

David Stubbs
Financial Conduct Authority
12 Endeavour Square
London E20 1JN

Also sent via email to cp24-12@fca.org.uk

18th October 2024

Dear David,

Response to CP24/12: Consultation on the new Public Offers and Admission to Trading Regulations regime (POATRs)

We are writing to outline our views on the new POATRs framework, which will replace the UK Prospectus Regulation. ShareAction is a registered charity established to promote transparency and responsible investment practices throughout the financial services sector. Among other activities, we work with the financial services sector to promote integration of sustainability factors in investment decisions, long-term stewardship of assets and the consideration of the views of clients, beneficiaries and pension scheme members.

We would like to thank your team for taking the time to meet to discuss our views on the consultation earlier this month. Our response is focussed on questions 41 and 42 on sustainability-linked bonds and use of proceeds bonds. From various discussions we have had with bond investors, we understand that our concerns are broadly shared, as they pertain primarily to credit materiality and the efficient pricing of risk on behalf of their clients. We welcome efforts by the FCA to raise standards through more rigorous disclosures by companies when issuing such bonds. However, we also recognise that thematic bonds represent a tiny proportion (c\$4.4tn)¹ of the overall bond market globally (c\$140tn)².

Most bonds are not labelled, but borrowers may often cause environmental and social impacts that end-clients have an interest in. Equally, issuers may be exposed to environmental and social risks that contribute to elevated default risk – both idiosyncratic and systemic. We recognise that the “necessary information test” provides some protection for investors in requiring the disclosure of material information. However, the determination of what constitutes material information is at the discretion of the borrower and thus risks mis-alignment with what investors might view as material. This is particularly pertinent in light of the rapidly evolving understanding of the economic implications of climate change. Transition risk is increasingly recognised as credit risk by investors. Minimum sustainability disclosure standards can protect investors against the risk that a borrower’s determination of materiality lags current scientific and financial analysis. We therefore strongly encourage the FCA consider how it can ensure that all bonds have higher disclosure requirements for ESG risks and impacts, not just labelled ones.

Question 41. Do you agree with the proposed new disclosure requirement and set of voluntary additional disclosures we are proposing to mitigate information gaps between bond frameworks (or similar documents) and prospectuses? Are there other disclosures that you think we should consider?

¹ https://www.climatebonds.net/files/reports/cbi_sotm23_02h.pdf

² <https://www.sifma.org/wp-content/uploads/2023/07/2024-SIFMA-Capital-Markets-Factbook.pdf>

Yes, we support the proposed disclosures for sustainability-labelled debt instruments. A lack of transparency and consistency between information presented in prospectus and bond framework documentation has resulted in challenges for investors wishing to understand the sustainability profile of these securities. Addressing this through the introduction of a new disclosure requirement for issuers to state in prospectuses whether their bonds have been marketed as 'green', 'social', 'sustainable' or 'sustainability-linked', or are issued under a bond framework is a welcome step forward. We also support the additional complementary disclosure items aimed at corporate issuers, though we strongly encourage the FCA to implement these proposals on a mandatory basis.

In addition to the proposed disclosures, we encourage the FCA to require issuers to additionally disclose:

- Whether the bond being issued is in-line with the framework;
- Whether the bond will be subject to a post-issuance review and, if so, what type and who will provide it.

We note the concerns of some respondents to EP4³ that regulatory intervention in this area may have an impact on the competitiveness of the UK market. We do not agree with these concerns. We support efforts to make the UK a good place to list, but this should not come at the expense of making it a less attractive place to invest. High standards around corporate disclosures are vital for UK savers, investors and for sustainable, long-term economic growth. Inherent flaws within the structure of sustainability-linked bonds is actively constraining demand; addressing these flaws by introducing improved disclosures on a mandatory basis can help to enhance UK market competitiveness by increasing investor appetite.

Question 42. Do you agree with the additional voluntary disclosures we are proposing to introduce in prospectuses for UoP bonds? Are there other disclosures that you think we should consider?

Yes. We support disclosures around project selection as an essential element of UoP bonds, including around post-issuance performance, though we strongly encourage the FCA to implement these proposals on a mandatory basis. In addition to information on the main elements that will be assessed, the relevance of the assessment in relation to the sustainability characteristics of the securities, and the person responsible for the assessment, the issuer should also disclose where the results of the post-issuance assessment can be located.

Taking a mandatory approach will help to ensure these disclosures do not lead to a lowest common denominator approach or significant differences in the types and amount of information being reported. Investors should be able to evaluate bonds on a level playing field. While we have heard feedback from some that smaller issuers may struggle to implement extensive disclosures, our view remains that where a company is big enough to come to the bond market, it is big enough to know and disclose its sustainability risks and impact. In addition to the disclosures around potential risks to social or environmental objectives, we also propose a new mandatory disclosure on the extent to which the issuance is aligned with the issuers' transition plan. This would help to accelerate the flow of information around issuers' alignment with the transition to net-zero, further boosting transparency, and enabling investors, financial regulators and HMG to understand how different companies, sectors and the broader economy is transitioning to net-zero.

³ <https://www.fca.org.uk/publication/call-for-input/non-equity-securities-engagement-paper-4.pdf>

More broadly, while we encourage the FCA to move forward with its proposals – on a mandatory basis – we also recognise a fundamental flaw in the structure of UoP bonds. Specifically, that such bonds prescribe what the funds being raised must be spent on, but ignore the broader activity of the company. This opens the potential for inconsistency between the sustainable purpose of the bond and the sustainability strategy of the company and can facilitate corporate greenwashing. This has the potential to decrease investor interest, constrain economic growth and undermine the entire regime – including our ability to tackle climate change. An example of this is where a fossil fuel company may issue a green bond to fund a wind-farm, while still investing in and growing fossil fuel production. Indeed, if the company was going to invest in that wind farm anyway (as part of a diversification strategy), then the green bond has actually increased its ability (i.e. its capital available) to fund fossil fuel growth. Assessing the credibility of green bonds therefore requires both how the proceeds will be used, as well as the broader sustainability footprint of the company. Anecdotal evidence suggests that less than a third of current green bonds are investible on such a double-test basis. We would therefore strongly encourage the FCA to consider how far the current structure of UoP bonds is undermining efforts to tackle climate change, the extent to which such activities count as greenwashing and whether a minimum sustainability threshold that ensures that unsustainable companies cannot issue sustainably labelled bonds is necessary.

We hope our views are clear. We would be delighted to answer any further questions you may have or to meet to discuss our response in more detail.

Fergus Moffatt

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