



Need to know

UK Government publishes Greening Finance: A Roadmap to Sustainable Investing

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This *Need to know* discusses the UK Government's *Roadmap to Sustainable Investing*, published in October 2021.

- The UK government has published a new policy paper, [Greening Finance: A Roadmap to Sustainable Investing \("the roadmap"\)](#), setting out how it intends to 'green' the financial system and align it with the UK's commitment to reach net zero greenhouse gas (GHG) emissions by 2050.
- The roadmap builds on the government's Green Finance Strategy, published in 2019, and is published against the backdrop of the [recent announcement by the IFRS Foundation](#) regarding the creation of a new International Sustainability Standards Board and development of global sustainability standards.
- The roadmap covers in detail the government's strategy for delivering the first of three phases towards greening the financial system, "Informing investors and consumers". This is broken down into three parts:
 - bringing together new and existing UK sustainability reporting requirements under a single framework of new economy-wide Sustainability Disclosure Requirements ("the SDR") for companies, asset managers and owners, and investment products. The SDR sets out expectations as to what requirements will be in place by 2022 (including those already published by the [Financial Conduct Authority](#) (FCA) and the [Department for Business, Energy and Industrial Strategy](#) (BEIS)) and in future years;
 - setting out more detail on plans for a new UK Green Taxonomy, which will require relevant companies and finance providers to report on which of their economic activities can be described as environmentally sustainable and therefore "taxonomy-aligned"; and
 - setting out government expectations as to investor stewardship and sustainability and indicating that progress against these expectations will be assessed in 2023.

For more information please see the following websites:

www.ukaccountingplus.co.uk

www.deloitte.co.uk

Background

In 2019, the UK committed to achieving net zero greenhouse gas (GHG) emissions by 2050. This was followed in 2021 by a further commitment to cut GHG emissions by 78% in 2035 compared to 1990 levels. Acknowledging that the financial system is critical to achieving these goals, the government's [Green Finance Strategy](#), published in 2019, set out policy commitments and actions to support the financial services sector and drive its transition towards green finance. In recent years significant progress has been made against these commitments; for example, premium listed companies are now required to report against the Recommendations of the Task Force for Climate-Related Financial Disclosures (TCFD) on a comply or explain basis, with further requirements set to take effect for standard listed companies, public interest entities, high turnover companies and LLPs, AIM companies, the financial sector, and investment products in 2022.

In October 2021, the UK government published a new policy paper, [Greening Finance: A Roadmap to Sustainable Investing](#) ("the roadmap"). This builds on the commitments made in the Green Finance Strategy by setting out three phases towards greening the financial system:



The roadmap goes on to explain the government's strategy for delivering the first of these phases, broken down into three parts: Sustainable Disclosure Requirements (the SDR), a new UK Green Taxonomy and investor stewardship. In this Need to Know we briefly explore each of these components.

Sustainable Disclosure Requirements

Overview

The objective of the SDR is to create an integrated framework for sustainability disclosures which will enable investors to make informed decisions. The roadmap illustrates the connectivity across the financial system and the interaction between investment and information in the following diagram.



To achieve this flow of information, the SDR proposes to introduce disclosure requirements at each of these three levels of the financial system:

- Corporate-companies, including those in the financial services sector, will need to report on sustainability in the context of their activities.
- Financial sector - asset managers and asset owners will need to explain how they take sustainability into account in making investment decisions, enabling investors to understand the extent to which their assets are held sustainably.
- Financial products - creators of investment products will need to report on the products' impact on sustainability including associated financial risks and opportunities. This will form the basis of a labelling regime to help investors identify and select investment products in line with their sustainability preferences. The FCA has recently published a [discussion paper DP 21/4](#) inviting views on how this regime might work.

Deloitte observation

At COP26, held in November 2021, the IFRS Foundation announced the formation of the International Sustainability Standards Board (ISSB). The ISSB is responsible for developing global sustainability disclosure standards, drafts of which are expected to be published for consultation in early 2022. The roadmap confirms that the government intends to incorporate these standards into the SDR once they are published and will develop a mechanism by which the standards may be endorsed for use in the UK.

More information about the ISSB, its publications to date and its planned work, can be found in Deloitte's publication [Purpose-driven Business Reporting in Focus — IFRS Foundation creates new board to set global sustainability standards](#).

The proposed SDR framework follows the four pillars of the TCFD Recommendations. It is summarised in the following table, which is taken from Figure B of the roadmap:

TCFD Pillar	Corporates	Asset Managers and Asset Owners	Investment Products
Governance	Governance around sustainability-related risks, opportunities, and impacts	Governance around sustainability-related risks, opportunities and impacts, and the implications for investment policies, strategies and outcomes	Governance around sustainability-related risks, opportunities and impacts, and the implications for investment products
Strategy	Actual and potential implications of sustainability-related risks, opportunities and impacts for the organisation's businesses, strategy, and financial planning	Actual and potential implications of sustainability-related risks, opportunities and impacts for the organisation's investment policies, strategies, and outcomes	Actual and potential implications of sustainability-related risks, opportunities and impacts for investment outcomes
Risk Management	Processes used to identify, assess, and manage sustainability-related risks, opportunities, and impacts	Processes used to identify, assess, and manage sustainability-related risks, opportunities and impacts, and the implications for the organisation's investment policies, strategies, and outcomes	Processes used to identify, assess, and manage sustainability-related risks, opportunities and impacts at product level
Metrics and Targets	<p>Metrics and targets used to assess and manage relevant sustainability-related risks, opportunities, and impacts</p> <p>Performance against targets</p> <p>Taxonomy alignment and relevant supporting information</p>	<p>Metrics and targets used to assess and manage relevant sustainability-related risks, opportunities and impacts, and implications for the organisation's investment policies, strategies, and outcomes</p> <p>Performance against targets (where relevant)</p> <p>Taxonomy alignment and relevant supporting information based on underlying investments</p>	<p>Product-level metrics and performance indicators on sustainability-related risks, opportunities, and impacts</p> <p>Performance against targets (where relevant)</p> <p>Product-level Taxonomy alignment and relevant supporting information based on underlying investments</p>

Deloitte observation

The ISSB standards will also be developed based on the four pillars of the TCFD Recommendations. These already form the basis for existing UK requirements, which took effect for periods beginning on or after 1 January 2021, for [premium-listed companies to report on consistency with the four recommendations and eleven recommended disclosures of the TCFD Recommendations on a comply or explain basis](#). This is expected to be extended to standard-listed companies for periods beginning on or after 1 January 2022. Forthcoming requirements for UK public interest entities, high turnover companies and LLPs and AIM companies, which were [published in draft in November 2021 and take effect from 6 April 2022](#), are also based on the TCFD Recommendations. These requirements will help to drive adoption of the principles of TCFD while the global standards are in development and serve as a stepping stone to application of the final standards, which the government intends to adopt for use in the UK.

The SDR will, in some cases, go beyond the TCFD Recommendations and the global standards. In particular it will require entities to disclose more detail about their impact on the environment, and this will be achieved primarily via disclosure against the UK Green Taxonomy (see below). Further disclosure requirements will also affect asset managers/owners and investment products as they will need to:

- substantiate claims that are made regarding funds and products about their sustainability (or other ESG matters) in a way that is comparable across products and accessible to consumers;
- disclose whether and how ESG-related matters are taken into account in their governance arrangements, investment policies and strategies; and
- disclose against the minimum safeguards (see below) which will be set out in the UK Green Taxonomy in the context of sustainable investments, including any related metrics.

As the UK has made a legislative commitment to achieving net zero GHG emissions by 2050, the SDR will require disclosures that explain how firms intend to achieve emissions-related commitments or targets that they have set; this will help investors and markets to hold firms to account on their progress. These disclosures will initially take the form of a requirement to publish transition plans that align with the government's own net zero commitment or explain why such plans have not been published. Going forward, the government and regulators will look to incorporate standards on disclosure of transition plans into UK legislation where possible to enhance consistency and comparability.

Delivering the SDR

The government intends that the SDR will be a fully integrated regime which operates across all sectors of the economy. The precise scope, detail, and timings of such requirements are still subject to consultation and finalisation by the relevant government departments and other regulators.

The [roadmap](#)² sets out the timeline for sustainable finance regulation over the next three years and beyond for different sectoral pathways. Sectoral requirements will be managed centrally by HM Treasury to ensure that the relevant information is made available across the economy. The report further encourages organisations to start taking the necessary steps to build their capabilities based on the indicative pathways.

Deloitte observation

Under the SDR roadmap, the government proposes to consult on the SDR Framework, including the UK Green Taxonomy and application of global sustainability standards issued by the ISSB, with the goal that all UK-registered companies will be subject to some form of disclosure in this regard by 2025. Availability of this information at a corporate level will then enable asset managers/owners, investment products and, potentially, financial advisers, to make disclosures which draw on those made by the corporates in which they invest.

UK Green Taxonomy

Overview

Companies are increasingly looking to highlight their sustainable business practices within their disclosures and several financial products are marketed as “green” or “sustainable”. However, there is currently no definition as to which economic activities are environmentally sustainable. This can result in ‘greenwashing’ as there is a risk that information disclosed by both companies and products may be misleading, may not be comparable between companies, consistent from year to year or easily understood.

What is greenwashing?

Greenwashing is the process of conveying misleading or unsubstantiated claims about environmental performance. The spread of misinformation can lead to incorrect decision making by investors, consumers, and other existing or potential stakeholders, undermining trust in the market.

² Figure C on page 18 and 19 - [Greening Finance: A Roadmap to Sustainable Investing \(publishing.service.gov.uk\)](#)

The government is aiming to address these issues by creating a UK Green Taxonomy ('the taxonomy'). The taxonomy, which will form part of the SDR, will define which economic activities can be described as environmentally sustainable and therefore "taxonomy-aligned". Once developed, UK companies will be required to disclose the proportion of their activities which are taxonomy-aligned and, in turn, investment funds and investment products will be required to disclose what proportion of their assets are taxonomy-aligned.

The government plans to develop an implementation process to ensure that the taxonomy is robust and evidence-based, available to both preparers and users of the related disclosures and designed specifically for the UK, while ensuring compatibility with other international frameworks.

How it works

The UK Green Taxonomy will take the [EU Green Taxonomy](#), which was published in 2020, as its starting point for development. In line with the EU Green Taxonomy, six environmental objectives are proposed:

- 1.Climate change mitigation
- 2.Climate change adaptation
- 3.Sustainable use and protection of water and marine resources
- 4.Transition to a circular economy
- 5.Pollution prevention and control
- 6.Protection and restoration of biodiversity and ecosystems

These will then be underpinned by a set of standards known as Technical Screening Criteria (TSC). Each economic activity included in the taxonomy will have an individual TSC, which identifies how that activity can make a significant contribution to that environment objective. For an activity to be considered taxonomy-aligned, three tests must be met:

- It must make a substantial contribution to one of the six environmental objectives.
- It must not do significant harm to any of the other objectives.
- It must meet a set of minimum safeguards, constituting alignment with OECD Guidelines for Multinational Enterprises, and the UN Guiding Principles on Business and Human Rights.

There are certain sectors where taxonomy-aligned activities may be limited and some economic activities cannot be carried out in a way that aligns to a net-zero emissions target; for instance, the manufacture of cement. In such sectors, TSCs will set the threshold for taxonomy-alignment based on the best in-sector emissions level. The affected sectors will still, however, be required to identify the proportion of their capital expenditure that is taxonomy-aligned. The objective being that the direction of investment towards taxonomy-aligned projects will demonstrate their direction of travel towards a more sustainable business.

The SDR will require certain companies to disclose the percentage of capital expenditure, operational expenditure and turnover that relates to taxonomy-aligned activities. This is intended to provide investors and consumers with a clear, understandable and comparable indicator of a company's current environmental performance. These can then be used as a basis for investment funds and investment products to provide informed disclosures on the extent to which the funds or products are taxonomy-aligned.

Development and implementation

As part of the development process the TSCs will be subject to public consultation. TSCs for the first two objectives (climate change mitigation and climate change adaptation) are currently being reviewed by the government ahead of a planned consultation in the first quarter of 2022 with final legislation expected by the end of 2022. The TSCs will be implemented into UK law via secondary legislation.

Once the taxonomy has been brought into law, the government plans to develop guidance to assist with implementation.

Deloitte observation

The [EU Green Taxonomy](#) takes effect in the EU for periods commencing on or after 1 January 2022, reporting on activities undertaken by EU companies in 2021. The environmental objectives set out above for the UK Green Taxonomy are the same as those used for the EU Green Taxonomy. In 2022 only the first two objectives will be reported against in the EU, but this will increase to all six for 2023. The implementation process in the EU will help to inform the development of the UK Green Taxonomy and supporting guidance.

UK companies offering financial products in the EU should also note that they will need to comply with the requirements of the EU Green Taxonomy. The scope also captures UK companies that are listed on EU regulated markets and EU subsidiaries of UK companies.

Investor Stewardship

The roadmap highlights the importance of investor stewardship in ensuring the responsible allocation of capital resources to create sustainable long term value. In line with this the government notes that investors and primary allocators of capital have a key role in driving change towards a low carbon economy and should seek to integrate ESG considerations into:

- their investment decision-making;
- engagement with their investees' management and boards on strategies to generate long term-growth;
- collaboration with other investors to strengthen their overall influence; and
- the exercise of their votes as shareholders of companies.

Institutional investors have stated that they need UK companies to disclose sufficient ESG and climate-related information to facilitate informed decision-making. Via its roadmap and, in particular, disclosures required under the SDR and UK Green Taxonomy, the government anticipates such information becoming increasingly available.

Further information

If you have any questions about the policy paper, please speak to your usual Deloitte contact.

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- Deloitte's authoritative, up-to-date, GAAP manuals which provide guidance for reporting under UK GAAP and IFRS Standards
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