

## SFDR REVIEW TIMELINE AND PRIORITIES



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### What the EU sustainable finance should have meant for companies and investors?

The Sustainable Finance Disclosure Regulation was the first sustainable finance law during the previous term of the European Commission. What it should have looked like is very different as to what the outcome was - just like with the other sustainability legislation currently under review from the Corporate Sustainability Reporting Directive to the EU Taxonomy.

Sustainability disclosures and reporting should mirror financial disclosures and accounting. It's as simple as that. You allocate elements into categories and include harmonised indicators and science-based methods into calculating the effects. The system also needs a clear beholder of standards, such as the ISSB. This would enable harmonised and comparable global standards and mechanisms.

Companies don't need many data points to estimate their actual sustainability impacts - be they adverse or positive. Resource use - materials, energy, water or waste; emissions and chemicals - CO<sub>2</sub> and emissions into water, soil and air; biodiversity and direct and indirect land use are the core of climate and environmental impacts. Of course, as in accounting, these main categories would then be divided in sub-categories to reflect different industries' needs.

Investors need comprehensive information to assess the risks, trade-offs and added value more precisely. With a holistic view of actual adverse and positive impacts both in the downstream and upstream value chain - including the full lifecycle from cradle to grave - investors are able to better appreciate long-lasting products, services or digital solutions.

Let's take the example of pallets, a sturdy staple of logistics everywhere. To make them, we're cutting down or using valuable wood, spraying them with toxic chemicals and despite improvements in reuse, a portion of them still end up lying in warehouse yards. The pallets could be taken towards a more service-based rental model with location tracking or we could boost the development of new composite materials for them.

When producing a new product or business model, it's almost impossible to optimise everything in the process. Therefore, the cumulative effects from resources, emissions and biodiversity are needed for informed investment decisions. What the current Omnibus I proposal does, is that it severs the information flow almost entirely, so investors will not have the enough knowledge for informed decisions and risk management. With the current draft, companies are soon forbidden to even ask for data from their value chain partners.

EU Taxonomy's challenge is that it measures inclusion not impact. The innovative and disruptive green products are exactly what we need to bridge the worsening gap between where we are and where science says we should have already been years ago. Without being Taxonomy-aligned or including the whole lifecycle assessment, it is difficult for investors to pick the targets for largest actual impacts.

The Taxonomy, and the SFDR classification, needs to be one of benchmarks supporting the transition

and set on an evolving scale. The highest benchmark would be for science-based activities fully carbon neutral and within the planetary boundaries. The best of the best, most likely new, highly innovative and super green - the solutions often outside the Taxonomy.

Coming to the current dark greens, these are the companies highly attractive to investors, receiving beneficial treatment as the Taxonomy pushes investment flows towards this category. Light greens should equally promote transition towards full alignment but the problem with the current static system is that for example natural gas remains a transitional raw material "forever". The scale would also need definitions for red and black categories. Red would mean inaction with regards to sustainability and black stemming from risk assessments - meaning fossil-based business activities, destructive to biodiversity and heightening land erosion, excessive water consumption as well as a disrespectful and bad governance around sustainability.

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Companies' transition plans should be based on this scale. If a large company pledges to let go of fossil-based raw materials and energy within six years, they need to implement their transition plan into annual milestones and audit them. Just having a plan and moving according to it makes a company light green - and lack of progress would move them back into the red sector. With advancements and reaching goals, the company would be included in the dark green class and with the benefits of preferential treatment.

The best side to this transitional scale would be accuracy and providing a more realistic image as to where companies truly are and what needs to be done. The super green share would most likely be under 5 % and the dark greens 15-20 % even on an optimistic assessment. The risk assessment would also highlight where investments are needed most urgently for most impact and possibly help investors move away from the impending problem of stranded assets.



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### Reforming SFDR and refocusing on climate action

The entry into force of the SFDR in March 2021 marked a significant milestone in the EU sustainable finance journey. By enhancing transparency with respect to sustainability-related products, the SFDR has helped shed light on the critical issue of addressing climate change impacts. It has encouraged market participants to bolster their offer of sustainability-related products. However, recently, we have observed a sustained decline in investor demand for the greenest investment offerings under SFDR - products disclosing under Article 9 of SFDR which are designed with a sustainable investment objective. Redemptions from funds disclosing under Article 9 have persisted and according to latest market intelligence, have reached an all-time high in Q1 2025. Funds disclosing under Article 8 of SFDR having been relatively spared, netting new money, which may be explained by the broad range of products Article 8 of SFDR accommodates.

The geopolitical context in which we are evolving is one of the factors that can help explain the observed trends. However, the impact of the legislation and its implementation also merit consideration. The sustainable finance

framework continues to put the EU in a pioneering role in the area but its implementation by market participants - and the supervision thereof by national competent authorities - remain challenging. This is mainly due to the absence of clarity on several foundational concepts of the regulation, like that of a sustainable investment, the computation of the proportion of sustainable investments, including the consideration of derivative instruments or how to ensure/measure alignment with the do no significant harm principle. This absence of clarity on such key concepts has resulted in several iterations of the regime. But revisions which do not bring the necessary clarifications only create legal uncertainty as well as undue complexity and, in the end, undermine the credibility of the framework. At the same time, the EU has further strengthened the existing regime through new regulatory initiatives. The latest initiative being the ESMA Guidelines on funds' names using ESG or sustainability-related terms in their names. The application of the Guidelines builds on the (unclear) foundational concepts of the SFDR. Also, they do not apply to all SFDR products but only to funds, which is conducive to contributing to market fragmentation. Because some of the core concepts underpinning the Guidelines - such as the list of ESG terms that trigger their application - are not clearly defined, the practical application of the related provisions is likely to lead to confusion. The recent Omnibus legislation on sustainability reporting, introduced in early 2025, proposes to narrow the scope of the CSRD. This shift is likely to have significant implications for the SFDR, particularly regarding the ability of market participants to comply with their quantitative disclosure requirements.

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Against this backdrop, two key elements stand out. First, while sustainability-related investments appear to suffer headwinds in recent times, it is a fact that climate change does not wait. Sustainability remains a globally critical priority, and the EU must continue to treat the issue as such. Secondly, the financial sector shall remain an important part of the jigsaw to mobilize private financing to reach the objective of the EU Green deal and hence allow the EU to become climate-neutral by 2050. The sine qua non condition is

the implementation of a trusted, robust and coherent sustainability framework that enables large-scale mobilization of private investments to drive the transition. The announced revision of the SFDR by the European Commission to address the shortcomings of the SFDR is thus welcomed. It is essential that the sustainability framework builds on commonly accepted foundational concepts that are clear and robust. The current disclosure categories under the SFDR need to be redefined. While SFDR has been used as a labelling regime, Articles 8 and 9 may fall short in enabling investors navigate the broad range of sustainability-related products. To enhance transparency, product categories based on clear and objective criteria - such as those under the Taxonomy Regulation - are needed to better inform investors on the investment objective of the product. Recognizing that greening the economy is not a linear process, the categories must accommodate transitional assets, which SFDR currently lacks. Product disclosures need to be revised to be more investor centric, adapting to varying levels of investor sophistication. The current templates are too complex for retail investors and might trigger an information overload.

A review of SFDR should now be undertaken in the spirit of resolving existing issues once for all, enabling a renewed focus on addressing the pressing issue of climate change. Investor trust is pivotal to any policy effort and only a well-designed framework can help uphold trust.



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### Reviewing the SFDR to better fit its purpose

The SFDR is a key pillar of the EU's sustainable finance framework designed to bridge the financing needs underlying the transition to a sustainable economy with investors seeking sustainable investment opportunities.

For the regulation to effectively achieve its objectives, investors should have access to simple, clear and useful information on the sustainability characteristics of financial products, while avoiding excessive disclosure burden on financial market participants (FMPs), notably when that disclosure does not add meaningful value to investors' decision-making.

A paper published by ESMA (in April 2025) shows that the use of ESG-related terms increased significantly among EU fund names between 2015 and 2024 and that adding an ESG term can significantly boost fund inflows. Furthermore, the impact of the 2024 ESMA guidelines on funds' names - leading to funds rebranding and/or portfolio changes - demonstrates the importance of having clear rules and criteria, rather than relying on vague concepts leading to different interpretations across Member States/FMPs. Effective supervision and supervisory convergence across EU Member States play a key role too in avoiding the potential misuse

of sustainability-related claims by investment funds. This evidence shows how important the information disclosed to investors is and, consequently, the key role that regulation addressing ESG-related disclosure requirements plays in this context.

While the SFDR has brought many challenges and there is still room for improvement as highlighted in the key findings of the ESMA Common Supervisory Action on the integration of sustainability risks and disclosures, there has also been a progressive and satisfactory level of compliance. However, after four years of implementation, there is broad recognition that the SFDR regime needs to be reviewed to improve the effectiveness of its rules as well as their coherence with other key elements of the EU's sustainable finance framework. The following aspects should be addressed:

Firstly, and to provide retail investors with information that is easy to understand and effectively useful for their investment decisions, the introduction of well-defined "sustainable" and "transition" product categories, clearly indicating the sustainability ambition and objectives of a product, seems the way forward. These two categories should be based on objective and measurable criteria, each with specific minimum quality and disclosure requirements, as well as rules governing naming and sustainability claims. MiFID should then be revised to take the introduction of these product categories into account.

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Secondly, the SFDR revision should be focused on product-level disclosure, providing the most relevant information to investors, while streamlining entity-level disclosure, whose usefulness to investors appears insufficient to justify the burden they impose on FMPs.

Thirdly, the ambiguity of certain key SFDR definitions should be addressed, especially the concept of "sustainable investments." By aligning it more closely with the EU Taxonomy, the definition should be made more prescriptive and harmonized, with a clear link to the criteria defined for the new product categories. This would greatly improve

transparency, comparability, and credibility across the market.

Ultimately the SFDR review should not only be aligned with the 'Omnibus' package focused on the simplification of sustainable finance regulation – as the underlying regimes (notably the Taxonomy Regulation and the CSRD/ESRS) are closely interlinked and it is therefore necessary to properly assess how the proposed changes affect each other –, but also with other ongoing initiatives such as (i) the RIS – whose main objective is precisely to empower retail investors to make investment decisions that are aligned with their needs and preferences; (ii) the SIU, to the extent that it aims to create better financial opportunities for EU citizens and reduce fragmentation in EU capital markets; and (iii) the Competitiveness Compass, the roadmap to restore Europe's dynamism and boost economic growth.

The implementation of the SFDR entailed significant investment, resources and time from FMPs. Striking a balance between revising the SFDR from a retail investor perspective and sparing FMPs from significant additional implementation costs is highly challenging. However, an investor-centric approach must be combined with a competitiveness check to ensure that this review addresses the concerns put forward by different stakeholders in a balanced manner, while promoting the transition to a more sustainable economy. Ideally, all proposed solutions should thus be tested with both retail investors and FMPs to ensure they meet the intended objectives.

Now is the time to improve consistency among the several EU sustainable finance regulatory building blocks and to guarantee the holistic approach that is needed concerning the broader EU regulatory strategy.





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### The SFDR review should not be a missed opportunity

The SFDR review started in September 2023 with the European Commission's extensive consultation on this revision process. Since then, many discussions held have resulted in the identification of two main pillars to simplify the understanding of retail clients and to facilitate their investment decision making: introduce 3 categories (Sustainable, Transition and other ESG) and massively simplify the disclosure requirements. These evolutions are going into the right direction. However, their concrete implementation will raise several challenges that must be properly addressed.

First, retaining a principle-based approach for the criteria applicable for each category would not be relevant. This approach is the one selected for the Sustainable Disclosure Regulation in the UK. It has proven quite difficult when effectively implemented, leading to numerous bilateral discussions between the UK authorities and the asset managers. In addition, there are 27 different member states within the EU. Lack of minimum binding criteria could result in diverging interpretations by national competent authorities (NCAs) and in the end to further fragmentation. Having minimum binding, clear and measurable criteria for each category should be the privileged option to ensure

the comparability between products and enhance the investor protection. At the same time, it should be possible to use a custom "other approach" on a case-by-case basis if it is demonstrated to the NCA that this approach has an equivalent outcome.

The diversity of asset classes must also be taken into consideration and criteria must be adapted to certain ones, with similar approach for all products investing in these asset classes. Typically data available for private assets is very limited, this specificity must be addressed. The treatment of sovereign bonds should also be properly covered. Some products, as insurance and pension products, have a large proportion of their investments in this asset class. Further technical analysis is required to identify the most appropriate solution, by covering the case of quasi-sovereign bonds and determining what would be the right calibration methodology for sovereigns. Extension of SFDR to structured products could also be envisaged provided that similar products are treated in the same way.

Second it must be clearly specified if the categories will be mandatory or voluntary, i.e. will it be possible for one non-categorized product to make some ESG claims? Opening the door to this possibility would create strong confusion among retail investors that could be offered non-categorised products when they have indicated some ESG preferences. In addition, there would be a risk that these products have ESG claims while not being submitted to the transparency requirements adopted for categorised products. It is of utmost importance that the new text mentions without any ambiguity that only categorised products can make ESG claims in all the legal and marketing documentation and that they cannot be offered to retail investors with some ESG preferences.

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Third there are intense discussions on the sustainable investment definition and lack of consistency resulted from the multitude of methodologies used. This being said, the sustainable investment concept should be maintained under the SFDR 2.0 with introduction of minimum criteria that should neutralize

the differences between proprietary methodologies. The selectivity approach that requires minimum proportion of investments in the products' investment universe, by excluding less performing ones, is one of those that could be applied. Alignment with the environmental taxonomy could be part of these criteria, however it should not be mandatory as initially suggested, especially following the revision of the Taxonomy Regulation that could result from the Omnibus package.

Lastly, the simplification of the disclosure requirements is essential. The purpose of standardised product disclosure is to facilitate the investment journey of retail clients. Thus, disclosures must be simple and synthetic. The precontractual document and the periodic report should be short and synthetic, containing only the binding ESG-related elements of the investment strategy. There is no rationale in maintaining the website disclosures as it is redundant with the pre-contractual document and too technical for retail investors. For the disclosure at entity level, the priority should be its rationalization with a limited number of indicators taking into consideration the data available for each of them.

In the end, the SFDR review should not be a missed opportunity. Any changes should lead to effective simplification and fixing of the identified issues. The design of the "categories should address the current too broad Article 8 classification. The new categories should also be fully aligned with the ESMA fund naming guidelines to leverage on the clarity they have provided and avoid any divergences between two different sets of rules.



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# Balancing simplicity and substance: impact of EU Omnibus Package on SFDR

## Introduction

The European Union is revisiting its sustainability regulatory landscape aiming to alleviate administrative burdens, streamline disclosures, and enhance the cost-effectiveness of compliance. This overhaul, inspired by the recent Draghi Report and a broader drive for competitiveness, puts the Sustainable Finance Disclosure Regulation (SFDR) at the center of a debate in relation with the simplification of rules, notably the Corporate Sustainability Reporting Directive (CSRD): How can rules be made more efficient and less burdensome, while still ensuring the integrity of sustainability information for investors?

## Regulatory reform in context

At the heart of the current discussion is the effort to align financial, industrial, and climate policies. The Draghi Report, commissioned by European Commission President Ursula von der Leyen, emphasizes that excessive regulatory

complexity can stifle innovation and global competitiveness, especially in critical sectors such as clean energy and digital technology. In response, the EU is advancing a simplification agenda, targeting major regulations under the “Omnibus package” that include, among others, the CSRD and the Taxonomy Regulation, to relieve administrative pressure on small and innovative businesses.

## The Omnibus Package: impact for SFDR

The Omnibus package seeks to rationalize and harmonize sustainability-related reporting duties. It includes the simplification of the CSRD by reducing by 80% the companies under its scope and decreasing the indicators and data to be reported. Therefore, the simplification of CSRD impacts the availability of market information needed in the investment decision making (allocation of capital to finance the sustainable projects and the transition) and therefore the proposal of review of the SFDR.

The simplification of rules of the Omnibus Package and SFDR should be aligned. The simplification approach of SFDR should seek coherence with CSRD (and other initiatives such as the EU Taxonomy and Green MiFID) and a balance between reducing the disclosure burden and the need to ensure availability of reliable data. The SFDR review should aim to avoid data gaps and greenwashing risk integrating any amendments to the CSRD, the Taxonomy Regulation, and their implementing rules, reducing the reporting burden through simplification and streamlining of requirements, ensuring consistency and coherence across the EU sustainable finance framework.

Omnibus-driven changes must likewise be carefully calibrated to maintain the actionable value of the data provided.

## Main areas for simplification of the SFDR

Within the SFDR, several areas have been identified for potential simplification:

- The clarification of legal concepts, such as “sustainable investments” to address legal ambiguity and ensure consistent interpretation.
- Product categorization, introducing clear product categories for sustainability-related financial products (like “sustainable” and “transition”) would enhance retail investor understanding and comparability (one of first’s SFDR initial goals) reducing legal uncertainty and greenwashing risks.

- Standardizing and clarifying the list and methodology for principal adverse impact indicators could reduce complexity, improve comparability, and cut reporting costs, especially for smaller market participants.
- Data Overlap and Redundancy: Aligning SFDR reporting requirements with those of the CSRD and Taxonomy Regulation would minimize duplicative disclosures and administrative inefficiencies, enabling firms to focus on material sustainability information.
- Set clear methodologies to ensure consistent and robust approaches when assessing eligibility (avoiding current inconsistencies in methodologies such as evidenced for government bonds)
- User-Friendly Templates: Simplifying pre-contractual and periodic disclosure templates can make information more accessible to retail investors, fostering better market comparability and decision-making.

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## Balancing simplification and data integrity

Policymakers now face the challenge of balancing the drive for simplicity with the need for robust, decision-useful sustainability data. If regulations are pared back too far, there is a risk that crucial information may be lost, diminishing the ability of markets to channel capital toward genuinely sustainable economic activities. On the other hand, failing to streamline could perpetuate high compliance costs and deter smaller players from participating in sustainable finance.

## Conclusion

The ongoing review of the SFDR and related frameworks, influenced by the Draghi Report and the Omnibus package, marks a crucial phase in Europe’s sustainability agenda. The EU should aim to simplify sustainability rules while preserving reliable and useful-decision data for investors. Achieving the right balance between reducing regulatory friction and preserving meaningful transparency is essential to ensure the financing of the transition to a net-zero economy.



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### SFDR reform: Balancing priorities and setting clear meaningful criteria

A consensus appears on how the Sustainable Finance Disclosure Regulation (SFDR) should evolve: Since the application of the SFDR in 2021, the lack of distinction between the two strategies specified in the Regulation has been a major criticism of the current framework. The new categorisation scheme should therefore reconcile the financing of sustainable activities with the support of businesses in their transition.

The creation of at least two product categories, one focusing on activities that are already sustainable, the other one focusing on transition activities, seems fundamental to reduce confusion among retail investors. However, the objective of transparency and simplification can only be achieved if the categories are attached to credible minimum criteria, in line with what investors could expect.

#### Setting ambitions to determine the right categories

Clear minimum criteria, leveraging existing tools such as the Taxonomy and climate benchmarks criteria, are essential to prevent greenwashing. This requires ensuring that the product meets investors' intuitive expectations in terms of positive contribution and

investment exclusion. While this approach will require a dedicated delegated act, the SFDR revision should already lay the groundwork for aligned criteria to ensure a common understanding of the proposed product categories. For example, reflections on minimum criteria will unavoidably lead to discussions on the necessity for an intermediate category following a do-not-harm principle under the rationale that ambitious criteria for a sustainable category will reduce the available offering for clients with sustainability preferences.

We recognize that the creation of a third category focused on not harming (DNH) could reflect the different shades of sustainability and that - with sufficiently stringent criteria - it may play a role to meet investors' values and prevent high concentration of sustainable investments. However, the SFDR experience has shown the limits of sector-agnostic DNH criteria and the development of a credible DNH category would necessarily come with a certain level of complexity. Moreover, it would put major reliance on the product distribution process while advisors tend to oversimplify product categories. Presenting DNH products as 'light green' and explaining to investors that unclassified products may still meet the DNH criteria could lead to unintentional misselling. Creation of a harmful category would allow clients to exclude harmful products and prevent such confusion.

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#### Fostering legal certainty and consistency across the framework

One of the important weaknesses of the SFDR is the flexibility left in the definition of key concepts, such as the notion of sustainable investments, making financial products incomparable between asset managers and leading to legal uncertainty. We should therefore ensure that the criteria are clear and comparable between financial institutions. However, the ongoing omnibus I initiative could strongly compromise this objective. First, the reduction of the scope of the Corporate Sustainability Reporting Directive (CSRD) will necessarily affect the quality of the information used

by asset managers, increasing legal and greenwashing risks. Secondly, the proposition to make the Taxonomy largely voluntary could divert sustainable investments away from activities that can substantially contribute to environmental objectives and increase concentration risk of sustainable funds. Finally, the attempts of the co-legislators to dilute the transition plan requirement under the Corporate Sustainability Due Diligence Directive (CSDDD) have reached a paroxysm, removing most of the substance from the provisions by relying on vague terms such as 'industry practices', 'contribution to limiting global warming' and 'reasonable effort'. This approach goes against the principle of legislative harmonization to reinforce the savings and investments union, but also reduces the possibility to leverage transition plan rules to develop credible criteria for the transition focused product category.

#### Meeting the preferences of retail investors

The revision of the SFDR will only reach its objectives if it is accompanied by adaptations to the consideration of sustainability preferences and consistent changes of the KID disclosures. In that respect, consistent implementation timing is a must to prevent repeating the legal uncertainty experienced in the first application of the rules.

#### The key ingredients for a successful revision

In conclusion, a balance needs to be found between fostering transparency, reducing complexity, meeting client preferences, as well as tailoring the framework for impact investors. Prioritising one of the four objectives will necessarily generate a risk for the four other objectives, which requires adequate mitigation measures.