

# SFDR disclosure rules for financial market participants

1 November 2023

The Sustainable Finance Disclosure Regulation (SFDR) is a European Regulation introduced to improve transparency in the market for sustainable investment products, to prevent greenwashing and to increase transparency around sustainability claims made by financial market participants.

The Sustainable Finance Disclosure Regulation (SFDR) is a regulatory framework that compels financial market participants and advisers to disclose information regarding the environmental and social impact of their investment decisions. It establishes a clear path for integrating sustainability factors, encompassing environmental, social, and governance (ESG) considerations, into the financial industry's practices. It applies to a range of financial market participants (FMPs) and financial advisers operating within the European Union.

## Disclosure requirements

- *ESG Integration:* The regulation encourages the incorporation of ESG factors and sustainability risks into investment decision-making. FMPs must demonstrate how they consider these factors when constructing and managing their investment portfolios.
- *Adverse Impact Disclosure:* SFDR necessitates that FMPs disclose the adverse effects of their investments on sustainability factors..
- *Pre-contractual Disclosures:* To better inform clients, firms must provide pre-contractual disclosures about their ESG policies, the integration of ESG factors, and potential adverse impacts.
- *Website Disclosures:* Firms are required to publish ESG-related information on their websites, ensuring that the public has easy access to data about their sustainable practices.
- *Annual Reporting:* FMPs must provide detailed annual reports on the implementation of their ESG policies and the impact of ESG factors on investment decisions and returns.

SFDR sets specific deadlines for various disclosure requirements, ensuring that firms adhere to the regulation's provisions in a timely manner.

According to the SFDR, Financial Market Participants (FMPs) are the following:

- **Investment Firms:** This includes various entities engaged in investment activities, such as portfolio management and advice.
- **Credit Institutions:** Banks and other financial institutions that provide credit and other financial services.
- **Insurance and Reinsurance Undertakings:** Insurance companies and reinsurers that offer insurance products and services.
- **Occupational Pension Providers:** Organizations managing occupational pension schemes.
- **Alternative Investment Fund Managers (AIFMs):** Firms responsible for managing alternative investment funds (AIFs).
- **Financial Advisers (FAs):** Financial advisers that provide investment advice or portfolio management services to clients also fall under SFDR's scope.
- **AIFs and UCITS Managers:** Alternative Investment Fund Managers (AIFMs) and Undertakings for Collective Investment in Transferable Securities (UCITS) management companies are subject to SFDR, particularly regarding their responsibilities related to ESG disclosures.
- **Investment Funds:** SFDR applies to the investment funds themselves, including AIFs and UCITS, ensuring that these funds disclose ESG-related information to investors.
- **Fund Promoters and Distributors:** Entities responsible for promoting or distributing investment funds within the EU must comply with SFDR's requirements.

# New sustainability disclosure rules for financial market participants

1 November 2023

## Classification of financial products and services

SFDR categorises products as either "Article 6," "Article 8," or "Article 9" products, based on their level of sustainability.

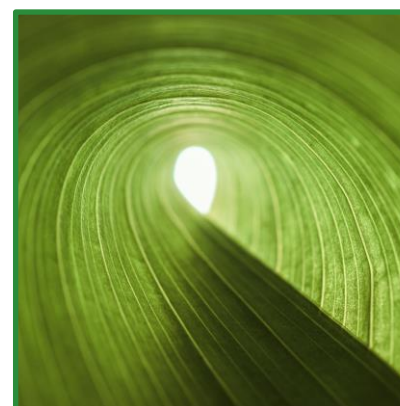


### Grey products (Article 6)

- **Definition:** Financial products or services that do not have specific sustainability characteristics or ESG goals. They may not consider ESG factors when making investment decisions and do not aim to promote sustainability.
- **Disclosure:** For Article 6 products, financial market participants must disclose limited ESG information in pre-contractual documents. These disclosures generally explain the absence of sustainability characteristics and ESG considerations in the investment strategy.
- **Target Audience:** Article 6 products are typically traditional financial products that do not prioritize sustainability factors and are designed for investors who do not require or seek ESG-related information.

### Light green products (Article 8)

- **Definition:** Financial products or services with a focus on promoting environmental or social characteristics. They incorporate ESG factors into their investment processes or have specific sustainability goals, but they do not necessarily have the primary objective of being sustainable.
- **Disclosure:** Financial market participants offering Article 8 products are required to provide more detailed ESG-related information, including how ESG factors are integrated into investment decisions and any potential adverse sustainability impacts. Pre-contractual disclosures should highlight these sustainability aspects.
- **Target Audience:** Article 8 products cater to investors who wish to consider ESG factors in their investment choices but are not exclusively focused on sustainability. They offer a middle ground between traditional financial products and dedicated ESG or sustainable investments.



### Dark green products (Article 9)

- **Definition:** Article 9 products are financial products or services with a primary objective of achieving sustainability goals. They are explicitly designed to promote environmental or social characteristics and prioritize ESG factors in their investment strategies. These products aim to have a significant positive impact on sustainability.
- **Disclosure:** For Article 9 products, financial market participants must provide comprehensive information regarding the alignment of the product with sustainability objectives and the methodologies used to achieve these goals. The pre-contractual disclosures emphasize the product's sustainability features.
- **Target Audience:** Article 9 products are tailored for investors who are committed to sustainable and responsible investing. These products offer a clear path for individuals or organizations seeking investments that have a demonstrable and positive impact on sustainability.



# New sustainability disclosure rules for financial market participants

1 November 2023

## How can we help?

Our multi-disciplinary team can support the entities that fall within the scope of SFDR as follows:

- Review and gap analysis
  - Review the existing sustainability disclosures at entity and product levels
  - Identify the SFDR requirements that are of relevance
  - Perform gap analysis and suggest corrective actions
- Advisory services in relation to the strategy to be followed with regards to ESG, examination of impact on existing activities and products/services offered.
- Support with decision-making and impact analysis in relation to classification of products as per SFDR requirements.
- Drafting of website disclosures as well as pre-contractual and periodic disclosures at entity and product levels in order to comply with the requirements of SFDR and SFDR RTS.

## Contact us



### **Monica Ioannidou Polemitis**

Director, Strategy and Management Consulting

p: +357 25 591515

e: [M.Polemitis@bakertilly.com.cy](mailto:M.Polemitis@bakertilly.com.cy)

Limassol, Cyprus

