CLIENT BRIEFING

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Draft SFDR 2.0 proposals

New sustainability categories for funds marketed in the European Union

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1 Introduction

The development of the European Commission's proposals to update the EU Sustainable Finance Disclosure Regulation (**SFDR**) may turn out to be one of the worst-kept secrets of recent years. It was widely expected that the Commission would formally publish the proposals (dubbed "SFDR 2.0" by the industry) on 19 November 2025 and indeed, it appears that this may well still be the case.

On 6 November 2025, a leaked draft of the SFDR 2.0 text was published. This proposes replacing the existing Article 6/8/9 framework with a new product category framework. Although the Commission refused to comment on the leak, the advanced state of the text strongly suggests that the proposals are relatively far along in their development, which is consistent with the above anticipated deadline for their formal release. Nonetheless, we understand that as the text is an interservice consultation draft, the Commission may receive further (potentially significant) internal comments before the final draft version is published.

Many of the proposals are consistent with rumours that were circulating long before the leak occurred and for the industry, it looks like SFDR 2.0 (assuming it is adopted in this form) would be relatively positive news. Once the formal proposal is published (expected later in November 2025), the European Commission will send it to the European Council and European Parliament. It will only become legislation if it is agreed by all three. To become functional, it will need to be supported by a revised Regulatory Technical Standard, which has yet to be published. We do not expect these proposals to come into effect until late 2027 or 2028 at the earliest. **There is no guarantee that the (broadly) pragmatic approach of the leaked text will survive into the final legislative amendments.**

In this briefing, we identify the key points arising from the leaked Commission draft and provide our own views on what this might mean for the asset management industry. As the discussion is based on a leaked text that has not yet formally been adopted by the Commission, some of these details may still change between now and the expected publication date.

2 The headlines

- As expected, the Commission is proposing a **new categorisation approach**, which will delete and replace the existing Article 6, Article 8 and Article 9 SFDR product categories.
- The **new product categories are likely to bring greater clarity**, with clearer criteria about when a product falls within a particular category. SFDR 2.0 uses a different set of categories to the UK FCA's Sustainability Disclosure Requirements.
- The Commission will have extensive powers to specify in new delegated acts further details of which underlying investments will be eligible for each category. **Much will therefore depend upon the approach that the Commission adopts in relation to those delegated acts.**
- There will be a clearer set of conditions for products to fall outside the new product categories. In practice, this should make it **easier for fund managers and other product providers to specify that a product does not fall within one of the revised categories**.
- There will be a new ability for **alternative investment funds (AIFs) that are marketed exclusively to professional investors to opt-out of the new product categories**. In practice, this means that the managers (**AIFMs**) of those funds

will be able to include sustainability-related claims in their fund documents or marketing materials without needing to comply with the detailed conditions applicable to the relevant product category. However, they will remain subject to certain other overarching requirements. Clearly, this will not be available to products available to retail investors either under the UCITS regime or through other retail-eligible products (see below).

- **Closed-ended funds that are fully raised and are no longer distributed after the date that the new SFDR 2.0 rules come into force will fall outside the SFDR regime entirely**. However, depending on the contractual commitments that they have made to their investors, they may in practice still need to comply with some requirements derived from SFDR 1.0.
- For **UCITS funds and open-ended AIFs that are not marketed exclusively to professional investors, there does not appear to be any transitional relief** in the draft text. Whether this is an issue is likely to depend upon whether or not those funds can easily update their fund documentation (and, where applicable, name) to meet the updated conditions to fall outside the new product categories. Where this is not practical, they will need to await the details of the Commission's delegated acts to determine if they can meet the criteria for the relevant product category.
- The requirements for **entity-level reporting on principal adverse impacts and on integration of sustainability-related risks into remuneration policies will be deleted**.

We discuss these points in more detail below.

3 New product categorisations

THE NEW PRODUCT CATEGORIES

Under the proposals, the existing categories of Article 6, Article 8 and Article 9 funds will be deleted and replaced with a new product categorisation system. Broadly, this would break down as follows:

Category	Updated SFDR provision	Headline description
Transition	Article 7	Invests in the transition of undertakings, economic activities or other assets towards sustainability, or contributes to such transition.
Integrating sustainability factors	Article 8	Integrates sustainability factors into the investment strategy beyond risk management considerations.
Sustainability-related objective	Article 9	Invests in sustainable undertakings, sustainable economic activities, or other sustainable assets or contributes to sustainability.
Combination	Article 9a	Constituted of two or more underlying products falling within the above three categories.
Impact	Article 7 or Article 9, together with Article 2(26)	A product falling within Article 7 (transition) or Article 9 (sustainability-related objective) above, with an objective of making a pre-defined positive and measurable social or environmental impact, and with investments directed towards undertakings, economic activities, or other assets which provide solutions to address specific social or environmental challenges.
Other	Article 6a	Products that do not fall within any of the above categories.

The "core" product categories will now be contained in Articles 7, 8 and 9 SFDR, and the Commission will be empowered to specify snappier names for each of those categories through a delegated act. The names will be chosen once SFDR 2.0 primary legislation is settled and then after consumer market testing. It is intended that, later, the MiFID sustainability preferences regime should be adapted so that EU financial advisors would be required to ask their clients how they would like to invest their portfolios by reference to these new categories.

The combination category (Article 9a) is effectively a blend of two or more of the core categories and will require an explanation of the composition of the combined product relative to those underlying constituent categories.

The impact category effectively operates as a sub-category of the Article 7 or Article 9 core categories.

NEW QUANTITATIVE THRESHOLDS AND ELIGIBILITY CRITERIA FOR INVESTMENTS FOR NEW CORE PRODUCT CATEGORIES (ARTICLE 7, 8 AND 9 FUNDS)

The revised rules would introduce new minimum investment thresholds for each of the core new product categories. In addition, they specify investments that can be used to meet the minimum thresholds, as well as investments which do not count towards the minimum investment thresholds and excluded investments in which the product is prohibited from investing. These categories are largely based on the December 2024 recommendations of the Platform on Sustainable Finance. SFDR 2.0 uses a different set of categories to the UK FCA's Sustainability Disclosure Requirements.

The following table provides a broad overview of the three new core product categories, with examples of their permitted and excluded investments:

Category	Updated SFDR provision	Required investment threshold	Examples of specified eligible investments	Excluded investments
Transition	Article 7	70% of assets in investments meeting a clear and measurable transition objective **OR** Align with an EU climate transition or an EU Paris-aligned benchmark **OR** At least 15% of investments in Taxonomy-aligned economic activities	• Investments accompanied with a credible sustainability-related engagement strategy, targeting specific changes with defined milestones and integrating escalation actions in case the expected changes do not happen • Investments in undertakings with credible transition plans as regards as least one sustainability factor	• Controversial weapons • Cultivation and production of tobacco • Companies where a benchmark administrator has found a violation of UNGC Principles or OECD Guidelines on Multinational Enterprises
Integrating sustainability factors	Article 8	70% of assets in investments integrating the sustainability factors	• Investments with an ESG rating that outperforms the average rating of the investment universe or reference benchmark • Investments that outperform the average investment universe or reference benchmark on a specific sustainability indicator • Investments that favour undertakings or economic activities with a proven positive track record of processes, performance or outcomes related to sustainability factors	• Controversial weapons • Cultivation or production of tobacco • Companies where a benchmark administrator has found a violation of UNGC Principles or OECD Guidelines on Multinational Enterprises
Sustainability-related objective	Article 9	70% of assets in investments with clear and measurable sustainability-related objectives **OR** Align with an EU Paris-aligned benchmark **OR**	• Portfolios replicating or managed according to EU Paris-aligned benchmarks • Taxonomy-aligned economic activities • Investments in EU issuances and funds backed by the EU budget with environmental, social and governance objectives	• Any company excluded from EU Paris-aligned benchmarks, including those mentioned above plus companies associated to varying degrees with coal, oil, gas or energy-intensive electricity generation

Category	Updated SFDR provision	Required investment threshold	Examples of specified eligible investments	Excluded investments
		At least 15% of investments in Taxonomy-aligned economic activities	• Other investments in sustainable undertakings, economic activities or other assets, provided that a proper justification is included in investor disclosures	• New projects to explore, extract, distribute or refine hard coal, lignite, oil fuels or gaseous fuels • New projects for, or projects that do not have a plan to phase out from, exploration, mining, extraction, distribution, refining or exploitation of hard coal or lignite for power generation

On the face of it, the eligible investments for each of the above categories seem relatively broad. Each category also includes a "catch-all", so that other investments which are not listed but which fit the theme may be included provided that a "proper justification" is included in the disclosure. Many of the sustainability features or initiatives currently frequently agreed between investors and managers find a place in one or more categories. The introduction of the new transition category under Article 7 and its associated permitted investments is also welcome, as fund managers seeking to develop transition finance products have frequently struggled under the existing SFDR regime due to a lack of clarity about how their investments would comply with the existing criteria.

However, for each of the new core categories, the Commission will be empowered to supplement the lists of permitted investments by specifying additional conditions that must be met for the investment to contribute towards the product's objective (and therefore to count towards the required threshold). **There is therefore a risk that, depending on the approach adopted by the Commission, further onerous requirements could be added to the basic eligibility criteria, which would affect whether a fund or other product can meet the necessary conditions in each case.** On the other hand, the Commission is also empowered to introduce a phase-in period for each category to reach the requisite threshold of eligible investments, which is likely to be welcomed. Firms will therefore need to keep a close eye on any consultations or proposals for the development of the relevant Commission delegated acts in due course.

IMPACT FUNDS

As a subset of Article 7 or Article 9 funds, these products will need to meet the Article 7 or Article 9 conditions (as applicable). They will also need to have as their objective the generation of a pre-defined, positive and measurable social or environmental impact, with their investments directed towards undertakings, activities or assets which provide solutions to address specific social or environmental challenges.

There are specific additional disclosure requirements contained within Article 7 and Article 9 for impact funds (for example, the requirement to set and disclose the intended impact(s) in terms of specific environmental or social objectives underpinned by a pre-set impact theory). In addition, financial products that do not comply with the conditions applicable to impact funds are prohibited from using the term "impact" in their name.

FUNDS THAT ARE NOT SUSTAINABILITY-RELATED PRODUCTS (ARTICLE 6a FUNDS)

The draft rules state that products other than those falling with the new Articles 7, 8 or 9 categories can include in their pre-contractual disclosures (for example the Article 23 pre-contractual disclosures made by AIFs) information on whether, and how, the product considers sustainability factors or sustainability risks. However, when doing so, the product provider must meet the following conditions (unless relying on an exemption mentioned below):

- It must not use any **sustainability-related information** in the **name of the fund or in marketing communications**;
- Any sustainability-related information must **not be a "central element" of the pre-contractual disclosures** for the product – a tightly defined concept, including meaning that the sustainability-related information must account for less than 10% of the space taken up in describing the investment strategy;
- Sustainability-related information must **not be included in any Key Investor Information Document (KIID)** prepared for the product; and

- The information must **not constitute a claim about that product that would fall within the new Article 7, 8 or 9** product categories.

This may provide a clearer framework for fund managers who wish to keep their funds outside of the new sustainability-related product categories, particularly if supervisors accept the use of explicit disclaimers to meet the last condition. **However, the prohibition on including any sustainability-related information at all in marketing communications could, in practice, limit the use of this category.**

4 Exemptions and transitional provisions

A critical question for fund managers will be how their existing SFDR 1.0 Article 8 and 9 products will be treated under the revised rules. This will depend on the type of fund and its current status, as follows:

FULLY-RAISED, CLOSED-ENDED FUNDS

- The draft indicates that in relation to existing closed-ended funds which are no longer being distributed on or after the date that the new rules take effect, managers may choose not to apply the new rules. This means that where a fund is fully raised and closed by that date, the manager will **not** need to transition the product to the new framework.
- Firms should note that there is some ambiguity in the draft text here. Read literally, the text appears to say that a fund manager could choose not to apply SFDR in its entirety to such funds, rather than just preserving the existing framework. It is unclear whether this is intended because if so, as a regulatory matter, it would also switch off all existing SFDR 1.0 requirements for those funds, including obligations to make periodic reports and to invest only in companies which exhibit good governance. Whether or not SFDR 1.0 processes and disclosures would need to continue would then be determined by reference to contract. The finalised text of the proposal may clarify this point.

FUNDS MARKETED ONLY TO PROFESSIONAL INVESTORS

- For AIFs (whether open- or closed-ended) which are marketed exclusively to MiFID professional investors (whether per se or elective professionals), the manager can choose not to apply the new product categorisation framework.
- This appears to mean that, for example, the manager could make claims about the integration of sustainability factors into the relevant AIF's investment strategy without needing to meet the new conditions in Article 8 (as amended), and without needing to satisfy the conditions for Article 6a.
- However, it appears that the manager may remain subject to certain other obligations under the revised SFDR, including an overarching obligation to ensure that any sustainability-related claims are clear, fair and not misleading and that they are consistent with the actual sustainability features of the product.
- In addition, the prohibition on using the term "impact" in the name of a fund would still apply to funds which exclusively have professional investors, unless the fund meets the specified impact conditions.
- AIFMs should also note that the MiFID definition of a professional client is also currently under review through initiatives such as the EU Retail Investment Strategy. It will therefore be important to continue to monitor those developments, as this may affect how this exemption will operate in practice.
- AIFMs that may be eligible for this exclusion will nonetheless need to consider the potential attitudes of their target investor base, as certain institutional investors may nonetheless expect their products to fall within a particular category.

OTHER FUNDS

- There will be a range of funds that cannot benefit from either of the above exemptions. This includes, for example, UCITS funds, and open-ended AIFs which are marketed to retail investors. The draft text is unclear on the transitional treatment for these funds.
- Although there is a proposed 12-month transitional provision in the text for certain types of pension products, as drafted it would not appear to apply to AIFs or UCITS funds. The effect seems to be that a UCITS fund, or an AIF which cannot benefit from either of the above exemptions, would need to comply with the revised framework immediately when SFDR 2.0 begins to apply (although it would presumably not apply before the Commission has published the relevant delegated acts which supplement the new Article 7, 8 and 9 product categories).

- Whether this is problematic is likely to depend on several factors. First, the manager would need to consider whether any existing claims in relation to the fund bring it within any of the new Article 7, 8 or 9 categories. If so, it would then need to assess whether it can amend the relevant fund documentation to bring the product within the new Article 6a conditions. If that is not possible, or if it wishes to fall within one of the new product categories immediately, it will need to ascertain whether it can meet the required investment conditions. However, that would require further details on the Commission's approach in its delegated acts. It is currently unclear how much time there would be between the publication of the relevant delegated legislation and its entry into force to allow fund managers in this situation to adjust their underlying investment portfolios to meet the supplementary conditions, where required.

5 Other changes

"SUSTAINABLE INVESTMENTS"

The proposals delete the concept of SFDR 2(17) "sustainable investments" currently relevant to SFDR 1.0 Article 8+ and 9 funds entirely. As a result, the "do no significant harm" principle will be deleted from SFDR and the unloved concept of portfolio companies exhibiting "good governance" no longer features as a standalone concept (but could find its way back). Deletion of this definition may increase focus on Taxonomy-alignment as a measure of environmental sustainability for funds in one of the new categories.

ENTITY AND PRODUCT LEVEL DISCLOSURE REQUIREMENTS

Under the proposals, the requirement for entity-level disclosures in relation to the principal adverse impacts (**PAIs**) of investment decisions on sustainability factors is also being removed.

In addition, firms will also no longer be required to include information in their remuneration policies on how those policies are consistent with the integration of sustainability risks or to disclose such information on their websites.

There will also be no requirement to report Taxonomy eligibility or alignment under the new framework – SFDR 2.0 will directly amend the Taxonomy regulation to delete Articles 5, 6 and 7 which required Article 8 and 9 products to disclose their percentage of Taxonomy alignment, and certain statements confirming that other investments did not take the Taxonomy into account. Nonetheless, this will not entirely remove Taxonomy reporting in practice, as funds could use the Taxonomy as one of the KPIs to demonstrate compliance with the requirements of the new product categories, and some investors may continue to require Taxonomy reporting as a contractual matter.

These changes are likely to be very well-received by industry, given the challenges in monitoring and evidencing PAIs and in obtaining reliable data (which will not be helped by the anticipated dilution of the EU Corporate Sustainability Reporting Directive (**CSRD**), previously expected to be an important source of PAI data).

However, firms will still need to publish information on their websites about how they integrate sustainability risks into their investment decision-making processes, as well as certain required disclosures and periodic reporting about Article 7, 8 or 9 products. Product level website disclosures will still be required for Article 7, 8 and 9 products. Existing practice is likely to continue under which private funds do not make product-specific disclosures on public websites but rather in password-protected sections available only to investors.

PORTFOLIO MANAGERS AND ADVISERS

Portfolio managers and financial advisers will be removed from the scope of SFDR, on the basis that the Commission considers that they do not manufacture or manage the underlying sustainable products in relation to which they provide their services.

DATA METHODOLOGIES

The draft text introduces new rules in relation to the use of data and estimates for the purposes of complying with the new product category rules and related disclosure and reporting requirements.

Broadly, where a firm is using data provided by external data providers for these purposes, it will need to ensure that the relevant arrangements with the data provider are formally documented. Where the firm uses estimates that are not based on data provided by an external data provider, it will need to ensure that it has formal, documented methodologies for determining those estimates.

Upon request, the firm will need to provide clients with information about the sources of data it uses and the methodologies it applies.

6 Implementation timeline

The leaked draft text does not set out a definitive timeline for the SFDR 2.0 changes to come into force and, even if it did, the Commission is not entirely in control of the timetable.

In the legislative assessment accompanying the draft, the Commission indicates that implementation could occur with a "*start-up period from 2027 to 2028*", although it is unclear exactly what this means in practice. Before it can take effect, the proposal would need to clear the EU's legislative process, which would involve negotiations between the European Parliament and the Council, and the Commission would need to adopt the detailed delegated acts underpinning many of the new provisions.

On that basis, late 2027 or early 2028 seems like the earliest feasible target date, but much will depend upon how controversial these proposals prove to be with the European co-legislators, as well as the Commission's capacity to draft detailed provisions at a time when its resources are already stretched.

Managers will want to keep an eye on the implementation timeline as it becomes clearer, as there may be potential complexities for fundraises that straddle the entry into force of the revised regime.

7 Travers Smith's view on the proposals

On the face of it, many of the proposals in the draft SFDR 2.0 text look positive and reflect a pragmatism from the Commission consistent with its competitiveness and simplification agenda. There is a refreshing candour in the recitals to the text, where the Commission openly acknowledges that SFDR implementation has been very challenging for the industry and notes that, in its view, this has resulted in the information provided to investors typically being insufficiently clear to allow them to understand the sustainable investments on offer.

As anticipated (particularly in light of the recommendations from the Platform on Sustainable Finance in December 2024), the new product categorisation framework has moved closer to a formal, although self-certifying, labelling regime. Once the detailed delegated acts are substantially advanced or passed, clearer criteria to qualify for the new product categories could remove a significant chunk of the uncertainty currently faced by product providers over the eligibility for the existing classifications and should facilitate better comparability between products for investors.

The opt-out for AIFs that are marketed solely to professional clients is pragmatic and welcome, recognising that the focus of the regime should be the protection of retail investors. The grandfathering arrangements for existing closed-ended funds that are no longer being distributed will also be a huge relief for the asset management industry, which was concerned about the prospect of a messy and complicated transition between the current classification framework and the new product categories. However, since some financial products could be forever committed to their SFDR 1.0 obligations as a matter of contract, it is possible that some legacy SFDR 1.0 concepts will remain current in the market, for example in discussions between insurers and the asset managers they appoint.

There is, of course, more that could be done to improve the SFDR framework. For example, while clearer rules for transition finance and impact products in the revised framework are welcome, there is still a lack of detail about how investments can qualify for the social sustainability objective, and no realistic prospect of a social Taxonomy being developed to fill the gap. Similarly, the data challenges that exist today may continue to persist to some extent, particularly while negotiations on CSRD rumble on.

Nevertheless, the biggest risk relates to the Commission's approach to the future delegated acts under SFDR 2.0. Under the draft text as it stands, the categories of eligible underlying investments within each of the new product categories seem relatively widely defined and are well-aligned with existing investor demand. If this pragmatic approach to investment eligibility prevails, then we anticipate that many fund managers will want to bring their products – including their institutional-only products – within one of the newly defined product categories.

Conversely, if the Commission chooses to apply a technical overlay in its delegated acts that significantly restricts investment eligibility or introduces excessive complexity, the new product categories are likely to become unappealing or tainted with uncertainty. In that scenario, fund managers may look to use the professional-only opt-out or revert to trying to ensure that their products fall within the new Article 6a regime.

If there's one thing that both the Commission and the industry will surely want to avoid, it's a repetition of the mistakes of SFDR 1.0.

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