THE INVESTMENT ASSOCIATION

SDR IMPLEMENTATION SURVEY RESULTS

May 2024

START

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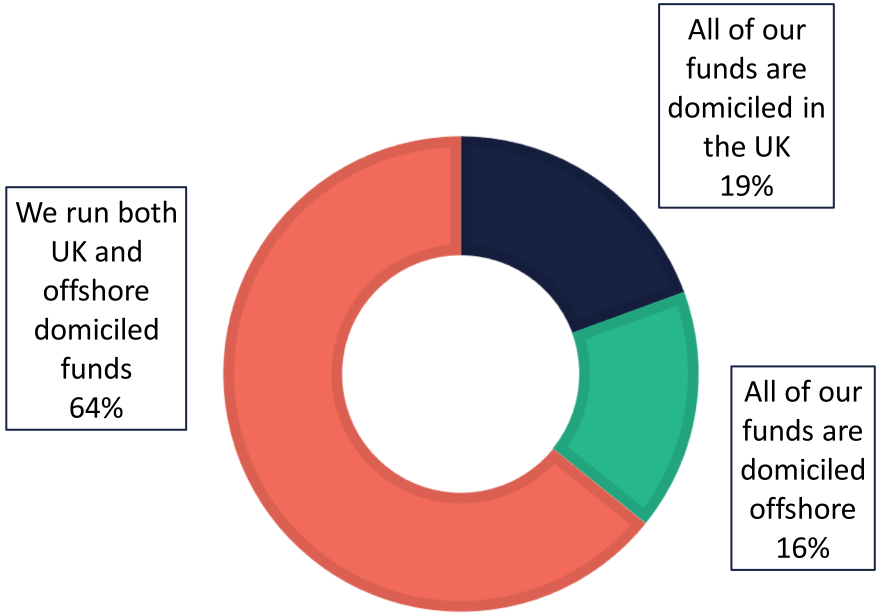
ABOUT THE SURVEY

From March-April 2024 the IA ran a survey to all members to build a comprehensive understanding of member experience and intentions regarding the implementation of the new FCA Sustainability Disclosure Requirements (SDR) and Investment Labels rules.



RESPONDENT PROFILE

The IA received 68 responses from member firms.

- Respondents to the survey between them run about 3,200 UK authorised and recognised funds with total funds under management of approximately £1.1 trillion.
- Based on IA reporting, respondents account for an estimated 80% of total FUM in UK domiciled Responsible and Sustainable funds.
- 83 % of respondents run UK domiciled funds and are currently in scope of the FCA's labelling and naming & marketing rules.
- The remaining 16% of firms running purely offshore funds have shared their views on the anti-greenwashing rule and the possible extension of SDR to offshore funds.

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SECTION ONE

Executive Summary

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EXECUTIVE SUMMARY

- Two-fifths of firms with UK domiciled funds intend to apply a sustainability label to at least one of their funds, with the majority doing so by the end of 2024. Of the firms not currently intending to apply a label in the next two years, most have said they may do so at some point in the future.

- Respondent firms currently intend to label over 200 funds, with the 'Sustainability Focus' label accounting for almost half of all labelled funds. The 'Sustainability Impact' label will be applied to the fewest number of funds, accounting for just over a tenth of labelled funds. Very few index tracking funds will be labelled.

- Almost all firms will not be including derivates and cash/cash-like products in the core 70% threshold required for the labels. Over a third of firms would consider sovereign bonds to be part of the core 70% calculations.

- Labelled funds will sit across 25 IA sectors. Equity funds will account for the majority of labelled funds by number and funds under management. Half of all labelled funds will sit in the IA Global, Volatility Managed, and UK All Companies sectors.

- Over a tenth of firms will change the name of at least one of their funds to comply with the new naming and marketing rules.

- 70% of firms with UK domiciled funds will have non-labelled funds with additional disclosure requirements.

- Over 300 funds will sit in the 'Non-labelled funds with sustainability characteristics' bucket – more than double the number of funds with a 'Sustainability- Focus' label.

- Almost two thirds of firms anticipate that not much change to current practices will be required to comply with the new anti-greenwashing rule, though many have cited the scale of the review required to confirm that they are complying with new regulations as one of the biggest challenges.

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SECTION TWO

Label intentions

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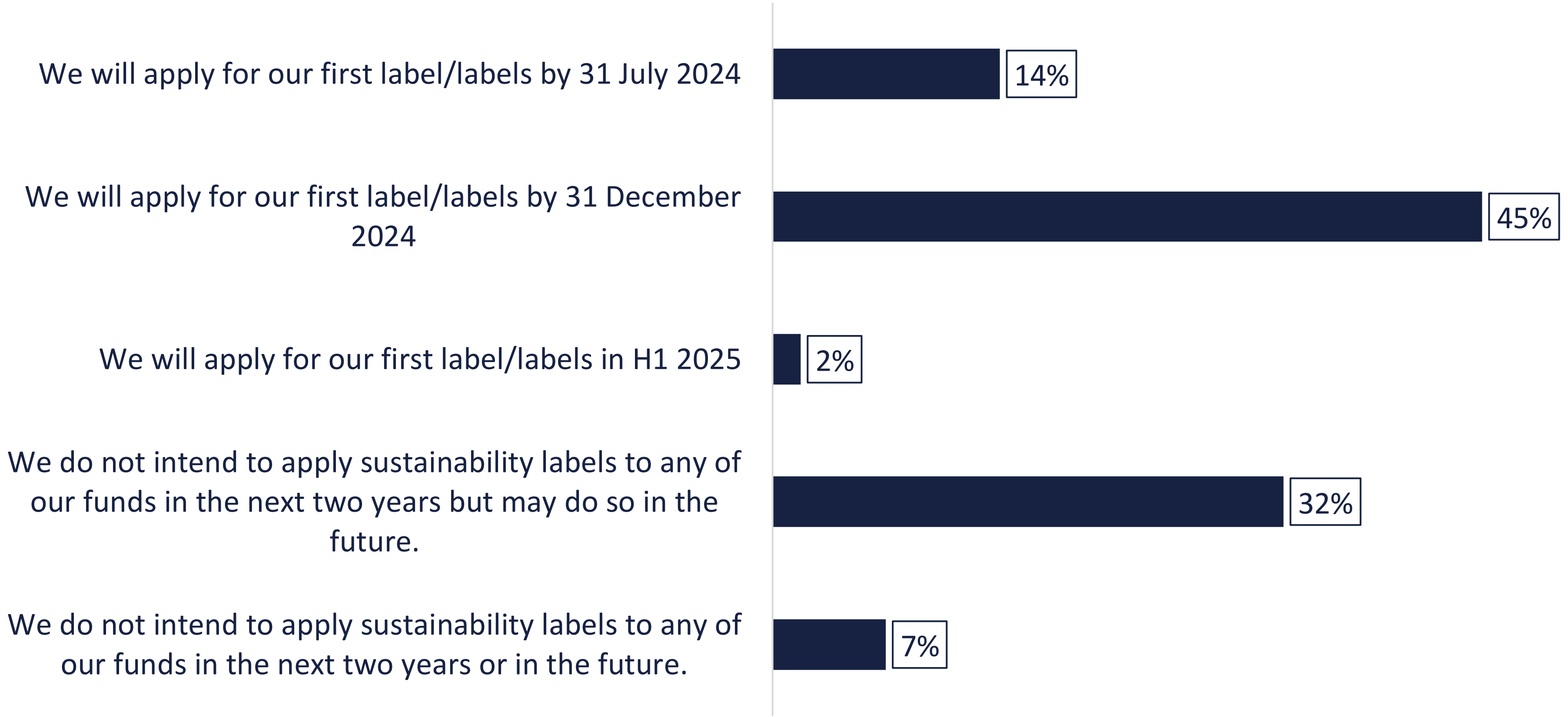
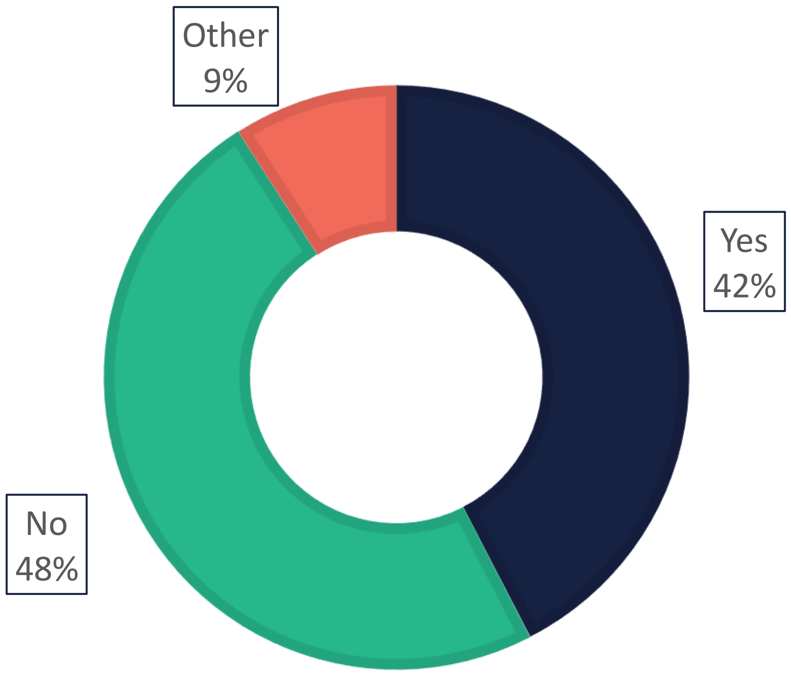
LABEL INTENTIONS

Two-fifths of in-scope firms intend to apply a sustainability label to at least one of their funds, with the majority doing so by the end of 2024.

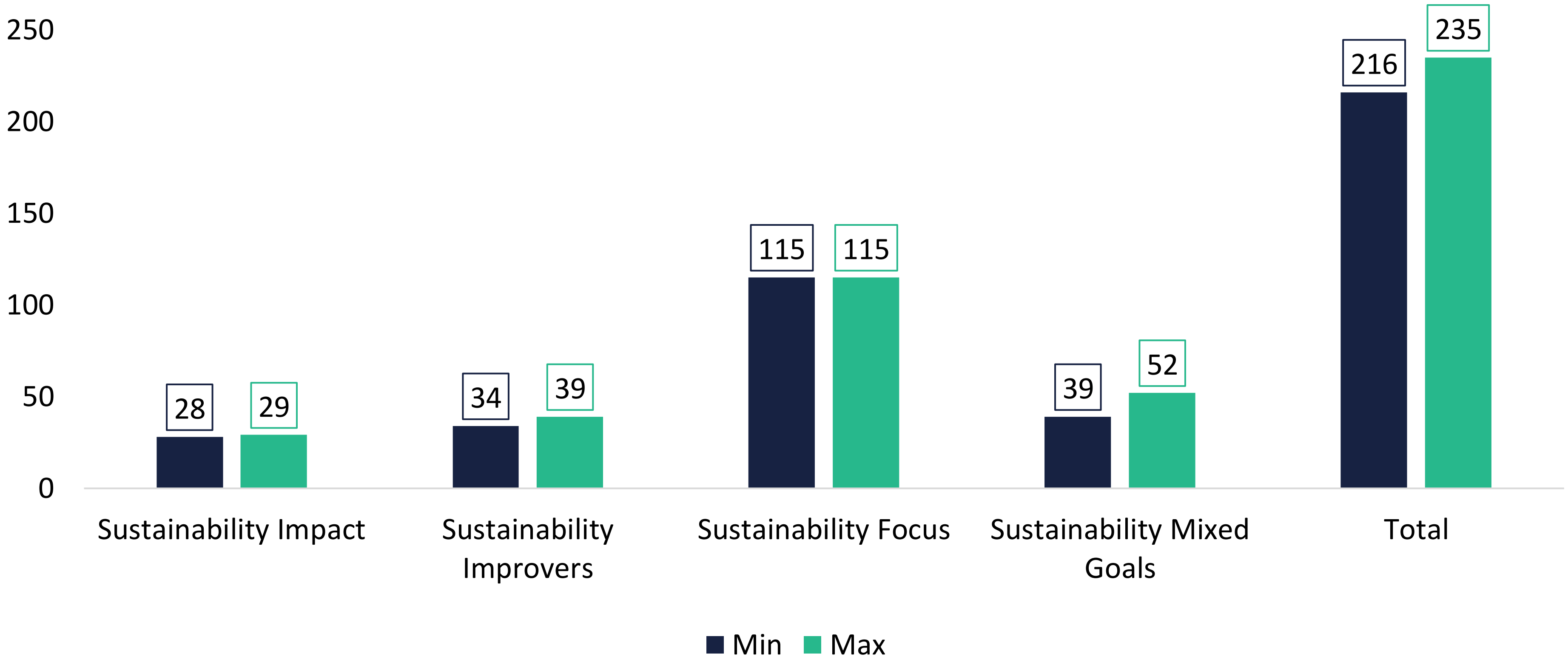


Half of firms applying sustainability labels will adopt a phased approach e.g. applying a first set of labels in July 2024 and applying further labels 6 months later.



LABEL INTENTIONS

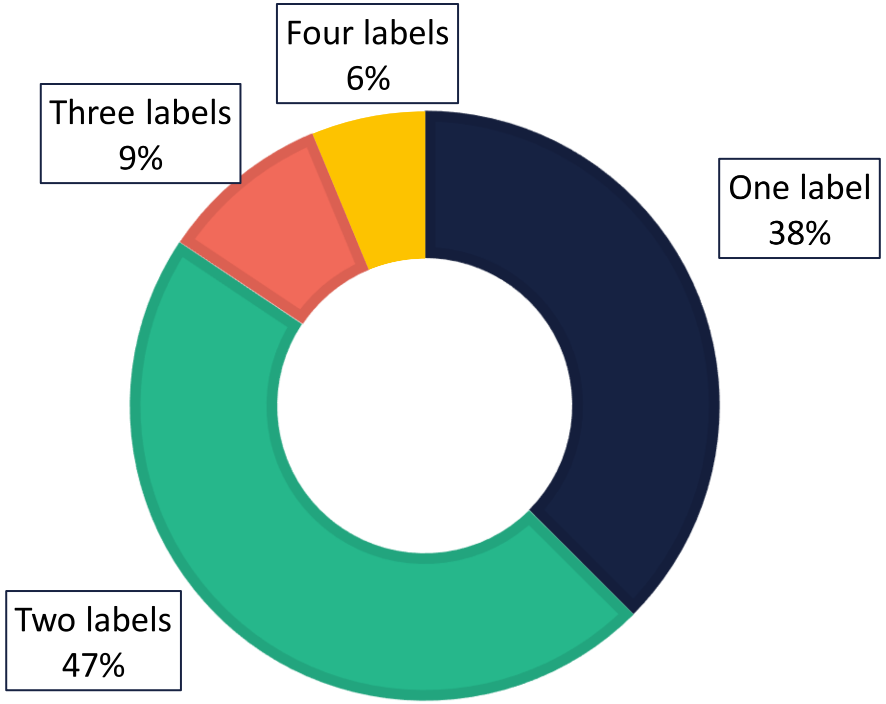
Over 200 funds* could be labelled, with the 'Sustainability Focus' label accounting for almost half of all labelled funds. The 'Sustainability Impact' label will be applied to the fewest number of funds, accounting for just over a tenth of labelled funds.



**Many firms are still working out the finer detail of the rules and were only able to provide a range of funds they think could end up with a label. The chart above represents a range for labelled funds to reflect these responses.*

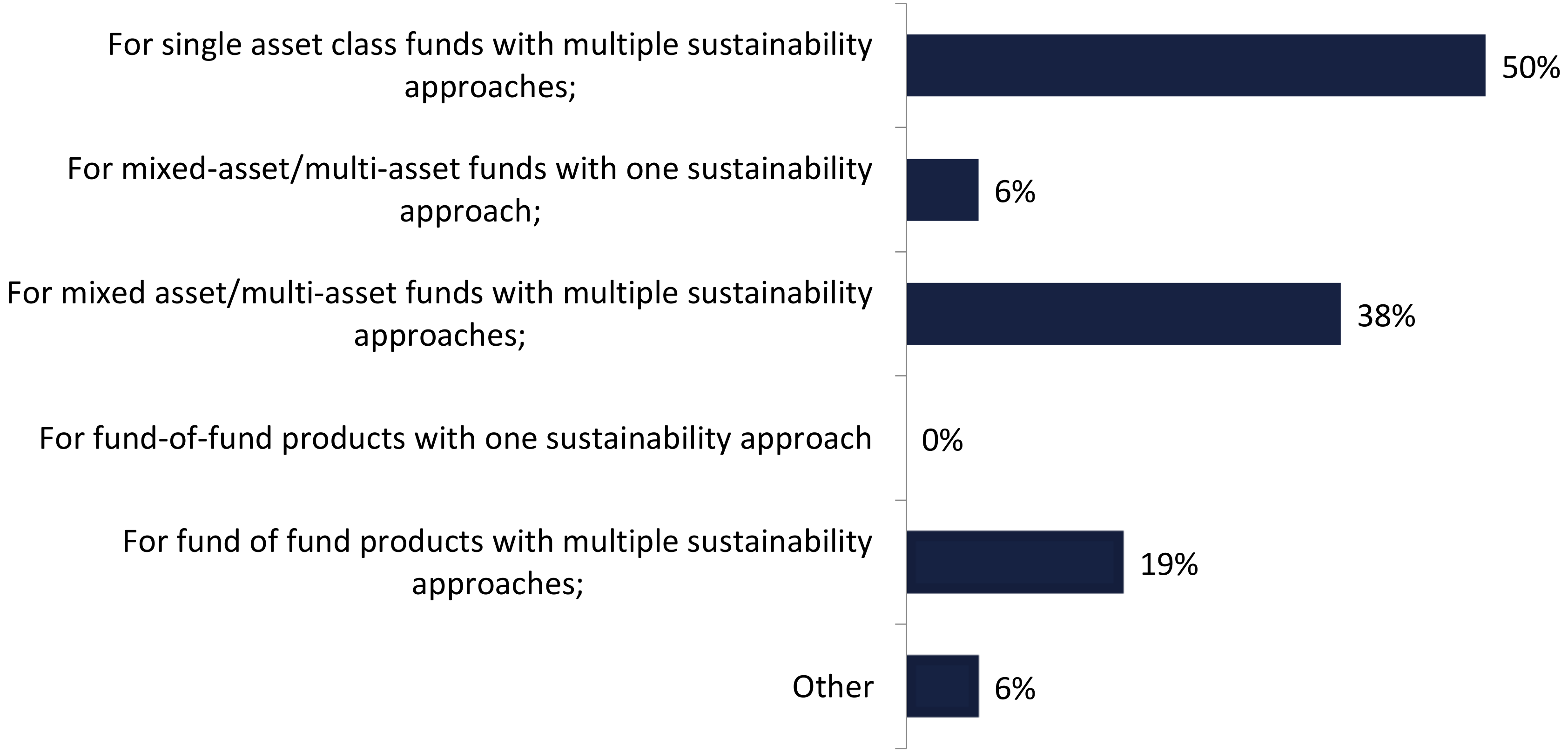
LABEL INTENTIONS

Most firms (84%) will use, at most, two of the four labels available to them.



LABEL INTENTIONS

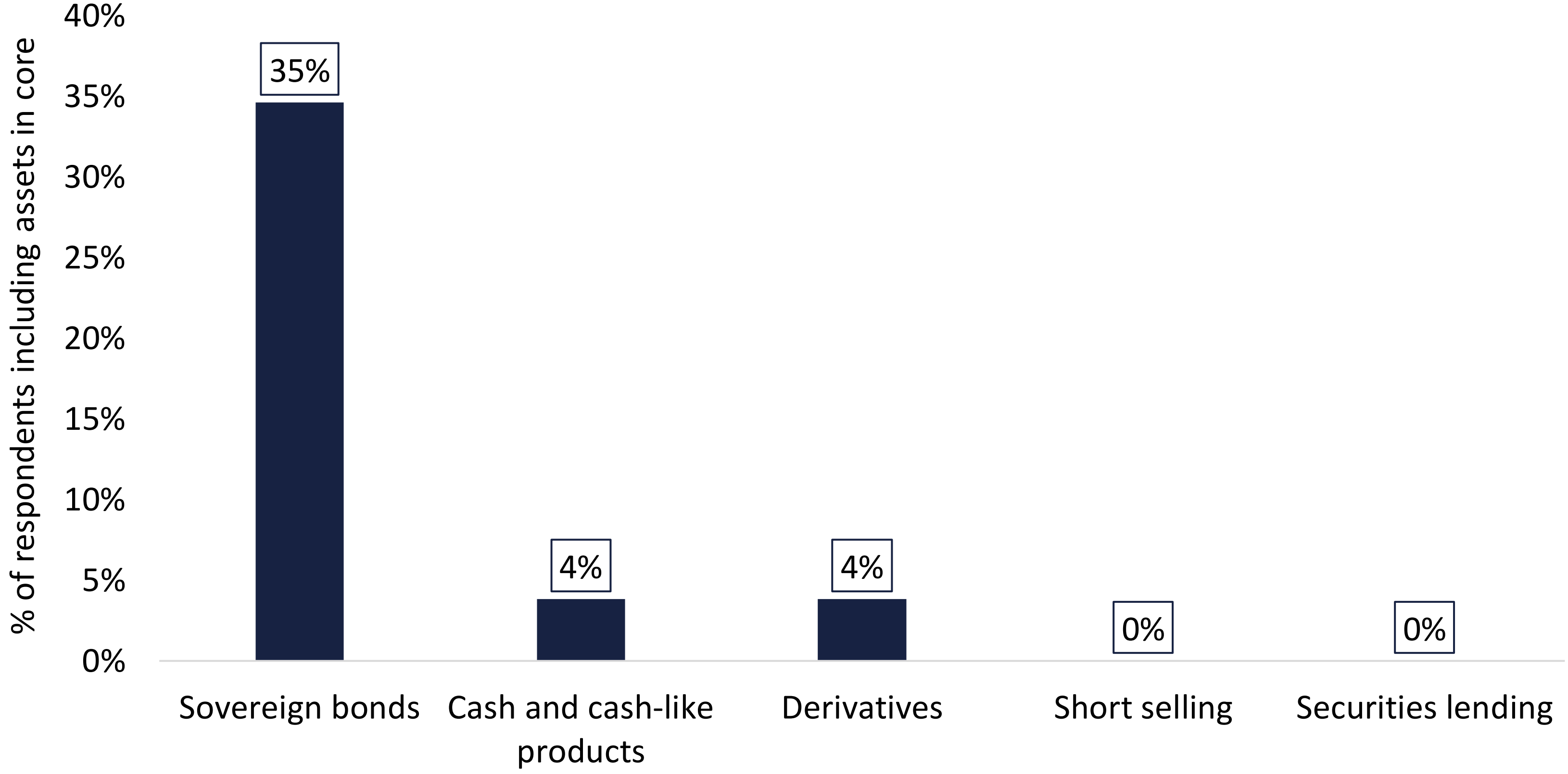
Almost all ‘Sustainability Mixed Goals’ labels will be applied to products pursuing multiple sustainability approaches. Members with sustainable funds-of-funds are facing some challenge in label applications.



“We are increasingly finding Mixed Goals to be better aligned to our current processes, allowing us to hold both Improvers and Focus assets which we believe better serves client’s sustainability and financial outcomes.”

LABEL INTENTIONS

Almost all firms will not be including cash, derivatives, securities lending & short selling assets in the core 70% threshold. Over a third of firms will include sovereign bonds in the core 70% threshold.



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SECTION THREE

Analysis of sustainability funds universe

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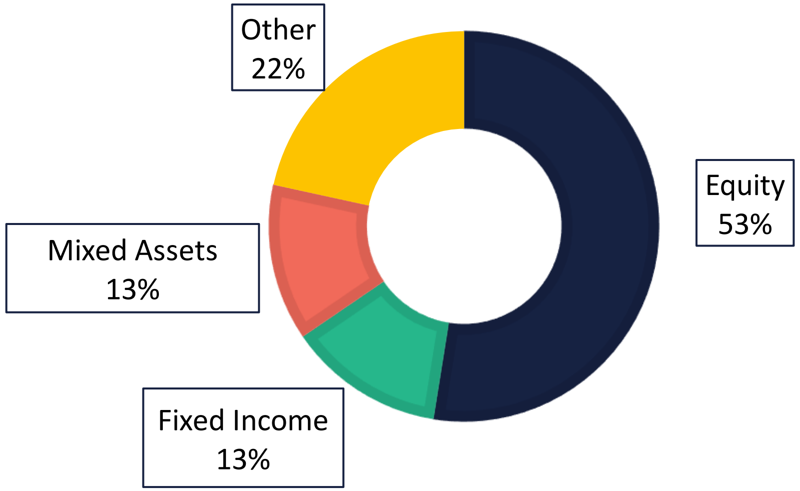
Equity funds will account for the majority of labelled funds by number and funds under management.

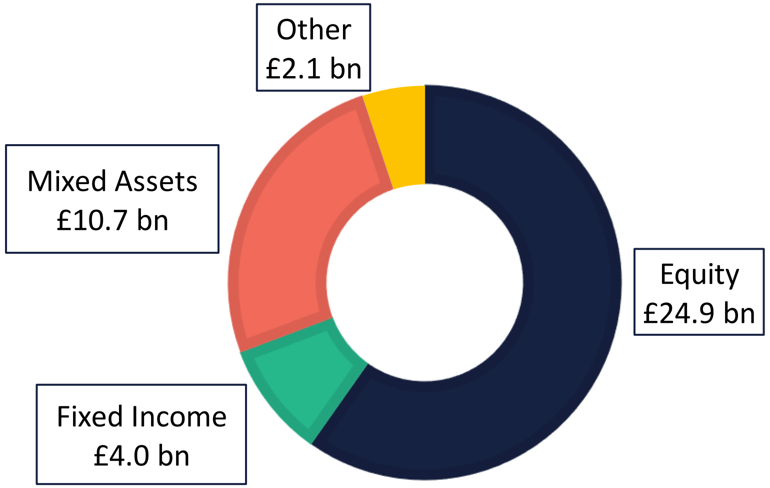
The IA received specific examples on labels for 154 funds, with total funds under management of £45.6 billion, equivalent to 3.2% of UK domiciled FUM.

- Over half of these will be equity funds, classified in 10 IA equity sectors.
- The vast majority of funds in the 'Other' asset class category sit in the Volatility Managed sector, which accounts for the second highest number of funds (22%). These funds are relatively small in terms of FUM, accounting for just 5% of the £41.7 billion.
- Although considerably smaller by number of funds, the mixed asset funds account for about a quarter of the £41.7 billion of FUM.
- Among this universe of funds, very few are index trackers

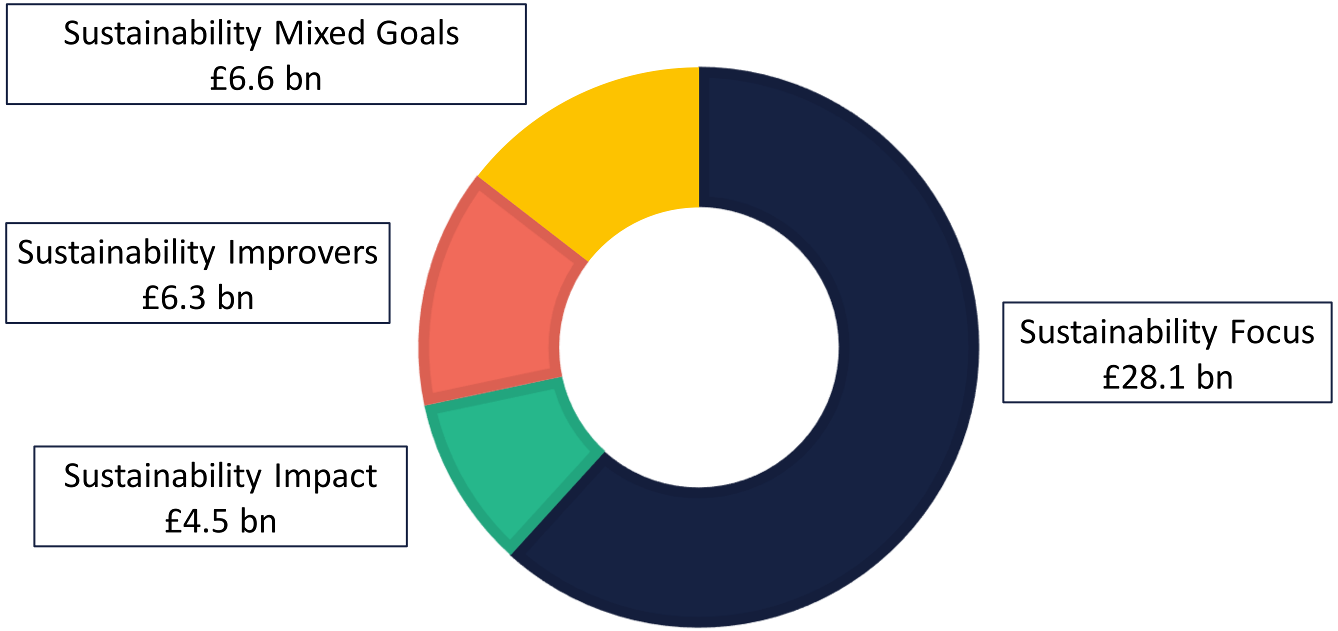
NUMBER OF LABELLED FUNDS- BY ASSET CLASS



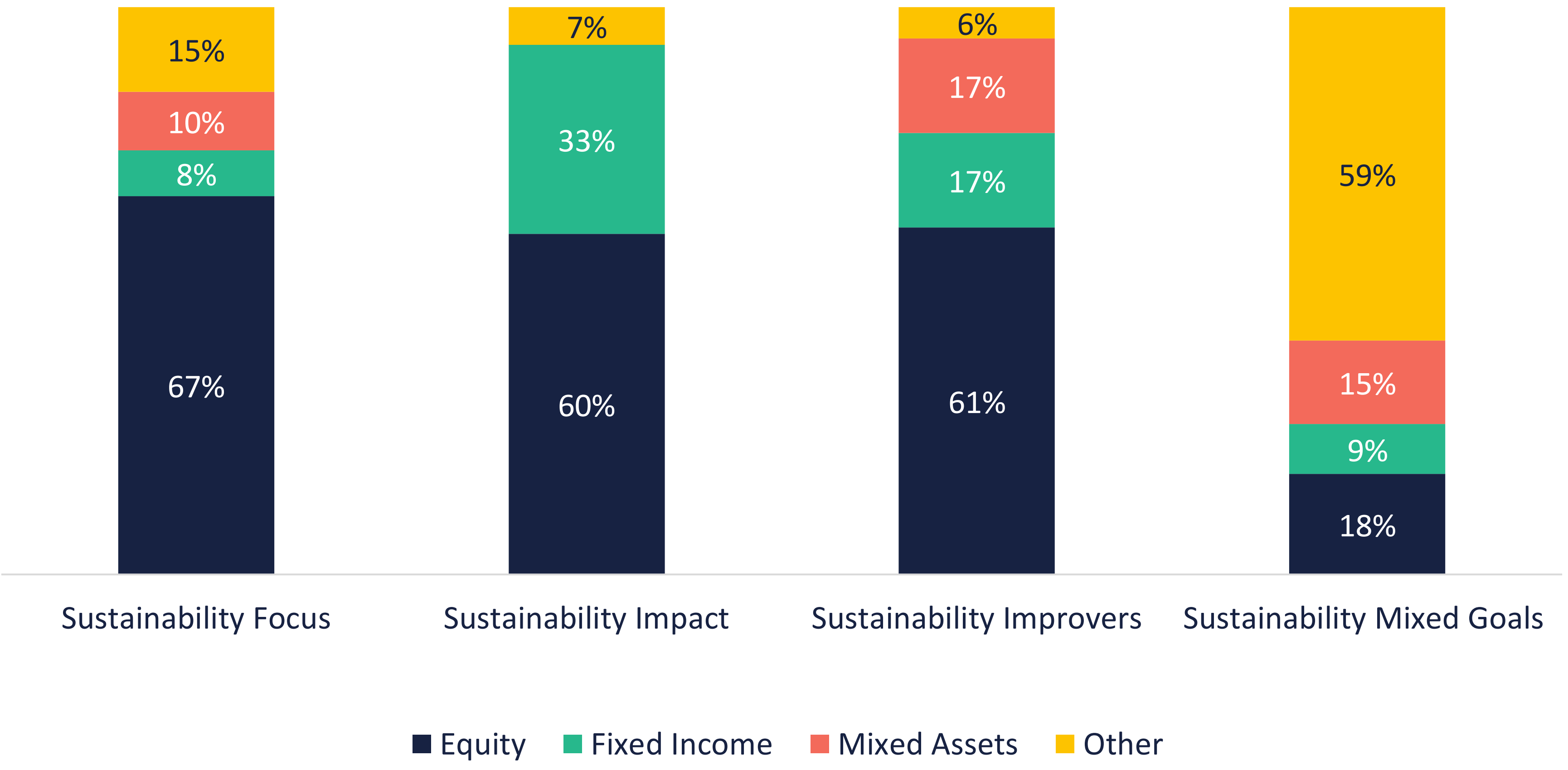
SIZE OF LABELLED FUNDS BY FUM



The Sustainability Focus label will account for three fifths of FUM in labelled funds.



Sustainability Focus, Impact and Improvers funds will predominantly be made up of equity funds. Mixed goals funds will be largely mixed asset and Volatility Managed funds.



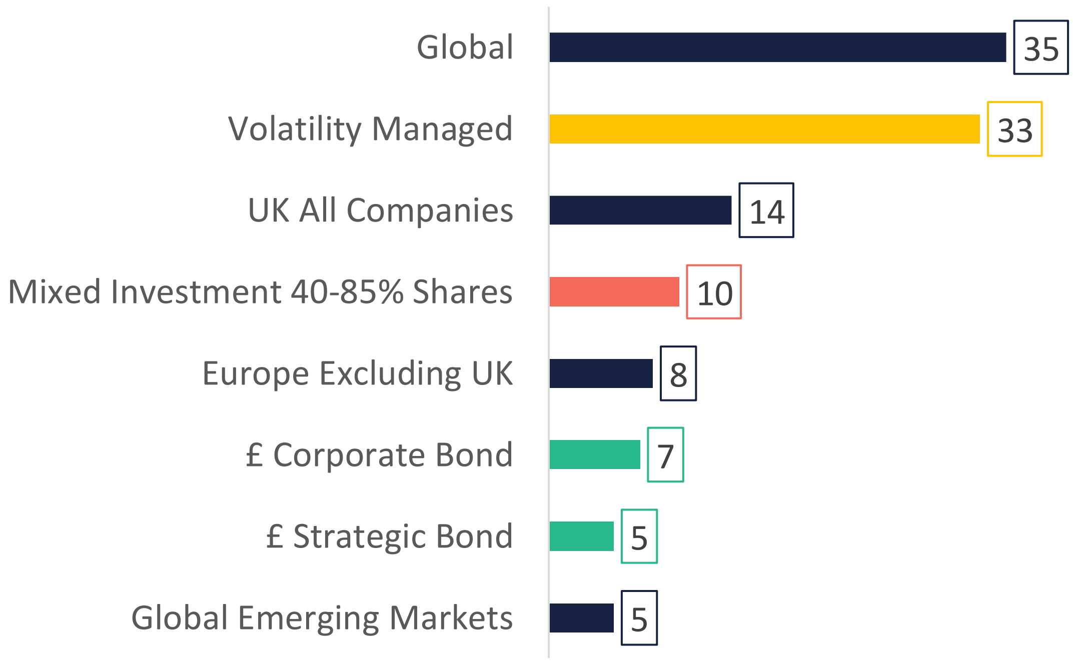
ANALYSIS OF FUNDS UNIVERSE

Over half of labelled funds will be in the Global, Volatility Managed and UK All Companies sectors.

Based on the examples shared with the IA:

- Over half of the equity funds that will be labelled will be in the Global and UK All Companies sectors.
- Two thirds of the labelled fixed income funds will be in the £Corporate Bond and £Strategic Bond sectors
- Volatility Managed funds account for about 85% of labelled funds in the 'Other' asset class bucket
- The chart on the right hand side presents the sectors which will have at least 5 labelled funds and represents 117 out of the 154 funds that we received examples for.
- The remaining 37 funds sit across 17 IA sectors.

SECTORS WITH AT LEAST FIVE LABELLED FUNDS*



** There were a small number of fund examples that we received that were not classified to the IA sectors. For the purposes of this analysis, these fund have been grouped according to the closest IA sector match to provide a clearer idea of the profile of funds within the sample.*

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SECTION FOUR

Naming and marketing rules

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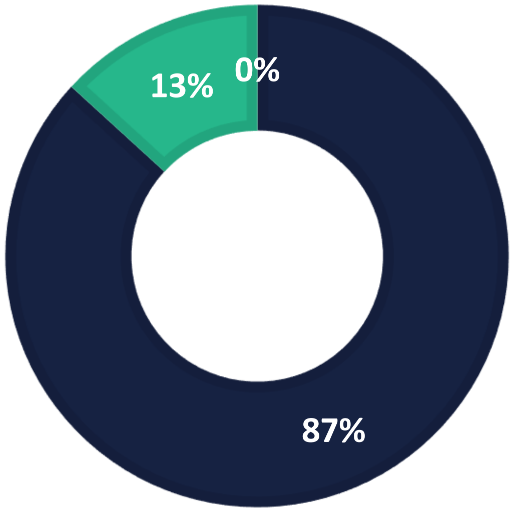
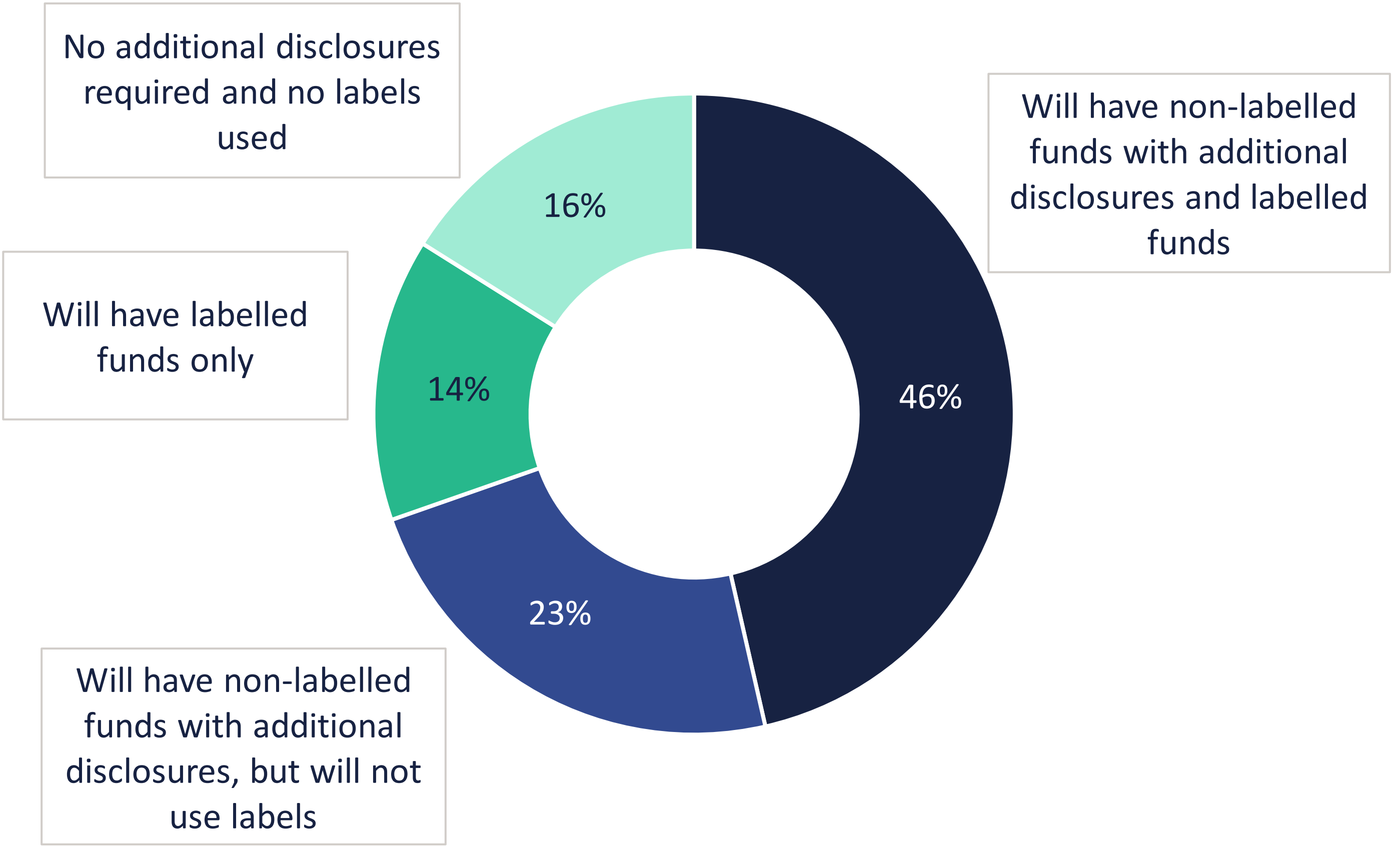
The vast majority of firms will not be changing the name of their funds to comply with the new naming and marketing rules.

- No, we have no plans to change the name of any of our funds;
- Yes, we plan to change the name of one or more of our funds by the end of 2024;
- Yes, we have already changed the name of one or more of our funds



70% of firms with UK domiciled funds, including those not intending to label any of their funds, will have non-labelled funds with additional disclosure requirements.



Non-labelled funds with sustainability characteristics will likely be the largest group- almost double the number of funds with a 'Sustainability Focus' label.

**Many firms are still working out the finer detail of the rules and were only able to provide a range of funds they think could end up with a label. The chart above represents a range for labelled funds to reflect these responses.*

Ethical, responsible and index tracking funds are unlikely to be labelled under SDR… for now.

A comparison of examples provided by members with the funds flagged as responsible investment products in the IA's database suggest that very few funds in the following categories will be labelled:

- Index- trackers – even where firms have provided a small number of examples, these are tentative and subject to further clarification from the FCA
- 80% of funds currently flagged as responsible by the IA but will not be labelled are applying exclusions (including 49% which are also applying fund specific ESG integration and Stewardship).
- The remaining 20% have a mixture of additional sustainability focused approaches, including positive tilt and best in class.
- 20% of funds that will not be labelled use the term 'Ethical' in the name. 29% use the term 'Responsible' in the name.
- Firms have also identified through comments the challenges of applying labels to Fund of Funds products (FoFs), including labelling FoFs that invest in funds with different labels, FoFs that invest in overseas domiciled funds and FoFs investing in externally managed funds.

"The issue of Ethical Funds having no natural home is one that we are concerned about and raising directly with FCA."

"It is unclear whether the FCA's intention is for the bar to be set so high that label adoption is limited to a small number of funds. It also remains unclear how a passive fund is intended to achieve a label beyond potentially being a more concentrated thematic strategy."

"It is unclear how products tracking a Paris-Aligned benchmark would qualify for the sustainability improvers label given that the carbon footprint reduction goal is at portfolio level rather than at asset level."

"There is still uncertainty around UK FOFs wanting to apply a label and include underlying overseas funds in the portfolio"

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SECTION FIVE

Anti-greenwashing rule

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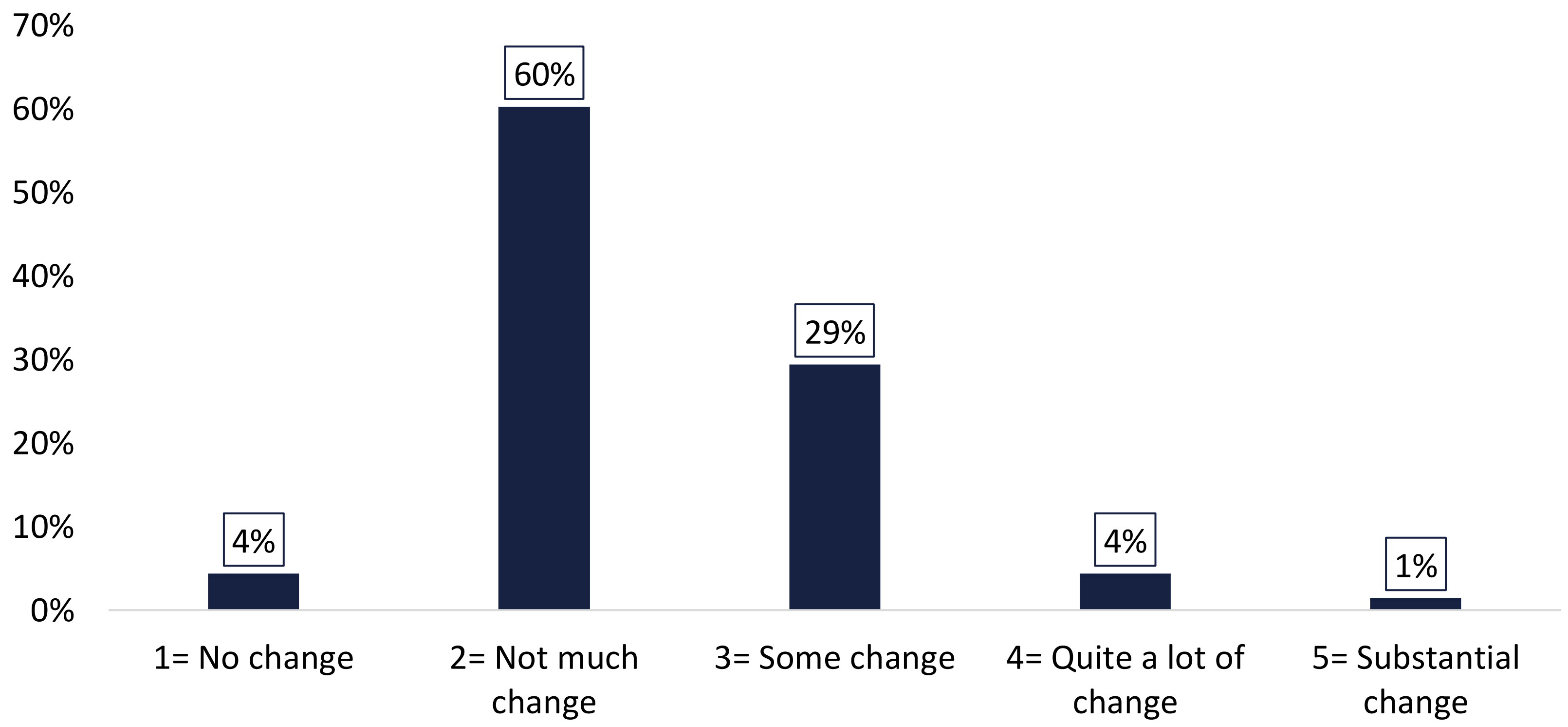
ANTI-GREENWASHING RULE

Most respondents to the survey anticipate that not much change to current practices will be required to comply with the new anti-greenwashing rule.



While firms feel the AGW rule reiterates existing COBS rules around being clear, fair and not misleading, the scale of the review required, the timeline for implementation and (at the time of surveying), the absence of final guidance from the FCA have been the biggest implementation challenges.

Top 5 challenges cited by survey respondents regarding the implementation of the anti-greenwashing rule	% of firms
Volume and type of material to review at entity and product level (incl. all communications, images, banners etc.)	39%
Absence of FCA guidance (incl. more detail on what disclosures are permissible, use of sustainability terms, use of imagery, examples of what good practice looks like, how firms should apply the 'claims should be complete' guidance principle)	25%
Establishing process to ensure future new documentation and communications are in compliance (including ownership of responsibilities, identifying key persons, keeping record of evidence)	25%
Timeline for updating internal documents and guidance (incl. challenges around communicating to investors large scale change)	23%
Staggered timeline of naming and marketing rules (re-isssuing literature, confusion in the market, inconsistency in adoption)	16%

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SECTION SIX

General challenges

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GENERAL CHALLENGES

Implementation timelines, the anti-greenwashing rule and resourcing are the most common challenges firms are facing.

Top 10 implementation challenges cited by survey respondents	% of firms
Implementation timeline (including timelines for launch for first mover advantage, client notifications, challenges of a staggered timeline)	29%
Anti-greenwashing rule (incl. compressed timeline (particularly for firm-wide reviews), cross functional nature of requirements, compliance with consumer duty, communication)	25%
Resource (incl. for implementation and ongoing governance, competing priorities with other FCA regulation such as consumer duty, need of qualified and skilled resources across functions)	19%
Determining what the KPI standards should be (Incl. limitations around underlying data availability)	17%
Uncertainty on future requirements (incl. potential future applicability to unit-linked funds, overseas funds and portfolio management services, treatment of ETF's unclear, other life and pension products)	15%
Establishing processes to ensure effective governance of content and the oversight of content creation (including adapting global practices to account for requirements in the UK)	13%
Interoperability/differences with other regimes such as SFDR (incl. how you communicate these difference with investors)	13%
Ambiguity on rules (including label criteria and whether trackers would qualify, what constitutes a short factual claim etc) and concerns about divergence	13%
Determining which funds should be 'Non-Labelled' or 'Other' and associated challenges (incl. concerns about implications for non-labelled funds)	10%
Developing disclosure template (incl. divergence due to lack of industry template, compatibility with TCFD, ISSB IFRS S1 and S2, TPT, how you describe ESG integrated funds)	10%
Complexities of the ongoing governance for labelled products (incl. complexities associated with reliance on third party reporting)	10%

Thank you to all members who participated in the survey.

For further enquiries on the results, please contact:

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