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ANNEX

**Question related to 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 (Sustainable Finance Disclosure Regulation 2019/2088)**

**ESA:** ESMA, EIOPA and EBA

**Question ID:**

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** points (1) and (4) of Article 2

**1. Question**

Does Regulation (EU) 2019/2088 (SFDR) apply to registered (sometimes referred to as sub-threshold) AIFMs referred to in Article 3(2) AIFMD?

**2. Answer**

It follows from points (1) and (4) of Article 2 Regulation 2019/2088 that for the purposes of the Regulation a ‘financial market participant’ comprises an ‘alternative investment fund manager’, as defined in point (b) of Article 4(1) of Directive 2011/61/EU<sup>1</sup>, including those which have their registered office in a Member State (EU AIFMs) and those which have their registered office in a third country (non-EU AIFMs). Directive 2011/61/EU lays down the conditions under which a non-EU AIFM, i.e. an AIFM from a third country, may carry out its activities within the Union. Given the absence of the activation of the AIFM third country passport under Article 67(4) and (6) of that Directive, access to end investors in individual Member States may be on the basis of national laws set out in National Private Placement Regimes. Where an AIFM from a third country enters the market of a given Member State by means of a National Private Placement Regime, that AIFM must ensure compliance with Regulation 2019/2088, including the financial product related provisions.

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<sup>1</sup> Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers (OJ L 174, 1.7.2011, p. 1).

**ESA:** ESMA, EIOPA and EBA

**Question ID:**

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** point (4) of Article 2, Article 17, points (a), (d) and (e) of Articles 6(3) and points (a), (d) and (e) of Article 11(2)

## **1. Question**

Does Regulation (EU) 2019/2088 (SFDR) apply to non-EU AIFMs, for example when they market a sustainable EU Alternative Investment Fund under a National Private Placement Regime?

## **2. Answer**

The reference in point (4) of Article 2 of Regulation 2019/2088 to point (b) of Article 4(1) of Directive 2011/61/EU means that ‘financial market participant’ also comprises AIFMs subject to registration referred to in point (a) of Article 3(3) of Directive 2011/61/EU.

Article 17 of Regulation 2019/2088 on exemptions from that Regulation and any other provision in that Regulation, lay down neither exemptions nor derogations from obligations under that Regulation for AIFMs subject to registration referred to in point (a) of Article 3(3) of Directive 2011/61/EU.

In consequence, entity and financial product related requirements of Regulation 2019/1088 apply to such AIFMs.

Since disclosures to investors referred to in Article 23(1) of Directive 2011/61/EU and annual reports referred to in Article 22 of Directive 2011/61/EU, as referred to in point (a) of Articles 6(3) and point (a) of Article 11(2) of Regulation 2019/2088 respectively do not apply to AIFMs subject to registration referred to in point (a) of Article 3(3) of Directive 2011/61/EU, such AIFMs should apply those provisions by analogy, i.e. information is to be included in pre-contractual and periodic documentation made available to end investors under national law.

Managers of qualifying venture capital funds and qualifying social entrepreneurship funds registered in accordance with Article 14 of Regulation (EU) No 345/2013 or Article 15 of Regulation (EU) No 346/2013 must include the relevant information in documents referred to in points (d) and (e) of Articles 6(3) and points (d) and (e) of Article 11(2) of Regulation 2019/2088 respectively.

**ESA:** ESMA, EIOPA and EBA

**Question ID:** not available

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** Article 4(3), Article 4(4), point (a) of Article 4(1)

## 1. Question

As regards Article 4(4) of Regulation 2019/2088, must the calculation of the 500-employee threshold to the parent undertaking of a large group be applied to both EU and non-EU entities of the group without distinction as to the place of establishment of the group and/or subsidiary and does the due diligence statement include impacts of the parent undertaking only or must it include the impacts of the group at a consolidated level?

## 2. Answer

### The “comply or explain mechanism”

The underlying objective of Article 4 of Regulation 2019/2088 is to encourage financial market participants to pursue more sustainable investment strategies in terms of reducing negative externalities on sustainability caused by their investments. The compliance with disclosure requirements under Article 4 should incentivise the interest in investing in activities that do not harm environment or social justice, curb greenhouse gas emissions of their investments, stimulate investee companies to transition away from unsustainable activities and improve their environmental impacts or and even induce portfolio adjustments and divest from investments in activities that are harmful to sustainability. Article 4 also encourages financial advisers to pay more attention to how the consideration of negative externalities is integrated in their investment or insurance advice.

This is why the “comply or explain mechanism” under Article 4(1) of Regulation 2019/2088 distinguishes between ‘*principal* adverse impacts’ and ‘adverse impacts’.

Whilst the “comply mechanism” under point (a) of paragraph 1 encompasses the consideration of *principal* adverse impacts of investment decisions, financial market participants that decide not to apply the “comply mechanism”, must under point (b) of that paragraph that establishes “explain mechanism”, provide clear reasons for why they do not consider ‘adverse impacts’ of investment decisions on sustainability factors. Under point (b), by way of example, financial market participants must provide clear reasons for why they do not consider degradation of the environment or social injustice caused by their investments.

The aim of Article 4(3) and (4) of Regulation 2019/2088 is to introduce a more stringent “disclosure mechanism” and reduce a hypothetical incidence of application of “explain mechanism”. Large financial market participants, on solo or group basis, as specified in those two paragraphs of Article 4, must publish and maintain on their websites statements on their due diligence policies with respect

to the *principal* adverse impacts of investment decisions on sustainability factors, i.e. in other words that and how they consider *principal* adverse impacts.

### **The 500-employee criterion**

The 500-employee criterion, as laid down in Article 4(3) of Regulation 2019/2088, relates to a financial market participant.

The 500-employee criterion as laid down in Article 4(4) of Regulation 2019/2088 relates to the large group, as referred to in Article 3(7) of Directive 2013/34/EU<sup>2</sup>, in its entirety; the calculation of the headcount takes into account the number of employees of a parent undertaking and of subsidiary undertakings regardless whether they are established inside or outside the Union. Article 4(4) of Regulation 2019/2088 sets out obligations on financial market participants that are parent undertakings which in that capacity, set the group wide policies, including due diligence policies. Therefore, such financial market participants publish and maintain the requested information, adapted to the specific situation of the parent undertaking and not to the group as a whole. The criterion of a group is just relevant for the headcount that triggers the reporting obligations by a financial market participant.

Subsidiary undertakings might still qualify as financial market participants subject to Article 4(3) or might be financial market participants that consider principal adverse impacts of investment decisions on sustainability factors as described in point (a) of Article 4(1) of Regulation 2019/2088.

**ESA:** ESMA, EIOPA and EBA

**Question ID:** not available

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** Article 9

### **1. Question**

Must a product to which Article 9(1), (2) or (3) of Regulation (EU) 2019/2088 applies only invest in sustainable investments as defined in Article 2(17) SFDR? If not, is a minimum share of sustainable investments required (or would there be a maximum limit to the share of “other” investments)?

Where an EU Climate Transition Benchmark (EU CTB) or EU Paris-aligned Benchmark (EU PAB) exists, is it necessary for a product to track an EU PAB or an EU CTB on a passive basis for Article 9(3) of Regulation (EU) 2019/2088 to apply to it?

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<sup>2</sup> Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ L 182, 29.6.2013, p. 19).

If the questions above are answered in the affirmative and if the minimum standards of an EU PAB or an EU CTB do not require the index components to be sustainable investments, can the product fall within the scope of Article 9(3) of Regulation (EU) 2019/2088?

## **2. Answer**

Recital 21 to Regulation (EU) 2019/2088 makes it clear that sustainable financial products with various degrees of ambition as to “sustainability” have been developed to date. Accordingly, where such financial products do not have ‘sustainable investment’ as their objective, as referred to in Article 9, they are considered to fall under Article 8.

Article 8 and Article 9 of Regulation 2019/2088 are two distinct product categories: financial products that promote environmental or social characteristics or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices, and financial products which have sustainable investment as their objective respectively.

The two distinct product categories are key to determine the access of end investors to financial products that are ambitious enough to meet their sustainability preferences.

### **Design of financial products subject to Article 9**

A financial product to which Article 9(1), (2) or (3) of Regulation (EU) 2019/2088 applies may invest in a wide range of underlying assets, provided these underlying assets qualify as ‘sustainable investments’, as defined in point 17 of Article 2. Article 5 and Recital 19 to Regulation (EU) 2020/852<sup>3</sup> also clarify that ‘sustainable investments’ include investments into ‘environmentally sustainable economic activities’ within the meaning of that Regulation.

A financial product, in order to meet requirements in accordance with prudential, product-related sector specific rules may next to ‘sustainable investments’, also include investments for certain specific purposes such as hedging or liquidity which, in order to fit the overall financial product’s sustainable investments’ objective, have to meet minimum environmental or social safeguards, i.e. investments or techniques for specific purposes must be in line with the sustainable investment objective. Since Article 9 of Regulation (EU) 2019/2088 remains neutral in terms of the product design, or investing styles, investment tools, strategies or methodologies to be employed or other elements, the product documentation must include information how the given mix complies with the ‘sustainable investment’ objective of the financial product in order to comply with the “no significant harm principle” of Article 2(17) of Regulation (EU) 2019/2088.

### **The objective of ‘a reduction in carbon emissions’**

By virtue of Article 9(3) of Regulation (EU) 2019/2088, the objective of ‘a reduction in carbon emissions’ is a specific category of ‘sustainable investment’ and, consequently, must comply with point 17 of Article 2.

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<sup>3</sup> 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 (OJ L 198, 22.6.2020, p. 13).

The first subparagraph of Article 9(3) of Regulation (EU) 2019/2088 lays down that the objective of ‘a reduction in carbon emissions’ includes the objective of low carbon emission exposure in view of achieving the long-term global warming objectives of the Paris Agreement. The second subparagraph takes into consideration two situations, namely where an EU Climate Transition Benchmark or EU Paris-aligned Benchmark does not exist and where an EU Climate Transition Benchmark or EU Paris-aligned Benchmark exists:

1. where an EU Climate Transition Benchmark or EU Paris-aligned Benchmark does not exist, the pre-contractual information must include a detailed explanation of how the continued effort of attaining the objective of reducing carbon emissions is ensured in view of achieving the long-term global warming objectives of the Paris Agreement;
2. where an EU Climate Transition Benchmark or EU Paris-aligned Benchmark exists, a financial product must be tracking these.

It follows from Article 9(3) of Regulation (EU) 2019/2088 that the implementation of minimum standards, as laid down in Commission Delegated Regulation (EU) 2020/1818,<sup>4</sup> by benchmark administrators, for the construction of EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks, must ensure compliance with point 17 of Article 2 of Regulation (EU) 2019/2088. The two EU Climate Benchmarks include as minimum standard the reduction of carbon emissions from one year to the other and the reduction of GHG intensity compared to a parent benchmark. The respective requirements of Regulation (EU) 2016/1011 must, therefore, be applied in conjunction with Regulation (EU) 2019/2088, in particular point 17 of Article 2.

**ESA:** ESMA, EIOPA and EBA

**Question ID:** not available

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** Article 8

## 1. Question

In terms of Article 8 of Regulation (EU) 2019/2088, can the name of a product, which may include words like “sustainable”, “sustainability”, or “ESG” be considered to qualify a product to be promoting an environmental or social characteristic or to be having sustainable investment as its objective?

While a financial product to which Article 8 of Regulation (EU) 2019/2088 applies does not need to explicitly promote itself as targeting sustainable investments (within the meaning of Article 2(17) of

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<sup>4</sup> Commission Delegated Regulation (EU) 2020/1818 of 17 July 2020 supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks (OJ L 406, 3.12.2020, p. 17).

Regulation (EU) 2019/2088), would a reference to taking into account a sustainability factor or sustainability risk in the investment decision be sufficient for Article 8 of Regulation (EU) 2019/2088 to apply? If the answer is yes, how can financial market participants that disclose mandatory information according to Article 6(1) or Article 7(1) of Regulation (EU) 2019/2088 ensure that this is not automatically considered as “promoting environmental or social characteristics”.

Must a product to which Article 8 of Regulation (EU) 2019/2088 applies invest a minimum share of its investments to attain its designated environmental or social characteristic in order to be considered to be promoting environmental or social characteristics?

In the absence of active advertising of an environmental or social characteristic of the product, would an intrinsic characteristic of the product, such as a sectoral exclusion (e.g. tobacco) which is not advertised, also qualify as “promotion”?

In addition, would complying with a national legal obligation, which applies to the financial market participant, such as a ban on investment in cluster munitions, also bring the product into the scope of Article 8 of Regulation (EU) 2019/2088?

## **2. Answer**

Recital 21 to Regulation (EU) 2019/2088 makes it clear that sustainable financial products with various degrees of ambition as to “sustainability” have been developed to date. Accordingly, where such financial products do not have ‘sustainable investment’ as their objective, as referred to in Article 9, they are considered to fall under Article 8 of Regulation (EU) 2019/2088.

Article 8 and Article 9 of Regulation (EU) 2019/2088 are two distinct product categories: financial products that promote environmental or social characteristics or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices (hereinafter ‘financial products that promote environmental or social characteristics’), and financial products which have sustainable investment as their objective respectively.

The two distinct product categories are key to determine the access of end investors to financial products that are ambitious enough to meet their sustainability preferences.

Article 8 of Regulation (EU) 2019/2088 lays down transparency rules for financial products that have a sustainability-related ambition lower than the ambition of financial products subject to Article 9. Where a product has an environmental objective and does not meet the do not significant harm as referred to in Article 2(17) of Regulation (EU) 2019/2088, qualifies as Article 8 product.

Like Article 9 of Regulation (EU) 2019/2088, Article 8 of that Regulation addresses a potential issue of greenwashing by financial products, i.e. conveying a false impression, or providing misleading information about how a financial product is performing in terms of ESG sustainability.

### **Environmental or social characteristics**

Article 8 of Regulation (EU) 2019/2088 remains neutral in terms of design of financial products. It does not prescribe certain elements such as the composition of investments or minimum investment

thresholds, the eligible investment targets, and neither does it determine eligible investing styles, investment tools, strategies or methodologies to be employed.

Therefore, nothing prevents financial products subject to Article 8 of Regulation (EU) 2019/2088 not to continue applying various current market practises, tools and strategies and a combination thereof such as screening, exclusion strategies, best-in-class/universe, thematic investing, certain redistribution of profits or fees. Certainly, many of those market practises, tools and strategies are also available to financial products subject to Article 9 of Regulation (EU) 2019/2088, provided the investments qualify as ‘sustainable investments’, as defined in point 17 of Article 2 of Regulation (EU) 2019/2088.

Financial products that fall under Article 8 may pursue reduction of negative externalities caused by the underlying investments, such as principal adverse impacts on sustainability factors referred to in point (a) of Article 7(1) of Regulation (EU) 2019/2088. In addition, as confirmed by Article 6 of Regulation 2020/852, nothing prohibits financial products that fall under Article 8 to be, in part, invested in ‘sustainable investments’ as defined in point 17 Article 2 of Regulation (EU) 2019/2088. On the other hand, integration per se of sustainability risks, as defined by point 22 of Article 2 of Regulation (EU) 2019/2088, is not sufficient for Article 8 to apply.

#### **Promotion of environmental or social characteristics**

Article 8 means that where a financial product complies with certain environmental, social or sustainability requirements or restrictions laid down by law, including international conventions, or voluntary codes, and these characteristics are “promoted” in the investment policy the financial product is subject to Article 8 of Regulation (EU) 2019/2088.

The term ‘promotion’ within the meaning of Article 8 of Regulation (EU) 2019/2088 encompasses, by way of example, direct or indirect claims, information, reporting, disclosures as well as an impression that investments pursued by the given financial product also consider environmental or social characteristics in terms of investment policies, goals, targets or objectives or a general ambition in, but not limited to, pre-contractual and periodic documents or marketing communications, advertisements, product categorisation, description of investment strategies or asset allocation, information on the adherence to sustainability-related financial product standards and labels, use of product names or designations, memoranda or issuing documents, factsheets, specifications about conditions for automatic enrolment or compliance with sectoral exclusions or statutory requirements regardless of the form used, such as on paper, durable media, by means of websites, or electronic data rooms.

Moreover, financial products in their pre-contractual disclosures must refer to those elements which relate to their environmental and/or social characteristics binding during the whole holding period and which are used for the description of the extent to which environmental or social characteristics are met, as referred to in point (a) of Article 11(1) of Regulation (EU) 2019/2088.

**ESA:** ESMA, EIOPA and EBA

**Question ID:** not available

**Regulation reference:** Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services

**Topic:** sustainable finance disclosures

**Article:** point 12 of Article 2, Article 10

## 1. Question

Regulation (EU) 2019/2088 applies to financial market participants and financial advisers. In particular, in respect of investment firms as defined in point (l) of Article 4(1) of Directive 2014/65/EU, Article 2(1)(b) of Regulation (EU) 2019/2088 defines ‘an investment firm which provides portfolio management’ as one of the financial market participants to which it applies and Article 2(11)(d) of Regulation (EU) 2019/2088 defines ‘an investment firm which provides investment advice’ as one of the financial advisers to which it applies.

For portfolios, or other types of tailored financial products managed in accordance with mandates given by clients on a discretionary client-by-client basis, do the disclosure requirements in SFDR apply at the level of the portfolio only or can they apply at the level of standardised portfolio solutions?

If the disclosure requirements of Regulation (EU) 2019/2088 apply at the portfolio level, how is it possible to maintain confidentiality obligations to the client in view of the disclosures required, especially the website disclosures required by Article 10 of Regulation (EU) 2019/2088?

## 2. Answer

The definition of ‘financial product’ in point 12 of Article 2 of Regulation (EU) 2019/2088 makes no distinction whether the products are tailored to specific preferences or requirements of end investors, or not.

Transparency of the promotion of environmental or social characteristics and of sustainable investments on websites in accordance with Article 10 of Regulation (EU) 2019/2088 must ensure compliance with Union and national law governing the data protection, and where relevant, also ensure confidentiality owed to clients. Where a financial market participant makes use of standardised product solutions, transparency of those solutions might be a way for complying with requirements on website disclosures laid down by Regulation (EU) 2019/2088.