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WORKING DOCUMENT

From:	General Secretariat of the Council
To:	Working Party on Financial Services and the Banking Union (Sustainable Finance) Financial Services Attachés
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SFDR PROPOSAL ARTICLE 6A & SUPERVISION

A. French financial markets Authority (AMF) rules on information to be provided by collective investment schemes incorporating non-financial approaches

In 2020, France introduced a regulatory framework setting minimum expectations for the non-financial communication of asset managers. Formalised in the so-called "Position-Recommendation DOC-2020-03", these expectations apply whenever asset managers communicate on the non-financial characteristics of their products – whether in their marketing materials or regulatory documents. They are grounded in the sustainable commitments undertaken by asset managers in their legal documentation and remain neutral as to the methods used to substantiate the sustainability of their approach.

The Position-Recommendation rests on a principle of proportionality between the effective integration of non-financial factors in portfolio management and the prominence afforded to them in investor communications. To that end, it establishes a three-tiered distinction based on the ESG practices and level of ambition of the collective investment undertakings:

- Case (a): Where a collective investment undertaking demonstrates a significant commitment to the integration of non-financial criteria (a "significantly binding" approach), it may place central emphasis on such considerations in its communications (so-called "**key communication**");
- Case (b): Where a collective investment undertaking integrates non-financial criteria without undertaking a significant commitment (a "not significantly binding" approach), it may engage in more "**limited communication**" on these aspects;
- Case (c): Where the approach fails to satisfy the previously cited standards applicable to cases (a) and (b), communication must remain strictly proportionate and confined to a brief reference in the prospectus. This is referred to as an "approach not meeting central or limited communication standards."

The scope of the "Position recommendation 2020-03" covers two broad categories of documents.

- "Regulatory documents" encompass:
    - The prospectus and, where applicable, the Key Investor Information Document ("KIID") or Key Information Document ("KID");
    - The instruments of incorporation of the collective investment scheme (rules or articles of association);
    - Any other document disclosed to investors which must be submitted beforehand to the AMF for authorisation or the issue of an approval of the collective investment scheme's offering document.
- "Marketing materials" refer to any information of a promotional nature sent directly to potential or existing subscribers, or likely to be passed on by distributors to their potential or existing clients, whether in writing or verbally.

B. "Limited communication" and 10% provision

Where a fund's communication is classified as "limited" (as referred to in case (b) above), disclosure concerning the consideration of non-financial criteria shall be deemed limited where such information is not presented as a central element and is provided as follows:

- in the Key Investor Information Document (KIID), in a concise and balanced manner, including a clear indication of the limitations associated with the integration of non-financial criteria in the management process, and included within the "Other Information" section within the meaning of the CESR/10-1321 guidelines;
- in marketing materials, in a concise manner; and

- in the prospectus, in a proportionate manner.

The concept of "concise" disclosure in marketing material is precisely defined along three cumulative criteria. Non-financial disclosures are considered concise when they are:

- secondary to the presentation of the product's characteristics, both in terms of scope and positioning within the document;
- neutral, meaning no particular emphasis, visuals, or other highlighting;
- limited to less than 10% of the space occupied by the presentation of the product's investment strategy, with space calculated by number of characters where font and format are comparable to those used for the investment strategy presentation.

The 10% threshold was introduced following market texting that revealed the need for a clear, operational benchmark, to ensure consistent supervisory practice. Prior to adoption, tests conducted with market participants highlighted a wide range of interpretations as to what should be considered "concise" and "proportionate" – making a purely principle-based approach likely to generate divergent supervisory practices. In this context, the 10% threshold has since proven particularly valuable in providing unambiguous guidance to market participants. Consequently, it is uncommon for the supervisory authority to request significant changes from market participants in the enforcement of this provision; it ensures that sustainability, transition, or ESG-related elements remain only marginal within a product's overall investment strategy.

C. <u>Supervision practices</u>

Six years of supervisory practice have demonstrated that the 10% threshold rule is both workable and effective, with few difficulties reported by market participants. In the vast majority of cases, ESG-related disclosures are limited to one or two sentences when compared to the overall volume devoted to the description of a product's investment strategy. In practice, the AMF has implemented the rule through a pragmatic approach. The principal challenge in supervisory activities does not lie in assessing the exact length of ESG disclosures, but rather in identifying precisely the sections of marketing materials that relate to the description of the investment strategy, particularly where such documentation takes the form of slide decks or brochures. As a result, minor variations in application may occur, though these have not proven to be a source of significant difficulty.

A quantitative threshold is easier in implementation for supervisory authority and ensures the integrity of "limited" communication without imposing disproportionate burdens on market participants or regulators. By contrast, the topic-based approach (one that would restricts communicating solely to a list of regulatory-defined subjects, such as applicable exclusions) inherently requires a higher degree of semantic precision, giving rise to divergent interpretations and increased risks of greenwashing. Such an approach would also to run counter to the EU's objective of simplifying the regulatory framework, by multiplying layers of specific definitions and thematic thresholds. An overall numerical threshold, on the other hand, limits the risk of market distortion and ensures investor protection without creating undue regulatory complexity.

The rule's implementation would ensure an appropriate limitation of ESG-related disclosures for non-categorised products if it concerns a broader scope of documents than currently envisaged at EU level. Under the existing EU framework, Article 6(a) of the SFDR applies exclusively to precontractual and periodic documents a category in which identifying information relating to the investment strategy is relatively straightforward. Regulatory documents, however encompass a wider set of materials, including the annual report in addition to precontractual documents, while marketing materials cover everything else of a promotional nature addressed to potential or existing investors. The following RTS proposal extends the limitation on ESG-related disclosures beyond precontractual

documents to also cover regulatory documents and marketing materials. Thus, it ensures a consistent and comprehensive framework that limits the risk of market distortion and protects investors across all communication channels, without imposing a disproportionate burden on financial market participants.

D. <u>RTS proposal</u>

Article 6a SFDR2 level 1 should be understood as establishing the general principle that financial products which are not categorised as sustainability-related financial products shall not present non-financial characteristics in a manner that could mislead investors as to their nature or prominence.

For the avoidance of doubt, the following proposals concerning Article 1 to 3 of the SFDR level 2 framework are predicated upon an extension of the scope of article 6a to encompass marketing disclosures. In this context, following proposal for Articles 1 to 3 SFDR level 2 could establish an operational framework for the implementation of this principle by specifying the conditions under which disclosures on non-financial criteria may be made, while ensuring that such disclosures remain proportionate and non-prominent.

- **Article 1** defines the notion of "non central" disclosure" across legal and marketing documentation, ensuring consistency with the overarching requirement laid down in Article 6a SFDR2 Level 1. It further specifies the criteria to be applied, thereby giving practical effect to the requirement that such disclosures remain secondary and non-prominent;
- **Article 2** clarifies the methodology to be applied by financial market participants in identifying the relevant sections of marketing communications against which the proportionality of ESG disclosures is to be assessed.
- **Article 3** clarifies the need for disclaimer for non-categorised products.

Having established the foregoing, we hereby submit proposals for certain recitals and a limited number of articles.

Proposal for recitals:
(1) Article 6a of *Regulation (EU) …/… [SFDR2]* provides that, financial products that are not categorised as sustainability-related financial products should not present, in precontractual documents, non-financial characteristics in a manner that could mislead investors, in particular as regards their prominence or their relevance within the investment strategy.

(2) In order to ensure a consistent and harmonised application of that provision, it is necessary to specify the conditions under which disclosures relating to non-financial criteria may be provided for such products, while ensuring that such disclosures remain proportionate and clearly secondary.

(3) To that end, a distinction should be made between regulatory documents and marketing communications, and appropriate criteria should be established to ensure that any reference to non-financial characteristics remains limited, neutral and non-prominent.

(4) In particular, disclosures in marketing communications should be considered concise where they remain ancillary to the description of the investment strategy, both in terms of their scope and their positioning, and where they do not exceed a limited proportion of the overall content.

(5) In order to ensure supervisory convergence, it is appropriate to establish both qualitative and quantitative indicators, including a maximum proportion of the space devoted to such disclosures.

(6) Financial market participants should also clearly identify the sections of their documentation that relate to the investment strategy, in order to enable an effective assessment of the proportionality of disclosures.

Proposed Level 2 SFDR2 aimed at clarifying the application of **Level 1 SFDR2 requirements:**

Article 1 – Non-central disclosures for products that are not categorised as sustainability-related financial products

Disclosures relating to the consideration of non-financial criteria for financial products not categorised as sustainability-related financial products shall be deemed "**Non-central"** where such disclosures comply with the conditions set out in Article 6a of *Regulation EU …/… [SFDR2] and* are not presented as a central element of the product's communication.

1. For the purposes of Article 6a *of Regulation EU …/… [SFDR2]* disclosures on non-financial criteria in precontractual documents and marketing materials shall meet following conditions:

(1) They are **secondary to the presentation of the product's characteristics**, both in terms of scope and their positioning within the document;

(2) They are **neutral** and do not include any visual, stylistic, or other elements that could give undue prominence to such disclosures;

(3) They do not exceed **10 % of the space** devoted to the presentation of the product's investment strategy. For the purposes of this calculation, the space may be assessed in terms of the **number of characters used**, provided that the font, format, and layout are comparable to those used for the presentation of the investment strategy.

In practice, where appropriate, and in proportion to the overall volume devoted to the description of the product's investment strategy disclosures meeting the criteria set out in this paragraph may be limited to **one or two sentences**.

2. For the purposes of Article 6(a), disclosures on non-financial criteria shall **not** be included in the **name** of the product.

Article 2 – Identification of investment strategy sections in marketing documentation

Financial market participants shall clearly identify, within marketing communications, the sections describing the investment strategy, including where such communications take the form of **presentations, slide decks, brochures, or similar formats**, in order to enable an effective assessment of the non-central disclosures on non-financial criteria.

Article 3 - Disclaimer for non-categorised financial products

Financial market participants shall ensure that precontractual disclosures and marketing communications relating to financial products referred in Article 6a include a clear and prominent statement that "This financial product is not categorised under Regulation (EU)…/… [SFDR2]"