



SFDR 2

Paving the way for a credible and coherent EU financial market

The Sustainable Finance Disclosure Regulation (SFDR) adopted in 2019 triggered a vast movement of self-labelling by asset managers. Intended as a classification that would put some order in the European Union sustainable funds market, SFDR's articles 8 and 9 quickly became a source of confusion. Indeed, the lack of clear criteria for the categories defined in the regulation gave too much leeway to asset managers to decide how to classify each of their funds. Category assignments were then regularly modified by asset managers depending on internal assessments of compliance risk, without clear justifications. These opaque changes created a major lack of clarity for those who wanted to use the SFDR categorization to make investment decisions¹.

Both the sheer complexity of the SFDR framework and its lack of clear minimum safeguards meant there was little added value for retail investors. On the contrary, article 8 and 9 classifications could even lead them to presume funds meet basic green credentials when this is not the case, leading to several scandals over the past years. Banking advisors are also struggling with the vagueness of the regulation and have limited knowledge of the exact meaning of article 8 and 9 and on the content of related products², thus potentially amplifying confusion.

It is in this context that the European Commission publishes its proposal to review the SFDR³. **The review provides a unique opportunity to address existing gaps and loopholes through a robust SFDR 2. Such a text is essential to combat greenwashing in the financial market, but also to make European finance more attractive.** Indeed, driven away by anti-climate initiatives in the U.S, asset owners are increasingly seeking asset managers and funds aligned with their

¹ According to Morningstar, article 8 and 9 funds represented [42.4% of the funds marketed in the EU](#), with total assets of EUR 4.05 trillion, by the end of 2021. However, the landscape of article 8 and 9 funds continued to evolve rapidly, with many funds being reclassified. In the last quarter of 2022 close to [420 funds were reclassified](#), with 307 downgraded to Article 8 from Article 9.

² The limited ability for counselor to advise clients on sustainability preferences, despite Mifid II obligations, and for clients themselves to understand the information provided is evidenced by the results of [the mystery visits](#) conducted by the French Market Authority.

³ The European Commission [released its proposal to review the SFDR](#) on November 20th 2025.

priorities and values⁴. At the same time, individual investors continue to massively seek sustainable investment options, with younger generations making it an essential priority⁵. This note provides recommendations to ensure the SFDR review fulfills these objectives.

I/ Excluding fossil fuel developers from all categories: the foundation of SFDR 2 credibility

Considering abundant scientific data⁶, the European Commission proposes excluding companies that develop new fossil fuel projects from the “sustainable” and “transition” categories. It complements it with Paris Aligned Benchmark (PAB) exclusions—based on fossil fuel revenue thresholds⁷—for the “sustainable” category. However, the Commission does not impose this exclusion on the “ESG” category, where only coal companies would be excluded⁸.

⁴ For example, some institutional investors are already taking strong measures. In December 2025, the second-largest Dutch pension fund, PFZW, [withdrew a €14 billion mandate from BlackRock](#), citing sustainability concerns. The British pension fund The People's Pension and the Danish pension fund Akademiker Pension [withdrew mandates from State Street](#) because of its poor ESG practices. Similarly, the [New York City Controller is recommending](#) three of the city's pension funds drop their \$42 billion management contract with Blackrock. Additionally, others are raising their voices, like the Asset Owner Statement on Climate Stewardship coalition which is [calling on managers to strengthen their climate-related shareholder engagement](#) with companies.

⁵ A [Morgan Stanley Institute survey](#) polled 1,765 individual investors with more than \$100,000 in investable assets in North America, Europe and Asia Pacific revealing that 88% are interested in sustainable investing. This climbs to an astounding 99% for Gen Z and 97% for Millennials.

⁶ As the [IPCC notes](#), [scientific studies](#) show that the consumption of currently exploited coal, oil and gas reserves would result in emissions exceeding the remaining carbon budget for limiting global warming to 1.5°C and even 2°C. In fact, a significant proportion of these reserves should not be extracted and a rapid and significant reduction in fossil fuel production is needed, as identified by the United Nations [Production Gap Report 2025](#). These findings mean that [no new fossil fuel production should be developed](#). The immediate end to fossil fuel development is thus [a common characteristic of credible 1.5°C scenarios](#), including those developed by the IPCC and the [International Energy Agency](#) (IEA), as acknowledged in [an analysis from the French Institute for Sustainable Finance](#) (IFD) composed of major financial institutions. Additionally, and in spite of [IEA calls](#) to shift their business model, it should be noted that oil and gas companies [are still focused on expanding fossil fuel production and only very marginally investing in “low carbon” alternatives](#).

⁷ The Paris Aligned Benchmark includes the following fossil fuel exclusions:

- Companies that derive 1 % or more of their revenues from exploration, mining, extraction, distribution or refining of hard coal and lignite;
- Companies that derive 10 % or more of their revenues from the exploration, extraction, distribution or refining of oil fuels;
- Companies that derive 50 % or more of their revenues from the exploration, extraction, manufacturing or distribution of gaseous fuels;
- Companies that derive 50 % or more of their revenues from electricity generation with a GHG intensity of more than 100 g CO₂ e/kWh.

⁸ Companies deriving more than 1% of their revenue from exploration, mining, extraction, distribution or refining of hard coal and lignite would be excluded from the “ESG” category.

The exclusion of fossil fuel developers is essential to the credibility and relevance of the SFDR 2 framework. It is:

1. **A necessary step to prevent greenwashing and restore retail investor confidence in “ESG” and “green” funds:** Recent research and investigations have repeatedly revealed that funds marketed as “green”, “sustainable”, or “ESG” contained assets from companies developing new fossil fuel projects⁹. Yet, as surveys show, savers and citizens consider that funds claiming to be “responsible” or “green” should not include these companies¹⁰. This led to many retail investors feeling misled and contributed to their low confidence in the sustainable finance market¹¹.
2. **A measure that addresses the shortcomings of the ESMA fund naming guidelines:** In August 2024, the ESMA published guidelines regulating the use of sustainability terms in fund names.¹² These new rules introduced fossil fuels exclusions for the use of “sustainable” linked terms but not for others including those related to “transition” or “ESG”. Recent studies show that hundreds of funds, whose original names would have required the exclusion of investments in fossil fuels under the new rules, were renamed by their providers following the adoption of the guidelines¹³. Providers removed regulated terms like “sustainable”, “ESG”, or “climate” and replaced them with unregulated ones like “selected” or “engaged.” Furthermore, an in-depth analysis of 26 European funds that added the term “transition” to their names revealed they contained 149 companies from the fossil fuel sector¹⁴.
3. **A catalyst for a clearer, a more effective and understandable SFDR:** The exclusion of fossil fuel developers is easy to apply, notably by relying on already widely used and freely available tools like the Global Coal Exit List (GCEL) and Global Oil and Gas Exit List (GOGEL)¹⁵.

⁹ For example, the investigation [covered in The Guardian in May 2025](#) revealed that European “green” funds held more than \$33bn of investments in major oil and gas companies.

¹⁰ [A survey](#) published by the European consumer organization BEUC in October 2025 to inform the SFDR review shows that 62% of consumers would exclude fossil fuel developers. A [previous survey](#) carried out in France during the review of the SRI label reached similar results.

¹¹ [A survey](#) by the French Sustainable Investment Forum (FIR) indicates that green promises are largely perceived as marketing.

¹² For an analysis of the ESMA fund naming guidelines, see [the article published by Reclaim Finance](#) in January 2025.

¹³ [A study conducted by Urgewald](#) revealed that 674 funds, whose original names would have required the exclusion of investments in fossil fuels under the new rules, were renamed by their providers following the adoption of the ESMA guidelines. 391 funds removed regulated terms—such as “sustainable,” “ESG,” “climate,” or “responsible”—from their names. Another 283 replaced them with non-regulated terms such as “selected,” “selection,” or “committed.” Specific examples are provided in [an article from Reclaim Finance](#).

¹⁴ This data originates from research conducted by Reclaim Finance that has not been published at this stage. Holdings data has been extracted for this research on 19.08.2025. Fossil fuel companies were defined as: 1) any coal company as listed in Urgewald’s 2024 GCEL list, 2) upstream & midstream oil & gas companies that are still exploring or developing new resources and/or planning to increase their LNG export capacity according to Urgewald’s 2024 GOGEL list.

¹⁵ On the use of GCEL and GOGEL, see WWF and Urgewald’s [briefing](#).

Furthermore, this exclusion is particularly important since the “Do No Significant Harm” (DNSH) principle is no longer in the Commission’s proposal. DNSH was central to SFDR 1 and ensured its compatibility with other EU rules but proved complex to implement and often failed to provide meaningful guarantees. Therefore, its removal could simplify the framework if the major greenwashing risks it creates are mitigated by sufficient minimum exclusions. Because fossil fuel development is incompatible with international and European climate goals and detrimental to many other sustainability objectives, such exclusions must include companies responsible for new fossil fuel projects. If companies stop developing fossil fuels, thus no longer directly impairing the transition and showing they could be responsible, they could immediately be reintegrated into funds from the “transition” and “ESG” categories.

Providing the above elements, **the exclusion of companies developing fossil fuels from the “sustainable” and “transition” categories—as proposed by the European Commission—should be supported and extended to the “ESG” category.** This recommendation is backed by over 120 signatories of a letter to the Commission¹⁶ and would play a key role in SFDR credibility.

II/ Defining “transition”: a need for clarity

When defining the “transition” category, the Commission allows fund managers to use several criteria to meet the 70% threshold of assets linked to a “clear and measurable” transition objective.¹⁷

These criteria make sense on paper. However, their vagueness leaves the door open to a vast diversity of practices that have drastically different environmental and climate impacts. For example, transition plans, engagement strategies, and decarbonization targets vary widely. They could as easily be tied to practices with a materially positive impact as they could be tied to empty commitments and policies (e.g. GHG reduction targets that only cover a very limited share of companies’ emission¹⁸; “transition” plans not aligned with the 1.5°C or even 2°C goal and that do

¹⁶ The letter called “There is no room for fossil fuel developers in any sustainable finance categories” was signed by CSOs, financial experts, financial institutions and corporate leaders and republished on [Reclaim Finance’s website](#).

¹⁷ These criteria are: the replication of CTB or PAB; investing in “transition” activities from the EU taxonomy or in eligible activities scheduled to become aligned; investing in companies that have a “credible” transition plan; the coverage of investment with a “credible” engagement strategy; the investment in companies with decarbonization targets; and others, when specific justifications and under specific conditions.

¹⁸ Companies can opt for targets that only cover a limited share of their activities and/or emissions. For example, oil and gas companies have often disclosed targets on scope 1 and 2 but not on scope 3, which is related to the emission of the fossil fuels they sell and constitute most of their emissions. This was notably the case of the targets pledged by 50 companies during COP28 as part of the [Oil and Gas Decarbonization Charter](#). In the sector, scope 3 targets can also be limited to certain geographical zones and not applying to all their operations (in 2021, TotalEnergies [adopted such a target](#) for European operations only). Similarly, banks often adopt targets that only cover lending activities

not include any action plan to reach targets and shift the business model¹⁹; engagement strategies with no effective escalation strategy²⁰; sustainability-linked bonds tied to insufficient or misleading key performance indicators²¹, etc.). If these criteria are to be used, much clearer definitions are needed to avoid “transition washing”.

It should be noted that many investors are already assessing the “transition stage” of companies through internal methodologies. They usually rely on a basket of indicators sourced from data providers, with good practices incorporating elements on historical emissions (scope 1-3), decarbonization targets (short, medium and long term) and investment allocation (in sustainable and polluting activities). **SFDR 2 should build on these practices by basing the assessment of the “transition” dimension on a basket of criteria that at least includes these three basic dimensions that are emissions, targets and investments.**

Additionally, the Commission proposal introduces a derogation from the 70% threshold in the “transition” category if the fund can justify at least 15% of EU taxonomy alignment. As it stands, this derogation appears inconsistent with the objective to support the EU “transition”. Indeed, taxonomy alignment alone is insufficient to justify such claims, and the EU economy was already estimated to be taxonomy-aligned by 12.9% in 2023²². Consequently, it should be removed from SFDR 2 or the related taxonomy alignment threshold should be higher²³. Similarly, the taxonomy alignment threshold used for the same derogation in the “sustainable” category should be significantly higher to reflect a material contribution to sustainability.

III/ Additional considerations: strengthening SFDR 2 consistency

With article 9a, the Commission proposal regulates claims from funds that combine funds classified under SFDR. In paragraph 2, it introduces the possibility for “non-categorised” products to claim that they invest in two or more categorized financial products while satisfying only limited

and not capital market activities. Furthermore, methodological issues can also mean that targets are not related to changes in “real world” emission, as [shown by Reclaim Finance](#) for the banking sector.

¹⁹ “Credible” transition plans require several essential elements, including decarbonization targets, an action plan to reach them, and clear elements on financial planning. Research – including [the one conducted by Reclaim Finance for the banking sector](#) – has shown that most current plans do not feature these elements and remain partial and flawed.

²⁰ For recommendations on what engagement policies should cover, see Reclaim Finance’s [Climate Stewardship guide](#). Acknowledging the limitations of engagement policies, asset owners have been setting increasingly precise expectations and objectives to asset managers, as the policy from the [New York City Comptroller](#) exemplifies.

²¹ See for example the case of the sustainability-linked bond (SLB) [emitted by Enbridge in 2021](#).

²² See [Sustainalytics’ research](#) on taxonomy alignment published in October 2024.

²³ The threshold could also increase progressively to reflect progress in the transition.

disclosure obligations. Concretely, this means that non-categorised financial products could make claims related to SFDR categories despite not meeting their requirements, including exclusions. To avoid this workaround, **SFDR 2 should require any fund making claims based on underlying funds' SFDR categorization to apply the exclusions of related categories on all its assets. An exception could be made for the units in unit-linked life insurance products that belong to SFDR categories, but claims should not extend to the level of the products themselves.**

The Commission proposal also proposes to drastically reduce the number of “Principle Adverse Impacts” (PAIs) at fund level and to suppress them at entity level. “Non-categorized” funds would not publish any PAI; and Member States would not be authorized to implement additional transparency requirements on sustainability-related financial products. This could have significant negative consequences, beyond the reduction in transparency:

4. The maximum harmonization clause that bans Member States from requiring additional transparency could directly conflict with preexisting and well-established requirements, and notably the French Article 29²⁴.
5. The absence of PAI disclosure for non-categorized funds indirectly penalizes categorized funds. If such funds can still disclose elements on the integration of sustainability factors – as per Article 6a – they would not provide the information necessary to compare them. Providing the very limited remaining number of PAIs, it could not be credibly argued that disclosure would be burdensome.

SFDR 2 should not prevent Member States from opting for more ambitious transparency rules – especially on the indicators at entity level, where SFDR would no longer contribute – and should apply remaining PAIs to all funds commercialized in the EU, categorized under SFDR or not.

²⁴ In France, the [Climate Transparency Hub](#) (CTH) – a platform operated by ADEME in partnership with the Sustainable Finance Observatory – centralizes the “article 29” reporting from financial institutions on their sustainability practices (climate and biodiversity strategies, exposure to the taxonomy and fossil fuels..). This notably includes entity level disclosures that have been used by market participants and stakeholders for several years. Financial institutions have been reporting on article 29 since 2022.