

ENHANCING CLIMATE-RELATED DISCLOSURES BY ASSET MANAGERS AND ASSET OWNERS

In November 2020 the Government published its roadmap towards mandatory climate-related disclosures across the UK economy by 2025. In January 2021 new Listing Rules requiring premium-listed companies to make climate-related disclosures in line with TCFD recommendations on a “comply or explain” basis started to apply. The FCA has now published a [consultation](#) on introducing climate-related disclosures for asset managers and asset owners, including life insurers, alongside a [consultation](#) on extending the Listing Rules disclosure requirements to standard-listed commercial companies. In this briefing we consider the proposed new requirements for asset managers and asset owners and how these fit in with the wider set of disclosure requirements at UK and international level.

Overview

The FCA’s proposed new requirements will apply to asset managers, life insurers and FCA-regulated pension providers. This includes SIPP operators but not trustees of defined benefit pension schemes, who will have separate disclosure obligations under regulations developed by the Department of Work and Pensions. An exemption will apply to asset managers and asset owners that have less than £5 billion in assets under management or administration (on a 3-year rolling average basis).

The proposals will apply in respect of (i) assets managed or administered by a firm; and/ or (ii) assets relating to particular financial products or services. There will be two separate disclosure requirements, as discussed further below. In either case, the disclosures are aimed at investors in the assets managed by the firm and at end-user customers. This is a different target audience from the Listing Rules disclosure requirements, which are aimed at existing and potential shareholders.

Compliance with the majority of the new disclosure requirements will be mandatory, unlike the Listing Rules requirements, which currently apply on a “comply or explain” basis.

Who do the proposals apply to?

The proposals will apply to three categories of firm:

Asset managers	Life insurers	Non-insurer FCA-regulated pension providers
<ul style="list-style-type: none"> • portfolio managers • UK UCITS management companies • full-scope UK AIFMs • small authorised UK AIFMs 	<ul style="list-style-type: none"> • life insurers offering insurance-based investment products • life insurers offering defined contribution pension products 	<ul style="list-style-type: none"> • platform firms • SIPP operators

The disclosure requirements

The new rules would require two sets of disclosures:

- an annual TCFD entity report on how the firm takes climate-related risks and opportunities into account in managing or administering investments on behalf of clients or consumers

- an annual set of consistent, comparable disclosures in respect of the firm’s products and portfolios, either in the form of a TCFD product report or disclosed on request to relevant institutional clients, depending on the nature of the business of the firm.

The FCA recognises that firms may have gaps in underlying data. The expectation is that these gaps will decrease over time as disclosure requirements increase across the financial sector. Where there are gaps firms can use proxy data or assumptions but must include an adequate explanation of this, including any methodologies used, in the report.

Timing

The FCA proposes a two stage approach to compliance with the new rules:

- from 1 January 2022: the rules will apply to asset managers with assets under management of more than £50 billion and asset owners with assets under management or administration in relation to in-scope business of more than £25 billion. Disclosures in relation to activities over the previous 12 months would need to be made by 30 June 2023, and then by 30 June in each calendar year thereafter
- from 1 January 2023: the rules will apply to all remaining firms within scope of the rules. Disclosures in relation to activities over the previous 12 months would need to be made by 30 June 2024, and then by 30 June in each calendar year thereafter.

Contents of the TCFD entity report

To allow for maximum flexibility, and recognising the number of different disclosure initiatives which may apply to firms, the FCA does not propose setting out detailed prescriptive disclosure requirements. Instead, disclosures must be consistent with the TCFD’s recommendations and recommended disclosures, including TCFD guidance and technical supplements. A senior manager will need to confirm in a statement in the TCFD entity report that the disclosures comply with relevant requirements.

Despite the principles-based approach, some specific requirements are proposed for entity level reports, including requirements to:

- explain how the firm’s TCFD strategy has influenced its process for delegating functions and relying on third party service providers and products
- explain the firm’s approach to climate-related scenario analysis, including the application of this analysis to investment and risk decision making processes (including quantitative examples where reasonably practicable)
- give details of any targets set by the firm to manage climate-related risks and opportunities, including the KPIs used to measure progress against targets, or explain why no targets have been set.

If a firm is a member of a group it can rely on cross-referencing and linking to climate-related disclosures made in other reports produced by the group when producing its TCFD entity report, provided the disclosures are relevant to the firm and cover the relevant assets. Many insurance and asset management groups already publish TCFD or other climate disclosure reports and are likely to use cross-referencing to these reports to comply with the new FCA requirements. They will need to ensure, however, that the reports provide the requisite level of granularity for each regulated firm within the group which is required to publish a TCFD entity report.

What is a TCFD product?

The FCA proposals define which products are in-scope of the new requirements.

For asset managers, relevant TCFD products are authorised funds, unauthorised Alternative Investment Funds (AIFs) and portfolio management services (broadly defined). Feeder funds and sub-funds in the process of winding up or termination are excluded. The FCA has stated its intention to bring into scope the “full range” of asset management activities. This is reflected in its proposals which would mean that authorised funds including UCITS, QIS NURS, and UK LTIFs, AIFs, as well as discretionary portfolio management services and private equity and private market activities, are all within scope.

For life insurers, relevant TCFD products are with-profits funds, linked funds or pre-set investment portfolios, in each case where they relate to an insurance-based investment product, personal pension scheme, stakeholder pension scheme or SIPP. Insurers are required to make disclosure at fund rather than product level as the insurance wrapper for an insurance-based investment product will usually allow a choice of funds and the climate-related disclosures will be different for each fund. Where underlying funds are managed by asset managers, the insurer can cross-refer to relevant

disclosures made by the asset manager. Where there is a pre-set investment portfolio associated with a product the product report should include disclosures in respect of that portfolio.

TCFD product reports

Requirements for TCFD product reports are slightly more granular. The report must include, for each relevant product:

- information on the following metrics:
 - scope 1 and 2 greenhouse gas emissions
 - scope 3 greenhouse gas emissions
 - total carbon emissions
 - total carbon footprint
 - weighted average carbon intensity
- contextual information on the metrics, including the use of proxy data
- information on the historical annual calculations of the metrics
- scenario analysis involving, at a minimum, a qualitative summary of how climate change is likely to impact the underlying assets under each of an “orderly transition”, “disorderly transition” and “hothouse world” scenario
- a discussion of the most significant drivers of impact on each product
- on a “best efforts” basis, climate “Value-at-Risk” metrics showing the climate warming scenario with which the product is aligned, and any other metrics which the firm considers will be useful to investors.

Where a product has “concentrated” or “high” exposures to carbon intensive sectors, the firm must also include a quantitative analysis of the “orderly transition”, “disorderly transition” and “hothouse world” scenario in respect of each relevant product. The FCA has chosen not to define what a “concentrated” or “high” exposure is, on the basis that this could unintentionally establish a category of products which is considered negatively by investors. Firms will therefore need to decide whether and when these additional requirements should apply.

The FCA acknowledges that many firms have not yet begun to build capabilities for quantitative climate-related scenario analysis and may have to depend on third party input. It does, however, see quantitative scenario analysis as an important part of the disclosure process. As well as potential practical difficulties, firms may be concerned about the uncertainties associated with scenario analysis and the risk that expected impacts on products turn out to be inaccurate.

On-demand product disclosures

For certain types of client, the FCA acknowledges that public disclosures are not appropriate and instead proposes a requirement for product or portfolio-level disclosures to be made available on request. This applies to discretionary portfolio management services and non-listed unauthorised AIFs.

Interaction with other UK disclosure requirements

A number of overlapping climate disclosure requirements have been introduced or are being proposed in the UK, all of which are likely to affect large asset managers and life insurers. The requirements are all based on the TCFD recommendations, which will hopefully streamline the compliance process. The specifics of each set of disclosure rules will, however, need to be checked, along with any rules around the format in which information should be presented. It is also important to be aware of the different audiences for different disclosures - Listing Rules disclosures, for example, are focused on enterprise risks and directed at shareholders, whereas the proposals in CP21/17 are focused on assets managed or administered by firms and are directed at clients and consumers.

Main existing and proposed UK disclosures relevant for asset managers and insurers:

- Listing Rules requirements for “comply or explain” TCFD disclosures in the annual report for premium-listed companies for financial periods beginning on or after 1 Jan 2021
- Proposed extension of the Listing Rules requirements to standard-listed companies for financial periods beginning on or after 1 Jan 2022

- FCA proposals for disclosures by asset managers and asset owners, as discussed in this briefing
- BEIS proposals for mandatory disclosure of climate-related financial information, to apply to a range of entities including large listed companies, large private companies and all insurance companies.

The BEIS proposals were set out in a [consultation paper](#) published in March. The proposals would apply to:

- all UK companies which are currently required under the Companies Act to produce a non-financial information statement. This applies to all companies with more than 500 employees which have transferable securities admitted to trading on a UK market, banking companies and insurance companies
- UK registered companies with securities admitted to AIM and more than 500 employees
- any other UK registered companies and LLPs with more than 500 employees and a turnover of more than £500 million.

The BEIS proposals would require mandatory disclosure by in-scope firms of climate-related financial information in line with the four overarching pillars of the TCFD recommendations. They would not require disclosure in accordance with all of the 11 more detailed TCFD recommendations, which sit below the four pillars. Disclosure in accordance with all of these 11 recommendations is required under the Listing Rules requirements, albeit on a comply or explain basis. BEIS considers this to be a proportionate approach as the more granular requirements would not be mandated, which also allows for future flexibility if international reporting standards are adopted.

Interaction with EU disclosure requirements

Groups which have EU subsidiaries may also have disclosure requirements under the Sustainable Finance Disclosure Regulation (Regulation EU 2019/2088) (the **SFDR**). The SFDR applies to financial market participants, including asset managers and insurers offering insurance-based investment products. Like the FCA's proposals for asset managers and asset owners, the SFDR requires climate-related disclosures at both entity and product level, although the SFDR is wider in scope and requires disclosures which encompass environmental, social and governance matters other than just climate change. In relation to climate-related disclosures, some of the details of the disclosure requirements differ from those proposed by the FCA and for groups operating in both the UK and the EU both will need to be taken into account. In addition, the FCA has proposed that where calculation methodologies for product disclosures differ between the TCFD recommendations and the SFDR, firms report according to the formulas under both regimes.

Climate change related disclosures and other sustainability issues are already high on the agenda for asset managers and insurers. The FCA's proposals are part of a wider backdrop of disclosure requirements at both the UK and international level. The number of different disclosure requirements being introduced does introduce an additional compliance burden for firms, and potentially some confusion, but there does seem at least to be the potential to use some of the same data in different contexts.

CONTACT



JONATHAN MARKS
PARTNER
T: +44 (0)20 7090 3056
E: jonathan.marks@slaughterandmay.com



PAUL DICKSON
PARTNER
T: +44 (0)20 7090 3424
E: paul.dickson@slaughterandmay.com



BETH DOBSON
PSL COUNSEL
T: +44 (0)20 7090 3070
E: beth.dobson@slaughterandmay.com



ALFRED KING
SENIOR PROFESSIONAL SUPPORT LAWYER
T: +44 (0)20 7090 3519
E: alfred.king@slaughterandmay.com

London
T +44 (0)20 7600 1200
F +44 (0)20 7090 5000

Brussels
T +32 (0)2 737 94 00
F +32 (0)2 737 94 01

Hong Kong
T +852 2521 0551
F +852 2845 2125

Beijing
T +86 10 5965 0600
F +86 10 5965 0650

Published to provide general information and not as legal advice. © Slaughter and May, 2021.
For further information, please speak to your usual Slaughter and May contact.

www.slaughterandmay.com

572757054