European Commission
DG FISMA
Rue de Spa 2
1000 Brussels
Belgium

30 January 2025

Re: Proposal of the Platform on Sustainable Finance on the Categorisation of Products under the SFDR

Dear Ms Bussières,

Invest Europe notes the publication of the Platform on Sustainable Finance's (the "Platform") Proposal regarding the categorisation of products under the SFDR on 17 December 2024 (the "Report"). We would like to take this opportunity to reiterate our appreciation for the Platform's continued dedication to developing proposals for refining the European sustainable finance framework ("SFDR 2.0") and our support for both the Platform and the Commission's work.

This letter follows on from the detailed conversations that Invest Europe held with the Platform in summer 2024. Having reviewed the Report, we would like to raise certain comments relating to the Platform's proposals. These comments and concerns reflect the collective views of our members and are set out in more detail in Annex 1. The ongoing implementation and future revision of the SFDR framework remains a priority issue for the private equity, venture capital and infrastructure (PE/VC) fund industry.

We have organised our comments by reference to each of the Platform's proposed categories in sections A-E and have made cross-cutting comments applicable more generally in section F.

For context, Annex 2 to this letter contains Invest Europe's original proposed approach to SFDR 2.0 which was initially submitted as part of our response to the European Commission's Targeted Consultation on SFDR 2.0 in December 2023.

As always, we would be delighted to meet with you, and/or any other relevant colleagues, to discuss any of the points raised in this letter if that would be helpful.

Yours sincerely,

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ANNEX 1

A. "Sustainable" Category

The Platform's proposed "Sustainable" category is intended to apply to those products that invest in assets, activities or economic actors that are already sustainable. While Invest Europe's membership is generally supportive of the introduction of this category, we would like to make a number of observations.

Amended definition of "sustainable investment"

Invest Europe supports the Platform's intention to revisit the definition of "sustainable investment" as the current definition has given rise to a number of difficulties. However, the Report's proposed changes to the definition of "sustainable investment" raise some **practical questions**.

- *Investment vs economic activity:* Currently, in accordance with Q&A from the Commission, it is open to FMPs to apply the "sustainable investment" test at either the investment level or the underlying economic activity level. The Platform has proposed that the amended "sustainable investment" definition may only be measured at the level of an underlying economic activity. This appears not to allow an FMP to qualify an investment as sustainable by reference to a company's operations (its manner of conducting business, such as its employment practices), as opposed to a company's underlying economic activity and, when qualifying a company's activity as Taxonomy-aligned, it appears to require the FMP to determine the precise proportion of the company's activity which is Taxonomy-aligned. **We do not agree with this approach** as we believe that it unduly curtails FMPs' existing flexibility and will likely introduce unnecessary complexity into FMPs' methodologies. Certain sustainable objectives (such as improved working conditions) can only be achieved by reference to a company's operations – its manner of conducting business. Also, there may be a lack of available data at the underlying economic activity level to measure the concept of "sustainable investment", particularly in the context of private investments and investments made outside the EU. Instead, **we believe the existing flexibility to measure the concept of "sustainable investment" on a pass/fail basis at the investment level should remain**. If the Commission is minded to introduce measurement at the underlying economic activity level, then we believe that a sensible compromise would be to introduce thresholds by reference to which the definition could be applied at the investment level (for example, an investment would be considered "sustainable" if 50% of its underlying economic activities could be categorised as such).

- *Clarity on social "sustainability":* The Platform's proposals indicate that positive contribution to a social objective should be identified by reference to an "eventual" social Taxonomy and that positive social contribution can be measured and defined by FMPs but do not provide details on how this can be achieved. Unfortunately, there doesn't seem to be a clear timeline towards developing the Social Taxonomy and so in the interim, we **call for greater clarity** to be provided to FMPs on how to determine social "sustainable investments" under SFDR 2.0.

- *Determining environmental "contribution" by reference to the EU Taxonomy*: The Platform has indicated that where economic activities are Taxonomy-eligible, environmental contribution should be determined solely by reference to the relevant EU Taxonomy technical screening criteria. Whilst we understand the Platform's policy objective to

promote use of the EU Taxonomy, we should point out that removing the existing flexibility for private funds to qualify a Taxonomy-eligible investment as a sustainable investment will make it in practice extremely difficult for any private fund to use the Sustainable label, as private funds to date have found the Taxonomy's technical screening criteria in practice too restrictive for investment in many types of environmentally sustainable projects, particularly those outside the EU. We urge the Commission to be mindful of the fact that private funds often invest globally in investments which are not, themselves, subject to EU disclosure requirements or in non-equity investments where FMPs have a limited ability to influence the gathering of investment level data. Furthermore, the underlying technical screening criteria for certain economic activities cross-refer to specific EU standards which simply do not apply outside the EU context (e.g., the substantial contribution to climate mitigation criteria for the economic activity of constructing new buildings refers to national measures implementing Directive EU 2010/31). By defining "contribution" so narrowly, such investments would, assuming their underlying economic activities are Taxonomy-eligible, never be able to positively "contribute" under the Platform's proposals due to data gaps.

The same concern arises in relation to use of the Transition category, as and when the Taxonomy is extended to cover transition investments. The likely outcome of being required to determine environmental contribution solely by reference to the Taxonomy screening criteria, where an activity is in scope of the Taxonomy, is that few private funds will be able to use either the Sustainable or Transition categories.

Where an underlying economic activity is not Taxonomy-eligible, the Platform has indicated that the concept of sustainable investment should be measured in a manner "*analogous to the EU Taxonomy*" (e.g., by reference to science-based targets) and that existing market practices to measuring the concept (e.g., by reference to "ESG ratings") will not be sufficient under the Platform's proposals. **We do not agree with this approach** and believe that it is **unduly restrictive**. As the Commission is aware, the EU Taxonomy currently only covers a limited subset of economic activities and therefore the vast majority of economic activities underlying private assets that are targeted by PE/VC funds are not covered. Managers will therefore have to invest significant time and resources into developing new and bespoke measurement systems "analogous" to the EU Taxonomy to determine whether underlying economic activities are in fact "sustainable".

Furthermore, while a science-based decarbonisation plan may be one way to measure contribution to the EU Taxonomy objectives of climate change mitigation or adaptation, it is unclear how such a plan could be an appropriate or relevant tool to measure positive contribution to other non-climate related EU Taxonomy objectives (e.g., the protection and restoration of biodiversity and ecosystems or the sustainable use and protection of water and marine resources). Far from introducing uniformity in market practice, we believe that the Platform's proposals will likely lead to **even greater divergence in market practice** and increased cost/complexity for managers of relevant financial products.

- *PAIs and DNSH:* Finally, the Platform's proposals indicate that for a product to qualify for the "Sustainable" category, subject to a narrow carve out for hedging and liquidity instruments, all of a product's investments that are not Taxonomy-aligned must pass the DNSH test using pre-defined PAI thresholds which would need to be "*sector, asset class, region specific and science based*". In the Platform's view, thresholds should be used to exclude the worst performing investments (unless a positive outlook combined with a credible escalation and/or escalation mechanism is in place). We urge the Commission to

be mindful of the practical difficulties that managers of private funds would face in setting and disclosing such pre-defined thresholds prior to a closed-ended fund's launch. This is because private funds typically invest on a blind pool basis and so cannot concretely commit to thresholds prior to or during the fundraising process, ahead of the fund's life because managers of such funds typically do not know which investment opportunities will arise during the fund's capital deployment, or even the sectors in which such opportunities will arise.

B. "Transition" Category

Invest Europe welcomes the Platform's proposal to introduce a dedicated category for financial products investing in the change towards a more sustainable economy/supporting the transition to net-zero. We wish to confirm our understanding that the Transition category covers investments that contribute to the transition through, for instance, renewable energy or technology that develops or enables climate solutions, as well as investments that improve their own environmental performance. At present, the Platform's proposals list a small number of criteria by reference to which a product may qualify for the "Transition" category (e.g., investments in portfolios tracking the EU Climate Benchmarks or investing in investments with a credible transition plan or science-based targets in place). It is unclear whether the Platform intends this list to be exhaustive or not. We note that the Platform's proposals suggest that an FMP must identify "*relevant criteria through **any or a combination of***" the criteria. This could be read as suggesting that only those financial products pursuing the specific types of strategies listed by the Platform could qualify for the "Transition" category. **We urge the Commission to ensure that flexibility is preserved for managers in general but specifically in the context of transition-related strategies** as these strategies need to be able to respond to the latest market and scientific developments. Should the "Transition" category only be available to those financial products pursuing one of the listed strategies this could stifle the development of more innovative transition strategies.

C. "ESG Collection" Category

As with the "Transition" category above, the Platform's proposals in relation to the "ESG Collection" category list a small number of ESG features (e.g., targeting vehicles that are sustainable, transition or ESG collection). Again, the Platform's proposals suggest that a product may qualify for this category through "*effectively either **one criterion or a combination of any** of the following*". It is unclear whether the list of criteria is intended to be exhaustive or comprehensive. If this is intended, we consider this to be too limiting and **reiterate the need for flexibility to permit managers of financial products to develop innovative solutions**. We also note that one of the criteria listed by the Platform as relevant to the "ESG Collection" category is an "effective reduction in the investment universe". We urge the Commission to reconsider this criterion as, in our experience, it is often difficult for managers of private funds, due to the specificity of the investment policy, a lack of data and the nature of blind pool investing, to evidence that an "effective reduction" in the investment universe has occurred.

We also urge the Commission to clarify that it is open to an FMP to conclude that an exclusion screen is sufficient to qualify a financial product for the "ESG Collection" category. Should this fail to be clarified, and an exclusion screen automatically qualify a financial product for the "ESG Collection" category, the elective nature of the "Unclassified" category would, in our view, be undermined.

Finally, we urge the Commission to reconsider the name of the "ESG Collection" category in the light of the fact that the current name is overly broad and may be difficult for investors (and

particularly retail investors) to understand and the fact that many FMPs raise funds with global investor constituencies in mind. Some of these investors have different ESG-related priorities, tolerances and sensitivities and would likely raise questions as to the inclusion of the term "ESG" in the category.

D. "Unclassified" Financial Products

The Platform has proposed the establishment of a residual "Unclassified" category for those financial products that: (a) do not have sustainability features, (b) have some sustainability features but do not fulfil the minimum criteria to fit within one of the three dedicated product categories, or (c) have not been categorised "*e.g., by the choice of the FMP including where requested by the product's investor*". The Platform's proposals give rise to several concerns for our members.

Single vs multiple investor products

Should the Commission adopt the Platform's proposals, we believe that it will be important for the Commission to make it abundantly clear that **the "Unclassified" category can be accessed at the simple election of the FMP (i.e., by choice)**, at least where the financial product targets professional or semi-professional investors[1]. As currently drafted, the Report indicates that it would be open to an FMP to categorise a product as "Unclassified" *in response to* a request by an investor (singular). Invest Europe is **fully supportive of the elective nature of the "Unclassified" category**, however, as currently drafted, the Report could be read as restricting the scope of the "Unclassified" category to single-investor vehicles only (e.g., SMAs). We see no policy reason why the "Unclassified" category ought to be restricted in this manner and do not believe that this can have been the Platform's intention. If the "Unclassified" category were to be restricted in such a fashion, this would curtail the ability of managers of pooled financial products (e.g., most AIFs) to tailor their financial products to their investor base.

Marketing literature

The Platform has recommended that "Unclassified" products ought to be prohibited from including any description of their ESG characteristics or sustainable/transition features in their marketing material. The Platform's rationale for this is to ensure that investors can "clearly distinguish" between "Unclassified" and categorised products.

While this rationale may be relevant to financial products directed at retail investors, we believe it is **wholly inapplicable to financial products targeting professional investors** and constitutes an unnecessary restriction on marketing materials. We urge the Commission to be mindful of the **longstanding distinction in European financial services rules that calibrates regulatory requirements and obligations to the requirements and needs of underlying investors**. Professional investors often conduct detailed pre-investment due diligence and engage in bilateral conversations with private fund managers to discuss the features of a particular financial product. Invest Europe believes that the use of a prominent disclaimer stating that a financial product is unclassified and doesn't fulfil the standards for a categorised product under SFDR 2.0 together with

[1] Invest Europe considers that the considerations outlined in this letter in respect of professional investors apply equally to semi-professional investors. As such, references in this letter to "professional investors" should be read as including semi-professional investors. Such investors are sophisticated and for the reasons outlined in this paper, Invest Europe believes that a distinction should be made between financial products that are marketed to retail investors and those that are restricted to more sophisticated professional and semi-professional investors.

the general requirement that the content of marketing material ought to be fair, clear and not misleading and Article 13 SFDR (which requires managers to ensure that the content of any marketing communications does not contradict information disclosed pursuant to the SFDR) ought to suffice to ensure that professional investors are protected. Additionally, we note that ESMA's Guidelines on Funds' Names already require funds using certain ESG, impact, transition or sustainability-related terms in their names to comply with minimum portfolio composition requirements and, in certain circumstances, minimum exclusions. In our view, **this feature of FMP choice should prevail even if certain ESG characteristics or features are described, or even promoted, in a financial product's marketing materials**, at least where a product targets professional investors.

Minimum reporting requirements

The Platform has indicated that its view is that "Unclassified" products should be subject to certain minimum reporting obligations (e.g., EU Taxonomy alignment and certain PAI indicators). Respectfully, **we do not agree**. Whilst we see the merit in the imposition of uniform minimum reporting obligations for all financial products from an investor comparability and transparency perspective, in Invest Europe's view, this should be **balanced against the needs of private fund managers** that strive to be able to offer a single financial product to competing global investor constituencies (many of whom have different ESG-related priorities and sensitivities and different tolerances for the costs associated with reporting).

Requiring "Unclassified" products to report against certain minimum requirements will necessarily impose a **significant operational cost and time burden** on managers to obtain underlying ESG-related data (e.g., in relation to GHG emissions). It is unlikely that ESG-sensitive investors globally will be willing to pay for such data. Financial products incurring such costs or subject to such minimum EU law derived regulatory obligations may face litigation or other challenges from certain anti-ESG campaigners or public officials. The consequence is likely that PE/VC managers offering "Unclassified" products will either be forced to avoid offering such products in the EU (which would narrow investor choice) and hamper the EU's international competitiveness or set up dedicated EU parallel vehicles at a higher cost to EU investors.

Notwithstanding the above, if the Commission believes that mandatory reporting should be required for "Unclassified" products, we urge the Commission to **make a distinction between those financial products which are marketed to retail investors** (as that term is defined for the purposes of AIFMD, by reference to MiFID) **and those that are restricted to professional investors**. The Platform has clearly indicated that its proposals put "*retail investors and their needs at its core*", and so we believe that limiting the scope of the minimum reporting requirements to financial products which are marketed to such investors is both **appropriate and proportionate** and in line with the Platform's policy objectives.

Additionally, we note that some professional investors maintain bespoke reporting frameworks and require financial products they invest in, by way of bilateral agreement, to report against such bespoke frameworks. Imposing minimum reporting requirements designed with the needs of retail investors in mind, on products these investors invest in is unlikely to align to their requirements.

As regards professional investor-only financial products, such investors are sophisticated and tend to allocate capital to financial products based on a holistic analysis of a financial product's features and not, for example, based on a financial product's reported GHG emissions, EU Taxonomy alignment or name. Therefore, we do not believe that comparability will be enhanced by mandating minimum reporting for such products.

E. "Impact" Category

Invest Europe welcomes the Platform's focus on "impact" investing. We believe that impact investing plays a vital role in advancing the EU's sustainable finance agenda and **support the Platform's recommendation that the Commission look to develop a "*common understanding*" of impact investing which builds on existing market practices**.

Given the diversity of investment strategies pursued by managers looking to generate an "impact", we are not, at present, supportive of the creation of a standalone category for "impact" funds. We acknowledge the Platform's concerns in Annex G that investors may feel "*uncertainty*" as to where "impact" investing fits within the current SFDR framework. We believe that this should be alleviated by the Commission **positively clarifying its view of how "impact" funds may fit within the future categorisation regime**.

Finally, we note that "impact" investing is, by its very nature, dynamic and varied and managers must be able to retain the flexibility to respond to investor demand to develop innovative strategies. A categorisation system, such as the one currently proposed by the Platform, which is based upon rigid positive contribution, portfolio composition, minimum exclusion and binding elements-related criteria is likely to be ill-suited to "impact" investing. Instead, we would urge the Commission to have regard to existing "impact" related labelling regimes (e.g., the FCA's "Sustainability Impact" label) which instead seek to set binding minimum requirements but leave it to individual managers to explain how these are met in practice (e.g., a requirement that to use the "Sustainability Impact" label, under the FCA's SDR regime, a fund must set an objective to achieve a pre-defined positive and measurable social or environmental impact – but the regime does not seek to define what that "impact" is, leaving managers to do so).

F. General

Grandfathering

Invest Europe welcomes the Platform's recommendation that the Commission "*evaluate the need for grandfathering and/or transition rules*" and reiterates its view that the **introduction of clear grandfathering provisions is essential for the PE/VC industry**.

As set out in Invest Europe's response to the Commission's 2023 Targeted Consultation, our view is that there ought to be an **optional exemption** from the requirements of SFDR 2.0 **for all closed-ended financial products** (whether currently Article 6, 8 or 9) **which are either: (a) fully closed to new EU investors or (b) established and in the process of concluding their fundraising period as at the date of SFDR 2.0's application – provided that such financial products continue to disclose to investors in line with the requirements of SFDR 1.0**. We believe that this is essential for such products as they were designed, marketed and sold on the basis of the requirements of SFDR 1.0. The application of SFDR 2.0 to such financial products would be contrary to the principle of non-retroactivity. Further, if a product is fully closed to the admission of new investors, any rationale relating to investor protection does not exist.

In addition to points of principle, the absence of appropriate grandfathering for such products would have a number of deleterious impacts. For example, investors in closed-ended funds invest based on contractual terms, including in relation to sustainability reporting, contained in a fund's pre-contractual documentation when committing to the fund and generally cannot later redeem

their investments in the fund if the fund terms change. Therefore, without grandfathering, changes caused by SFDR 2.0 affecting sustainability-related reporting terms would change the deal that investors agreed to without their consent and with no option for them to exit the fund if they feel that they would not have agreed to the new terms (as they could in an open-ended context), thereby effectively binding them in a deal they did not agree to (absent formal consent to amend the terms).

Secondly, we do not believe that transitional provisions of e.g., a year, would suffice to address these concerns. Such transitional provisions will impose a significant and potentially unworkable burden on managers who would, at the very least, have to engage legal counsel to ascertain the impact of SFDR 2.0 on their financial products and extensively re-paper documentation. We urge the Commission to be mindful of the fact that investors and sponsors have invested significant time and resources into building procedures and disclosure materials to comply with the requirements of SFDR 1.0, which cannot be changed in a short period of time (e.g., a year). In view of this, it would be a considerable challenge to impose the requirements of SFDR 2.0 on financial products launched under the SFDR 1.0 regime. This is, of course, separate to the conceptual question of how closed-ended private financial products would even be able to re-constitute their portfolios to be compliant with the updated requirements of SFDR 2.0 within a transitional period without opening themselves to allegations of mis-selling by investors who previously subscribed to the financial product on the basis of its stated investment policy at the time of SFDR 1.0.

Blind pool and commitments

As set out in more detail in Annex 2, private PE/VC funds investing in illiquid asset classes are typically blind pool. As a result, any portfolio composition rules, thresholds or minimum standards, should, in our view, be measured only after a disclosed "ramp-up" period has ended. We are **supportive of the fact that the Platform has recommended taking account of "ramp-up" and "wind-down" periods when applying any minimum criteria, binding elements and indicators** and urge the Commission to ensure that this flexibility is baked into the proposals for the minimum criteria for each of the future categories.

CTB exclusions

We note that the Platform has recommended the introduction of minimum exclusions which "build upon" the CTB exclusions for both the "Transition" and "ESG Collection" categories. While the precise detail of the Platform's proposals is yet to be confirmed, we note that **the CTB exclusions** (contained in Article 12(1)(a)-(c) of CDR (EU) 2020/1818) **pose certain operational complexities for private fund managers**. Article 12(1)(c) which excludes companies that are found by benchmark administrators to be in "violation" of the United Nations Global Compact principles, or the Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises is particularly problematic. At present, benchmark administrators do not routinely publish this information on their websites so data availability is partial at best and so fund managers may find it difficult (if not impossible) to obtain the necessary information to comply with this exclusion. Should the Commission agree with the Platform's suggestions and introduce the CTB exclusions as part of the minimum criteria relevant to certain product categories, we would be **grateful if the Commission could clarify its expectations in such cases and provide a safe harbour for fund managers who have used reasonable efforts to obtain data on relevant violations**.

Do not undermine

Under the Platform's proposals, for a product to qualify for any of the categories, investments which do not count towards the minimum percentage allocation threshold "*must not undermine*" the financial product's "sustainability objective", transition objective or ESG characteristics/ features of the product (as relevant). This concept of "not undermining" is, to our knowledge, a new concept that is not found in SFDR 1.0 or the current EU Taxonomy. In our view, it is **unhelpfully vague,** and should either be removed in favour of the better-understood SFDR "DNSH" test or be the subject of further, careful and detailed consultation and then clarified early on in the legislative process, so as to avoid the drawn out and iterative interpretative challenges which arose under SFDR 1.0 in relation to similar concepts.

ANNEX 2

Invest Europe approach to SFDR II

In the context of the European Commission consultation on the SFDR review

13 December 2023

Invest Europe welcomes the opportunity to participate in the European Commission targeted consultation on the implementation of the Sustainable Finance Disclosure Regulation (SFDR). The ongoing implementation and application of the SFDR and the interplay with the EU Taxonomy Regulation remain a key operational issue for both private fund managers and investors and hence, a main priority for Invest Europe as an association.

This note accompanies the formal Invest Europe consultation response. More concretely, it:

1. provides background information on the specific business model and nature of the private equity, venture capital and infrastructure (PE/VC) industry;

2. sets out Invest Europe's views on a possible future SFDR II regime; and

3. summarises the main priorities and key concerns of the pan-European PE/VC industry in light of the forthcoming SFDR review.

Invest Europe is the association representing Europe's private equity, venture capital and infrastructure sectors, as well as their investors. Our members take a long-term approach to investing in privately held companies, from start-ups to established firms. They inject not only capital but dynamism, innovation, and expertise. This commitment helps deliver strong and sustainable growth, resulting in healthy returns for Europe's leading pension funds and insurers, to the benefit of the millions of European citizens who depend on them.

1. Background – Why PE/VC funds are different

Despite often subject to the same or similar rules, PE/VC funds do not share the same characteristics and purpose, nor do they bear the same risks as UCITS and hedge funds. In contrast to these funds, PE/VC funds:

- make direct and active investments into unlisted businesses (as opposed to directly or indirectly managing listed securities, often based on a reading of indexes rather than an active selection process);

- are set up as long-term, illiquid, closed-ended and unleveraged structures, which cannot be regularly traded and whose assets are not easily tradable; and
- are vehicles of choice to institutional investors looking for long-term returns and are generally not marketed to retail clients.

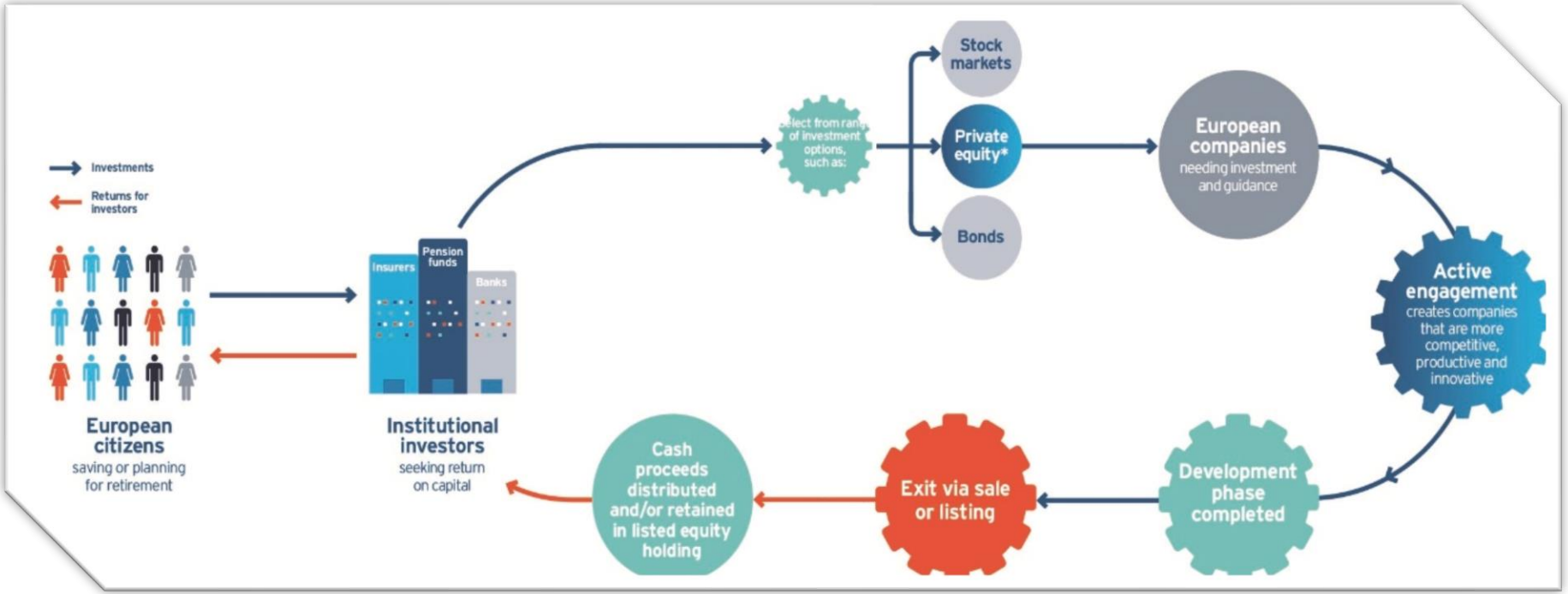
The PE/VC industry is composed of managers:

(a) investing into businesses with a potential to grow;

(b) through long-term, closed-ended equity funds;

(c) with the capital of institutional and sophisticated investors.

Each of these three aspects is explained in more detail below.


Investments
Returns for investors
European citizens
saving or planning for retirement
Insurers
Pension funds
Banks
Institutional investors
seeking return on capital
Select from range of investment options, such as:
Stock markets
Private equity*
Bonds
European companies
needing investment and guidance
Active engagement
creates companies that are more competitive, productive and innovative
Development phase completed
Exit via sale or listing
Cash proceeds distributed and/or retained in listed equity holding

(a) From start-ups to turnarounds: In which companies does private equity invest?

- Private equity managers will commit capital to a wide range of companies in all sectors of the economy and all stages of development, from the smallest start-ups to the largest conglomerates, from promising scale-ups to businesses in distress.

- There are several types of private equity investments (venture, growth, infrastructure, turnaround, etc.), with limited distinctions between these from an operating perspective. They will all invest patiently (for five years on average) in the businesses and actively use their ownership positions to ensure those businesses become successful. In other words, private equity managers do not only choose the companies in which they invest after a long due diligence process, they also take minority or majority equity ownership and are actively involved in their running for several years.

- Private equity managers offer operational guidance and assistance to the businesses they own until the very last moment of the investment period. As the success of the company in which they have invested will make the success of the fund, managers need to spend a significant amount of time with these businesses.

(b) Illiquid and closed-ended: How are private equity funds set up?

- Enabling invested companies to have sufficient time to grow and develop requires funds to be structured in a certain way. This has shaped how managers are marketing to their investors. This distinguishes private equity as an asset class.

- While there is no definition of private equity funds in EU law, the proxy that has been used in various EU laws ("closed-ended and unleveraged funds") is a good indication of the industry's particularity. Private equity funds indeed have the following characteristics:

    - They are long-term and closed-ended: Funds are typically set up for a 10-year period, extendable by two years.

    - They are illiquid: All capital is committed at the beginning of the fund and cannot be redeemed. Indeed, investors will subscribe to a private equity fund at the beginning of its life – during a time-limited subscription period – and will not be in a position to redeem their investment for the entire life of the fund.

    - They are unleveraged: Funds are typically not authorised to borrow more than the capital committed.

    - They are international: Managers very often operate cross-border. Private equity funds by nature almost always operate on a cross-border basis: investments are usually made globally; teams are very often located in different countries; and investors will also be dispersed across Europe and the wider world.

(c) Investors of a third kind: Who commits capital to private equity?

- Committing capital to a private equity fund requires careful consideration and a strong liquidity profile from investors in the asset class. Typically, private equity is an institutional asset class reserved for knowledgeable investors able to commit larger sums of capital.
- The typical composition of a private equity fund investor base will be:
    - 70% of institutional investors: pension funds, insurers, banks, sovereign wealth funds, funds of funds; and
    - 30% of other experienced investors: family offices, entrepreneurs.
- The vast majority of direct investors into private equity funds are therefore sophisticated, professional clients with an expertise of the market who invest large sums of capital after having negotiated their entry in the fund with the manager.

In summary, the private equity model is built on a three-step process:

1) Commitments received from investors are pooled into a fund;
2) The capital collected will over the years be invested in the portfolio companies; and
3) Once an investment in a portfolio company is divested, the capital is returned to the investor, along with the overall profits that have been made.

2. Future SFDR II regime

Set out below is Invest Europe's stance on what a future SFDR II regime could look like, building on the existing framework and considering current market practices, expectations and needs. As explained above, the management of private capital funds differs fundamentally from that of liquid asset funds for a number of reasons and these idiosyncrasies are not reflected in the current version of SFDR. There are a wide range of investment strategies, geographic focuses, and sizes of fund present across Invest Europe's membership and hence a variety of views on the path to ensuring any future regime has sufficient proportionality and flexibility to work effectively for investors in the full spectrum of private capital funds. The below represents a compromise position and is an attempt to reflect the breadth of views and investment approaches across Invest Europe's membership.

As a starting point, we believe it is essential that any new SFDR II regime includes a "disclaimer" category. There are many reasons for this, such as:

a) the need for private fund managers to offer a single financial product to competing investor constituencies globally with different ESG priorities and for which a formal classification under the SFDR may be problematic in other jurisdictions;

b) the need for managers to reconcile competing labelling frameworks where such labels may not be reconcilable (e.g., the UK's SDR framework, the SEC's proposals and the SFDR); and/or

c) for complex fund structures involving aggregator/master/feeder or similar vehicles, a desire to avoid unnecessary work classifying multiple fund vehicles.

For more information on the proposal below, please see our answer to Question 4.1.1 in the comprehensive response to the targeted consultation.

Category	**Disclaimer rule**	**Disclosure rule**	**"New SFDR II Article 8"**	**"New SFDR II Article 8+"**	**"New SFDR II Article 9"**
Qualification	Funds that may (or may not) mention ESG and provide reports on ESG to their investors but include a prominent warning on all fund and marketing documents that *"EU law does not regulate any ESG commitments this product might make (if any) beyond requiring all claims to be clear, fair and not misleading and EU SFDR disclosure*	Bespoke E, S or G claims are made about the fund, which do not contain a commitment or "binding element" in the investment strategy (distinction from "New SFDR Article 8"). But there is a commitment to disclose in accordance with certain templates (to be determined by the SFDR) and report on an ongoing basis (by using	In respect of all or a specified minimum proportion of investments, the manager must commit to "binding elements" with an ex-ante and/or ex-post effect on the fund's investments, either by: (a) selecting or excluding investments in order to meet a	Must commit to making more than 0% Article 2(17) "sustainable investments" or Taxonomy-aligned investments and up to 70% "sustainable investments" and/or Taxonomy-aligned investments (distinction from "New SFDR II Article 9").	Must commit to making more than 70% SFDR Article 2(17) "sustainable investments" and/or Taxonomy-aligned investments. The definition of "sustainable investment" in SFDR Article 2(17) should be amended as in the previous column.

Category	Disclaimer rule	Disclosure rule	"New SFDR II Article 8"	"New SFDR II Article 8+"	"New SFDR II Article 9"
	obligations are not applicable to this fund." This category is only available to funds marketed directly to professional investors.	such templates) about underlying investments' performance with respect to sustainability criteria (outlined in the pre-contractual disclosure). This category is only accessed intentionally by self-declaration and can e.g., be used for approaches focussing on ESG data collection, non-binding targets or engagement targeting but without committing to a specific binding engagement result.	clear characteristic or investment objective (thereby narrowing the fund's investment universe); and/or (b) pursuing a meaningful stewardship strategy to achieve outcomes after an investment has been made. A product in this category could (but need not) align to the PRI's definitions for responsible investment approaches. An exclusion screen may qualify under (a) if sufficiently ambitious,	The definition of "sustainable investment" in SFDR Article 2(17) should be amended: (a) to include investments which are not sustainable on day one but have a credible path to becoming so within a reasonable period (to be defined based on ESG topic, geographical and sector-specific criteria) and on the basis of specific measures supported by an underlying budget	

Category	Disclaimer rule	Disclosure rule	"New SFDR II Article 8"	"New SFDR II Article 8+"	"New SFDR II Article 9"
			by reference to rules to be set.	(thus including transition and impact investments); and (b) to add an express materiality qualifier to the DNSH test.	
All fund documents and communications must be clear, fair and not misleading. An "anti-greenwashing rule".	Yes	Yes	Yes	Yes	Yes
Pre-contractual and periodic disclosure templates must be provided to investors (only, not public).	No	Yes	Yes	Yes	Yes

Category	Disclaimer rule	Disclosure rule	"New SFDR II Article 8"	"New SFDR II Article 8+"	"New SFDR II Article 9"
We intend to make suggestions to improve the templates where targeted at professional investors.					
Good governance assessment required	No	No	Yes However, the requirement should not apply on day one but to give sufficient time to have these in place within the investee companies. It should be possible to take a proportionate approach taking into account the geography, size, nature and sector of the investee business.	Yes, with regard to the proportion of investments which are not either (a) SFDR "sustainable investments" or (b) Taxonomy-aligned investments (for these investments, "good governance" is already covered by alignment with international standards/minimum safeguards). However, the requirement should not apply on day one but to	Yes, with regard to the proportion of investments which are not either (a) SFDR "sustainable investments" or (b) Taxonomy-aligned investments (for these investments, "good governance" is already covered by alignment with international standards/minimum safeguards).

Category	Disclaimer rule	Disclosure rule	"New SFDR II Article 8"	"New SFDR II Article 8+"	"New SFDR II Article 9"
				give sufficient time to have these in place within the investee companies. Note the comments in the prior column re: proportionality.	However, the requirement should not apply on day one but to give sufficient time to have these in place within the investee companies. Note the comments in the "New SFDR II Article 8" column re: proportionality.
Consider PAIs at product level	No	No	No	Yes[1]	Yes[2]
Other requirements	None	None	Some detailed requirements	Some detailed requirements	Some detailed requirements

[2] Note that we suggest that entity-level PAI disclosures ought to be phased out. If entity-level PAI disclosures are not phased out, we suggest that the link between entity and product-level PAI disclosures ought to be removed – this would prevent a manager being required to report PAIs at entity level across all of its funds merely due to having a single "New SFDR II Article 8+" or "New SFDR II Article 9" product.

3. Key priorities

Recognising the characteristics of the PE/VC industry and its specific business model (see Section 1 above), Invest Europe believes it is crucial to consider and address the following issues and concerns during the forthcoming SFDR review – in addition to the need for a "disclaimer" category outlined above.

Each of these points is also covered in Invest Europe's full response to the targeted consultation. References to where equivalent wording can be found in that response are included below.

PE/VC/Infrastructure-specific concerns

1. Grandfathering: Private funds are typically closed-ended and long-term (albeit of finite duration). It will be essential to introduce clear grandfathering provisions from SFDR I, which last for the life of a product, which could be 12 years or more. These provisions would work by providing an optional exemption from SFDR II requirements for all closed-ended funds (whether Article 6, 8 or 9) which were fully closed to new EU investors or established and in the process of concluding their time-limited fundraising period as at the date of SFDR II's application provided that such funds continue disclosing to investors in line with SFDR I requirements – this is the basis on which these products were marketed and sold. The reason this is essential relates to the inherent features of closed-ended private capital funds which makes them different to open-ended products investing in liquid assets:

    a. Private capital fund terms can typically be formally amended with consent from investors. The level of consent required typically depends on the type of change to the terms, and it is often contractually possible for the fund manager to amend terms unilaterally where the necessary change is clear and is required to comply with changes in law or regulation. However, rule changes being contemplated under SFDR II seem likely to require active decisions, e.g. on whether to opt-in to a label etc., that go beyond simple "change of law" amendment powers granted to the manager in the fund contract. Therefore, we think it likely that investor consent procedures would need to be executed for closed-ended funds to adapt to any SFDR II requirements. At best this would be expensive for investors (not least because it would require sophisticated legal advice), and at worst in the case of divided opinions amongst a fund's investors it could lead to failure to gain clear consent and potential conflicts between contracts, regulation and investors' wishes;

    b. Given that closed closed-ended funds pose limited risk of greenwashing because they (a) are professional products subject to extensive due diligence by and monitoring from sophisticated investors and (b) cannot admit new investors anyway (except as replacements for individual investors that wish to sell their interests), we consider that these negative impacts on (private capital fund) investors would be heavily

disproportionate and should be avoided in the interests of well-functioning capital markets and the EU's competitiveness in the eyes of global institutional investors; and

c. Investors and firms agree certain contractual terms, including in relation to sustainability reporting, when committing to the fund and cannot later redeem their investments in the fund if the fund terms change. Therefore, without grandfathering, changes to regulation affecting reporting terms would change the deal that investors agreed without their consent and with no option for them to exit the fund if they feel that they would not have agreed to the new terms (as they could in an open-ended context), thereby "trapping" them in a deal they did not agree to (absent formal consent to amend the terms).

Open-ended products (which are less common in private capital) should be subject to an 18-month transition period starting on the date of SFDR II's application permitting them to either change the strategy to keep the classification or to scale down. On an ongoing basis it should be clarified that only funds that are marketed to investors in the EU will be subject to SFDR (and not funds which are only managed but not marketed). *For more information, please see our narrative explanation in respect of Questions 1.5, 1.6 and 1.7, and our answer to Question 4.1.9.*

2. Website disclosures: We believe that the existing product-level website disclosure requirements are largely duplicative of the pre-contractual product disclosure requirements and therefore ought to be abolished. Should the European Commission disagree, we suggest that the requirements be refined for private funds. Firstly, the requirement to translate the "Summary" section of the website disclosure into one of the official languages of each host EU member state where a financial product is made available is of limited value to professional investors who are used to reviewing disclosures in English. We consider that this requirement should be dropped. Secondly, private funds are restricted by other global laws from making their offering documents public. To the extent that product-level disclosures are retained, public website disclosure obligations under SFDR II should be confined to retail funds or those which are publicly offered. Private funds should have the option to make product-level disclosures available to investors – through website access which is password protected or by any other suitable means having similar effects (e.g., in a data room). *For more information, please see our answer to Question 3.2.5.*

3. Firm-level PAI reporting: Private fund managers manage funds with diverse strategies. The firm-level PAI regime should be abolished because the aggregated data at manager level is meaningless, and costly to obtain. Aggregate reporting is of no benefit to investors, data is simply not available for certain strategies and managers are required to estimate, which is misleading. If the firm-level PAI regime should nevertheless be maintained, it should be clarified that the firm-level PAI regime is detached from product-level PAI consideration, meaning that managers are permitted to consider PAI for certain products even if they do not consider PAI at firm level. *For more information, please see our answer to Question 3.1.1 (narrative response in respect of Article 4).*

4. Blind pool and commitments: Private funds investing in illiquid assets are typically blind pool. Any portfolio composition rules, thresholds, or numerical commitments or minimum standards, should be measured only after a disclosed "ramp-up" period has ended. We note that in the context of UCITS funds, Article 57(1) of Directive 2009/65/EC disapplies the UCITS portfolio composition spread requirements for a period of six months from initial authorisation. The same principle should apply to private funds, for which it would be most logical to measure any thresholds or numerical commitments and comply with minimum standards once the fund is fully invested, i.e. after a suitable ramp-up period – provided this ramp-up period is transparently disclosed and noting that the "ramp-up" period in private capital funds (typically known as the "investment period") typically lasts around five years until the fund is effectively fully invested – this is the point at which any portfolio construction threshold requirement should be measured in order to be meaningful. The regime should also allow sufficient flexibility for compliance to be layered in over time, especially to encourage adoption amongst existing strategies (such as "evergreen" private capital products, that may be listed on an exchange) which are already focussed and making ESG-related progress. Such requirements should equally not apply during the divestment period which for illiquid assets can extend to several years. We suggest the same flexibility is provided for open-ended funds, with ramp-up and divestment periods adequate to the nature of the assets held in the fund. The basis of measurement for this purpose should generally be NAV. However, certain private funds, often those investing in infrastructure, generally set their minimum commitments with reference to alternative non-NAV related measures (e.g., total capital deployed at cost over the lifetime of the fund). We suggest that SFDR II should introduce flexibility for such funds to set commitments with reference to alternative measures provided they are transparently and clearly disclosed to investors. *For more information, please see our answers to Question 3.2.7 and Question 4.1.11(a).*

5. Targets v commitments and investment restrictions: We understand that regulators expect to treat commitments made in relation to achievement of certain ESG-related outcomes (e.g., the proportion of SFDR Article 2(17) "sustainable investments" or Taxonomy-aligned investments) as investment restrictions with a dedicated methodology to track and remedy any breaches. However, private funds investing in illiquid assets on a blind pool basis typically cannot concretely commit to minimum binding commitments prior to or during fundraising because, at the start of the fund's life, managers of such funds cannot guarantee what investment opportunities will arise during the fund's investment period (which typically lasts around five years). While we agree that target commitments made to investors should be tracked and their achievement reported periodically to investors, not achieving such commitments in a private fund investing in illiquid assets on a blind pool basis should not result in any breach of investment restrictions unless the manager has failed to take all reasonable steps to ensure the attainment of the target commitment. More importantly, even if at the point of making the investment the requirements of a sustainable investment are met, they may no longer be met over the holding period without the manager being at fault (for example, where a minority venture capital fund holds a portfolio company whose management team decides to change the company's strategy in a way that makes it fall out of the definition). Moreover, mere passive breaches of target commitments caused by fluctuations in NAV should equally not be treated as breaches, given the illiquidity of the fund's assets which makes short-term rebalancing through acquisitions or disposals not feasible. Neither situation ought to result in a requirement to allocate the fund to another product category (i.e., to "downgrade" the fund). Grace periods for the remediation of breaches ought to be granted, which flex dependent on the size, geography, sector and nature of the relevant investment business. We would suggest that

a minimum of two years would be advisable considering the generally longer holding periods of private funds. *For more information, please see our answer to Question 4.1.11(a).*

6. Data gaps: Private funds often invest in global portfolio companies with no connection to the EU, and/or in small companies and/or in securities other than equities. These companies are unlikely to be subject to CSRD or any EU-mandated corporate disclosure framework. Private funds will often hold a minority of an unlisted portfolio company's share capital (this is especially but not only true amongst venture capital and growth funds) which means the fund manager will not have control of the portfolio company and therefore will have limited influence over the amount and type of sustainability reporting data it can obtain from the company. This lack of influence over underlying companies, when combined with the absence of investor or public sustainability reporting requirements for smaller companies, is a critical reason why many private capital fund managers are in a different position to fund managers managing products that invest in liquid securities. It means that private capital fund managers investing in early-stage companies often cannot obtain the same amount of sustainability information from investee companies as is available to managers of products investing in listed companies (or large private companies subject to CSRD or other sustainability reporting rules). In this context, data gaps (in relation to investor reporting, Taxonomy alignment data, PAI data, etc.) should be recognised as appropriate on the same proportionality grounds that underpin the policy decision to exclude smaller companies from corporate reporting frameworks (both in the EU and elsewhere). For venture capital funds (and for other fund products where data gaps are particularly prevalent due to lack of influence that could compensate for the absence of investee reporting requirements, such as growth equity funds, private capital funds of funds and private credit funds), we do not believe that fund managers should be forced to close these gaps using estimates in all instances. This is because, for many private capital asset classes, as well as a general lack of data, there is also, unsurprisingly, a consequent lack of credible estimates. Instead, we believe that managers of these kinds of products should be allowed the flexibility to either explain data gaps or to use estimates where appropriate. *For more information, please see our narrative explanation in respect of Questions 1.12 to 1.12.5.*

7. Good governance: Private funds may invest in special purpose vehicles, or other bespoke corporate structures, and/or in new or developing companies and/or globally. Where a "good governance" obligation applies, it should be proportionate and flexible (designed to screen out bad governance) and not based on assumptions about listed company governance standards in developed markets. It should also be possible for the good governance requirement to be satisfied by implementing changes following the acquisition to ensure good governance, rather than it being a pre-requisite at the time of the initial investment. Private equity is well placed to make a real difference by improving portfolio companies, including addressing governance issues that existed prior to the acquisition. It seems contrary to the policy objectives behind SFDR for the regime to prevent a private equity investor from fixing bad governance by prohibiting their investment in the respective portfolio company. *For more information, please see our answer to Question 4.1.12(a).*

8. Product-level PAI reporting: Where the PAI regime applies at product level, it should be capable of being satisfied by taking post-investment steps to mitigate adverse impacts (as clarified by the European Commission in its April 2023 Q&A). *For more information, please see our answer to Question 3.2.2(b).*

Other

9. ESRS: At product level, the existing PAIs should be conformed to ESRS, meaning that instead of having a pre-defined set of mandatory PAI indicators which may not be material to the pursued investment strategy of the fund, managers should be in a position to define (based on a reasonable materiality assessment) which PAI indicators are material to the fund's strategy. *For more information, please see our narrative explanation in respect of Question 1.8.*

10. Fund names: Any restrictions on fund names should be confined to funds marketed directly by the manager to retail investors. *For more information, please see our narrative explanation in respect of Question 4.4.2.*

11. "Sustainable investment" definition: The current definition of "sustainable investment" set out in Article 2(17) SFDR should be broadened to include investments which are not sustainable on day one but have a credible path to becoming so within a reasonable period (to be defined based on ESG topic, geographical and sector-specific criteria) and on the basis of specific measures supported by an underlying budget. This would result in transition and impact investments being able to qualify as SFDR "sustainable investments". Private capital funds are well placed to make a real difference by improving the sustainability profile of portfolio companies, including ensuring contribution to an environmental or social objective, and not significantly harming any of those objectives. And we believe that this is aligned with the current approach under the EU Taxonomy which recognises that "transition activities" are capable of qualifying as environmentally sustainable economic activities as well as with the intention of the EU Taxonomy "safe harbour" set out in the European Commission's Q&As issued in June 2023 and the ESAs' recently published Final Report confirming that investments whose underlying economic activities are Taxonomy-aligned qualify as "sustainable investments". *For more information, please see our narrative explanation in respect of Question 4.1.15.*

12. "Promoting environmental and social characteristics": In our proposal set out above, we distinguish between the Disclaimer and Disclosure rule on the basis of intentionality rather than on the basis of the concept of "promoted characteristics". Should the European Commission adopt a different approach and retain the existing framework, we believe that it would be helpful to clarify the boundary between SFDR Article 6 and Article 8. In particular, we believe that there is a need to clarify the concept of "promotion" to confirm that it refers to *how* the financial product is presented and "characteristics" in this context refers to features of a financial product, for example binding investment restrictions regarding investment in a particular activity or not investing in a particular activity. Furthermore, we believe that the concept of "sustainability indicators used to measure the attainment of each of the environmental or social characteristics" should continue to be broadly understood and managers should have the freedom to define such indicators as they see fit. For example, a "sustainability indicator" could be confirmation that 100% of the portfolio aligned to the relevant investment restrictions as set out appropriately in a financial product's pre-contractual and periodic disclosures. *For more information, please see our answer to Question 4.1.13.*

13. Application of the RTS: On 4 December 2023, the ESAs published their Final Report on draft Regulatory Technical Standards on the review of PAI and financial product disclosures in the SFDR Delegated Regulation. Given the imminent review of SFDR Level 1, it is of utmost importance to delay implementing the RTS. Doing so would alleviate the substantial resource allocation needed by financial market participants for compliance. This is particularly critical considering that they would be required to comply with the new RTS requirements proposed by the ESAs for a limited period of time before those requirements are likely further changed by the results of this ongoing review - which in addition hugely increases legal uncertainty. In particular, if the proposals set out in the ESAs' Final Report come into effect without a suitable delay, they will require financial market participants to make a host of changes such as:

    a. For those products which consider PAIs, firms will be required to change their existing data collection and reporting systems to account for both (a) the methodological changes introduced for a number of the existing PAI indicators and (b) to reflect the addition of new social PAI indicators;

    b. The proposed changes to the pre-contractual and periodic disclosure templates and to the website disclosure rules are significant and will require fund managers to revise their disclosure documentation and procedures, both for existing and for new funds. Given the lack of appropriate grandfathering provisions, closed-ended products in their fundraise period and open-ended funds will be required to "re-paper" their documents to comply with the revised pre-contractual disclosure templates and the new website disclosure rules set out in the draft RTS annexed to the Final Report. As noted above, in relation to 1, this could trigger investor consent and other regulatory procedures (such as a requirement for UCITS funds to update their Prospectus disclosures and seek regulatory approval for doing so); and

    c. For those products setting "GHG emissions reduction" targets, comply with a host of new disclosure requirements and build new processes to gather the data required to make those disclosures.

In the light of the above and the imminent review of SFDR Level 1, we believe that implementation of the RTS ought to be delayed as it risks imposing a significant burden on financial market participants at a time when the entire SFDR regime is itself subject to review. *For more information, please see our narrative explanation in respect of Question 1.7.*