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18 June 2024

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# Joint ESAs Opinion

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On the assessment of the Sustainable Finance Disclosure Regulation  
(SFDR)

# Content

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<b>1. Executive Summary</b>	<b>2</b>
<b>2. Overarching principles and considerations</b>	<b>6</b>
<b>3. ESAs' Opinion to the Commission</b>	<b>10</b>
<b>3.1 A system of product classification</b>	<b>10</b>
<b>3.2 Sustainability indicator</b>	<b>13</b>
<b>3.3 Sustainable investment definition</b>	<b>16</b>
<b>3.4 Relevant documentation for product disclosures</b>	<b>18</b>
<b>3.5 Products in scope</b>	<b>18</b>
<b>3.6 Transparency of adverse sustainability impacts</b>	<b>19</b>
<b>Annex I: Other technical issues</b>	<b>21</b>
<b>Annex II: Product type by sustainability objective</b>	<b>23</b>

# 1. Executive Summary

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## Legal Basis

1. The European Supervisory Authorities (the ESA's) have decided to deliver this Opinion on their own initiative under Article 16a of Regulations (EU) No 1093/2010, (EU) No 1094/2010 and (EU) No 1095/2010.<sup>1</sup>
2. In accordance with Article 44(1) of those Regulations, the Boards of Supervisors of the ESAs have adopted this Opinion which is addressed to the Commission. A copy of this Opinion has been sent to the European Parliament and the Council.

## Content and reasons for publication

3. In September 2023 the European Commission (hereinafter 'the Commission') launched a targeted consultation<sup>2</sup> and a public consultation<sup>3</sup> on Regulation (EU) 2019/2088 (hereinafter 'the SFDR').<sup>4</sup>
4. The ESAs have developed through the Joint Committee (JC) several sets of draft Regulatory Technical Standards (RTS) under the SFDR. In particular, the ESAs were first empowered by the SFDR, and later through further amendments to the SFDR made by Regulation (EU) 2020/852<sup>5</sup> (the 'EU Taxonomy'), to deliver several draft RTS on the content, methodologies and presentation of sustainability-related disclosures<sup>6</sup>. Moreover, following the most recent mandate from the Commission<sup>7</sup>, on 4 December 2023 the ESAs also published the Final Report on draft RTS on the review of principle adverse impact (PAI) and financial product disclosures in the Commission

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<sup>1</sup>Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12); Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48); and Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC (OJ L 331, 15.12.2010, p. 84).

<sup>2</sup>[finance-2023-sfdr-implementation \(europa.eu\)](#)

<sup>3</sup>[Sustainable Finance Disclosure Regulation - assessment \(europa.eu\)](#)

<sup>4</sup> The SFDR lays down harmonised rules for financial market participants and financial advisers on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes and the provision of sustainability-related information with respect to financial products.

<sup>5</sup> 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 (OJ L 198, 22.6.2020, p. 13).

<sup>6</sup> Under empowerments in Articles 2(3)(a), 4(6) and (7), 8(3), 9(5), 10(2) and 11(4) of the SFDR.

<sup>7</sup> [Mandate to esas on pai product.pdf \(europa.eu\)](#)

Delegated Regulation (EU) 2022/1288<sup>8</sup> supplementing the SFDR, ('the SFDR Delegated Regulation')<sup>9</sup>.

5. The ESAs have also developed practical application responses to questions on the SFDR<sup>10</sup> and have coordinated how the competent authorities have started supervising the SFDR disclosures. This is why the ESAs, and competent authorities, in their role as national supervisors, are well placed to offer the Commission their unique perspective on how instrumental SFDR has been in both increasing transparency on sustainability features for the benefit of investors in the context of the Green Deal objective and to channel capital towards sustainable investment.
6. The ESAs acknowledge that the framework could be improved and that the disclosures to investors in the SFDR may be complex by nature and difficult to understand, in particular for retail investors. This has been shown by two consumer testing exercises. The latest round of testing in the context of the Final Report on draft RTS on the review of PAI and financial product disclosures in the SFDR Delegated Regulation showed that respondents found the SFDR templates 'complicated and hard to read'<sup>11</sup>. In addition, while the SFDR was designed to enhance transparency around sustainability, the ESAs have noted that, in practice, disclosures have been used by financial market participants to classify their financial products. Status as 'Article 8' or 'Article 9' products have been used since the outset in marketing material as 'quality labels' for sustainability, consequently posing greenwashing and mis-selling risks. The Commission has rightly identified this shortcoming in its consultation, asking for feedback about the usefulness of uniform disclosure requirements for financial products across the board, regardless of related sustainability claims, consulting on the option to depart from the general philosophy of the SFDR on product disclosures.
7. To eliminate the risk of misuse of the SFDR, this Opinion focuses on the merits of the introduction of a categorisation system and/or an indicator of sustainability for financial products to allow for simplified disclosures that empower retail investors to better understand the underlying sustainability profile of financial products. Other topics covered include the review of the definition of 'sustainable investment' under Article 2(17) of the SFDR and the interaction with a categorisation system, the potential to expand the products in the scope of the SFDR, the simplification of the relevant documentation, and improvements to the transparency of adverse sustainability impacts at financial product level. Finally, this Opinion includes a series of technical changes that the Commission could consider in its assessment of the SFDR [in Annex I].
8. This Opinion calls for a coherent sustainable finance framework that caters for both sustainable finance transition and investor protection, taking into account the lessons learned from the

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<sup>8</sup> Commission Delegated Regulation (EU) 2022/1288 of 6 April 2022 supplementing Regulation (EU) 2019/2088 of the European Parliament and of the Council with regard to regulatory technical standards specifying the details of the content and presentation of the information in relation to the principle of 'do no significant harm', specifying the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts, and the content and presentation of the information in relation to the promotion of environmental or social characteristics and sustainable investment objectives in pre-contractual documents, on websites and in periodic reports (OJ L 196, 25.7.2022, p. 1).

<sup>9</sup> [JC 2023 55 - Final Report SFDR Delegated Regulation amending RTS \(europa.eu\)](#)

<sup>10</sup> [JC 2023 18 Consolidated JC SFDR QAs \(europa.eu\)](#)

<sup>11</sup> [Final Report on draft RTS on the review of PAI and financial product disclosures in the SFDR Delegated Regulation \(europa.eu\)](#)

functioning of the SFDR and building on the objectives of the proposals of the Retail Investor Strategy to enhance retail investor's trust, confidence, and participation in financing the economy. A summary of the key recommendations is included below.

## Next steps

9. The Commission is assessing stakeholders' responses to support policy considerations to improve the European framework for sustainable finance based on the experience on the implementation of SFDR.
10. In this Opinion the ESAs strongly encourage the Commission to undertake consumer testing when developing policy options to have a stronger evidence basis for changing the regulatory framework and to therefore ensure more successful outcomes. In that respect, empowering retail investors to better understand how the underlying sustainability profile of financial products ultimately serves the purpose of facilitating capital allocation to sustainable investment. The ESAs stand ready to support the Commission in providing any necessary additional technical assistance related to the disclosure elements in the SFDR, within the appropriate timeframe.

## Summary of the ESAs' recommendations to the Commission

- a) The Commission could consider the introduction of a product classification system, based on regulatory categories and / or sustainability indicator(s) to help consumers navigate the broad selection of sustainable products and support the full transition to sustainable finance;
- b) The categories should be simple with clear objective criteria or thresholds, to identify which category the product falls into. The ESAs encourage, at least, categories of 'sustainability' and 'transition';
- c) A sustainability indicator could refer to environmental sustainability, social sustainability or both, illustrating to investors the sustainability features of a product in a scale;
- d) Options for product categorisation and /or sustainability indicator(s) should be consumer tested and consulted on. With clear product categories and/or sustainability indicator(s), sustainability disclosures would not need to be as detailed and extensive;
- e) The Commission could revisit the coexistence of the two parallel concepts of "sustainable investment" as defined in the SFDR and Taxonomy-aligned investment as defined in the EU Taxonomy. The EU Taxonomy constitutes a science-based reference point against which to measure environmental sustainability, whereas the SFDR is more principle based and less prescriptive than the EU Taxonomy when it comes to measurement of sustainable investments. The Commission should prioritise completing the EU Taxonomy and extend it to social sustainability;
- f) The ESAs strongly recommend that the Commission ensures that sustainability disclosures cater to different investor needs, and improvements in sustainability disclosures should take into account different distribution channels, including digital ones, and ensure consistency of information provided. The Commission should prioritise only essential information for retail investors while professional investors may benefit from more detailed information;
- g) The Commission could carefully reflect on whether to include other products in the SFDR scope to ensure harmonised disclosures for both products currently in the scope of SFDR and any other products that could be brought in to the scope;
- h) Information on key adverse impact indicators could be considered for all financial products, based on a cost-benefit analysis justifying the introduction of such requirement; and
- i) The Commission could evaluate the introduction of a framework to assess the sustainability features of government bonds, taking into account the specificities of that asset class.

## 2. Overarching principles and considerations

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### 2.1 Consumer testing

11. The comprehensibility of any proposed new disclosure regime to retail investors will be important for the success of any future changes to the SFDR framework. This is why the ESAs consider it of utmost importance that the Commission, as part of its impact assessment of any revisions to the legal text, undertakes consumer testing that is designed according to behavioural science on any part of the assessment of the SFDR that can affect consumers' use of sustainability-related disclosures before proposing policy changes.
12. Bearing in mind the Better Regulation agenda<sup>12</sup> (ensuring that EU policymaking is based on evidence, EU law is made simple and better, based on citizens', businesses, and stakeholders' involvement in the decision-making process) consumer testing will ensure that information is provided to consumers in a simple, unambiguous, and non-technical language. The key objective is to establish a system of classification that does not give false impressions about sustainability to end investors and guides consumers in selecting products that meet their sustainability preferences. In addition, to the extent feasible, a public consultation allowing industry feedback would also be useful to generate input from the financial market participants offering relevant financial products.

### 2.2 Overarching principles and policy considerations

13. As a starting point, the ESAs would like to provide the following suggestions on the principles and policy considerations for the Commission when setting up a classification system in the review of SFDR:
  - a) **Usability and understandability of the product categories:** past ESAs consultations, engagement with consumer organisations and consumer testing conducted on the SFDR documents have shown the challenges retail investors face in understanding and navigating the complexity of the current disclosures. The approach to build product categories needs to focus on clear, simple and concise consumer facing information that steer away from technical jargon and the complexity of underlying technical concepts. With clear product categories, it could also be argued that sustainability disclosures would not need to be as detailed and extensive. The product categories could be applied by financial market participants on a voluntary basis, but the Commission could also test a mandatory regime similar to how SFDR currently works.

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<sup>12</sup> The Better Regulation Toolbox: [9c8d2189-8abd-4f29-84e9-abc843cc68e0\\_en \(europa.eu\)](https://ec.europa.eu/better-regulation/)

- b) **Comparability across different types of financial products:** while it is important to consider the purpose of the underlying sectoral disclosures to which the SFDR templates are attached, the ESAs encourage consistency on the content between the SFDR disclosures and other documents, including pension schemes' Benefit Statements or Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs KID).
- c) **Digitalisation and layering:** In the context of the ongoing discussions within the Retail Investment Strategy proposal, the Commission should also reflect on the ongoing digital transformation of the economy and facilitating the provision of information to retail investors in a digital format which allows layering and is engaging when delivered on a screen.
- d) **The ability for the categorisation to cater for the sustainability transition:** the Commission is encouraged to include the concept of "transition investment" in the SFDR<sup>13</sup>, with clear objectives and expectations, to allow the development of a 'transition financial product category' where the focus is on investments in economic activities, assets or portfolios, not yet sustainable, but aiming to become sustainable over time. The pathway to sustainability should be compatible with EU and global headline environmental and social objectives, in terms of ambition and timeframe. This category is expected to support investments that will help deliver on the 'Fit for 55' package, the EU commitment of climate neutrality by 2050 and the objective of limiting global warming to 1.5 degrees. The category could support progress towards other environmental objectives, and if feasible also social objectives.
- e) **Clear eligibility requirements:** clear requirements (and, for environmental categories, science-based eligibility requirements), to facilitate investors' understanding of the key characteristics and objectives of the product, uphold the integrity of the categories and build investor trust.
- f) **Treatment of government bonds:** The Commission could consider how to treat the sustainability of government bonds, on the basis of general criteria<sup>14</sup> that should take into account the fact that developing such methodology can be challenging, considering the connection with the public policies of sovereign issuers, especially where the use of proceeds is unknown. Without at least general criteria to assess the sustainability of investments in government bonds, it will be very difficult for products heavily invested in government bonds, such as insurance-based investment products and pension schemes to fully disclose on the sustainability features of their investments. Therefore, a framework for government bonds – useful for all financial products which may invest in government bonds – could be developed gradually over

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<sup>13</sup> The Commission could build this concept on [Commission Recommendation \(EU\) 2023/1425 of 27 June 2023 on facilitating finance for the transition to a sustainable economy \(\(OJ L 174, 7.7.2023, p.19\)](#)

<sup>14</sup> There is already a relevant review clause related to government bonds in Article 9(1)(a) of Delegated Regulation 2021/2178 with regard to the inclusion of central governments and central banks in the key performance indicators of financial undertakings disclosed pursuant to Article 8 of Regulation 2020/852.



time and phased in to allow market participants, including issuers and investors, sufficient time to adapt to the new criteria.

- g) **Naming and marketing:** Existing behavioural research shows that product names are important for retail investors, whose investment decisions may be driven by product names and marketing material (in particular on websites/social media). To ensure investor protection, the name should accurately reflect the sustainability profile of the product. In addition to the Commission's focus with SFDR on transparency, certain sustainability-related terms should only be allowed for products that fall in a certain category to ensure consistency with product categories and avoid the use of names that are misleading. Products that do not qualify for any category should be restricted from using certain sustainability-related terms in their name. Similarly, having more detailed rules in place to ensure that a product's marketing material is in line with the product's sustainability profile would also help in tackling greenwashing risks.
- h) **Transparency obligations:** concrete, and quantifiable transparency about sustainability features, for products that qualify for categories, to enable investors to assess the ambition of the products and whether the investment strategy is compatible with delivering on the objectives. Disclosures could also be specifically linked to the product category. However, as mentioned under point a), with clear product categories, it could also be argued that sustainability disclosures for products disclosing within the categories would not need to be as detailed and extensive any longer.
- i) **EU Taxonomy as a pillar to inform the environmental categorisation:** the EU Taxonomy stands at the core of the EU Sustainable Finance ambition. The Commission should build on science-based tools developed so far (the six environmental objectives and the ESRS disclosures).
- j) **Consistency with other EU laws on sustainable finance:** in the spirit of adopting a holistic approach, it is important for the Commission to carefully test the consistency across the various pieces of legislation that include sustainability references, and check inconsistencies and misalignment, both in the current texts (i.e. Taxonomy and Benchmarks Regulations, Corporate Sustainability Reporting Directive, Markets in Financial Instruments Directive and Insurance Distribution Directives, the ESG Ratings Regulation and the Corporate Sustainability Due Diligence Directive) but also those legal acts currently negotiated that might interact with the SFDR in the future (i.e. Regulation on key information documents for Packaged Retail and Insurance-based Investment Products (PRIIPs) in the context of the Commission's Retail Investment Strategy).
- k) **Interoperability with international initiatives:** the EU framework does not work in a vacuum, and other jurisdictions are moving in the same direction of considering product categories for retail investors. If feasible, the Commission should consider efforts made by jurisdictions such as the UK, the US and recently Australia, to avoid

unnecessary duplication and to ease interoperability amongst the various frameworks.

## 3. ESAs' Opinion to the Commission

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### 3.1 A system of product classification

14. The ESAs are in favour of the introduction of regulatory product categories that would help address the greenwashing problems arising from the misuse of the disclosures under Article 8 and Article 9 of the SFDR and generate clarity for investors, in particular retail investors.
15. Despite SFDR being conceived by the co-legislators as a disclosure regulation, the two disclosure regimes set out in Article 8 and Article 9 of the SFDR have been used as sustainability labels by financial market participants and understood as labels by investors<sup>15</sup>. This approach has undermined the intended goal of the disclosures and created confusion for investors.
16. A problem observed by the ESAs so far is that the category of financial products under Article 8 of the SFDR is too broad, because the “promotion of environmental or social characteristics” referenced in that Article encompasses a very broad range of sustainability ambition, making it difficult for investors to understand how sustainable the financial product may be. The Commission confirmed the broad nature of Article 8 in an interpretative Q&A in July 2021<sup>16</sup>.
17. On the other hand, disclosures under Article 9 of the SFDR have also been problematic, despite the link with sustainable investments defined in Article 2(17) of the SFDR. Investors and distributors have relied on the requirement that products under Article 9 of the SFDR must make sustainable investments. However, the definition of sustainable investments has itself led to limited comparability as to what is considered a sustainable investment, because of wide discretion given to product manufacturers<sup>17</sup>.
18. In its targeted public consultation on the assessment of the SFDR, the Commission has explored the option of building product categories on existing disclosures under Articles 8 and 9 of the SFDR. The Commission noted that this could be done by developing further the distinction between the two articles and existing concepts embedded in them. This approach would entail less drastic changes to the existing framework as it elaborates on current concepts and further define existing elements, such as the application of the ‘Do No Significant Harm’ (DNSH) principle, the interaction between the notion of taxonomy-alignment and sustainable investments and adding criteria to distinguish between products disclosing under Articles 8 and 9 of the SFDR. However, it is noted that the current SFDR concepts such as ‘sustainable investment’ or ‘environmental and/or social characteristics’ have been interpreted disparately.

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<sup>15</sup> Please see ESMA [Progress Report on Greenwashing](#) and ESMA Consultation Paper on Funds names Guidelines: [esma34-472-373\\_guidelines\\_on\\_funds\\_names.pdf \(europa.eu\)](#) and EIOPA Progress Report on Greenwashing at [EIOPA's Progress Report on Greenwashing - Advice to the European Commission - European Union \(europa.eu\)](#).

<sup>16</sup> Q&A V.2 in the [Joint SFDR Q&As](#).

<sup>17</sup> This was clarified in the European Commission’s interpretative Q&A II.1 in the Joint SFDR Q&A. The Commission stated that “The definition of sustainable investment set out in Article 2, point (17), SFDR does not prescribe any specific approach to determine the contribution of an investment to environmental or social objectives. Financial market participants must disclose the methodology they have applied to carry out their assessment of sustainable investments, including how they have determined the contribution of the investments to environmental or social objectives, how investments do not cause significant harm to any environmental or social investment objective and how investee companies meet the ‘good governance practices’ requirement”.

19. Through this Opinion, the ESAs provide the Commission with some overarching principles and policy considerations for the Commission to use when setting up a product classification system, which would enable investors to assess and compare different products based on their sustainability objectives.

### 3.1.1 Categories for products that have sustainability features

20. The ESAs are of the view that the introduction of categories of products that have sustainability features, will improve consumer understanding of the sustainability features of financial products, which is what the products are meant to deliver in terms of sustainability. Such categories would replace the current practice of categorisation in Article 8 and 9 of the SFDR, i.e., products would no longer be differentiated between those promoting environmental/social characteristics and those with sustainable investment as their objective.

#### 3.1.1.1 New categories

21. Building on the considerations expressed so far, the ESAs suggest, as a starting point, the following new categories. The product categories should consist of minimum criteria and not labels of excellence of “best in class” products:

- a) **Sustainable product category:** for products that invest in economic activities / assets that are already environmentally and/or socially sustainable. Considering the difference in maturity between environmental and social topics, and in the absence of a social taxonomy, the Commission could consider whether “sustainable products” should be (1) merged in a single category or (2) split in two different categories (environmental or social). Sustainable products should comply with a minimum “sustainability threshold” as part of the product’s investments. For environmentally sustainable products such a threshold should be based on investments in taxonomy-aligned economic activities. The required minimum taxonomy-alignment could evolve over time as taxonomy-aligned activities are expected to grow in the coming years. The part of the investment that is not taxonomy-aligned should at least respect the DNSH principle for environmental and social objectives and good governance requirements, provided those concepts are more precisely defined than what is currently in the SFDR. Without appropriate specifications, the DNSH principle could impede product comparability and contribute to legal uncertainty faced by financial market participants. In order to be able to apply this category across products, the sustainability of government bonds could be assessed as referred to in paragraph 13(f).
- b) **Transition product category:** for products that invest in economic activities / assets that are not yet sustainable, but which improve their sustainability over time to become environmentally or socially sustainable. The investment strategies of these products could build on a mix of EU taxonomy KPIs to reflect the progressive improvement of environmental performance, transition plans disclosed by underlying assets and their analysis, product decarbonisation trajectories, and mitigation of PAIs at product level (provided that specific and relevant indicators are designed and that a minimum level of mitigation is set out in the Regulation). Additionally, this product category could consider certain appropriate exclusions

and criteria for a credible transition plan.

The ESAs recommend that the Commission reflect on the benefits and drawbacks of requiring that an ambitious but realistic share of the product's investments initially complies with the requirements of the transition product category and that such a share can subsequently increase over time. This would make it possible to include some long-term products, in particular profit participation<sup>18</sup> products and pension funds, that face restrictions or disincentives to change their asset allocation over time. The matching principle requires insurers and pension funds to hold certain long-term assets, such as government bonds<sup>19</sup>, with cashflows that match their long-term liabilities. Over time, with a clear path, a gradually higher share of these products' investments should comply with the requirements of this transition product category. Care should be taken to calibrate the share of transition investments growing over time appropriately, because the transition product category could include diverse products and transition paths.

Transparency obligations for transition products should provide investors with clarity on the level of ambition and performance in the short and long term (including quantitative targets and intermediate milestones) and how the investment strategy delivers on the ambition. Furthermore, it would be not necessary to apply the DNSH principle to all investments to support investments to activities that are currently harmful, but which are in a transitioning trajectory, or in activities that are permanently harmful, but which are in the process of being decommissioned. This could be demonstrated by measurable transition plans by companies engaged in such harmful activities. Lastly, the Commission could also reflect on whether there could be a sub-category under the transition category for "investor's impact"<sup>20</sup>, designed for products that invest in economic activities / assets that aim to offer solutions to sustainability-related problems (i.e., a positive measurable impact on an environmental or social objective) together with a financial return. Alternatively, this could be a cross-cutting indicator for all categories based on the "impact potential" scoring. It is important that any "impact" sub-category would have to be sufficiently clear for retail investors to understand.

### *3.1.1.2 Disclosures and marketing for products inside and outside the categories*

22. The ESAs propose that the sustainability disclosures for products that would fall under the proposed new categories could be adjusted to focus on the theme of the category. Financial products that would not qualify for any of the categories could be divided into financial products that have sustainability features and those that do not have sustainability features.

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<sup>18</sup> Product participation products are insurance contracts which provide insurance benefits through eligibility to participate materially in periodic discretionary distributions based on product arising from the insurance undertaking's business, the so called 'general account' of the insurer. These products usually have a minimum guarantee return or capital protection. These products generally offer a biometric risk cover (e.g. death, life, disability...)

<sup>19</sup> Government bonds with specific durations can be used to match the duration of these liabilities, helping to manage interest rate risk. Such investments' sustainability contribution cannot yet be assessed, hence the request for the Commission to develop minimum criteria to assess investments in government bonds, duly taking into account the specificities of such asset class and with the aim of detecting situations clearly not compatible with sustainable principles.

<sup>20</sup> The literature about impact differentiates between "company impact" and "investor impact". The former is defined as "the change in the world caused by company activities, while the latter is "the change in company impact caused by investment activities. See F. Heeb, J. Kölbel, *The investor's guide to impact*, pp.8-9.

- 23. Products that have sustainability features but that do not qualify for the categories should be required to disclose on their sustainability features in regulatory documents (but not the KID because this type of disclosure is more technical and substantial in nature and therefore fits best in a prospectus and not in a KID which is supposed to be non-complex /short) and should face restrictions on using ESG or sustainability-related terms in naming and marketing to prevent greenwashing.
- 24. The ESAs recommend that products that do not have sustainability features at all should be required to include a disclaimer (e.g., like the disclaimer in Article 7 of the Taxonomy Regulation) and should not be allowed to use ESG or sustainability related terms in naming and marketing. The ESAs suggest that, after considering the costs and benefits, the disclaimer could be supplemented by some minimal disclosures on the product’s negative impact on sustainability while differentiating these products from those within the product categories.
- 25. Furthermore, current disclosures under Article 6(1) SFDR covering how sustainability risks are integrated into investment decisions remain relevant for all financial products. A table summarising these ideas is provided below.

Type of financial product	Disclosures and marketing suggestions
Category products	<ul style="list-style-type: none"> <li>- Disclosures in regulatory documentation appropriate to the category</li> <li>- Naming and marketing consistent with category</li> </ul>
Products that have some sustainability features but do not qualify for categories	<ul style="list-style-type: none"> <li>- Limited disclosures in regulatory documentation on sustainability features</li> <li>- Restrictions on naming and marketing</li> </ul>
Products with no sustainability features	<ul style="list-style-type: none"> <li>- Minimal disclosures on adverse impact on sustainability</li> <li>- Disclaimer to make clear that product has no sustainability features</li> <li>- Restrictions on naming and marketing</li> </ul>

**3.2 Sustainability indicator**

- 26. A sustainability indicator for all financial products covering environmental sustainability, social sustainability, or both, illustrating to investors the sustainability features of a product in a scale could simplify complex sustainability information into a format that is more easily digestible for consumers and has been successful in other sectors. For instance, the PRIIPs KID has a synthetic

risk indicator giving retail investors a simple guide to the risk of the product or the Energy Performance Certificate which provides an explanation on the energy consumption and efficiency of a building.

27. Consumer testing and feedback from consumer associations indicates that consumers struggle to understand the different sustainability objectives of financial products and distinction between different objectives, when reading the SFDR disclosures. Consumers found it difficult to grasp how sustainable products are.
28. Subject to consumer testing, such an indicator could group products according to how sustainable the investments are, while also identifying which products foster the transition. One option could be to focus narrowly, at first, on a sustainability indicator measuring climate change mitigation based on financed emissions which is translated to a contribution to climate change presented in nutri-score like system<sup>21</sup>. Another option would be to focus on a broader indicator that would grant the best grade, equally, to sustainable investments and to those transition and transformational investments where the expected impact on the environment or society is significant, based on a decarbonisation target or a social improvement expected from the investment strategy.
29. Furthermore, a grading scale could refer to letters (such as the nutri-score for food products or the energy certificate performance, EPC, for buildings) or colours: those letters and/or colours would reflect the category a product belongs to. For example, the most harmful products could be identified by a red colour, while green and blue colours could signal the most ambitious products (e.g. green for environmental topics and blue for social ones).
30. To ensure it is a trustworthy indicator for end investors, this system should rely on clear and objective criteria, so the scope of each category of this indicator is clearly defined. These criteria could, among others, relate to the EU taxonomy, decarbonisation targets or indicators such as fossil fuel exposures or GHG intensity. For its assessment of the criteria, the Commission could evaluate, by way of the testing highlighted in Section 2 above, whether a single generic sustainability indicator may be implemented in a way that prevents any risk of misunderstanding of the indicator by consumers. Where the Commission determines that there is risk of misunderstanding, it could alternatively consider simplifying the indicator, for example by focusing on a more specific feature like climate change mitigation.
31. The development of a sustainability indicator is not without risks and technical challenges. The ESAs have summarised in the table below some pros and cons of a single indicators working across all products.

<b>Single sustainability indicator</b>	
<b>Pros</b>	<b>Cons</b>

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<sup>21</sup> The nutri-score is a simplified presentation of nutritional information on food packaging. It is currently used in a number of EU Member States (France, Belgium, Germany, Luxembourg, the Netherlands and Spain) as label with the purpose to make it easier for consumers to identify the foods they are buying.

<ul style="list-style-type: none"> <li>- A sustainability indicator referring to letters and/or colours would be easier to understand for retail investor and thus help to reduce information asymmetry.</li> <li>- Benefit of clarity to consumers could justify technical imperfections of indicator approach.</li> <li>- The SFDR already has many concepts on which such a grading scale could be based, such as sustainable investments, taxonomy-alignment and/or PAI consideration.</li> <li>- As investors feel more empowered by the clarity of the indicators, this would ease the advisor-client relationship as the former would not have to explain the different underlying concepts like sustainability or transition to his or her clients.</li> </ul>	<ul style="list-style-type: none"> <li>- The development of a single indicator would require aggregating different topics and their related criteria. It makes it difficult for the Commission to develop precise and objective criteria, and difficult for investors to understand the difference between products.</li> <li>- The requirement to provide some information for all products will increase compliance costs.</li> <li>- Unless specifically addressed, a grading system could raise the risk that investments in transition would be perceived as less desirable than “sustainable investments”.</li> <li>- Unless accompanied by clear categories, a single indicator would not be able to show retail investors what the specific objective of the sustainable investments is.</li> </ul>
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32. A sustainability indicator need not be mutually exclusive with product categories. It may also be possible to consumer test a sustainability indicator working separately within each of the categories proposed in Section 3.1.1.1, for instance by using different shades of the same colour in a given category. However, this could increase complexity for retail investors who may not necessarily be able to compare the sustainability of products in different categories or think that the different indicators are the same grading.

33. Another alternative would be designing the sustainability indicator to work outside the categories. The sustainability indicator would still show the sustainability of the products, defining the intensity of sustainability alongside a categorisation framework. I.e., a product could qualify for a category while also being given a grade in a sustainability indicator. Such an approach could be designed without putting at disadvantage transition category products. The highest ‘grade’ could treat equally products in transition category and sustainability category products. It could also increase the complexity for retail investors who would have to understand how the categories interact with the “grade” in the indicator, but at least all products would be assessed on the same scale.

### 3.2.1 Options for sustainability indicator

34. Therefore, the Commission could test three scenarios to determine what works best:

- a) a framework consisting only of product categories outlined in paragraph 21 of this Opinion;



- b) a framework consisting only of a mandatory single sustainability indicator described in paragraphs 26-31 of this Opinion; or
- c) a combination of the two: product categories and a sustainability indicator (either working separately within each category or working outside the product categories) showing the sustainability intensity of all products as described in paragraph 32-33 of this Opinion.

35. The ESAs have illustrated in Annex II of this Opinion how these scenarios could work in practice for different types of hypothetical financial products.

### 3.3 Sustainable investment definition

36. The SFDR has played a crucial role in the sustainable finance framework, as it has provided a framework and structure for enabling consumers and investors to make informed investment decisions in relation to sustainable matters. While the intention of the SFDR was to increase the comparability and disclosures of financial products on sustainable matters, since the key parameters of ‘sustainable investment’ under Article 2(17) of the SFDR are principle based, those parameters gave financial market participants flexibility, but this also led to differences in application<sup>22</sup>. To ensure a more uniform application, the ESAs therefore suggest that the Commission should consider making these key parameters under Article 2(17) of the SFDR prescriptive. Depending on how criteria for a categorisation system and/or sustainability indicator(s) are developed, and/or there is a full taxonomy covering also social sustainability, the Commission could revisit the need for a sustainable investment definition.

37. Under Article 2(17) of the SFDR, the concept of ‘sustainable investment’ means an investment in an economic activity that contributes to an environmental or social objective, where the investment does not significantly harm any environmental or social objective and investee companies follow good governance. By contrast, the Taxonomy Regulation is based on the classification of economic activities as environmentally sustainable, based on substantial contribution and not doing significant harm to six prescribed environmental objectives and that the economic activities are carried out in compliance with the minimum safeguards laid down in Article 18 of the Taxonomy Regulation. Detailed technical screening criteria outline compliance with substantial contribution and the DNSH test.

38. The result of consumer testing<sup>23</sup> has also shown that consumers find the distinction between the concepts of ‘taxonomy-aligned’ and ‘sustainable’ investments challenging, finding it artificial and difficult to grasp. As shown in the consumer testing reports<sup>24</sup>, ‘sustainable investments’ are perceived as more sustainable than taxonomy-aligned investments despite efforts by the ESAs to explain the differences in explanatory boxes in the margins of the templates.

39. The ESAs note the efforts made by the Commission in clarifying the definition of sustainable

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<sup>22</sup> [JC 2023 18 Consolidated JC SFDR QAs \(europa.eu\)](#)

<sup>23</sup> [Final Report on draft RTS on the review of PAI and financial product disclosures in the SFDR Delegated Regulation \(europa.eu\)](#)

<sup>24</sup> [ESAs put forward amendments to sustainability disclosures for the financial sector \(europa.eu\)](#)

investment in a series of published Q&As<sup>25</sup>. In particular, the Commission explained that the notion of sustainable investment can be measured at the level of a company and not only at the level of a specific economic activity. In an FAQ26, the Commission has also introduced the concept of ‘safe harbour’ to partly clarify the relationship between environmentally sustainable economic activities and sustainable investments, since taxonomy-aligned investments can be automatically qualified as ‘sustainable investments’ in the context of the product level disclosures under SFDR. This clarification addresses the issue of the double assessment of those investments under both the Taxonomy Regulation and SFDR. However, the Commission notes that, for investments in an undertaking with some degree of taxonomy-alignment through a funding instrument that does not specify the use of proceeds, which represent most investments, financial market participants would still need to check additional elements under the SFDR in order to consider the whole investment in that undertaking as a sustainable investment. This means that the financial market participants would still need to: (i) check whether the rest of the economic activities of the undertaking comply with the environmental elements of the SFDR DNSH principle; and (ii) assess whether they consider the contribution to the environmental objective sufficient.

40. The ESAs consider that it is important to reflect not only on the question of the co-existence of these two parallel concepts in the sustainable finance framework that are difficult to understand for investors, but also the role that the sustainable investment definition under Article 2(17) of the SFDR could play in case a categorisation system is implemented.
41. If the Commission decides to make the key parameters of ‘sustainable investments’ prescriptive as suggested by the ESAs, the ESAs believe that it will ensure a more uniform application across the EU financial sector and strengthen the comparability of the proportion of the sustainable investments across the financial products. At a minimum, the relationship between sustainable investments and investments in taxonomy-aligned activities should be clarified by the Commission in the current legal framework. The Commission could, e.g., clarify that if an economic activity is described in the technical screening criteria to the environmental objectives of the Taxonomy Regulation (i.e., is taxonomy-eligible), the financial market participant should only consider the economic activity to be (environmentally) “sustainable” and thus only assess if the economic activity fulfils the criteria for environmentally sustainable economic activities in the Taxonomy Regulation (i.e. is taxonomy-aligned). This also means that where an economic activity is not described in the technical screening criteria (i.e., it is not taxonomy eligible), the financial market participant would rely on appropriate sustainability metrics and minimum requirements under SFDR to consider whether the activity is sustainable.
42. The ESAs believe that the EU Taxonomy constitutes a science-based reference point against which sustainability performance can be measured and invite the Commission to complete it for (1) all activities that can substantially contribute to environmental sustainability and (2) social sustainability.
43. In the interim period, since there is no social taxonomy for the moment, the Commission could amend the current definition in Article 2(17) of the SFDR to rely on the EU Taxonomy for disclosures on environmental sustainability. For other economic activities (i.e., non-eligible economic activities and

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<sup>25</sup> [JC 2023 18 Consolidated JC SFDR QAs \(europa.eu\)](#)

<sup>26</sup> [EUR-Lex - 52023XC0616\(01\) - EN - EUR-Lex \(europa.eu\)](#)

social sustainability) the ESAs suggest the Commission should use appropriate sustainability metrics, e.g., related to the current PAI indicators developed by the ESAs in the SFDR Delegated Regulation and the current requirements on DNSH and good governance. This would lead to a distinction between 'environmental sustainability' and 'social sustainability'. Social sustainability could refer to a social taxonomy (when developed) or specific PAI indicator or ESRS datapoints to identify social objectives and related contributions.

### 3.4 Relevant documentation for product disclosures

44. The ESAs have long considered that identical pre-contractual financial product disclosures are very challenging when the underlying pre-contractual documents listed in Article 6(3) of the SFDR are of such a heterogeneous nature.
45. It has not always been possible to fully take on board all the results of previous consumer testing exercises (i.e., heavily reducing the level of complexity used in the language in the templates) due to the need *inter alia* to ensure comparability across all the different types of underlying sectoral disclosures in Article 6(3) of the SFDR. The results have shown that the simplified disclosures for retail investors should be in the form of a Key Investor Document, while more complex information could be separately included on websites and in documents like the prospectus.
46. The ESAs would like to suggest the following considerations when considering rules on pre-contractual disclosures, starting from the principle that differentiation does not necessarily limit standardisation:
  - a) **the audience of the document:** more sophisticated approaches should be envisaged to cater for the differing needs of investors and the market: very simple disclosures to retail investors and more comprehensive information for more sophisticated investors if applicable. It is important to differentiate information that is key for retail (such as the level of greenness disclosed in a simple and understandable manner in a sustainability indicator as mentioned above) as opposed to technical information relevant to sophisticated investors (i.e. PAI) that would still be available and disclosed to provide full transparency; and
  - b) **adapting the format of the disclosure to the increased digital consumption of the information:** allowing investors to read or process information electronically through layering.

### 3.5 Products in scope

47. The Commission could carefully reflect on appropriate disclosures for products currently outside the scope of SFDR, such as structured products issued under a Euro Medium-Term Note (EMTN) programme, which could benefit from standardised sustainability disclosure requirements comparable to SFDR disclosures. Sustainability disclosure requirements for such products should ensure that the sustainability disclosures do not mislead investors about the sustainability features of these products and are comparable to sustainability disclosures on the investments made by

the existing products in scope of the SFDR.

48. As structured products, like those issued under an EMTN programme, may be financial instruments under MiFID, they may be distributed to clients displaying sustainability preferences. However, in practice this raises many interpretation challenges as it is not clear whether sustainability should be assessed at the level of the issuer of structured EMTN (to whom the investor is exposed), or at the level of the assets or index whose performance will determine the payout to the client. The absence of sustainability disclosures comparable to SFDR-disclosures for structured products therefore leaves room for greenwashing as the actual assessment of their sustainability features is currently made at the sole discretion of their manufacturers.
49. Moreover, structured products may take the legal form of a formula fund, and therefore be subject to the SFDR, or of a structured non-equity note, currently outside the scope of the SFDR. When they have some sustainability features, these two types of financial products should be required to disclose comparable information about those features as suggested in Section 3.1.1.2 above.
50. Amongst the different products in scope, the SFDR also applies to insurance-based investment products. However, there are some specific categories of investment options offered in multi-option products (MOPs) that are currently not addressed in the SFDR disclosures (according to Article 2(12) of the SFDR). The definitions under Article 2(12) of the SFDR have created legal challenges in particular for those products such as MOPs that are not directly mentioned in the Level 1 text.
51. In the case of MOPs operating under non-discretionary management (that is to say the investor decides himself/herself the options he/she invests in), the manufacturer cannot commit to a minimum proportion of Taxonomy-aligned or sustainable investments, and does not know ex-ante whether the product will invest “in an economic activity that contributes to an environmental objective”, Therefore, the Commission may analyse what would be the relevant disclosures at wrapper level.

### 3.6 Transparency of adverse sustainability impacts

52. The current regulatory requirements under Article 4 and 7 of the SFDR have triggered several questions from financial market participants and competent authorities. Notwithstanding the Commission’s Q&A (see ESAs consolidated Q&As<sup>27</sup>) clarifying the meaning of “consideration” of PAIs<sup>28</sup>, further legal certainty is required on what such “consideration” of PAIs entails from products or entities, in particular as to whether the consideration is only about mitigation and whether there is any time horizon or year-on year improvement required.
53. In a future framework, the ESAs believe that while “consideration” is intended to capture disclosure and mitigation of the PAIs of investment decisions on sustainability factors, there is

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<sup>27</sup> [JC 2023 18 - Consolidated JC SFDR Q&As \(europa.eu\)](#)

<sup>28</sup> Joint SFDR Q&A IV.3: “consideration” is not only disclosure of PAIs but also procedures put in place to mitigate those PAIs.

merit in also considering “information” on PAIs. “Information” on PAIs could exclude a requirement to mitigate them, but still provide useful information so that investors have a better idea about the negative consequences of potential investments. By clearly differentiating between “consideration” and “information” the Commission would establish better expectations about the disclosures. Furthermore, “information” would not generate a false expectation that the financial market participant was actually taking actions to reduce the negative consequences.

54. The Commission could consider making “consideration” of PAIs of investment decisions on sustainability factors, based on the indicators in Annex I of the SFDR Delegated Regulation, mandatory for products qualifying for the new sustainability product category. By contrast, the Commission could consider making “information” on all PAIs mandatory for transition category, and some minimal disclosures such as “information” about select key PAIs, selecting a list of priority indicators, mandatory for all financial products that should always be disclosed.
55. If the current framework of PAI disclosure at product level persists, the ESAs believe that the language in Article 7(1)(b) of the SFDR related to the ‘statement’ that the information about the PAI is available in the periodic reports should be clarified, as it is not clear what kind of statement is needed. Furthermore, the ESAs also believe that the language in Article 7(1)(b) of the SFDR, second subparagraph of the SFDR related to “quantifications of principal adverse impacts” should be clarified as it is not clear what the obligation applies at which stage of the product disclosure.
56. For entity level disclosures, the ESAs recognise that where there is overlap with information disclosed under Directive (EU) 2022/2464 (the Corporate Sustainability Reporting Directive or CSRD) the SFDR requirements could be considered to be satisfied. However, where there are requirements attached to the disclosure beyond simply “information”, such as in the consideration of PAIs, that disclosure should not be removed from the SFDR.
57. Any changes to PAI disclosures under Article 7 of the SFDR have to be considered consistently with the recommendation on minimum sustainability disclosures and reflect the broader changes agreed on product categorisation. The ESAs stress that given the current lack of other obligations on due diligence with regard to their investments, PAI disclosure is a very useful source of information and an indirect requirement for financial market participants to ensure some control and due diligence about the negative consequences of their investments.

# Annex I: Other technical issues

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58. In addition to the core elements of the Opinion outlined above, the ESAs would like to use this opportunity to highlight several other technical changes that could be addressed by the Commission in the potential review, based on direct observations and feedback from stakeholders and competent authorities.

- a) *Clarification of the scope of disclosures under Article 4 of the SFDR* - The wording of Article 4 of the SFDR (or the 'Financial Market Participant' definitions in Article 2(1) of the SFDR) could be amended to clarify that unit-linked products should be in the scope of the PAI disclosures at entity level.
- b) *Clarification of the interaction between Articles 3, 4 and 5 of the SFDR and CSRD reporting* – The first CSRD annual reports will be published in 2025, on year 2024, in accordance with sector-agnostic European sustainability reporting standards (ESRS). Sector-specific standards may complement them in the future, including three standards dedicated to financial institutions namely banking, insurance and capital markets. Where there is overlap with comparable SFDR disclosures in Article 3, 4 or 5 of the SFDR, the Commission may consider the potential overlaps and discrepancies between these two reporting frameworks.
- c) *Appropriate requirements for naming and marketing of financial products* – The ESAs have not to date utilised the empowerment to create standardised marketing presentation in Article 13 of the SFDR. Due to the diversity of marketing material, the creation of “standard presentation” appears to be challenging. The Commission might consider deleting the empowerment laid down in Article 13 of the SFDR. Furthermore, the Commission may - consider that both naming and marketing should be subject to specific requirements regarding sustainability features, possibly on the lines suggested in Section 2.2, paragraph 13(g) of this Opinion.
- d) *SFDR related audit and role of funds' depositaries* – As there is currently uncertainty in the market about how the SFDR related disclosures should be audited under sectoral legislation, including *where* the SFDR related disclosures should be included in the periodic reports under Article 11 of the SFDR. This could be the opportunity for the Commission to provide those clarifications in the SFDR text, or where relevant to clarify this under the sectoral legislation. Similarly, it would be useful if the Commission could also clarify the role of funds' depositaries and the extent of the controls to be performed on the SFDR related disclosures where not clear under sectoral rules.
- e) *Report under Article 18 of the SFDR* – Consistent with the recommendation already included in the 2023 Joint ESA's Report on the extent of voluntary disclosures, the ESAs would like to reiterate their views about the need to reduce the frequency of the assessment of the PAI disclosures under the Article 18 of the SFDR (currently on an annual basis). The ESAs see value in these reports, but a less frequent reporting timeline would allow the ESAs and NCAs to focus more resources to deliver a more meaningful analysis of those disclosures. If the Commission

concludes that the report is no longer necessary to evaluate voluntary PAI disclosures, the mandate to issue a report could be deleted altogether.

- f) *Information flow to competent authorities* – Supervisory experience of SFDR information has been mixed to date. Despite pre-contractual and periodic disclosures being subject to sectoral rules (listed in Article 6(3) and Article 11(2) of the SFDR), the transfer of SFDR templates from financial market participants, especially fund managers, to competent authorities in some jurisdictions has not always worked well. Furthermore, SFDR information disclosed on websites is not always sufficiently well identified to competent authorities. The ESAs note that the establishment of the European Single Access Point (ESAP) is expected to resolve many of these challenges, but until then the Commission may consider interim measures to improve the information flow of disclosures from fund managers to competent authorities.
- g) *Harmonisation of website disclosures* – There are diverging practices among market participants regarding the content and presentation of the disclosed information under Article 10 SFDR, including regarding the granularity and exhaustivity of the information provided by the market participants which hampers comparability of products for investors.
- h) *Requirements for the advisers' disclosures to be in a prominent place* – While the disclosures for financial products are subject to the SFDR Delegated Regulation, which include requirements that disclosures are made available in a prominent location that is easy to find, the same does not apply to most of the financial adviser disclosures. The Commission may therefore wish to consider making financial advisers' disclosures also more easily locatable.

# Annex II: Product type by sustainability objective

59. In order to illustrate the categorisation scenarios described in paragraph [34], the ESAs show below the potential treatment of different types of hypothetical financial products under hypothetical scenarios and hypothetical non-defined criteria:

<b>Product type</b>	<b>Scenario 1: Categories only</b>	<b>Scenario 2: Indicator only</b>	<b>Scenario 3: Combination</b>
<b>A: Product with high proportion of sustainable investments</b>	Qualifies for “sustainable” category due to high share of sustainable investments	Benefits from highest grading due to high level of sustainable investments	Qualifies for “sustainable” category with highest grade in the indicator
<b>B: Transition investment focused product</b>	Qualifies for “transition” category based on defined criteria or thresholds	Qualifies for second highest grading due to transition-focused investments	Qualifies for “transition” category with second highest grade in the indicator due to lower share of sustainable investments compared to first product
<b>C: Profit participation product with some sustainability features</b>	Qualifies for “transition” category <u>initially</u> , must comply with increasing share of transition category investments over time to stay in category	Qualifies for third level of grading	Qualifies for “transition” category <u>initially</u> (must comply with increasing share of transition category investments over time to stay in category) and third level of grading in the indicator
<b>D: Generic equity or bond product with simple exclusion criteria</b>	Does not qualify for any category	Qualifies for second lowest (fourth) level of grading	Does not qualify for any category with second lowest, fourth, level of grading in the indicator



<b>E: Generic equity or bond product with no sustainability features and may contain coal and oil investments</b>	Does not qualify for any category	Subject to the lowest possible (fifth) level of grading	Does not qualify for any category and the lowest, fifth, level of grading in the indicator
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