

Updated ICMA commentary and recommendations on the SFDR 2.0

Introduction

On 20 November 2025, the European Commission (EC) [published](#) its long-awaited proposal for the review of the Sustainable Finance Disclosure Regulation (SFDR). In its [note](#) of February 2026, ICMA provided an overview, commentary and recommendations on the EC's proposed [draft](#) for SFDR 2.0. Since then, ICMA has also engaged with the relevant EC, European Parliament (EP) and Council representatives ahead of the trilogue process.

In June 2026, the Council [adopted](#) its negotiating position, followed by the EP in October 2026. This paper provides more targeted feedback regarding the key rules for the future sustainability-related fund categories under SFDR 2.0 ahead of the trilogue process. It complements the initial positions and recommendations from ICMA's [February 2026 note](#), of which a summary is provided in Annex 1.

In short, ICMA welcomes the co-legislators' converging positions on not adding new entity-level exclusions for use-of-proceeds (UoP) bonds under the proposed categories. Otherwise, ICMA provides below its commentary and alternative proposals on how to improve the categorisation rules even in areas of considerable convergence between the co-legislators. These relate notably to: (i) the general exclusion regime applicable to fund categories; (ii) the treatment of standard public debt; (iii) the proposed engagement requirement for categorised products; and, (iv) the eligible investment type examples for the ESG Basics category.

This paper has been prepared by ICMA staff with the input of the association's key constituencies including the Asset Management and Investors Council (AMIC), the Executive Committee of the Principles, and the Regulatory Policy Committee (RPC). It does not, however, necessarily represent the view of each individual member of these committees or of the Association.

Overview of the EU legislators' positions and ICMA commentary and proposals

A considerable degree of convergence has emerged between the EU co-legislators regarding the names and the rules for the future sustainability-related fund categories under the SFDR 2.0.

To start with, all three co-legislators have opted for the categories to be named "Transition" (Art. 7), "ESG Basics" (Art. 8) and "Sustainable" (Art. 9), reflecting the sustainability objectives of the funds.

Also, all three co-legislators propose to introduce a 70% minimum threshold for investments that comply with the fund categories' specific objectives. The alternative route of 15% fund-level EU Taxonomy alignment proposed by the EC for the Transition and Sustainable categories is maintained by the Council but increased by the EP to 20% for the Sustainable category.

The table below identifies and summarises other key areas on which ICMA provides commentary and alternative proposals:

Key areas	Overview of EC, Council, and EP positions	ICMA commentary and alternative positions
Application of exclusions to use-of-proceeds (UoPs) bonds	Under the EC draft, it appeared that the Transition category applied a stricter regime than the Sustainable category by introducing an additional entity-level exclusion for issuers developing new fossil fuel supply projects or new coal and hard-lignite power generation (or no-phase out). Under both the Council and EP versions, this now seems corrected. As a result, the exclusion regime for UoP bonds follows a look-through approach broadly consistent with the existing ESMA Q&A guidance in relation to fossil-fuel exclusions for UoPs instruments. Accordingly, the relevant fossil-fuel and other activity-based exclusions are generally assessed at the level of the activities financed by the UoP proceeds, rather than automatically at issuer level. EU Green Bonds benefit from an exemption from this exclusion test under all categories.	ICMA welcomes the Council and EP positions, which ensure a great degree of consistency with ESMA's Q&A guidance and avoid further fragmentation.
	In addition to the exclusions of Climate Transition Benchmarks (CTB) (for the	ICMA disagrees with the expansion of the exclusions to cover legacy upstream fossil

General exclusion regime for fossil fuel exposure	Transition and ESG-Basics) and Paris-aligned Benchmarks (PAB)¹ (for the Sustainable category), the EC proposed to apply new exclusions due to revenues ($\geq 1\%$) from hard coal and lignite activities under the Transition and ESG Basics categories, and new fossil fuel supply projects (or coal power generation) for both Transition and Sustainable categories. The most important change to the general exclusion regime introduced by the Council and the EP concerns the Transition category. Rather than relying on the CTB/PAB fossil fuel exclusions and excluding companies because they are developing new fossil fuel supply projects (as proposed by the EC), both co-legislators propose to exclude companies from the Transition category because of their existing (legacy) business revenues from upstream activities involving any fossil fuel type and, unlike under the PAB exclusions, without any tolerance thresholds. To counterbalance this, however, the Council provides an exception where a company has a minimum of 20% EU Taxonomy-aligned CapEx and a strategy to reduce Scope 1 and 2 emissions compatible with the Paris Agreement. In addition to these two conditions, the EP introduces two further conditions for the exception: a phase-out plan for coal power generation, and the company's EU Taxonomy-aligned CapEx must be higher than its CapEx for new upstream fossil fuel	fuel revenues under the Transition category. Excluding companies based on their legacy business undermines the overall objective of the Transition category, which should be to accompany and incentivise hard-to-abate and fossil fuel industries towards transition rather than excluding them at the outset. It also creates further fragmentation with the CTB/PAB exclusions and goes much beyond the ESMA Guidelines as the latter only applies the CTB exclusions to funds with transition-related names and incorporates tolerance thresholds even for funds with sustainable-related names². The exception rule is similarly problematic, as it refers only to EU Taxonomy alignment and does not introduce any path for recognising equivalence with other jurisdictions' taxonomies, decarbonisation pathways, roadmaps or policies, nor does it refer to other globally recognised proxies such as credible entity-level transition plans. This disregards the global nature of markets and assumes that third-country companies can align with the EU Taxonomy, which is not necessarily possible given its EU-centric criteria. In the context of O&G companies, referencing only Scope 1 and 2 emissions also does not signal a strategic transition away from the fossil fuel business that can be "compatible with the Paris Agreement", as over 90% of emissions in the sector are due to Scope 3 emissions, notably from the use of sold products. Furthermore, the exception rule may not even be available for companies with revenues ($\geq 1\%$) from legacy hard coal
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¹ See Annex 2 for the PAB and CTB exclusions.

² See Annex 2.

	projects over a three-year rolling period.	and lignite activities due to a reference to point (d) of Regulation 2020/1818 under Article 7/1(b). This also overlaps and creates fragmentation with Article 7/1(c) and therefore warrants clarification. <u>ICMA recommends an alternative approach that distinguishes between fossil fuel types and between legacy exposure and new projects, and that would align with market-based frameworks and initiatives regarding the application of fossil fuel exclusions:</u> i. For coal: Legacy coal supply turnover exposure does not lead to exclusion, at least if the company has a credible coal-exit/transition plan, while any new upstream coal supply or coal power generation project does lead to exclusion. ii. For other fossil fuels such as oil and gas: Neither legacy exposure nor new projects lead to exclusion if the company is decarbonising in line with a credible transition trajectory backed by a credible transition plan. Any potential future definition of a “credible” transition plan should be usable, practical and inclusive. It should also consider and recognise several sources of international guidance and proxies that now coexist with a considerable degree of convergence, such as the Net-Zero Asset Owner Alliance’s position (see p. 34 of the Target Setting Protocol), ICMA’s Climate Transition Finance Handbook, the UK Transition Finance Council’s publications and the ASEAN Transition Finance Guidance v.2. Third-party organisations also provide evaluation and rating services. Moreover, in our February position paper, we recommended that the EU encourage,
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		on a voluntary basis, a single universal disclosure for all relevant funds (i.e. all regulated funds, going beyond only ESG-categorised funds) to disclose their exposure (%) to entities implementing credible transition plans or targets for investments in high-climate-impact sectors. This intends to create to adopt and implement transition plans which are essentially investment plans (CapEx and OpEx) and could therefore contribute to the EU's overall competitiveness objective by generating additional economic activity.
Treatment of standard (non-UoPs) bonds of public entities	Under the EC draft, the standard bonds (non-UoPs) of public entities were excluded from counting into the 70% threshold of Transition and Sustainable categories, while allowed into the ESG Basics. Under both the Council and EP drafts, investments in standard bonds of EU public entities would count under the Transition category up to 15% within the 70% threshold but remain excluded from the Sustainable category. Under both drafts, however, MDBs are removed from the definitional scope, meaning that exposure to MDB standard bonds would not face such restrictions for inclusion in the Transition and Sustainable categories.	ICMA argues against limiting the eligibility to only EU public entities' standard bonds as this risks creating an unjustified geographic bias and reducing investment flexibility for globally diversified strategies. Also, many non-EU countries have issued sustainability-linked bonds committing to forward-looking sustainability outcomes which should be allowed in the Transition category. At a minimum, sustainability-linked bonds (SLBs) of all public entities (not only from the EU) aligned with the ICMA Principles should be allowed in the Transition category <u>up to an unlimited extent</u>. ICMA otherwise reiterates its position that asset managers should have the option to count standard bonds of all public entities into the 70% threshold of the Sustainable and Transition categories when backed by transparent methodologies and based on the principle of "proper justification" embedded in the EC draft <u>and up to an unlimited extent (vs. 15%)</u>.
Engagement	Under both the EC and Council drafts, assets subject to credible engagement	Most asset managers apply engagement processes at the entity level (rather than

	strategies are among the examples of eligible investment types for the Transition category. The EP draft would however make engagement process and disclosures a “comply or explain” type requirement across the three product categories.	the fund level), prioritising exposures with the weakest ESG performance. Engagement strategies would also be less relevant for assets that are already deemed sustainable and included in the Sustainable category, which would also apply comprehensive exclusion filters. For the ESG Basics and Sustainable categories, if maintained, the implementation of an engagement strategy and related actions should be provided as ex-post disclosures.
Eligible investment type examples under the ESG Basics category (Article 8/2)	Under the EC, the Council, and the EP drafts, Article 8/2(a) refers to <i>“investments with an ESG rating...that outperforms the average rating of the investment universe or the benchmark”</i>. Also, both the Council and the EP drafts would introduce a qualification under Article 8/2(b) so that investments should outperform the average investment universe or reference benchmark on at least two specific sustainability indicators instead of one as proposed by the EC. Also, under the EP’s version, Article 8/2(e) references points (a) and (d), which may read as prescriptive and undermining the open-list, non-exhaustive, and exemplary nature of the list for eligible investment types.	Article 8/2(a) should clarify that outperformance on ESG ratings can also be satisfied at the portfolio level, not only at the level of individual assets. The drafting can be revised as <i>“investments or a combination of investments with an ESG rating...that outperforms the average rating of the investment universe or the benchmark”</i>. ICMA believes that the proposed amendment under Article 8/2(b) (requiring the use of two indicators) is arbitrary and would unnecessarily and significantly reduce the eligible investment universe and the applicable scope of the ESG Basics category. It may create confusion, since investors essentially expect investments to be aligned with the product’s stated objective, but not to outperform on a multiplicity of metrics that may not be directly connected to that objective. We recommend adopting the EC’s approach to ensure that investments that outperform the average investment universe or reference benchmark on a specific, appropriate sustainability indicator can qualify. More generally, the lists of eligible investment types under Article 7/2,

		Article 8/2 and Article 9/2 are designed as non-exhaustive, open lists intended to guide potential strategies without strictly requiring all strategies to fall within them. Therefore, adding restrictive drafting to provisions of an illustrative nature creates an inconsistency.
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ICMA believes technical thresholds such as “X”% of Taxonomy alignment should be set at Level 2 to give EU policymakers greater flexibility to amend them later, notably if the initial thresholds prove to be too lenient or too tight. Otherwise, such numbers embedded in Level 1 text could quickly become outdated.

Several market participants expressed concerns about the disclaimer language under Article 2 (Amendments to Regulation (EU) No 1286/2014) in the EP draft, which is too broad and misleading. To the extent that it falls within the scope, it may be misread or perceived by retail investors as suggesting, for example, that an EU Green Bond does not comply with the European Green Bond Regulation (2023/2631), or that a sustainable bond aligned with an ICMA standard is not credible. It may also create a negativity bias against non-ESG products with no ESG claims. Ideally, this statement would be removed. If not, we would propose an amended version of the Council’s draft so that it is strictly factual and limited to the product’s status outside SFDR: *“This financial product does not fall under the scope of Regulation (EU) 2019/2088 and thus is not categorised under that Regulation”*.

Finally, as set out in our February 2026 paper, we would like to reiterate the importance of effective implementation, including the immediate application of simplification measures, the timely publication of operational delegated acts, and the synchronised alignment and entry into application of various interlinked sustainable finance regulations, such as MiFID/IDD ESG Preferences and the ESG Benchmark Delegated Regulations.

Annex 1 - Summary of ICMA commentary and recommendations of February 2026

ICMA welcomes the direction of travel of the SFDR 2.0. The EC proposal broadly accommodates the call of ICMA and broader industry for a simplified disclosure regime and a clearer ESG fund categorisation system. Regarding the latter, the proposal reflects a shift towards a more prescriptive regime when compared with the current Article 8 and 9 disclosure-based system but accommodates some important flexibilities.

It is important to note that the text is subject to further changes which may be proposed by the EU Parliament and the Council. Also, as per the EC proposal, a future Delegated Act (DA) may further specify the eligibility conditions and disclosures for the proposed product categories.

Our general comments on the [EC's] SFDR 2.0 proposal are in summary:

- For the Transition and ESG Basics categories, we argue against the extension of the exclusion list to cover entities with legacy turnover exposure to hard coal and lignite as it could conflict with objective of accelerating their transition.
- Asset managers should have the option to count non use-of-proceeds bonds of public entities into the 70% threshold of the Sustainable and Transition categories based on the principle of “proper justification” which is already embedded in the proposal, backed with transparent methodologies.
- Effective implementation should be ensured notably through the immediate application of the simplification measures (including the removal of entity-level Principal Adverse Impact (PAI) disclosures) and the timely publication of the operational Delegated Act(s), if any.
- Many market participants call for further voluntary guidance on some key terms, such as what it means to have a “credible” transition plan based on usable, practical, and inclusive definitions considering also international guidance in the space.
- The EU can encourage, on a voluntary basis, a universal disclosure for all relevant funds to disclose their exposure (%) to entities with credible transition plans/targets for their investments in high climate impact sectors.

Our specific comments regarding the treatment of use-of-proceeds (UoP) bonds and funds are in summary:

- While eligible investment types, standards, indicators, and tools for each new product category are not specified in an exclusive manner, we recommend explicit recognition of sustainable bonds aligned with established and credible market standards such as the ICMA Principles³.
- The exemptions foreseen for EU Green Bonds (EuGBs) from several exclusions should also apply to all UoP bonds aligned with established and credible international standards such as the [ICMA Principles](#).
- For both EuGBs and ICMA-aligned UoP bonds, the new exclusions triggered by greenfield fossil fuel supply projects and coal power should not apply at the entity-level under Transition and Sustainable categories if the new project is not related to hard coal and lignite and the issuer is pursuing a credible transition trajectory backed by an entity-level strategy/plan. As a potential

³ The ICMA Principles refer to the Green Bond Principles, the Social Bond Principles, the Sustainability Bond Guidelines, the Sustainability-Linked Bond Principles, the Climate Transition Bond Guidelines, and other relevant guidance which is administered and supported by the ICMA.

unintended drafting, the proposed EC draft currently implies a stricter regime for the Transition category than the Sustainable one, and therefore requires clarification or correction.

- Under the future potential Delegated Act(s), permitted limited deviation from the Paris-aligned Benchmarks exclusions should be introduced for the Sustainable category for Green UoP bonds which allocate only a small (non-meaningful) portion of their proceeds to climate transition projects in line with the ICMA's recently published [Climate Transition Bond Guidelines](#). The limited flexibility pocket introduced by Article 5 of the EuGB Regulation for EuGBs may serve as a precedent to that effect.

Annex 2 - The PAB and CTB exclusions

Article 12(1) of the Commission Delegated Regulation 2020/1818 lists the specific exclusions for the Climate Transition Benchmarks (see items "a" to "c") and the Paris-aligned Benchmarks ("a" to "g").

Exclusions under PABs	Exclusions under CTBs
(a) companies involved in any activities related to controversial weapons; (b) companies involved in the cultivation and production of tobacco; (c) companies that benchmark administrators find in violation of the United Nations Global Compact (UNGC) principles or the Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises; (d) companies that derive 1 % or more of their revenues from exploration, mining, extraction, distribution or refining of hard coal and lignite; (e) companies that derive 10 % or more of their revenues from the exploration, extraction, distribution or refining of oil fuels; (f) companies that derive 50 % or more of their revenues from the exploration, extraction, manufacturing or distribution of gaseous fuels; (g) companies that derive 50 % or more of their revenues from electricity generation with a GHG intensity of more than 100 g CO₂ e/kWh.	(a) companies involved in any activities related to controversial weapons; (b) companies involved in the cultivation and production of tobacco; (c) companies that benchmark administrators find in violation of the United Nations Global Compact (UNGC) principles or the Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises;