

KEY MESSAGES

AFG believes that the European Commission's objectives for the SFDR level 1 review should be the following:

Simplify, ensure consistency and credibility in the sustainable finance regulatory framework

- Ensure consistency between the different pieces of regulation ; CSRD is the founding ground
- Support SFDR evolution from a transparency regime only to an approach including minimum requirements
- Pursue equivalence with ESMA Funds naming guidelines

Define mandatory product categorisation and clearly include the transition concept in the SFDR framework

- Include a binding and measurable sustainable objectives for all ESG products
- Define product categories: "Sustainable", "Transition", "E, S, G focus"
- Leverage on the existing well-known national ESG and green labels as well as EU Climate Benchmarks

Put the final client at the centre of the sustainable finance regulatory framework

- Align SFDR & MIF/ IDD Sustainability Preferences
- Simplify disclosures by means of unique, shortened, and investor-friendly templates
- Supports the concept of entity-level disclosures on investments made on behalf for third parties under SFDR – and not under CSRD

CONTEXT

The French Asset Management Association (AFG) totally supports the efforts of European co-legislators towards financing a more sustainable economy, in particular legislative and regulatory initiatives to ensure greater transparency and achieve the EU Green Deal objective to reorient capital towards a more sustainable economy.

The Sustainable Finance Disclosure Regulation (SFDR) framework has been in application for a few years now and our members already see a positive impact.

The implementation of this sustainable finance regulatory framework has however been raising numerous challenges and concerns among authorities, financial market participants (FMPs) and investors. **An ambitious review of SFDR is necessary, including a realignment of MiFID/IDD Sustainability Preferences.**

The launch of the "Omnibus" initiative (**CSRD, Taxonomy and CS3D**) is also raising additional questions regarding the implementation of SFDR, the need for interoperability between texts becomes even more stringent now. AFG is closely monitoring the Omnibus file as the post Omnibus CSRD reporting framework (regarding reporting entity coverage and indicators) is the founding ground for the other sustainable finance texts.

AFG believes that the review of SFDR by the European Commission (EC) is the perfect opportunity to address these concerns and has identified key considerations to be taken into account.

1. Inconsistencies between the different pieces of regulation

Sustainable Finance regulations are interconnected by design, and several inconsistencies have impeded their robust implementation and, ultimately, even their very purpose.

We believe that the SFDR review is the perfect opportunity to fix some inconsistencies in the sustainable finance framework and/or reflect on the opportunity to reopen other pieces of regulations to align this framework.

2. Lack of clarity

Some concepts introduced in the regulations seem not to be clearly defined, which may lead to different interpretations between financial market participants and to unlevel playing field across jurisdictions depending on each NCA's own interpretation.

This lack of clarity can also generate confusion among investors, for example:

- The definition of “sustainable investment” is principle-based and leaves room for different approaches between financial market participants.
- The definition of the “promotion of E or S characteristics” is very broad and captures most ESG funds with diverse degrees of ESG commitments.
- There are difficulties to reconcile the product categorisation under the SFDR (“Article 8” vs “Article 9”) and questions asked by financial advisors to assess their clients’ sustainability preferences under MIF and IDD (relying on taxonomy alignment, % of sustainable investments and PAI consideration).
- Complexity of the ESG concepts used by MIF and IDD (taxonomy alignment, sustainable investments, PAI) versus the market reality (very low % of taxonomy alignment of the economy or medium level of sustainable investments) does not help investors in their understanding pertaining to their informed expression of ESG preferences.

The initial objective to have a clear and understandable framework for final investors has not yet been achieved. It is hence essential to simplify and clarify the current framework to allow investors to grasp the real intentionality of offered financial products.

3. Complexity of information to be disclosed

For Article 8 and Article 9 products, FMPs are required to disclose a quite extensive range of information in both the pre-contractual template and the annual periodic report. These disclosures have proven to be quite difficult to be understood by end-investors in most instances. This complexity has disincentivized end-investors from re-allocating their savings towards a more sustainable economy instead of helping them to determine clear sustainable preferences that can be used to offer them most suitable products.

As a general rule, the understanding and knowledge that retail investors have to carry out due diligences on the financial products in which they invest should not be overestimated by the authorities – which has been the case with the current SFDR disclosures.

4. The transition concept is not clearly recognized in the Sustainable Finance Disclosure Regulation

AFG believes it is essential to clearly express the inclusion of the transition finance both in the Sustainable Finance Disclosure Regulation and MIF/IDD, notably through investment strategies which clearly include transition objective. This is essential to allow financial market participants to support companies in the reorientation of capital towards sustainable finance. It should be reminded that the “transition” should also include the social question (“fair transition”).

MAIN OBJECTIVES OF THE SFDR LEVEL 1 REVIEW AND AFG PROPOSALS

The European Commission’s objectives for the SFDR level 1 review should be the following:

- **Simplify, ensure consistency and credibility** in the sustainable finance regulatory framework,
- **Clearly include the transition concept** in the SFDR framework through financial products with a transition strategy objective,
- **Putting the final client at the centre** of the sustainable finance regulatory framework.

AFG believes that the level 1 review should particularly focus on the following points:

1. Ensure consistency between the different pieces of regulation

First, AFG would like to highlight the fact that **regulatory reviews must follow a logical sequence**.

For example, **SFDR revision should be coordinated with the CSRD, CS3D and Taxonomy reviews**. More precisely, SFDR level 2 – delegated regulation 2022/1288 – should be modified to align with the simplification of the ESRS datapoints and the revised VSME, without waiting for the revision of SFDR level 1, notably the simplification of SFDR’s PAI indicators (SFDR level 2 – Annex I) concomitantly to the simplification of the ESRS (quick fix). Such regulatory coordination would avoid burdensome bilateral data requests to companies and reduce dependency on third-party, often non-EU, data providers.

AFG also believes that **the SFDR review should aim at fixing several inconsistencies** that have been identified in the sustainable finance framework, such as for example (unexhaustive list):

- SFDR and Benchmark Regulation (BMR) (ex: Information that benchmark providers are required to disclose under BMR are insufficient for the benchmark users to meet their obligations under the SFDR (i.e. PAIs, SI methodology, “good governance practices”, etc.).
- SFDR and ESMA’s Fund Naming guidelines (ex: need for consistency between the categories used by both texts and to include Fund Naming constraints in the SFDR scope)¹.

¹ This need for consistency should also be taken into account at local regulators’ levels and, more especially, AFG reminds that a large majority of its members supports the French AMF 2020-03 Doctrine to become optional.

2. The SFDR should evolve from a transparency regime only to an approach including minimum requirements

AFG believes that SFDR should not only be a “disclosure regulation” but should evolve to a text that includes sustainable minimum investment requirements for investments products.

To allow for an alignment between financial products objectives and final clients’ needs, it is essential **to clearly define the financial products’ objectives** as well as the improvement of performance indicators with a benchmark reference.

Thus, the notion of “promotion of environmental or social characteristics” should be deleted.

We believe that, without any hierarchisation principle, the framework should focus on the financial products’ strategies and distinguish three mandatory categories:

- **Financial products with a “Sustainable” strategy**

Products whose investments are recognised as sustainable, i.e., positively contributing to a green economy and / or to social objectives. This category typically refers to environmental products with an EU Taxonomy alignment or products investing in green bonds, green infrastructure, green equity, impact investing funds relating to Environment, Social products investing in social bonds or impact investing funds relating to Social, etc. This category also covers products with a high rate of *Sustainable Investments*. We believe that *Sustainable Investments* should be defined at undertakings’ level in a way which is **common, comparable and homogeneous among all FMP²**.

- **Financial products with a “Transition” strategy:**

Products financing the transition to a climate-neutral and sustainable economy. This category may become one of the most important categories facilitating capital reallocation to the transition. The objective will be to be able to capture “transitioning issuers” that need support the most.

This approach typically refers to Environmental products like Net Zero aligned funds, decarbonisation funds, transition-linked-bonds, sustainability-linked-bonds, Paris Aligned Benchmarks, Climate Transition Benchmarks, etc.

The fund objective is measured at the product level and/or on a line-by-line basis.

- **Financial products with a “E, S, G focus” strategy:**

Other products with substantial sustainability features that provide for a credible degree of sustainability materiality. These products can state and demonstrate the presence of **binding environmental, social, and/or mixed ESG factors at the heart of the investment process**, applicable to the whole investment portfolio³.

² AFG highlights the importance for the European Commission to provide a clear definition of sustainable investments in order to make the category both pragmatic and ambitious enough. This definition should be covered by the Level 1 or 2 work of the European Commission.

³ i.e. coverage of more than 80% of the investment portfolio. AFG reminds that the calculation can be done as a NAV (meaningful part) proportion or in number of issuers. In any case, only the meaningful invested part of the portfolio is concerned, not cash nor Efficient Portfolio Management techniques. Derivatives that are entered with an ESG objective, either long or short, are part of the calculation.

The financial product would be required to have one or more relevant E, S and/or G KPI indicators objective(s) pursued that is binding and measurable on the investment portfolio⁴.

Unclassified financial products that are not categorised or not qualified for any other categories should not be allowed to promote sustainability, transition or ESG features.

3. Binding and measurable sustainable objectives

Defining product categories such as **“Sustainable”, “Transition” and “E, S, G focus”** will require a careful balance between rigor and flexibility in order to avoid the risk to define niche categories. As such we believe that minimum investment requirement should be defined at high level without too prescriptive indicators.

Regarding **the PSF recommendations, AFG believes they should be simplified** and that, for all categories, at least **one criterion should be binding and measurable by the FMP, among the list** available in Table 1⁵.

Table 1: Minimum criteria per product category as selected by AFG

Product Category	Minimum Criteria
Sustainable	X% of the investment weighted assets contribute positively through Sustainable Investments and / or Environmental Taxonomy
	PAB exclusions
Transition	Y% of the portfolio is transitioning, measured with credible transition pathways or plans on portfolio and/or investment level.
	Reduction on portfolio level at least in line with best market and/or regulatory standards (decarbonisation, etc..)
	Investments in portfolios tracking Climate Transition Benchmarks (CTBs) and Paris-Aligned Benchmarks (PABs) also known as “EU Climate BMs”
	Committed Taxonomy- aligned CapEx or transitional activities (revenues or CapEx)
	Investments with credible transition plan or science-based targets to be demonstrated by the FMP. Up to Z% (e.g., 20%) investments in companies without transition plan, provided credible engagement strategy with escalation mechanism and ultimately divestment
	Sovereign debt based on Nationally-Determined Contributions (NDCs), climate mitigation, adaptation, just transition and other environmental objectives and performance
	Social and Biodiversity Transition once objectives are developed and recognised
	CTB exclusions
E, S, G focus	W% better than the reference benchmark or investable universe or year- on-year improvement on specified indicators
	Effective reduction of investment universe of at least (e.g. 20%)

⁴ The PAI indicator(s) could be used to measure the progress of the product towards attaining its objective(s) and may be used for setting engagement targets with investee companies. In the event that the fund is able to justify the absence of PAI indicator(s) linked to its E,S,G objectives, it may select another KPI indicator(s) of its choice

⁵ The values for quantitative criteria should be defined by the European Commission as part of its Level 1 or 2 work.

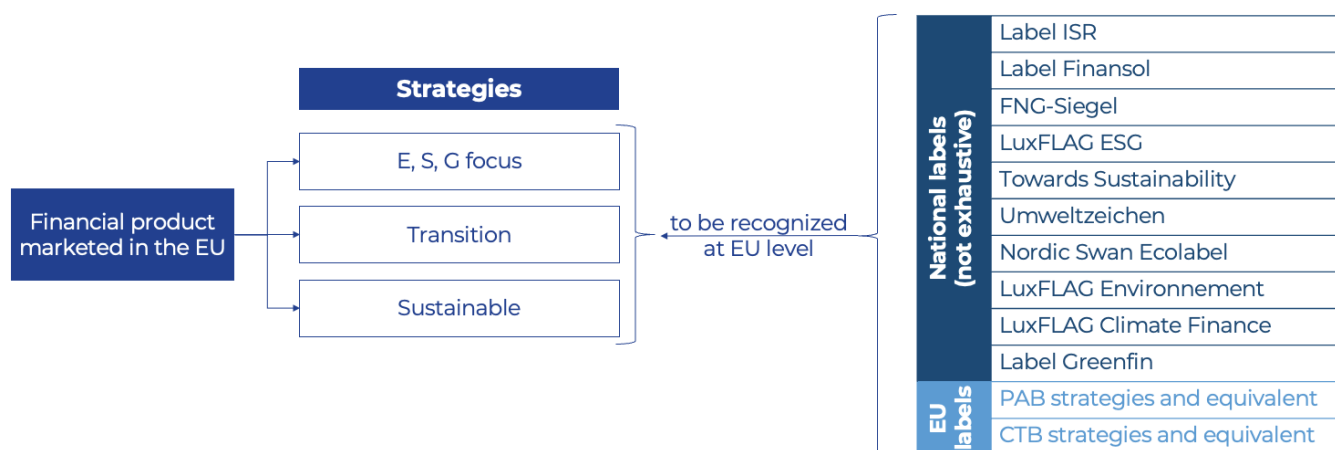
	Target vehicles that are sustainable, transition or E, S, G focus (ex: Funds of funds)
	FMP may determine one other binding criterion (excluding engagement)
	CTB exclusions

Where widely used/recognised frameworks, standards or agreements exist (Paris agreement, Kunming-Montreal biodiversity agreement, impact investing framework, PSF Final report on Minimum Social Safeguards⁶, ICMA, EU GB etc...), a reference should be made to them by the fund.

4. Relation with recognised frameworks and labels

The European Commission should also recognize existing labels:

- **Leverage on the existing well-known market efforts: National ESG and green labels could be maintained.** It would be very useful to have the possibility for these national labels to be recognised as EU labels. Numerous Home member states have developed national labels that are widely used and recognized by both financial market participants and final retail clients. Moreover, each label has developed detailed specifications to identify which products can have the label. For these reasons, national labels should be automatically considered as either “Transition”, “Sustainable” strategies or “E, S, G focus” depending on their theme and level of ambition. The European Commission should adopt an equivalence decision (passporting principle across Europe) to classify these labels under the above-mentioned categories until a European label is created.
- **Funds that have strategies equivalent to the European Paris Aligned Benchmark and Climate Transition Benchmark**, which have been recognized by the European Commission to be “useful and reliable labels for investment products” and that are therefore considered as having a transition objective.



⁶ [Final Report on Minimum Safeguards](#), EU Platform on Sustainable Finance, October 2022

5. Equivalence with ESMA Funds naming guidelines

AFG recognises that ESMA Funds naming guidelines have been structuring the market since their implementation and we believe that the new SFDR product categories should articulate with these guidelines as followed.

As such, AFG believes that the concepts defined in the **ESMA Funds naming guidelines⁷ should be embodied in the new SFDR framework** with the CTB exclusions applying to the “E, S, G Focus” and “Transition” categories and the PAB exclusions applying to the “Sustainable” category. In addition to comply with the ESMA guidelines, the funds names should be consistent with their SFDR categories.

Funds names	Generalist	Social or Governance	Transition	Impact	Sustainable Incl. Environmental
Examples of terms	Declined from transversal characteristics , including “ESG”, “SRI”, etc.	Declined from social characteristics , e.g. “social”, “equality”, etc. OR focus on governance , e.g. “governance”, “controversies”, etc.	Declined from “transition” OR “improve”, “progress”, “evolution”, “transformation”, “net-zero” etc.	Declined from “Impact” e.g. “impacting”, “impactful”, etc.	Declined from “sustainable” e.g. “sustainably”, “sustainability”, etc. but also “green”, “environmental”, “climate”, etc.
SFDR Strategies	E, S, G focus	E, S, G focus	∅	∅	∅
	∅	∅	Transition	∅	∅
	∅	Sustainable	∅	Sustainable	Sustainable

6. Minimum requirements applicable to all sustainable strategies

SFDR should define **a common basis of minimum requirements for classified products**.

The following criteria should be considered:

- Tracking and reporting a **minimum set of indicators to measure** the performance of the product in line with its objective and to be declined per category
- Reporting on a set of few PAIs** common to all the categories
- Applying **CTB or PAB exclusions** as considered by ESMA for the purpose of Fund naming guidelines⁸ and without further modifications or additions.

7. Realigning SFDR & MIF and IDD Sustainability Preferences

Many retail investors have difficulties understanding the disclosures with the volume and technicality of information they contain.

⁷ Including the recent specifications given by ESMA on CTB/PAB exclusions (“The Q&A on controversial weapons specifies that the reference for the exclusion related to controversial weapons should be the one referred to in SFDR principal adverse impact indicator 14”).

⁸ Including the Q&A specifications regarding exclusions.

Moreover, as already explained, the inconsistency between SFDR and MIF/IDD, the complexity of MIF/IDD concepts (taxonomy alignment, sustainable investment, PAI) and the market reality (very low % of taxonomy alignment of the economy or medium level of sustainable investments) do not help investors in their understanding.

Therefore, it seems essential to carry out a thorough work to update the rules on the collection of sustainability preferences. This in-depth work will have to be carried out by taking the time to build an adapted system, starting from the needs of the client. This review work should be carried out at the same time as the review of SFDR with the aim of being perfectly intelligible to a retail investor and focused on the fundamental decision criteria of a retail investor. It will be relevant to adopt a "portfolio" approach to maintain diversification possibility. Indeed, a client could express sustainability preferences without requiring those preferences to apply to their entire portfolio. This work should of course complement the necessary efforts in terms of training advisors and educating the public on sustainability issues.

The proposed modifications under the SFDR should be reflected in the MIF and IDD Sustainability Preferences. In this context, the concept should only be explained to the client based on the financial product's strategy and commitment.

Only the three following questions should be asked to the client:

- **Question 1: Does the client want his/her investment to factor in Climate, Environmental or Social criteria?**
- **Question 2: (If, yes) What strategy does the client want to invest in: "Sustainable", and/or "Transition" and/or "E, S, G focus"?**
- **Question 3: (If yes) Up to how much X% of your portfolio can be invested in these previous choices?**

Until the texts are reviewed at European level, AFG supports putting the implementation of MiFID/IDD criteria on hold. This means that financial advisors would still be required to ask to clients if they want their investments to factor Climate, Environmental or Social criteria but, if the answer is yes, no further question would be asked. The financial advisor would then have latitude to offer products that are part of the SFDR categories as long as they ensure full transparency regarding their sustainability strategies.

8. Disclosure

For Article 8 and Article 9 products, FMPs are required to disclose a quite extensive range of information in both the pre-contractual template and the annual periodic report. These disclosures have proven to be quite difficult to be understood by end-investors in most instances. This complexity risks to disincentivize end-investors from re-allocating their savings towards a more sustainable economy instead of helping them to determine clear sustainable preferences that can be used to offer them most suitable products.

This point has been already addressed in the last closed ESAs consultation on the review of the SFDR Level 2. This concern should be also taken into account when considering the potential options for the revision of the SFDR Level 1 text.

As a general rule, the ability and willingness of retail investors to carry out due diligences on the financial products in which they invest should not be overestimated by the authorities – which has been the case with the current SFDR disclosures

AFG supports the need for a simplification of the disclosure to enable investors to make informed investment decisions and ensure a better understanding of financial products and avoid a disproportionate burden and complex outcome that is fragilizing credibility of the financial market system.

AFG believes that only financial products which include sustainable measurable, comparable and binding objectives should be authorized to be considered as “Sustainable”. Financial products can have different level of ambition. In this context, and to avoid drawbacks identified in the past years, we believe that financial products should clearly specify which level of ambition they are deemed to achieve.

8.1. Pre-contractual template and PRIIPs KID:

Regarding the PRIIPs KID : **Add a new section** within the existing PRIIPs KID in order to describe the ESG Strategy’s type : **“None” / “Sustainable” / “Transition” / “E, S, G focus”.**

Regarding the precontractual template (as of Annex 2) :

- Require a single simplified (and investor friendly) template template with a maximum of 3 pages⁹.
- Include clear explanation of the binding and measurable objective, engagement, some technical criteria such as main PAI indicators (ie carbon footprint) or main exclusions. It will not be efficient to develop the disclosure with only technical criteria as proposed by the consultation.

8.2. Post-contractual (periodic) template:

Require a single simplified and investor-friendly template as for the precontractual template.

Keep a 2 or 3 pages maximum quantitative periodic report with limited amount of text (ie the Annex 4).

8.3. Website

Regarding website disclosures, it's noteworthy that the engagement is minimal, with very few to no individuals accessing the provided information. Website disclosures must be fully aligned with binding precontractual and periodic disclosures to ensure consistency and clarity of information.

The website sustainability disclosure (WSD) document should be abolished and replaced by the standard pre-contractual document (future ESG section of the PRIIPs KID) and by the post-contractual (periodic) document (the Annexe 4).

8.4. EET

EET files are already widely used by our professional and distributors clients and data disseminators so we don't support the need for a “machine readable” format. Here again it is important to not multiply formats, documents etc. that will be costly to produce for no benefit. It would be good that our regulator does not create a new data disclosures format.

8.5. Digitalization

Globally full digitalization can be a target, but we need time, developments etc. to be ready. And it is also the case for our clients and distributors. It should be taking into consideration that IT developments will cause significant costs for the end-clients, knowing that we are at a time where there is a clear focus on reducing the funds costs.

⁹ Funds with non ESG strategy (“None”) would only fill in the meaningful sections.

8.6 Reporting at entity level

AFG supports the concept of entity-level disclosures on investments made on behalf for third parties under SFDR – and not under CSRD.

- Look for coherence in the asset management space:

AFG supports the concept of entity-level disclosures which enable investors to better understand the sustainable ambition and intensity of the FMPs and will help to drive change at the entity level. Furthermore, we understand that only two European asset managers are currently required to publish a sustainability report, that some managers are either consolidated in the reports of insurers or banking groups, and that many will be falling outside the CSRD scope (notably large non-EU groups established in the EU which are not subject to a full consolidated CSRD reporting and whose EU subsidiaries will most likely be individually below the threshold). Whereas, under SFDR, each management entity acting in the EU (and each financial product marketed in the EU) is subject to SFDR.

- Avoid duplication of reporting on managed assets:

Publications at the asset manager level must be streamlined to avoid duplication and confusion for users, particularly between SFDR and CSRD. AFG believes CSRD is the adequate framework for corporate matters, but not the place to report datapoints on investments made on behalf of third parties (assets under management are not controlled by the management company, they are not on its balance-sheet as they are client's assets subject to fiduciary duty/client guidelines such as geographical allocations). It would be particularly misleading to mix assets under management with corporate topics in the CSRD report.

Conversely, SFDR should remain the place for transparency reports on financial products, and thus, at the FMP level, on the assets under management [which are nothing else than a compilation of the financial products (funds, mandates)] and on the application of global investment and engagement policies. This does not prevent the entity level reporting to be refined under SFDR revision for a better reading.