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THE GERMAN FINANCIAL REGULATOR BAFIN CLARIFIES THE EU
COMMISSION'S Q&AS REGARDING SFDR

The German Financial Regulator BaFin Clarifies the EU Commission's Q&As Regarding SFDR



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The German Financial Regulator, ("**BaFin**"), published guidance ("[Guidance](#)") on 5 September 2022, that provides some further clarity on various questions on the Sustainable Finance Disclosure Regulation ("**SFDR**"). BaFin has previously stated it generally welcomed the European Commission's ("**EU Commission**") responses to questions raised by the Joint Committee of the European Supervisory Authorities ("**ESAs**") on certain aspects of SFDR and the Taxonomy Regulation which it had published in [July 2021](#) and [May 2022](#), as well as [clarifications from the ESAs](#) relating to the practical implications of the SFDR regulatory technical standards. However, according to BaFin, the EU Commission's answers have raised further questions with regards to the application of SFDR. BaFin stated on its website its intention to analyse the EU Commission's responses and to examine its own scope for providing further clarity, whilst being mindful of the limited availability of ESG-related data.



base its administrative practice on the legal interpretation contained in its answers until further notice, its Guidance may change if the EU Commission or the ESAs publish assessments that diverge from BaFin's interpretation.

In the Guidance, BaFin discusses, amongst other things:

- How the term "promote" is to be understood in the context of Article 8 of SFDR;
- Whether the taxonomy alignment of financial products must always be assessed; and
- Whether SFDR applies to financial products that were no longer made available to investors before SFDR came into force on 10 March 2021.

Question 1:

The first question that BaFin asks, and subsequently answers, relates to financial intermediaries that operate under the exemption granted by Article 3(1)(a) – (c) of MiFID as implemented in Germany ("**Exemption**"). These intermediaries play a material role in the placement of funds in Germany. As a result of the Exemption, these financial intermediaries are neither investment firms nor financial services firms and are not regulated by BaFin. According to BaFin's interpretation these financial intermediaries are not subject to SFDR because Article 2(5) of SFDR defines investment firms by reference to the definition in Article 4(1)(1) of MiFID. Accordingly, financial intermediaries benefit from the exemption contained in Article 17(1) of SFDR, by virtue of the fact that Germany does not make use of the "exception to the exemption" under Article 17(2) of SFDR.



The EU Commission's July 2021 response (page 8), sought to explain its understanding of "promote" in the context of Article 8 of SFDR by reference to the English language version. However, the EU Commission's response raised the question of how this interpretation can be reconciled with the German language version of Article 8 of SFDR which uses the term "*bewerben*". The literal translation of the German term "*bewerben*" is closer to "advertise" than to "promote".

In its July 2021 questions and answer ("**July 2021 Q&A**"), the EU Commission set out its understanding of the term "promote":

"The term 'promotion' within the meaning of Article 8 of Regulation (EU) 2019/2088 encompasses, by way of example, direct or indirect claims, information, reporting, disclosures as well as an impression that investments pursued by the given financial product also consider environmental or social characteristics in terms of investment policies, goals, targets or objectives or a general ambition in, but not limited to, precontractual and periodic documents or marketing communications, advertisements, product categorisation, description of investment strategies or asset allocation, information on the adherence to sustainability-related financial product standards and labels, use of product names or designations, memoranda or issuing documents, factsheets, specifications about conditions for automatic enrolment or compliance with sectoral exclusions or statutory requirements regardless of the form used, such as on paper, durable media, by means of websites, or electronic data rooms."

Following the EU Commission's statement, BaFin's view is that "promotion" can no longer be viewed per its German



this. BaFin now interprets "promote" in the context of Article 8 of SFDR to mean undertaking any activities to encourage the sale of a financial product and for that information to be communicated externally. Although both active and passive investment strategies can be the subject of promotion, BaFin's view is that, in principle, "promote" does not apply when simply holding investments in sustainable economic activities.

This revised interpretation means that it is not necessary to advertise (for example issue marketing communications or television advertising) a financial product in order to "promote" it.

Consequently, complying with requirements to provide information relating to a financial product could be viewed as "promotion". However, if information is provided in respect of sustainability risks⁶ that are considered when making investment decisions, BaFin's view is that this is not "promotion".

Question 3:

Does every investment underlying a financial product necessarily have to be assessed for taxonomy alignment? How should the EU Commission's May 2022 questions and answer ("**May 2022 Q&A**") (from page 9, in particular page 10) on the disclosure of the proportion of investments that are in environmentally sustainable investments per Article 6 of the Taxonomy Regulation be understood in this respect?

According to BaFin's interpretation, the EU Commission's answer does not imply any obligation to assess every underlying investment for "taxonomy alignment" and to collect corresponding data.



environmental characteristics, the disclosure obligations under Article 6 in conjunction with Article 5 of the Taxonomy Regulation must always be satisfied – meaning the degree of taxonomy alignment would need to be disclosed. This obligation exists irrespective of whether the financial product includes an obligation to make a minimum proportion of sustainable investments as such term is defined in Article 2(17) of SFDR.

However, BaFin's view is that the disclosure of the proportion of investments that are in environmentally sustainable investments can be "zero". In the May 2022 Q&A, the EU Commission stated:

"Therefore, where a financial market participant fails to collect data on the environmental objective or objectives set out in Article 9 of Regulation (EU) 2020/852 and on how and to what extent the investments underlying the financial product are engaged in economic activities that qualify as environmentally sustainable under Article 3 of that Regulation by a given financial product, the precontractual and periodic product related disclosures must indicate zero."

In BaFin's view, this wording leaves it unclear whether an investment is to indicate "zero" in the numerator of the proportion of investments that are taxonomy aligned if no data is collected at all (option 1) or whether "zero" is to be included if reasonable efforts to collect data were made but these efforts were partially or completely unsuccessful (option 2). BaFin considers option 1 ("no data collected") to be acceptable in principle. This understanding gives financial market participants, especially if they have not committed to make environmentally sustainable investments within the meaning of



taxonomy alignment in order to provide a higher proportion of investments that are taxonomy aligned. The same interpretation should apply where a financial market participant commits to make a minimum proportion of taxonomy- aligned investments, provided that the minimum commitment is achieved. Since this approach may result in a lower proportion of investments being reported as taxonomy-aligned than are taxonomy-aligned, BaFin does not see that this interpretation gives rise to any risk of greenwashing.

Question 4:

The EU Commission's May 2022 Q&A (page 6) clarified that financial products in existence on 10 March 2021, even if they were no longer made available to investors, must still comply with the website and periodic reporting disclosure obligations of Articles 10 and 11 of SFDR.

BaFin specifically seeks to address the following questions:

- a) The EU Commission's answer refers to a question that does not address the additional disclosure obligations of Articles 8 and 9 of SFDR. Does the EU Commission's answer mean that the disclosure requirements of Articles 10 and 11 of SFDR apply to all existing financial products?
- b) Many financial market participants have not taken precautions to make disclosures for financial products that ceased to be available to investors before 10 March 2021, as they assumed (in accordance with the wording of SFDR) that the product-related disclosure obligations would not apply to financial products that were in existence before SFDR applied. Does BaFin see room for a general implementation deadline for this requirement?



to be fulfilled retrospectively for existing financial products, irrespective of when those financial products ceased to be available to investors?

Answer 4:

a) According to BaFin, the EU Commission does not address the factual requirements of Articles 10 and 11 of SFDR in its answer. From this and from the missing reference to Articles 8 and 9 SFDR of the question answered by the EU Commission, BaFin's view is that it cannot be concluded that Articles 10 and 11 of SFDR must be fulfilled for all existing financial products that were no longer made available to investors on or before 10 March 2021. According to the EU Commission's interpretation, this obligation would only apply to financial products that meet the requirements of Articles 8 or 9 of SFDR. The assessment as to whether disclosures must be made should be based on the circumstances that were present when the relevant financial product was offered to investors.

b) Even if the disclosure obligations under Articles 10 and 11 of SFDR apply to those financial products that contain information relating to sustainability within the meaning of Article 8 or 9 of SFDR and where those financial products were no longer made available to investors before 10 March 2021, an assessment must be made on a case by case basis as to whether information on the sustainability was provided to the investor during the offering phase, for example on the homepage, in contractual terms and conditions, in pre-contractual information or with other advertising material. To perform such an analysis, financial market participants would have to "make available" the archived sales documents, read through them and determine or decide whether any ESG-



For existing financial products that have not been sold since 10 March 2011 (i.e. were sold more than 10 years prior to the date of first application of SFDR), BaFin is of the view that it seems appropriate for financial market participants to assume that no information on sustainability is available, provided that the financial market participants are not aware of any contrary findings, (i.e. unless there are indications that it had been agreed or the financial market participant had committed itself to consider ESG-related aspects).

BaFin further clarifies that the EU Commission's interpretation on the scope of application came as a surprise, and accordingly BaFin will take into account the effort and associated time that would need to be spent to comply with the obligations in individual cases when making its supervisory assessment.

c) In BaFin's view – notwithstanding obligations resulting from other legal provisions – there are no pre-contractual disclosure obligations under SFDR for financial products that are no longer offered, regardless of when their offering was discontinued. BaFin's view is that there is no longer a pre-contractual relationship in which (updated) pre-contractual sustainability disclosures must be made available to the potential end investor. BaFin assumes that the EU Commission had this in mind at the time it drafted its answer and that the response accordingly focused on the obligations to be fulfilled and not on those that do not apply.

BaFin made clear that its answers are in particular subject to a future, possibly different interpretation by the EU Commission or by the ESAs.



It is encouraging, and somewhat unusual, to see a European financial regulator expressly interpret the EU Commission's answers and to take steps to address the uncertainties that some of those answers created for the financial industry. It also shows that some of the EU Commission's answers came as a surprise to the regulators as well as the industry.

BaFin's approach is a positive one and could be an example of how to implement provisions resulting from SFDR without losing sight of potential practical implications and the scarce availability of data, while at the same time not diluting the obligations.

This update was authored by Angelo Lercara, Mikhaelle Schiappacasse and Philippa List.

Related Professionals

SEARCH BY: 



PARTNER

Angelo Lercara LL.M. EuR

Munich +49 89 21 21 63 15



PARTNER

Mikhaelle Schiappacasse

London +44 20 7184 7845

VISIT BIO



PROFESSIONAL SUPPORT COUNSEL

Philippa List

London +44 20 7184 7872



NATIONAL PARTNER

Arne Bolch

Luxembourg + 352 45 62 62 27

Frankfurt +49 69 7706194238

VISIT BIO



PARTNER

Cyril Fiat

Paris +33 1 57 57 80 16

VISIT BIO



LAWYER

Clara O'Leary

Dublin +353 1 436 8554

VISIT BIO



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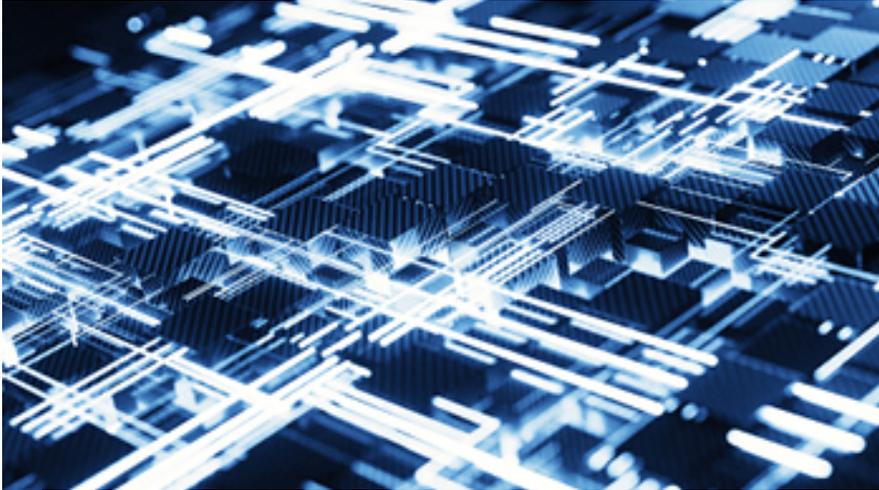
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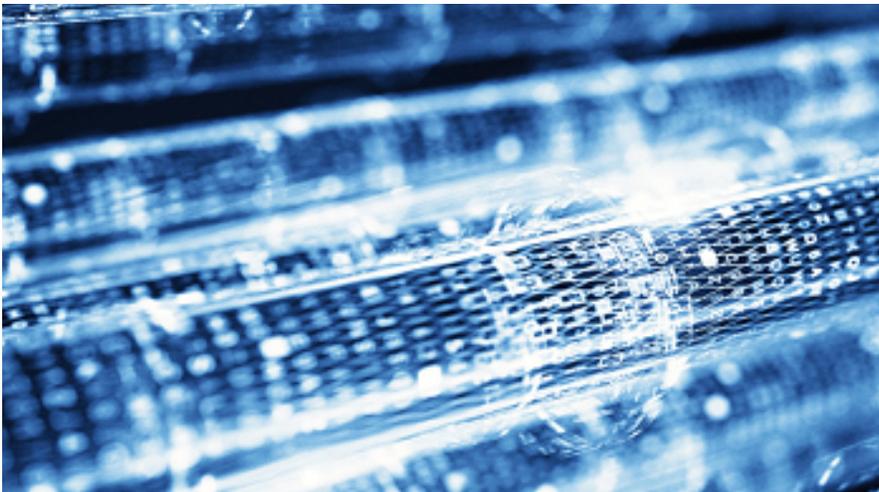


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