simmons+simmons

FCA proposals for climate-related disclosures by asset managers
Top 10 things that asset managers need to know

On 22 June 2021, the FCA published its long-awaited consultation paper, CP21/17 on climate-related disclosures by asset managers (the consultation).

The new disclosure obligations will be based on recommendations published by the Task Force on Climate-related Financial Disclosures (TCFD).

The consultation is a significant development in the UK ESG regulatory landscape and creates material new obligations for groups with UK regulated asset management entities.

This briefing note summarises the top 10 things that asset managers need to know about these important proposals:

1. **What is the TCFD and what is the purpose of the FCA consultation?**
2. **How will the FCA implement the TCFD Recommendations into the UK regulatory regime?**
3. **Which firms and products will be subject to the new rules?**
4. **Are non-UK firms going to be subject to the new rules?**
5. **When will the new rules come into force?**
6. **What disclosures must be included in the entity report?**
7. **What disclosures must be included in the product-level or portfolio-level report?**
8. **Is there a mandatory format for the reports?**
9. **Can firms rely on disclosures made in other documents or made by affiliates or delegates?**
10. **How do the UK proposals differ from the EU SFDR?**

This note focuses on the elements of the consultation which are relevant to **asset managers**.

1. What is the TCFD and what is the purpose of the FCA consultation?

The consultation sets out the FCA's proposals to implement a new climate-related disclosure regime for asset managers, based on the TCFD Recommendations.

What is the TCFD?

The Financial Stability Board established the TCFD to **develop recommendations** for more effective **climate-related disclosures** that could promote more informed investment decisions. The TCFD states that it believes that better information will allow companies to incorporate climate-related risks and opportunities into their risk management and strategic planning processes.

What are the TCFD Recommendations?

The TCFD recommendations on climate-related financial disclosures (**the Recommendations**) were published in 2017. The Recommendations are intended by the TCFD to be adoptable and applicable to organizations across different sectors and jurisdictions. TCFD states that the Recommendations will solicit decision-useful, forward-looking information that can be included in financial filings.

There are **eleven** Recommendations, structured around **four themes**:

(a) governance

(b) strategy

(c) risk management

(d) metrics and targets.

What is the policy purpose of the FCA consultation?

The consultation sets out the FCA's proposals to introduce climate-related financial disclosure rules for asset managers, based on the Recommendations.

The policy purpose is to address the climate change challenge, by requiring harmonised disclosure of information on **how climate-related risks are managed** along the investment chain.

The FCA hopes that this will ultimately result in capital being more effectively allocated across companies and projects, with financial flows supporting the transition to net-zero carbon emissions.

The FCA believes that it is appropriate for the UK regime to be based on TCFD, as many UK firms have a **global reach**, and the Recommendations are now **widely accepted internationally**. The FCA is therefore looking to ensure that the new UK regime is consistent with existing international standards.

Next steps

The consultation closes on **10 September 2021**, with a policy statement expected **in late 2021.**

The FCA has also separately published a consultation aimed at extending the TCFD-derived disclosure requirements to all **UK listed issuers** (see **here**) extending the TCFD-derived disclosure requirements for premium listed companies which were published in December 2020 (see our note **here**).

2. How will the FCA implement the TCFD Recommendations into the UK regulatory regime?

The FCA is proposing to create a new rulebook for the FCA Handbook, which will be known as the **Environmental, Social and Governance (ESG) Sourcebook**.

The ESG Sourcebook will initially set out the disclosure obligations derived from the TCFD Recommendations. However, the FCA intends that it will be expanded over time to include other sustainability-related rules.

The ESG Sourcebook creates two parallel new disclosure obligations, derived from the TCFD Recommendations:

	Obligation	Disclosure	Medium	Frequency
1	Entity-level disclosure	How the firm takes into account climate-related risks when managing investments, consistent with the Recommendations	Public website	Annual
2	Product-level or portfolio-level disclosure	Baseline set of core mandatory carbon emissions and carbon intensity metrics, additional metrics where possible, and scenario analysis	• Public website (subject to exception below for "on demand" reports – see question 7) • and in client communications	Annual

The FCA states in the consultation that (although the entity-level disclosure applies at the level of the FCA regulated firm) firms will be permitted to make group-wide or global disclosures, if preferred.

The TCFD Recommendations and related TCFD guidance papers are not specifically incorporated into the FCA Rules; instead, they are cross-referenced by the ESG Sourcebook. The FCA states in the consultation that it is doing so to allow firms to retain a principles-based approach to compliance with the Recommendations.

3. Which firms and which products will be subject to the new rules?

Firms in scope

The new rules will apply to a defined sub-set of UK regulated asset management entities (**asset managers**):

- portfolio managers
- UCITS management companies and self-managed UCITS funds
- full-scope UK AIFMs
- small authorised UK AIFMs

There is an important **exception** from this general application provision. The new disclosure obligations will not apply to an asset manager which has **less than GBP 5 billion** of assets under management, calculated as a 3-year rolling average. (In the remainder of this note, references to asset managers are to managers not falling within the GBP 5bn exception.)

The FCA has calculated that, following the application of this exception, 140 asset management firms will be in-scope of the rules, representing 98% of the AuM in the UK market.

In addition to asset managers, the rules apply in parallel to certain categories of life insurer and pension product provider, in their capacity as **asset owners**, and to certain financial products offered by those firms. The application of the new rules to asset owners is summarised in a separate briefing note.

Other UK firms are **not** in-scope of the new rules.

Products in scope

In relation to asset managers, the disclosure obligations will apply both at entity-level, and also in respect of in-scope financial products and services (**TCFD products**):

- authorised funds (whether UCITS or AIFs)
  - but excluding feeder funds
  - and treating each sub-fund of an umbrella as a separate product
- unauthorised AIFs
- portfolio management services
  - note this has a specific extended definition in the context of private equity or other private market activities to include investment advice

Overseas funds and overseas assets, managed by an in-scope UK asset manager, are in scope of the disclosure obligations.

4. Are non-UK firms going to be subject to the new rules?

No.

The FCA proposal is that the new rules will only apply directly to UK firms, in respect of business carried out from the UK. This means that **non-UK firms** will **not** be subject to the new rules, as a UK regulatory matter.

This includes the following firms, which will be out-of-scope:

- Non-UK firms which market products and services cross-border into the UK, in reliance on private placement rules or reverse enquiry
- EU firms which are currently in the Temporary Permission Regime (TPR) for a temporary period post-Brexit

There is **no exception** for UK firms which operate exclusively as sub-investment managers to their international affiliates. Such UK firms are therefore in-scope.

It would of course be open to out-of-scope firms to voluntarily make disclosures.

5. When will the new rules come into force?

There is a phased approach to implementation, depending on which of the following two categories applies to the relevant asset manager:

- **Phase 1:** asset managers with **more than GBP 50 billion** of AuM, based on the test set out in the SMCR for Enhanced Firms. The FCA expects that **34** firms will be captured by Phase 1.
- **Phase 2:** all remaining in-scope asset managers (i.e. those with **more than GBP 5 billion, but less than GBP 50 billion** AuM). The FCA expects that **106** firms will be captured by Phase 2.

The timelines for the two phases are as follows:

Phase 1 firms	**1 January 2022**	**30 June 2023**	**1 July 2023**
	Rules first apply	Deadline for publishing first reports	Start date for "on demand" disclosures
Phase 2 firms	**1 January 2023**	**30 June 2024**	**1 July 2024**
	Rules first apply	Deadline for publishing first reports	Start date for "on demand" disclosures

Phase 2 therefore applies on a one-year lag, compared to Phase 1 firms. Note that, for both phases, firms will have an initial year to gather the data required for publishing the first reports by 30 June in the following year.

Please see **questions 6, 7 and 8** below for more details on the content of the reports.

6. What disclosures must be included in the entity report?

Asset managers will be required to publish an entity-level TCFD report, which is consistent with the TCFD Recommendations and recommended disclosures. The FCA will include in the ESG Sourcebook a mandatory list of TCFD-published documents which must be used by an asset manager in preparing the disclosures.

The eleven disclosure topics are divided into four themes, as summarised in the table below:

Governance	Strategy	Risk Management	Metrics and Targets
Disclose the organization's governance around climate related risks and opportunities.	*Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.*	*Disclose how the organization identifies, assesses, and manages climate-related risks.*	*Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.*
a) Describe the board's oversight of climate-related risks and opportunities.	a) Describe the climate-related risks and opportunities the organization has identified over the short, medium, and long term.	a) Describe the organization's processes for identifying and assessing climate-related risks.	a) Disclose the metrics used by the organization to assess climate related risks and opportunities in line with its strategy and risk management process.
b) Describe management's role in assessing and managing climate-related risks and opportunities.	b) Describe the impact of climate related risks and opportunities on the organization's businesses, strategy, and financial planning.	b) Describe the organization's processes for managing climate-related risks.	b) Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks.
	c) Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.	c) Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organization's overall risk management.	c) Describe the targets used by the organization to manage climate-related risks and opportunities and performance against targets.

Firms will also be required to disclose their use of **scenario analysis** (including quantitative examples), and the use of **metrics** and **net zero targets**.

There is also a requirement for a member of the firm's **senior management** to sign a **compliance statement**, confirming that the disclosures comply with the requirements of the ESG Sourcebook.

7. What disclosures must be included in the product-level or portfolio-level report?

The product-level or portfolio-level disclosures comprise both a number of core metrics, and a set of additional metrics.

	Core metric	Notes
(a)	Scope 1 and 2 greenhouse gas emissions	
(b)	Scope 3 greenhouse gas emissions	1 year deferral to 30 June 2024
(c)	Total carbon emissions	Only including scope 3 GHG from 30 June 2024 To be disclosed using both TCFD and SFDR methodologies
(d)	Total carbon footprint	To be disclosed using both TCFD and SFDR methodologies
(e)	Weighted average carbon intensity	To be disclosed using both TCFD and SFDR methodologies

As noted, some of the metrics will be required to be calculated using **both** the **TCFD** methodologies, **and also** separately the methodologies under the EU Sustainable Finance Disclosures Regulation (**SFDR**). These disclosures must be supported by contextualised information, and a historical time series for comparison.

The **additional metrics** include climate Value-at-Risk metrics that show the climate warning scenario with which a product or portfolio is aligned, and other metrics as helpful. The additional metrics must be provided on a best-efforts basis.

Firms must include **scenario analysis** in the product-level reports. For firms with **concentrated exposure or higher exposure** to carbon-intensive sectors, the firm must also disclose specific scenario analysis on orderly or disorderly transition scenarios.

Are there any exceptions to the publication of product-level reporting?

Yes.

The FCA acknowledges that public disclosure of product-level information will not be appropriate for **portfolio management services** or for **unauthorised and unlisted AIFs**. The managers of such products are not required to publish the product-level information on a public website.

Instead, the FCA has created the concept of "**on demand**" TCFD product reports. The clients of such services will be entitled to make a once-a-year demand for reports, which must be provided by the asset manager on request.

8. Is there a mandatory format or mandatory reporting period for the reports?

No, there is no mandatory format for the report.

There is no specific reference period for the reports. Firms can therefore choose their own reference periods, provided that the report is published by 30 June each year.

9. Can firms rely on disclosures made in other documents or made by affiliates or delegates?

Yes. In producing the TCFD report, firms are permitted to **cross-refer** to disclosures made in certain other reports as specified by the rules. This would include reports of an affiliate / **group-level** report, the reports of any **delegates**, or any report the firm is required to produce under the **Listing Rules**. The FCA acknowledges that this may result in some reports being relatively short.

10. How do the UK proposals differ from the EU SFDR?

The EU SFDR regime does not apply in the UK as a domestic matter. This is because it came into force in the EU on 10 March 2021, which was after the end of the Brexit implementation period in the UK (which ended on 31 December 2020). The UK government did not on-shore SFDR into UK domestic law, and therefore it does not apply directly to UK firms as a matter of either UK or EU law.

Please see our SFDR briefing notes page for more information on SFDR, including how it applies indirectly to non-EU firms doing certain cross-border business into the UK.

The FCA helpfully acknowledges in the consultation that some UK firms undertaking cross-border business into the EU will already be complying with SFDR (or other international sustainability disclosure standards) and so is seeking to design a regime which is compatible with those obligations.

For firms which are going to be subject to both the new UK regime derived from TCFD, and SFDR, we set out below a comparison of the key features of the two regimes:

	EU SFDR regime	UK TCFD-dervived regime
ESG scope	Generally applies to a wide range of Environmental (E) and Social (S) risks and objectives Governance (G) is treated as a baseline requirement for in-scope products, rather than a goal in itself	Applies only in respect climate risk, as a sub-set of Environmental (E) Does not address S or G issues
Entity-level disclosures	Requires publication of the manager's sustainability risk policy No prescriptive requirements on the contents of that disclosure	Requires disclosure of how the firm takes into account climate-related risks when managing investments More prescriptive content requirements following the 11 TCFD Recommendations and related TCFD guidance

10. How do the UK proposals differ from the EU SFDR? (cont'd)

	EU SFDR regime	UK TCFD-dervived regime
PAI regime	For firms complying with the principal adverse impacts (PAI) regime, requirement applies to publish both qualitative and quantitative information on how the firm mitigates adverse harm to sustainability factors	No direct equivalent of the PAI regime, although there are requirements at both entity-level and product-specific levels to disclose against climate metrics (which overlap to an extent with the PAI indicators)
Article 8 and 9 regime	Additional product-level disclosures required for products which promote sustainability characteristics (article 8 / "light green") or have a sustainable investment objective (article 9 / "dark green") Article 8 and 9 disclosures are required in pre-contractual disclosures as well as periodic reports	No direct equivalent of the article 8 and 9 regime No specific requirement for pre-contractual product disclosures
Product specific metrics	Periodic reports required for article 8 and 9 products, to report against attainment of sustainability characteristics or objectives	Requirement to publish core and additional climate metrics for all in-scope financial products Not limited to products with a sustainability focus
Mechanics of disclosure	Certain disclosures required on a firm's public website Certain disclosures required in pre-contractual product documentation and periodic reports No exceptions for public disclosures for AIFs or portfolio management services	Generally required on firm's public website Product-specific disclosures to be cross-referenced in periodic reports Certain exceptions available for AIFs or portfolio management services, to exempt firms from public website disclosure
Application to firms	Applies directly to all in-scope EU firms Indirect impact on non-EU firms which market funds into the EU	Applies directly to all in-scope UK firms No indirect impact on firms marketing in the UK

How Simmons & Simmons can help

Simmons & Simmons would be pleased to assist with scoping, advising on decision-making, advising on application, project plans and drafting disclosures.

In addition, we will be developing a set of templates that clients can use as the basis for document updates.

Simmons & Simmons resources

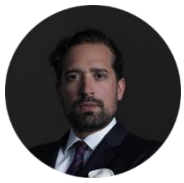
For more information, please see our ESG – notes for clients webpage on our online Sustainable Financing and ESG Investment resource.

Simmons & Simmons key contacts

Lucian Firth
Partner
T +44 20 7825 4155
E lucian.firth@simmons-simmons.com

Craig Bisson
Partner
T +44 20 7825 4691
E craig.bisson@simmons-simmons.com

Sarah Crabb
Partner
T +44 20 7825 3597
E sarah.crabb@simmons-simmons.com



Daniel Lühmann
Supervising Associate, Rechtsanwalt
T +49 69 907454 25
E daniel.lühmann@simmons-simmons.com

Richard Perry
Partner
T +44 20 7825 4310
E richard.perry@simmons-simmons.com

Niamh Ryan
Partner
T +353 1266 2115
E niamh.ryan@simmons-simmons.com

Neil Simmonds
Partner
T +44 20 7825 3151
E neil.simmonds@simmons-simmons.com

Catherine Weeks
Partner
T +44 20 7825 3940
E catherine.weeks@simmons-simmons.com

Ursula Goniszewska
Supervising Associate
T +44 20 7825 3108
E ursula.goniszewska@simmons-simmons.com

Grace Chong
Of Counsel
T +65 6831 5 626
E grace.chong@simmons-simmons.com

Nick Colston
Partner
T +44 20 7825 4147
E nicholas.colston@simmons-simmons.com

Dr Harald Glander
Partner
T +49 69 907454 44
E harald.glander@simmons-simmons.com

Louise Tudor Edwards
Managing Associate
T +44 20 7825 4539
E louise.tudor-edwards@simmons-simmons.com

Iris Dingemans
Partner
T +31 20 722 2335
E iris.dingemans@simmons-simmons.com

Matthew Pitman
Partner
T +44 20 7825 4629
E matthew.pitman@simmons-simmons.com

Devarshi Saksena
Partner
T +44 20 7825 3255
E devarshi.saksena@simmons-simmons.com

Augustin de Longeaux
Partner
T +352 26 21 16 34
E augustin.delongeaux@simmons-simmons.com

David Williams
Partner
T +44 20 7825 4150
E david.williams@simmons-simmons.com

James Wallace
Supervising Associate
T +44 20 7825 4249
E james.wallace@simmons-simmons.com

Katherine Tracey
Supervising Associate
T +44 20 7825 4820
E katherine.tracey@simmons-simmons.com

simmons-simmons.com

© Simmons & Simmons LLP and its licensors. All rights asserted and reserved. This document is for general guidance only. It does not contain definitive advice.

Simmons & Simmons LLP is a limited liability partnership registered in England & Wales with number OC352713 and with its registered office at CityPoint, One Ropemaker Street, London EC2Y 9SS, United Kingdom. It is authorised and regulated by the Solicitors Regulation Authority and its SRA ID number is 533587. The word "partner" refers to a member of Simmons & Simmons LLP or one of its affiliates, or an employee or consultant with equivalent standing and qualifications. A list of members and other partners together with their professional qualifications is available for inspection at the above address.