

EU SUSTAINABLE FINANCE DISCLOSURE REGULATION (SFDR)

The Sustainable Finance Disclosure Regulation (SFDR) is the latest legislative tool from the European Union to make Europe's economy more sustainable. The Regulation is part of a much larger framework, which is the EU's action plan on financing sustainable growth, originally adopted in 2018 and has an overall aim to connect finance with sustainability.

Who?

The EU Sustainable Finance Disclosure Regulation (SFDR) applies to financial market participants (FMPs) and financial advisors. FMPs are defined as professional players in the financial market, like pension funds, asset managers, insurance companies, banks, venture capital funds, credit institutions offering portfolio management or financial advisors.

Why?

The goal of the EU SFDR is to increase transparency on sustainability among financial institutions and market participants. It consists of disclosure requirements on the entity and the product levels, to standardise sustainability reporting. This is needed to improve industry-wide comparability and prevent greenwashing. The action plan has three clear objectives: 1) to reorient capital flows towards a more sustainable economy, 2) to mainstream sustainability into risk management, and 3) to foster transparency and long-termism.

When?

The regulation was officially implemented on 10 March 2021.

Where?

The regulation applies to FMPs whose business is in Europe, non-EU FMPs (and their subsidiaries) who do business in the EU or sell products to the EU, and non-EU firms that sub-manage EU assets or funds.

What?

First, FMPs need to disclose information on an entity level about their sustainability policies. Second, FMPs need to disclose information regarding their financial products. On both entity and product level, FMPs need to report on their Principal Adverse Impacts (PAI). PAI consists of a list of sustainability factors (e.g. greenhouse gas emissions (GHG), waste, biodiversity, human rights) that firms need to start disclosing in their investment policies and decisions. It consists of mandatory and voluntary indicators, both related to environmental, social and governance (ESG) topics. Some of the PAI indicators are not yet finalised. This will be part of the Regulatory Technical Standards (RTS), whose purpose is to provide further detail and guidance to ensure that firms take a similar approach in their sustainability disclosure. However, it will still take some time before financial actors have to comply with this "juicy" part of the legislation: after intensive lobbying from the finance industry, the piece of legislation covering the RTS will only enter into force in January 2022.