but nonetheless adopt some sustainability-related features that are integral to the product's investment policy and strategy, firms must still make disclosures that are proportionate to the sustainability profile of the product.

  In addition, firms must produce a **sustainability product report** for products that qualify for a sustainable investment label. Where the product does not otherwise have a prospectus or other prior information document, the pre-contractual information required may be included in this report

("Part A" of the report). The report must also contain disclosures on the sustainability-related performance of the product and the progress towards meeting its stated objective on an ongoing basis ("Part B" of the report). Part B of the report must be updated on an annual basis. The FCA recognises that public disclosure may be inappropriate for certain client relationships (for example, where UK AIFMs manage unlisted UK AIFs). As with the existing TCFD rules, the FCA is, in those circumstances, proposing that firms make the relevant disclosures *on client request* once a year ("on-demand reporting").

At the entity-level, in-scope asset managers will be required to produce an annual **sustainability entity report**. Implementation will be phased so that larger firms (assets under management (AUM) above £50 billion) will need to make such disclosures (provisionally) by 30 June 2025, with smaller firms (excluding those with AUM below £5 billion) to follow a year later. A member of senior management must confirm in the report that the disclosures comply with the requirements of the ESG Sourcebook.

These disclosures are aimed at enabling clients and consumers to understand the firm's approach to sustainability-related risks and opportunities. Again, this is intended to build on the existing TCFD entity report, and the content will be based on the same TCFD framework and its four disclosure pillars (governance, strategy, risk management and metrics and targets) to be extended so that disclosures cover all sustainability-related matters, and not just climate-related matters. Acknowledging that sustainability covers a whole range of topics, the FCA is not being prescriptive on content requirements and is offering firms some flexibility in taking different approaches for some of the matters and to prioritise the management of different sustainability-related risks and opportunities, depending on the profile of the assets they manage.

There are, of course, a myriad of existing disclosure requirements that already apply to asset managers and their relevant products (not least FCA's existing TCFD-aligned disclosure requirements). Firms will undoubtedly be interested in how the proposals interact, or fit with, existing disclosure requirements.

As the detailed disclosure requirements will build on existing TCFD requirements, the FCA is allowing the sustainability product report and sustainability entity report either to incorporate the climate-related disclosures required under the existing rules or include a link to the relevant information contained in the relevant TCFD report(s). Acknowledging the compliance burden on firms, the FCA is also proposing to retain as much flexibility as possible in allowing cross-references to relevant disclosures included elsewhere (including a third party's sustainability product report or, in relation to the entity report, to disclosures made in a group, affiliate or third party's sustainability report). Such cross-referenced disclosures must be "clear and easily navigable" and there must be clear signposting to where the other disclosures can be found.

While the attempt to reduce the reporting burden for firms is laudable, there is always the risk that, notwithstanding requirements for clear signposting and "easily navigable" cross-references, cross-referencing to other documents would lead to disclosures that are less accessible and harder to understand, with the potential for some of the clarity and context in which the disclosures are made to be lost. For retail investors in particular, it is likely that the consumer-facing document would do the 'heavy-lifting' in ensuring that investors have a good understanding of the sustainability-related features of the particular product.

International coherence and inter-operability

The FCA is very aware that many firms would already have to comply with other sustainability-related disclosure regimes, including the EU SFDR and US SEC proposals. The FCA has therefore tried to take into account developments in other jurisdictions, with the stated aim of trying to maintain coherence with international regimes. In particular, as the UK is likely to adopt the ISSB standards, the FCA's proposals assume those standards will form the basis for entity-level disclosures – with the draft rules already referring to IFRS S1 as being relevant in determining the content of the sustainability entity report. The FCA also considers that SASB standards may be used for disclosures relating to relevant sector-specific matters.

While the FCA is keen to ensure, as far as possible, inter-operability between the different regimes, the SFDR and SEC proposals take a very different approach as their starting point. The FCA's proposals are designed from the start as a labelling regime, whereas both the SFDR and SEC proposals are disclosure regimes which categorise products in order to determine disclosure requirements.

At the entity-level, by taking the proposed ISSB standards and TCFD framework as its basis, the FCA acknowledges that entity-level disclosure requirements under its proposals will not fully align with EU SFDR or SEC requirements. In particular, the FCA will not require disclosure of "principal adverse impacts" in contrast to the SFDR.

At the product level, as the FCA's proposals are designed as a labelling regime, the disclosure requirements are tied to the criteria that firms must meet in relation to a product in order to ensure the product qualifies for the use of a particular label. As noted above, the SFDR is a disclosure-only regime and firms effectively "self-classify" their products *in order to* determine what disclosures are required. Putting aside this fundamental difference, the main differences between the SFDR product-level disclosures and FCA's proposals include the following:

- SFDR has mandated the use of templates for many disclosures, which is not the case (at least at this stage) for the FCA's disclosure requirements.

- The FCA proposals require much more granular information relating to investment policy and strategy.
- The FCA has decided not to include disclosures relating to "do no significant harm" concept or principal adverse impacts. Taxonomy-alignment will be considered once the UK Green Taxonomy is developed.
- As noted above, separate standalone consumer-facing disclosures are required under the FCA proposals for in-scope products. There is no equivalent under the EU SFDR.

Naming and marketing

In order for the labelling to be effective as a means to ensure consumers can easily navigate the sustainable investment product landscape, the FCA is proposing additional regulatory intervention to tackle potential consumer harms arising from the "over-eager" marketing of products as sustainable. The intervention comprises two elements:

- Firstly, the introduction of a general "anti-greenwashing" rule requiring all FCA-regulated firms to ensure that any reference to the sustainability characteristics of a financial product or service is: (i) consistent with the sustainability profile of the product or service; and (ii) clear, fair and not misleading. Existing FCA conduct rules already require any client communication be clear, fair and not misleading, but the explicit link between sustainability claims and conduct rules would enable the FCA to more easily challenge any greenwashing practices.
- Secondly, firms are prohibited from using sustainability-related terms (such as "ESG", "environmental", "social", "climate", "impact", or "sustainable") in the naming and marketing of in-scope products made available to retail investors if those products do not qualify for and use one of the proposed sustainable labels. Products offered to institutional investors are not within scope of this rule. This is potentially very restrictive and may well require firms to review their existing retail product range to consider whether they qualify for the relevant labels. If not, they may need to re-name or drop the use of certain names for non-qualifying products.

Many products may not qualify for the labels but nonetheless still employ certain sustainability-related strategies. The prohibition does not restrict the use of such terminology in pre-contractual disclosures or consumer-facing disclosures where the terms are being used (in relation to such products) to disclose *factual information* in a manner proportionate to the profile of the product. Nonetheless, it will be interesting to see where the parameters of what constitutes "marketing" in the FCA's eyes lie for purposes of this rule.

It is also interesting to note that the naming and marketing of investment products has recently been the focus of other regulators as well. ESMA requested, earlier this year, EU Member States to investigate fund names to see if firms are including terms such as "sustainable" or "impact" without basis. The SEC is also proposing to expand the scope of its rules on fund names which, if adopted, will require funds with names that suggest a focus on investments with "particular characteristics" (such as an "ESG" fund) to meet certain thresholds in respect of its investment allocation. While some firms have already objected to the SEC proposals as placing undue weight on a fund name, regulators clearly take the view that a fund's name is influential in the consumer decision making process. Given the regulatory trajectory, we should see a more judicious use of "ESG" or other sustainable-related terms in product names.

Distributors

Distributors will be required to prominently display on a relevant digital medium (for example, product webpage or page on an app) the sustainable investment label for any in-scope products offered to retail investors which have such a label, as well as provide access to the accompanying consumer-facing disclosures. The distributor cannot use a sustainable investment label for a product other than the label that has been assigned by the firm. Where products do not use a label, the distributor will be required to provide retail investors with access to the consumer-facing disclosure. These proposals are consistent with existing requirements relating to distribution of financial products in the FCA's PROD Sourcebook and under the new Consumer Duty.

What next?

Pension products and IBIPs: The FCA intends to bring pension products and other IBIPs offered to retail investors within the regime so that consumers have greater transparency on sustainability-related matters with respect to both their direct investments and their savings.

Transition plans: The Government's high-level Taskforce on transition plans is intending to publish initial outputs relating to its development of a transition plan framework and guidance in the fourth quarter of 2022. Any outputs from the Taskforce are expected to be used to develop any further disclosure expectations on regulated firms relating to transition plans.

Overseas funds: While the proposals apply to UK products only, the FCA is also actively considering how the proposals might apply to overseas products. A separate consultation on this will follow.

Taxonomy alignment: It is expected that product-level disclosure requirements will include relevant Taxonomy-related disclosures once the UK Green Taxonomy is developed. The disclosure requirements will also continue to evolve to take into account the development of further ISSB standards.

The FCA has deliberately set a high threshold criteria for products to qualify for the proposed sustainable labels. If properly implemented, the labels may be effective in serving as a "badge of approval" marking out "genuine" sustainable investment products. Whether or not the products manage to achieve real-world outcomes is, of course, uncertain, but the labels should at least enable consumers to clearly distinguish between different products, and form the basis on which consumers can determine and compare the sustainable performance of each product within each category. The FCA's proposed introduction of restrictions on the naming and marketing of so-called sustainable products is also far-reaching in effect. As a package, it is clear that the FCA is intent on cracking down on greenwashing and in building consumer trust in a market where un-substantiated and overstated claims are perhaps more prevalent. The FCA's hope is that this will lead to better informed consumer decisions and capital allocation, which ultimately can "help facilitate the transition to a more sustainable future".

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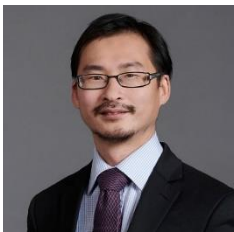

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Appendix 1

A. Summary of labelling regime

Label	Consumer-facing description	Distinguishing features	Channels to achieve sustainable outcomes
Sustainable Focus	Invests mainly in assets that are sustainable for people and/or planet	Products with an objective to maintain a high standard of sustainability in the profile of assets by investing to (i) meet a credible standard of environmental and/or social sustainability; or (ii) align with a specified environmental and/ or social sustainability theme	**Primary channel:** This category of product would pursue its sustainability goals primarily via the market-led channel of influencing asset prices, and thereby reducing the relative cost of capital of sustainable economic activities/projects. **Secondary channel:** Products in this category will also typically pursue continuous improvements in the sustainability performance of assets through investor stewardship activities.
Sustainable Improvers	Invests in assets that may not be sustainable now, with an aim to improve their sustainability for people and/or planet over time	Products with an objective to deliver measurable improvements in the sustainability profile of assets over time. These products are invested in assets that, while not currently environmentally or socially sustainable, are selected for their potential to become more environmentally and/or socially sustainable over time, including in response to the stewardship influence of the firm	**Primary channel:** This category of product would pursue its sustainability goals primarily via the channel of investor stewardship. The product's stewardship approach would be directed towards encouraging and accelerating improvements in the environmental or social sustainability profile of its assets, including through participation in system-wide initiatives, with flow-on positive implications for environmental and/or social sustainability. **Secondary channel**: Portfolio construction and asset selection in 'sustainable improvers' products would be geared towards identifying those assets that are best-placed to improve their sustainability profile over time. So, a secondary channel would be the market-led channel of influencing asset prices and the relative cost of capital of more sustainable economic activities/ projects.
Sustainable Impact	Invests in solutions to problems affecting people or the planet to achieve real-world impact	Products with an explicit objective to achieve a positive, measurable contribution to sustainable outcomes. These are invested in assets that provide solutions to environmental or social problems, often in underserved markets or to address observed market failures	**Primary channel**: This category of product would pursue its sustainability goals by directing typically new capital to projects and activities that offer solutions to environmental or social problems, often in underserved markets or to address observed market failures. Products would be expected to have a stated theory of change, and to pursue a highly selective asset selection strategy aligned with that theory of change. **Secondary channel**: Driving continuous improvements in the sustainability performance of assets through investor stewardship activities would be a secondary channel.

B. Category-specific criteria

Note: The table below sets out the category-specific criteria **only**. Note there are **key considerations** under each of Principles 1 to 5 that apply across the three categories that must also be met before the relevant labels can be applied.

Label	Principle 1	Principle 2	Principle 3	Category-specific disclosures
Sustainable Focus	The sustainability objective must align with requirements in the 'investment policy and strategy' section ie to invest 'predominantly' (at least 70%) in assets that meet a credible standard* for environmental and/ or social sustainability; or that align with a specified environmental and/or social sustainability theme.	The firm must ensure that at least 70% of the product's assets either meet a credible standard of environmental and/ or social sustainability; or align with a specified environmental and/or social sustainability theme. If reasons for beyond the firms' control, the assets cease to meet the requirements above, the firm must take action to restore compliance as soon as reasonably practicable, having regard to the interests of the firm's investors (ie clients and consumers).	In specifying KPIs to assess performance of the product, a firm must ensure that those KPIs include metrics that demonstrate the ongoing alignment of the product's assets with a target environmental and/ or social sustainability profile, and the product's ongoing adherence to asset-level sustainability features in accordance with its investment policy and strategy.	**Product report:** The firm must disclose the KPIs specified in accordance with the requirements for this category. In relation to its stewardship strategy, the firm must disclose how that strategy has been applied to achieve continuous improvement in environmental and/or social sustainability of the product's assets; and the outcomes achieved.
Sustainable Improvers	The sustainability objective must align with requirements in the 'investment policy and strategy' section ie to invest in assets that have the potential to become more environmentally and/or socially sustainable over time, including in response to active investor stewardship.	The firm must ensure that the product is invested in assets that have the potential to become more environmentally and/or socially sustainable over time, including in response to active investor stewardship.	In specifying KPIs to assess performance of the product, a firm must ensure that those KPIs include metrics that demonstrate: • a clear and measurable target for improvements in the sustainability profile of the assets in which the product invests • the long-term sustainability profile of a product's assets, as projected over a period of more than one year • the extent to which improvements in the sustainability of a product's assets have been achieved over time, including through investor stewardship • how the firm's stewardship strategy has been applied to support improvements in the environmental and/or social sustainability of assets, in accordance with the sustainability objective • the stewardship activities undertaken in relation to improving the sustainability profile of the product's assets in accordance with its	**Pre contractual information:** The firm must describe (in relation to its asset-level selection criteria) how it assesses potentially investible assets to determine the extent to which improvements in sustainability can be achieved over time, including through investor stewardship. **Product report:** The firm must disclose details of the KPIs specified in accordance with the requirements for this category.

Label	Principle 1	Principle 2	Principle 3	Category-specific disclosures
			sustainability objective; the outcomes achieved (including any improvements in the sustainability profile of the product's assets over time); and matters escalated (in accordance with the expectations under Principle 5, Stewardship) • how the product's assets meet the asset-level selection criteria • the changes (if any) in the sustainability profile of the product's assets over time, distinguishing between any improvement or deterioration in the sustainability profile of individual assets and changes arising from asset rotation	
Sustainable Impact	The sustainability objective must be to achieve a predefined, positive, measurable real-world environmental and/or social outcome.	The firm must specify: • a theory of change, in line with the product's sustainability objective, emphasising how its investment process aims to contribute to addressing either environmental and/or social problems • a robust method to measure and demonstrate that its investment activities have had a positive environmental and/or social sustainability impact • its escalation plan should the real-world outcome no longer plausibly be achievable, including potential divestment of assets	In specifying KPIs to assess performance of the product, a firm must apply enhanced impact measurement and reporting based on industry best practices.	**Pre contractual information:** The firm must include the following information: • its theory of change, with clear examples that emphasise how its investment process aims to contribute to addressing environmental and/or social problems, in line with its sustainability objective • a robust method to measure and demonstrate that its investment activities have had a positive environmental and/or social sustainability impact • its escalation plan should the real-world outcome no longer plausibly be achievable, including potential divestment of assets • in relation to specifying its asset-level selection criteria, how it assesses potentially investible assets to determine: • whether those assets align with the product's theory of change, while also

Label	Principle 1	Principle 2	Principle 3	Category-specific disclosures
				avoiding unintended negative consequences; and • the extent to which a positive, measurable, environmental and/or social outcome can be achieved. **Product report**: The firm must disclose the KPIs specified in accordance with the requirements for this category, also including: • its analysis as to how its actions have contributed to the impact achieved; or • an explanation as to why its actions have not done so. The firm must also disclose details as to how its rights and influence (including through direct control as relevant) have been applied to pursue the pre-defined, positive, measurable real-world outcome specified in the product's sustainability objective, in line with its theory of change for the product.

Appendix 2

Provisional timeline for implementation