

## Cabinet News and Views

Informed analysis for the financial services industry



### European Commission Consultation on SFDR



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On 14 September 2023, the European Commission published a targeted consultation and a public consultation on the implementation of Regulation (“EU”) 2019/2088 on sustainability-related disclosures in the financial services sector (“SFDR”), which focus on potential shortcomings of SFDR, including legal certainty, the usability of the legislation and its ability to stop greenwashing. Of particular interest is the Commission’s acknowledgment that the SFDR is being used as a labelling scheme (when it was designed as a disclosure regime). There is currently no EU regulatory definition of, or label for, an environmental, social and governance (“ESG”) investment product, although several industry and national fund labels exist and the Commission has observed that Articles 8 and 9 of SFDR are being used as product “labels.” Accordingly, the Commission is seeking views on the merits of developing a more precise EU-level product categorisation system based on defined criteria as well as views on the use of ESG terminology in fund names and whether further rules on the use of terminology in fund names and marketing communications are required.

Four proposed criteria are being consulted on:

1. Products investing in assets that specifically strive to offer targeted, measurable solutions to sustainability-related problems that affect people and/or the planet; e.g., investments in firms generating and distributing renewable energy, or in companies building social housing or regenerating urban areas.
2. Products aiming to meet credible sustainability standards or adhering to a specific sustainability-related theme; e.g., investments in companies with evidence of solid waste and water management, or strong representation of women in decision-making.

3. Products that exclude activities and/or investees involved in activities with negative effects on people and/or the planet.
4. Products with a transition focus aiming to bring measurable improvements to the sustainability profile of the assets in which they invest; e.g., investments in economic activities becoming taxonomy-aligned or in transitional economic activities that are taxonomy-aligned, investments in companies, economic activities or portfolios with credible targets and/or plans to decarbonise, improve workers' rights or reduce environmental impacts.

The two consultations both close to comments on 15 December 2023. The Commission intends to adopt a report on the SFDR in the second quarter of 2024.

### **ESMA report on sustainable fund names and claims**

On 2 October 2023, the European Securities and Markets Authority ("ESMA") published a study on ESG names and claims in the EU funds industry (ESMA50-524821-2931), complementing the Commission's current consultation on SFDR and EU regulators' drives to continue to monitor ESG-related disclosures and to scale up the monitoring and supervision of greenwashing.

ESMA has created a comprehensive list of ESG words and phrases, which has allowed it to apply natural language processing ("NLP") techniques to several large text and numerical datasets, including one containing the historical names of over 36,000 unique EU-domiciled investment funds. Key findings from the study that include:

- An increasing number of funds include ESG terms in their names and ESMA has found evidence of high investor appetite for funds with an ESG-related term in their name. For example, the share of EU UCITS investment funds with ESG words in their name has increased from less than 3% in 2013 to 14% in 2023.
  - Managers prefer to include generic ESG terms (such as "sustainable") rather than more specific terms, which can make it more difficult for investors to verify that the fund portfolio is in line with the name.
  - Funds with ESG-related language in their names, and funds disclosing under Article 9 of SFDR, provide more extensive ESG disclosures in their investment strategies and documentation than other funds.
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