European Securities and Markets Authority

Reply form for the Consultation Paper on Guidelines for the use of ESG or sustainability-related terms in funds' names

18 November 2022

European Securities and Markets Authority

Date: 18 November 2022

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the Consultation Paper on Guidelines for the use of ESG or sustainability-related terms in funds' names published on the ESMA website.

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered);
- do not remove the tags of type <ESMA_QUESTION_FUNA_0> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
- if you do not have a response to a question, do not delete it and leave the text "TYPE YOUR TEXT HERE" between the tags.

Responses are most helpful:

- if they respond to the question stated;
- indicate the specific question to which the comment relates;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

Naming protocol

In order to facilitate the handling of stakeholders' responses please save your document using the following format:

ESMA_CP_FUNA_NAMEOFCOMPANY_REPLYFORM.

e.g. if the respondent were ABCD, the name of the reply form would be:

ESMA_CP_FUNA_ABCD_REPLYFORM

Deadline

Responses must reach us by 20 February 2022.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the headings 'Legal notice' and 'Data protection'.

General information about respondent

Name of the company / organisation	CFA Institute
Activity	
Are you representing an association?	☒
Country/Region	Europe

Introduction

Please make your introductory comments below, if any:

<ESMA_QUESTION_FUNA_0>

TYPE YOUR TEXT HERE

<ESMA_QUESTION_FUNA_0>

Q1 : Do you agree with the need to introduce quantitative thresholds to assess funds' names?

<ESMA_QUESTION_FUNA_1>
Yes, we believe that the introduction of quantitative thresholds would be helpful in providing more clarity for investors on the alignment of funds' names using ESG or sustainability-related terms with their investment objectives, principal investment strategies, and types of securities held.
However, focusing exclusively on a quantitative threshold to assess funds' names could be deceptive and misleading for investors when it comes to funds' names including terms like "free" or "zero". Investors may understand that such funds do not hold certain types of securities (i.e., they may think that fossil fuel-free funds have no investments with exposure to fossil fuels). A fund's name implying zero exposure may be deceptive for investors if the fund's investment policy allows investments to certain types of securities below a determined quantitative threshold.
<ESMA_QUESTION_FUNA_1>

Q2 : Do you agree with the proposed threshold of 80% of the minimum proportion of investments for the use of any ESG-, or impact-related words in the name of a fund? If not, please explain why and provide an alternative proposal.

<ESMA_QUESTION_FUNA_2>
CFA Institute agrees that the proposed threshold of a minimum proportion of investments for the use of ESG or sustainability-related terms in the name of a fund would assure investors that they are investing in funds with a minimum level of investments meeting environmental or social characteristics, or with certain sustainable investment objectives in accordance with the binding elements of the investment strategy. However, such an approach would not provide increased investor protection if funds' names included terms, such as "free" or "zero", as explained in our response to Q1.
Our members from Cyprus emphasised that the proposed threshold would potentially reduce the number of funds available in the market with a green label. The number of greenwashing cases will also likely fall and, thus, provide more transparency to investors when choosing investments.
A member from the Netherlands expressed concern that the introduction of a threshold could lead to issues in case of large cash positions (investment phase of a fund) or when market moves lead to soft breaches of the threshold. Such problems can be avoided by considering some exceptions (e.g., a reference in the fund documentation) or allowing a range for the market to drift to a lower percentage, such as 70%.
A member from the United Kingdom underlined that ESMA should produce some guidelines on the different meanings of the terms ESG and Sustainability as the use of these two words implies a hierarchy (or that the two terms differ from each other) when they have previously been used interchangeably in legislation. Moreover, the 80% threshold diverges from the UK Financial Conduct Authority approach of having a threshold of 70% sustainable investments under the UK Sustainability Disclosure Requirements, labelling and disclosure regime.
A member from Poland believes that organisations should claim compliance only if the threshold would be of 100%, while our members from Ireland remarked that neutral assets, such as cash and European government bonds also should be taken into consideration.
<ESMA_QUESTION_FUNA_2>

Q3 : Do you agree to include an additional threshold of at least 50% of minimum proportion of sustainable investments for the use of the word "sustainable" or any other sustainability-related term in the name of the fund? If not, please explain why and provide an alternative proposal.

<ESMA_QUESTION_FUNA_3>
Yes, we would agree on the inclusion of this additional threshold for funds using the word "sustainable" or any other term derived from the word "sustainable" in its name. However, ESMA should clearly provide a list of derived terms that would fall under this threshold, which should cover any name referring to a sustainability objective.
<ESMA_QUESTION_FUNA_3>

Q4 : Do you think that there are alternative ways to construct the threshold mechanism? If yes, please explain your alternative proposal.

<ESMA_QUESTION_FUNA_4>
A member from the Netherlands underlined that an alternative mechanism could consist in having a threshold based on more dimensions, namely a threshold regarding the investments made by the fund, and another one on the level of stewardship that fund managers perform for the companies in which they invest. Regulators could encourage good stewardship in this manner.
A member from Finland highlights that a strict approach on thresholds without exceptions might cause a slowdown of money floating into funds that might not be sustainable today but aim for transition.
<ESMA_QUESTION_FUNA_4>

Q5 : Do you think that there are other ways than the proposed thresholds to achieve the supervisory aim of ensuring that ESG or sustainability-related names of funds are aligned with their investment characteristics and objectives? If yes, please explain your alternative proposal. If yes, please explain your alternative proposal.

<ESMA_QUESTION_FUNA_5>
An alternative approach could be for all funds having an ESG or sustainability-related term in their names, and with an investment focus, to be required to make prospectus disclosures, including the definitions for all ESG or sustainability-related terms used in the fund's name that relate to the investment focus and the selection criteria the fund uses to make investments, and describe them.
<ESMA_QUESTION_FUNA_5>

Q6 : Do you agree with the need for minimum safeguards for investment funds with an ESG- or sustainability-related term in their name? Should such safeguards be based on the exclusion criteria such as Commission Delegated Regulation (EU) 2020/1818 Article 12(1)-(2)? If not, explain why and provide an alternative proposal.

<ESMA_QUESTION_FUNA_6>
We agree on the need for minimum safeguards for investment funds with an ESG or sustainability-related term in their name. However, these exclusions criteria should not only be applicable to Paris-aligned Benchmarks in the Benchmark Regulation Delegated Regulation, but also take into account other criteria, such as "Do No Significant Harm" principles under the SFDR, as well as social and biodiversity factors.
Our members from CFA Society Cyprus believe that the proposed safeguards based on exclusion criteria would be too restrictive. For example, implementing the exclusion criteria in accordance with the Commission Delegated Regulation (EU) 2020/1818 Article 12(1)-(d)-(f) would probably eliminate most of the energy sector in the equities space, which has been essentially the main driver of stock market gains along with financials for most of 2022. Hence, ESMA could allow for some flexibility for a maximum of 20% to the fund manager to pursue other strategies that can optimise the returns of the fund, without imposing additional restrictions.
A member from Finland also highlighted that these minimum safeguards should not apply to fossil fuels as the exclusion of oil and gas would result in the exclusion of many renewable energy investment opportunities. For these sectors, ESMA could adopt other thresholds so as to enable investments in "best" companies, which still hold investments in fossil fuels, but aim to transition to renewables energies.
<ESMA_QUESTION_FUNA_6>

Q7 : Do you think that, for the purpose of these Guidelines, derivatives should be subject to specific provisions for calculating thresholds?

<ESMA_QUESTION_FUNA_7>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_FUNA_7>

a) **Would you suggest the use of the notional value or the market value for the purpose of the calculation of the minimum proportion of investment?**

<ESMA_QUESTION_FUNA_1>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_FUNA_1>

b) **Are there any other measures you would recommend for derivatives for the calculation of the minimum proportion of investments?**

<ESMA_QUESTION_FUNA_2>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_FUNA_2>

Q8 : Do you agree that funds designating an index as a reference benchmark should also consider the same requirements for funds' names as any other fund? If not, explain why and provide an alternative proposal.

<ESMA_QUESTION_FUNA_8>
Yes, we agree that funds designating an index as a reference benchmark should be subject to the same requirements for funds names.
<ESMA_QUESTION_FUNA_8>

Q9 : Would you make a distinction between physical and synthetic replication, for example in relation to the collateral held, of an index?

<ESMA_QUESTION_FUNA_9>
No, we would not be in favour of a distinction in the thresholds between physical and synthetic replication as the same approach should apply to similar products, irrespective of the choice of replication method.
<ESMA_QUESTION_FUNA_9>

Q10 : Do you agree of having specific provisions for "impact" or impact-related names in these Guidelines?

<ESMA_QUESTION_FUNA_10>
CFA Institute agrees with the inclusion of specific provision for "impact" or impact-related names in the ESMA Guidelines. However, defining the term "impact" would be particularly challenging as it is difficult to prove causality.
<ESMA_QUESTION_FUNA_10>

Q11 : Should there be specific provisions for "transition" or transition-related names in these Guidelines? If yes, what should they be?

<ESMA_QUESTION_FUNA_11>
Yes, specific provisions for "transition" or transition-related names could be included in the ESMA Guidelines. Particular thresholds on investment characteristics and objectives related to the green transition could be taken into consideration.
<ESMA_QUESTION_FUNA_11>

Q12 : The proposals in this consultation paper relates to investment funds' names in light of specific sectoral concerns. However, considering the SFDR disclosures apply also to other sectors, do you think that these proposals may have implications for other sectors and, if so, would you see merit in having similar guidance for other financial products?

<ESMA_QUESTION_FUNA_12>
We believe that the ESMA proposals should apply to all the sectors covered under the SFDR disclosures in order to ensure a level playing field for all financial products. In particular, our members from Cyprus underlined that the scope should be expanded to also cover insurance products which are related and often offered as a substitute for investment funds. The application of the proposed guidelines to insurance products would result in greater competition between market participants and provide more transparency for investors, while mitigating instances of greenwashing.
<ESMA_QUESTION_FUNA_12>

Q13 : Do you agree with having a transitional period of 6 months from the date of the application of the Guidelines for existing funds? If not, please explain why and provide an alternative proposal.

<ESMA_QUESTION_FUNA_13>
Yes, a transitional period for the application of these Guidelines for existing funds would be necessary to allow funds to adapt their investment allocations to the proposed thresholds of minimum proportion of investments for the use of ESG or sustainability-related terms in their name.
A member from Finland stressed that the transitional period should be at least one-year long to allow gradual changes for funds with illiquid constituents.
<ESMA_QUESTION_FUNA_13>

Q14 : Should the naming-related provisions be extended to closed-ended funds which have terminated their subscription period before the application date of the Guidelines? If not, please explain your answer.

<ESMA_QUESTION_FUNA_14>
No, the proposed provisions should not be applied to closed-ended funds which have terminated their subscription period prior to the application date of the Guidelines because these funds are no longer marketed for investors, and the application of these rules could potentially lead to issues for fund managers and investors who have committed their capital, given that some funds may feature a lock-up period or restrictions for investors to disinvest their capital.
<ESMA_QUESTION_FUNA_14>

Q15 : What is the anticipated impact from the introduction of the proposed Guidelines?

<ESMA_QUESTION_FUNA_15>
The proposed Guidelines would improve transparency and provide more clarity on the nature of the funds in which they may invest.
A member from Finland believe that the provisions would result in many changes in funds’ names and investment strategies, while a member from the Netherlands warns that the absence of specific provisions for transition or transition-related funds’ names could result in the misperception that investing in these funds is not sustainable. This would lead to lower investments directed to this typology of funds.
<ESMA_QUESTION_FUNA_15>

Q16 : What additional costs and benefits would compliance with the proposed Guidelines bring to the stakeholder(s) you represent? Please provide quantitative figures, where available.

<ESMA_QUESTION_FUNA_16>
As mentioned in our response to Q15, the proposed guidelines would help investors understand whether funds with an ESG or sustainability-related term in their name are truly sustainable. With regard to the costs, asset owners may experience an increase in management fees, while funds would bear higher costs related to the changes in their names, and any update on prospectuses, and marketing materials.
<ESMA_QUESTION_FUNA_16>

Q17