

Sustainable Finance – Next Steps for Investment Funds

With the passing of the 10 March 2021 deadline for compliance with the Level 1 requirements under the **EU Sustainable Finance Disclosure Regulation** (“SFDR”), investment funds and fund management companies are now in the next phase of preparing for compliance with both the SFDR requirements and the **EU Taxonomy Regulation** by the next key date of 1 January 2022. The tables below set out the key steps that have been taken so far and the next steps in implementing these new requirements.

Website Disclosures
 Prospectus Disclosures
 Periodic Disclosures

A lot done ...

10 March 2021

Website Disclosures

Financial market participants (“FMPs”), which are defined to include alternative investment fund managers (“AIFMs”) and UCITS management companies, had to make the following website disclosures by 10 March 2021:

- Sustainability risk policy
- Updated remuneration policy
- Principal adverse impact statement (“PAIS”) for those financial market participants (“FMPs”) opting to consider principal adverse impacts of investment decisions on sustainability factors

Prospectus Disclosures

Irish UCITS and AIFs existing prior to 10 March 2021 had to file updated prospectuses and supplements with the Central Bank of Ireland (“Central Bank”) by 10 March 2021 under a fast-track submission process specifically for SFDR-related updates, including the following disclosures:

- How sustainability risks are integrated into investment decisions and the results of the assessment of the likely impacts of sustainability risks on the returns of the fund or clear and concise reasons why sustainability risks are not relevant for returns of the financial product
- Where FMPs opted out of publishing a PAIS on their website, prospectuses were updated to include a statement to that effect
- Additional disclosures for Article 8 SFDR Light Green Funds (funds promoting environmental or social characteristics) and Article 9 Dark Green Funds (funds with a sustainable investment objective)

A lot more to do...

30 June 2021

Website Disclosures

PAIS by large entities. While the requirement to publish a PAIS generally applies on a comply or explain basis, from 30 June 2021, where an FMP has an average of 500 employees or is the parent undertaking of a large group which has an average of 500 employees, the FMP must publish a PAIS. FMPs complying with the PAIS requirements from this date will only comply with the Level 1 SFDR requirements until the regulatory technical standards (“RTS”) specifying the detail to be included in the PAIS apply, expected to be 1 January 2022.

1 January 2022

On 4 February 2021, the European Supervisory Authorities (“ESAs”) published their **final report** on draft RTS on SFDR disclosures, which are expected to apply from 1 January 2022 (the “SFDR RTS”). The SFDR RTS cover:

- the “do no significant harm” principle for sustainable investments;
- the PAIS template for those electing to consider principal adverse impacts;
- Article 8 SFDR and Article 9 SFDR product pre-contractual disclosures;
- Article 8 SFDR and Article 9 SFDR product website disclosures; and
- Article 8 SFDR and Article 9 SFDR product periodic disclosures.

The SFDR RTS are not in final form as yet as they have yet to complete the EU legislative process. However, they are not expected to change significantly prior to publication in the Official Journal of the EU.

In addition, the EU Taxonomy Regulation is due to apply from 1 January 2022, with respect to the first two climate-related environmentally sustainable economic activities set out in that regulation (climate change mitigation and climate change adaptation), which will impose additional disclosure requirements. On 17 March 2021, the ESAs published a **consultation** on Taxonomy-related disclosures, which proposes to amend the SFDR RTS to create a single rule book for sustainability disclosures, and addresses the additional disclosures required by Article 8 SFDR and Article 9 SFDR funds that make investments in environmentally sustainable economic activities (ie, taxonomy-aligned activities) (the “Taxonomy RTS”).

Website Disclosures

- The SFDR RTS set out the detailed website disclosures to be made by Article 8 SFDR and Article 9 SFDR products in a “Sustainability-related disclosures” section of the website under Article 10 SFDR.
- Where an FMP considers principal adverse impacts of investment decisions on sustainability factors, from 1 January 2022, it will have to publish on its website a PAIS using the mandatory template set out in Annex I to the SFDR RTS. This means that, by 30 June of each year, FMPs must publish certain information on a separate section on their websites titled “Principal adverse sustainability impacts statement”. Where a PAIS is being published for the first time, there is no need to disclose information relating to a previous reference period. Therefore, the first time a PAIS will be published that includes information relating to a reference period will be 30 June 2023 relating to a reference period of 2022.

Prospectus Disclosures

- Article 6 SFDR funds (that is, those funds that do not promote environmental or social characteristics and do not have a sustainable investment objective) must state in the prospectus: “The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.”
- Article 8 SFDR and Article 9 SFDR funds will be required to make pre-contractual disclosures using the mandatory templates set out in the SFDR RTS, as amended by the Taxonomy RTS.

Periodic Reports

- Fund annual reports must comply with the SFDR from 1 January 2022, irrespective of reference periods (see the ESAs’ Joint Supervisory Statement issued on 25 February 2021). The SFDR RTS provide mandatory templates for periodic reporting. The ESAs have recommended to the European Commission in their **Joint Supervisory Statement**, that a phased approach to the periodic reporting requirements may be required if the SFDR RTS are not adopted sufficiently early to allow FMPs six months to gather the necessary information. This proposed phased approach would mean that the SFDR RTS would only apply to periodic reports published in or after 2022 in relation to reference periods starting from 1 January 2022, while periodic reports published in 2022 in relation to reference periods starting before 1 January 2022 would apply the high level and principle based requirements in the Level 1 SFDR text.
- Article 6 SFDR funds must state in the annual report: “The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities.”

30 June 2022

Website Disclosures

As noted above, by 30 June of each year, FMPs must publish certain information on a separate section on their websites titled “Principal adverse sustainability impacts statement”.

30 December 2022

Prospectus Disclosures

Where an FMP considers principal adverse impacts of investment decisions on sustainability factors, there must be pre-contractual disclosure as to whether and how each fund considers the principal adverse impacts on sustainability factors. The prospectus should also include a statement that information on principal adverse impacts on sustainability factors is available in the periodic report.

Periodic Disclosures

Where an FMP considers principal adverse impacts of investment decisions on sustainability factors, the annual report must include information on principal adverse impacts on sustainability factors.

1 January 2023

Prospectus Disclosures

Article 8 SFDR and Article 9 SFDR funds will be required to make disclosures in relation to investments in the remaining four non-climate environmentally sustainable economic activities set out in the Taxonomy Regulation. These are: sustainable use and protection of water and marine resources; the transition to a circular economy; pollution prevention and control; and protection and restoration of biodiversity and ecosystems.

30 June 2023

Website Disclosures

PAIS: The first time a PAIS will be published in respect of a reference period will be 30 June 2023 relating to a reference period of 2022.

Comment

From the outset, with the publication of the Commission’s Sustainable Finance Action Plan in March 2018, the implementation timeline for the various proposals outlined in that plan appeared highly ambitious and challenging for stakeholders. Delays in the legislative process, resulting in the Taxonomy Regulation being finalised six months after the SFDR and the publication of the draft SFDR RTS just one month before the March 2021 SFDR implementation deadline, have led to a complicated matrix of requirements with which stakeholders must contend.

The recent pace of developments has been swift, with a number of significant publications since January of this year including:

- the ESAs letter to the Commission dated 7 January 2021 seeking clarity on a number of issues;
- the draft SFDR RTS;
- the ESAs’ Supervisory Statement;
- the ESAs’ consultation on Taxonomy-related disclosures;
- the Commission’s delegated acts amending the UCITS, MiFID and AIFMD Level 2 measures;
- the Commission’s delegated act on technical screening criteria for the climate related environmentally sustainable economic activities under the Taxonomy Regulation;
- the Commission’s proposal for a Corporate Sustainability Reporting Directive amending the SFDR Reporting Directive; and
- the Commission’s delegated act on Article 8 Taxonomy Regulation disclosures.

The questions posed by attendees at the ESAs open hearing on the taxonomy-related disclosures on 29 April 2021 demonstrated that stakeholders are still grappling with key Level 1 issues such as what is meant by “promoting” environmental and social characteristics and how to distinguish between Article 8 SFDR and Article 9 SFDR funds, never mind the more detailed granular requirements set out in the draft RTS. At present, the interconnecting requirements and initiatives present like an unsolved Rubik’s cube, with some more twists and turns required to meet the next key deadline of 1 January 2022.

There is ongoing engagement between the ESAs and the Commission, and between industry representative associations including Irish Funds and the European Fund and Asset Management Association, to try to resolve some of the outstanding issues. Tara Doyle, Head of Matheson’s Asset Management and Investment Funds Department, chairs the Irish Funds ESG Working Group and is a member of the EFAMA ESG Steering Group. We will continue to keep our clients and contacts informed of further developments.

Please get in touch with your usual Asset Management and Investment Funds Department contact or any of the contacts listed in this publication should you require further information in relation to the material referred to in this briefing note.

Full details of the Asset Management and Investment Funds Department, together with further updates, articles and briefing notes written by members of the Asset Management and Investment Funds team, can be accessed at www.matheson.com.

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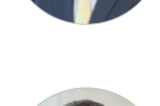
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