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| 18 November 2022 |

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

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| --- | --- |
| Name of the company / organisation | Association of the Luxembourg Fund Industry |
| Activity | Other Financial service providers |
| Are you representing an association? |[x]
| Country/Region | Luxembourg |

# Introduction

Please make your introductory comments below, if any:

<ESMA\_QUESTION\_FUNA\_0>

The Association of the Luxembourg Fund Industry (ALFI) represents the face and voice of the Luxembourg asset management and investment fund community. The Association is committed to the development of the Luxembourg fund industry by striving to create new business opportunities, and through the exchange of information and knowledge.

Created in 1988, the Association today represents over 1,500 Luxembourg domiciled investment funds, asset management companies and a wide range of business that serve the sector. These include depositary banks, fund administrators, transfer agents, distributors, legal firms, consultants, tax advisory firms, auditors and accountants, specialised IT and communication companies. Luxembourg is the largest fund domicile in Europe and a worldwide leader in cross-border distribution of funds. Luxembourg domiciled investment funds are distributed in more than 70 countries around the world.

We thank ESMA for the opportunity to participate in this consultation regarding Guidelines on funds’ names using ESG or sustainability-related terms.

<ESMA\_QUESTION\_FUNA\_0>

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

<ESMA\_QUESTION\_FUNA\_1>

ALFI agrees that it is of utmost importance to protect investors against unsubstantiated or exaggerated sustainability claims and to have harmonized requirements to achieve this goal.

However, we are of the view that the suggested approach (linking ESG-related names to specific minimum thresholds on the fund’s holdings) is not the most appropriate way to foster this. In particular, we have some concerns regarding the underlying terminology as well as the methodology to construct the threshold mechanism and the concrete percentage used. Moreover, we have concerns regarding the timing, in particular the short transitional period, and scope of the proposed guidelines.

Regarding the thresholds proposed, it is not fully clear to us based on which considerations ESMA has chosen the concrete percentages. In addition, we do not believe that a calculation solely on the base of holdings allows for a comprehensive understanding on whether / how the investment process reflects the strategy that is marketed and is being reflected in the fund’s name. Only focusing on thresholds could eventually also be misleading for the investor whereby it is transparency on underlying investment processes and methodologies applied to meet the respective environmental / social characteristics / sustainable investment objectives that the fund is committed to including in its name that can guide investors in informed decisions and address greenwashing risks. It follows that we are not convinced that the use of quantitative thresholds will foster the regulatory objectives to promote convergence, transparency or tackling the risk of greenwashing. We suggest instead to focus prudential supervision on the requirement for clear demonstration of the underlying methodologies and the binding elements that justify outcomes, which in combination with prudential supervision is the main way to ensure that funds with ESG/sustainability-related terms in their name provide adequate transparency around the underlying investment methodologies and processes used (reference is made to our response under question 4).

Furthermore, the terminology “ESG-related words” and “’sustainable’ or any other sustainability-related term” on which the calculation is based is very broad and not sufficiently clearly defined. It leaves room for ambiguity. Accordingly, the interpretation and subsequent methodologies used to calculate these thresholds may vary largely per fund and jurisdiction. The outcome of the respective assessments will consequently not be comparable. We therefore suggest to avoid linking at this stage the criteria to terms that remain to be further clarified. For instance, the term “sustainable investments” is expected to be further clarified at EU level, therefore, we suggest in particular that the notion of “sustainability-related words” used in the guidelines remains as close as possible to the terminology of article 2 (17) SFDR, and wait until the time such clarification is in place to assess the need to include this term in the criteria. To complement clarifications, we propose to provide a clear, non-exhaustive list of examples for fund names that would fall under each category, including a clear distinction between “ESG-related words” and “sustainability-related words” and how this distinction ties in with funds disclosing under article 8 and article 9 SFDR.

Regarding the timing to issue guidelines on fund naming, it should be kept in mind that key definitions are still not completely clarified (e.g. sustainable investments/impact investments/promotion of ESG characteristics). This is also to be seen in the context that both the EC and ESAs are still in the process of publishing Q&As and further guidance to clarify metrics and application in relation to the SFDR and Taxonomy Regulation. Moreover, Commissioner McGuinness has recently announced a broad assessment of SFDR. From the recent open hearing on 23 January, we understand that ESMA is aware of these concerns but may nonetheless want to reconsider whether the outcome of these developments should not be awaited before applying rules on fund naming.

We note that ESMA’s intention is that the guidelines are not meant to interfere with SFDR, however they are nonetheless likely to have a significant impact on the regulatory approach taken in respect of SFDR generally.

To conclude, we believe a more structured approach to reviewing and amending the sustainable finance framework would be beneficial for all stakeholders concerned rather than by way of an ad hoc and piecemeal approach.

<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>

We refer to our answer to Q1 and Q4 in which we suggest an alternative methodology and criteria to construct the threshold mechanism. However, if the mechanism proposed by ESMA will be implemented, we would like to address the following points.

With regard to the underlying terminology of ESG and Sustainability related terms, and as regards the proposed percentage of at least 80% of a fund’s investments that will need to be used to meet the environmental or social characteristics or sustainable investment objectives, it is not fully clear to us based on which considerations ESMA has chosen the concrete approach / percentage. We believe it to be beneficial to clarify this. Moreover, it should be determined on which basis the 80% minimum threshold is calculated (i.e. aggregate commitments, NAV) and as of which point in time (i.e. after the transition period or from day-1).

Furthermore, we invite ESMA to consider whether the proposed threshold could contradict existing regulatory limits. We note as an example that the CSSF FAQ on the Law of 17 December 2010 provide that UCITS funds may temporarily hold ancillary liquid assets beyond 20% under certain conditions in exceptionally un-favourable market conditions (for instance in highly serious circumstances such as the September 11 attacks or the bankruptcy of Lehman Brothers in 2008 – see Question 14, p. 19 of the CSSF’s FAQ). As recognised by ESMA during the open hearing, there may be situations when a fund may be below the threshold due to unforeseen market movements for example (such a relatively high proportion of cash during a market downturn) and we would recommend that this possibility is clearly mentioned in the guidelines. We would also like ESMA to reconsider its position expressed during the hearing that closed-ended funds with an investment ramp up period during which the relevant threshold would not be met, would not be able to use ESG-related names as they would be in breach of the requirement to maintain the threshold at all times, even during the ramp up. We would welcome a more flexible approach in this regard.

Should ESMA wish to maintain the threshold approach, we believe that the concrete threshold to be applied should be lower (e.g. 60%). This would allow to reflect the current market situation. Currently, there are various data sources used and different methodologies applied to determine these percentages. “For example, two approaches that may lead to higher or lower levels of sustainable investments: 1) revenue-weighted approach, i.e. the entirety of a sustainable company is considered, or 2) pass-fail approach, i.e. only the proportion of revenue attributed to those activities may be applied (reference is made to Q1 addressed by ESAs to EC the European Commission and Morningstar 2022 Q4 review, p. 35). As another example, one could mention the Taxonomy-alignment calculation. In absence of data, estimates, e.g. based on proxies may be used which can be ambiguous, i.e. may be different depending on the provider reflecting the different methodologies and data used (cf. recent ESMA report TRV Risk Analysis on EU Ecolabel, footnote 18, page 6).

In particular, many different approaches are used as regards investments by article 8 funds. The EC Q&A on SFDR of July 2021 also clearly stated that article 8 SFDR remains neutral in terms of design of financial products. Our recommendation is also to make a distinction between different categories of assets and that the thresholds that would be retained would be lower in case of high yield / emerging / small caps.

As a final point, we noted the introduction of a requirement to treat certain deviations from the thresholds as breaches that should be corrected, respectively may be considered as risk indicator by NCAs (paragraphs 21 and 22 of the guidelines). We believe that neither the proposed guidelines on fund naming nor the supervisory briefing note on sustainability risks and disclosures are adequate means to cover the topic of investment breaches.

<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 refer to our answer to Q1 and Q4 in which we suggest an alternative methodology and criteria to construct the threshold mechanism. However, if the mechanism proposed by ESMA will be implemented, we would like to raise the following points.

From a first reading of the consultation paper, we understood that “within” the 80% of investments to “meet the characteristics/objectives” at least 50% of minimum proportion of sustainable investments should be allocated in order for funds to use the word “sustainable” or any other sustainability-related term in the name of the fund (p. 9, paragraph 15 b) of the consultation paper). However, ESMA explained during the open hearing that the 50% should be applied on the total of all investments. We would suggest to explicitly clarify this requirement in the guidelines in order to avoid any uncertainty regarding the approach.

In addition, we believe that a lower percentage of e.g. 30% or 35% sustainable investments can be meaningful for a sustainable fund. A balanced approach remains important as there is a risk of unnecessarily excluding a variety of different approaches to sustainability, such as funds making investments on a pathway to transition to being sustainable, high yield funds, emerging market funds, small caps, private assets etc. It is important to offer investors a broad range of sustainable funds in order to foster the objective to re-orient private capital flows to sustainable investments. Therefore, we propose that, as long as there is a meaningful contribution to sustainable investments, it should be possible to include the term “sustainable” in the name of the fund without imposing a hard limit of 50% sustainable investments. We believe that such an approach would not mislead investors as we would expect that an investor will indeed look beyond the name of the fund and will be interested to learn about the actual strategy and investments.

Referring to the requirement in paragraphs 21 and 22 to treat certain deviations from the thresholds as breaches which should be corrected, respectively may be considered as risk indicator by NCAs, we believe that neither the proposed guidelines on fund naming nor the supervisory briefing note on sustainability risks and disclosures are adequate means to cover the topic of investment breaches.

<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>

As mentioned under our response to question 1, we suggest that rather than focussing on hard limits, requiring clear demonstration of the underlying methodologies and the binding elements of the fund’s investment strategy, in combination with supervisory focus on these aspects is a more appropriate mechanism to address greenwashing risks and ensure investor protection. The main concept should be on transparency regarding the underlying investment processes and methodologies applied to meet the respective environmental / social characteristics / sustainable investment objectives that the fund committed to and that are reflected in the fund’s name.

Transparency requirements would take into account the importance of taking a balanced approach as outlined in our answer to Q2 and Q3.

Should however the approach suggested by ESMA be maintained in the final guidelines, we refer to our proposals under Q2 and Q3 on the application of the two thresholds.

<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 would like to refer to our response to Q1 and Q4.

<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>

We do not see the need for any additional safeguards other than those listed by article 8 and 9 funds themselves and the ones applicable by virtue of a regulation. If any minimum safeguards were to be introduced, this should be done by way of an update of SFDR itself.

<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>

As there is more regulatory clarity needed on the treatment of derivatives under SFDR, we would suggest to exclude these from the application of the guidelines until such clarity has been provided. In general, we suggest to apply rules on fund names only for investments in transferrable securities. For other assets such as derivatives, sovereign bonds, cash/cash equivalents and given lack of clarity as to their treatment we suggest not including them in the method/calculation for the purpose of these Guidelines.

<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>

TYPE YOUR TEXT HERE

<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>

TYPE YOUR TEXT HERE

<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>

There are currently no clear requirements regarding the methodologies used by index providers. In addition, more regulatory clarity is needed on the treatment of indexed funds under SFDR. Therefore, we would suggest to exclude these funds from the application of the guidelines until such clarity has been provided.

<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>

As there is more regulatory clarity needed on the treatment of synthetic replication under SFDR, we would suggest to exclude these from the application of the guidelines until such clarity has been provided.

<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 agree on having specific provisions for “impact” or impact-related names in the guidelines. We appreciate that ESMA defines the term “impact” in its guidelines (paragraph 20) as to the best of our knowledge there is no official regulatory definition in guidelines or legislation on European level yet (notwithstanding the use of this definition in the ESMA supervisory briefing of 17 November 2022). We note that ESMA uses one definition provided by the [global impact investing network](https://thegiin.org/impact-investing/).

<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 are of the opinion that specific provisions for “transition” or transition-related names would be pre-mature. There is still a lack of legal clarity on which assets qualify as “transitional” respectively under which circumstances investments in transitional activities can be considered as contributing to an environmental or social objective respectively as sustainable investments. We refer in particular to the ESAs questions to the European Commission of 9 September 2022.

Should specific provisions of the guidelines be linked to article 10 (2) of the Taxonomy Regulation covering transitional activities which substantially contribute to climate change mitigation and the respective Climate Delegated Act, it is to be noted that there is still a lack of data reported by investee companies.

Keeping the above in mind, we suggest, instead of establishing specific provisions for “transition” or transition-related names, to await the expected clarifications as well as a more mature data environment. Should nonetheless such provisions be included in the guidelines, we suggest to require transparency on the underlying investment process of a fund regarding investments in transitional activities and how these are implemented to meet the environmental or social characteristics or sustainable investment objectives as reflected in the fund’s name.

<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>

ALFI would indeed see merit in having similar guidance for other financial products. We do not see any particular reason why investment funds should be singled out while the current discussion goes even further than the scope of products under SFDR, covering, e.g. also benchmarks. Enlarging these proposals to other sectors would provide for a welcomed level-playing field.

<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>

We note from the hearing that ESMA is aware of the challenges in terms of timing but we would like to briefly recap. The implementation time provided to market participants is likely to be challenging. It will take time until market participants become familiar with the new requirements and establish market practices in this regard. An understanding of the new requirements and their nuances will also have to be developed by NCAs. Market participants’ review of fund names would require an extensive check of the existing methodologies and data used by funds to determine the percentages of investments to meet the environmental or social characteristics or sustainable investment objectives. In addition, a potential subsequent need to amend fund names and related administrative effort will be very time-consuming as well: a name change of a fund may imply a change in the constitutional documents of the fund requiring – in most cases – a decision of the general meeting with certain quorum and majority requirements and, for regulated funds, an NCA pre-approval. Finally, there may be additional workstreams concerned by the changes made, e.g. when it comes to the preparation of the European ESG Template (EET).

Therefore, we are of the view that the transitional period of six months for funds launched prior to the application date would not be sufficient. We propose a transitional period of 18 months from the application date of the guidelines.

<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>

We are of the view that closed-ended funds should be excluded provided they are closed to investors prior to the application date of the guidelines, as a change in fund name would not provide an added value for the investor.

<ESMA\_QUESTION\_FUNA\_14>

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

<ESMA\_QUESTION\_FUNA\_15>

If the guidelines will be issued as proposed including hard thresholds, we expect the following impact:

* As there is a lack of clarity on key definitions for the underlying terminology, interpretations and methodologies by both NCAs and industry may vary largely. The establishment of thresholds would consequently, at this stage, not provide for more comparability, convergence, transparency or less risks of greenwashing. It may eventually also render the EU marketing of funds more difficult.
* The proposed percentage of thresholds would lead to all kinds of nuances in meeting environmental or social characteristics or sustainable investment objectives not being reflected in the funds’ names anymore.
* Two cumulative requirements may increase the risk of confusion on investor side.
* The foreseen transition period will lead to challenges as it will take time and resources
	+ to interpret the new requirements and establish market practices
	+ to review fund names, underlying methodologies and data used
	+ to implement amendments to fund names and re-publish documentation
	+ to implement the changes made by related workstreams e.g. EET preparation.

Enlarging the guidelines to other sectors would provide for a welcomed level-playing field.

<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>

We expect that there will be legal and compliance costs for funds and asset managers.

<ESMA\_QUESTION\_FUNA\_16>