

List of additional SFDR queries requiring the interpretation of Union law

Introduction

1. The European Supervisory Authorities (ESAs) have submitted to the European Commission further queries relating to the interpretation of Union law with reference to Regulation (EU) 2019/2088 (the Sustainable Finance Disclosure Regulation “SFDR”).¹

Queries related to interpretation of SFDR

Article 2(17) SFDR

Question 1: How does the definition of “sustainable investment” in Article 2(17) SFDR apply to investments in funding instruments that do not specify the use of proceeds, such as the general equity or debt of an investee company? For example, would an investment in an investee company which has one economic activity, among several other economic activities, that contributes to an environmental or social objective (and none of the economic activities significantly harm any environmental or social objective and the company follows good governance practices) be considered to be a “sustainable investment” as a whole or in part?

In other words, assume a financial market participant that invests EUR 100.000 in the general equity of an investee company which follows good governance practices. None of the investee company’s economic activities significantly harm any environmental or social objective, and that investee company reports that 20% of its economic activities contribute to environmental or social objectives. Can the financial market participant consider (1) the entire holding (EUR 100.000) as a “sustainable investment” according to Article 2(17) SFDR; or (2) only 20% of that holding (i.e. EUR 20.000) as a “sustainable investment” according to Article 2(17) SFDR?

Question 2: How should “investment in an economic activity that contributes to an environmental objective” or “investment in an economic activity that contributes to a social objective” in Article 2(17) SFDR be interpreted? Are any (or all) of the following features sufficient for an economic activity to

¹ Under the ESA Regulations (e.g. Regulation (EU) No 1095/2010) Article 16b(5)

meet the definition of Article 2(17) SFDR, i.e. to contribute to an environmental (or a social) objective?

- a) Should the economic activity being carried out by the investee company in itself contribute to an environmental or social objective (for example, an issuer investing in micro-finance activities in the developing world to assist in the development of socially disadvantaged communities)?; and/or
- b) Can any economic activity potentially contribute to an environmental or social objective simply because it is carried on in a sustainable manner by the investee company (examples: (1) an investee company manufacturing a product in a more environmentally sustainable way than its peers/the sector, or (2) an undertaking that stands out for its social impact, for instance through its HR management or the representation of women); and/or
- c) Can any economic activity contribute to the general environmental objective of climate change mitigation if it is only covered by a transition plan (for instance a plan aiming to reach climate-neutrality based on the ACT methodology)?

More generally, can any economic activity contribute to an environmental or a social objective solely because the company that carries out such an activity makes commitments towards, or adopts a strategy aiming at, reducing its environmental or social harm (referring for instance to the SBTi methodology)?

Finally, where there is a transition plan or strategy aiming to achieve that the whole investment does not significantly harm any environmental and social objectives (without actively contributing to environmental or social objectives), could that investment be considered “sustainable” under Article 2(17) SFDR?

Article 9(3) SFDR, carbon emissions reductions and other benchmark questions

Question 3: From Article 9(3) SFDR and the Commissions Q&A answer regarding this article in July 2021 (which outlined the principle that SFDR is neutral in terms of product design), is it correct to consider that financial products that have an Article 9(3) objective of reduction in carbon emissions can be either products with a passive or active investment strategy? If financial products with an active investment strategy can be financial products that have reduction in carbon emissions as their objective under Article 9(3) SFDR, are there any specific requirements they should meet when they have designated an index as a reference benchmark?

Question 4: Can a financial product “promote” carbon emissions reduction as an “environmental characteristic”, as opposed to having it as an “objective”? In other words, can a financial product disclose carbon emissions reduction as an environmental characteristic under Article 8 SFDR, or should any financial product which targets carbon emissions reduction as a feature always be considered to be having “carbon emissions reduction” as an “objective” and therefore be required to disclose the information required by Article 9(3) SFDR? In this example, if the financial product

is considered an Article 8 SFDR product, what would be the criteria to differentiate it from an Article 9 SFDR product?

Question 5: Can financial products with a passive investment strategy which designate as a reference benchmark either a Paris Aligned Benchmark or (from 1 January 2023) a Climate Transition Benchmark automatically be deemed to fulfil the conditions of Article 9(3) SFDR in conjunction with Article 2(17) SFDR?

Likewise, can financial products with an active investment strategy focused on carbon emissions reduction be deemed to satisfy the conditions of Article 9(3) SFDR in conjunction with Article 2(17) SFDR where they apply the same requirements (regarding portfolio composition, etc.) as those applied by PAB and CTB pursuant to BMR framework and in particular Delegated Regulation 2020/1818?

PAI consideration

Question 6: What is the meaning of “consider” in Article 7(1)(a) SFDR? Could “consideration” of principal adverse impacts by a financial product mean that a financial product only discloses the relevant principal adverse impacts of the investments, for example total greenhouse gas emissions, or does “consideration” require action taken by the financial market participant to address the principal adverse impacts of the product’s investments, such as engagement with investee companies, and are there any minimum criteria for such actions?

500 employee PAI threshold

Question 7: For the purpose of Articles 4(3)-4(4) SFDR, should “the average number of 500 employees” be understood to include workers who are assigned to the FMP even though they are employed by a third party that invoices their services back to the FMP, e.g. interim workers or workers that are employed by other organisations within a group for instance as part of shared-service centres? Furthermore, can the exemption in Article 23(5) of the Accounting Directive (2013/34/EU), which grants Member States the right to exempt parent companies that are themselves the subsidiary of a larger group from drawing up consolidated financial statements and a consolidated management report under that Directive, apply to a “parent undertakings of a large group” referred to in Article 4(4) SFDR?

Periodic disclosure frequency for portfolio management services

Question 8: The frequency of periodic reports in case of portfolio management services is determined by Article 11(2)(i) SFDR, which refers to Article 25(6) of Directive 2014/65/EU. Article 60 of Commission Delegated Regulation (EU) 2017/565 provides the details of the periodic reporting requirements for portfolio management services including their frequency. Based on that text, this

reporting should be provided quarterly, with certain exceptions. However, Recital 21 of SFDR states that “...*Those disclosures by means of periodic reports should be carried out annually*”. Considering all the above, should FMPs in scope provide a quarterly (with exceptions according to Article 60 of Regulation 2017/565) periodic report based on the SFDR templates for portfolio management, or can the FMPs use one of the quarterly reports to present a yearly report based on the SFDR templates for portfolio management?