

# UK Greening Finance Roadmap

20 October 2021

The long-awaited successor to the 2019 UK Green Finance Strategy, the UK Greening Finance: A Roadmap to Sustainable Investing was published this week, just in time for COP26. The Roadmap is a blend of updates on existing workstreams with a few new features.

## The “UK SDR”

When UK Chancellor, Rishi Sunak, announced in his Mansion House speech this summer that the UK would introduce new “Sustainability Disclosure Requirements” – abbreviated to the “SDR” – it led some to believe the UK was planning to introduce its own version of the SFDR, the EU Sustainable Finance Disclosure Regulation.

In fact, the SDR is a combination of the next iteration of proposals under the TCFD-aligned roadmap which we discussed earlier this year, together with some new elements. This will comprise:

### Corporate disclosure:

The UK government was already contemplating introducing mandatory climate disclosure for a broad range of public and private companies and LLPs. The Roadmap confirms that new requirements aligned to the expected new international sustainability reporting standards will be introduced for certain UK-registered companies and financial services firms and certain UK-listed issuers. This will include obligations to report alignment of activities with the new UK Green Taxonomy (discussed below). The precise scope of entities has not been specified at this stage.

### Asset manager and asset owner disclosure:

Certain UK pension schemes will be required to disclose their sustainability-related risks, opportunities and impacts, which disclosures are aimed at helping savers to make clear choices. The new requirements could be combined with the TCFD-aligned requirements introduced this year, which we discussed in our series on sustainability and UK pension schemes.

Sustainability disclosure requirements will also be introduced for asset managers, life insurers providing investment products and FCA-regulated pension schemes (which were the subject of a recent FCA consultation on TCFD-aligned disclosures). This will include Taxonomy-alignment reporting requirements.

### Investment product disclosure:

Firms will be required to disclose the sustainability attributes of the investment products and portfolios they offer. The new requirements will include sustainability risks, opportunities and impact disclosure, a core set of product level climate metrics and Taxonomy-aligned disclosures. These appear to apply to all investment products regardless of whether they have an ESG badge.

Any provider making claims about the sustainability of its investment products will be required to substantiate the claims.

The new requirements will build on the expectations the FCA set out in its “Dear Chair” letter regarding ESG and sustainable investment funds earlier this year, and be the subject of further consultation.



One of the weaknesses of current approaches to sustainability reporting is the lack of consistency across sectors and even intra-sector. The SDR aims to address this by maintaining the same framework and metrics across the whole economy, based on the TCFD framework. HM Treasury (HMT) will play a coordinating role across sectors to make sure that information is made available across the investment chain.

The government has made it clear that it expects the new international sustainability reporting standards to be based on the same framework.

### **Broadening the focus beyond climate?**

Whilst the TCFD framework is, as the name suggests, based on climate risk, the government may go further than climate action in its new requirements. The UK has been a strong supporter of the development of an equivalent framework to TCFD for nature-related risk, and, despite the reference to “greening finance” in the title, the language of the Roadmap refers to “sustainability”, which captures a much wider range of objectives.

### **Mandatory transition plan reporting**

The UK plans to introduce mandatory disclosure of net zero transition plans. This will be phased in under the SDR framework for certain firms on a “comply or explain” basis initially, with more stringent requirements as standards for transition plans mature. This echoes the approach of the European Commission, with the proposed Corporate Sustainability Reporting Directive requiring organisations to report their sustainability targets and progress against them, and the possible new guidance on voluntary pledges to adopt strategic science-based climate and environmental targets, as mentioned in the Strategy for Financing the Transition to a Sustainable Economy.

## **UK Green Taxonomy**

**Post-Brexit, the UK onshored the main classification framework of the EU Taxonomy, which is based on six environmental objectives:**

- climate change mitigation;
- climate change adaptation;
- sustainable use and protection of water and marine resources;
- transition to a circular economy;
- pollution prevention and control; and
- protection and restoration of biodiversity and ecosystem.

**Like the EU Taxonomy, an activity under the UK Green Taxonomy must comply with the following four criteria:**

- substantially contributes to one or more environmental objectives;
- does not significantly harm (DNSH) any environmental objective;
- complies with minimum safeguards aligned with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights; and
- complies with the Technical Screening Criteria (TSC), which are the detailed conditions for the first two limbs above.



The EU TSC had not been finalised at the time of the UK's withdrawal from the EU, so the UK has been developing its own TSC.

The UK Taxonomy will also include transitional or enabling activities, which will be activities that support the transition by enabling substantial contributions to environmental objectives in other sectors but don't yet meet the green threshold. The Roadmap cites manufacture of components of wind turbines as an example.

The TSC for each objective will be "evidence-based, accessible and built for the UK market", subject to public consultation and implemented by statutory instruments. The TSC for the climate change objectives will be based on those currently subject to co-legislator scrutiny in the EU and are expected to be finalised by the end of next year. The TSC for the remaining objectives are expected to be tabled in Parliament in Q1 2023.

## New sustainable investment labelling

The FCA and the government will introduce a new sustainable investment labelling regime for investment products, which will apply to all products regardless of whether they are ESG-badged, with the aim of allowing consumers to "intuitively navigate" the sustainability characteristics of the products. The design of the labels will be determined following consultation with experts/advisors and following a discussion paper and consultation.

## Regulation of the ESG ratings market

ESG ratings and research play an important role in allowing market participants to assess companies' environmental social and governance performance and how they manage sustainability risks. A key feature of ESG ratings is the relatively high degree of divergence between ratings providers, lack of comparability and potential for gaps in the raw data.

The UK government is now considering bringing ESG data and ratings providers within its regulatory perimeter, with further detail to be announced in 2022.

## Digitisation of reported data

Digital solutions to the problem of access to consistent verified data has for a long time been a key hurdle in channelling capital towards sustainability goals at scale and managing sustainability risk. The European Commission plans to make publicly reported data under various EU regulations and directives more accessible via a common data platform, the European Single Access Point (ESAP).

The UK government and regulators are now also considering digital solutions to the data challenge, looking at possibilities that build on existing digital reporting infrastructure. This could include a central register for data. It will be interesting to see whether the UK plans to extend the principle of international alignment to such a register and make it interoperable with the ESAP.





## Stewardship

Stewardship is defined in the UK Stewardship Code 2020 as “the responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.” Given the importance of attenuating short termism to sustainability policy, stewardship and shareholder engagement play key roles in the transition to a sustainable economy.

The UK government and regulators have been focusing on strengthening stewardship since last decade, including the publication of the UK Stewardship Code 2020, the Asset Management Taskforce’s Stewardship Report and the Taskforce on Pension Scheme Voting and Implementation’s report on use of voting in the investment chain, and a number of FCA consultations on the topic. The Roadmap confirms that the FCA is considering further work to promote active investor stewardship that positively influences sustainability strategies.

The Roadmap also sets out its expectations that the pensions and investments sectors utilise the data generated by the SDR to strengthen its stewardship on sustainability issues. This may result in further policy intervention at a later date.

## Key contacts



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## Work on international alignment ahead of COP26

As we discussed in [our overview of COP26 and the Paris Agreement](#), one of the aims of landmark climate agreement is to make finance flows consistent with its “well below 2 degree/aiming for 1.5 degree” goals. The Roadmap notes that the UK government has been working with international partners to:

- introduce disclosure of climate impact, risks and opportunities. As we have noted previously, the G20 Finance Ministers and Central Bank Governors meeting communique from July supported promotion of the implementation of TCFD-aligned disclosures.
- ensure the financial system can measure and manage climate-related risk. This is expected to be discussed further at the G20 Rome Summit, which takes place immediately before COP26.
- measure how investment is aligned to the net zero transition by developing more “sophisticated, transparent and consumer-friendly metrics”.
- requiring credible net zero transition plans and regular progress reporting, with supervisory oversight.

Detail on these workstreams is thin in the Roadmap, but they could be a signal for what to expect at next month’s COP.

For more insights on COP26 and related development like the UK Green Financing Roadmap, see our [Countdown to COP & Beyond blog](#).

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