

January 21, 2021

URGENT CLARIFICATION SOUGHT BY EUROPEAN SUPERVISORY AUTHORITIES ON THE APPLICATION OF THE SUSTAINABLE FINANCE DISCLOSURE REGULATION

To Our Clients and Friends:

On 7 January 2021, the Joint Committee of the European Supervisory Authorities (“**ESAs**”) wrote to the European Commission, requesting “urgent” clarification on several important areas of uncertainty in the application of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (the “**SFDR**”) prior to the application of the majority of its requirements on 10 March 2021.

One such area raised, which will be of particular importance to a number of fund managers, is whether the SFDR will apply to non-EU alternative investment fund managers (“**AIFMs**”) when marketing funds in the EU under applicable national private placement regimes.

Application to non-EU AIFMs

To date, the industry has generally taken the view that non-EU AIFMs will be caught by the product level disclosure requirements of the SFDR, when marketing their funds in the EU. This is primarily as a result of the cross-reference in the SFDR to Article 4(1)(b) of the Alternative Investment Fund Managers Directive (2011/61/EU), which itself includes non-EU AIFMs.

The posing of this question by the ESAs, however, casts doubt on the presumption by many non-EU AIFMs that they will fall within the scope of the SFDR. The industry will be watching very closely in the coming days and weeks to see how the European Commission responds. In the interim, this uncertainty clearly presents a challenge for non-EU AIFMs, which will need to think about whether to continue with implementation for now, on the assumption that they will be caught, so as not to be on the “back foot” should the European Commission confirm they are within scope.

Other key priority areas identified

The ESAs have also asked for clarification in relation to a further four areas (set out below at a high level):

- **application of the 500-employee threshold for principal adverse impact reporting on parent undertakings of a large group** – this is particularly significant in light of the fact that where the threshold is met, from 30 June 2021, firms will have to consider adverse impacts of their investment decisions on sustainability factors (rather than use a “comply or explain” approach);

- **the meaning of “promotion” in the context of products promoting environmental or social characteristics** – the ESAs noted that, in general, clarification on the level of ambition of the characteristics through the provision of examples of different scenarios that are within, and outside, the scope of Article 8 of the SFDR would assist with the orderly application of the SFDR. Fund managers will need to determine whether the fund falls within Article 8, as additional disclosure obligations apply where that is the case;
- **the application of Article 9 of the SFDR** – the ESAs asked for further clarification on what would constitute an Article 9 product. For example, they asked whether a product to which Article 9(1), (2) or (3) of the SFDR applies must only invest in sustainable investments as defined in Article 2(17) of the SFDR. If not, is a minimum share of sustainable investments required (or would there be a maximum limit to the share of “other” investments)? As above, in relation to Article 8 products, fund managers will need to make additional disclosures if the fund in question falls within Article 9 of the SFDR; and
- **the application of the SFDR product rules to portfolios and dedicated funds** – one question asked by the ESAs was whether, for portfolios, or other types of tailored financial products managed in accordance with mandates given by clients on a discretionary client-by-client basis, the disclosure requirements in the SFDR apply at the level of the portfolio only or at the level of standardised portfolio solutions. This is clearly another area in which further clarification from the European Commission would be very welcome.

Conclusion

It is, to say the least, far from ideal that there is so much uncertainty surrounding the application of the SFDR so close to 10 March. This is particularly the case given that these areas are by no means peripheral – there will, for instance, be a significant number of non-EU AIFMs holding their breath at the moment. The industry will be waiting with great interest to see how the European Commission responds.



Gibson Dunn’s lawyers are available to assist in addressing any questions you may have regarding these developments. If you wish to discuss any of the matters set out above – whether issues raised or potential solutions – please contact the Gibson Dunn UK Financial Services Regulation team:

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