SFDR update alert: AMF proposes revisions to SFDR

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AMF: Articles 8 and 9 SFDR should set minimum environmental standards for financial products

*On 10 February 2023 the French regulator (Autorité des Marchés Financiers ("**AMF**")) published its proposals as to changes it believes the European Commission should consider recommending be made to Sustainable Finance Disclosure Regulation ("**SFDR**")[1] as part of its review of the regulation. The proposals include the introduction of minimum environmental requirements that would need to be met by financial products in order for them to be classified as Article 8 or Article 9 under the SFDR. In this OnPoint we report on these proposals.*

Introduction

Historically, the AMF has taken a close interest in the regulation of sustainable finance, the prevention of 'greenwashing'[2] and investor protection. Prior to SFDR taking effect in March 2021, the AMF published Position-Recommandation AMF 2020-03[3] ("**AMF ESG Doctrine**"), that imposes specific obligations on asset managers marketing information (including information on ESG/sustainability).

The aim of the AMF ESG Doctrine was to ensure that (i) information asset managers provide to investors in relation to non-financial criteria (and in particular relating to sustainable investing) is proportionate to the actual importance of these factors in the investment process; (ii) investors receive information that is consistent and enables comparison with similar products; and (iii) the prevention of 'greenwashing'.

The AMF also provided guidance clarifying how, in its view, the requirements of the AMF ESG Doctrine and SDFR interact. Please refer to our previous OnPoints to better understand the impact of the AMF ESG Doctrine "*New requirements for marketing UCITS and retail AIFs in France*" and how the AMF ESG Doctrine and SFDR interact "*AMF ESG Doctrine: Goldplating SFDR by another name?*"[4]

Sustainable finance and greenwashing remain high on the AMF regulatory agenda. In January 2023, the AMF published its actions and supervisory priorities for 2023 focusing on four areas, including (i) developing the regulatory framework for sustainable finance and combating greenwashing, and (ii) ensuring a robust and efficient supervision (see *here*). In particular, the AMF stated that its supervisory actions will advocate in favor of the clarification of legislative texts (including SFDR) to ensure proper application and to better combat the risk of greenwashing. Publication of the AMF's proposals on 10 February 2023 is the first step towards achieving this.

It is important to note that the AMF's proposals in relation to SFDR do not impact on the requirement for in-scope asset

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The AMF's Findings

In the publication, the AMF states that SFDR and the current Article 8 and Article 9 classifications do not make it possible for investors to appropriately assess or compare the degree of sustainability of the investment strategies conducted by financial products. The AMF also points out that SFDR does not set any minimum requirements for products to meet to be Article 8 or Article 9 compliant, it only requires financial market participants ("**FMPs**") to disclose information about their claims and practices on sustainability matters.

The AMF also asserts that the use of the current Article 8 and Article 9 SFDR classification by FMPs may be misinterpreted by investors as a guarantee that they are allocating part of their financial resources to the financing of a more sustainable European economy.

The AMF's Proposals

Having conducted an informal consultation on existing market practices and regulations, the AMF published its proposed changes to SFDR (the AMF publication is available *here*):

- **Introduce minimum standards for Article 8 and Article 9 financial products.** The AMF proposes that the European Commission keeps the Articles 8 and 9 categories, but that it should include additional minimum standards that products should have to meet. Compliance with these additional minimum standards would be subject to national supervision. The requirements for Article 9 financial products should remain more demanding than those for Article 8 financial products.

out in Article 2(17) of SFDR is worded vaguely, which has led to varying interpretations of what constitutes a sustainable investment. The AMF proposes that Article 2(17) of SFDR should be replaced with a new definition that is based on objective requirements to make it tangible and more concrete. The AMF also proposes that these proposed objective requirements should include a minimum level of product alignment with the EU Taxonomy Regulation.[5]

- **A minimum proportion of assets underlying Article 9 financial products should consist of investments aligned with the EU Taxonomy Regulation.** This percentage should be "dynamic" and increase over time as the European economy advances towards sustainability. This minimum requirement could be formalized in investment strategies as follows:
  - providing an initial percentage fixed above the estimated alignment of the European economy;
  - a subsequent, step-by-step increase of this percentage, depending on how the European economy's alignment with the EU Taxonomy Regulation progresses over time;
  - a grandfathering clause should be provided for closed-ended funds, so that the closed-ended funds would only need to commit to a minimum percentage when the financial product is made available to investors (and are not subject to changes during the fund's term).
- **FMPs managing Article 8 or Article 9 financial products should be required to adopt pre-determined "acceptable" binding ESG approaches in their investment decision-making process.** The AMF suggests creating an EU framework for minimum standards that would identify a set of acceptable

including the conditions under which such approaches may be deemed to be sufficiently binding, for example by setting a certain degree of reduction in the investment universe. The AMF suggests that these ESG approaches could include, for example, "rating upgrade", "selectivity" or "non-financial upgrade".[6] The AMF also suggests specific approaches could be approved on a case-by-case basis by National Competent Authorities in certain circumstances, for instance in the case of investments in real estate or private equity.

- **Article 9 financial products should exclude investments in fossil fuel activities that are not aligned with the EU Taxonomy Regulation.** Investment in such activities would be possible for Article 8 financial products provided they meet strict conditions.

In addition to its core recommendations, the AMF proposes requiring FMPs of Article 8 and Article 9 financial products to (i) disclose engagement policies, and (ii) to do mandatory product-level principal adverse impacts (PAI) reporting. Lastly, the AMF suggests introducing the concept of transition assets that would be investible assets by both Article 8 and Article 9 funds.

Next Steps

The AMF states that the aim of the proposals is to initiate discussions on the minimum standards in view of the European Commission's review of SFDR.

If implemented, the proposals would likely have a significant impact on the asset management industry and require many FMPs to not only reevaluate the categorization of their funds

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However, the introduction of transition assets could be a helpful development for those managing real estate, private equity and venture capital funds.

Footnotes

1) Regulation (EU) 2019/2088.

2) The EU Taxonomy Regulation (Regulation (EU) 2020/852) states at recital 11 that "*greenwashing refers to the practice of gaining an unfair competitive advantage by marketing a financial product as environmentally friendly, when in fact basic environmental standards have not been met.*"

3) The French version of the AMF ESG Doctrine is available here and the English version here.

4) Note, the original AMF ESG doctrine dated 11 March 2020 has been updated several times, but from an ESG perspective the important update was made on 27 July 2020 and is discussed in our *OnPoint: AMF Doctrine Alert: Changes to the doctrine*.

5) Regulation (EU) 2020/852.

6) The AMF's view is that such ESG approaches cover the vast majority of ESG practices developed by financial players, such as "best-effort", "best-in-class" or "best-in-universe".

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LAWYER

Katie Carter

London +44 20 7184 7433

VISIT BIO

PARTNER

Sabina Comis

Paris +33 1 57 57 81 30

VISIT BIO

PARTNER

Cyril Fiat

Paris +33 1 57 57 80 16

LAWYER

PROFESSIONAL SUPPORT COUNSEL

Philippa List

London +44 20 7184 7872

VISIT BIO

ASSOCIATE

Antoine Pian

Paris +33 1 57 57 82 29

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