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28 July 2022

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# Joint ESAs' Report on the extent of voluntary disclosure of principal adverse impact under the SFDR

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Report to the Commission under Article 18 of Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector

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# 1. Executive Summary

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## Reasons for publication

1. Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector (hereinafter 'SFDR') tasks the ESAs, under its Article 18, to *'take stock of the extent of voluntary disclosures in accordance with point (a) of Article 4(1) and point (a) of Article 7 (1)'* and that *'By 10 September 2022, and every year thereafter, the ESAs shall submit a report to the Commission on best practices and make recommendations towards voluntary reporting standards'*. Article 18 also states: *'That annual report shall consider the implications of due diligence practices on disclosures under this Regulation and shall provide guidance on this matter'*.

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2. To gather information for the purposes of this report, the European Supervisory Authorities (ESAs) have launched through the Joint Committee (JC), as well as through the relevant Standing Committees of the ESAs, a survey of its members, the National Competent Authorities ('NCAs'), with the purpose of gathering feedback on the current state of entity level voluntary disclosures under Article 4 (1) point (a) SFDR<sup>1</sup>. With the view of getting a complete picture of the state of voluntary disclosures in the market, the ESAs have decided to ask NCAs for their feedback also on the disclosures for financial market participants (FMPs) choosing to explain why they do not consider adverse impacts of investment decisions on sustainability factors as per Article 4 (1) (b) SFDR<sup>2</sup>, even if not explicitly requested by Article 18 SFDR. The survey has not covered disclosures under Article 7 (1) SFDR<sup>3</sup> as it is expected that FMPs will start applying those by 30 December 2022.
3. The ESAs have carefully analysed the 33 responses received and developed an indication of good examples of best practices observed by April 2022 and preliminary recommendations. Those are based on a combination of responses from the NCAs, of which the most relevant

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<sup>1</sup> Article 4 (1) (a) SFDR – Financial market participants shall publish and maintain on their websites: (a) where they consider principal adverse impacts of investment decisions on sustainability factors, a statement on due diligence policies with respect to those impacts, taking due account of their size, nature and scale of their activities and the types of financial products they make available.

<sup>2</sup> Article 4 (1) (b) SFDR – Financial market participants shall publish and maintain on their websites: (b) where they do not consider adverse impacts of their investment decisions on sustainability factors, clear reasons for why they do not do so, including, where relevant, information as to whether and when they intend to consider such adverse impacts.

<sup>3</sup> Article 7 (1) SFDR- 1. By 30 December 2022, for each financial product where a financial market participant applies point (a) of Article 4(1) or Article 4(3) or (4), the disclosures referred to in Article 6(3) shall include the following: (a) a clear and reasoned explanation of whether, and, if so, how a financial product considers principal adverse impacts on sustainability factors; (b) a statement that information on principal adverse impacts on sustainability factors is available in the information to be disclosed pursuant to Article 11(2). Where information in Article 11(2) includes quantifications of principal adverse impacts on sustainability factors, that information may rely on the provisions of the regulatory technical standards adopted pursuant to Article 4(6) and (7).

extracts are reported anonymously in Section 4.3 of this report, and ESAs' staff's desk-based research.

4. The first report's preliminary conclusions are that the extent of compliance with voluntary disclosures under Article 4 (1) (a) varies significantly across jurisdictions and FMPs under the scope of SFDR, and it is difficult to identify definite trends. It was not possible to draw conclusions in terms of the differences across FMPs based on size, nature and scope of activities. At this stage, the ESAs have identified that the disclosures for FMPs that do not take into account adverse impact of investment decisions on sustainability factors under Article 4 (1) (b) are lacking in detail, and FMPs largely fail to provide clear reasons for why they do not do so, with insufficient information as to whether and when they intend to consider such adverse impacts. Finally, NCAs have reported overall low level of disclosure of the degree of alignment with the objective of the Paris agreement, with disclosures on the alignment being vague and high level.
5. Section 2 this report includes the background and rationale of this exercise and lessons learned from the first year of implementation of the voluntary disclosures, based on responses from NCAs. Section 3 provides an overview of good examples of best practices, and other less good examples of voluntary disclosures under Article 4 (1) (a) and (b) SFDR. The last part of this section also includes recommendations to the Commission and NCAs. The Annex provides an overview of the questions included in the survey with some highlights from the responses received from the NCAs.

## Next steps

6. The ESAs would like to state that SFDR has become applicable on 10 March 2021. However, as the detailed Regulatory Technical Standards (RTS) on these disclosures are not yet applicable and given the still emerging NCAs' supervisory practices on voluntary disclosures by FMPs, the indications of good examples of best practices and recommendations included in this report must be considered preliminary at this stage and will be complemented further in subsequent reports. In addition, as it is too early to offer meaningful guidance on the implications for due diligence disclosures more generally, the ESAs plan to address this in future iterations of the report.
7. Finally, the future iterations will also cover voluntary disclosures under Article 7 (1), which will only be fully applicable from 30 December 2022.
8. In terms of next steps, the Commission may consider the ESAs' findings and take those into account in any preliminary evaluation on the functioning of the SFDR. The ESAs may also consider the findings in the work on the new mandate received on 28 April 2022 to review the PAI framework<sup>4</sup>.

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<sup>4</sup> <https://www.eiopa.europa.eu/document-library/letter/mandate-esas-develop-sfdr-regulatory-technical-standards-principal-adverse-en>

## 2. Introduction

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### 2.1 Background and rationale

9. The SFDR sets out sustainability disclosure requirements for a broad range of FMPs, financial advisers and financial products. It was enacted to address the twin objectives of increasing transparency of sustainability-related disclosures and to increase comparability of disclosures for end investors.
10. The ESAs, through the Joint Committee, were empowered by SFDR, and later through Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment (the Taxonomy Regulation, hereinafter 'TR'), to deliver a number of draft RTS on the content, methodologies and presentation of sustainability-related disclosures under empowerments in Articles 2(3)(a), 4(6) and (7), 8(3), 9(5), 10(2) and 11(4) of the SFDR.
11. The ESAs' final report containing the first draft RTS (JC 2021 03) was published on 4 February 2021. The final report on draft RTS (JC 2021 50) containing the second set of taxonomy-related product disclosures was delivered on 22 October 2021. On 6 April 2022, the European Commission adopted the draft Delegated Regulation (C(2022)1931), published in the Official Journal as Commission Delegated Regulation (EU) 2022/1288 on 25 July 2022.
12. From 10 March 2021, Article 4(1)(a) SFDR mandates disclosure, on a comply or explain basis, of the Principal Adverse Impacts (PAI) that investment decisions have on sustainability factors on the website of FMPs. The disclosure should take the form of a statement on due diligence policies with respect to the adverse impacts of investment decisions on environmental and social sustainability factors. Article 4(1)(b) requires that, where an FMP does not consider adverse impacts of investment decisions on sustainability factors, it must publish and maintain on its website clear reasons for why it does not do so, and where relevant, information as to whether and when it intends to do so.
13. Under Article 4(3)-(4) SFDR, from 30 June 2021, FMPs exceeding on their balance sheet dates the criterion of the average number of 500 employees during the financial year (hereinafter the '500-employee threshold') must publish and maintain on their websites a statement on their due diligence policies with respect to the principal adverse impacts of investment decisions on sustainability factors.
14. On the basis of Article 18 of SFDR, the ESAs are required to submit a report to the European Commission by 10 September 2022 (and every year thereafter) taking stock of the extent of voluntary disclosures in accordance with Article 4(1)(a) of SFDR, and providing recommendations on best practices towards voluntary reporting standards.

15. To determine the extent of voluntary disclosures under Article 4 (1)(a) SFDR, in March-April 2022 the ESAs conducted a survey of the NCAs asking for feedback through a series of nine questions about the current state of voluntary disclosures published by FMPs below the 500-employee threshold - referred to in Article 4(3)-(4) SFDR - in their respective jurisdictions and highlight any best practice on PAI reporting.
16. To gather evidence for recommendations on best practices, the ESAs included in the set of questions a request to share best practices and examples of insufficient disclosures, under both Article 4(1)(a) and 4(1)(b) SFDR.
17. The ESAs have already developed mandatory reporting templates provided in the Annexes of the draft RTS and adopted by the Commission through the Delegated Regulation supplementing SFDR with regard to the content, methodologies and presentation of information in relation to sustainability indicators and adverse sustainability impacts which will become applicable from 1 January 2023. Therefore, as evidence will be needed on the application of the RTS, the ESAs will not be recommending voluntary disclosure presentation or any different methodology than the one provided in the Delegated Regulation. Nonetheless, some of the conclusions from this and subsequent annual reports under Article 18 SFDR may be useful for FMPs complying with the disclosure templates in the future.

## 2.2 Lessons learned from voluntary disclosures - one year on

18. From the responses received and the sample analysed by NCAs, the ESAs conclude that the extent of compliance with voluntary disclosures varies significantly across respondents.
19. The ESAs' assessment is that the level of compliance is higher when the FMPs are part of a larger group, the latter being more likely to provide a full definition of the group's approach to PAI, including the description of policies they have put in place to identify and prioritise PAI and other engagement policies. However, divergent approaches towards disclosures make comparability across FMPs challenging. There are also some practises to include in the due diligence statement disclosures of sustainability risks or exclusion policies, ranking of the counterparties on the basis of ESG factors or preferences for the counterparties which have better ESG features. As that information is not required under PAI disclosures, the ESAs deem such disclosures as potentially misleading for investors.
20. The overall level of compliance with the details required for explaining why FMPs do not take into account PAI under Article 4(1)(b) appears to be low. As a general weakness, there is no indication from FMPs about when they intend to consider such adverse impacts and lack of explanation of the reasons for not considering PAI. When an explanation is offered, the most common reasons are: challenging, uncertain and incomplete regulatory requirements, lack of information and clear methodology on how to obtain data from issuers and more broadly lack of publicly available data, expensive processes to implement, no common criteria/practices for defining the necessary indicators, application of proportionality criteria such as size, internal organisation and the nature, scope and complexity of the activities in question.

21. A number of NCAs have noted that they will follow up individually with supervised entities to inquire the reason for non-compliance and have already included this follow up action as part of their annual supervisory programmes. Some other NCAs admitted that ensuring compliance with the obligation set under Article 4 (1) (a) and (b) of SFDR was not amongst their supervisory priorities.
22. There are no definite conclusions regarding differences on FMPs' disclosures depending on size, nature and scope of activities, nor types of financial products they make available. As it emerges from NCAs responses, differences are difficult to generalise. Some respondents note that bigger FMPs in size, nature and scale of activities have higher level of compliance, while others note the opposite trend.
23. The majority of NCAs responding to the survey note that information on disclosures is overall easy and straightforward to find, and that they come up through a web search using the name of the FMP and 'statement on principal adverse impacts'. Several FMPs place such statement under the menu item 'sustainability' on their websites. A few NCAs report however that such statements are fragmented and hidden either in legal documents in pdf form or in the section of the annual report on the integration of sustainability risks, or even mixed with risk management related information.
24. NCAs have reported an overall low level of disclosure of the degree of alignment with the objective of the Paris agreement, noting that when disclosure of alignment is made, it is often vague and lacking details.
25. As expanded on in Section 3 of this report, the ESAs have highlighted some examples of best practices shared by the NCAs, and in particular 1) making disclosures prominent on websites (as opposed to footnotes or hidden links) and 2) improving the overall visibility of the disclosures. Furthermore, including the date in disclosure documents or sections, allowing them to be quickly found through a web search, and having a title with the language/ wording closely aligned with SFDR should also be promoted.
26. The ESAs note that the questionnaire increased the level of NCAs' awareness of entity level disclosures under Article 4 (1) (a) and (b) SFDR, and their need to undertake specific offsite supervision, investigation and where relevant, guidance to supervised entities to help them comply with the Regulation.
27. Finally, as one NCA pointed at the fact that FMPs have issues identifying whether they fall under the obligations of Article 4 (4) SFDR<sup>5</sup>, the ESAs would like to point out that FMPs should carefully consider their status as parent undertakings under Article 4 (4) SFDR, and consult the

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<sup>5</sup> Article 4 (4) SFDR: By way of derogation from paragraph 1 of this Article, from 30 June 2021, financial market participants which are parent undertakings of a large group as referred to in Article 3(7) of Directive 2013/34/EU exceeding on the balance sheet date of the group, on a consolidated basis, the criterion of the average number of 500 employees during the financial year shall publish and maintain on their websites a statement on their due diligence policies with respect to the principal adverse impacts of investment decisions on sustainability factors. That statement shall at least include the information referred to in of paragraph 2.

Commission's July 2021 Q&A<sup>6</sup>, which contains interpretation about the 500-employee threshold and the responsibilities of parent undertakings.

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<sup>6</sup> [https://www.esma.europa.eu/sites/default/files/library/sfdr\\_ec\\_qa\\_1313978.pdf](https://www.esma.europa.eu/sites/default/files/library/sfdr_ec_qa_1313978.pdf), Question 1.

## 3. Best practices and preliminary recommendations

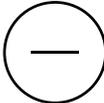
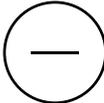
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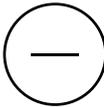
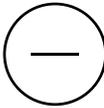
### 3.1 Good examples of best practices on disclosures under Article 4(1) (a) and (b) SFDR

28. The ESAs have provided below a preliminary, indicative, and non-exhaustive overview, based on both direct observations from desk research or examples reported from NCAs, of good examples of best practices and examples of less good practices for disclosures under Article 4 (1) (a) and (b) SFDR. This list represents a subjective assessment of the helpfulness of the disclosures to understand how FMPs consider, or why they do not consider, the principal adverse impacts of their investment decisions on sustainability factors.
29. It is important to note that the new mandatory disclosure obligations provided in the Commission Delegated Regulation (EU) 2022/1288 will become mandatory from 1 January 2023. The examples below on statements made under Article 4 (1) (a) should not be understood to affect disclosures made under the mandatory templates.

#### Table overview

'Comply or explain'	Issue	Example (if applicable)	Assessment	Reasoning
4 (1)(a)	Full PAI statement	Document prominent on the sustainability section of the website including a description of principal adverse sustainability impacts, indicators applicable to investments in investee companies, identification of PAIs, prioritisation of PAIs, methodology and data used for the assessment of each PAI, stewardship activities (engagement and voting) engagement policies and references to international standards, changelog		This type of statement represents a clear example of voluntary disclosure (i.e. prior to the disclosure through the mandatory template in the Delegated Regulation) and easily accessible through web search

4 (1)(a)	Limited PAI statement without any detail	FMP acknowledges the importance of disclosing transparency of PAI of investment decisions on sustainability factors without further details on methodology used		This type of statement, while strictly complying with Article 4 (1) (a), does not provide any information on e.g. the methodology used for the assessment of adverse impacts, so this type of statement risks the disclosure becoming a tick box exercise
4 (1)(a)	Efforts towards consideration of PAI	FMP provides a clear description of the process concerning consideration of PAI – while mentioning the lack of available data in a specific field, disclosure is still made based on national and international standards		This statement is a helpful example to show efforts towards consideration of PAI while acknowledging the lack of data in certain fields
4 (1)(b)	No consideration of sustainability adverse impact	FMP does not consider adverse impacts, as it says that PAI metrics have yet to be finalised, and reserves the right to voluntarily comply in the future, based on a regular/annual assessment		This type of statement under Article 4 (1) (b) is considered a helpful example of FMPs not considering PAIs albeit it could include further information notably on 1) which PAI metrics the statement refers to by reference to the sustainability factors and 2) provide an estimate on when the FMP intends to consider such adverse impacts

4 (1) (b)	Mixing criteria from Article 4 (1) (a) or from Article 3 in the non-compliance statement	FMP states the decision not to comply with Article 4 (1) (b) but includes in the same statement also elements on the integration of the FMP's integration of ESG risks, or adherence to responsible business codes and international standards		This statement is considered potentially misleading for investors as it includes details / elements of ESG (integration of ESG risks or adherence to business codes or international standards) which are not relevant for an Article 4 (1) (b) SFDR statement. The latter could be published in a separate section of the website
4 (1) (b)	No consideration of sustainability adverse impact	FMP does not currently consider adverse impacts as the relevant data are not yet available on the market to a sufficient extent		This statement, while strictly speaking compliant with the rules, could also include details on whether and when the FMP plans to consider adverse impacts by reference to the sustainability factors.
4 (1)(a)	Confusion between PAI and sustainability risks	FMP assesses the impact of the issuer's business on sustainability risks when making investment choices		The statement under Article 4 (1) (a) should only include considerations of adverse impacts, not of sustainability risks
4 (1) (a) – 4 (2) (d)	Alignment with Paris Agreement	FMP supports climate action in line with the objectives of the Paris Agreement		The simple statement of support to the objectives of the Paris Agreement, without further details about decarbonisation

				paths does not represent helpful transparency under Article 4 (1) (a)
4 (1) (a) – 4 (2) (d)	Alignment with Paris Agreement	FMP includes credible decarbonisation objectives, upstream and downstream emissions, setting out scale and timeline for action to achieve the trajectories consistent with the Paris Agreement, aligning specific investments with carbon neutral trajectories		This statement includes details on decarbonisation objectives as a way to disclose PAI of investment decisions
4 (1)(b)	Statement refuses to take PAI into account	FMP believes that the targeted and systematic consideration of adverse impacts is not currently envisaged but there are substantial reasons to believe that their investment decisions have a positive impact on sustainability factors outlined under SFDR		This statement is not helpful as it is based on vague explanations about why the FMP does not consider adverse impacts, yet claiming a positive impact on sustainability factors

### Legend:



Considered by the ESAs as good examples of best practices in the disclosures



Considered by the ESAs as bad practices in the disclosures, which could be failures of compliance



Considered by the ESAs as examples where there is margin for improvement

## 3.2 Recommendations to the Commission

- As the Commission Delegated Regulation (EU) 2022/1288 supplementing the SFDR, which includes the detailed requirements for the disclosure on the due diligence statement on principal adverse impacts of investment decisions on sustainability factors, is not yet

applicable, the ESAs do not make recommendations with regards the SFDR requirements to the Commission at this stage, as practices of FMPs are expected to become more easily comparable with the application of the Delegated Regulation. Instead, the ESAs have made some recommendations to NCAs to ensure an appropriate supervision of FMPs' practices.

### 3.3 Recommendations to NCAs

31. The ESAs deem it useful to provide some preliminary recommendations to the NCAs designated in accordance with sectoral legislation to monitor the compliance of FMPs and financial advisers with the requirements of SFDR.
32. The following recommendations will assist NCAs in their ongoing applicable supervisory actions, as well as for the purpose of subsequent annual surveys requested by the ESAs for the purpose of Article 18 SFDR:
  - a. Continuous market observation to identify FMPs that are not compliant with the voluntary disclosures and ensure compliance with Article 4 (1) (a) and (b) SFDR - NCAs should be able to undertake a supervisory dialogue with FMPs that, as reported by some NCAs, 'did not show an interest in disclosing voluntarily their method of inclusion of the PAI'. As the obligations for FMPs to publish and maintain on their websites PAI considerations are set out in the Level 1 of SFDR entered into force on 10 March 2021, FMPs should comply with the disclosures or ensure that reasons for not doing so are outlined, including, where relevant, information as to whether and when they plan to consider adverse impacts. NCAs must ensure compliance with such obligations;
  - b. Greater sample size and more details in reporting figures – As the report under Article 18 SFDR will have to be submitted to the Commission annually, the ESAs recommend all NCAs in the subsequent surveys to provide responses based on a greater sample size to ensure a representativeness of the sample. Exact figures on data sample are also recommended;
  - c. Regular own market surveys/questionnaire – Following the survey, some NCAs have communicated that they would be sharing targeted questionnaire / surveys in their own market. The ESAs encourage NCAs to undertake regular surveys in their own market to determine whether supervised entities comply with the Article 4 SFDR disclosures;
  - d. Offsite inspections – The ESAs welcome the effort from some NCAs to include the follow up to the survey in their annual supervisory plan and identify regulatory breaches from FMPs which will be object of offsite inspections during the course of the year. The ESAs suggest that other NCAs follow this approach;
  - e. Use of IT tools – The ESAs recognise that while experience is already established with supervision of mandatory disclosure documentation, website supervision is a newer field which may require more systematic verification of compliance with the mandatory disclosures such as the use of IT and/ or other SupTech tools which would allow easier assessment;
  - f. Additional instruction on voluntary disclosures – The ESAs welcome that some NCAs have provided – or are in the process of providing – additional instructions to supervised entities

regarding technical aspects of website disclosures indicating the ESAs draft RTS as reference for applying the provisions of Article 4 SFDR in the interim period.

## 4. Annex: Supervisory Survey – questions’ overview and summary

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### 4.1 Supervisory survey – overview of survey’s questions

1. ESAs received a total of 33 responses from NCAs, covering a significant proportion of EU supervised entities under the scope of the SFDR. The level of detail in the responses differed across NCAs and jurisdictions, with some NCAs providing short responses based on varying levels of desk research, while other NCAs provided detailed responses, often based on own supervisory surveys or questionnaires.
2. As respondents were not given specific minimum coverage thresholds in relation to the size of the sample to assess, NCAs were asked to provide figures about how many market participants were considered in their assessment and whether this was a fair reflection of the market size in their jurisdiction, in terms of both total number of supervised entities and Assets under Management (AuM).
3. The ESAs asked NCAs for their assessment about the extent to which FMPs below the 500-employee threshold comply with voluntary disclosures under Article 4 (1)(a) and for those who decide not to consider adverse impacts of investment decisions, whether they provide information as to whether and when they intend to consider such adverse impacts. In addition, NCAs were asked to assess the extent of non-compliance with the rules since the entry into force of the Regulation.
4. NCAs were also asked to provide observations about differences with regards to FMPs’ disclosures depending on size, nature and scale of their activities and the type of products they make available, as well as whether the disclosures were ‘easy’ and ‘straightforward’ to find on the FMPs’ websites. The ESAs were also particularly interested in finding out whether the information disclosed included a reference to the FMPs’ degree of alignment with the objectives of the Paris agreement as referred to in Article 4 (2)(d) SFDR.
5. To gather evidence for recommendations on best practices, the ESAs included in the set of questions a request to NCAs to highlight best practices, under both Article 4(1)(a) and 4(1)(b) SFDR, and to share any additional comments or consideration.
6. The ESAs have provided below more details on the content of the survey responses, upon which their preliminary recommendations are based.

## 4.2 Supervisory survey - summary of responses

### **1) To what extent are financial market participants (FMPs) in your jurisdiction – below the thresholds set in Article 4(3)-(4) SFDR – complying with the voluntary disclosure under Article 4(1)(a) SFDR to publish and maintain on their websites information on how they consider principal adverse impacts of the investment decisions on sustainability factor, in the statement on due diligence policies with respect to those impacts?**

7. The extent of compliance with voluntary disclosures varies significantly across respondents.
8. A number of respondents stated that they were not able to provide responses on the extent to which FMPs in their jurisdictions below the 500 employees threshold were complying with voluntary disclosures under Article 4(1)a SFDR as their supervisory analysis will only start in the coming months. The most detailed responses came from NCAs which had already autonomously launched surveys and questionnaires to FMPs under their supervision to assess the operational readiness and preparedness of FMPs and financial advisers on the SFDR.
9. From the responses received, the ESAs conclude that the level of compliance tended to be higher when the FMPs are part of a larger group; however, divergences of approaches towards disclosures make comparison challenging. In addition, compliance with voluntary disclosures for investment firms seems relatively low compared to other FMPs listed in Article 2(1) SFDR.
10. Some highlights from the responses received by NCAs are included below:
  - g. One NCA stated that they are applying a risk-based approach, hence it is not expected that they will analyse compliance with voluntary disclosures for FMPs in 2022. The same NCA noted the efforts towards developing an automated IT tool, otherwise checking compliance would be too burdensome.
  - h. One NCA noted that for smaller entities practices vary across the market. The same NCA stated that after consulting FMPs below the Article 4(3)-(4) SFDR threshold, none ‘showed an interest’ in voluntarily disclosing their method of consideration of the PAI.
  - i. One NCA reported that out of the 14 investment firms supervised, only one published information on PAI under Article 4 (1)(a) SFDR, although that firm took into consideration the impact of the product on sustainability factors rather than the impact of investment decisions themselves.
  - j. One NCA noted that half of market participants in their jurisdictions comply with voluntary disclosures under Article 4(1)a SFDR. Six out of 15 market participants do not publish voluntary information because it is too expensive or because of lack of information to assess the impact.
  - k. One NCA found in their assessment that out of a sample of 29 FMPs operating in the market, only one voluntarily disclosed information. The case for banks providing portfolio management was reported as being very low. Conversely, over 60% of the investment management companies complied with voluntary disclosures.

- l. One NCA stated that institutions for occupational retirement provisions (IORPs) in that market are overwhelmingly choosing not to voluntarily publish PAI consideration, although this is not based on detailed observations.
- m. One NCA noted that self-managed investment companies are less compliant than authorised ones.
- n. One NCA noted a low level of compliance (10%) of insurance undertakings fulfilling the condition to comply under Article 4 (1)(a) SFDR. In one jurisdiction, about 33% of the insurance undertakings below the thresholds set in Article 4 (3)-(4) SFDR, declare on their website that they consider the PAIs in their investment decisions on sustainability factors. However, only 11% complement those disclosures with the requirements under article 4(2) SFDR.
- o. One NCA noted that in their jurisdiction the majority of FMPs are part of domestic or foreign groups, and those groups are in charge of publishing and maintaining statements on due diligence policies with respect to the PAI of investment decisions on sustainability factors on their websites. The disclosure of PAI of investment decisions is shown by the exclusion of certain types of investments.
- p. One jurisdiction said that out of the large sample of insurance undertakings and IORPs taken into account, 'most of them' comply with the rules. One third of asset managers comply with the rules. Conversely, less than 20% of investment firms take PAI into account.
- q. One NCA said that the entirety of the investment fund managers in their jurisdiction comply with voluntary disclosure requirements, whereas another NCA said that 21% of FMPs comply with the rules.
- r. One NCA stated that the vast majority of FMPs used the draft RTS as a reference and guidelines for the purposes of applying the provisions of Article 4 of the SFDR in the interim period.

**2) To what extent are FMPs below the thresholds set in Article 4(3)-(4) SFDR choosing to explain that they do not take into account adverse impact of their investment decisions under Article 4(1)(b) SFDR?**

11. With the exception of some jurisdictions, the extent of the disclosures where FMPs do not take into account adverse impact of investment decisions on sustainability factors is lacking in detail. A general weakness observed is that there is no indication from FMPs as to whether and when they intend to consider such adverse impacts in the future.
12. The ESA note from NCAs responses that when an explanation is offered, the most common reasons are: challenging, uncertain and incomplete regulatory requirements, lack of information and clear methodology with respect to obtaining data from issuers or more broadly lack of publicly available data, expensive processes to implement, no common criteria/practices for defining the necessary indicators, application of proportionality criteria such as size, internal organisation and the nature, scope and complexity of the activities in question.

13. There is evidence of some recognition of the negative impact of investment decisions in some FMPs, and many such FMPs do not exclude that they would change their approach in the future while awaiting the Delegated Regulation complementing the SFDR to be in place.
14. Some NCAs have stated that they do not have such information for the time being and will struggle to obtain them before the end of 2022.
15. Some highlights from the responses received by NCAs are included below:
  - a. One NCA reported that two banks explicitly mention that they do not consider adverse impact of their investment decisions under Article 4(1)(b) SFDR. The statements are very concise and do not give clear reasons for why they do not so and there also no concrete commitments to consider PAI going forward.
  - b. One NCA noted that most of the investment firms disclosing under Article 4(1)(b) state that they do not consider adverse impacts of investment decisions because of the lack of information and clear methodology on how PAI should be considered; it is worth noting that they state that they would be willing to disclose such information in the future as long as a clear methodology is in place (i.e. on how to obtain information from issuers).
  - c. One NCA noted that the extent of FMPs choosing to explain that they do not consider adverse impact of their investment decisions under Article 4(1)(b) SFDR is minimal.
  - d. One NCA said that 8 out of 29 considered investment management companies (28% of the sample) disclose a statement on the reasons for not considering PAI. The most typical explanations are: lack of data/information necessary to conduct the impact analysis; incomplete regulatory framework; or lack of expertise in the area.
  - e. One NCA noted that often the disclosures of fund managers and self-managed funds are limited to a statement that such entities do not consider adverse impacts of their investment decisions with little to no additional explanation provided.
  - f. One NCA responded that FMPs include in their investment policies several elements which could be recognised as a direction towards compliance with Article 4(1)(a): exclusion policy regarding some types of counterparties/investments, ranking of the counterparties regarding ESG factors, preferences for the counterparties which have better ESG features. Most of such undertakings do not exclude that they will change their approach in the future. Some of them indicate that they are waiting for the full legislation to apply before deciding whether to change the approach.
  - g. One NCA noted that while IORPs and insurance undertakings in its jurisdiction are fully aware of the importance of sustainability factors, they do not take them into account because from their perspective they cannot be clearly and correctly quantified and duly taken into account.
  - h. One NCA stated that 20 out of the 39 investment management companies in the sample have chosen to explain that they do not take into account adverse impact of their investment decisions under 4(1)(b) SFDR because of the application of the proportionality criteria (size, internal organisation and nature, scope and complexity of the activities in

question), lack of data and comparable information regarding sustainability, or the need for further development in the regulatory space which would provide more certainty on how to comply with the requirements.

- i. One NCA noted that those FMPs choosing to explain why they do not consider adverse impacts of their investment decisions use the argument that measuring the effects of such policies on sustainability would not be proportional to their organisational, technical and personnel structure.

### **3) Have you observed any examples of FMPs not complying under Article 4(1)(a) SFDR nor explaining under Article 4(1)(b) since March 2021?**

16. From the responses received, the level of compliance varies across jurisdictions and FMPs. For those FMPs who are compliant, NCAs observe room for improvement on the quality of the disclosures and completeness of information provided, noting that in some cases it was difficult to discern whether FMPs were not in compliance or whether the information was too difficult to find (i.e. breach of disclosure rules versus improvement of the website structure).
17. A number of NCAs have noted that they will follow up individually with supervised entities to inquire the reason for non-compliance.
18. Some NCAs admitted that ensuring compliance with the obligation was not a supervisory priority.
19. Some highlights from the responses received by NCAs are included below:
  - a. One NCA responded that while all FMPs have complied with the relevant provisions by setting out disclosures in the required documentation, there is a lot of room for improvement in the quality and depth of the documentation disclosures.
  - b. One NCA stated that their priority was to supervise pension schemes' adaptation to IORP II requirements following the recent transposition into national law. More attention to website disclosures will only be done once this process is completed.
  - c. One NCA responded that in their analysis of the market they found cases of non-compliance in terms of absence of provision of website disclosure links or overall limited disclosures. The vast number of the investment firms and credit institutions providing portfolio management in the sample informed that they are still 'studying the ramifications of the SFDR'.
  - d. One NCA responded that out of the 26 FMPs analysed, 10 FMPs are not disclosing any information on PAI, and when information is available, it is very difficult to find. All fund managers supervised by the NCA included in the sample were compliant.
  - e. One NCA included in their annual supervisory plan the off-site supervision of branches of investment firms and alternative fund managers which are not compliant with voluntary disclosures.

**4) How many FMPs have been considered in your assessment under questions 1-3? Is that a reflection of the market size in your jurisdiction? Where available, please provide a breakdown by sector (asset management, insurance, pensions, banks).**

20. The ESAs have decided not to provide a specific threshold in terms of minimum number of market participants or AuM to be included in the sample for this first Report.
21. NCAs have taken a different approach in the selection of the sample of FMPs to be considered in the assessment of questions 1-3, based on a relatively small size of total number of FMPs, but in some cases still representing more than half share of the sector (in terms of assets under management).
22. Some highlights from the responses received by NCAs are included below:
- a. One NCA noted that the sample chosen reflects different business models, organisational structure, and size, with a about 10% of insurance undertakings, 20% of asset management companies and around 1% credit institutions/investment institutions. Another NCA has selected a sample of 28% of investment firms, 25% of banks providing investment service of portfolio management and about 20% of the management companies representing about 70% of the total AuM. Another NCA has chosen to assess 20% of banks providing portfolio management services, 15.4 % of investment firms and 20% of authorised AIFMs.
  - b. One NCA responded that they chose 17 banks for their assessment (about 4.3% of the Member State's total assets).
  - c. In one jurisdiction, the sample chosen represents 80% of all life insurance undertakings and 80% of pension funds; on the asset management side, the sample totalled 93% of the sector in terms of total assets under management.
  - d. Other NCAs operating in small jurisdictions have managed to take 100% of the FMPs as sample for the purpose of this survey.
  - e. For the remaining NCAs, some provided absolute numbers of FMPs included in the sample or stated that they have included in the sample a "high percentage" of either the total number of FMPs or the total AuM.
  - f. One NCA reported that a total 15 FMPs have been questioned in their jurisdiction, being in the top 20 in terms of AuM (after exclusion of the FMPs that are above the Article 4 (4) SFDR thresholds) and are all asset managers part of a larger group. They represent 35% of total AUM at the end of 2020.

**5) Have you observed any differences with regard to FMPs' disclosures under Article 4(1)(a) depending on their size, the nature and scale of their activities and the types of financial products they make available? Please explain, possibly with examples.**

23. The reply to this question varies across NCAs and market participant so specific trends could not be identified.

24. Some respondents noted that bigger FMPs in size, nature and scale of activities have higher level of compliance, while other NCAs observed the opposite trend, with smaller FMPs having higher level of compliance compared to bigger ones. The reason for the latter trend is that the larger a FMP's investments, the more difficult it is to assess all the adverse impacts.
25. Those FMPs which are part of larger groups adopt strategies stemming from parent companies and are counting on higher degree of 'technical' support. In addition, FMPs that are signatories of the Principles for Responsible Investment (UN PRI) tended to show a greater degree of disclosure provided to investors.
26. Some highlights from the responses received by NCAs are included below:
- a. One NCA noted that while differences are detectable, they could hardly be generalised as some small FMPs comply better with their obligations compared to some bigger ones. The same NCA adds that FMPs that are part of larger foreign groups adopt strategies stemming from those parent companies.
  - b. One NCA observed that FMPs with higher AuM tend to have more detailed information on the disclosures under Article 4(1) SFDR. In the same way, FMPs signatories of the Principles for Responsible Investment (UN PRI) also have a deeper degree of disclosure provided to investors.
  - c. One jurisdiction noted that universal cross border banks tend to provide more granular disclosures on the website, even if beyond SFDR requirements, as they leverage from group policies, while smaller institutions do not even have a dedicated sustainability section on their websites.
  - d. One NCA noted that insurance undertakings are more representative in their disclosures compared to IORPs, because of the size and the transparent investment policy of the IORP.
  - e. One NCA observed that disclosures of smaller FMPs (including market size and number of employees) result being more on high level principles with less information in comparison with larger FMPs, especially those which are part of parent groups.
  - f. One NCA confirmed that the difference is relevant when the company is a member of a larger group, in which case they can receive greater technical support from parent undertakings and better-quality disclosures.
  - g. One NCA stated that disclosures by larger FMPs are in general more comprehensive but not necessarily easier to find.
  - h. One NCA noted that cases have been identified that they did not comply with neither 4(1)(a) nor 4(1)(b). These cases concerned insurance undertakings with insignificant level of production of IBIPs.

**6) Do you believe the website disclosures of PAI under Article 4 SFDR are 'easy' and 'straightforward' to find? Please provide any relevant comment or example**

27. The majority of NCAs responding to the survey note that information on disclosures are overall, easy and straightforward to find.
28. Some NCAs note when website disclosures of PAI under Article 4 SFDR are not easy to find, it is because they are provided at the bottom of the website or fragmented, i.e. presented in several documents and /or sub-webpages.
29. While the statement is generally located under the ‘sustainability’ tab, from a number of responses it emerged that the search of such sub-pages is not so easy and subject to long search paths, sometimes hidden by high level statements or voluntary initiatives that the FMP undertakes which have no regulatory relevance.
30. No definitive conclusion can be drawn regarding to the size of the FMP. There are also some differences across some FMPs in different jurisdictions (i.e. information in savings banks in one jurisdiction are not so easy to find compared to those from another jurisdiction).
31. Some highlights from the responses received by NCAs are included below:
- a. One NCA noted that some FMPs place the statement on due diligence policies with respect to the adverse impacts of investment decisions on environmental and social sustainability factors under Article 4 SFDR on their websites under the menu item “Sustainability”, which helps to find these disclosures easily, even though these statements are difficult to find on most of FMPs’ websites.
  - b. One NCA noted that information on ESG/sustainability is often difficult to find and fragmented (presented in a several document and/or sub-webpages) rather than in one document or one sub-webpage. Along the same lines, another NCA noted how long the search path is for the disclosures, due to the different structure of the websites.
  - c. One NCA noted that website disclosures are mainly focused on the positive impact of sustainable finance policies, consequently disclosures of PAI are presented in the background of such disclosures, but still disclosed.
  - d. One NCA observed that a small number of FMPs do not disclose on PAI under Article 4 SFDR in a visible, nor easy or straightforward to find, and this will be addressed during off-site supervision during 2022.
  - e. One jurisdiction noted that banks often do not include the statement on due diligence policies with respect to the adverse impacts of investment decisions on environmental and social sustainability factors on their sustainability pages but rather on legal documentation pages, and often mixed with risk management related information.
  - f. One NCA noted that in most of the cases in the sample, the statement on due diligence policies with respect to the adverse impacts of investment decisions on environmental and social sustainability factors can be found easily in an investment management company’s website, either under a specific section of the website called ‘sustainability’ or in the legal information section. In a few cases, when information could not be found directly on the

management company's website, then it was in the corporate group's website, often together with other sustainability related information and was relatively easy to find.

**7) As part of the statement under Article 4(1)(a) SFDR, do FMPs disclose the degree of their alignment with the objectives of the Paris Agreement? Please provide any relevant information or example**

32. There is an overall low level of disclosure of the degree of alignment with the objective of the Paris agreement, with few examples provided by the survey respondents.
33. When disclosure is made, it is often vague and in high level terms, with information related to the degree of alignment with the objectives of the Paris Agreement unclear, and without indicators reported to show how the institutions measure the decarbonisation path of their portfolios.
34. Some highlights from the responses received by NCAs are included below:
  - a. One NCA noted that only one out of the 28 investment management companies in the sample discloses the degree of alignment in a concise form in its homepage's text on sustainability and deepens this topic in brochures as well as in a Q&A.
  - b. Another NCA noted that it is common to find quite general references the alignment to the Paris Agreement objectives in the policy on the integration of sustainability risks in their investment decision-making process.
  - c. One NCA stated that they had no experience in the assessment of the insurance undertaking disclosures of the degree of alignment with the objectives of the Paris Agreement.
  - d. One NCA provided examples of high-level statements to show alignment, such as 'in the future, we are moving in line with the Paris Agreement's goal of not exceeding a 1.5 °C increase in planetary temperature' and 'we are committed to transforming our investment portfolio into a zero-carbon portfolio by 2050'.
  - e. One NCA noted that several investment management companies in their jurisdiction make general and at times vague references to the alignment with the Paris Agreement and take into account the recommendations of the Task Force on climate related financial disclosures (TCFD).
  - f. One jurisdiction reported a low level of compliance for banks and investment firms. On the asset management side, around 80% of fund managers make a reference to their adherence to responsible business conduct codes and internationally recognised standards for due diligence and reporting, and where relevant, the degree of their alignment with the objectives of the Paris Agreement. However, the information was quite general and standardised.
  - g. One NCA stated that some FMPs mention their ambition to meet the objectives of the Paris Agreement, however, in general no degree of alignment is disclosed.

- h. Finally, one NCA noted that multiple FMPs mention or refer to the Paris Agreement and its 2°C or 1.5°C alignment. 5 out of the 12 actors mention it explicitly and 2 others refer implicitly to it through the mention of the 1.5°C and 2°C alignment. However, none actually report in their PAI statement the degree of their alignment with the Paris Agreement objectives.

**8) Do you have any best practices you would like to share or highlight in terms of voluntary reporting standards?**

35. Most respondents did not provide best practices or preferred to not respond to the question at this stage.
36. We have highlighted below some of the NCA input relevant to this question:
  - a. One NCA provided two examples from market participants in their own jurisdictions worth sharing with the ESAs: the first one is from a credit institution providing portfolio management (above the 500-employees threshold) which indicated that PAI will have an important role in determining the exclusion of some investments and that it intends to use (where available) the breadth and depth of a widely used commercial financial data provider; the second example, from the insurance sector, substantiated their disclosures as to the degree of their alignment with the objectives of the Paris Agreement through the publishing of a Report, accessible through a link on the same website disclosure, which provides further information on that alignment.
  - b. One respondent noted that improving visibility and making disclosures more prominent on websites (as opposed to footnotes or hidden links) is a good practice.
  - c. One respondent noted that as general best practice, disclosure documents should be dated, and have in the title a language / wording which are closely aligned and identifiable with SFDR.

**9) Is there any comment or consideration you would like to share with the ESAs at this stage?**

37. A number of respondents' comments focused on the current level of uncertainty, noting that through the application of the Delegated Regulation and clarity on the timing for the mandatory disclosure templates the situation will be improved.
38. Some NCAs flagged that policies disclosed in terms of risk management and PAI considerations are often confused or mixed, and in many occasions, exclusion policies are used to justify both ESG risks management and PAI mitigation actions. In addition, a number of NCAs have called for further guidance on where and how to publish the disclosure requirements (dedicated field available on the home page of the websites of the entities, etc.).
39. The key comments and considerations shared with the ESAs are as follows:
  - a. One NCA noted that it is evident that FMPs are still amending and further improving disclosure-related information, while just formally fulfilling their obligation. As an example, the NCA mentioned an FMPs signing up and referring to international conventions and standards ahead of the entry into force of the SFDR.

- b. One NCA informed the ESAs that they are currently developing a survey that will be circulated to all UCITS and AIF management companies. It aims to determine whether these companies comply with Article 4 of the SFDR on a voluntary basis and whether the statements published by these companies comply with the SFDR.
- c. One NCA noted that FMPs usually mix up principal adverse impacts of investment decisions on sustainability factors and sustainability risks, and this results confusion for the investors. A bad practice developing in that jurisdiction is stating for example: "The Asset Manager also assesses the impact of the issuer's business on sustainability risks when making investment choices...".
- d. One NCA noted that supervised entities tend to consider their disclosures to be dependent on corporate structures and proportionality (costs of the disclosures compared to the size). In general, supervised entities are in favour of sustainability reporting but there is still uncertainty about how to implement it correctly.
- e. One NCA informed the ESAs that it has recently contacted those AIFMs and self-managed AIFs below the 500-employee threshold to evaluate their level of compliance with SFDR and such information will be assessed by the NCA in the coming months to obtain a complete picture of the industry's level of compliance.
- f. One NCA raised the issue of the low level of financial literacy of retail investors in that jurisdiction, and the potential risks of misleading PAI disclosures for FMPs when those entities are not offering products disclosing under Article 8 and 9 SFDR.
- g. Finally, one NCA noted that there is confusion amongst FMPs on the interpretation of Article 4(4) SFDR, mainly related to the issues around the definition of parent undertaking.