AFM response to SFDR Call for Evidence

The AFM would like to take this opportunity to highlight main areas for simplification and burden reduction, for all stakeholders in the market, incl. market participants, distributors, and investors. Attached you may also find a letter co-signed by the AFM, BaFin and FMA (Annex II).

- **The revised framework should be <u>easy to understand</u> and <u>easy to implement</u> for all stakeholders. The creation of reliable, clear and enforceable regulatory product categories** serves both these needs and would constitute a great improvement.
- **The scope of categories should focus on <u>two</u> main categories with credible ESG ambitions: "sustainable" and "transition".** To keep the categorisation framework easy to implement and understand, categories should align with the overarching principles of the ESMA Guidelines on Fund Names. The categories should have clear minimum quality requirements, accompanied by related disclosure requirements (see annex I attached).
- **Categories should be based on objective minimum criteria enabling confidence in the market that a financial product claiming to be "sustainable" or "transition" deserves such claim.** This also enables investors and distributors to compare products belonging to the same category or across categories and supports an easy selection of appropriate products.
- **We see risks for investors in the policy proposal of a third "light" or "ESG collection" category.** We urge caution and careful consideration regarding the need for such a category. Meaningful minimum requirements would be necessary. The name of a potential third category should be duly tested with investors before being finally determined. They should be enabled to clearly understand the limited ambition of such a product. A catch-all category for products with only very limited ESG aspects and no clear sustainability characteristics should be avoided, such a category could lead to a replication of the misinterpretation issues we currently witness for SFDR art. 8.
- **An alternative, consumer- and industry-friendly approach, is to maintain the possibility for products that cannot meet requirements of a sustainable or transition product category, to showcase their ESG properties**. It should however, in marketing and disclosure, be very clear that these are not at the level of the respective product categories for the entire product.
- **For those products, we see merit for the regulatory framework to encourage disclosure of a % of alignment of the product with a sustainable or transition product category**. This would incentivise sustainable or transition investments even for products that cannot fully comply with a product category. In the case a third "light" category is introduced despite the risks mentioned above, meeting an x% of the "transition" or "sustainable" category could act as a floor for this category. This would also create consistency for the distribution of products.
- **We strongly advocate to introduce only a limited number of product categories (max 2-3), and refrain from the introduction of thematic categories.** Additional categories would create a new level of complexity and rules, which runs counter to the objective of simplification of the framework. SFDR itself does not restrict any thematic approach to a product nor does it prohibit any specific sector.
- **With regard to distribution, MIiFID and IDD requirements should be amended in line with the introduction of product categories.**
- **Finally, for the purposes of simplification and burden reduction, we point out the importance of SFDR disclosures for both professional and retail investment products.** Limiting scope to retail-focused products could have a knock-on effect in the SIVC, as many professional products feed into products that target non-professional investors. For those products this would substantially add to the difficulty to collect the necessary information for their disclosures to end-clients, increasing the complexity and burden for such products.

Annex I – Minimum quality and disclosure requirements proposal (AFM response to SFDR Call for Evidence)

Table 1:
In the table below we outline potential minimum quality requirements and accompanying disclosure requirements for a "transition" and a "sustainable" product category. We point out that most of these disclosure requirements are already requirements under the current SFDR and therefore do not constitute additional burden.

Minimum quality requirements	Minimum disclosure requirements (both precontractual and periodic annually)
Products with "transition" label	
- Product has objective to generate positive, measurable social or environmental impact alongside a financial return. - The investment strategy provides additionality through active management (i.e. engagement), and the products accordingly have an engagement strategy. - Apply exclusion criteria referred to in Article 12(1)(a)-(c) of Commission Delegated Regulation (EU) 2020/1818 [align with ESMA fund name GLs proposal]. - Investee companies have a credible transition plan (with short, medium, and long term targets). Where possible based on the CSDR standards.[1] Investee companies that do not yet have a plan in place should have one within two years of being part of the portfolio. - Product has transition targets in line with Paris (decarbonisation) and/or Kunming/Montreal agreements (biodiversity). - Product invests a minimum of 80% of AuM according to its sustainability strategy.	- Report (y-o-y) on negative impact indicators[2], such as: o GHG emissions o Biodiversity o Human Rights o Labour Rights - Report on investor impact strategy (i.e. theory of change), including: o Impact targets (KPIs); o Engagement strategy (incl. how shareholder engagement is integrated into the investment strategy of the product, how the investee companies are monitored and how voting rights are exercised as well as how dialogue is conducted with investee companies); o Exit thresholds; o Metrics regarding measurement of investor contribution. - Report on overall product transition plan incl. short-term, medium-term and long-term targets, in line with CSRD requirements. - Report annually on progress with regard to transition plan targets.
Products with "sustainable" label	
- Product has objective to invest in sustainable assets.[3]	- Report (y-o-y) on negative impact indicators[5], such as:

[1] Where possible the transition plan should be based on standards and guidance available under Directive (EU) 2022/2464 and its reporting standards. See also the Commission recommendation on facilitating finance for the transition to a sustainable economy, in particular recommendation 7 on the use of a credible transition plan.
[2] These indicators can be based on the PAI indicators of the SFDR delegated regulation (or a subset thereof).
[3] E.g. sustainable investments in companies, real estate or corporate bonds.
[5] These indicators can be based on the PAI indicators of the SFDR delegated regulation (or a subset thereof).

- On Taxonomy as a requirement, a growth path can be envisioned depending on uptake of Taxonomy and availability of data. - In the case of an environmental objective: where investments are in activities covered by the EU Taxonomy, investments should be taxonomy-aligned in order to qualify as sustainable. - Where investments are in activities that are not covered by the taxonomy or that have a social objective, the FMP should have its own set of criteria in order to qualify investments as sustainable. - No investments in companies that do significant harm to ecological or social objectives. - Minimal to apply exclusion criteria referred to in Article 12(1)(a)-(g) of Commission Delegated Regulation (EU) 2020/1818 [align with ESMA fund name GLs proposal]. - All sustainable assets are aligned with Paris goals (excluding instruments for specific purposes)[4]. - Product invests a minimum 80% of AuM according to its sustainability strategy, provided that all AuM adhere to "do no significant harm" criteria.	o GHG emissions o Biodiversity o Human Rights o Labour Rights - Report on taxonomy alignment of investments. - Report on the criteria and % of other sustainable assets (i.e. where not covered by the EU Taxonomy). - Report on the content of other assets (where relevant).

[4] Investments for certain specific purposes such as hedging or liquidity (see EC SFDR Q&A July 2021).