

## BVI's<sup>1</sup> messages for the upcoming SFDR review

### I. BVI's positions at a glance

1. **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 in correspondence to the PSF proposal:
  - **Focus on positive contribution to an environmental/social objective (“sustainable”):** This category would encompass products that aim at making a measurable positive contribution to either environmental and/or social objective.
  - **Focus on sustainable transition (“transition”):** This category should apply to products aiming at facilitating sustainable transition and measuring the relevant progress.
  - **Focus on adherence to ESG standards or values including mixed/multi-asset approaches (“ESG basic” or “ESG collection”):** This broader “sweep-up” category could include process-based strategies and rely on adherence to sustainability standards without aiming at achieving measurable outcomes in sustainability terms.

**All product categories should be designed in a 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. **Each category should be complemented by a set of clear-cut criteria** that provide equivalent safeguards for all asset classes to enable self-assignment by product manufacturers. Those should comprise certain minimum standards and build upon useful elements of the current regulatory framework, including the ESMA rules for sustainability-related fund names.

**Product categories should be designed to reflect different investor preferences and not be put in a hierarchical order. They should be simple and intuitively comprehensible for retail investors.** This should be facilitated by rigorous consumer testing and input from market practitioners. **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. In the meantime, the **exploration of sustainability preferences** in the advice process under MiFID and IDD should be simplified by means of a **Level 2 quick-fix** that would **waive the binding definition** currently in place.

2. **Product-level disclosures:** We are in favour of maintaining the current concept of sustainability-related disclosures **applicable only to products with explicit sustainability claims**. Disclosures should be **fundamentally simplified** and focused on the **key features of an investment**, comprising:

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<sup>1</sup> 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 116 members manage assets of EUR 4.5 trillion for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 26%, 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](http://www.bvi.de/en).



- 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.

Should the Commission nonetheless see added value in introducing transparency in sustainability terms for all financial products, we request that such future requirements:

- Are strictly limited to a few key sustainability indicators that are meaningful and comparable across different markets and different asset classes (such as indicators on GHG emissions),
- 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. **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**. CSRD application to asset managers in terms of managed client assets should be clarified under the Omnibus I initiative with a view to the current market practice for reporting PAIs. **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**. In particular, the annual PAI reporting involves significant costs and efforts, even though the reported aggregated figures are meaningless for investors.
4. **Implications from Omnibus I:** It is of utmost importance that **any sustainability-related information to be disclosed by financial market participants under SFDR can still be sourced from CSRD reports by investee companies** after the Omnibus I revision. Any reductions or modifications of the CSRD reporting standards should be assessed against SFDR and if necessary, directly entail corresponding changes in the transparency requirements for the financial sector. **In no event must asset managers and other financial market participants be expected to compensate for the loss of reported data by companies by making assumptions or estimations.**



## II. Categorisation system for sustainable products

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

- **Focus on positive contribution to an environmental/social objective (“sustainable”):** 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 strategies focusing on generating new impact, but also so-called 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 (“transition”):** This category should apply to products aiming at facilitating sustainable transition by investing in transitioning companies/other assets or in materials/technological solutions that foster transition progress of the wider economy. Measurability of outcomes/interim progress in transition should be ensured in either case by means of binding sustainability indicators as stipulated in the product terms.
- **Focus on adherence to ESG standards or values including mixed/multi-asset approaches (“ESG basic”):** This product category could be more process-based and rely on adherence to ESG standards, including certain minimum safeguards, without aiming at achieving measurable outcomes in sustainability terms. Products in this category should be suitable for investors that wish not to invest in particularly harmful activities, are interested in certain ESG themes or in ESG standards better than the market.

### 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)**.

All product categories should **require 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 objective 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. The regulatory efforts should focus on defining minimum standards for positive contribution to sustainability and avoidance of significant harm. They should build upon those elements of the EU sustainable finance framework that have proven useful in practice and take into account the market experience with the



ESMA fund naming guidelines. Calculation methodologies for minimum commitments at the product level need to be standardised as well in order to warrant a common minimum level of sustainability ambition and comparability for investors.

In this context, we strongly reject any concept that would require a third-party verification of a product's sustainability approach. A mandatory verification is inappropriate for a system that establishes minimum standards instead of a fully-fledged label. It would add costs and complexity to the issuance process and make sustainable product launches commercially less attractive, especially in comparison with traditional investment products.

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. This is particularly relevant in case specific data points are used for defining common metrics (e.g. for "Do Not Significant Harm" assessment) or minimum exclusion criteria for product categories.

## 2. Investor-centric approach

**Ultimately, 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 go hand in hand with the SFDR review, otherwise the reform would be of no practical value:

- The new product categories must focus on the needs and the level of understanding of retail investors,
- Practical testing at the point of sale with both investors and distributors will be very important and should be planned sufficiently in advance of specific decisions in terms of product categorisation at Level 2.

The new regime should also aim at **facilitating communication with investors** with reference to the new product categories:

- Not all technical features of sustainable products need to be explained to investors;
- Investor's level of knowledge and absorption capacities should be realistically assessed;
- More flexibility for appropriate client communication at the point of sale would be very helpful;
- Ultimately, the outcome of the financial suitability test should take precedence over sustainability preferences, meaning that financial advisors should be allowed to recommend financially suitable products even if they do not fully match investor's individual preferences in sustainability terms.

Since the SFDR reform will only take effect in several years, it is **crucial to simplify the advice process in the meantime.** Immediate relief could be achieved by a **Level 2 quick-fix waiving the application of the binding criteria for sustainability preferences under MiFID and IDD**, while leaving all other rules untouched. In particular, the general obligation on advisors and portfolio managers to ask their clients about sustainability preferences would remain in place. The alleviation should pertain to the definition of sustainability preferences in Article 2(7) MiFID DR and Article 2(4) IDD DR respectively. By this means, the overly prescriptive and quixotic criteria for sustainability preferences could be dispensed and distributors would regain the discretion on how to approach the



topic of sustainability-related investments with their clients. This would also rebalance the regulatory disequilibrium and put sustainability preferences on an equal footing with other elements of the suitability test (investment objectives, risk tolerance etc.) for which no prescriptive regulatory requirements exist.

### 3. Distinction between sustainable product categories

**General caveat:** We advise against too rigid minimum criteria for sustainable product categories. Sustainable products should be 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.

#### Focus on positive contribution to an environmental/social objective (“sustainable”):

- 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 designing the scope of this product category to **include not only strategies committed to generating new impact, but also so-called 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.
- **Positive contribution to environmental and/or social objectives** should be assessed against a **revised concept of “sustainable investments”** with better defined criteria and metrics and a clearer integration of the EU Taxonomy as a sub-category of sustainable investments:
  - Whereas environmental objectives should be derived from the EU Taxonomy, more **work for clearly defining legitimate social objectives is needed**,
  - The **“Do Not Significant Harm” assessment should be based on the mandatory PAI indicators** while leaving the decision about the appropriate methodological approach to the product manufacturer (the future standards could still prescribe the minimum level of ambition, e.g. by excluding a certain percentage of the worst performing investments),
  - There should be a **standardised methodology for calculating sustainable investments** at the product level, preferably aligned with the EU Taxonomy calculations (activity-based).
- Under this scenario, a negative filter would be anyway applied as part of the DNSH test (based on PAI indicators). Potential additional exclusions could build up upon the PAB exclusion criteria that are required by the ESMA fund naming guidelines, but only in relation to environmental objectives. For social objectives, the application of CTB exclusion criteria would be appropriate.
- **The EU Taxonomy should be considered one possible methodological approach for assessing environmental sustainability of investments, but it must not preclude other approaches**, especially when it comes to investments in non-reporting companies. In view of the limited market relevance of the EU Taxonomy and the reductions in Taxonomy reporting proposed under Omnibus I, we cannot support the PSF proposal to put the EU Taxonomy at the heart of the future sustainability definition and to assess any investments with environmental objectives against



the EU Taxonomy criteria.

- The relevance of (shareholder) 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).

#### **Focus on sustainable transition ("transition"):**

- **This category should apply to products aiming at facilitating sustainable transition by investing in transitioning companies/other assets or in materials/technological solutions that foster transition progress of the wider economy.**
- **In either case, measurability of outcomes/interim progress should be ensured** by means of binding sustainability indicators as stipulated 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 "transition" 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.

#### **Focus on adherence to ESG standards or values including mixed/multi-asset approaches ("ESG basic"):**

- **This product category could be process-based and rely on adherence to ESG standards, including certain minimum safeguards, without aiming at achieving measurable outcomes in sustainability terms.**
- Should be per definition a **"sweep-up" category eligible for a wide variety of products**, including multi-asset/multi-strategy offerings and products with innovative approaches to sustainable finance, provided they all comply with the relevant minimum standards.
- "ESG basic" would 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.



- Conceivable are e.g. 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) or sustainability-related thematic investments.
- Some index-tracking strategies may be eligible for this category, where they track selective benchmarks that reflect the credible standard for environmental or social sustainability as specified in the investment objective.
- As regards **minimum exclusions**, “ESG basic” products should comply with the **CTB exclusion criteria** that are established as a common minimum standard under the ESMA fund naming guidelines.

#### 4. Regulatory approach to product categories

Ensuring a proper calibration of the product categories with a system that balances the need for sufficient ambition and clear minimum criteria to prevent greenwashing with the practicability of solutions that facilitates innovation and competition will be a complex exercise. We are not convinced that regulatory technical standards currently foreseen as Level 2 measures under SFDR are the right tools to tackle this challenge. Instead, we recommend

- To specify **detailed requirements** for the future sustainable product categories **by means of Delegated Acts** under Art. 290 TFEU and
- To **involve broad market expertise in the development of such detailed requirements**. This could be facilitated by setting up an expert group composed of market practitioners that would provide technical advice to the Commission in relation to the minimum criteria for the product categories.

The regulatory proceeding for Delegated Acts under the EU Taxonomy Regulation involving consultations with the EU Platform on Sustainable Finance could also be utilised for this purpose, provided that the future PSF will ensure broad representation of the financial industry.

#### 5. Transitional provisions

- **A sufficiently long transitioning period that accounts for the applicable Level 2 process would be needed in case of introduction of a new product categorisation system.** More than 50 percent of retail investment funds and a significant share of other EU investment products currently disclose 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 necessitate a 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 keeping transitioning efforts manageable.





### III. Disclosure requirements at product and entity level

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

**The quality of sustainability-related disclosures and its usefulness from investors' perspective need to be significantly improved.** 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 regulatory focus should be put on the following measures:

- **Precontractual and periodic disclosures should be fundamentally 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.

Moreover, it is of utmost importance that **any sustainability-related information to be disclosed under SFDR can still be sourced from CSRD reports by investee companies** after the Omnibus I revision. Any reductions or modifications of the CSRD reporting standards should be assessed against SFDR and if necessary, directly entail corresponding changes in the transparency requirements for the financial sector. **In no event asset managers and other financial market participants must be expected to compensate for the loss of reported data by companies by making assumptions or estimations.**

#### 2. Transparency at the product level: all products

Our preferred solution is to maintain the current concept of sustainability-related disclosures where transparency 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 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) are strictly limited to selected key sustainability indicators that can be deemed meaningful and comparable across different markets and potentially different asset classes, (2) be disclosed only in periodic reports to avoid misapprehensions for sustainability claims and (3) be mandatory only for financial 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 creates 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 regulatory ESG information.**
- **Regulatory standards for sustainability-related disclosures should thus focus on financial products that are primarily offered to retail investors.**
- ESG information for products without dedicated sustainability commitments should be limited to a small number of key indicators that are meaningful for different markets and asset classes. Suitable indicators could reference in particular to GHG emissions of investee companies or other invested assets.
- In products without dedicated sustainability claims, **information on sustainability factors should be disclosed only as part of periodic 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. 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. CSRD application to asset managers should be clarified under the Omnibus I initiative with a view to the current market practice for reporting PAIs. 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.**

- The CSRD reporting regime currently covers all information to be disclosed under Art. 3, 4(2)(b) and 5 SFDR with consistent reporting standards for all companies and sectors in the ESRS.
- The CSRD regime is currently under general review with the aim of cutting red tape and significantly reducing the administrative burden for companies. The ultimate goal is to focus the CSRD reporting on decision-useful and relevant information concerning material sustainability impacts, risks and opportunities. These objectives are legitimate also for the financial sector.
- As it stands, the **annual PAI reporting at entity level is causing significant nuisance** in the fund industry. Data needs to be collected for all assets on all mandatory PAIs, involving significant



expenses for commercial ESG data vendors, but due to the aggregation at the entity level for all managed portfolios, the **reported figures are meaningless for investors**. Consequently, the interest in the published reports is negligible (annual downloads reported regularly in the low two-digit space) and the cost-benefit-ratio very critical.

- Abolishing the requirements of Art. 3, 4(2)(b) and 5 and focusing on reasonable CSRD application would contribute to streamlining sustainability-related disclosures at entity level in future. In this regard, the relevance of assets under management for CSRD disclosures should be clarified with a particular view to the already established market practice for PAIs reporting.
- Effectively, information would not get lost, but would be delivered under a different framework in a manner that is consistent across sectors.