SFDR REVIEW

PROPOSALS OF THE FRENCH FINANCIAL ASSOCIATIONS

AMAFI, FBF and AFPDB welcome the considerable work undertaken by the co-legislators to establish a clearer and more workable framework for sustainable products through the revision of the Sustainable Finance Disclosure Regulation (SFDR).

As the European Parliament prepares to finalise its position ahead of the trilogue negotiations, there are still some important issues though that remain to be addressed to ensure the revised framework remain sufficiently simple, coherent and operational for market participants.

Aiming for simplicity (I.), ensuring that the PRIIPs KID of products outside the scope of SFDR remain meaningful to investors (II.) and maintaining clear differentiation between the three SFDR product categories (III.) should remain key priorities throughout the negotiations.

Moreover, it is important to ensure that ESG-related naming is not limited to SFDR products (IV.).

These priorities are essential to achieving the review's overarching objectives: providing retail investors with clear and meaningful information, while ensuring that the framework remains proportionate and workable for manufacturers and distributors across different product types.

Against this background, the Associations would like to share a few proposals which, in their view, would further strengthen the effectiveness of the final framework while preserving the overall balance of the compromise reached by the co-legislators.

I. SIMPLIFICATION SHOULD REMAIN A GUIDING PRINCIPLE

The review of SFDR was launched because the existing framework had become too complex, too difficult to interpret and increasingly inconsistent across Member States.

As negotiations have progressed, successive compromise texts have naturally sought to accommodate a broad range of policy priorities and stakeholder views. While this has strengthened certain aspects of the framework, it has also introduced additional layers of detail, exceptions and eligibility conditions, moving away from the simplicity originally sought.

As regards in particular sustainability categories, detailed exclusion criteria with multiple exceptions[1] and cumulative conditions have substantially increased the complexity of the categories, moving away from the simplicity of the Commission's original approach.

The Associations call for striving to preserve this simplicity, as a framework that is easier to understand, implement and supervise will ultimately strengthen investor confidence in sustainable finance and contribute to investments in sustainable assets.

II. PRIIPS' KIDS SUSTAINABILITY DISCLOSURES SHOULD BE MEANINGFUL TO INVESTORS

The Associations support the objective of ensuring that retail investors receive clear, reliable and comparable sustainability information to help them make informed investment decisions.

[1] *"(b) they exclude investments in companies as referred to in Article 12(1), points (a), (b), and (d) of Commission Delegated Regulation (EU) 2020/1818,*
(c) they exclude investments in companies that derive revenues from the exploration, extraction, mining or refining of hard coal and lignite, oil fuels or gaseous fuels, unless such companies:
(i) allocate at least 20% of their total capital expenditure to Taxonomy-aligned activities;
(ii) allocate, over a rolling three-year period, a higher average proportion of their total capital expenditure to Taxonomy-aligned activities than to activities that develop new projects for the exploration, extraction, mining or refining of hard coal and lignite, oil fuels or gaseous fuels; and
(iia) ensure, over a rolling three-year period, a decrease of allocation of capital expenditure on activities that develop new projects for the exploration, extraction, mining or refining of hard coal and lignite, oil fuels and gaseous fuels by 10 percentage points until it reaches zero; and
(iib) have in place a time-bound and measurable strategy to reduce their Scope 1 and Scope 2 greenhouse gas emissions, compatible with the limiting of global warming in line with the Paris Agreement; and
(iic) where hard coal or lignite is used for power generation, have a time-bound and measurable plan to phase-out from the exploration, mining, extraction, refining or exploitation of hard-coal or lignite
(ca) they exclude investments in companies that are involved in severe human rights and humanitarian law abuses which have not been effectively addressed and remediated in accordance with the OECD Guidelines for Multinational Enterprises and UN Guiding Principles on Business and Human Rights." (European Parliament's 6th compromise text amending Regulation (EU) 2019/2088 and Regulation (EU) No 1286/2014, Art. 7).

Against this background, we suggest qualifying the EP ECON's proposed PRIIPs' KID statement indicating "*that the financial product is not categorised under the EU standards for defining sustainable financial products*" when a product is not categorised as a sustainability-related product under SFDR[2].

The proposed disclosure would apply to all PRIIPs outside the SFDR categorisation framework, including products that make no sustainability-related claims. This appears disproportionate as such information are not material to the investment decisions of investors who are not seeking sustainable investments.

More fundamentally, such a statement would only be appropriate if the scope of SFDR matched that of the PRIIPs Regulation. This is not the case. The co-legislators deliberately limited the review to financial products already covered by SFDR, considering that the time available did not allow for extending the framework to all PRIIPs that may incorporate sustainability characteristics. The proposed statement would therefore primarily reflect whether a product falls within the scope of SFDR rather than its actual sustainability characteristics. This is particularly problematic because, in any case, PRIIPs that fall outside the scope of SFDR could never qualify as sustainability-related financial products under that Regulation, even if they met its requirements. The proposed wording therefore risks creating an artificial hierarchy between products based on their regulatory status rather than their underlying sustainability characteristics.

Some non-SFDR products may indeed incorporate robust sustainability characteristics or provide exposure to sustainable assets, like SFDR products. This is notably the case for structured investment products, which are outside the scope of SFDR, even though they may provide exposure to the same sustainable assets or investment strategies as SFDR products. For example, a structured product whose underlying is consistent with Article 9 "Sustainable" would still have to state that it "*is not categorised under the EU standards for defining sustainable financial products*". **This statement could easily lead retail investors to believe that the product is not sustainable, whereas it simply reflects the fact that SFDR does not apply to that type of product. Such an approach raises serious concerns in terms of the level playing field between retail products, in relation to sustainability.**

The Associations therefore suggest removing this mandatory statement.

Should the co-legislators nevertheless consider that a clarification remains appropriate, the Associations believe that the Council's approach (see below) offers a more proportionate alternative. It allows products outside the scope of SFDR to continue communicating, where relevant, about their environmental or social characteristics, while simply clarifying that they are not in the scope of SFDR. This approach accurately reflects the regulatory status of such products, provides clear information to retail investors and avoids introducing unnecessary competitive distortions between products based solely on whether they fall within the scope of SFDR.

[2] EP ECP's proposed amendment Article 8 paragraph 3 of Regulation (EU) No 1286/2014 "[…] *for a PRIIP that is not a sustainability-related financial product as defined in Article 2, point (25), of Regulation (EU) 2019/2088, under a section titled 'How sustainable is this product?', a statement confirming that the financial product is not categorised under the EU standards for defining sustainable financial products;"*

"Article 8 of Regulation (EU) No 1286/2014 is amended as follows:

(cb) for a PRIIP that does not fall under the scope of Regulation (EU) 2019/2088, any information on whether and how it considers sustainability factors or contributes to a sustainability objective shall be accompanied by the following statement: "This financial product does not fall under the scope of Regulation (EU) 2019/2088 and thus cannot be categorised as sustainability-related financial product under that Regulation."

However, stating that products falling outside the scope of SFDR "*cannot be categorised as sustainability-related products"* may still be interpreted as implying that such products are inherently less sustainable than products within the scope of SFDR. When presented alongside information on their environmental or social characteristics, such a statement may be particularly confusing for retail investors, as it does not clearly distinguish between the regulatory scope of SFDR and the sustainability characteristics of the product itself. We therefore suggest a technical amendment to the proposed Article 8 of Regulation (EU) No 1286/2014to clarify that non-SFDR products are not subject to the SFDR categorisation:

*"(cb) for a PRIIP that does not fall under the scope of Regulation (EU) 2019/2088, any information on whether and how it considers sustainability factors or contributes to a sustainability objective shall be accompanied by the following statement: "This financial product does not fall under the scope of Regulation (EU) 2019/2088 and thus **is not** ~~**cannot be**~~ categorised ~~**as sustainability-related financial product**~~ under that Regulation."*

III. THE THREE SFDR CATEGORIES SHOULD REMAIN CLEARLY DIFFERENTIATED

The value of the new categorisation framework lies in its ability to enable investors to distinguish clearly between products reflecting different levels of sustainability ambition. To achieve this objective, the three categories must remain clearly distinct.

As the negotiations have progressed, however, the requirements relating to contribution criteria, exclusions and safeguards have become increasingly similar, making the distinction between the categories less apparent[3].

This is of particular concern because the SFDR categories are to become the reference for sustainability preferences under MiFID II. Distributors will need to explain the different categories to clients in a simple and consistent manner so that they can make informed choices. If the distinctions between the categories become too complex or too subtle, this objective will be undermined, potentially recreating some of the difficulties encountered with the current Articles 8 and 9.

[3] For example, the PAI requirements show significant similarities across the three categories. Articles 7, 8 and 9 all require disclosure of GHG emissions and fossil fuel exposure. Articles 7 and 9 are particularly similar, as both also require at least one additional PAI relevant to the product's transition or sustainability objective. Additionally, Article 8 expressly allows investments pursuant to Article 7(2) or Article 9(2) to count towards its own category contribution threshold. The ESG Basics category can therefore be built partly from investments that already qualify under the Transition or Sustainable categories, which mechanically reduces differentiation between the three categories.

Clear differentiation is also necessary to ensure that products belonging to different categories are different from each other in substance and not only formally. This is essential to allow a broad range of sustainable investment solutions reflecting different investment strategies and to support innovation.

The Associations therefore encourage the co-legislators to preserve a clear distinction between Articles 7, 8 and 9, ensuring that the categorisation framework remains intuitive for investors while supporting a diverse and competitive European sustainable finance market.

IV. NON- SFDR PRODUCTS SHOULD BE ALLOWED TO USE SFDR CATEGORY DENOMINATIONS WHERE THEY COMPLY WITH EQUIVALENT INVESTMENT REQUIREMENTS

The Associations strongly recommend allowing financial products that fall outside the scope of SFDR, but incorporate sustainability features, to use the denominations of the three SFDR categories ("Transition", "Sustainable" and "ESG Basics"), provided that they comply with investment requirements equivalent to those applicable to the corresponding SFDR category.

The use of sustainability denominations should depend on the investment characteristics of the product and the requirements it complies with, rather than on whether the product formally falls within the scope of SFDR. **The same denomination should convey the same meaning to investors, irrespective of the legal or regulatory wrapper of the product.**

The objective should therefore be to ensure that **products complying with equivalent sustainability investment requirements can be presented to investors using the same terminology**. This would provide investors and advisers with one common European language for sustainable financial products, improve comparability and avoid the unnecessary proliferation of different sustainability concepts for products pursuing equivalent investment strategies. This approach is also necessary to ensure a level playing field across financial products.

At the same time, access to SFDR category denominations must not provide non-SFDR products with a competitive advantage. It should therefore be **strictly conditional on demonstrable compliance with investment requirements equivalent to those imposed on products within the relevant SFDR category**. In other words, the same denomination should be subject to the same substantive investment conditions and supervisory framework.

The final Level 1 text should therefore expressly allow products outside the formal scope of SFDR to use the relevant SFDR category denomination where they meet these equivalent investment requirements. This principle should preferably be established in an article and, at a minimum, be clearly recognised in a recital.