Central Bank of Ireland SFDR Workshop

November 2024

On 22 October 2024, the Central Bank of Ireland ("**Central Bank**") held a Sustainable Finance Disclosure Regulation ("**SFDR**") workshop with industry representatives as a follow up to the workshop it held in November 2023 to address SFDR implementation issues. This latest workshop addressed outstanding issues since the previous meeting, the implementation of the European Securiteis and Markets Authority ("**ESMA**") Guidelines on Funds' Names using ESG or Sustainability-related terms (the "**Guidelines**") and the outcome of the common supervisory action ("**CSA**") on sustainability.

Following the workshop, Irish Funds shared a note of the meeting with its members, as a precursor to guidance due to be issued by the Central Bank in the coming months. The Central Bank has highlighted that the requirements and expectations set out in the note should be considered by all funds and taken into account in new fund applications going forward.

SFDR Implementation Issues

The table below summarises the key points made by the Central Bank in relation to various SFDR implementation issues discussed at the workshop.

Article 8
 	
Exclusion only funds
	▪ Possible for a fund which implements an exclusion-only strategy to be categorised as an Article 8 fund, subject to it providing appropriate disclosures to investors.
	▪ Exclusions applied to be disclosed in detail as "binding elements" of the investment strategy.
	▪ Disclosures should detail:
	    ▪ the exclusions, with a positive disclosure of the environmental and / or social characteristics which are promoted by the fund as a result of the application of the exclusion strategy;
	    ▪ the thresholds applied (expectation on how these thresholds are disclosed in relation to passive funds is in discussion);
	    ▪ define what is meant by terms such as "involved in"; and
	    ▪ if there are ESG scores that result in exclusions, these ESG scores (and relevant thresholds) should be described.

Article 8 & 9 Funds **Asset allocation for entire portfolio – no exclusion for cash or derivatives**	▪ The entire portfolio must be accounted for when calculating the minimum commitments disclosed in the asset allocation - calculations based on portfolio holdings excluding cash or derivatives, for example, is not permitted. ▪ The Central Bank does not accept disclosures that state, for example, "100% sustainable except cash". ▪ ESMA is not supportive of the use of ranges for the asset allocation.
Article 8 & 9 Funds **Consideration of minimum proportions**	▪ The Central Bank expects the minimum commitment figures disclosed in the pre-contractual annex to be based on normal market circumstances (ie, disclose a positive minimum commitment figure instead of referencing a 0% minimum commitment figure). ▪ Additional disclosures should be included in the fund supplement and the annex outlining the circumstances (ie, rules-based market events) where the fund would have 0% environmental or social aligned investments / have 0% investment in sustainable investments.
Article 8 & 9 Funds **Taxonomy Disclosures** **"What is the sustainable investment objective of this financial product?"**	▪ When a fund is not Taxonomy-aligned but makes sustainable investments, the Central Bank has seen examples of funds not listing Taxonomy Regulation environmental objectives as per the requirements in the Annexes. ▪ Central Bank view is that, where a fund invests in environmental sustainable investments, it should list the relevant Taxonomy Regulation environmental objectives. Industry's concern that this is confusing for investors and not in line with requirement to be "fair, clear and not misleading". ▪ Central Bank agreed it is reasonable to include an explainer that the fund has 0% commitment to Taxonomy-alignment and therefore does not commit to investments contributing to the environmental objectives in Article 9 Taxonomy Regulation. ▪ It was agreed that Irish Funds would draft and share sample wording with the Central Bank to provide it with the rationale for the approaches being taken in response to this question.

Article 8 & 9 Funds
 	
Disclosure of minimum sustainable investment commitment
	▪ Where possible, the minimum proportion set for sustainable investments with environmental and social objectives in the box on first page of SFDR Annex should equal the overall minimum proportion of sustainable investments set out in the asset allocation section.
	▪ Where this is not feasible, the fund may disclose the most representative minimum proportion of sustainable investments with environmental and social objectives on page 1 provided:
	  ▪ the overall minimum proportion of sustainable investments is high in accordance with the Commission's Q&A; and
	  ▪ an explanation is included as to why minimum proportions disclosed on page 1 do not add up to the overall minimum proportion of sustainable investments disclosed in the asset allocation section.

Article 9(3) Funds **Paris-Aligned Benchmark / Climate Transition Benchmark Tracking Funds**	▪ The fund (while benefitting from an exemption from disclosing how the objective is obtained) must disclose the minimum proportion of sustainable investments and be able to classify the minimum proportion of sustainable investments in its portfolio either as having an environmental or social objective. ▪ The Central Bank advised that it will not approve an Article 9(3) fund that discloses no commitment or a low commitment to sustainable investments within the meaning of Article 2(17) of the SFDR, citing the Commission Q&A from July 2021 (stating Article 9 funds are required to invest only in sustainable investments save for hedging / liquidity instruments). ▪ It is up to each individual manager to determine whether or not they can stand over the approach taken to satisfy themselves that the PAB / CTB tracking fund has been appropriately classified under the SFDR. ▪ Article 9(3) funds must substantially invest in sustainable investments. The Central Bank does not intend to impose a threshold for determining what is meant by "substantially invest" for this purpose.

ESMA's Fund Naming Guidelines

Irish Funds outlined at the workshop that the Central Bank's recently announced streamlined filing process relating to changes required to comply with the ESMA Guidelines would only apply to a very small proportion of impacted funds if the fast-track was limited to changes to funds' names only. The Central Bank subsequently updated its process clarification to confirm that the streamlined process would apply to changes to funds' names and minor changes to prospectuses, supplements and SFDR Annexes.

Specific concerns were raised in relation to the timing of exchange traded funds rebalancing, with funds tracking the MSCI being required to rebalance towards the end of May, after the 21 May 2025 compliance deadline. The Central Bank noted that they were mindful of the issues for index tracking funds and that some form of forbearance would be available. Firms should engage with the Central Bank on bilateral basis in this respect.

Outcome of CSA on Sustainability

ESMA is expected to publish its finding from its CSA on sustainability in Q1 2025. The Central Bank will follow up with its own findings in report form rather than in the form of a Dear CEO letter. A number of risk mitigation programmes will address firm specific issues identified and requiring action. Direct engagement with specific firms will take place immediately, rather than waiting for the ESMA findings to be published.

Next Steps

As noted above, firms should refer to the expectations noted at the workshop pending the publication of guidance by the Central Bank next year. There is no fixed timeline for publication. Industry asked that the timeframe for complying with any publication that the Central Bank issues could be aligned with the timeframe for updating documentation to address the revised SFDR Level 2 measures. The Central Bank noted that, where guidance is published, the Central Bank's expectation is that managers implement any changes to the pre-contractual disclosures necessary to comply with the publication the next time the fund documentation is being revised for another reason.

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

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

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