|  |
| --- |
| 18 November 2022 |

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

|  |
| --- |
| 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](http://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](http://www.esma.europa.eu) under the headings ‘Legal notice’ and ‘Data protection’.

# General information about respondent

|  |  |
| --- | --- |
| Name of the company / organisation | Vontobel Asset Management S.A. / Vontobel Asset Management |
| Activity | Other Financial service providers |
| Are you representing an association? |  |
| Country/Region | Luxembourg |

# Introduction

Please make your introductory comments below, if any:

<ESMA\_QUESTION\_FUNA\_0>

Dear Sir or Madam

Please find below our replies for the Consultation Paper on Guidelines for the use of ESG or sustainability-related terms in funds’ names.

Vontobel Asset Management S.A. is a UCITS management company and AIFM domiciled in Luxembourg. We are an affiliate of Vontobel Holding AG with headquarters in Zurich, Switzerland.

We manage with 37.5 billion assets under management as of 31 January 2023 in four Luxembourgish umbrella-funds with 68 sub-funds (Art. 9 SFDR: 5 sub-funds; Art. 8 SFDR: 36; Other: 27).

The investment management for a significant part of the sub-funds has been delegated to investment managers domiciled in Switzerland, the United Kingdom and the United States of America.

Best regards

Vontobel Asset Management S.A.

<ESMA\_QUESTION\_FUNA\_0>

1. : Do you agree with the need to introduce quantitative thresholds to assess funds’ names?

<ESMA\_QUESTION\_FUNA\_1>

We believe it is of outmost importance to protect investors against exaggerated sustainability claims and to have harmonized requirements to achieve this goal. However, we have some concerns about the way the threshold mechanisms are designed, and the timing of this consultation (the proposed guidelines rely on a concept, namely “sustainable investments”, that still needs further clarification (we refer to Question 1 of the “List of additional SFDR queries requiring the interpretation of Union law” (JC 2022 47) of 9 September 2022 where the answers of the European Commission are still outstanding).

Fund names should be clear, fair and not misleading. A fund with a name that is ESG-related should apply an investment process that is in line with the name. We basically agree on quantitative thresholds to assess funds’ names as this principle already applies beyond ESG and seems to be a common administrative practice among national authorities. Based on this, an additional threshold specifically addressing the use of ESG-related terms in the name of a fund should not be needed, but we recognize the benefit of clarifying expectations through the introduction of such quantitative threshold to be applied in all members states of the EU.

Threshold references should be in any case quite clear to ensure comparability of products. The previous discussion with regards to the proposed 50% minimum for sustainable investments (50% of 100% of TNA vs. ½ of 80% assets aligned with E/S characteristics, i.e. 40% of TNA) already proved that the proposed description is not adequately clear to various market participants.

We are actually surprised that ESMA is of the view that the proposed “Guidelines are not intended to interfere with the requirements of the Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (SFDR)…”. From our point of view, the proposed guidelines clearly have an impact by creating an additional layer of rules for a wide range of funds categorized under article 8 and 9 SFDR.

We have noted that no list of “ESG-related words” will be provided, which might result in the application of different approaches by national competent authorities. We would rather support a consistent approach to be applied between national competent authorities.<ESMA\_QUESTION\_FUNA\_1>

1. : 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>

First of all, we would like to highlight that one of the key aspects of the draft guidelines is confusing. In fact, it is not clear what kind of assets should be included in the denominator of the proposed minimum percentages. Are the draft guidelines referring to (1) The total NAV of the Sub-Fund; or (2) The NAV of the Sub-Fund excl. cash and derivatives (only securities) or (3) The NAV of the Sub-Fund excl. cash and derivatives that do not have security exposure (direct and indirect exposures to securities)?

For the purpose of issuing a guidance ensuring fund names are proportionate, we believe two aspects are key:

* Thresholds should be set for assets to which ESG criteria can be applied (“assets in scope of the ESG criteria”), i.e. aligned with environmental and/or social characteristics.
* Investors should be assured that no investments are made in contradiction with the Sub-Fund’s name.

Accordingly, we propose the thresholds mechanisms to be applied as follows:

* More than 50% of the Sub-Fund’s Net Asset Value excl. cash and derivatives that do not have security exposure (direct and indirect exposures to securities) have the ESG criteria applied, i.e. shall be aligned with environmental and social characteristics.
* The remaining investments shall not be in contradiction environmental and social minimum safeguards defined by the investment manager considering the fund’s overall theme (minimum safeguards).

Regarding the threshold level to be applied: We do not think a different threshold level should be applied depending on the ESG-related term. The same thresholds mechanisms should apply. In case of data gaps, the Investment Manager should put reasonable efforts in ensuring investments are made within the meaning of the Sub-Fund’s name.<ESMA\_QUESTION\_FUNA\_2>

1. : 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>

We recognize the need to establish a framework around terms that may be appealing to investors. However, we do not believe investing in “sustainable investments” as the definition stands today is the only way to run an investment strategy that fosters a transition to a more sustainable world, which is the main goal of the EU Action Plan on Sustainable Finance. Here are the reasons:

* While “sustainable investment” seems to be a uniform concept in appearance, we observe a wide range of implementations on the market. Introducing thresholds related to sustainable investments as part of a guidance on fund naming could give investors the impression that the market has found a consensus on how to interpret this definition. Overall, we believe that there should remain a certain level of freedom on how to develop a sustainable investments approach, in order to foster innovation in this space, and to do not limit such approaches to the boundaries of the definition of sustainable investment according to Article 2 (17) SFDR. We are convinced this is in investors' best interests that a diversity of sustainable investments approaches remains. At the same time, clarity is needed on definitional and methodology issues to ensure support and confidence in sustainable investments overall. A list of key questions that has been sent to the EU commission on sustainable investments is still pending. Also in this context, definitions and threshold reference basis should be in any case quite clear to ensure comparability of products.
* It is not clear if and if so, how investments in sovereign bonds can find their place in the “sustainable investments” definition given by Article 2 (17) SFDR, while governments play a systemic role in the sustainable transition.
* While investing in sustainable investments consist in screening companies based on certain positive criteria, we believe other strategies such as active ownership can contribute to the transition to a more sustainable world. We would like to refer to the following research paper, which shows how that in a competitive world “exit” (understood as exclusion, divestment of brown firms) is less effective than voice (understood as active ownership) in pushing firms to act in a socially responsible manner (Broccardo, Eleonora, Oliver Hart, and Luigi Zingales. "Exit versus voice." Journal of Political Economy 130.12 (2022): 3101-3145). There are other ongoing research works on the potential positive im-pacts of tilting. For example, the following working research paper shows that a more effective strategy may be tilting, understood as “holding a brown stock if the firm has taken a corrective action” (Edmans, Alex and Levit, Doron and Schneemeier, Jan, Socially Responsible Divestment (November 11, 2022). European Corporate Governance Institute – Finance Working Paper No. 823/2022, Proceedings of the EUROFIDAI-ESSEC Paris December Finance Meeting 2022).
* Finally, as of today, we fear that SFDR does not adequately recognize the value of investing in companies in transition outside of transitional activities under the EU taxonomy. Under the EU Taxonomy, criteria have been defined for the definition of transitional activities. These activities have a dedicated place in the SFDR RTS precontractual and periodic annexes. However, there is not such space for companies transitioning towards a contribution to social objectives or towards activities that contribute to an environmental objective not aligned with the EU Taxonomy. As of today, it is not clear whether investments in such companies can be recognized as sustainable investments under the proposed definition. At the same time, we believe investing in such companies, for instance combined with a sound active ownership strategy, should be considered a “sustainable” investing approach.

We believe there are diverse ways of building an investment strategy that fosters the transition towards a more sustainable world. If a fund has an ESG-related term in its name, at least the majority of the assets in scope (assets excluding cash and derivatives that do not have security exposure) should have ESG criteria applied, and no investments should be made in contradiction with the Sub-Fund’s name.

We believe evaluation criteria should be implemented consistently by national competent authorities and communicated transparently to financial market participants. It would be desirable that the national authorities that will evaluate these strategies develop a common and coherent understanding for the evaluation. <ESMA\_QUESTION\_FUNA\_3>

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

<ESMA\_QUESTION\_FUNA\_4>

Yes, we believe there are alternatives, and we would like to refer to our answers to Question 1 and 2.

To summarize, we propose the following points:

* At least 50% of the Sub-Fund’s NAV excl. cash and derivatives that do not have security exposure (direct and indirect exposures to securities) have the ESG criteria applied.
* The remaining investments are not in contradiction with the fund name (minimum safeguards).

We believe evaluation criteria should be developed by national competent authorities and applied consistently, taking into account the diversity of investment strategies that can be designed to foster the transition towards a more sustainable world.<ESMA\_QUESTION\_FUNA\_4>

1. : 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>

We recognize the need of having thresholds in order to reiterate the importance of having the ESG criteria applied to at least 50% of the Sub-Fund’s NAV excl. cash and derivatives that do not have security exposure (direct and indirect exposures to securities). We believe the guidelines should take into account the diversity of approaches.<ESMA\_QUESTION\_FUNA\_5>

1. : 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>

Yes, if a Sub-Fund has an ESG-related term in its name, then we believe an investor should not expect in-vestments in contradiction with the name in the Sub-Fund. Accordingly, we also believe applying minimum safeguards for Sub-Funds with ESG or sustainability-terms is a good way to ensure this.

However, we do not believe applying standardized exclusion with a strong focus on the environmental side will help to ensure the Sub-Fund invests in “companies with policies, practices, or characteristics that are consistent with ESG standards”, and accordingly “help to prevent potential greenwashing risk in fund names”.

Instead, we believe financial market participants should develop, disclose (in the SFDR precontractual and periodic disclosures) and apply minimum safeguards, in order to ensure no investments are made in contra-diction with the Sub-Fund’s name. For example, if a Sub-Fund is promoting a strategy on “good health and well-being”, we believe it should avoid investments in companies that are “significantly harming health”. At the same time, we also recognize that companies are actively transitioning towards better practices. We do not believe these companies should be excluded by applying these minimum safeguards<ESMA\_QUESTION\_FUNA\_6>

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

<ESMA\_QUESTION\_FUNA\_7>

Yes, we believe the use of derivatives should be regulated in order to be aligned with the ESG approach, which is in line with SFDR RTS Recital 20 ("In particular, financial market participants should explain how the use of derivatives is compatible with the environmental or social characteristics that the financial product promotes or with the objective of sustainable investment.").

When it comes to using derivatives in a product that integrate ESG criteria, we believe:

* the fund should not benefit from harmful activities due to derivative exposure
* minimal safeguards should be put in place for the derivatives portion of such products.

Accordingly, to address these potential moral and ethical considerations from the fact that a financial product use derivatives to actively seek exposure to harmful activities, we recommend to apply the following rules:

* With the absence of a regulatory guidance and a recognized market practice on ESG integration for derivatives, we recommend excluding derivatives on broad equity and fixed income market indices from the ESG process (from assets considered “aligned with the environmental and/or social characteristics”) and to focus on the collateral pool.
* The use of derivatives on single underlying, a similar selection process as for direct investments must be followed.

Regarding derivatives with ETFs as their underlying, the possibility to use derivatives on ESG indices should be monitored when this market matures, but we do not recommend to apply rules on these instruments as of today.<ESMA\_QUESTION\_FUNA\_7>

1. 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>

We recommend to apply the market value for the purpose of the calculations mainly for transparency reasons.<ESMA\_QUESTION\_FUNA\_1>

1. Are there any other measures you would recommend for derivatives for the calculation of the minimum proportion of investments?

<ESMA\_QUESTION\_FUNA\_2>

We recommend counting these instruments, based on their market value, under “#2 Other” investments.<ESMA\_QUESTION\_FUNA\_2>

1. : 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>

While Vontobel Asset Management does not manage passive funds, we believe these funds should comply with the same requirements, to avoid confusion on the investors’ side.<ESMA\_QUESTION\_FUNA\_8>

1. : 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>

We believe funds that use synthetical replication should not be considered funds that promote ESG criteria, as the flow in real world economic activities are not guaranteed. Making use of such methods is not in line with the purpose of sustainable finance.<ESMA\_QUESTION\_FUNA\_9>

1. : Do you agree of having specific provisions for “impact” or impact-related names in these Guidelines?

<ESMA\_QUESTION\_FUNA\_10>

We believe any ESG related word in a fund name should be subject to the same principles:

* The majority % of investments to be applied by national competent authorities should be in line with the name.
* Remaining investments should not be in contradiction with the name and minimum environmental and social safeguards should be applied.
* Evaluation criteria should be implemented by national competent authorities, allowing financial market participants to demonstrate the “impact” character of their strategy. It would be desirable that the national authorities that will evaluate these strategies develop a common and coherent understanding for the evaluation of what should be considered a sustainable financial product.

We also note that the ESMA had provided examples of funds that can have the word “impact” in their name in the Supervisory Briefing of May 2022: “A 'climate impact’ fund investing in companies with business in activities focused on enabling the adaptation to, or mitigation of, climate change can refer to the impact in its name”. We support this approach.<ESMA\_QUESTION\_FUNA\_10>

1. : Should there be specific provisions for “transition” or transition-related names in these Guidelines? If yes, what should they be?

<ESMA\_QUESTION\_FUNA\_11>

We believe any ESG related word in a fund name should be subject to the same principles:

* The majority ***%*** of investments to be applied by national competent authorities should be in line with the name.
* Remaining investments should not be in contradiction with the name and minimum environmental and social safeguards should be applied.
* Evaluation criteria should be implemented by national authorities, allowing financial market participants to demonstrate the “transition” character of their strategy. It would be desirable that the national authorities that will evaluate these strategies develop a common and coherent understanding for the evaluation of what should be considered a sustainable financial product.

Regarding this particular term, we believe there should be the possibility to have the words “sustainable transition” in a fund name to characterize a strategy that focus on issuers that are in transition or that contribute to the sustainable transition.<ESMA\_QUESTION\_FUNA\_11>

1. : 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 the scope should be extended to financial products, and not only funds. A consistent approach is easier to navigate for investors.<ESMA\_QUESTION\_FUNA\_12>

1. : 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>

A transitional period of 6 months sounds reasonable under two conditions:

* 6 months are given to the Financial Market Participants to work on potential amendments, excluding time to be allocated to the filing process. It may be more realistic to have a transition period of 12 months.

Clarity on all key aspects is available. For example, if the concept is based among other on “sustainable investments” as defined by Article 2 (17) SFDR, Financial Market Participants should have sufficient clarity on this concept. We are specifically referring to the questions that have been asked to the EU commission by the ESAs and that have not been answered yet.<ESMA\_QUESTION\_FUNA\_13>

1. : 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>

As the fund name would not be used anymore for marketing purposes, we believe this guidance does not need to be applied to these funds anymore.<ESMA\_QUESTION\_FUNA\_14>

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

<ESMA\_QUESTION\_FUNA\_15>

As of today and based on the open questions on the concept of “sustainable investments”, it is not possible to assess precisely the impact of the introduction of such guidelines. However, the large majority of Article 8 funds do not currently comply with the guidelines. For instance, based on data provided by Morningstar via the EET, as of January 2023, above 70% of Article 8 funds do not comply with the proposed guidelines. Accordingly, implementation costs should be expected.

Considering the current regulatory developments on ESG fund naming conventions in diverse regions (Switzerland, USA, UK,…) that do not currently converge, two consequences can be expected:

* Global investment managers might be forced to develop different ESG products by region. The development and launch of these products will induce product management related costs.
* Financial Market Participants having their funds domiciled in European Union could have a competitive disadvantage compared to peers that have their funds domiciled in other regions that are less strict in terms of naming conventions.

There is no definition or exhaustive list of “ESG-related words” but only very limited examples. We could expect some different views/subjective assessment on a same word (depending also in the investing strategy of the Sub-Fund).<ESMA\_QUESTION\_FUNA\_15>

1. : 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>

Depending on the outcome of these guidance, we expect a significant number of internal stakeholders involved, to analyse and implement the changes, resulting essentially in personnel costs. As we follow a robust governance process, these changes will be subject to internal and external approvals. We may have recourse to external consultants supporting us in the implementation, especially the update of the documentation.

Additionally, we currently observe the development of diverging guidance on fund naming across regulations. We believe costs will result from such conflicting regulations. As we are acting as a glob-al investment manager, we may have to launch different financial products by region, in order to remain competitive locally. Launching such local financial products will require to build up competence and address these local requirements, which will in turn result in additional costs at all levels of our value chain (including investment management, product management, legal, monitoring of local investment criteria).

The implementation of additional specific ESG criteria will be linked to significant data costs.

Going forward, we expect a significant lengthening of new fund creation timescales.<ESMA\_QUESTION\_FUNA\_16>