



Matheson

SFDR Factsheet:
Specific Requirements for
Article 8 Light Green Funds



January 2021

The European Commission (“**Commission**”) launched its Sustainable Finance **Action Plan** in March 2018, including three legislative proposals aimed at: creating an EU sustainability taxonomy; requiring disclosures relating to environmental, social and governance (“**ESG**”) factors; and the creation of low carbon and positive carbon impact benchmarks. This note focuses on the **Sustainable Finance Disclosure Regulation**, known as the SFDR or the Disclosure Regulation, and in particular the requirements for investment funds that fall within the scope of Article 8 of the Disclosure Regulation, known as “Light Green” funds.

WHAT DOES THE DISCLOSURE REGULATION AIM TO DO?

The Disclosure Regulation requires alternative investment fund managers (“**AIFMs**”) and UCITS management companies (each a “**Manager**”) (amongst others, but for the purposes of this note, we focus on investment funds and their Managers)¹ to consider and disclose in a consistent and harmonised manner how ESG factors are adopted in their decision making processes. It aims to harmonise disclosure standards among EU member states to facilitate the comparability of different financial products and services. Many of the provisions of the Disclosure Regulation apply to all asset managers, whether or not they have an express ESG or sustainability focus. The Disclosure Regulation applies different requirements and implementation timeframes in respect of disclosures:

- in prospectuses;
- on websites; and
- in periodic reports.

¹ The Disclosure Regulation applies to “financial market participants” which includes MiFID firms providing the service of portfolio management, AIFMs and UCITS managers. It applies to AIFs, UCITS and portfolio management services / managed accounts. The Disclosure Regulation also applies rules to financial advisers, which are not addressed in this note.

WHEN WILL THE DISCLOSURE REGULATION APPLY?

The main provisions of the Disclosure Regulation will apply from **10 March 2021**. The requirements relating to disclosures in the periodic reports of ESG-focused products are stated to apply from **1 January 2022**.

WHEN WILL THE TECHNICAL STANDARDS BE AVAILABLE?

The European Supervisory Authorities (“**ESAs**”) are mandated under various provisions of the Disclosure Regulation to provide further detail on the exact level of information to be disclosed. In April 2020, the ESAs published a joint **consultation paper** setting out their proposals, including some draft templates (with further templates in respect of pre-contractual and periodic disclosures to be provided at a later date) and draft regulatory technical standards (“**RTS**”). The ESAs were required under their mandate to submit their final advice on RTS to the Commission by the end of December 2020 but they indicated in October 2020 that they will not submit the advice until January 2021. As a result, it is expected that the final RTS will not be issued until early / mid 2021.

On 20 October 2020, the Commission confirmed in a **letter** to the ESAs that all application dates are being maintained as laid down by the SFDR with effect from 2021, notwithstanding the delay to the publication of RTS. Fund managers will be required to comply with the high level and principle based requirements of the Disclosure Regulation from 10 March 2021 but the RTS will become applicable “*at a later stage*”.

WHAT ARE “ARTICLE 8 FUNDS”?

An Article 8 fund is a fund that “promotes environmental and social characteristics” provided that the companies in which the investments are made follow good governance practices. The Disclosure Regulation does not include a specific definition of what is meant by a product which promotes environmental or social characteristics, nor does it clarify how managers should distinguish between such products and Article 9 products, which are products which have “sustainable investment” as their objective (known as “Dark Green” products). It is unlikely that the ESAs will issue further guidance on this as they have stated that the interpretation of promotion is a level one matter ie, it can only be addressed in the primary, or level 1, regulation and not in delegated acts or guidance to be developed by the ESAs and therefore can only be addressed by the Commission.

In a **speech** delivered on 3 November 2020, Mr Gerry Cross, Director of Financial Regulation Policy and Risk at the Central Bank of Ireland (“**Central Bank**”), recognised that there are questions around product classification, specifically with respect to the scope of application of Article 8 as distinct from Article 9 products that were to be addressed in the technical standards. The Central Bank stated, “*In the first instance, therefore, the decision regarding classification will rest with the relevant manager.*” The Central Bank does not intend to issue any guidance on classification at this time. The Central Bank may follow up with individual managers to query their classification in due course.



WHAT UPDATES MUST BE MADE FOR ARTICLE 8 FUNDS TO COMPLY WITH THE DISCLOSURE REGULATION?

As outlined above, certain disclosures will need to be made on the website of the Manager, in the prospectus of the Article 8 fund (or its umbrella fund) and in the periodic reports of the Article 8 fund (or its umbrella fund) in order to comply with the requirements of the Disclosure Regulation.

PROSPECTUS

Article 6

While Article 8 applies additional disclosure requirements to funds that fall within its scope, Article 6 of the Disclosure Regulations applies disclosure requirements to every type of investment fund within the scope of the Disclosure Regulation. Article 6 requires a Manager to include descriptions of the following in the prospectus of the relevant fund (or its umbrella fund):

- the manner in which sustainability risks are integrated into the investment decisions of the Manager; and
- the results of the assessment of the likely impacts of sustainability risks on the returns of the funds they make available.

Where an AIFM or UCITS management company deems sustainability risks not to be relevant, Article 6 requires the Manager to include a clear and concise explanation of the reasons for taking such approach in the prospectus of the relevant fund.

Article 8

Where a fund falls within the scope of Article 8, the following disclosures will also be required:

- information on how environmental and social characteristics are met;
- where an index has been designated as a reference benchmark, information on whether and how the index is consistent with those characteristics; and
- information as to where the methodology used for the calculation of the reference index can be found.

WEBSITE

Article 3

Article 3 of the Disclosures Regulation requires each Manager to publish information about their policies on the integration of sustainability risks in their investment decision-making process on their websites.

Article 4

Article 4 of the Disclosures Regulation furthers the requirements in Article 3 and sets out additional information to be published and maintained on the websites of Managers; including:

- 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, the nature and scale of their activities and the types of financial products they make available. The information to be provided is required to include: (i) information about the policies of the Manager on the identification and prioritisation of principal impacts and indicators; (ii) a description of the principal adverse sustainability impacts and of any actions in relation thereto taken or, where relevant, planned; (iii) brief summaries of the policy of the Manager with respect to shareholder engagement pursuant to the Shareholder Rights Directive where the Manager is required to have such a policy; and (iv) a reference to 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; or
- where the Manager does not consider adverse impacts of 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.

While the decision as to how to comply with the requirements of Article 4 is generally at the discretion of the Manager, from 30 June 2021 large Managers (ie, those with more than 500 employees) will be required to implement the due diligence policy outlined above.

Article 5

Article 5 of the Disclosures Regulation requires a Manager to update their existing remuneration policy which is published on its website to include information on how such remuneration policy is consistent with the integration of sustainability risks.



Article 10

In addition to the requirements outlined above, Article 10 of the Disclosures Regulation requires the Manager's website to include certain additional information where the Manager has been appointed to an Article 8 fund. The relevant information to be disclosed on the website includes:

- a description of the environmental and social characteristics;
- information on the methodologies used to assess, measure and monitor the impact of the sustainable investments selected for the fund, including its data sources, screening criteria for the underlying assets and the relevant sustainability indicators used to measure the overall sustainable impact of the financial product;
- the information that is required to be disclosed in the prospectus under Article 8 as outlined above; and
- the information that is required to be disclosed in annual report of the fund (or its umbrella fund) under Article 11 as outlined below.

PERIODIC REPORTS

Article 11

Pursuant to Article 11 of the Disclosure Regulation, the annual report of a fund which falls within the scope of Article 8 is required to include information on the extent to which the environmental or social characteristics are met.

Unlike the prospectus and website requirements, which apply from 10 March 2021, as outlined above the Disclosure Regulation outlines that the periodic report requirements for ESG-focused funds will apply from **1 January 2022**. While it is not clear from the level 1 text and further clarification on this point would be welcome, this requirement may be interpreted to mean that the disclosures must be included in annual reports beginning on or after 1 January 2022, such that the disclosures will first appear in the annual reports of Irish funds in early 2023 (ie, for those funds with an accounting period of 1 January 2022 to 31 December 2022).

COMMENT

Before the required disclosures can be made under the Disclosure Regulation, Managers must make a number of business decisions and conduct an exercise to categorise their funds. If categorised as an Article 8 fund, the above requirements will need to be complied with by the relevant deadlines set out in the Disclosure Regulation. There is a considerable amount of work to be undertaken to do this and to update policies and documentation in advance of the **10 March 2021** deadline.

In order to deal with the large volume of updates that must be filed by the March deadline, on 4 November 2020, the Central Bank confirmed that there will be a fast-track process for filing updates for UCITS (QIAIF will continue to benefit from the existing 24 hour filing process). UCITS funds and their managers will be expected to self-certify compliance with the requirements of the level 1 Disclosure Regulation requirements. The Central Bank will not conduct a review of these level 1 disclosures prior to the 10 March deadline. The Central Bank will review disclosures in full prior to the implementation of the level 2 technical standards (the general market sense is that the level 2 technical standards will apply from 1 January 2022).

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 update.



SFDR FACTSHEET: SPECIFIC REQUIREMENTS FOR ARTICLE 8 LIGHT GREEN FUNDS

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