INSTITUT DE LA FINANCE DURABLE
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POSITION PAPER

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POSITION PAPER ON THE EUROPEAN COMMISSION'S CONSULTATION REGARDING THE REVISION OF SFDR

The Institute of Sustainable Finance (IFD) applauds the efforts of European co-legislators in developing European regulations to promote a more sustainable economy. This ambitious framework must be designed to redirect capital flows towards sustainable activities and finance the ecological transition.

IFD specifically supports legislative and regulatory initiatives aimed at ensuring greater transparency and achieving the goals of the European Green Deal.

The Sustainable Finance Disclosure Regulation (SFDR), which came into effect on March 10, 2021, laid the initial foundations for a regulatory framework designed to allow final investors and asset managers to harmoniously characterize the numerous sustainable investment strategies available within the European Union and to select them more easily.

The objective of this framework is to ensure greater transparency in financial markets through standardizing information disclosure and providing a framework for better comparability of financial products.

While maintaining this initial ambition, the implementation modalities of the SFDR need to be reviewed as they have raised several difficulties and concerns among financial market participants and their clients.

In general, IFD believes that the European Commission should formulate recommendations in the coming months to update the architecture and content of regulatory texts related to sustainable finance. This will prioritize ensuring better consistency between texts, greater transparency of data from economic and financial sectors, and providing financial actors and savers with more robust tools to align their financing decisions with their sustainability preferences.

Regarding the SFDR specifically, stakeholders in the Paris financial centre unanimously support the need for a more transparent and accessible system for end users.

IFD highlights three challenges that the SFDR still needs to address: (i) better implementation of transparency requirements, (ii) implementation of transparency requirements, (ii) greater coherence between European texts on sustainable finance, and (iii) clarification of the definitions of key terms.

Transparency requirements

IFD advocates for a more effective transparency framework under the SFDR regulation, based on harmonised, comparable and robust information — a prerequisite for meaningful product categorisation.

Transparency rules should apply to all financial products, with a selection of essential information reflecting the sustainability content of the entity's product portfolio. However, the assessment of a product's sustainability should consider the specificities of different asset classes.

IFD proposes, on the other hand, that the list of mandatory PAI indicators at the entity level be revised in order to retain a minimum set of standard PAI indicators to be published. Indeed, the objective of these indicators should above all be to enable financial actors to inform their investment decisions — an objective which, in our view, seems to have been lost sight of.

In general, certain obligations required by this regulation may create confusion for end investors — both professional and retail — due to a lack of clarity and clearly defined objectives for financial products. Instead of facilitating the proper matching of products with investors' preferences, this complexity may hinder the effective reallocation of capital towards sustainable activities. Many financial institutions have, in fact, slowed down their financing explicitly oriented towards sustainable activities, due to concerns over potential accusations of "greenwashing" — a phenomenon that appears to be gaining momentum.

IFD supports the rationalisation and simplification of the information to be disclosed. The volume of data required should be reassessed to focus on the most relevant elements, that is, those that are objective, widely accepted across financial markets, and easily understandable for end clients. **This need is all the more urgent given the recent publication of the FCA's categorisation system, which, in the absence of a swift EU response, could make the UK market appear significantly more readable and therefore more attractive in the field of sustainable finance.**

Greater coherence across sustainable finance frameworks

IFD considers it essential for the revision of the SFDR regulation to fully align with the CSRD (Corporate Sustainability Reporting Directive) and its associated delegated act to ensure consistency in requirements for issuers and investors.

More generally, the European Commission should conduct a thorough analysis of inconsistencies and divergences among various European texts related to sustainable finance to achieve more aligned frameworks. Specifically, better coherence should be ensured between the SFDR regulation and the European Taxonomy, the CSRD directive, ESRS (European Single Reporting Format) delegated acts, as well as the Benchmark Regulation

(BMR). A good alignment between SFDR product categorization and the MiFID II/IDD/PRIIPS framework is also crucial.

In the context of the SFDR revision, IFD supports the idea of 'no further mandatory PAI,' meaning the avoidance of multiplying Principal Adverse Impacts (PAI) subject to mandatory reporting.

The coherence of the regulatory architecture should primarily be ensured in Level 1 texts but also in delegated acts, RTS (Regulatory Technical Standards), and guidelines derived from them. It can also involve the publication of explanatory documents and FAQs to provide financial market actors with a better understanding of the entire regulatory framework.

The Paris financial sector indeed advocates for greater consistency across texts applied to different types of actors to develop a regulatory package that, from issuer to investor, is logical, understandable, and therefore effective.

<u>Clarification of Definitions</u>

IFD emphasizes the need to clarify general concepts and the definitions of several key notions applicable to a broad range of financial products, in order to harmonise approaches and prevent the risks of greenwashing and fragmentation within the European market.

To accelerate responsible investment, it is essential to create the conditions for trust — which requires clarifying and simplifying key concepts, whose definitions must urgently be aligned across the various sustainable finance texts.

The concept of 'sustainable investment' on which the SFDR is based appears too general. This definition should be reconsidered, and the concepts used by the SFDR should be appropriate to properly guide financial market actors. A more suitable concept should be based on binding and measurable objectives for each financial product.

Moreover, the concept of 'transition' is not clearly included in the SFDR. IFD considers 'transition' a central concept that should be explicitly integrated into investment strategies through clear definitions and objectives. This aligns with the Recommendation published in June 2023 by the European Commission, expanding the approach beyond elements specified in the Taxonomy and recognizing the central role of transition plans.

While many sustainable finance concepts are crucial for understanding the nuances related to the sustainable characteristics of financial products, they are currently defined too broadly, leading to substantial differences between actors. Therefore, **IFD calls on the European Commission to specify these definitions to ensure a clear and common interpretation for the market**. To achieve this, IFD recommends building on existing definitions in various texts related to sustainable finance, ultimately ensuring that the information required by investors is available through publication requirements imposed on issuers. The coherence of this information chain is an essential condition for the quality of information and trust.