

Sustainable Finance Disclosure Regulation (SFDR)



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1. Background

The new **Sustainable Finance Disclosure Regulation**¹ (SFDR) introduced various disclosure-related requirements for financial market participants and financial advisors at entity, service and product level. It aims to provide more transparency on sustainability within the financial markets in a standardised way, thus preventing **greenwashing** and ensuring **comparability**. The majority of the new disclosure obligations will be applicable as of **10 March 2021**.

In light of this, on 23 April 2020 the three European Supervisory Authorities launched a joint public consultation on **draft regulatory technical standards**² for ESG disclosures. The consultation document provides concrete proposals for the **content, methodologies and presentation** of sustainability disclosures in the fields of:

- principal adverse impact disclosure
- pre-contractual product disclosure
- website product disclosure
- product periodic disclosures.

The consultation is open until 1 September 2020 and the final texts are expected in **December 2020**, leaving a **very challenging implementation timeline** (3 months).

Key facts

Topic	Sustainable finance
Impact	<ul style="list-style-type: none">• Financial institutions (banks, investment firms, asset managers, insurers)• EU entities – direct impact• Non-EU entities – indirect impact through:<ul style="list-style-type: none">– EU subsidiaries– provision of services in the EU– market pressure
Status	Number of measures already applicable and legally binding Others still in proposal phase
Timeline	Moving target through 2022/2023
Recommended actions	Impact assessment Implementation

¹ Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector.

² JC 2020 16, Joint Consultation Paper ESG Disclosure – Draft regulatory technical standards with regard to the content, methodologies and presentation of disclosures pursuant to Article 2a, Article 4(6) and (7), Article 8(3), Article 9(5), Article 10(2) and Article 11(4) of Regulation (EU) 2019/2088.

2. Legal entity level disclosure – corporate level

The SFDR introduces new obligations for the financial institutions in its scope related to disclosures on legal entity level. It differentiates between financial market participants (providing SFDR products) and financial advisers (advising on SFDR products).

The following corporate-level information must be disclosed on the website:

	Financial market participants	Financial advisers
Sustainability risk policy	<ul style="list-style-type: none"> Information about policies on the integration of sustainability risks into the investment decision-making process 	<ul style="list-style-type: none"> Information about policies on the integration of sustainability risks into the investment advice or insurance advice
Adverse sustainability impact	<ul style="list-style-type: none"> Consideration of principal adverse impacts of investment decisions on sustainability factors Statement on due diligence policies Mandatory for large entities and large holdings Comply or explain for all other entities 	<ul style="list-style-type: none"> Consideration of principal adverse impacts on sustainability factors in the investment advice or insurance advice Comply or explain
Remuneration policies	<ul style="list-style-type: none"> Information on how remuneration policies are consistent with the integration of sustainability risks 	

Of particular importance is the adverse sustainability impact.

Principal adverse impact on sustainability factors

- negative, material or likely to be material effects on sustainability factors that are caused, compounded by or directly linked to investment decisions and advice performed by the legal entity

The proposed Level II measures define a **catalogue of mandatory and voluntary adverse sustainability indicators** with corresponding metrics in relation to:

- climate and the environment
- social and employee, respect for human rights, anti-corruption and anti-bribery matters.

The Regulation requires to understand:

- scope,**
- severity,**
- probability of occurrence and**
- potentially irremediable character** on sustainability factors.

The sustainability factors are **pre-defined in a template** and consist of:

32 mandatory indicators	<ul style="list-style-type: none"> 16 environmental 16 social
18 voluntary indicators	<ul style="list-style-type: none"> 11 environmental 7 social

For large entities and parents of large groups, the disclosure of adverse sustainability impact is mandatory. These entities need to start considering the principal adverse impact by 30 June 2021 at latest. The first mandatory reporting is required by 30 July 2022 for the reference period in 2021.

3. Product-level disclosure

The SFDR imposes various new obligations for product disclosures in relation to sustainability. It includes requirements not only for ESG-related products, but also for mainstream, or non-ESG-related, products.

To fulfill the new product disclosure obligations, financial entities have to classify the products they manufacture or advise on into three categories:





Mainstream products	Products promoting environmental or social characteristics	Products with sustainable investment objective
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This affects the following documentation:

- pre-contractual disclosure
- periodic reporting
- website product disclosure

3.1 Product pre-contractual disclosure

The SFDR imposes new requirements regarding **pre-contractual disclosure**. Certain obligations are included in the **new EU Taxonomy Regulation**³.

	Mainstream products	Products promoting environmental or social characteristics	Products with sustainable investment objective	
Integration of sustainability risks	<ul style="list-style-type: none"> • The manner in which sustainability risks are integrated in the investment decision/investment or insurance advice • Assessment of the likely impacts of sustainability risks on the financial return • Where sustainability risk is deemed not to be relevant, explanation of the reasons for this 			 Financial Market Participant  Financial Advisor
Principal adverse impact	<ul style="list-style-type: none"> • Where the FMP considers it: consideration of the product's principal adverse impacts on sustainability factors • Where the FMP does not consider it: statement on non-consideration + reasons for this 			 Financial Market Participant
Additional sustainability disclosures	n/a	<ul style="list-style-type: none"> • How the characteristics are met • Consistency of the index with the characteristics 	<ul style="list-style-type: none"> • How the objective is to be attained • Alignment of the index with the objective 	 Financial Market Participant



Where to disclose

Existing pre-contractual documents (e.g. information to clients Art. 24 [4] MiFID II, UCITS prospectus, etc.)

According to the proposed regulatory technical standards, the information on additional sustainability disclosures has to be provided using a mandatory template (not yet available) and integrated as an annex into the existing pre-contractual documents.

³ Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

3.2 Product website disclosure


Financial market participants are further required to disclose certain product information on their website for each SFDR product supplementing their pre-contractual disclosure.

The following table provides an excerpt of the required information:

Mainstream products	Products promoting environmental or social characteristics	Products with sustainable investment objective
<ul style="list-style-type: none"> n/a 	<ul style="list-style-type: none"> Summary Description of the characteristics Information on the methodologies for assessing, measuring and monitoring of the characteristics Due diligence on the underlying assets Data sources, screening criteria for the underlying assets and relevant sustainability indicators Limitation to methodologies and data 	<ul style="list-style-type: none"> Summary Description of the objective Information on the methodologies for assessing, measuring and monitoring of the impact Due diligence on the underlying assets Data sources, screening criteria for the underlying assets and relevant sustainability indicators Limitation to methodologies and data

3.3 Product periodic reports

The SFDR imposes new requirements regarding **periodic disclosure documentation**. Again, certain obligations are included in the **new EU Taxonomy Regulation**.

	Mainstream products	Products promoting environmental or social characteristics	Products with sustainable investment objective
Principal adverse impacts	<ul style="list-style-type: none"> Where the financial market participant considers it: information on principal adverse impacts on sustainability factors 		
Additional sustainability disclosures	n/a	<ul style="list-style-type: none"> The extent to which the environmental or social characteristics are met 	<ul style="list-style-type: none"> The overall sustainability-related impact A comparison between the product impact and the impacts of the designated index and of a broad market index
Additional green taxonomy-related information	<p>Statement The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities</p>	<ul style="list-style-type: none"> Requirements as for products with sustainable investment objective as applicable Additional statement that the DNSH principle is applied only to investments in Taxonomy 	<ul style="list-style-type: none"> Taxonomy objective(s) to which the product contributes % investments in Taxonomy activities % of enabling and transitional activities



Where to disclose

Existing periodic reporting documents (e.g. periodic report Art. 25 (6) MiFID II, UCITS annual report, etc.)

Similarly to the pre-contractual disclosures, the information on additional sustainability disclosures will have to be provided using a mandatory template (not yet available) and integrated as an annex into the existing periodic reporting documents.

How can we support you?

- SFDR scoping and impact analysis
- Regulatory gap analysis
- Interrelation with other regulatory frameworks
- Guidance, workshops and SME support
- Identification of required underlying data
- ESG data provider selection
- Implementation



Contacts

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