

## GREAT FUND INSIGHTS

# New RTS for sustainable finance disclosure regulation (SFDR) – key points for funds and asset managers

Up to date as of 11 February 2021

## 1. Speed read

Firms are continuing to press on with work to implement the Sustainable Finance Disclosure Regulation (2019/2088) (**SFDR**), which begins to apply on 10 March 2021 across the EU. This regulation will require certain firms, including fund and asset managers, to comply with new rules on disclosure as regards sustainability risks and other ESG-related matters. As many firms are aware, there has been a delay in the finalisation of the Level 2 measures for SFDR which will take the form of a Regulatory Technical Standard or RTS. Although the Level 2 measures were originally intended to apply from

10 March, this has been delayed and delayed, with the final proposed RTS text only now being published by the European Supervisory Authorities (**ESAs**) in a highly detailed report of c.200 pages.

Given the late timing, it has been conceded that the application of the RTS must be delayed – it will now begin to apply from **1 January 2022**, although firms will still have to start complying with the Level 1 SFDR requirements from **10 March 2021**.

This briefing gives further detail on the RTS and how firms can make sense of the new regime.

## 2. How did we get here?

The EU Council adopted the text of SFDR on 8 November 2019 (for a copy see [here](#))<sup>1</sup>. It entered into force on 29 December 2019 and will start to apply from 10 March 2021. The EU Council subsequently adopted the Taxonomy Regulation (2020/852) (for a copy see [here](#))<sup>2</sup>, which entered into force on 12 July 2020. The Taxonomy Regulation both supplements and amends certain provisions in SFDR.

Under SFDR, the ESAs have been mandated to develop various Level 2 measures for SFDR, to take the form of a Regulatory Technical Standard (**RTS**).

On 4 February 2021, the ESAs published their final report on a draft RTS. For a copy, see [here](#)<sup>3</sup>. We have also produced a comparison against the consultation proposals and this can be found [here](#)<sup>4</sup>.

The European Commission will now review the draft measures and either adopt or reject them. Assuming the Commission adopts the recommended measures “as is”, the co-legislators will have a three-month scrutiny period to accept or reject them. We understand that the Commission currently intends to adopt the measures at the end of March or beginning of April. However, there is no guarantee that this timeline will be adhered to or that no further changes will be made.

For a copy of our previous briefings on SFDR fund and asset managers, see [here](#)<sup>5</sup> and [here](#)<sup>6</sup>.

“...there is **no guarantee** that this timeline will be adhered to or that **no further changes** will be made.”

### 3. When will it apply?

The Level 1 SFDR requirements begin to apply from **10 March 2021**. The implementation date for the RTS has been pushed back, however. It is now proposed to come into effect on a phased basis starting from 1 January 2022, subject to the following:

- Principal adverse impact reporting – The additional detail prescribed by the RTS is to be phased in. In particular, the RTS requires reports on principal adverse impacts by 30 June each year, with a reference period of the previous calendar year. In practice, this means that the first report is required

in 2023 for the reference period of 2022.

- Periodic reports – Financial market participants must draw up periodic reports in compliance with SFDR in 2022.
- Certain disclosures are only required to be made at a later date – eg *“the reporting on Scope 3 GHG emissions in Tables 1 and 2 of Annex I [ie the mandatory reporting templates] shall apply from 1 January 2023”* (Article 74(3) of the RTS).

### 4. How should I interpret SFDR level 1 given the delay to level 2?

Strictly speaking, you are entitled to begin to comply with the Level 1 requirements of SFDR on 10 March 2021, ignoring the requirements of the RTS. In other words, you can totally put to one side the prescribed disclosures and templates in the RTS. Alternatively, if you wish, you can begin to comply with some or all of the RTS requirements – eg if you prefer to do this to avoid having to re-write pre-contractual disclosures at a later stage or limit systems or IT changes. This is a commercial point.

In our view, however, any guidance provided in the recitals to the RTS as to matters of interpretation in relation to SFDR should be taken on board (although as noted in paragraph 2 above, we cannot guarantee that no further changes will be made). You may also wish to have regard to the RTS to the extent it contains comments on potential greenwashing risks, shows the regulatory “direction of travel”, or indicates how regulators are generally interpreting the regime and its policy goals. You may also wish to consider some of the more generic sections of the RTS and boilerplate requirements – eg Article 2 on the presentation of information.

### 5. What do I need to look at in the RTS for “day 1” – ie 10 March 2021?

- Look at the guidance in the recitals to the RTS and consider if your internal project has been interpreting SFDR Level 1 requirements in line with this.
- Look at Article 2 of the RTS on the presentation of information – if you can, you may wish to comply with this from “day 1”.
- Briefly review the other articles in the RTS, but only to look out for articles that cast light on how SFDR should be interpreted, contain references to boilerplate disclosures, or deal with how information should be presented when the RTS comes into force. Eg:
  - **Example 1:** Article 24 of the RTS suggests that a firm with an Article 9 product must consider principal adverse impacts (ie as per the PAI regime in Article 4). This may have a bearing on whether (for day 1) a manager with an Article 9 product would otherwise have wished to “opt in” or “opt out” of that regime.

- **Example 2:** Article 20 of the RTS requires pre-contractual disclosures for an Article 9 product to be included in an annex – eg for a UCITS, in an annex to a prospectus, or for a MiFID portfolio manager, in an annex to the manager’s usual MiFID II required pre-contractual document. It also requires the body of the document to include a prominent statement that information relating to sustainable investment is available in that annex, and requires certain other boilerplate wording to be used. You may wish to consider approaching your “day 1” disclosure in a way that is broadly in line with this (leaving aside the substantive disclosure requirements).
- **Example 3:** Article 31 of the RTS contains some “rules of the road” for your website disclosures on Article 8 and 9 products, including how to organise and label relevant website pages. You may wish to consider structuring your website in this way for “day 1” if commercially convenient.

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## 6. What does the RTS contain?

From a high-level perspective, the RTS essentially deals with three matters:

- (1) It provides guidance on certain points of interpretation in relation to SFDR, and greenwashing risk – this is done in various recitals to the RTS, but the detailed articles of the RTS can also be helpful on certain questions the industry has been grappling with to date.
- (2) It provides detailed requirements as to the various disclosures required by Article 4(1) to (5) (principal adverse impacts), including indicators for environmental and social impacts.
- (3) It provides detailed requirements as regards the pre-contractual, website and periodic disclosures required to be provided by financial market participants in relation to:

- Article 8 products – being those with environmental or social characteristics, referred to by the ESAs as “**light green**”, and falling within the scope of Article 8 of SFDR; and
- Article 9 products – being those with a sustainable investment objective (including a reduction in carbon emissions objective), referred to by the ESAs as “**dark green**”, and falling within the scope of Article 9 of SFDR.

This includes requirements relating to the “do no significant harm” (DNSH) principle, being a key component of the definition of a “sustainable investment” under SFDR.

As regards the second and third points above, the RTS is highly detailed and prescriptive, including (among other things) templates required to be used in an attempt to ensure that information is standardised in form. A key driver behind the RTS is a desire “to increase [the] comparability of disclosures for end investors”, meaning product by product and firm by firm.

## 7. What is the RTS relevant to? Where can I find what I need?

SFDR (Level 1)	Draft RTS (Level 2)
<b>General points</b>	
<b>How to categorise products for SFDR purposes</b>	
Eg Article 6 vs Article 8 vs Article 9	<ul style="list-style-type: none"> <li>– See recitals 18, 19, 20, 21, 22 and 25 of the RTS</li> <li>– See also recitals 27 and 32 of the RTS</li> </ul>
References to exclusions	– See recitals 18 and 25 of the RTS
References to baseline safeguards	– See recital 23 of the RTS
<b>How to interpret various SFDR requirements</b>	
References to good governance	– See recitals 27 and 35 and Articles 15, 22, 36 and 49 of the RTS
References to direct vs indirect investments/exposures	<ul style="list-style-type: none"> <li>– See recitals 4 and 31 and Articles 37 and 50 of the RTS</li> <li>– The ESAs commentary notes that the disclosure of direct vs indirect investments has been moved from pre-contractual and periodic disclosures to the website disclosures</li> <li>– NB: The PAI disclosure must cover “direct and indirect investments of financial market participants in assets such as investee companies, sovereigns, supranational entities and real estate”</li> </ul>
References to funds, fund of funds, holding vehicles, SPVs etc	<ul style="list-style-type: none"> <li>– See recitals 4 and 31 of the RTS</li> <li>– NB: The RTS confirms that, where the investee company is “a holding company, collective investment undertaking or special purpose vehicle”, firms that have sufficient information about PAI should make the disclosures on a “look through basis”. Where they do not have the information, they cannot be considered to take PAI into account</li> </ul>
References to hedges or derivatives	– See recitals 21 and 31 and Articles 16, 23, 59 and 65 and the annexes (templates) of the RTS

## SFDR (Level 1)

## Draft RTS (Level 2)

References to sovereign debt/bonds

- See recital 4 and Annex I (template) of the RTS
- NB: “For investments in sovereigns..., the ESAs have included one mandatory climate and environmental indicator on the greenhouse gas emission intensity” and “For investments in sovereigns..., the only mandatory social indicators regard [sic] the investment in countries subject to social violations.”

References to real estate

- See recital 4 and Annex I (template) of the RTS

References to due diligence

- See recital 11 and Articles 4, 9, 32, 42, 45 and 55 and Annex I (template) of the RTS
- NB: The reference to “internal and external controls on [the] due diligence” suggest these are expected

References to engagement or engagement policies

- See recital 8 and Articles 4, 8, 32, 43, 45, 56, 62 and 68 and Annex I (template) of the RTS

References to adviser obligations

- See recital 14 and Articles 10 and 12 of the RTS regarding PAI disclosures
- See also Article 2 and a small point in Article 3
- NB: The bulk of the RTS applies to financial market participants (eg fund and portfolio managers) rather than advisers

## Other key SFDR and Taxonomy Regulation concepts

References to the DNSH principle

- See recitals 10, 19 and 33, Articles 16, 23, 34, 45 and 47 and Annex I (template) of the RTS
- See also below re minimum standards under the Taxonomy Regulation

References to minimum safeguards, baseline protections or international standards

- See recitals 12, 23 and 33 and Articles 4, 9, 16, 23, 30, 34, 47, 61 and 67 and Annex I (template) of the RTS
- NB: The ESA commentary notes that, compared to the consultation, the final report has added an additional requirement to the DNSH provisions throughout. In addition to disclosing how the firm takes into account the indicators for adverse impact in Annex I, the DNSH reporting must also show whether the investments are aligned with the OECD Guidelines for Multinational Enterprises etc. The goal is to align the DNSH disclosures under SFDR with the minimum safeguards in Article 18 of the Taxonomy Regulation

References to monitoring

- See recital 26, Articles 32, 38, 45 and 51 and Annex I (template) of the RTS
- NB: The RTS states that “it is expected that financial market participants monitor throughout the lifecycle of a financial product how it complies with the disclosed environmental or social characteristics, or sustainable investment objective. Consequently, financial market participants should explain, as part of their website disclosures, the internal or external control mechanisms put in place to monitor such compliance on a continuous basis”. The reference to “related internal and external control mechanisms” in relation to monitoring suggest these are expected

References to an index or benchmark

- See recitals 3, 28, 29, 30 and 38 and Articles 3, 13, 19, 20, 26, 27, 32, 44, 57, 58, 63, 69 and 70 and the annexes of the RTS

## Disclosure requirements

### Article 3 – Sustainability risk disclosure

– NA – RTS does not cover this SFDR provision

### Article 4 – PAI disclosures

– The RTS provides detailed “rules of the road” as to how a firm must make its Article 4 disclosures  
– These must be published on a firm’s website  
– See also above re direct and indirect investments and the “look through” for funds etc  
– See also recitals 4-14, 19, 33 and 40 and Articles 34 and 47 of the RTS  
– See also the definition of reference period in Article 1

Financial market participant that considers PAI

– See Articles 4-9 of the RTS  
– Among other things, this prescribes five mandatory headings  
– It also requires a maximum two-page summary  
– NB: One heading reads “*Description of policies to identify and prioritise principal adverse sustainability impacts*”, which suggests such policies are expected  
– NB: The PAI indicators are divided into mandatory indicators and opt-in indicators. Compared to the April 2020 draft RTS, there are now fewer mandatory and more opt-in indicators. Separate indicators are also provided for impacts from investments in investee companies, sovereigns and supnationals and real estate assets (see Annex I)  
– Note also Article 24 of the RTS

Financial market participant that does not consider PAI – ie “opt out”

– See Articles 4 and 11 of the RTS  
– Note also Article 24 of the RTS

Financial adviser disclosures

– See Articles 10 and 12 of the RTS  
– See also recital 14 of the RTS

### Article 5 – Remuneration disclosure

– NA – RTS does not cover this SFDR provision

### Article 6 – Pre-contractual disclosures on sustainability risks

– NA – RTS does not cover this SFDR provision

### Article 7 – Pre-contractual PAI disclosures at product level

– The RTS does not speak directly to this obligation, but Article 7(1) of SFDR notes that “*Where information in Article 11(2) [of SFDR] includes quantifications of principal adverse impacts on sustainability factors, that information may rely on the provisions of the regulatory technical standards adopted pursuant to Article 4(6) and (7) [of SFDR].*”  
– NB: Article 7(1) of SFDR only applies from 30 Dec 2022

### Article 8

Pre-contractual disclosures for “light green” products – ie products with “E” or “S” characteristics, provided the good governance test is met

– The RTS provides detailed “rules of the road” as to how a firm must make Article 8 pre-contractual disclosures  
– See Articles 13-19 of the RTS  
– See recitals 22-24, 32, 34-36, 40, 43 and 44 of the RTS  
– Use the template in Annex II of the RTS, which shows a creative approach in terms of “look and feel”  
– Among other things, this prescribes five mandatory headings, plus a sixth if an index is relevant  
– Under the second heading (“*What investment strategy does this financial product follow*”), the manager must, among other matters, set out a description of its policy to assess good governance practices of investee companies and provide a reference to the website for more information on the investment strategy

### Article 9

Pre-contractual disclosures for “dark green” products – ie products with a sustainable investment objective, including a reduction in carbon emissions

– The RTS provides detailed “rules of the road” as to how a firm must make Article 9 pre-contractual disclosures  
– See Articles 20-27 of the RTS  
– Use the template in Annex III of the RTS, which again shows a creative approach in terms of “look and feel”  
– Among other things, this prescribes five mandatory headings, plus additional headings where the product has the objective of a reduction in carbon emissions or an index is relevant

## Disclosure requirements

### Article 10

Website disclosures for Articles 8 and 9 products

- The RTS provides detailed “rules of the road” as to how a firm must make these website disclosures
- See Articles 2 and 31-57 of the RTS
- See recitals 26, 32, 34 and 35
- Note the obligation to prominently display the “E”/“S” characteristics of an Article 8 product and the sustainable investment objective of an Article 9 product (Article 31 of the RTS)
- There is no mandatory template for this

General instructions re presentation etc

- See Articles 31 and 32 of the RTS

For Article 8 products

- See Articles 32-44 of the RTS
- Among other things, this prescribes 11 mandatory headings, plus a 12th if an index is relevant
- It also requires a maximum two-page summary
- The second heading must read “*No sustainable investment objective*”. The following words must then be used: “*This financial product promotes environmental or social characteristics, but does not have as its objective a sustainable investment.*”
- Under the fourth heading (“*Investment strategy*”), among other matters, the manager must set out a description of its policy to assess good governance practices of investee companies, “*including*” with respect to sound management structures, employee relations, remuneration of staff and tax compliance. This suggests that more than just these items must be covered

For Article 9 products

- See Articles 45-57 of the RTS
- Among other things, this prescribes 12 mandatory headings
- It also requires a maximum two-page summary
- Under the fourth heading (“*Investment strategy*”), the manager must set out a description of its policy to assess good governance practices of investee companies, “*including*” with respect to sound management structures, employee relations, remuneration of staff and tax compliance. This suggests that more than just these items must be covered

### Article 11

Periodic reports for Articles 8 and 9 products

- The RTS provides detailed “rules of the road” as to how a firm must make these website disclosures
- See Articles 58-73 of the RTS
- See recitals 22, 32, 35-38, 40 and 45 of the RTS
- Use the templates in Annex IV and Annex V of the RTS – again, these show a creative “look and feel”
- Among other things, this prescribes four mandatory headings, plus a fifth if an index is relevant
- In general, the top 15 investments must be listed
- Historic comparisons are required between a reference period and previous reference periods

## References

<sup>1</sup> The full name of this regulation is “Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector”, see <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32019R2088>

<sup>2</sup> The full name of this regulation is “Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088”, see <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32020R0852>

<sup>3</sup> [https://www.eba.europa.eu/sites/default/documents/files/document\\_library/Publications/Draft%20Technical%20Standards/2021/962778/JC%202021%2003%20-%20Joint%20ESAs%20Final%20Report%20on%20RTS%20Under%20SFDR.pdf](https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Draft%20Technical%20Standards/2021/962778/JC%202021%2003%20-%20Joint%20ESAs%20Final%20Report%20on%20RTS%20Under%20SFDR.pdf)

<sup>4</sup> [https://www.aohub.com/aohub/publications/sfdr-level-2-requirements\\_1?nav=FRbANEucS95NMLRN47z%2BeeOgFCt8EGQ71hKXzqW2Ec%3D&key=BcJlLtdCv6%2FJTDZxvL23TQa3JHL2AIGr93BnQjo2SkGJpG9xDX7S2thDpAQsCconWHAwe6cJTnjeeHbuC84r367L3C3Rzay&uid=LCQI%2F1P2Lj%3D](https://www.aohub.com/aohub/publications/sfdr-level-2-requirements_1?nav=FRbANEucS95NMLRN47z%2BeeOgFCt8EGQ71hKXzqW2Ec%3D&key=BcJlLtdCv6%2FJTDZxvL23TQa3JHL2AIGr93BnQjo2SkGJpG9xDX7S2thDpAQsCconWHAwe6cJTnjeeHbuC84r367L3C3Rzay&uid=LCQI%2F1P2Lj%3D)

<sup>5</sup> <https://www.allenoverly.com/en-gb/global/news-and-insights/publications/new-esg-disclosure-regulation-sfdr-what-private-banks-wealth-managers-and-advisers-need-to-know>

<sup>6</sup> <https://www.allenoverly.com/en-gb/global/news-and-insights/publications/esg-and-sfdr-regulatory-developments-for-funds-and-asset-managers>

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