

# SFDR – new RTS – What you should know

## Executive Summary

- Latest developments in the process of implementation of the **EU Sustainable Finance Disclosure Regulation (SFDR)**
- Joint **ESAs supervisory statement** on the application of SFDR
- The **Final Report on draft Regulatory Technical Standards (RTS)** on content, methodologies and presentation of disclosures under the SFDR
- New reporting obligations introduced by the **EU Taxonomy Regulation** under the SFDR

The EU Sustainable Finance Disclosure Regulation, 2019/2088 (the **SFDR**)<sup>1</sup>, was adopted as of end of 2019 and amended by the EU Taxonomy Regulation, 2020/852 (the **Taxonomy Regulation**)<sup>2</sup> in 2020 whereby supplemental pre-contractual and reporting disclosures related to financial products were added.

### I. Where are we now? - SFDR and Regulatory Technical Standards

The implementation process of the SFDR has come to the first step of its long-time journey - application of the high-level principle-based requirements under the SFDR as of 10 March 2021.

Pursuant to the SFDR, a joint committee of the European Supervisory Authorities (**ESAs**) had to develop by 30 December 2020 Regulatory Technical Standards (**RTS**),

i.e. level 2 measures with regard to the content, methodologies and presentation of disclosures under the SFDR.

On 23 April 2020, the ESAs issued a Joint Consultation Paper on the SFDR including draft RTS (the **April 2020 RTS**) which were then reviewed in light of the comments received by the stakeholders until 1 September 2020. The publication of the final RTS was expected by 30 December 2020, but it was postponed to a later date.

Finally, on 4 February 2021 just a few weeks before the 10 March 2021 SFDR application deadline, the ESAs published the Final Report on draft RTS<sup>3</sup> (the **Revised RTS**), which should be endorsed by the EU Commission and would apply as of 1 January 2022.

Furthermore, on 25 February 2021, the ESAs issued a supervisory statement on the application of the SFDR (the **Statement**), addressing the risk of divergent application of the SFDR and the level 2 measures contained in the Revised RTS within the period from 10 March 2021 to the application date of the RTS.

The Annex of the Statement contains application timelines with view to specific provisions of the SFDR, the Taxonomy Regulation and the RTS.

### II. What is next? - Adoption of RTS and guidance for interim period

As specified in the Statement, the final version of the RTS may differ from the Revised RTS. Nonetheless, the ESAs recommend national competent authorities to refer

<sup>1</sup> Regulation (EU) 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial services sector, available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32019R2088&from=EN>.

<sup>2</sup> Regulation (EU) 2020/852 of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending EU

Regulation 2019/2088, available here: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852&from=EN>.

<sup>3</sup> ESAs Final Report on draft Regulatory Technical Standards <https://www.eiopa.europa.eu/sites/default/files/publications/reports/jc-2021-03-joint-esas-final-report-on-rts-under-sfdr.pdf>.



financial market participants (FMPs) and financial advisers (FAs) to the requirements set out in the Revised RTS and to encourage them to use the interim period from 10 March 2021 until 1 January 2022 to prepare for the application of the RTS.

On 12 March 2021, the CSSF announced that in line with the ESAs Statement, the CSSF also encourages the FMPs and FAs to use the Revised RTS as reference for the purposes of applying the respective articles under the SFDR during the interim period.

### Final Report on draft RTS – Executive Summary

The Revised RTS provide specific rules on content, methodologies and presentation of disclosures under the SFDR and, in particular, regarding the publication of: (A) **Principal Adverse Impacts Statement** on the entity's website in relation to the adverse impact of investment decisions on sustainability factors under articles 4(6) and 4(7) of the SFDR; (B) **Pre-Contractual Disclosures** for financial products under art. 8 and art. 9 of the SFDR; (C) **Website Product Disclosures** in accordance with art. 10 of the SFDR; (D) **Product-Level Periodic Disclosures** in accordance with art. 11 of the SFDR.

Furthermore, the Revised RTS contain five **mandatory templates** to be used by FMPs in order to disclose information required under the SFDR.

#### A. Transparency of Adverse Sustainability Impacts

According to art. 4(1) of the SFDR, FMPs shall publish and maintain on their websites:

- a) where they **consider** principal adverse impacts of investment decisions on sustainability factors, **a statement on due diligence policies with respect to those impacts**; or
- b) where they **do not consider** principal adverse impacts of investment decisions on sustainability factors, **clear reasons why they do not do so**.

The Revised RTS provide that such information shall be published in a separate section on the FMPs' website

titled "*Principal adverse sustainability impact statement*", which should be divided into the following sections: (i) summary; (ii) description of principal adverse sustainability impacts; (iii) description of policies to identify and prioritise principal adverse sustainability impacts; (iv) engagement policies; and (v) references to international standards.

The FAs are subject to the same obligations and shall disclose whether or not they **consider in their investment advice or insurance advice the principal adverse impacts on sustainability factors**. In case of non-consideration, they need to provide the reasons therefor. In case of consideration, the FAs shall publish on their websites details on the selection process of the advised financial products including: (i) how the information referred to in the SFDR published by FMPs is used; (ii) whether the FA ranks and selects financial products based on at least the indicators provided for in Table 1 of Annex I of the Revised RTS, where applicable, a description of the ranking and selection methodology used; and (c) any criteria or thresholds used to select financial products and advise on them based on those impacts.

Where FMPs or FAs do not consider adverse impacts of investment decisions on sustainability factors, they shall disclose that the information in a separate section on their website titled "*No consideration of sustainability adverse impacts*" which shall include: (i) prominent statement of non-consideration of sustainability adverse impacts; (ii) clear reasons for non-consideration and, where relevant, information whether and when they intend to consider adverse impacts by reference to indicators pursuant to the Revised RTS.

In comparison to the April 2020 RTS, the Revised RTS added a translation requirement with regard to the "*summary*" section of the principal adverse sustainability impacts statement, clarifying that, where a financial product is marketed in a host Member State, the FMP shall also provide the summary section in one of the official languages of that corresponding host Member State. Even though, this relates only to the summary section, still that may create additional burden for the FMPs.



Furthermore, the Revised RTS set out a list of 14 mandatory indicators that FMPs shall insert in the section related to principal adverse impacts. FMPs shall also include at least (i) one additional indicator related to principal adverse impacts on a climate or other environment related sustainability factor; (ii) at least one additional indicator related to principal adverse impacts on a social, employee, human rights, anti-corruption or anti-bribery sustainability factor, and (iii) any other indicators used. It is important to highlight that the Revised RTS reduced the number of mandatory indicators in comparison to the April 2020 RTS which provided in total for 50 indicators (32 mandatory and 18 additional indicators).

Moreover, pursuant to the Revised RTS, in the section dedicated to the disclosure of adverse sustainability impacts, FMPs shall provide a description of the actions taken or planned during the reference period in order to avoid or reduce the principal adverse impacts identified.

## B. Pre-Contractual Product Disclosures

The Revised RTS govern the presentation of pre-contractual information in respect of the following financial products:

- Products under art. 8 of the SFDR (the **Light Green Products**), i.e. products that promote, among other characteristics, environmental or social characteristics, or a combination of those characteristics; and
- Products under art. 9 of the SFDR (the **Dark Green Products**), i.e. products which have sustainable investment as their objective.

According to the Revised RTS, FMPs shall include a **prominent statement** in the main body of pre-contractual documents that information related to environmental or social characteristic of the financial product is contained in a **specific annex** to the pre-contractual document (the **Pre-Contractual Annex**), in accordance with template Annex II for **Light Green Products** and template Annex III

for **Dark Green Products**. The template Annex II and Annex III are mandatory for those product types.

For **Light Green Products**, the statement to be inserted at the beginning of the Pre-Contractual Annex shall clarify: (i) whether the financial product intends to make any sustainable investment; (ii) that the financial product promotes environmental or social characteristics, but does not have as its objective a sustainable investment; and (iii) whether an index has been designated as a reference benchmark for the purpose of attaining environmental or social characteristics promoted by the financial product.

Furthermore, the Pre-Contractual Annex shall contain these main sections: (i) environmental and/or social characteristics promoted by the financial product; (ii) investment strategy followed by the product; (iii) asset allocation planned for the financial product; (iv) consideration of principal adverse impacts on sustainability factors; (v) further product information online; (vi) alignment of the reference benchmark, if any, to the characteristics of the product.

As regards the **Dark Green Products**, the means of disclosure are essentially the same, except that it should be clearly stated that the financial product has a **sustainable investment objective**, which is the sustainable investment objective of the financial product, and to mention, if the financial product has a reduction in carbon emissions as its objective.

It is worth noting that even if the consideration of principal adverse impacts is mentioned for both **Light Green Products** and **Dark Green Products** pre-contractual disclosures, these disclosure requirements seem to be applied differently for each of those products. In fact, the consideration of principal adverse impacts seems to be mandatory for Dark Green Products, while not for Light Green Products.



### C. Website Product Disclosures

In accordance with art. 10 of the SFDR, FMPs shall publish and maintain on their websites specific information as regards Light Green Products and Dark Green Products in order to ensure transparency in the promotion of environmental and social characteristics and of sustainable investments.

The Revised RTS also outline the structure and the contents of the website disclosures, again adapting the model of presentation to Light Green Products or Dark Green Products.

FMPs shall furthermore insert a specific section in the website named “*Sustainability-related disclosures*” containing: (i) summary; (ii) indication of no sustainable investment objective (for Light Green Products) or Do Not Significant Harm principle (for Dark Green Products); (iii) environmental or social characteristics of the financial product (for Light Green Products) / sustainable investment objective of the financial product (for Dark Green Products); (iv) investment strategy; (v) proportion of investments; (vi) monitoring; (vii) methodologies; (viii) data sources and processing; (ix) due diligence; (x) engagement policies; (xi) alignment to a reference benchmark, if any.

### D. Product Disclosures in Periodic Reports

The Revised RTS provide detailed measures in relation to the presentation and content requirements of periodic reports for **Light Green Products** and **Dark Green Products**.

Similarly, to the regime of pre-contractual disclosures, the ESAs established that FMPs shall include in periodic reports a **prominent statement** ensuring that information related to environmental or social characteristic of the financial product is contained in a **specific annex**, in accordance with the template set out in Annex IV and template Annex V of the Revised RTS, respectively for Light Green Products and Dark Green Products. The information to be inserted in the periodic reports is made up of the sections titled: (i) to what extent the environmental and/or social characteristics are

promoted, or the sustainable investment objective of the financial product is met; (ii) what were the top investments of this financial product; (iii) what was the proportion of sustainability-related investments; (iv) what actions have been taken to meet the environmental and/or social characteristics during the reference period; and (v) how the financial product performed compared to the designated reference benchmark, if any.

In comparison with the April 2020 RTS, in the Revised RTS the number of “*top investments*” to be included in periodic reports has been reduced from 25 to 15. Furthermore, according to the Revised RTS, FMPs need to provide historical comparison with at least five previous reference periods, and not ten previous reference periods as stated in the April 2020 RTS.

### III. Impact of the Taxonomy Regulation on the SFDR

By amending the SFDR, the Taxonomy Regulation introduced additional sustainability-related disclosures in pre-contractual and reporting documents in relation to **Light Green Products** - products under art. 8 of the SFDR which promote environmental characteristics and **Dark green products** - products under art. 9 of the SFDR which invest in an **economic activity that contributes to an environmental objective**.

With respect to Dark Green Products, the Taxonomy Regulation provides that pre-contractual documents and periodic reports shall include: (i) the information on the environmental objective or environmental objectives set out in art. 9 the Taxonomy Regulation to which the investment underlying the financial product contributes; and (ii) a description of how and to what extent the investments underlying the financial product are in economic activities that qualify as environmentally sustainable as defined under the Taxonomy Regulation.

With respect to Light Green Products, the Taxonomy Regulation provides that pre-contractual documents and periodic reports shall include the same information as stipulated above and a specific statement that “*do no significant harm principle applies only to those investments underlying the financial product that take*



*into account the EU criteria for environmentally sustainable economic activities”.*

The Taxonomy Regulation will apply as of 1 January 2022 with regard to the first two environmental objectives set out by art. 9 thereof, i.e. climate change mitigation and climate change adaptation, and as of 1 January 2023 as regards the other environmental objectives.

Furthermore, in order to align the presentation of the new disclosures introduced by the Taxonomy Regulation under the SFDR, the ESAs were empowered to develop further RTS on taxonomy-related sustainability disclosures. Finally, on 17 March 2021, ESAs issued a Joint Consultation Paper regarding taxonomy-related disclosures. The consultation period will be open until 12 May 2021.

It is worth noting that, the FMPs should not lose any time and shall take the required preparatory actions already now in order to be able to meet the required deadlines.

#### **Conclusion and where we can assist you**

As of the date hereof, the SFDR high-level principle-based requirements should already be complied with by the FMPs and FAs, while the RTS level 2 measures would apply only as of 1 January 2022. The Taxonomy Regulation will apply in two steps as abovementioned. Therefore, it is crucial for the FMPs and FAs to understand and keep a track of all the deadlines with view to the SFDR application.

Furthermore, it is important to note that there are still lots of uncertainties regarding the interpretation of some of the provisions of the SFDR. In particular, the questions raised in the ESAs letter as of 7 January 2021, to the EU Commission with five main issues related to interpretation of the SFDR, such as (i) applicability of the SFDR to registered AIFMs, Non-EU AIFMs, (ii) definitions of art 8 and art 9 products and so on, that still remains unanswered.

It is however clear that SFDR and the related provisions are becoming a hard law and it will be difficult to escape

those mandatory disclosures in the future. Therefore, every asset manager needs to have a complete picture of what needs to be done, when and to which extent.

We can assist you with product categorisations, respect of mandatory provisions under the SFDR, the Taxonomy Regulation and RTS, respectively and guide you through this long time-journey to ensure the best possible efficiency.

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