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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 | BEUC, The European Consumer Organisation |
| Activity |  |
| Are you representing an association? |  |
| Country/Region | Belgium |

# Introduction

Please make your introductory comments below, if any:

<ESMA\_QUESTION\_FUNA\_0>

BEUC, the European Consumer Organisation shares ESMA’s concerns about greenwashing in retail investment products and welcomes ESMA's efforts to use supervisory tools to curb it. We further agree that names are an important means to communicate information about a fund to retail investors and that the name is often the first fund feature they take note of. Misleading fund names are therefore a real consumer protection issue that requires action in the form of supervisory requirements for funds that use terms like 'sustainable', 'ESG', 'green' etc. in their names.

However, it is important to acknowledge the limitations of this approach, which should be a stopgap measure until such time as a more robust legal framework for sustainable investment products is in place. For example, the German consumer association VZBV has conducted research by searching for sustainable funds on online portals. It found some funds with names that were clearly sustainability-related, like “klimaVest” or “Greenfolio”, but also many funds that had neutral names like “Bond Deutschland 2023/2029” or “GLSonlineinvest” but were nevertheless advertised as ESG- or Impact-Funds. When a retail investor's first contact with sustainable investment offers is made through an online comparison or search portal, he or she will be shown all funds that are (self-)classified as somehow sustainable or ESG, regardless of the name. The names are still important and it makes sense to restrict the current naming-freedom, but it may be only one of several fund characteristics that the consumer sees. Supervisory action with regard to greenwashing in distribution channels for investment products is therefore equally necessary. (The recently closed joint ESAs consultation on greenwashing in financial services is also looking into the distribution channel, and we hope that there will be follow-up actions.)

In the longer run, retail investors will be best served by labelling, classification and/or grading schemes for investment products that are based on standardised definitions and criteria. The UK Financial Conduct Authority, for example, is currently exploring the option of defining categories and labels for different types of sustainable investment products. Another option could be the use of a colour grading system similar to the well-known EU energy label, with colours ranging from dark-green for most energy efficient to dark-red for least efficient. Independent third-party verification of these classifications or grading would further boost the credibility and trust in sustainable investment products. The SFDR in particular needs a thorough revamp, especially through the introduction of minimum criteria for Article 8 and Article 9 products. The [recommendations](https://www.beuc.eu/sites/default/files/publications/beuc-x-2022-027_joint_recommendations_for_min_criteria_for_sustainable_investments_and_products_with_esg.pdf) made by BEUC and other civil society organisations in 2021 remain relevant in that regard.<ESMA\_QUESTION\_FUNA\_0>

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

<ESMA\_QUESTION\_FUNA\_1>

Yes, we agree with the introduction of quantitative minimum requirements for funds that use terms like 'sustainable', 'ESG', 'green', 'climate' etc. in their names, but we do not agree with the distinction between funds that use the term 'sustainability' or related terms, and those that use ESG-related terms.

ESMA proposes that funds that use ESG- or ESG-related terms in their names, like 'climate change solutions fund' or 'biodiversity equity fund‘, are subject to less stringent rules than funds that use the word 'sustainable' or other sustainability-related terms, e.g. 'sustainable water equities fund‘ or 'sustainable society fund'. This distinction appears based on the implicit assumption that the term 'sustainability' contains a stronger, more ambitious promise than 'mere' ESG words and should therefore be held to a higher standard.

From a retail investor perspective, there is no reason to assume that naming differences like these have an influence on how people perceive the sustainability promise of an investment product. Another problem with the special rule for ‘sustainable’ names is that it can be avoided too easily by substituting that term with an ESG-term. To use the example from the ESMA paper: it would be possible to rename the ‘Sustainable Society Fund’ to something like ‘Fair and Inclusive Society Fund’. Would that make the fund’s name less attractive and greenwashy? We suggest therefore to eliminate the distinction and apply the same set of rules to all sustainable/ESG/Green investment funds, regardless of which ESG- or sustainability-related term they use. By this we refer to both the minimum share of investments that must be used to meet the social or environmental investment objective and the minimum share of sustainable investments as defined by Article 2(17) of the SFDR. The answers to subsequent questions in this questionnaire have to be understood in light of our rejection of the afore-mentioned distinction. (It is worth noting that neither the German BaFin’s proposed [naming guidelines](https://eur02.safelinks.protection.outlook.com/?url=https%3A%2F%2Fwww.bafin.de%2FSharedDocs%2FDownloads%2FDE%2FKonsultation%2F2021%2Fdl_kon_13_21_WA4_Leitlinien_Investmentvermoegen.pdf%3F__blob%3DpublicationFile%26v%3D6&data=05%7C01%7Cdavide.tassi%40esma.europa.eu%7C5973fd48ac2f4a413e8708db09cc8301%7Ce406f2684ae74c80899402493da00c03%7C0%7C0%7C638114546373221148%7CUnknown%7CTWFpbGZsb3d8eyJWIjoiMC4wLjAwMDAiLCJQIjoiV2luMzIiLCJBTiI6Ik1haWwiLCJXVCI6Mn0%3D%7C3000%7C%7C%7C&sdata=5g4B6NSgFiiC7daS7Xd2L9wlwcW0zWes2IgD90sbIdE%3D&reserved=0), nor the UK’s [FCA proposals](https://eur02.safelinks.protection.outlook.com/?url=https%3A%2F%2Fwww.fca.org.uk%2Fnews%2Fpress-releases%2Ffca-proposes-new-rules-tackle-greenwashing&data=05%7C01%7Cdavide.tassi%40esma.europa.eu%7C5973fd48ac2f4a413e8708db09cc8301%7Ce406f2684ae74c80899402493da00c03%7C0%7C0%7C638114546373377366%7CUnknown%7CTWFpbGZsb3d8eyJWIjoiMC4wLjAwMDAiLCJQIjoiV2luMzIiLCJBTiI6Ik1haWwiLCJXVCI6Mn0%3D%7C3000%7C%7C%7C&sdata=hNjqDSHXWpSlUPwfkkAa8SWE4izTNTxVkvS7toWg4oA%3D&reserved=0) for sustainability disclosure requirements and investment labels use this distinction.)

<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 have no strong opinion about the exact quantitative level, but we note that there does not seem to be a clear rationale behind the 80% figure. If a fund is marketed as ESG, green or sustainable, why should 20% of its assets be allowed to be deployed in a way that does not further the fund's investment objective? There may be some legitimate reasons for exempting a share of fund assets, e.g. because they are used for legitimate hedging, but 20% seems on the high side for that. We would therefore suggest adjusting the 20% exemption so that it can only be used for legitimate purposes that do not contradict the fund's overall sustainable investment objective. We expect that such a review would result in an exemption of less than 20%, and therefore a higher minimum proportion of assets that must be deployed in pursuit of the investment objective.

However, more important than the exact figure for the minimum proportion is that the remaining assets be subject to the do-no-significant-harm principle, similar to what is suggested in paragraph 18 of the proposed guidelines. However, we do not feel that the exclusion list in Article 12(1f.) of the Benchmark Delegated Regulation 2020/1818 is a suitable tool for that. (Please consult our response to question 6 of this questionnaire for more details.)

<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>

Yes, but the minimum share should increase over time to reflect the fact that the universe of sustainable investment is likely to grow over the coming years, which will make it easier to create investment products that are nearly fully sustainable. Moreover, since we do not support drawing a distinction between investment funds that use ESG-related terms and investment funds that use sustainability-related terms we suggest that *all* funds that use terms like ‘ESG’, ‘sustainable’, ‘green’, ‘climate change’ and so on their names should have to apply the minimum share of sustainable investments requirement. <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>

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<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>

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<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, we agree with the introduction of minimum safeguards. Not all consumers who consciously buy a sustainable retail investment product do so because they want to be part of the solution, but because they want to avoid being part of the problem by contributing through their investments to global environmental and social problems. All products that use terms like 'sustainability', 'ESG' or 'green' in their names should therefore be subject to the do-no-significant-harm principle, which can indeed be operationalised through exclusion lists. Therefore, we support the approach taken in paragraph 18 of the proposed guidelines (Annex III of the consultation paper), although we suggest strengthening the language from a mere recommendation to a supervisory expectation. We also note a discrepancy between paragraph 18 of Annex III and paragraph 19 of the consultation paper. The latter suggests applying the exclusion criteria only to that part of a fund’s assets that are not deployed in pursuit of the sustainable investment objective, while the former appears to apply to the entire fund. We suggest making it clear that exclusion criteria apply in principle to all fund assets. (We realise that this cannot apply in the same way to create problems for so-called transition funds. Please refer to our response to Q11 for details.)

Moreover, instead of using the exclusion criteria for Paris-aligned Benchmarks in the Benchmark Regulation Delegated Regulation we suggest drawing on the list of exclusions in the latest version of the [JCR technical report](https://susproc.jrc.ec.europa.eu/product-bureau/sites/default/files/2021-03/2021.03.05%20-%20EUEL%20financial%20products%20-%20Technical%20Report%204%20FINAL.pdf) that sets out criteria for an EU Ecolabel for retail financial products. This list is more comprehensive and well-elaborated than the exclusion criteria for the BMR and is more in line with what consumers would expect from a sustainable investment product.<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>

TYPE YOUR TEXT HERE

<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>

Yes, we agree.

<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>

Yes, we think it makes sense to distinguish between synthetic and physical replication for index-tracking funds. ESMA should explore whether synthetic funds should be allowed to be called 'sustainable' etc. at all, seeing as there is no connection between the companies in the synthesised index and the fund itself and therefore no sustainability-relevant effect worth speaking of.<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>

Yes. Many sustainability-minded retail investors do not only wish to avoid doing harm, they want to make a positive impact through their investment decisions. There is no shortage of products that promise to do so, but these promises are frequently unsubstantiated and questionable. It makes sense, therefore, to have specific guidelines for impact investment products.

However, the guideline for impact funds in paragraph 20 only requires that the investments be made 'with the *intention* to generate' (emphasis added) positive and measurable impact. This is not enough. If a fund is marketed with the implicit or explicit promise of making an impact consumers and supervisors can legitimately expect from the fund's manager that it can at least demonstrate a plausible link between the funds' asset selection and/or stewardship activities and material positive impacts on people or planet in its regulated marketing information. This can happen in a variety of ways. For example, if securities issued by companies in a nascent industry that genuinely contributes to sustainability are not sufficiently liquid, sustainable investor interest in them can improve liquidity and reduce the companies' cost of capital and help them invest more. Another possible impact mechanism is through sustained and systematic engagement with company managers to become more sustainable (investor stewardship). In contrast, some common investment strategies cannot normally claim to produce an impact, for example pure exclusion or negative screening strategies or best-in-class approaches. Any real-world effects of these approaches would be highly indirect and could not be legitimately attributed to the investment decisions.

Providers of impact products should also have to describe in their pre-sale information and periodic disclosures how they track and measure impact and report past performance.

None of this guarantees real world impact, which is even more difficult to ascertain. But in the absence of a regulation that defines impact in investment products and develops a framework to measure it, the stricter requirements suggested here would be a reasonable supervisory solution for the short and medium term. In elaborating the supervisory expectations vis-à-vis impact investment products, ESMA should draw on the substantial body of existing work and ongoing discussion, e.g. the work by the UK Financial Conduct Authority ([here](https://www.fca.org.uk/publication/consultation/cp22-20.pdf)), the 2Degrees Investing Initiative ([here](https://2degrees-investing.org/wp-content/uploads/2021/11/Impact-Potential-Green-Finance-Products.pdf)) or the in-depth study commissioned by the German consumer association VZBV ([here](https://www.vzbv.de/sites/default/files/downloads/2021/02/11/gutachten_wilkens_und_klein_nachhaltige_geldanlagen.pdf))..<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>

In principle, it would be highly desirable to have specific provisions for funds that use ‘transition’ or similar terms in their names. Similar to impact funds, the use of the term ‘transition’ suggests to retail investors that their investment will have a discernible effect on the real world, rather than simply not doing harm. However, this is hard to achieve and even harder to demonstrate, therefore there is a high risk of greenwashing or, at the very least, over-promising. However, the types of requirements that would be needed to ensure that ‘transition’ becomes a meaningful investment strategy that does not mislead retail investors probably go beyond the powers of the supervisor.

If we understand ‘transition funds’ in more or less the same way as the UK Financial Conduct Authority defines ‘sustainability improvers’, i.e. as investments in assets that are not sustainable now, but will hopefully be made sustainable in the future through investor stewardship, then the do-no-harm requirements or exclusions that should apply to all other types of sustainable investment funds cannot apply. In other words, transition funds would be allowed to invest unsustainably based on a promise that they will do what they can to change that. To make sure that a transition fund does what it promises, there should be a number of requirements, some of which may well exceed supervisory powers.

* There must be a clearly explained and plausible investment and stewardship strategy that contains, among other things, goals for measuring improvement as well as criteria for divestment from a company that does not improve sufficiently.
* The minimum proportion of fund assets that must be deployed in pursuit of the fund’s investment objective in accordance with paragraph 16 (Annex III) of the proposed guidelines.
* The minimum threshold of 50% of sustainable investments would not apply.
* While the do-no-harm or exclusion criteria that should apply to all other sustainable investment products would not apply to transition funds, different exclusion criteria could still apply. For example, a transition fund should not invest in, or divest immediately from, companies that expand fossil fuel extraction capacities.
* We are sceptical about an asset selection-only approach to transition, i.e., a fund that claims to promote the sustainable transition simply on the basis of an asset selection strategy that focuses on companies that have made transition, net-zero or similar claims and/or sectors in which there are tendencies towards transition, such as the automotive industry which is currently strongly moving towards electric vehicles. Transition names should normally refer to systematic and clearly described stewardship strategies.
* There should be clarity over whether the fund promotes transition of investee companies or broad economic transition towards internationally agreed goals, such as the climate goals of the Paris Agreement. Aiming for the former does not necessarily guarantee the latter. Funds with names that refer to the Paris Agreement, net-zero, the Sustainable Development Goals etc. would be of the latter type and should be held to a higher standard.

<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>

Yes, greenwashing is not restricted to investment products, therefore we would encourage issuing similar guidance for other financial products.

<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>

From a retail investor perspective, six months are a long time to correct mismatches between funds' names and their actual investment strategies and/or portfolios that amount to misleading information, but we understand that it is a compromise between the interests of investors and the need to give fund managers the time needed to make the necessary adjustments. As such we can agree to it.

<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>

Yes, the naming-related provisions should also apply to closed funds whose subscription period ended before the Guidelines become applicable. Closed-end funds are traded after initial offering is over, therefore names still matter. Moreover, customers who do not wish to sell their shares in a closed-end fund that use ESG or sustainability-related terms should be informed whether the fund they hold conforms, or not, to the more stringent requirements that the Guidelines will introduce.

<ESMA\_QUESTION\_FUNA\_14>

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

<ESMA\_QUESTION\_FUNA\_15>

We would expect the introduction of naming-related requirements, if well-designed and properly implemented, to have a positive effect on the market for investment products, although we expect this effect to be moderate. A more far-reaching reform of the regulatory framework, especially a full review of the SFDR, is needed to achieve more fundamental positive change. Moreover, the expected positive effects of the naming-related requirements hinge on their application and enforcement by supervisors. It should, for example, not be possible for a fund manager to evade these rules through a name change that maintains the sustainable 'sound' of the fund name and thus its marketing appeal, but puts it outside the area of applicability of the guidelines. Any sustainability/green/ESG fund name should be covered by these rules. The positive effects of the naming-related requirements could be amplified if flanked by supervisory action in other areas, especially the distribution of funds through online search and comparison portals.

In particular, we expect a clearer and more visible differentiation in the market for investment products between those that aim, in some way, for sustainability and traditional return-only products. Fund managers would have to think more carefully about the kind of product they are creating/offering because they would have to meet certain requirements when making a sustainable product, at least if that fact is also to be advertised through the product's name.

<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>

As stated in our response to Q15, we think that well-designed and well-enforced naming-related requirements, especially if flanked by supervisory action in other areas of the investment fund value chain, will lead to a clearer and more visible differentiation in the investment product markets. This would make it easier for retail investors to find the right type of product for them, even when they do not want to invest sustainably, but are looking for a conventional return-only fund.

Well-designed naming requirements that include a do-no-harm exclusion list would also contribute to the fight against greenwashing, because they define a minimum sustainability content that would reduce the frequent discrepancies between the promises contained in fund names and the reality of the fund portfolios and/or stewardship. That said, putting an end to greenwashing would require more far-reaching regulatory reform as well as exploring how existing mechanisms like the Unfair Commercial Practices Directive under the competence of the consumer authorities could complement the work of ESMA by providing a safety net to the sector specific requirements.

<ESMA\_QUESTION\_FUNA\_16>