

## SFDR REVIEW



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## SFDR, a tempered shift towards simplification

Since March 2021, the European Union has been a pioneer, leading the way in the development of global sustainable finance, implementing the Sustainable Finance Disclosure Regulation (SFDR). The thesis of this regulation, a milestone in European financial regulation, was none other than promoting and encouraging sustainable investments as a starting point for the transformation of the existing economic models in Europe into more environmental, social and governing-friendly ones (ESG). The aim is to channel capital and investment flows towards more sustainable products that would allow a transition towards a greener and more resilient economy.

To this end, the key aspect where regulation needed to focus was transparency and trust in sustainability, as these two characteristics determine the behavior of financial markets. Three targets were pursued: informing investors so that they could make more informed decisions about the sustainability of their investments; encouraging financial market players

to integrate ESG criteria into their investment decision-making processes; and at the same time, mitigating the risk of deception or greenwashing through standardised and strict disclosure that would also facilitate the comparison of financial products based on their sustainable features.

The SFDR had a huge challenge ahead. Years later, we can see that the pursued objectives have been partially achieved. The regulation has been a key instrument in increasing transparency and allowing investors to access data on sustainability risks and the adverse impacts of their investments. However, it has also resulted in high complexity. Therefore there is a lack of clarity for retail investors and it has added an operational burden for financial market participants.

For instance, the concepts of 'sustainable investment' under the SFDR and 'taxonomy-aligned investment' under the Taxonomy Regulation have generated interpretation difficulties. This same effect has been seen with the use of the regulation as an implicit labeling system for the quality (in terms of the level of sustainable investments) of investment funds (articles 8 and 9) for marketing purposes. When selling a fund to investors, many relevant factors come into play, but the name stands out as a way to effectively and succinctly convey the investment's purpose. Using the nomenclature of article 8 or 9 funds, which refer to disclosure requirements, is not the most appropriate from a commercial and societal understanding standpoint, for investors and their preferences when adopting ESG criteria for investment. We could also mention that the lack of clear criteria for the evaluation and disclosure of the sustainability of products has led to an increase in operational and administrative costs and has had indirect effects on underlying companies, especially those not directly subject to SFDR, but that must provide relevant information to investors. This has been one of the objectives of recent ESMA's guidance.

The recommendations to the European Commission (EC) are not simple. If Europe wants to continue leading in sustainable finance, as desirable and necessary as it is, it should undertake a process of regulatory simplification. In the process of revising SFDR, the Commission will also have to take into

account the foreseeable changes that will be introduced in other legislative pieces such as CSRD, CSDDD and the taxonomy regulation, after the publication of the new Omnibus Directive.

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simplification.**

This process should reduce the quantity and complexity of information through specific simplifications that do not imply a complete review of the regulation nor a renunciation of the principle of double materiality, but rather a lesser category of information for small and medium-sized companies with temporary deferrals of information. Additionally, the alignment of SFDR with the Taxonomy Regulation, CSRD, and other regulations is necessary to avoid inconsistencies. From the investor's perspective, it is necessary to address a product rating system based on clear and objective criteria that differentiate between sustainable and transitional products, as well as to advocate for sustainability indicators that evaluate environmental and social sustainability and even clarify the concept of sustainable investment to ensure uniform application.

The SFDR regulation has been a fundamental element in improving transparency in sustainable finance, but it still presents significant challenges in terms of applicability and clarity. It is necessary to simplify the framework that is already yielding positive results. Now is the time to perfect it, so that it strengthens investor protection, their preferences, and their knowledge, and also reduces the administrative burden on market participants, encouraging them to support greater growth in green finance with their efforts.



## SACHA SADAN

Director of ESG – Financial  
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### Navigating the complexities of sustainable finance

Last time I was at Eurofi, we were in the early stages of the Sustainability Disclosure Requirements (SDR) implementation. The FCA introduced this package to help consumers navigate the sustainable investment market, reduce greenwashing, and build trust. Opportunities for international compatibility were sought at every stage of the policymaking process. The framework includes an anti-greenwashing rule, labels, naming and marketing rules, simple consumer-facing disclosures and more detailed ongoing disclosures, as well as distributor requirements. Only products with specific sustainability goals as part of the investment objectives can qualify for an investment label – and the naming and marketing requirements mean that firms can't call their products 'sustainable' or 'impact' unless they are using a label.

There has been good progress made by firms to comply with the new rules, including many applications for changes to fund disclosures in order to use a label. We are now aware of over 100 funds intending to use labels. Firms are also amending their fund names and disclosures to meet our naming and marketing rules.

Investment products are however just one piece of the puzzle. As we transition to a net zero economy, financial

markets will increasingly want better information on how companies plan to adapt their business models, their operations and their products and services. And investors are telling us clearly that transition plans will provide this information.

We are strong supporters of the work of the ISSB to develop guidance on transition plans drawing from the Transition Plan Taskforce (TPT) framework. As securities regulators move forward with their respective regulatory regimes, alignment will be critical for easing costs and burdens on multinational firms. That is why we are engaging with the International Transition Plan Network (ITPN), the TPT's successor, and have been pleased to see the level of interest from our peers, including EFRAG. We encourage other authorities to engage with the Network in the interest of greater cooperation. For transition plans to be successful, they need to be internationally interoperable, so we hope to see a convergence in regulatory expectations. This consistency would support a regulatory environment which helps investors make more informed investment decisions, based on comparable information, while fostering competition and growth through reduced compliance costs.

Meeting the UK's net zero target will require a significant increase in transition capital, and we recognise the challenges and complexities for firms in structuring this kind of finance. The FCA is committed to ensuring the UK is globally competitive for raising transition capital and we support the UK government-commissioned Transition Finance Market Review (TMFR) which found that credible transition plans will be a valuable source of information about corporate strategy for providers of transition finance, when making decisions about capital allocation.

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**The FCA enjoys a close relationship with our European counterparts on sustainable finance.**

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Looking ahead, we know there is more work to be done domestically and by working with our international regulatory counterparts. First, we should welcome the positive feedback we received on our anti-greenwashing efforts; this is an area we continue to focus on to enable a well-functioning market. Second, an estimated 60% of the world is expected to adopt the

ISSB standards, and this adoption should happen in the UK this year. We welcome the cooperation between the ISSB and EFRAG to deliver greater interoperability. Third, following the government's announcement to bring ESG ratings into our perimeter, we are working to develop a proportionate risk-based regime for ESG rating providers in line with IOSCO recommendations which focus on good governance, transparency, managing conflicts of interest and proper systems and controls. This follows our support for the launch of an industry-led Code of Conduct for ESG data and ratings providers in 2023. Hong Kong has leveraged this code in the development of their own, while Japan and Singapore have similar initiatives. It's great to see the EU publishing ESG ratings regulation, setting a strong example for international collaboration and alignment on sustainability standards. Fourth, we will continue our important work on SDR labelling, ensuring funds using these labels genuinely meet the criteria for sustainability. Fifth, we are committed to raising standards for transition plan disclosures. These disclosures provide companies with the opportunity to back up their climate targets with clear implementation plans, which may serve as a useful tool for managing reputational and legal risks.

As sustainability matures and initiatives evolve into regulations, we'll continue to encourage and actively support increased international coordination and compatibility. At the FCA and IOSCO, we remain committed to listening and working closely with our fellow regulators to advance these efforts.



## DELPHINE DIRAT

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### SFDR: An opportunity to put the transition to Net Zero

#### Rethinking SFDR: The opportunity to align, simplify, and drive transition

The EU is a pioneer in sustainable finance, shaping the global agenda with key regulations such as the Sustainable Finance Disclosure Regulation (SFDR) and the EU Taxonomy. SFDR has brought greater transparency to the market, pushing asset managers to disclose sustainability-related information and helping institutional and retail investors make more informed choices.

Today, a majority of investment funds in EU fall under SFDR's Article 8 or 9, meaning they either integrate ESG factors or have sustainable investment objectives. This demonstrates the financial sector's alignment with sustainability goals and the growing importance of ESG considerations in investment strategies. However, the implementation of the SFDR has proved challenging with uncertainty around definitions and terms and evolving interpretations that have created instability, funds' requalifications and confusion.

The forthcoming SFDR review is an opportunity to refine the framework, ensure its coherence with other

sustainable finance regulations, and make strong choices that affirm EU's vision for sustainable finance, striking a balance between competitiveness and regulation that provides clear guidance for market participants.

#### Ensuring alignment with corporate reporting to ensure high-quality data

One of the biggest challenges of SFDR is its misalignment with corporate reporting requirements. As a result, asset managers often struggle to access reliable data from companies, leading them to rely on estimated data of varying quality.

To enhance the credibility and usability of SFDR, it is essential to align reporting requirements with the Corporate Sustainability Reporting Directive (CSRD) and ensure that the data asset managers need is effectively reported by companies. This will improve data quality, reduce reliance on estimates, and provide a more consistent framework for investors.

#### Clear ESG fund categories that fit all investment strategies

For SFDR to be effective, its fund categories must be clear, robust, and adaptable to different investment strategies. The framework should recognise the diversity of ESG investment approaches, ensuring that passive management strategies, which represent a significant portion of the ESG market, are adequately considered.

A revised SFDR should provide well-defined categories that reflect different levels of sustainability ambition while ensuring that all types of asset managers can contribute to financing the transition.

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**The SFDR review is a chance to ensure better data quality and clearer ESG fund categories.**

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#### A robust fund category that supports the transition to net zero

One of the key shortcomings of the current SFDR framework is that it does not fully capture the complexity of transition finance. A revised framework should introduce a dedicated category for funds that invest in high-emitting companies with credible transition plans.

Encouraging the inclusion of transition plans as a core criterion of this fund category would help integrate companies

that are actively working toward decarbonisation. A strategic and robust transition plan should be a key eligibility criterion, ensuring that asset managers can support businesses that are genuinely committed to net-zero objectives while avoiding greenwashing risks.

#### Robust minimum criteria without overly restrictive rules

To enhance credibility and prevent greenwashing, SFDR must establish minimum criteria that are both robust and enforceable. However, these criteria should not be so rigid that they prevent asset managers from applying the most relevant KPIs for their investment strategies.

It is crucial to test the proposed criteria with market participants before finalizing them, ensuring that they are practical and feasible. This process should also reflect the structure of the market, which is primarily composed of institutional investors, who require consistent and reliable standards to make long-term investment decisions. By engaging with the industry early in the process, regulators can ensure that the criteria are ambitious yet workable, allowing SFDR to be effective without becoming overly prescriptive.

It is also essential to provide visibility to market participants so they can anticipate the requirements of future fund categories, ensuring a smooth transition from existing Article 8 and 9 funds.

#### Conclusion

The SFDR review is a chance to refine the EU sustainable finance framework, ensuring better data quality, clearer ESG fund categories, and stronger support for transition finance.

Europe now has the chance to lead by example, reinforcing its position as the global standard-setter for sustainable finance while ensuring that regulation empowers rather than hinders market players.



## LAURENCE CARON-HABIB

Head of Public Affairs – BNP  
Paribas Asset Management

### SFDR Review must be a full part of the Commission's competitiveness compass

The adoption of the Sustainable Finance Disclosure Regulation (SFDR) was a major step in the move to a more sustainable economy with harmonised transparency requirements for all European ESG products. However, and despite several level 2 and 3 measures, there is a strong consensus that the current framework could be amended to further increase allocation of capital to a more sustainable economy.

The various reports published in 2024 on this review by the European Supervisory Authorities, ESMA and more recently by the Sustainable Finance Platform of the European Commission indicate that there is a general consensus on the introduction of new categories to replace the existing Article 8 & 9 classification and that existing reporting obligations should be substantially simplified. These proposals are going into the right direction provided that a number of crucial conditions are properly met.

First this review should be full part of the Competitiveness Compass of the European Commission. Primary objective should refer to the absolute necessity to ensure that EU financial

market participants benefit from a suitable framework that does not put them in a competitive disadvantage resulting from too complex, unclear and burdensome requirements, notably in terms of transparency obligations.

Second objective should be around the importance of end-clients being central in the whole European sustainable finance framework. These clients should have access to the right information on extra-financial matters when making their investment decisions. On one side, most of the information to be disclosed under the SFDR is of no use for them as too complex and detailed. On the other side, criteria at their disposal for their sustainable preferences are too technical as they refer to taxonomy, sustainable investments and consideration of Principal Adverse Impacts. This does not properly incentivize end-clients to select products with ESG/sustainable features.

In these conditions, the revision of the SFDR should be articulated around two main evolutions. First the introduction of new categories if designed to facilitate the identification of products that best suit the sustainable preferences of each client. And second the simplification of current reporting requirements with a focus on information that is of real use for end-investors.

Having three different categories seems to be the best approach for capturing most of the investors' money into ESG products. Main challenge is to reach the right balance between a categorization scheme that capture a sufficient number of investment products while requiring a minimum level of ambition in the ESG dimension of the product. For avoiding the adoption of niche categories, criteria retained for each category should take into account the reality of investments universes and types of products. Typically, limiting sustainable investments to assets with a minimum percentage of revenue/capex derived from taxonomy-aligned activities or similar approach would be too restrictive. Other methodologies to identify investments with a positive contribution should be permitted, while further harmonizing the sustainable investment definition. Otherwise the number of products offered in this category would be too limited.

For ensuring the required ambition, it is crucial to have clear, objective, scalable criteria and measurable indicators for each category. A too large third category would be counterproductive. It would result in a situation similar to the one observed today with the Article 8 classification that includes a too wide range of products. In addition, the criteria should be adapted to specific

cases, such as funds investing in private assets, funds of funds or funds replicating indices. Criteria should be decided by an ad hoc experts' committee to ensure this balance between ambition and reality.

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On simplification of transparency requirements, the number of mandatory indicators should be reduced and the current format of templates streamlined. Having a common set of a limited number of indicators for all products would provide the minimum information investors need in a harmonized way, for the sake of comparability between products. Additional information can be disclosed in a voluntary mode and according to the specificities of each product.

Last but not least, the SFDR review should be envisaged in full articulation with the Omnibus I evolutions. There should be full alignment between the indicators to be disclosed under the SFDR and those to be published by corporates, including on taxonomy reporting. Beyond the scope of indicators, the availability of data will also be a key topic for attention. It should be avoided that financial market participants are faced with a concerning lack of data and have no other alternative than further relying on external data providers. Transition periods with the new CSRD framework while SFDR has not been yet revised will be part of issues to be properly tackled.



## JULIA SYMON

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Advocacy – Finance Watch

### Foundations for simple, transparent and meaningful SFDR product categories

The Sustainable Finance Disclosure Regulation (SFDR) has played an important role in raising awareness and paving the way for the sustainable finance framework. However, the design of SFDR as a pure disclosure framework has quickly proven to have limits. As sustainable finance regulatory framework has expanded, concerns have emerged regarding legislative inconsistencies, flexibility left for defining key concepts and the misuse of product classifications as sustainability labels. Time has come to step back, reflect on the achievements and the limits of the SFDR and propose necessary legislative revisions.

As the Platform on Sustainable Finance (PSF) has published a long awaited report providing concrete recommendations to revise the SFDR, legislators should weigh their options in light of four competing objectives that the revision must achieve.

First, the revised framework should foster transparency to allow assessing the sustainability level of products. A consensus seems to appear on the need for a product categorisation scheme to reconcile the objective of financing sustainable activities with the support

of businesses in their transition. The lack of distinction between the two strategies is a major source of criticism of the current framework, which has led to confusion among investors. Development of two distinct product categories - a sustainability-focused and transition-focused category - is a fundamental step to promote transparency, prevent greenhushing and reduce greenwashing accusations.

Second, the revision of the SFDR should simplify the framework to make it easily understood and accessible for retail investors. In that context, greater transparency may compromise the objective of understandability. The current disclosures are perceived by retail investors as too complex and difficult to find. The new product categories and disclosures should therefore be more intuitive and focus on what retail investors may consider relevant.

Third, the legislators should ensure that the framework allows investors to express their sustainability preferences. In that respect, there may be more merit in creating a harmful product category, allowing investors to exclude “brown” investments from their portfolio, rather than introducing the do-not-significantly-harm (DNSH) category proposed by the PSF. A DNSH category will not enable an exhaustive distinction between harmful investments and neutral investments. While financial market participants may voluntarily categorise products under the “ESG collection” category, as proposed by the PSF, unclassified products will not necessarily be harmful. As a result, advisors could encourage retail clients to invest in unclassified products under the rationale that ESG considerations could be integrated, despite the fact that some of those product may also be harmful.

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**A revised SFDR should be understandable to retail investors and inclusive of impact investors.**

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Finally, an SFDR revision is an opportunity to accommodate for impact-driven investments. The integration of impact has been considered by the PSF, without recommending a separate category. There are several ways to integrate the notion of impact contribution, but the challenge to find a standardised definition of impact could restrict ambitions. The legislators should also bear in mind that such a niche category would mostly cover alternative investments inaccessible to retail

clients, leading to product availability limitations when considering client preferences. A separate impact product category would also create challenges in explaining it to retail investors, while a disclosure-based integration would simplify the categorisation scheme. In that context, introducing disclosures on impact contribution without introducing a separate category appears as the most adequate approach.

To conclude, striking a balance between transparency, simplicity, and investor preferences will be key to ensuring the effectiveness of the revised SFDR. However, the future Commission’s proposal should also take into account the ongoing discussion on the first omnibus package that introduces new thresholds defining the scope of the CSRD and the Taxonomy Regulation. Making disclosure of the Taxonomy alignment largely voluntary, as currently proposed by the European Commission, will inevitably affect functioning of a new SFDR framework. Without access to Taxonomy disclosures, financial market participants will face uncertainties on how to treat eligible economic activities for companies that would opt out of disclosing their taxonomy alignment. As a result, sustainable funds could rely on the notion of sustainable investment which could, as per the PSF proposal, focus on activities that are not (yet) covered by the Taxonomy. Asset managers may therefore divert their investments away from economic activities covered by the Taxonomy, which are deemed to contribute the most to EU environmental objectives. Ultimately, such an approach could increase the concentration risk in sustainable products due to the reduction of their investment universe.