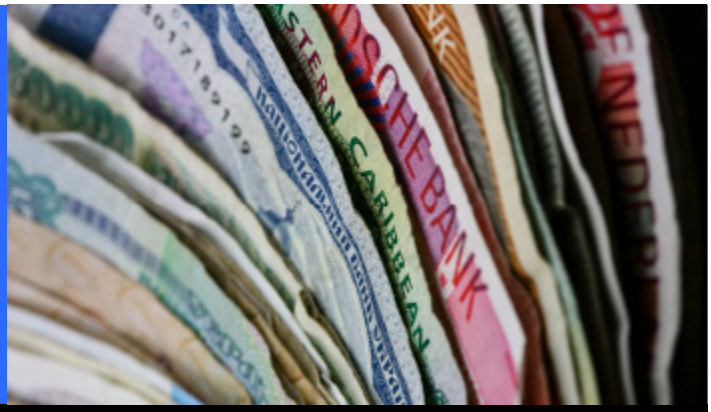
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GIBSON DUNN



Financial Regulatory Update November 5, 2026

EU Sustainable Finance Disclosure Regulation 2.0: The Likely Compromise and What It Means for Funds Raising Capital Now

The new rules are unlikely to apply before 2029. In this update, we provide our view on where the negotiations are likely to end up and what managers should be doing in the meantime.

The trilogue negotiations on the reform of the Sustainable Finance Disclosure Regulation (Regulation (EU) 2019/2088) (**SFDR**) began in Strasbourg on 22 October 2026, and a second meeting is fixed for 19 November. The European Commission (the **Commission**), the Council of the EU (the **Council**) and the European Parliament (the **Parliament**) start from the same basic design, and the debate is now about detail. For private fund managers, that detail matters a good deal: it will determine whether a fund needs to be categorised at all, whether existing funds will be protected, and what managers can say about sustainability in their fund names and marketing.

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Summary

All three institutions would replace the current Article 8 and Article 9 framework with three product categories (Transition, ESG Basics and Sustainable), each requiring at least 70% of investments to meet the relevant criteria, and would remove the existing definition of “sustainable investment”.

The Council and the Parliament both support allowing alternative investment funds (**AIFs**) that are made available exclusively to per se professional clients (that is, professional clients within Section I of Annex II to Directive 2014/65/EU (**MiFID II**)) to opt out of categorisation. Elective professional clients would not meet that test. An opt-out is very likely, but the Parliament would continue to restrict the sustainability-related terms that funds which opt out may use in their names and marketing.

Existing closed-ended funds are likely to benefit from some form of transitional relief. The question that matters is where the line is drawn, particularly for funds that are still raising money when the new rules take effect.

In our view, the most immediate exposure for many managers lies in their contracts, rather than in the regulation itself. Side letter and LPA provisions requiring a fund to "maintain Article 8 status" or to "qualify as an Article 9 product" may become ambiguous, or simply impossible to perform as written, once the current categories fall away.

Finally, the European Securities and Markets Authority (**ESMA**) has said that it will decide the future of its guidelines on fund names by the fourth quarter of 2027. Managers should name new funds in line with the current guidelines and hold back from any wider renaming exercise until both the final SFDR text and ESMA's decision are known.

Where the negotiations stand

The Irish Presidency is aiming for political agreement before the end of 2026, although early 2027 seems the more realistic expectation. The Council and the Parliament both favour a 24-month implementation period. On that basis, if the text is published in mid to late 2027, the new rules would apply from 2029.

Milestone	**Date**
Commission proposal	20 November 2025
Council negotiating mandate	24 June 2026
Parliament negotiating mandate	5 October 2026
First trilogue (Strasbourg)	22 October 2026
Second trilogue (Brussels)	19 November 2026
Political agreement	End 2026 or early 2027 (expected)
Publication and entry into force	Mid to late 2027 (expected)
ESMA decision on fund names guidelines	By Q4 2027
Application	2029 (expected)

Reports of the first trilogue suggest that the main differences between the institutions concern the eligibility criteria for each category, the sectoral exclusions and the marketing rules. The Level 2 measures are likely to follow some way behind.

The Council and the Parliament would both remove certain existing obligations, including the entity-level statement on principal adverse impacts (**PAIs**), as soon as the new regulation enters into force, rather than waiting for the application date. Otherwise, managers should expect the current regime, including the Article 8 and 9 templates and the ESMA guidelines on fund names, to continue to apply until the new rules take effect.

Our view on the likely compromise

On most of the issues that matter to private fund managers, the Council and the Parliament are already close to each other, and we do not expect the Commission to hold out against them both. The table below summarises the three positions on each open point, taken from the Council's comparative document of 12 October 2026 (ST 14335/26), together with our view. These are, of course, predictions: trilogues frequently produce trade-offs between unrelated points.

Issue	The three positions	Our view
Professional-investor opt-out	The Commission's proposal has no opt-out. The Parliament would allow Articles 6a, 7, 8 and 9 to be disapplied for an AIF made available exclusively to per se professional clients, provided that no retail investor can access it, and would require the pre-contractual documents to say that the fund is not categorised and why. The Council would go further, also disapplying the restrictions in Article 13(3) on the use of sustainability-related terms in names and marketing, and would not require reasons to be given.	We are confident that an opt-out will survive, and expect a prescribed statement in the offering documents. Whether funds that opt out can still make sustainability claims in their names and marketing is the most contested point and could go either way. If the Parliament prevails, opting out may not be a way to keep an ESG-themed name.
Existing closed-ended funds	The Commission's test covers closed-ended products created and distributed before the application date. The Parliament adopts the same test and adds that commitments and disclosures made under the current SFDR and Regulation	Some transitional relief is very likely. Its form is less certain, but the Council's test is the more workable of the three and may well be adopted, together with the Parliament's protection for existing commitments. On the Council's formulation, a

	(EU) No 1286/2014 (the **PRIIPs Regulation**) continue to apply, without being treated as sustainability claims under the new rules. The Council's test is whether the product is closed to new investors and no longer offered once the new rules apply.	fund that is still open to new investors on the application date may not qualify.
70% threshold and private assets	All three texts use a 70% threshold. Only the Council expressly provides for a build-up period, of up to three years, subject to sectoral legislation. The Council would also allow private and real assets to qualify under the residual "other investments" route on the basis of "documented, asset-class-appropriate evidence and methodologies".	We expect the 70% threshold to stand. A build-up period and some flexibility for private assets are likely but not assured. A build-up period would be particularly valuable to funds with a multi-year investment period.
ESG Basics	The Commission would accept outperformance on a single sustainability indicator; the Parliament and the Council would both require at least two. The texts treat a proven positive track record differently, and the Council folds it into the residual route.	We expect a requirement for two indicators. Some form of track record route is likely to survive, and private equity and infrastructure strategies that have no obvious benchmark may well depend on it.
Taxonomy shortcut	The Commission and the Council treat 15% alignment with Regulation (EU) 2020/852 (the **Taxonomy Regulation**) as sufficient for both the Transition and the Sustainable categories. The Parliament would raise the figure for Sustainable products to 20%.	We expect 15% for Transition products and a figure of between 15% and 20% for Sustainable products.
Fossil fuel exclusions (Transition)	The Commission would exclude companies developing new coal, oil and gas projects. The Parliament and the Council	We expect a conditional exclusion based on revenues, closer to the Council's version.

	would instead exclude companies with fossil fuel revenues unless they meet certain conditions, including a 20% Taxonomy-aligned capital expenditure test and an emissions reduction plan. The Parliament's conditions are stricter.	
Product-level PAIs	All three texts would make PAIs a condition for Transition and Sustainable products. The Commission leaves the choice of indicators open; the Council and the Parliament would each prescribe indicators, but in different ways.	We expect mandatory product-level PAIs, probably with a common core set of indicators.
Impact products	All three texts would limit the use of "impact" in a fund's name to products that meet a category threshold and have a pre-defined, measurable impact objective.	We expect this to be adopted as proposed. Impact funds will need a documented theory of change and a measurement framework if they are to keep the name.

Funds raising capital in 2027 and 2028

A fund launched in 2027 will be set up under the current SFDR and may then need to be recategorised, or to opt out, during its life. Its documents should allow for either outcome.

Holding a final close comfortably before the application date will improve a fund's chances of transitional relief, but managers should not treat final close as decisive. Each fund will need to be tested against the final conditions, and later closings, increases in commitments and transfers to new investors all need to be looked at. Successor, parallel and continuation vehicles will ordinarily be separate products.

As to the fund documents, we suggest that sustainability commitments should be described by reference to what the fund will actually do (its exclusions, targets, engagement and reporting) rather than solely by reference to its SFDR classification. The LPA should also give the manager the flexibility, on notice to investors, to make the changes reasonably needed to comply with the new regime, including changing the fund's classification or relying on an exemption. That flexibility should be limited to changes that do not materially alter the fund's strategy, its binding sustainability commitments or investors' economic rights. A change in classification can matter to an investor even where the investment policy is unchanged, so institutional investors will often ask for LPAC consultation or consent where a change is material.

Side letters need particular care. A number of EU institutional investors now ask for covenants to maintain Article 8 or Article 9 status. It may be tempting simply to add a reference to "the nearest equivalent category" under the new regime, but we would advise against it: the phrase is uncertain and could commit the fund to a higher standard than anyone intended. A better approach is for the general partner to decide in good faith how the fund should be treated under the new rules, having regard to its strategy and binding commitments, and to notify investors of that decision. The side letter should also make clear whether the fund may opt out. Managers should be wary of giving a single investor a covenant that would, in practice, determine the regulatory treatment of the whole fund, and should check whether any most-favoured-nation provisions would require a revised covenant to be offered to other investors.

Even where an opt-out is legally available, commercial considerations will often decide whether it is used. Insurers, pension funds and funds of funds frequently need categorised products for their own reporting, and wealth platforms may bring in investors who are not per se professional clients. We therefore expect many funds aimed at EU institutional investors to choose to be categorised even where they could opt out.

Much of the remaining detail will be left to Level 2. For private funds, the key questions will be how the 70% threshold treats undrawn commitments, uninvested cash, subscription facilities and holding structures, and what happens if a fund falls below its threshold, including whether there is a cure period and the consequences under the LPA and side letters.

Fund names: the ESMA guidelines and UK Sustainability Disclosure Requirements (UK SDR)

ESMA's guidelines on fund names that use ESG or sustainability-related terms continue to apply to EU funds with such names. ESMA said in its 2027 work programme that it would decide on the future of the guidelines by the fourth quarter of 2027, in light of the outcome of the SFDR negotiations (IPE). Withdrawal is widely expected but not certain. New funds should be named so as to satisfy the current guidelines and, as far as possible, the category they are likely to fall into under SFDR 2.0. Renaming existing funds can wait.

SFDR 2.0 will not apply in the UK, and we do not expect the UK to follow it. The UK SDR, including the labelling regime and the naming and marketing rules, is aimed principally at UK funds and their managers, and overseas funds currently fall outside the labelling regime. The Financial Conduct Authority's anti-greenwashing rule is wider. It applies when an authorised firm refers to the sustainability characteristics of a product or service in its communications with clients in the UK, or in financial promotions that it communicates to, or approves for communication to, persons in the UK. That can include a UK manager's communications about a non-UK private fund offered only to professional investors. A UK manager marketing in both the EU and the UK will need to consider the fund's name and sustainability claims under both regimes.

UK and US managers marketing into the EU

The Commission's view, set out in its 2021 Q&A, is that a non-EU alternative investment fund manager marketing a fund in the EU under a national private placement regime (in reliance on Article 42 of Directive 2011/61/EU (**AIFMD**)) must comply with the SFDR product disclosure

requirements. None of the three negotiating texts would change that.

The professional-investor opt-out could, however, make a real difference to these managers. Private placement is generally limited to professional investors, so if the opt-out is adopted in the form proposed by the Council, a non-EU manager marketing only to per se professional clients could choose not to categorise its fund, leaving it largely with the sustainability risk disclosure under Article 6.

There are three limits on this. First, some Member States allow private placement to investors who are not per se professional clients, such as Germany's semi-professional investors. Each of those investors would need to be tested against Section I of Annex II to MiFID II; some will qualify, but any who do not would take the fund outside the opt-out. Second, if the Parliament's position on names and marketing is adopted, a fund that opts out could remain subject to restrictions on sustainability-related terms in its name and EU marketing materials. Third, EU investors may insist on categorisation in any event.

Next steps

For funds now being raised, managers should review their side letter and LPA sustainability provisions so that they are built around the fund's substantive commitments, with a mechanism for dealing with the new regime, rather than tied to Article 8 or 9 status. They should also include a suitably limited regulatory change provision in the LPA, plot each fund's expected final close against the likely application date, ask anchor investors whether they will require a categorised product, and add ESG information rights to new portfolio company documents.

Once political agreement is reached, managers should test each strategy against the agreed threshold, exclusions and PAI requirements, starting with the funds that will still be investing in 2029, and decide, strategy by strategy, whether to be categorised or to opt out.

Before the new rules apply, managers will need to move to the new disclosure templates, review fund names once ESMA's position is known, and confirm that funds relying on transitional relief still meet their existing commitments.

The following Gibson Dunn lawyers prepared this update: Michelle M. Kirschner, Martin Coombes, Jack O. Collins*, Saad Khan, and Josephine Kroneberger.

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, please contact the authors or any leader or member of Gibson Dunn's Financial Regulatory practice group:

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