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Frankfurt am Main,
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BVI's[1] key messages concerning the EU consultation on SFDR review

I. BVI's positions at a glance

1. **Entity-level disclosures:** Sustainability-related disclosures at entity level should be streamlined by a horizontal application of CSRD reporting requirements in line with the double materiality principle across all sectors, including the financial services sector. Entity-level transparency requirements under Art. 3, 4(2)(b) and 5 SFDR impose additional burden solely upon financial market participants without discernible benefits and should be deleted.

2. **Product-level disclosures:** We are in favour of maintaining the current concept of sustainability-related disclosures where detailed disclosure requirements apply only to products with explicit sustainability claims. However, should the Commission see added value in introducing transparency in sustainability terms for all financial products, we request that such future standards:

   - focus on a small number of key sustainability indicators that are comparable across different markets and different asset classes,
   - be disclosed only in period reports to avoid misapprehensions for sustainability claims and
   - be mandatory only for financial products that are available to retail investors.

3. **Product classification:** We support the establishment of a voluntary system of product categorisation based on the sustainability propositions of financial products. We recommend distinguishing three product categories:

   - **Focus on positive contribution to an environmental/social objective (corresponding to a wider category A):** This category would encompass products that aim at making a measurable positive contribution to either environmental and/or social objective.
   - **Focus on sustainable transition (corresponding to category D):** This category should apply to products aiming at facilitating sustainable transition and measuring the relevant progress.
   - **Focus on credible sustainability standards including exclusion-based strategies (corresponding to combined categories B and C):** This broader "sweep-up" category could be process-based and rely on credible sustainability standards without aiming at achieving measurable outcomes in sustainability terms.

   All products categories should be designed in a principle-based manner that works for different asset classes as well as for products investing in a variety of assets. **They should require intentionality of outcomes** in line with a product's specific sustainability commitment. **For each category, there should be a set of clear-cut criteria** to enable self-assignment by product manufacturers. **Product categories should be designed to reflect different investor preferences and not be put in a hierarchical order. They should be simple and intuitively**

[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 117 members manage assets of some EUR 4 trillion for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 27%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

comprehensible for retail investors. This should be facilitated by rigorous consumer testing and practical input from distributors. **Introduction of sustainable product categories should be directly linked to a review of sustainability preferences under MiFID and IDD** to enhance their practical relevance and regain confidence of investors.

II. Disclosure requirements at entity and product level

1. Entity-level disclosures

Sustainability-related disclosures at entity level should be streamlined by a horizontal application of CSRD reporting requirements in line with the double materiality principle across all sectors, including the financial services sector. Entity-level transparency requirements under Art. 3, 4(2)(b) and 5 SFDR impose additional burden solely upon financial market participants without discernible benefits and should be deleted.

- CSRD reporting regime covers all information to be disclosed under Art. 3, 4(2)(b) and 5 SFDR with consistent reporting standards for all companies and sectors under the ESRS.
- Reporting of quantitative PAI figures and potential remediating actions/measures under Art. 4(2)(b) SFDR is fully integrated in the ESRS (cf. Appendix B to ESRS 2)
- Quantitative indicators for PAIs are key components of the CSRD disclosures subject to the materiality principle (only material adverse impacts need to be reported); the same approach should apply across all sectors. For the financial services sector, application of the materiality principle would help focusing mitigating or remediating measures, e.g in terms of shareholder engagement, on adverse impacts that are truly material for the environment and/or the society.
- Art. 5 SFDR corresponds to the reporting standard GOV 3 in ESRS 2 on integration of sustainability-related performance in incentive schemes.
- Art. 3 SFDR should be covered by the general standard IRO-1 in ESRS 2 requiring description of the process to identify and manage material impacts, risks and opportunities.
- On balance, there is no need for separate entity-level disclosures under SFDR, abolishing the requirements of Art. 3, 4(2)(b) and 5 would contribute to streamlining sustainability-related disclosures at entity level in future.
- Information would not get lost, but would be delivered under a different framework in a manner that is consistent across sectors.

2. Transparency at the product level: all products

We do not support introduction of uniform disclosure requirements relating to sustainability matters for all financial products offered in the EU. Our preferred solution would be to maintain the current concept of sustainability-related disclosures where detailed disclosure requirements apply only to products with explicit sustainability claims (current Art. 8 and 9). Given that sustainability-related disclosures are often mistaken for dedicated commitments to certain sustainability outcomes, such limited application of sustainability disclosure requirements would help avoiding confusion among investors and might mitigate greenwashing allegations.

However, should the Commission see added value in introducing broader transparency on sustainability-related issues, we request that such future standards (1) focus on a small number of key sustainability indicators that can be deemed comparable across different markets and potentially different asset classes, (2) be disclosed only in period reports to avoid misapprehensions for sustainability claims and (3) be mandatory only for financial

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products that are available to retail investors.

- Professional investors such as insurance companies, pension funds, large corporations etc. generally require much more detailed information that is tailored to their particular needs. Standardised ESG information is of no value to this group of investors, but only create unnecessary burden and nuisance for both product providers who need to provide for it and for investors who eventually have to pay. **Financial products offered solely to professional investors should thus be exempted from mandatory disclosures, unless the investor explicitly requests provision of ESG information.**
- **Regulatory standards for sustainability-related disclosures should thus focus on financial products that are primarily offered to retail investors.**
- As regards details of ESG information, i.e. sustainability indicators and relevant calculation methodologies, proper differentiation between asset-based product categories (securities vs. real estate/other real assets) might be necessary.
- Size of assets under management is subject to volatility and should not be considered an appropriate criterion for differentiating disclosure requirements.

It makes a huge difference whether sustainability-related information is disclosed in pre-contractual documents (as part of product offering) or included in regular reporting. In products without dedicated sustainability claims, information on sustainability factors should be disclosed only as part of regular reporting in order to avoid misapprehensions in terms of product commitments and yet another rise of greenwashing allegations. Such basic sustainability reporting should be clearly distinguished from reporting about implementation of a product's investment strategy.

3. Transparency at the product level: products with sustainability-related claims

The current rigid structure of pre-contractual and periodic disclosures in the standardized ESG annexes leads to many duplications on the one hand and improper breaking up of information that is closely interrelated on the other. The use of legalistic terms in the leading questions for each section further impedes comprehensibility for investors. **The quality of sustainability-related disclosures and its usefulness from investors' perspective could be significantly improved by the following measures:**

- **Precontractual and periodic should be streamlined and focused on the key features of an investment**, comprising:

  - Sustainable investment objectives or characteristics
  - Binding elements of the investment strategy, including potential minimum commitments, for attaining the sustainability objectives or characteristics
  - main KPIs for measuring sustainability performance

- **There should be a clear link between pre-contractual commitments and periodic reporting** (reporting should relate to the attainment, or progress in attaining, of sustainable investment objectives).
- **A clear and logical structure should be consistently applied to pre-contractual and periodic disclosures**. Elements that are not necessary to understand the main features of the ESG proposition as outlined above should be removed. This applies for instance to the current section on asset allocation in pre-contractual disclosures that duplicates the information on minimum commitments already included in other sections of the ESG annexes.

- Standardised pre-contractual and periodic ESG disclosures should be made available on the website in the same format; duplications or overlaps of information for the purpose of website disclosures should be avoided.
- Disclosure of ESG-relevant policies (e.g. engagement policy, internal approach to data and methodologies, sustainable investment approach) should be possible on the website (not in the product-specific section, given that such policies generally apply at entity level) with the option to provide links in legal documents.

III. Categorisation system for sustainable products

BVI supports the establishment of a voluntary system of product categorisation based on the sustainability propositions of financial products. We recommend distinguishing three product categories.

- **Focus on positive contribution to an environmental/social objective (corresponding to a wider category A):** This category would encompass products that aim at making a measurable positive contribution to either environmental and/or social objective as defined in the specific product terms. In order to avoid scientifically sophisticated debates about the definition of sustainable impact, we recommend widening the scope of this product category to include not only impact-generating strategies, but also impact-aligned products that aim at supporting impactful companies and projects. The broader term “contribution” should be used to encompass both impact-generating and impact-aligned investments.
- **Focus on sustainable transition (corresponding to category D):** This category should apply to products aiming at facilitating sustainable transition and measuring the relevant progress. Measurability should be based on sustainability indicators stipulated as binding in the product terms; such indicators should be able to refer in particular to the standardised PAI indicators alongside the EU Taxonomy criteria and other recognised metrics that enable measuring progress in transition.
- **Focus on credible sustainability standards including exclusion-based strategies (corresponding to combined categories B and C):** This product category could be more process-based and rely on credible sustainability standards without aiming at achieving measurable outcomes in sustainability terms (for instance norm-based strategies; thematic investments); could function as a “sweep-up” category.

1. General considerations

The suggested product categories represent **different types of investment approaches and different contributions to sustainability without a specific hierarchy.** They should be designed in a **principle-based manner that works for different asset classes as well as for products investing in a variety of assets (so-called multi-asset-products).** A separate product category for real estate/infrastructure investments not considered necessary.

All product categories should r**equire intentionality of outcomes in line with a product’s specific sustainability commitment.** Financial products should be required to be transparent about the progress in attaining to their commitment but must not be held liable if the outcome falls short of the objective. A guarantee of positive sustainability results, e.g. effective reduction of GHG emissions at the level of target companies or effective mitigation of the gender pay gap, must not be expected. Attainment of sustainability objectives in the real world depends on a variety of

factors, from the macroeconomic parameters to the commitment and success at the level of individual companies/other assets.

For each category, there should be **a set of clear-cut criteria to enable self-assignment by product manufacturers.** This would be particularly relevant in case of mutually exclusive product categories and with regard to potential minimum requirements in sustainability terms. Calculation methodologies for minimum commitments at the product level would need to be standardised in order to warrant a common minimum level of sustainability ambition and comparability for investors.

Introduction of sustainable product categories will only be helpful if it addresses the investors' perspective on sustainability. Plain product categories that are easy to grasp are needed to facilitate understanding of especially retail investors. A review of the criteria for sustainability preferences under MiFID and IDD should be considered an integral part of the initiative at hand, otherwise the reform would be of no practical value:

- The new product categories must be developed with the needs of retail investors in mind,
- Practical testing with real world distribution channels and consumers will be very important and must take place sufficiently in advance in order to be fully evaluated and processed for the final decisions in terms of product categorisation.

2. Distinction between sustainable product categories

<u>General caveat</u>**: We advise against too rigid minimum criteria for sustainable product categories. Sustainable products should be rather required to account for certain elements such as having a dedicated predefined sustainability objective or adopting sustainability indicators for the measurement of outcomes. These key features should, however, not be defined in each and every detail in order to (1) facilitate investment solutions involving different asset classes and different geographical/sectoral focus and (2) avoid inflexibility of the regulatory system that would stifle innovation.**

The new categorisation system should aim at facilitating communication with investors:

- Not all ESG features of sustainable products need to be explained to investors at the point of sale;
- Investor's level of knowledge and absorption capacities should be realistically assessed;
- More flexibility for appropriate client communication would be very welcome.

Disclosures requirements also need to be simplified and focused on the key elements of the sustainable product proposition (objective – strategy – outcome).

<u>Product category A:</u>

- **This category should encompass products that aim at making a measurable positive contribution to either environmental and/or social objective as defined in the specific product terms**.
- In order to avoid scientifically sophisticated debates about the definition of sustainable impact, we recommend widening the scope of this product category to include not only impact-generating strategies, but also impact-aligned products that aim at supporting impactful companies and projects. The broader term "contribution" should be used to encompass both impact-generating and

impact-aligned investments.

- Products with focus on climate or other environmental aspects covered by EU Taxonomy criteria could be obliged to make a minimum commitment to investments in line with the EU Taxonomy; no specific minimum should be prescribed in order to account for different asset classes and regional/industry focus of the individual investment strategy.
- If sustainable investments according to the current concept of Article 2(17) SFDR were maintained as a basis for investments with measurable contribution (focus of product category A), then the future framework would need to address the following challenges:

    - Availability of data for different geographical locations and different asset classes; the approach should be asset class neutral and not discriminate investments e.g. in emerging markets;
    - Sufficiently clear definitions for the relevant criteria establishing sustainable investments and the underlying standards;
    - Introduction of a common calculation methodology for the proportion of sustainable investments at the portfolio level.

- Under this scenario, exclusions would be anyway part of the DNSH test (based on PAI indicators) and should not be required as minimum standard in addition.
- Whatever approach is chosen, availability of data must be thoroughly considered when determining the minimum standards; avoiding an EU-centric approach and applying an international perspective is essential when it comes to assessing data availability.
- Engagement depends on the relevant asset class and progress made by the individual portfolio company, it is hardly standardisable as an element of investment strategy and should not be enforced or required in all circumstances.
- Engagement can only support a company’s activities but cannot be seen as obligation of results for the financial product (no positive outcome can be guaranteed).
- Other criteria relevant for category A: Predefined sustainability indicators to measure and report progress in solving environmental or social problems either by investor’s contribution (impact-generating concept), investment’s contribution (impact-aligned concept) or a combination of these features (e.g. in case of investment in companies that contribute to attaining the SDGs and investor’s engagement for further facilitating the company-driven solutions).

Combined product category B+C:

- **This product category could be more process-based and rely on credible sustainability standards without aiming at achieving measurable outcomes in sustainability terms.**
- Should be per definition a wide “sweep-up” category for products that adhere to credible sustainability standards or invest in sustainability themes.
- Conceivable are norm-based approaches (e.g. investments with a focus on fostering the UNGC or OECD Guidelines for multinational enterprises; the pursuit of SDGs without a specific impact intention), green bond strategies or potentially strategies focused on engagement, alongside sustainability-related thematic investments.
- Some index-tracking strategies may fall under category B as well, where they track selective benchmarks that reflect the credible standard for environmental or social sustainability as specified in the investment objective.
- Category B will meet the needs and preferences of those consumers who are seeking a highly ‘ESG screened’ portfolio that invests predominantly in assets with certain sustainability characteristics or that is demonstrably aligned with a sustainability-related theme (positive screening) – and equally that avoids investments in assets that they do not associate with sustainability (negative screening).
- Both approaches – positive and negative ESG screening – should be admissible either on a stand-alone basis or in combination, provided that they conform to the credible sustainability standard as specified in the product terms.
- The key distinguishing features of category B should thus be:

  - Sustainability objective. Alongside its financial risk/return objective, a category B product should have an objective to invest in assets that meet a credible standard of environmental and/or social sustainability, or that align with a specified environmental and/or social sustainability theme, and thus to constrain investment choices by certain sustainability factors.
  - Consequently, category B products should define binding sustainability factors that support implementation of the credible sustainability standard or sustainability theme and report about their implementation.

Product category D:

- **This category should apply to products aiming at facilitating sustainable transition and measuring the relevant progress.**
- Measurability should be based on sustainability indicators stipulated as binding in the product terms; such indicators should be able to refer in particular to the standardised PAI indicators alongside the EU Taxonomy criteria and other recognised metrics that enable measuring progress in transition.
- Engagement is essential for facilitating sustainable transition in companies but must not be required in any circumstances and not deemed appropriate for all assets.
- Engagement can only support a company’s activities and endeavours but cannot be seen as obligation of results (no positive outcome can be guaranteed – escalation process needed in case ESG progress falls behind the product’s objectives/commitments).
- Application of minimum exclusions for category D products seems counterproductive, given that the entire economy needs to make progress in transition. The concept of transition generally relates to investee companies that often engage in different economic activities (e.g. utility companies provide for power generation and supply from fossil fuels as well as increasingly from regenerative sources). Making progress in transition, companies can phase-out/decommission harmful activities

and expand or build up new business lines, this should not be prevented by exclusions.

- Other criteria relevant for category D: Predefined sustainability indicators to measure and report progress in transition (for example by reference to PAI indicators); in case of strategies aiming at reduction of GHG emissions, such indicators should comprise dedicated decarbonisation pathways.

3. Transitional provisions

- **A sufficiently long transitioning period would be needed in case of introduction of a new product categorisation system**. A high share of the retail investment funds and other EU investment products currently discloses under Article 8 or 9 SFDR and would need to be evaluated and possibly adapted to the new system. Such adaptation will often involve modifications to the product terms, product names and potentially also renewal of product authorisation.
- **Grandfathering rules should apply to products that are closed to new subscriptions.**
- A clear focus on product categorisation for the retail market would help to keep transitioning efforts manageable.