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From:	General Secretariat of the Council
To:	Working Party on Financial Services and the Banking Union (Sustainable Finance) Financial Services Attachés
Subject:	SFDR Review - CWP 4 May 2026 - Spanish non-paper for reviewing exclusion criteria under Articles 7 and 8

Non-paper for reviewing exclusion criteria under Articles 7 and 8

This document puts forward proposals on the exclusion criteria applicable to the ESG basics category (Article 8) and the Transition category (Article 7). The proposals pursue two overarching objectives:

1) Ensuring that the exclusion framework of Article 8 does not create a backdoor into the ESG basics category for companies that should access the investable universe exclusively through the Transition channel.
2) Recalibrating Article 7 exclusions around a forward-looking metric — capital expenditure (CAPEX) — that better captures a company's genuine investment direction in relation to fossil fuels, as opposed to the current "new projects" criterion, which is both conceptually vague and ill-suited to the transition logic of that category.

1. Exclusion criteria for the ESG basics category

1.1. Background

The ESG basics category is designed to accommodate multi-dimensional investment strategies that integrate sustainability factors in a broad sense (environmental, social and governance). This holistic character enables market participants to offer products reflecting diverse sustainability profiles without being required to adopt a primarily environmental orientation.

Article 8(1)(b) as currently proposed reproduces only points (a), (b), (c) and (d) of Article 12(1) of Commission Delegated Regulation (EU) 2020/1818 (the Climate Benchmarks Delegated Regulation). Points (e) to (g) — which cover companies with high fossil fuel revenue exposure above defined thresholds, high-intensity power generators, and companies with elevated GHG intensity — are not included. As a result, **companies with significant fossil fuel exposure can enter the ESG basics investable universe without restriction, irrespective of the environmental ambition of the strategy in question.**

This creates a coherence problem specifically where a financial product under Article 8 adopts an environmental focus. In such cases, companies excluded from the Transition category for failing to meet credible transition requirements could freely enter the ESG basics investable universe. The Transition category is thereby undermined as the appropriate vehicle for financing companies with high fossil fuel exposure within the SFDR categorization framework.

1.2. Proposed approach

Two layers of exclusion are proposed:

1) **Universal exclusions** — points (a), (b) and (c): These cover prohibited weapons, tobacco, and companies violating the UN Global Compact or OECD Guidelines for Multinational Enterprises. They respond to absolute ethical and conduct-based criteria applicable irrespective of the sustainability focus of the strategy. They apply to all ESG basics products.
2) **Conditional exclusions** — points (d), (e), (f) and (g): These cover coal and lignite exposure, oil and gas revenue exposure above defined thresholds, high-intensity electricity generation, and elevated GHG intensity. They reflect climate-related criteria that are directly relevant only where the strategy integrates environmental factors. It is proposed that they be activated automatically when the financial product integrates environmental factors in its investment strategy — using the "integrate" language already present in the Article 8 chapeau, preserving the internal logic of the provision without importing external definitions.

This architecture preserves the full flexibility of the ESG basics category for strategies that do not adopt an environmental focus, while ensuring coherence where they do. Where an environmental focus is declared, companies with high fossil fuel exposure should access the investable universe only through the Transition channel (Article 7), which demands credible transition commitments. The proposal does not expand obligations on all Article 8 products; it establishes consistency where the manager has already chosen to integrate environmental factors.

The proposed architecture also generates an important degree of coherence with the Sustainable category (Article 9). Where an Article 9 product pursues an environmentally sustainable investment objective, the exclusion of high-fossil-exposure companies follows from the logic of that category. The conditional exclusions proposed for Article 8 environmental products align with that result, ensuring that the same companies are excluded at both levels where the environmental dimension is at stake. The meaningful distinction between Article 8 and Article 9 products with an environmental focus is then properly located in the contribution pillar — that is, in the second paragraphs of each provision.

1.3. Drafting proposal on Article 8(1)(b)

(b) they exclude investments in companies as referred to in Article 12(1), points (a), (b)~~,~~ and (c) ~~and (d)~~ of Delegated Regulation (EU) 2020/1818; where those financial products integrate environmental factors in their investment strategy, they shall also exclude investments in companies as referred to in Article 12(1), points (d), (e), (f) and (g), of that Delegated Regulation,

with the exception of investments in use of proceeds instruments issued by companies:

(i) in accordance with Article 3 of Regulation (EU) 2023/2631; or

(ii) where the proceeds do not fund any underlying activities as referred to in Article 12(1), points (a), (b) ~~and~~, (d), (e), (f) and (g), of Delegated Regulation (EU) 2020/1818, provided that the issuer of the use of proceeds instruments is not excluded under Article 12(1), point (c), of that Regulation.

2. Exclusion criteria for the Transition category

2.1. Background

The current Article 7(1)(c) as proposed by the Commission presents a structural complexity — the disjunction between sub-conditions (i) and (ii) applies to overlapping but not identical activities, which makes the provision difficult to read — and, more substantively, relies on a criterion that is conceptually inadequate for the purpose it is meant to serve.

The notion of "new projects" is inherently imprecise. It is unclear what qualifies as a new project, what materiality threshold applies and how compliance is to be verified in practice. More fundamentally, the criterion does not capture a company's investment behaviour comprehensively. A company could have no ongoing "new project" in the strict sense while allocating substantial capital expenditure to the maintenance, expansion or optimisation of existing fossil fuel assets. Such a company would not be captured by the current criterion, yet it is precisely the type of undertaking that the Transition category should not accommodate without credible transition commitments.

2.2. Proposed approach

Merger of Articles 7(1)(b) and (c) into a single restructured provision

A merger of the current Articles 7(1)(b) and (c) into a single restructured paragraph (b) is proposed. The current Article 7(1)(b) already contains exclusions for points (a) to (d) of the Climate

Benchmarks Delegated Regulation. Consolidating the fossil fuel exclusions into one coherent provision — with a clear delineation between ethical exclusions and transition-related exclusions — improves legibility and eliminates the fragmentation arising from the current structure.

Replacing "new projects" with CAPEX-based thresholds

The central modification proposed for the Transition category is the replacement of the "new projects" criterion with CAPEX-based exclusion thresholds.

Capital expenditure is a more precise and more appropriate metric for the Transition category than activity-based criteria such as "new projects". CAPEX measures the actual allocation of investment resources by a company, capturing not only genuinely new development activity but also the reinforcement and expansion of existing fossil fuel assets — activity that does not qualify as a "new project" but is equally relevant from the perspective of transition finance. A company that is not committing significant CAPEX to fossil fuel activities, regardless of what it operates today, is the paradigmatic candidate for the Transition category. This forward-looking dimension of CAPEX is precisely what the current "new projects" criterion fails to capture.

The choice of CAPEX over revenue as the exclusion metric is equally deliberate. Revenue reflects where a company's income currently comes from — a function of investment decisions made in the past, often years or decades ago. A company may carry high fossil fuel revenues simply because it operates mature assets, while actively redirecting all new capital towards decarbonisation. Excluding such a company on the basis of its revenue profile would bar it from the Transition category without any corresponding gain in environmental integrity, and would do so precisely when transition finance is most needed. CAPEX, by contrast, is forward-looking: it captures where a company is deploying its investment resources today, making it the more coherent metric for a category whose purpose is to finance the transition.

A further consideration supports the use of fossil fuel CAPEX specifically, rather than alternative CAPEX-based metrics. An exclusion criterion is by definition a negative test: it defines what should not be in the investable universe. It is therefore more coherent to anchor it in the behaviour to exclude — capital allocation to fossil fuel activities — than in the presence of a positive counterpart such as a minimum level of green investment. The absence of sufficient green CAPEX is not equivalent to the absence of significant brown CAPEX: a company can simultaneously invest in green activities and continue to expand its fossil fuel asset base. A direct fossil fuel CAPEX threshold targets the relevant signal precisely, without relying on a proxy that may not capture the underlying behaviour.

The thresholds proposed would be calibrated against the same percentage levels as the revenue thresholds in Article 12(1) of the Climate Benchmarks Delegated Regulation (1 % for hard coal and lignite, 10 % for oil fuels, 50 % for gaseous fuels and high-intensity power generation). This calibration is inspired by the one proposed in December 2024 in the report of the EU Platform on Sustainable Finance on Investing for Transition Benchmarks[1]. **These thresholds are put forward as a reference calibration and may be subject to further discussion**: alternative levels could be considered for specific fuel types, provided they remain anchored in an objective and verifiable metric.

Maintaining the phase-out requirement as an autonomous exclusion

The phase-out requirement is retained as an autonomous exclusion criterion, separate from the CAPEX thresholds. The two conditions are complementary, not equivalent: CAPEX thresholds

[1] The EU Platform on Sustainable Finance, in its December 2024 report on Investing for Transition Benchmarks, proposed new benchmark categories in which companies are excluded if they exceed defined thresholds in either fossil fuel revenues or fossil fuel CAPEX. **The present proposal departs from that approach by relying on CAPEX alone**, on the basis that a revenue-based exclusion would bar from the Transition category precisely the companies whose transition financing needs are greatest.

test current investment behaviour; the phase-out requirement tests future commitment. A company could have CAPEX below all relevant thresholds while having no intention of reducing its fossil fuel activities over time. Without an explicit phase-out requirement, such a company could access the Transition category without any binding forward commitment — a risk described here as “snapshot compliance”.

It should be noted that Article 7(2) does not address this risk. The routes set out in that paragraph operate at portfolio level or through engagement strategies and do not function as company-level exclusion criteria. A product could comply with Article 7(2) through portfolio-level targets while holding individual companies with no phase-out plan.

Use of proceeds carve-out

The use of proceeds exception should apply to the transition-related exclusions in points (ii) to (vi) but not to the ethical exclusions in point (i). A company excluded on ethical/conduct grounds — prohibited weapons, tobacco, UNGC or OECD violations — cannot issue a use of proceeds instrument that would justify its inclusion in the Transition category. The carve-out is conceptually reserved for companies excluded on grounds of fossil fuel exposure, where a use of proceeds instrument can credibly finance the decarbonisation of the issuer’s own activities.

2.3. Drafting proposal

(*b*) *they exclude investments in companies:*

(i) as referred to in Article 12(1), points (a), (b), and (c) ~~and (d)~~ of Delegated Regulation (EU) 2020/1818;

(ii) that allocate [1 %] or more of their capital expenditure to the exploration, mining, extraction, distribution or refining of hard coal and lignite;

(iii) that allocate [10 %] or more of their capital expenditure to the exploration, extraction, distribution or refining of oil fuels;

(iv) that allocate [50 %] or more of their capital expenditure to the exploration, extraction, manufacturing or distribution of gaseous fuels;

(v) that allocate [50 %] or more of their capital expenditure to electricity generation with a GHG intensity of more than 100 g CO_2e/kWh;

(vi) that do not have a plan to phase out from the exploration, mining, extraction, distribution, refining or exploitation of hard coal, lignite, oil fuels or gaseous fuels;

with the exception, for points (ii) to (vi), of investments in use of proceeds instruments issued by those companies

(i) in accordance with Article 3 of Regulation (EU) 2023/2631 of the European Parliament and of the Council; or

(ii) where the proceeds do not fund any underlying activities as referred to in points (ii) to (v) ~~Article 12(1), points (a), (b) and (d), of Delegated Regulation (EU) 2020/1818~~, provided that the issuer of the use of proceeds instruments is not excluded under point (i) ~~Article 12(1), point (c), of that Regulation~~.

~~(c) they exclude investments in companies that~~

~~(i) develop new projects for the exploration, extraction, distribution or of hard coal and lignite, oil fuels or gaseous fuels; or~~

~~(ii) develop new projects for, or do not have a plan to phase-out from, the exploration, mining, extraction, distribution, refining or exploitation of hard coal, or lignite for power generation~~

2.4. Note on the CAPEX metric

CAPEX is a well-understood financial concept, reported in standardised form in companies' financial statements. As an exclusion criterion, it is considerably more tractable than "new projects". It has a clear definition, a natural unit of measurement, and is subject to external audit. The question of what constitutes a "new project", by contrast, is inherently fact-specific, dependent on project classification conventions that vary across sectors and jurisdictions, and not readily verifiable by investors or supervisors.

The precise methodology for calculating fossil fuel CAPEX as a share of total CAPEX — including the treatment of joint ventures, minority stakes and capital expenditure under concession arrangements — could be addressed in a delegated act at Level 2, following the model of the Climate Benchmarks Delegated Regulation for revenue-based thresholds.

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