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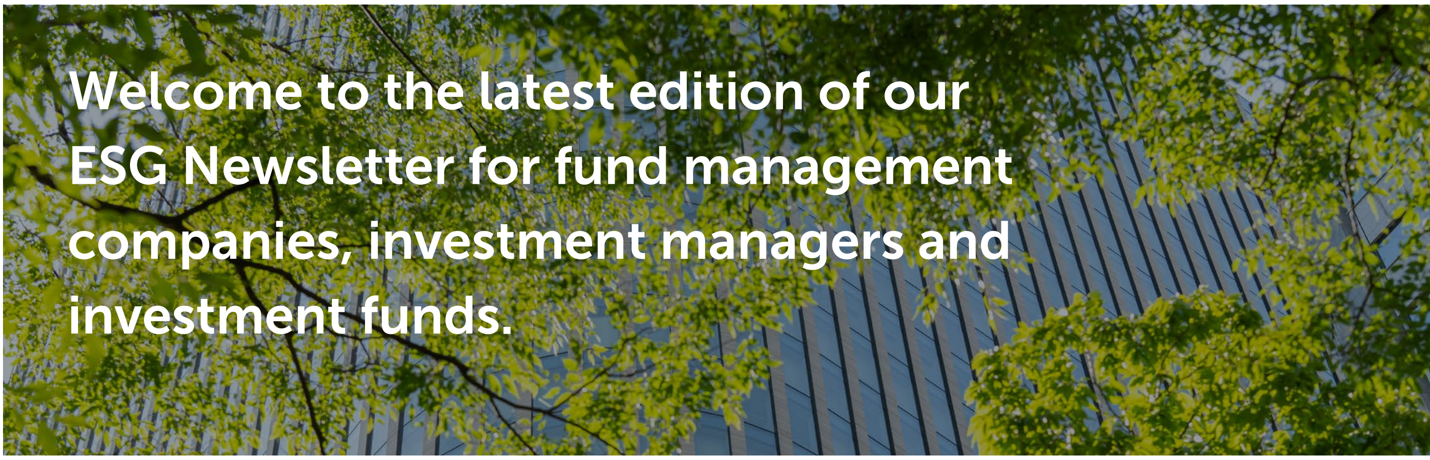
Asset Management & Investment Funds ESG Newsletter

October 2024 – January 2025



Welcome to the latest edition of our ESG Newsletter for fund management companies, investment managers and investment funds.

Table of contents

Section	Page
1. SFDR Related Developments	5
1.1 Platform Report on Transition Plans	5
1.2 Platform Report on Categorisation of products under SFDR	5
1.3 ESMA Q&A on the application of ESMA's Fund Names Guidelines	7
1.4 Central Bank Streamlined Filing Process for UCITS and AIFs complying with ESMA's Fund Names Guidelines	7
(a) Issue 10	7
(b) Issue 9	7
1.5 Central Bank's SFDR follow-up workshop	8
1.6 ESAs 2024 joint report on PAI disclosures under SFDR	8
2. Sustainability Reporting Related Developments	9
2.1 EU (Corporate Sustainability Reporting) Regulations 2024 (S.I. No. 336/2024) Update	9
2.2 Commission Notices concerning sustainability reporting published in the OJ	9
2.3 Taskforce on Nature-related Financial Disclosures ("**TNFD**") draft guidance on nature transition planning	9
2.4 ESMA reports on carbon markets	10
3. Taxonomy Related Developments	11
3.1 Commission frequently asked questions ("**FAQs**") on the implementation of the EU taxonomy for sustainable economic activities	11
3.2 Commission Notice	11
4. Other ESG- Related Developments	12
4.1 Platform Report on investing for transition benchmarks ("**ITB**")	12
4.2 ESG Rating Regulation	12
4.3 ESAs climate scenario analysis	13
4.4 IOSCO final report on good practices in voluntary carbon markets	13
4.5 IOSCO report on transition plans disclosures	13
4.6 ESMA sustainable finance implementation timeline	13
4.7 ESA report on implementing technical standards (ITS) regarding certain tasks of the collection bodies and functionalities of the European Single Access Point ("**ESAP**")	13
4.8 ESMA risk analysis article: "Assessing portfolio exposures to climate physical risks"	14
4.9 ESMA and ESA joint committee work programmes 2025	14

This is a condensed version of our Asset Management and Investment Funds Legal and Regulatory Report setting out key environmental, social and governance ("**ESG**") developments during the period from 1 October 2024 to 31 January 2025.

Key dates

2024	
14 October 2024	ESMA published its latest sustainable finance implementation timeline. The implementation timeline covers developments relating to the Sustainable Finance Disclosure Regulation (EU) 2019/2088 ("**SFDR**"), Taxonomy Regulation, Benchmarks Regulation and on European Green Bonds Regulation.
30 October 2024	ESMA & the European Supervisory Authorities ("**ESAs**") published their third annual report on disclosures of principal adverse impacts ("**PAI**") under the SFDR.
14 November 2024	IOSCO published its final report on good practices in voluntary carbon markets ("**VCMs**"). VCMs are markets where entities buy carbon credits for voluntary use (for example, to offset carbon emissions and support a claim about their climate performance, or otherwise finance mitigation activities with traceable results).
21 November 2024	ESMA guidelines on funds' names ("**Fund Names Guidelines**") using ESG or sustainability-related terms apply for new funds.
November 2024	The Central Bank of Ireland ("**Central Bank**") hosted the Sustainable Finance Disclosure Follow-up workshop. This was an in-person engagement with representatives from Irish Funds, asset managers and legal advisors. The aim of the workshop was to discuss SFDR follow up disclosure matters from the November 2023 workshop, the Fund Names Guidelines, and the ESMA Common Supervisory Action ("**CSA**") on sustainability-related disclosures and the integration of sustainability risks.
2025	
1 January 2025	Reporting obligations commence under the Corporate Sustainability Reporting Directive (EU) 2022/2464 ("**CSRD**") for certain in-scope large companies (with their first annual CSRD-compliant financial reports to be published in 2026).
26 February 2025	Omnibus simplification package. European Commission (the "**Commission**") intends to publish details relating to potential omnibus legislation to combine the sustainability reporting frameworks contained in the Taxonomy Regulation, CSRD and the corporate sustainability due diligence directive.
Q2 2025	ESMA report expected on the CSA on sustainability-related disclosures and the integration of sustainability.
21 May 2025	Fund Names Guidelines apply (for funds in existence at 21 November 2024).
Q4 2025	Proposal for revision of the SFDR expected to be published by the Commission.

Highlights during the period

In this quarterly edition of the Walkers ESG newsletter, we identify a number of key highlights during from European legislative and regulatory developments and advances in the global sustainable finance framework more broadly.

Platform on Sustainable Finance: Report on Categorisation of products under SFDR

The Platform on Sustainable Finance (the "**Platform**") published a report on the 'Categorisation of Products under SFDR' as part of the Commission's review of the functioning of the SFDR and different interpretations by national competent authorities ("**NCAs**"), auditors, and lawyers. While the proposal in the report is both high level and not binding on the Commission, the proposal outlines the categorisation scheme and considerations that the Platform recommends the Commission implement as part of the SFDR review process for the benefit of all investors.

The Commission now intends to publish a proposal for review of Level 1 of the SFDR in Q4 of 2025. The proposal will likely reflect the detailed proposals recently published in December 2024 by the Platform.

More details can be found under section 1.2 of this newsletter.

ESMA Q&A on Fund Name Guidelines

ESMA published Q&As with further details on specific aspects of the Fund Names Guidelines. ESMA published three new questions which provided some clarification on some of the key elements within their Fund Names Guidelines. The Q&A centred around;

1. applicability of Eu Paris-Aligned Benchmarks or EU Climate Transition Benchmarks (together, the "**PAB/CTB criteria**") to Green Bonds/ use of Proceeds Bonds,
2. defining "Meaningfully" investing in sustainable investments, and
3. clarifying what is included with "Controversial weapons".

More details can be found under section 1.3 of this newsletter.

Central Bank's notice of intention on Fund Names Guidelines

The Central Bank markets update (issue 9) includes the Central Bank's notice of intention for full compliance with ESMA's Fund Names Guidelines.

More details can be found under section 1.4 of this newsletter.

Central Bank follow-up SFDR workshop

The aim of this workshop was to discuss sustainability related disclosures under SFDR as well as the Fund Names Guidelines and ESMA's CSA on sustainability related disclosures and the integration of sustainability risks. The member note summarises discussions on a number of Central Bank expectations for SFDR disclosures.

More details can be found under section 1.5 of this newsletter.

ESG Ratings Regulation

In mid-December, the ESG ratings regulation (EU) 2024/3005 was published in the official journal of the EU (the "**OJ**") and will take effect from 2 July 2026. ESG rating providers within the EU will need to be authorised and supervised by ESMA. Providers are required to notify ESMA by **2 August 2026** to be able to continue operating in the EU and are required to apply for authorisation or recognition by **2 November 2026**.

More details can be found under section 4.2 of this newsletter.

ESMA sustainable finance implementation timeline

ESMA published its most recent sustainable finance implementation timeline.

More details can be found under section 4.6 and the timeline itself can be found on page 16.

SFDR-related Developments

Platform Report on Transition Plans

On 22 January 2025, the Platform published its latest report on corporate transition plans entitled 'Building trust in transition: core elements for assessing corporate transition plans'.

The report identifies core elements for evaluating corporate transition plans, offering recommendations to the Commission for enhancing the effectiveness of its policy framework and supporting the market to provide and access transition finance while addressing risks of greenwashing.

Key takeaways from the report include practical guidance for financial institutions to assess corporate transition plans based on four key elements:

- science-based and time-bound targets;
- key levers and actions to achieve these targets;
- financial planning; and
- governance of the plan and its implementation.

The report notes that for the purposes of transition finance, corporate transition plans have become essential in helping turn high-level climate and environmental targets into actionable strategies and investment plans that can be clearly communicated to financial market participants. Section 2 in the report provides a summary of existing EU requirements relating to transition plans.

Platform Report on Categorisation of products under SFDR

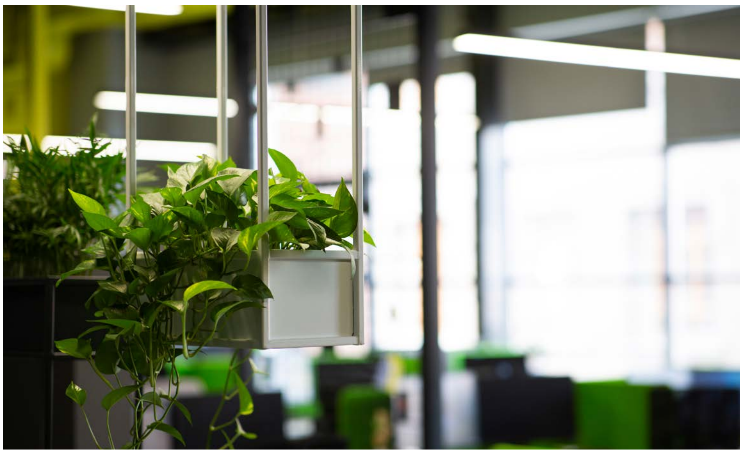
On 17 December 2024, the Platform published a report on the 'Categorisation of Products under SFDR', taking into account the stated need for simplification and streamlining of EU sustainable finance disclosure regulations and outlining key considerations for the Commission as part of its SFDR review.

The report aims to ameliorate inconsistencies in approach throughout the EU in respect of the categorisation of products under SFDR which have arisen as a result of varying national labelling regimes and different interpretations by NCAs, auditors, and lawyers. While the proposal in the report is both high level and not binding on the Commission, the proposal outlines the categorisation scheme and considerations that the Platform recommends the Commission implement as part of the SFDR review process for the benefit of all investors including retail. The proposal takes due consideration of the need for a smooth transition from the existing disclosure regime including the potential impact on existing offerings, the SFDR implementation efforts and the benefits to all investors including in relation to their sustainability preferences and the basis on which investors have invested in such products.

The Platform recommends categorising products with the following sustainability strategies:

- Sustainable: adherence to a share of EU taxonomy-aligned Investments or Sustainable Investments with no significant harmful activities adhering to the exclusion criteria, or assets based on a more concise definition consistent with the EU Taxonomy Regulation *((EU) 2020/852)* (the "**Taxonomy**").
- Transition: foster the transition to a net zero and an overall sustainable economy by 2050 and milestones in line with the EU goals through investments or portfolios supporting the transition to net zero and a sustainable economy, avoiding carbon lock-ins, per the Commission's Transition Finance guidelines.
- ESG collection: (select or exclude sectors or companies based on ESG performance) through investments excluding significantly harmful investments / activities, investing in assets with better environmental and/or social criteria or applying various sustainability features. The Platform notes that funds of funds, while eligible for any of the categories, will likely be most suited to the ESG collection category.
- All other products should be identified as **unclassified products**. In relation to unclassified products, the Platform proposes that unclassified products should still be required to report on Taxonomy-alignment and PAI greenhouse gases ("**GHG**") emissions.

The Platform proposes a number of criteria and reporting requirements for each of the above categories but does not propose any actual thresholds for the percentage of investments which must meet those minimum criteria. The proposal acknowledges the need for "identifying approaches to address different asset classes, investment strategies and types of products" which suggests that various assets classes and products may be subject to specific thresholds.



The proposal outlines mandatory minimum criteria with an underlying selection of binding elements that could meet these criteria, along with potential indicators. Financial market participants ("**FMPs**") should identify the binding elements relevant to their products, determine their specific details, and select the indicators they will use for measurement. Products within the relevant categories will be subject to pre-contractual disclosure and periodic reporting requirements. Unclassified products will not be subject to pre-contractual disclosure requirements, although it is proposed that they be subject to the periodic reporting report of Taxonomy-alignment and PAI GHG emissions as outlined above.

The Platform does not include an "Impact" category noting that there is no common definition of the term and recommending that the Commission develop a common understanding of how impact investing relates to the SFDR and the Taxonomy.

Before setting specific thresholds for the categories, the Platform recommends conducting further analysis on the potential impact of thresholds for all SFDR products. Additional next steps should comprise identification of sources, collection and analysis of data for SFDR products other than liquid funds, in particular insurance and pension products, as well as private market funds, analysis of the different potential thresholds and identification of approaches to address different asset classes, investment strategies, and types of products.

The Platform also proposes changes to the rules regarding the collation of sustainability preferences from investors.

Under the MiFID II Directive (2014/65/EU), where a client indicates that they have sustainability preferences, an EU investment firm or asset manager will only be able to recommend certain categories of product to that client which are consistent with the sustainability preferences confirmed by the relevant investors. Sustainability preferences are the minimum proportion which the client wishes to invest in products which make Taxonomy aligned or sustainable investments under SFDR, or in products that consider PAIs under SFDR. In this regard, the Platform proposes amendments such that investors are asked broader and more general questions in order to more easily determine their sustainability preferences to which the relevant product or service should correspond and that these should be consistent with the relevant product categorisation as set out above (i.e., Sustainable, Transition, ESG Collection).

Finally, it should be noted that the Platform's proposal does not contain significant detail on any specific disclosure or naming provisions and as such does not contemplate significant changes to the disclosure rules under SFDR. The Platform has emphasised the importance of category names only being attached to products that qualify for that categorisation. The report notes the proposed categorisation scheme leverages the positive elements of the SFDR and the broader sustainable finance framework. Categories would have precise minimum criteria, clearly defined objectives, and measurable performance indicators. Products within these categories should measure and disclose their sustainability performance.

This report is intended to serve as the basis for the Commission to build a complete and detailed categorisation scheme. The report urges the Commission to consider strong interlinkage with investors sustainability preferences, a seamless transition by streamlining existing elements of the SFDR and the wider sustainable finance framework, in particular indicators used to measure sustainability and the potential implications of introducing a new categorisation system on existing financial products.

ESMA Q&A on the application of ESMA's Fund Names Guidelines

On 13 December 2024, ESMA published Q&As with further details on specific aspects of the practical application of the Fund Names Guidelines. The new Q&As address green bonds [UCITS ID2368, AIF ID 2370], the convergence on "meaningfully investing in sustainable investments" [UCITS 2373, AIF 2374] and the definition of controversial weapons [UCITS 2371, AIF 2372]. The objective of the Q&As are to ensure a smooth application of the Fund Names Guidelines through a common understanding of key concepts and among other matters address the following:

- Q&As on **green bonds** explain that the exclusion criteria (applicable to either EU PAB or CTB) do not apply to investments in European Green Bonds given the high level of protection guaranteed by the EU legal framework for such investments. ESMA has decided to clarify the treatment of Green Bonds in light of the application of the European Green Bonds Regulation from 21 December 2024 as well as the reference in the AIFMD II mandate noting that sectoral legislation takes precedence.

  For other green bonds, fund managers may use a look-through approach to assess whether the activities financed are relevant for the exclusion criteria and accordingly such assessment does not need to be performed with respect to the issuer of the green bond itself.
- Q&As on the term "**meaningfully investing in sustainable investments**" present a common understanding among NCAs that funds may not be "meaningfully investing in sustainable investments" if they contain **less than 50%** of sustainable investments. While NCAs should carry out a case-by-case analysis of how any sustainability-related term is used in the name of a fund, they may find that investment funds with "sustainable" terms in their names investing less than 50% of the proportion of investments in sustainable investments are not "meaningfully investing in sustainable investments". That amount could be higher, subject to the circumstances of the case; and
- The Q&A on **controversial weapons** specifies that the reference to the exclusion related to controversial weapons is as referred to in PAI indicator 14 in Annex I to Commission Delegated Regulation (EU) 2022/1288.

ESMA's Q&As provide a welcome clarification on the application of some key aspects of the Fund Names Guidelines. It remains to be seen, however, whether the Q&As go far enough to ensure a consistent application of the Fund Names Guidelines by NCAs throughout the EU.

Walkers' Asset Management & Investment Funds group have published a recent advisory which outlines in further detail each of the new Q&As.

Central Bank Streamlined Filing Process for UCITS and AIFs complying with ESMA's Fund Names Guidelines

(a) Issue 10

On 1 November 2024, the Central Bank published markets update (issue 10 of 2024) which contained the following key updates:

- Updates to Streamlined Filing Process for UCITS and AIFs following publication of ESMA's Fund Names Guidelines

The Central Bank has updated its streamlined filing process for the Fund Names Guidelines. The changes in scope of the process, will allow funds in addition to changes to fund names, to incorporate minor updates to disclosures (in the prospectus, supplements and SFDR annexes) made solely for the purpose of bringing the fund into compliance with the Fund Names Guidelines' requirements. Any such minor changes to disclosures should not represent a material change to either of the investment objective, investment policy, strategy or risk profile of the fund.

For such minor changes to SFDR-related disclosures, which may also include a change to fund name, the Board of the fund as well as the legal advisor to the fund, shall additionally attest that:

- the amendments made do not represent a material change to either of the investment objective, investment policy, strategy or risk profile of the fund; and
- the amendments have been made solely to bring the fund into compliance with the Fund Names Guidelines.

In an evolving area such as ESG and SFDR in particular, this streamlined process demonstrates the Central Bank's continued commitment to pragmatism and, to the extent possible, reducing any undue administrative burden on fund managers associated with SFDR compliance.

b) Issue 9

On 21 October 2024, the Central Bank issued markets update (issue 9) which includes the Central Bank's notice of intention wherein the Central Bank expects full compliance with the Fund Names Guidelines from 21 November 2024.

The Central Bank will, in due course, consult on the incorporation of related provisions in the Central Bank UCITS Regulations and AIF Rulebook.

Central Bank's SFDR follow-up workshop

During the period, Irish Funds circulated a member note of the SFDR follow-up workshop attended by industry with the Central Bank. The aim of the workshop was to discuss SFDR disclosure matters following up on its November 2023 workshop, as well as the Fund Names Guidelines and the ESMA CSA on sustainability-related disclosures and the integration of sustainability risks.

The member note summarises discussions on a number of Central Bank expectations for SFDR disclosures including in the following areas:

- sustainable investments disclosure and the requirement to disclose the underlying environmental and/or social sustainable investments commitments;
- Article 8 and 9 Funds: Asset allocation matching the total portfolio;
- Taxonomy disclosure expectations;
- consideration of minimum proportions;
- exclusion-only fund being categorised as an Article 8 fund; and
- Article 9(3) funds that are passively tracking a PAB or CTB.

The expectations set out in the workshop note are a precursor to an SFDR publication due to be issued by the Central Bank in 2025. In the meantime, the Central Bank has highlighted that the expectations noted should be considered by all funds and be taken into account by new fund applications going forward. Where information is published, the Central Bank's expectation is that managers implement any changes to the pre-contractual disclosures necessary to comply with the publication at the next update to fund documentation where revised for another reason.

On the ESMA CSA on sustainability-related disclosures and the integration of sustainability, the Central Bank outlined that ESMA will publish its CSA findings likely in Q1 2025. Following the ESMA publication, the Central Bank will publish its own findings in a report form instead of in the form of a Dear CEO letter. The Central Bank industry report will include observations identified under the parameters of the assessment scope, which includes sustainability risk monitoring, data limitations, SFDR regulatory guidance and fund disclosures. A number of risk mitigation programmes are proposed to address firm specific issues identified and requiring action. The Central Bank's industry report also intends to share insight on the background, methodology, and details of findings for the benefit of those firms who were not included in the assessment sample.

ESAs 2024 joint report on PAI disclosures under SFDR :

On 30 October 2024, the ESAs published their third annual report on disclosures of PAIs under SFDR ("**2024 Report**").

This is the ESAs' third annual report to the Commission on PAI disclosures, which has been produced under Article 18 of the SFDR. PAI disclosures aim at showing the negative impact of financial institutions' investments on the environment and people and the actions taken by FMPs to mitigate them. The 2024 Report refers to PAI disclosures published by 30 June 2023, (reference period from 1 January 2022 to 31 December 2022) and assesses entity and product-level PAI disclosures. The ESAs have broadened the scope of the 2024 Report to also cover the disclosures made under the SFDR Delegated Regulation template, available for the first time since 30 June 2023.

Overall, the ESAs noted positive progress on several elements compared to previous years, in particular, improvements on the location of the PAI disclosures (which are becoming more accessible to retail investors), and on the level and quality of the information disclosed. Also, significant improvements were identified in product PAI disclosures, although the share of products disclosing PAI information remains quite low. However, it views the level of compliance with the SFDR provisions (at both level 1 and level 2) is not yet fully satisfactory. Additional efforts are still needed to achieve full compliance.

The 2024 Report also includes an overview (Annex I) of recommended good and bad/non-compliant practices including on the location, clarity, complexity of the disclosures based on a survey of NCAs. The report includes recommendations to NCAs to ensure convergent supervision of FMPs' practices. It also includes recommendations to the Commission for its comprehensive assessment of the SFDR.

The findings of the 2024 Report show that financial institutions have continued to improve the accessibility of their PAI disclosures. There has also been positive progress regarding the quality of the information disclosed by financial products, and, in general, in the quality of the PAI statements.

Looking ahead, the ESAs will monitor the recommendations to NCAs contained in the 2024 Report that seek to ensure convergent supervision of financial market participants' practices, and recommendations to the Commission for its assessment on the SFDR.

Sustainability Reporting Related Developments

EU (Corporate Sustainability Reporting) Regulations 2024 (S.I. No. 336/2024) Update

During the period, the Department of Enterprise, Trade & Employment published and updated a set of FAQs on interpretation of European Union (Corporate Sustainability Reporting) Regulations 2024 (S.I No. 336/2024), as amended (the "**Irish CSRD Regulations**"). The FAQs purport to provide additional clarification on topics including the scope of the upcoming second phase CSRD application which includes the CSRD 'large' undertakings criteria on turnover, balance sheet and employees.

"What companies are included in the second wave of sustainability reporting, that is, for financial years commencing 1 January 2025?"

Large companies being companies satisfying at least 2 of 3 criteria – balance sheet greater than €25 million, turnover greater than €50 million and more than 250 employees.

* In line with the Irish transposition of the EU Accounting Directive (Directive 2013/34/EU) through the Companies (Accounting) Act 2017, companies deemed 'large' for the purpose of the Irish transposition of that Directive are also deemed 'large' for the purpose of CSRD reporting under SI 336/2024. See Section 280H of the 2014 Act, and the definition of "ineligible entities" under sections 275, 1116A, 1267A and 1400A of the 2014 Act.

The FAQs provide the Department's view on the interpretation of the Irish CSRD Regulations while containing a disclaimer that the FAQs do not constitute a legal interpretation. Accordingly, the FAQs should not be treated as legal advice. Notwithstanding the publication of the FAQs, there remains some areas requiring clarification including the interpretation within the Irish CSRD Regulations regarding "applicable company" which may inadvertently result in certain regulated financial service providers being brought within the scope of the CSRD at this stage. It remains to be seen whether the Department of Enterprise, Trade & Employment or the Central Bank will offer further clarification to industry.

Commission Notices concerning sustainability reporting published in the OJ

On 13 November 2024, the Commission notice containing a set of FAQs to provide guidance and clarification on sustainability reporting requirements introduced by the CSRD and certain provisions of SFDR was published in the OJ. The Commission published a draft of the notice in August 2024.

The replies to the FAQs in the notice clarify the rules in the applicable legislation. They do not introduce any additional requirements and are intended to help financial undertakings implement the legislation.

Taskforce on Nature-related Financial Disclosures ("TNFD") draft guidance on nature transition planning

On 27 October 2024, the TNFD published a discussion paper setting out draft guidance for companies and financial institutions on developing and disclosing a nature transition plan.

The draft guidance includes:

- a definition of a nature transition plan and an overview of related initiatives;
- guidance on what a nature transition plan should include, how it should be presented and how it should be disclosed; and
- areas of further work needed on development and assessment of nature transition plans.

A nature transition plan lays out an organisation's goals, targets, actions, accountability mechanisms and intended resources to respond and contribute to the transition goals of the Kunming-Montreal Global Biodiversity Framework.

The discussion paper is open for feedback until 1 February 2025 from corporates, financial institutions and other interested stakeholders. Based on the feedback received through the consultation, and insights gained through potential pilot testing, the TNFD will develop guidance on nature transition plans that will be published in 2025. The TNFD also encourages businesses and financial institutions to pilot test the draft guidance set out in this discussion paper.

ESMA reports on carbon markets

On 7 and 8 October 2024, ESMA issued two publications on carbon markets.

Firstly, ESMA published the 2024 EU Carbon Markets report.

This report is provides details and insights into the functioning of the EU Emissions Trading System ("**EU ETS**") market. The key findings of the report include:

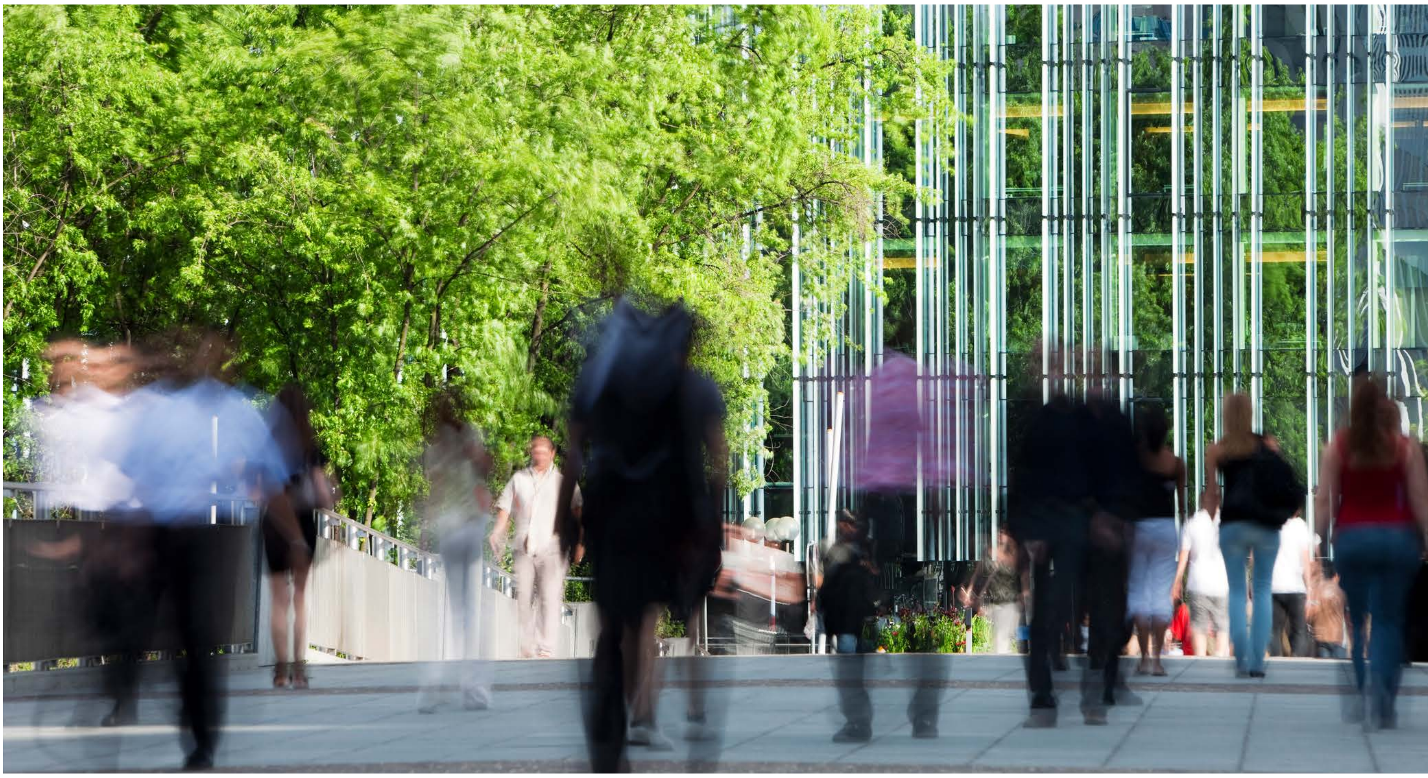
- Prices and volatility: Prices in the EU ETS have declined since the beginning of 2023. This was due to a combination of lower demand for emission allowances from weak industrial activity, falling natural gas prices and decarbonisation of the European energy sector, along with increased supply following the decision to auction additional allowances to finance the REPowerEU plan;
- Auctions: Emission allowance auctions remain significantly concentrated, with 10 participants buying 90% of auctioned volumes, reflecting a preference by most EU ETS operators to source allowances from financial intermediaries; and
- Trading and positions: The vast majority of emission allowance trading in secondary markets takes place through derivatives, reflecting the annual EU ETS compliance cycle where non-financial sector firms hold long positions (for compliance purposes) while banks and investment firms hold short positions.

The report builds on ESMA's 2022 report on the trading of emission allowances, mandated in the context of rising energy prices and a three-fold increase of emission allowances' prices in 2021.

The 2024 EU Carbon Markets report was drafted in line with ESMA's mandate under the EU ETS Directive that is establishing a system for greenhouse gas emission allowance trading in the EU. The ESMA carbon markets report will be produced annually as per ESMA's mandate.

Secondly, ESMA published a statement '*Clearing the smog: Accounting for Carbon Allowances in Financial Statements*' aimed at improving financial reporting for issuers engaging in carbon allowance programmes.

The statement also calls for consistency between the assumptions used in estimations and measurements related to climate matters and the information provided across the different sections of the annual financial report and with respect to carbon allowances in the financial statements with the disclosures required under the European Sustainability Reporting Standards ("**ESRS**").



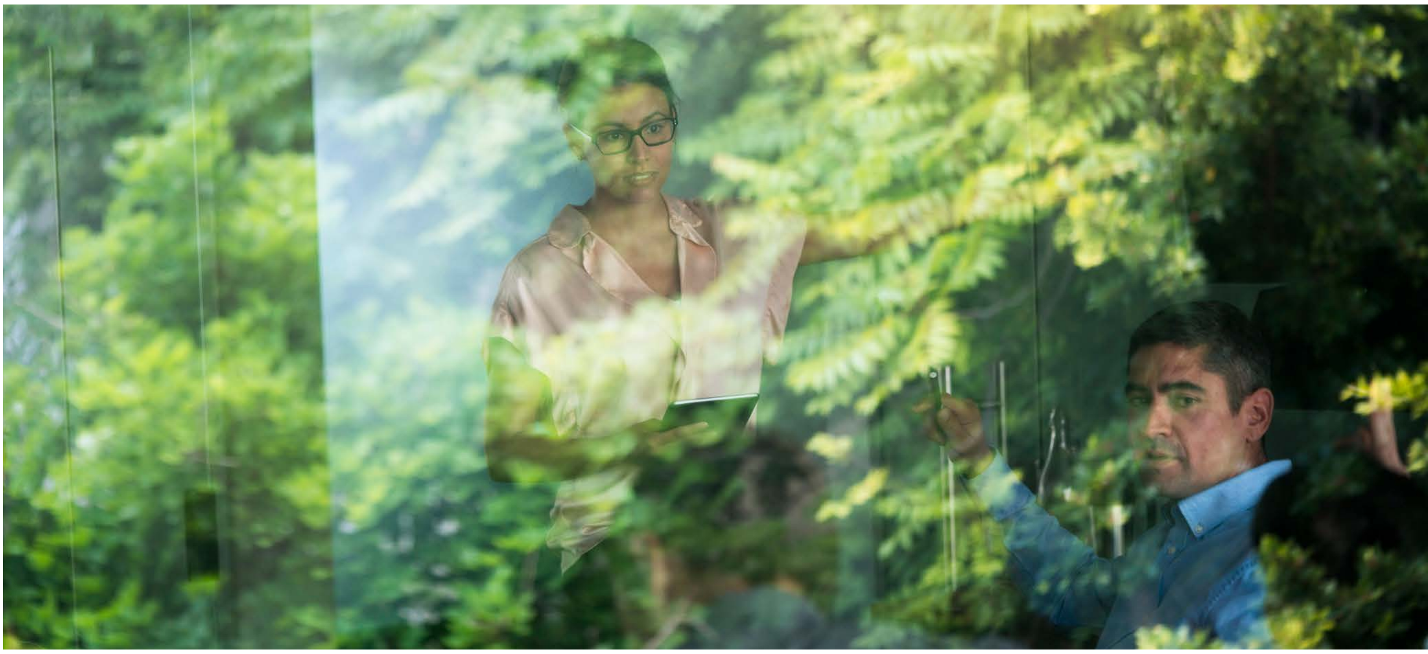
Taxonomy Related Developments

Commission frequently asked questions ("**FAQs**") on the implementation of the EU taxonomy for sustainable economic activities

On 29 November 2024, the Commission published a draft Commission notice containing a set of FAQs to facilitate the implementation of the EU taxonomy for sustainable economic activities.

The press release provides that these FAQs provide technical explanations on various facets of the Taxonomy Regulation for sustainable economic activities, encompassing the application of general requirements, technical screening criteria for specific activities outlined in the Climate and Environmental Delegated Acts, and the generic 'do no significant harm' (DNSH) criteria.

The guidance also includes clarifications the reporting obligations for activities covered by the Climate Delegated Act ((EU) 2023/2485) and the Environmental Delegated Act ((EU) 2023/2486) and interoperability of the Taxonomy Regulation with the ESRS and CSRD.



Commission Notice

On 8 November 2024, the Commission notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act ((EU) 2021/2178) made under Article 8 of the EU Taxonomy Regulation ((EU) 2020/852) on the reporting of Taxonomy-eligible and Taxonomy-aligned economic activities and assets was published in the OJ. The Commission published a draft of the notice in December 2023.

Other ESG- Related Developments

Platform report on investing for transition benchmarks ("ITB")

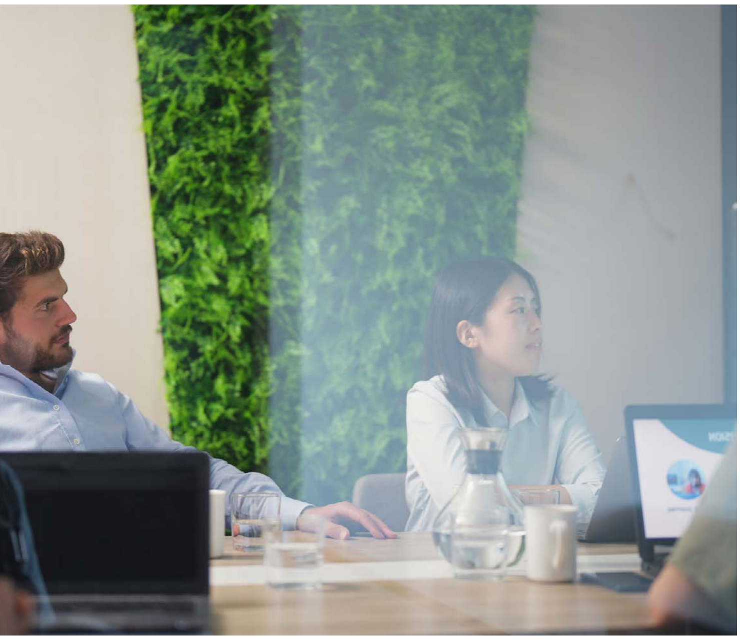
On 19 December 2024, the Platform published a report on ITB. The report proposes two voluntary benchmark labels (investing for transition benchmarks, with and without exclusions) to highlight the pivotal role can play in shaping climate and environmental benchmarks as well as in transition finance.

The ITB are inspired by the success of PAB and the success in the growth of taxonomy aligned capital expenditures.

ESG Rating Regulation

On 12 December 2024, the ESG Rating Regulation (EU) 2024/3005 (the "**Regulation**") was published in the OJ. The Regulation establishes a new European framework to govern the provision and distribution of ESG ratings and entered into force on 2 January 2025 (20 days after publication in the OJ) and will apply from 2 July 2026.

The Regulation imposes obligations on both ESG rating providers within the EU and on certain ESG rating providers outside the EU in specific circumstances. The Regulation primarily regulates ESG rating providers operating within the EU and provides that ESG rating providers established in the EU will need to be authorised and supervised by ESMA and comply with transparency requirements with regard to their methodologies and sources of information. ESG ratings providers are required to notify ESMA by 2 August 2026 to continue operating in the EU and are required to apply for authorisation or recognition by 2 November 2026.



The Regulation details the various requirements that need to be complied with in order to operate as an ESG ratings provider in the EU including the application process or how an ESG ratings provider might benefit from an equivalence decision, an endorsement or a recognition where they are established outside the EU. The Regulation details the transparency and organisational requirements that ESG ratings providers must comply with as well as the processes and documents concerning governance, independence and conflicts of interests that providers must put in place.

Under the Regulation, ESMA will establish and maintain a publicly accessible register on its website that contains the identities of the ESG rating providers including those that are authorised in the EU, registered under a temporary regime for small ESG rating providers and those ESG ratings providers that are established outside the EU.

The Regulation also amends the SFDR to require those FMPs or financial advisors which issue and distribute a rating in their marketing communications to comply with certain disclosure requirements. The ESAs are mandated to prepare draft regulatory technical standards to specify the information required.

ESG ratings play an important role in global capital markets, as investors, borrowers and issuers increasingly use ESG ratings as part of the process of making informed decisions relating to sustainable investment and financing. Consequently, ESG ratings have a significant impact on the operation of markets and on the trust and confidence of investors and consumers. ESG ratings play an enabling role for the proper functioning of the EU sustainable finance market by providing investors and financial institutions with important information for their investment strategies, risk management and disclosure obligations. At the same time European policy makers have acknowledged that the production and distribution of ESG ratings suffers from a lack of transparency and reliability.

The Regulation seeks to address this and ensure that ESG ratings used in the EU are independent, comparable where possible, impartial, systematic and of adequate quality. It is important that ESG rating activities are conducted in accordance with the principles of integrity, transparency, responsibility and good governance, while contributing to the sustainable finance agenda of the EU. Entities which provide ESG ratings or use ESG rating providers should consider whether they fall within the scope of the Regulation and if so, begin preparations to ensure they will be in a position of compliance by 2 July 2026.

The ESAs climate scenario analysis

On 19 November 2024, the ESAs published its report with the results of its one-off "Fit-For-55" climate scenario analysis. The Commission had invited the ESAs and the European Central Bank to assess the impact on the EU banking, investment fund, occupational pension fund and insurance sectors of three transition scenarios incorporating the implementation of the Fit-for-55 package, as well as the potential for contagion and amplification effects across the financial system. Under the scenarios examined, the report indicates transition risks alone are unlikely to threaten financial stability. However, when transition risks are combined with macroeconomic shocks, they can increase losses for financial institutions and may lead to disruptions.

The press release notes that report calls for a coordinated policy approach to financing the green transition and the need for financial institutions to integrate climate risks into their risk management in a comprehensive and timely manner.

IOSCO final report on good practices in voluntary carbon markets

On 14 November 2024, IOSCO published its final report on good practices in VCMs. VCMs are markets where entities buy carbon credits for voluntary use (for example, to offset carbon emissions and support a claim about their climate performance, or otherwise finance mitigation activities with traceable results).

The report aims to promote the financial integrity and orderly functioning of the VCMs and sets out 21 good practices, which cover regulatory frameworks, primary market issuance, secondary market trading (including market functioning and transparency, governance and risk management, and market abuse), and use, disclosure and retirement of carbon credits.

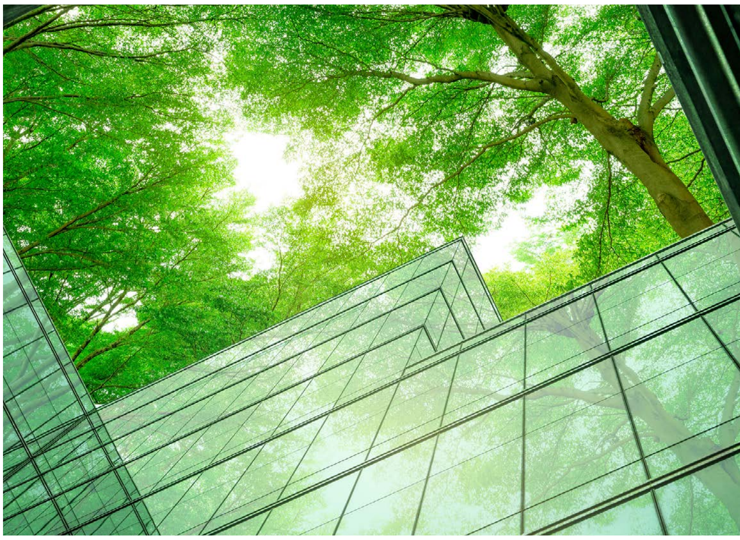
IOSCO report on transition plans disclosures

On 13 November 2024, IOSCO published a report developed by its Sustainable Finance Taskforce on how transition plans disclosures can support the objectives of investor protection and market integrity.

The Report highlights the five most useful components of transition plans disclosures that were suggested by market participants in IOSCO's outreach:

- ambition and targets;
- decarbonisation levers and action plan;
- governance and oversight;
- financial resources and human capital; and
- financial implications.

On consistency and comparability, stakeholders suggested additional guidance on transition plans disclosures could clarify disclosure expectations and lead towards more standardised information. IOSCO also encourages relevant standard setters to consider providing markers on what would constitute forward-looking information, in accordance with their standards and governance processes.



ESMA sustainable finance implementation timeline

On 30 October 2024, ESMA published its most recent sustainable finance implementation timeline.

The current implementation timeline reflects the possibility of material relating to the Commission's review of the SFDR being published in mid-2025. The Commission has subsequently stated in its work programme for 2025 that it now expects to publish its report on the SFDR Level 1 Review in Q4 2025.

In addition, the implementation timeline covers forthcoming developments relating to SFDR, Taxonomy, Benchmarks Regulation and on European Green Bonds Regulation.

Please see the final page of this Newsletter for a graphic of ESMAs latest timeline.

ESA report on implementing technical standards (ITS) regarding certain tasks of the collection bodies and functionalities of the European Single Access Point ("**ESAP**")

On 29 October 2024, the ESAs published the Final Report on the draft ITS regarding certain tasks of the collection bodies and functionalities of the ESAP.

The ESAP will facilitate access to publicly available information relevant to financial services, capital markets and sustainability. The ESAP is expected to start collecting information in July 2026, while the publication of the information will start no later than July 2027. The Final Report has been sent to the Commission for adoption.

ESMA risk analysis article: "Assessing portfolio exposures to climate physical risks"

On 9 October 2024, ESMA published a TRV article on assessing portfolio exposures to climate physical risks. The articles notes that within the financial sector, a key challenge is the management of the indirect exposure to climate physical risks through financial assets. While investment funds' portfolio vulnerabilities to physical risks appear limited given their ability to rebalance portfolios quickly and the short-term nature of their liabilities, some funds may still be exposed to climate physical risks.

The accuracy of these assessments is subject to various limitations and their interpretation requires context to understanding the implications of choices made with respect to measurements, aggregation methodology and time horizon. This article illustrates how two different assessment methodologies and data sources provide insights on climate physical risk exposures, based on an analysis of EU investment fund portfolio holdings. As expected, funds domiciled in northern Europe tend to be more exposed to companies subject to flood risks, while those domiciled in southern Europe are relatively more exposed to the consequences of water supply-and-demand imbalances.

Going forward, ESMA will continue to monitor EU fund exposures to climate physical risks by including some of these indicators into its regular risk assessments.

ESMA and ESA joint committee work programmes 2025

On 1 October 2024, ESMA published its 2025 Work Programme and accompanying press release. The press release notes that a significant portion of ESMA's work in 2025 will comprise policy work to facilitate the implementation of the large number of mandates received in the previous legislative cycle, and the preparation of new mandates, such as the European Green Bonds (EU) 2023/2631 and the ESG Rating Regulations.

ESMA will intensify its focus on implementing the sustainable finance legal and supervisory framework, combating greenwashing, and promoting transparency in sustainable investments.

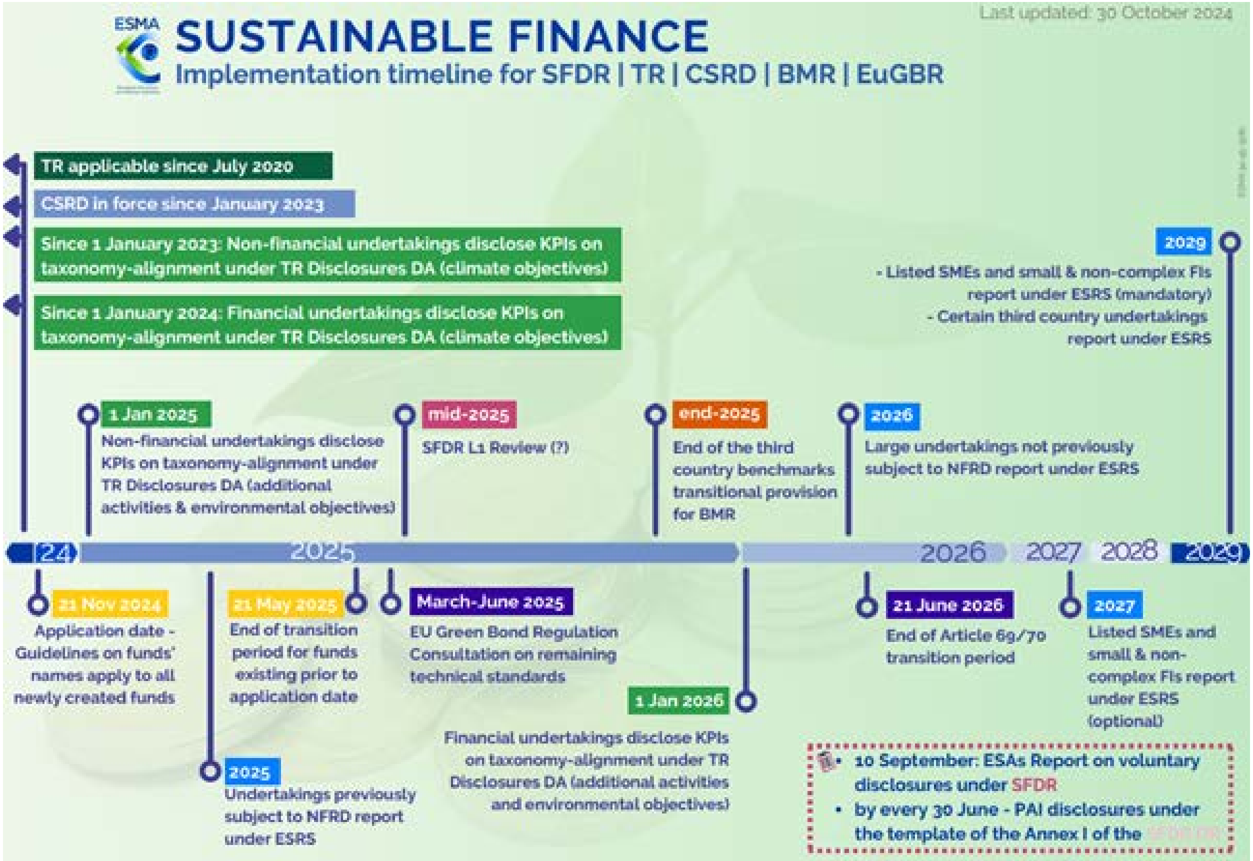
Key ESMA deliverables

Annex IV to the work programme sets out an overview of ESMA's 2025 deliverables by output type together with a brief description of each type, e.g. technical standards, technical advice, reports and statutory guidelines to be delivered in 2025. These include:

- RTS under the ESG Rating Regulation & Green Bond Regulation.
- ESMA's ESG guidance outputs to be delivered in 2025 which are currently known include guidance on sustainability claims to FMPs.
- ESMA will also build on the various CSAs that have been conducted in 2023-2024 with a sustainability angle. ESMA intends to develop machine-readable templates for SFDR disclosures (subject to Commission adoption of revised standards). The Commission's assessment and potential review and revision of SFDR (expected to be published in Q4 of 2025) may also generate requests for advice in 2025. ESMA will also monitor the implementation of the Fund Names Guidelines.
- In 2025, ESMA will work to further strengthen supervision focusing on effective coordinated supervision across the EU financial markets. ESMA will continue to use all the tools in its convergence toolkit to further harmonise supervisory approaches and practices across its remit, including common supervisory actions, and practical exchanges on specific supervisory cases and challenges.
- ESMA will work closely with the NCAs to enhance cross-border cooperation and data-sharing. Through the continued implementation of its data strategy and the development of common SupTech (technology used by supervisory authorities) and data projects, ESMA will be contributing to the EU strategy on supervisory data in financial services. In 2025, ESMA is expected to finalise preparations to launch the first phase of the ESAP in 2026, aiming to create a centralised platform for easy access to public data and information on securities markets.

ESMA Sustainable Finance Timeline

Further to item 4.6 above, please see below ESMA's most recent sustainable finance timeline.



Further information

We continue to see a high number of asset managers considering how to integrate ESG criteria in the investment strategies they employ for funds under management. Walkers has extensive experience advising on the impact that sustainable financing initiatives will have on such asset managers and investment funds.

This newsletter is for information purposes only, does not purport to represent legal advice and assumes a working knowledge of EU sustainable finance developments. Should you wish to discuss the implications on your business of the EU's sustainable finance framework or of the Central Bank's supervisory expectations regarding the implementation of the framework please speak to your usual contact in Walkers or any of the Walkers' contacts in your region.

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