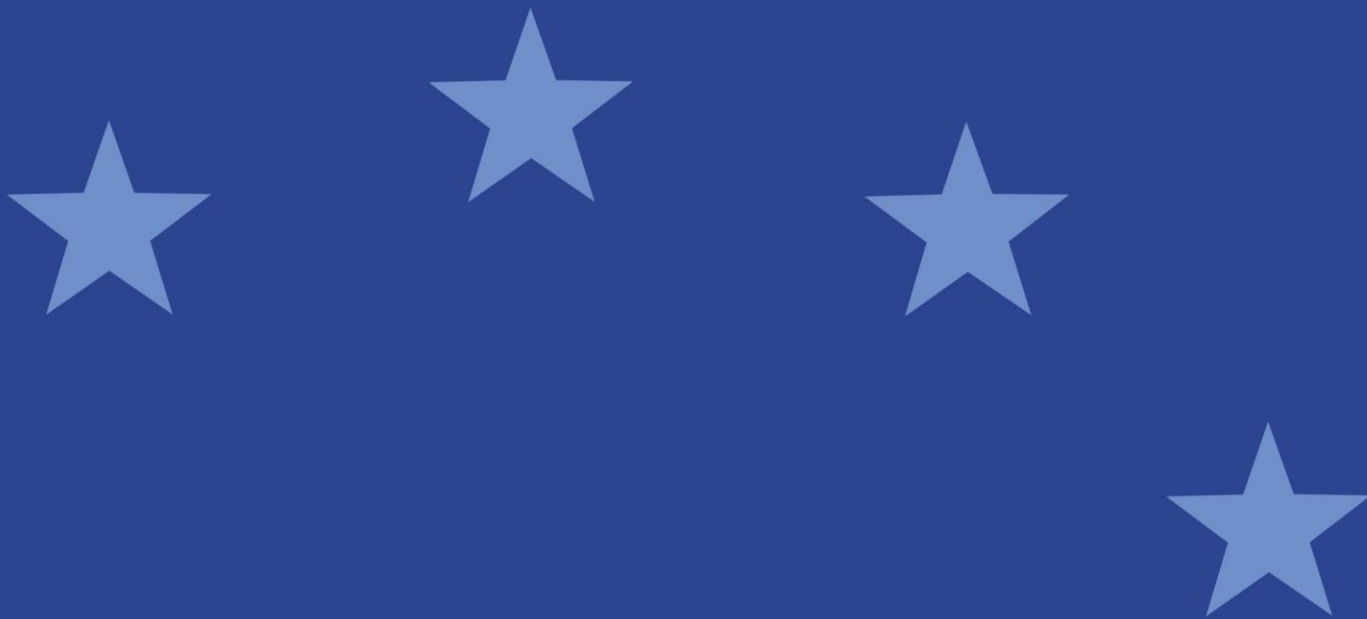


## **Reply form for the Consultation Paper on Guidelines for the use of ESG or sustainability-related terms in funds' names**



## 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 `<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	AFG
Activity	Investment Services
Are you representing an association?	<input checked="" type="checkbox"/>
Country/Region	France

## Introduction

**Please make your introductory comments below, if any:**

<ESMA\_QUESTION\_FUNA\_0>

AFG welcomes ESMA's consultation on Guidelines on funds' names using ESG or sustainability-related terms.

AFG agrees with the overarching objective of seeking to limit greenwashing allegations risks, increase legal certainty and avoid misleading information for investors.

This said, AFG would like to express some doubts over the timeline for this consultation. Indeed, the EU regulatory framework on sustainable finance is not complete yet and some initiatives are currently still being discussed:

- the ESAs are currently working on a report on « greenwashing ». An interim report is due in May 2023 and a final report in May 2024.
- some elements of the SFDR are still not clear enough: for instance, “sustainable investment” definition, “investments used to meet the environmental or social characteristics of the product” definition.
- the ESAs sent some questions to the European Commission (EC) on concepts included in this consultation (i.e. “sustainable investment”) and an answer is due by the EC in the first quarter of 2023.
- the EC is supposed to be working on minimum criteria for article 8 and article 9 products.
- the EC is also working on minimum standards and transparency requirements of EU ESG benchmarks.

Hence, we believe that if ESMA wants to proceed and publish guidelines, these should be aligned with future initiatives that might be launched at EU level (please refer to our comments above).

We also believe that introducing thresholds on elements yet to be defined could have a detrimental impact on the sustainable finance market and impede the reorientation of capital towards sustainable finance. This situation could lead to:

- increasing the risk of greenwashing as the thresholds are based on concept not clearly defined.
- risk of “green hushing”, the rules being too complex to implement, financial market participants could be diverted from the sustainable finance market until rules are clearer.

Beyond the subject of this consultation on the naming of funds, AFG members think that the EC and ESMA should more generally inspire themselves from AFG proposals and also specify the

expectations with regards to the treatment of derivatives. The lack of clarification at level 1 and level 2 of the regulations can leave significant room for interpretation to local regulators, which can ultimately lead to differences in treatment between players.

<ESMA\_QUESTION\_FUNA\_0>

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

<ESMA\_QUESTION\_FUNA\_1>

We fully concur with the objective of these guidelines to seek to set common rules in order to avoid misleading information and to enhance trust in the market, more particularly the fast evolving “ESG” market. To this extent, we agree in setting product naming rules so that product names fit the actual investment strategy of the product and are not deceptive to the investor.

This consultation paper is focusing on ESG or sustainability-related terms only and is introducing quantitative thresholds based on the pre-contractual information of committed % investments pertaining to the promotion of E/S characteristics, or % of sustainable investments as per SFDR art. 2(17).

We strongly advise that proportionality should be introduced between the “marketing” disclosures of a financial product (among which the name) and the degree of ESG commitment and related impact in the financial product. Unlike some national rules (such as the French non-financial disclosure rules or German ones), or label rules in some Members States, SFDR disclosures are not dealing with this issue. In July 2021, the European Commission (EC) clarified that the definition of funds disclosing under SFDR art8 is quite large, while the definition of funds disclosing under art9 has been narrowed due to the “sustainable investments only” requirement. On this basis, introducing fund naming rules may allow to introduce some proportionality among the art8 funds.

On top of introducing measurable **proportionality**, in theory, quantitative thresholds rules have the **merit to be simple**: based on pre-contractual asset allocation, simple to check for the regulator (against periodic reports).

But **such apparent simplicity in using quantitative thresholds is actually bringing confusion**:

- i. The most notable confusion would stem from the threshold based on “**sustainable investment**” (SI). ESAs are fully aware that different methodologies to assess SI can lead to quite different proportions of SI for one same portfolio. To this extent, in September 2022, ESAs have duly questioned the European Commission<sup>1</sup> to get more clarity on how to interpret SFDR’s SI concept (art 2(17)).

**As long as there is no precise clarification about the concept of SI, aligning the fund’s name to the proportion of SI in the fund may be amplifying the impact of SFDR’s current lack of clarity: market fragmentation across the EU, confusion of investors and increase in “greenwashing allegation risks”.**

- ii. More confusion is added through the MiFID Delegated Regulation and Directive that define “sustainability preferences” with three different concepts and not only the “sustainable investment” as per SFDR (SI). Founding these guidelines on the SI concept will bring even more confusion to the broad “sustainable” term.
- iii. In addition, the proposed guidelines themselves require **additional clarity on the threshold calculation methodology (numerator, denominator) prior to determining the level of the thresholds**. Typically, the level of the SI proportion threshold (50%) cannot be set “in abstracto” in the absence of a common definition of a SI. It should be aligned with the real economy stance, and relatively to a single common definition. The same for the 80% threshold for an ESG name, which is also dependent upon a clear definition and calculation methodology of such threshold. If an ESG fund holds 20% of cash, which is the maximum

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<sup>1</sup> ESA’s list of additional SFDR queries requiring the interpretation of Union law – 9 September 2022

ancillary cash a UCITS funds may have in France, the 80% ESG characteristic is already out of reach.

Clarity is also expected on other items: what is an “ESG-related” name? What is the objective of minimum safeguards? Etc... In terms of proportionality of disclosures, we believe that **what matters the most is the significance of the binding commitment in terms of goal and strategy**, and the adherence of **the investment process to meet this objective** [ex ante and ex post]. If set too high, quantitative thresholds may put aside some strategies, asset classes or geographical areas while they could contribute to enhance the ESG/sustainability features of the fund and most importantly finance the transition of a more sustainable economy. This could lead to some **confusion in the readability of the product range** offered to clients having sustainability preferences.

- iv. At last, we believe that **introducing two different thresholds for the use of “ESG” and “sustainable” may bring more confusion and complexity of understanding for retail investors**. In addition, there is no reason to treat “sustainable” differently than other “ESG” terms, investors do not perceive a strong difference between these two terms. In other jurisdictions, like UK or USA, the use of “sustainable” does not have a special treatment. This is not the case for “impact”, a word that investors do perceive differently compared to other ESG/sustainable terms.

AFG therefore:

- urges ESMA to consider that a pre-requisite to any guideline based upon SI proportions should be a sufficiently precise set of rules to assess “sustainable investments” which would not leave room for too much diverging interpretations. Unless the reference to SI is removed, these draft guidelines should be on hold until a *precise* definition is obtained and the threshold can be revised accordingly. More generally, we call for more clarity in these guidelines. AFG also advises that Authorities should take into account the available data, the status of the alignment of the economy and the EC’s long term Sustainable finance objectives like the financing of the transition.

believes there are alternative approaches and to this extent AFG has done its best effort in the limited consultation timeframe to propose definitions and alternatives in the subsequent answers.

<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>

AFG believes the draft guideline relating to the 80% minimum proportion of investments used to meet the E/S characteristics of the product should bring more clarity to assess whether the 80% is appropriate.

We understand the objective of ESMA to set ambitious thresholds to limit greenwashing allegations risks and avoid misleading information for investors. Nevertheless, we believe that requirements should be further clarified.

- (i) Indeed, AFG believes that there could be an inconsistency between the proposed level of the threshold (i.e. 80%) and the methodology

If ESMA was to keep the level of the threshold at 80%, it should be clarified that cash and derivatives should be excluded from the ratio calculation. Indeed, in France, UCITS funds can hold up to 20% of cash (the maximum ancillary cash a UCITS funds may have in France), in that sense the 80% ESG characteristic is already out of reach. This threshold would also be incompatible with asset classes that cannot be compliant with ESG characteristics (portfolio diversification as well as multi-asset portfolios). In addition, this level can depend upon the category of assets (OECD vs emerging,...).

Therefore, AFG proposes the following:

- **The denominator** would be the exposure without cash and derivatives (e.g FX or market risk hedging).
- **The numerator** would be the **exposure that contributes to meet the ESG characteristics of the fund**. For instance, depending on the ESG objective/strategy, this could mean all assets and underlyings that are subject to the assessment of a non-financial analysis or rating or ESG indicator in line with the strategy of the fund.
- This ratio requirement should be **coupled with an explicit ESG binding and measurable objective of the fund**. For example, the asset manager could be able to demonstrate that the fund has a better ESG profile than its investment universe / benchmark (e.g. ESG score of the fund versus benchmark, carbon footprint of the fund versus benchmark, or any other ESG KPI relevant for this strategy). In case the fund uses exclusion strategy, the asset manager could be able to demonstrate that the exclusions are relevant to this strategy and material compared to the investment universe.

**This approach would be in line with ESMA interpretation of SFDR.** Indeed, during the hearing held by ESMA on 23<sup>rd</sup> January, ESMA indicated that E/S characteristics can refer to the underlying investments (eg. investee companies have a net zero target) and/or the characteristics of the investment process.

Moreover, **the inclusion of a “binding and measurable objective” will tackle criticisms made towards the SFDR definition of “promotion of ESG characteristics” that is very wide.**

Would this approach not be retained by ESMA, a relative approach could also be considered instead of an absolute ratio (e.g. ensure that the ESG score of the fund is above its benchmark or its investment universe).

The following points should also be taken into consideration:

- When it comes to **debt funds and private equity funds**, it should be made clear that the ratio to be considered for the name is the committed ratio at the end of the “investment period”.
- It should be made clear that **indicators** on the basis of which the investments have been selected to meet the E/S requirements of the fund can be **reasonably estimated** data, or based on estimated data (such as ratings)

As per guideline § 21, it is important to clarify that the threshold would apply in “normal circumstances” and thus a “passive breach” process would be applicable otherwise. This is in line with any other regulatory ratio applicable to UCITS and AIFs.



(ii) In addition, guidelines should define **what an “ESG-related” name means**. To this extent we propose the following :

- By default an “ESG-related” word would allude to any environmental and/or social and/or governance theme in the name other than “sustainable” [translations in MS’ language to be agreed upon] or “impact”.
- Moreover, in order **to avoid discrepancies between NCAs’ interpretations and to allow a level playing field in cross-border distribution**, we believe **that ESMA should publish a list of “ESG related” terms, even if non-exhaustive**.

<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>

First, as a general comment, **we do not agree with the introduction of a minimum proportion of sustainable investment to be able to use “sustainable” related terms**. Indeed, an ESG strategy is meant to be « sustainable ». In addition, MiFID deals with « sustainability preferences » which is another concept (based on taxonomy, SFDR SI and PAI). It might bring even more confusion to link the broad “sustainable” term to the SFDR fund applicable SI concept. Which is the level playing field with a sustainable EMTN? Or with a regulated “sustainable and solidarity development deposit account” (in France)?

Second, as already explained in our previous answers, **at this stage, the definition of SI is unclear and leads to quite different interpretations and methodologies in the market**. We hence believe that **as long as the regulator has not *precisely* clarified the assessment of a sustainable investment, we strongly disagree to include such a threshold based on a concept subject to many interpretations**. Neither do we agree with a level (50%) that it may be seen as “arbitrary” in the absence of comparison due to the lack of a common definition. Including such a threshold would amplify market fragmentation, end investors’ confusion and possibly the risk of greenwashing.

If ESMA still wants to proceed, AFG suggests an alternative that may solve the definition problem: measure the SI proportion of the fund **relative to the SI proportion of its benchmark or its investment universe**, using the same assessment methodology. In such a case, the word “sustainable” could be used provided that the fund commits to have a % SI exceeding significantly the % SI of its investment universe (but in no case as high as 50%).

For funds without a reference benchmark or investment universe, the fund could identify a proxy reference to be in line with this requirement. It should be made clear that such option would apply as long as the European Commission has not *precisely* clarified the definition of “SI”.

For the avoidance of any doubts, the investment universe should be clearly defined in the fund’s prospectus.

In any case, should a SI threshold be set (in absolute after a common SI definition is determined by the EC, or in relative terms), the same provisions as in our response in Q2 would apply:

- (i) clarity is needed on the calculation of the ratio (in line with comments provided in Q2 with regards cash and derivatives).

- (ii) the level of the threshold would need to be assessed based upon a common SI definition and the “sustainability” of the real economy.

**As a conclusion, we would like to reiterate our concerns about setting a threshold on a notion that is not clearly defined by the regulation.**

<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>

Please refer to our answer to Q2 for the “ESG” threshold and alternative proposals of clarification.

Please refer to our answer to Q3 for the “SI” threshold alternative approach (relative ratio instead of absolute ratio, with the investment universe).

<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>

We believe that taking into account the assets covered by a non-financial analysis, rating, indicator, and adding a requirement by which the fund should have an explicit measurable (KPI) and binding ESG objective is a solid alternative (see our response in Q2).

For instance, strategies that are compliant with the approaches proposed by the French Market Authorities (AMF) in its doctrine could be considered as alternative to the threshold mechanisms. “Selectivity” i.e. exclusion of at least 20% of the worst ESG performers in a universe definition, or “rating upgrade” approach, after eliminating at least 20% of the worst ESG performers in a universe definition could be used. The same with a ESG KPI minimum level strategy.

It is important that any alternative approach should (i) apply proportionality (the name being granted only if there is a sufficiently significant commitment) (ii) be measurable and, (iii) fit with many types of strategies as long as there is a clear “ESG objective”.

<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>

As a general comment, we believe that exclusions are not appropriate as minimum safeguards for investment funds.

AFG strongly disagrees with using Paris Aligned Benchmark (PAB)’s exclusions listed in art 12(1) and 12(2) of the BMR delegated regulation 2020/1818 for the following reasons:

- (i) SFDR art. 8 funds already have some “good governance practices” safeguards as a minimum standard. In addition, if they hold SI, then investments are subject to SFDR’s DNSH and those are related to PAI which don’t only cover Environmental criteria.

- (ii) **The PAB is a label dedicated to Paris aligned targets.** Exclusion criteria in art 12(1) are mainly **climate focused** and the high level of exclusions is specifically fitting this label and the PAB objective; it is neither suitable for other labels nor for strategies which are not fully climate oriented. **The approach should not only focus on climate. It largely exceeds a notion of “minimum” safeguards and would be disproportionate.**
- (iii) Article 12(2) states that companies that “*significantly harm one or more of the environmental objectives referred to in Article 9 of Regulation (EU) 2020/852*” should be excluded. The notion of DNSH is not clearly defined and, in SFDR, such notion applies to “sustainable investments”.
- (iv) It is impossible to apply these criteria to cash.

In the current transitioning state of the real economy, applying all the PAB min. standards of art 12(1) and 12(2) would disqualify many funds from an “ESG” related name and create major confusion with end investors.

So as to enhance the minimum standards of art8 funds qualifying for an ESG-related name in a proportionate manner, an alternative proposal could be the following:

- (i) No investment can be made in the production of weapons prohibited by the Oslo Convention on Cluster Munitions and the Ottawa Treaty on Anti-Personnel Mines.

The product considers the SFDR mandatory PAI in a quantitative or qualitative manner.

<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>

Asset managers act in the best interest of the unitholders by fulfilling the fund’s investment promise, that includes the financial and non-financial objectives of the fund. Derivatives are essential tools to hedge fund’s risks, like market risks, raising interest rates, currency, inflationary, volatility risks etc. and therefore should continue to be allowed in any fund, having an ESG profile or not.

AFG believes that derivatives should be taken into account for the calculation of the minimum proportion of investments used to meet the environmental or social characteristics or sustainable investment objectives.

Asset management strategies can use derivatives to attain their investment objective since more than 30 years. It is unconceivable today to erase value added portfolio management techniques that the founding European Directives (like the UCITS Directive) authorize since 1985. As a reminder, the use of derivatives is regulated through the global risk exposure rules and limits as well as other pieces of regulation (EMIR, CCP Recovery and Resolution Regulations, SFTR...).

**The founding principle is:**

- 1. If the derivative is meant to help attain the ESG investment objective, it should be taken into account as it is in other investment ratios (eligibility, diversification, concentration).**
- 2. The derivative should be disregarded if its use is not meant to attain the ESG objective as its use is purely financial (i.e. for example if it is used for instance as tactical derivative and/or temporary for market (beta) hedging/exposure [non ESG-related] purposes, or for FX or duration purposes, to manage subscriptions...).**

Importantly, the use of derivatives must not distort the ESG objective or the main ESG features of the fund, whether the derivative is taken into account or disregarded for the purpose of exposure ratios

- When the derivative is taken into account by transparency of an index (or basket of assets) for instance, the prospectus should set strict limits on the indirect resulting proportion of assets that are contrary to the ESG characteristics of the fund, for instance in contradiction to the fossil fuels strategy, (it is intended to be strictly limited to a negligible proportion, in general no more than 1 or 2%).

When the derivative is not taken into account, the asset manager has the responsibility to ensure that the derivative uses are not interfering with the ESG objective or strategy of the fund.

In the fund's ex ante implementing strategy disclosure, detailed transparency should be given by each fund on each type of derivatives it may have to use, what types of usages it may implement (market hedging, exposure, forex hedging, yield curve management, risk neutrality to benchmark setting, volatility target management, stop loss controls, CPPI management, monetization, etc) and the conditions under which they are meant to contribute to attain the ESG strategy/characteristics or conversely, if they are not meant to contribute.

The philosophy of the proposed approach is based on (1) a similar approach with cash investing when the use of derivatives is rather structural (targets single-underlying derivatives, ESG indices and the transparency of non-ESG indices or baskets) and (2) in addition the acknowledgment of a tactical use and or temporary use (temporary period to be further defined and less than one year in a any case), both types of use being useful for the effective management of the portfolio.

Very simply, AFG suggest dividing derivatives into two categories:

1. Single-underlying derivatives
2. versus index/basket derivatives

1. On a single-underlying derivative, the approach and use are the same as on the cash asset.
2. On index/basket derivatives, there are 2 situations:
  - 2.1. when used for market hedging/market exposure tactical purposes or when the impact on real economy (real investment flows) of the exposure through derivatives is negligible, the exposure is not taken into account.
  - 2.2. Otherwise, and unless they are already based on an ESG index\* (or basket of ESG assets), then the index is transparised, underlying by underlying. It should be mentioned that transparency requires a sufficient period of time for proper implementation\*\*.

\*It should be clarified that the ESG index market is not yet mature and liquid enough to switch from current index derivative market to an ESG derivative market. This market continues to be in progress for several years from now on.

\*\*It should be clarified that transparency proposal is right but authorities should be aware that is not going to be easy and achievable every time because for instance access to granular data is limited and/or very expensive and would require specific management and IT tools to manage exclusions in particular. This is even more applicable on non-European exposure indices, owners of local stock exchanges on which asset managers do not have access to the exact composition. Therefore, in some limited cases and on a temporary stance, funds could apply ex-ante cautious ESG rules/limitations to take into account the derivative index underlying positions on ESG without having to perform the transparency line by line.

It is important to remind that investors should continue to benefit from both effective portfolio and risk management (Efficient Portfolio Management techniques - EPM) and ESG management in a same investment. Investors both financial and non-financial needs and preferences must be considered in this derivative and ESG discussion.

<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>

AFG suggests the use of the exposure value, i.e. the one referring to the delta approach which reflects the economic exposure that the derivative provides to the underlying asset(s) / companies. We propose to refer to the CESR 10-788 conversion methodologies

<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>

AFG suggests that the following principle should be respected: derivatives should not be used in contradiction with the ESG objective or the main ESG features of the fund.

Counterparty: Although there is not directly linked to the issue discussed, AFG suggests an additional safeguard on a different level, i.e. linked to the counterparty risk. AFG suggests that listed derivatives be considered compliant from an ESG standpoint and that OTC derivatives' use require that the asset manager applies ESG guidance's in his counterparties' selection process.

<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>

Is this question related to index funds? In this case, the question is very relevant indeed.

It should be noted that index providers are not in the SFDR's scope and that BMR only gives criteria for CTB and PAB indices with only some transparency asked for other ESG benchmarks. Asset managers agree that the same requirements should apply as soon as index providers are in the scope too. For the time being, they are not in the SFDR's scope and not in these Guidelines' scope. From an ecosystem point of view, there is thus a regulatory mismatch between index funds and their indices' regulations in terms of ESG rules. The same applies for other products than funds marketed to retail clients, like structured notes for instance, which are not subject to the same rules. Regulators have a global responsibility of bringing forward a coherent ESG approach towards retail, whatever the investment product they are proposed.

Thus, taking into account the current context is of utmost importance. Therefore, some members of AFG believes that index and structured funds should for the time being be granted a temporary exemption. Some of our members believe for instance that as long as the Sustainable Investment (SI) definition is not harmonised, asset managers (that have both active and index products) must have the choice, for the index products, between using their own SI metrics or using the index provider's ones. In the same vein, until benchmark producers are not in the scope of SFRD and all linked guidelines, it is unconceivable that they will apply strictly on their own initiative the naming conventions on their products. It is thus very uncomfortable in terms of end investors coherent



information to track an index (or offer exposure to) and not be able to use the index name. The resulting transparency owed to the investors would be flawed.

### *Index funds*

It should also be reminded contractual obligations upon the asset manager to use the index name (that they pay). In index funds, the use of indices is managed according to the license agreement signed by the asset manager with the index provider. This contract defines do's and don't asset managers have to comply with:

- Use the index name in the fund's name
- Constraints in terms of fund's disclosures and portfolio transparency

It is not always easy (from an asset manager's perspective) to change the name of a product... especially if the index is managed by a non-European entity or an index provider (for ex a stock exchange) for which delta-one products are not considered as strategic products. In other words, index providers (being a global entity or not) are not bound (nor always interested from a business point a view) to comply with European regulations and there is little incentive to change the index name according to European constraints. In addition CTB and PAB indices should still be named as they are today.

### *Structured funds*

Regarding structured funds (like formula funds), some members think they should also be excluded at this stage to allow these rules to be adapted to the required management techniques. Indeed, when a formula fund offers indexation to an underlying index, the name of the fund must be able to reflect the reality and the theme of this exposure, otherwise the investor may be misled as to the economic exposure to which the fund is committed.

At the very least, (1) it is essential that existing structured funds (and in particular formula funds) benefit from a grandfather clause until their maturity, because:

- These funds are closed to marketing: they are therefore no longer subject to new investments,
- The financial conditions have been set for the entire life of the fund on the basis of the regulations applicable at their launch: changing the terms of structuring is therefore impossible without calling into question the terms of the fund,- A change of name would risk casting illegitimate suspicion on the world of management and reliability of offers, and generating confusion of requests for redemptions before maturity which, given market conditions, could be made to the detriment of investors, at levels significantly below the protection level.

And that (2) only the risky part at inception could follow the same rules as mutual funds.

Last but not least, ESMA should ensure with the other ESAs that there is level playing field with other index or formula-based products that are not funds and that also target retail like notes, EMTNs, etc for instance.

<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. For funds replicating "ESG" index/ reference benchmark with derivatives instruments, we consider that Indirect (TRS) based replication has in terms of exposure the same effects as the direct replication of the index. The portfolio held by the fund is swapped against the exposure of the portfolio held by the counterparty and unitholders bears the risk and opportunities linked to the exposure portfolio, not the portfolio held by the fund.

Nevertheless, the portfolio held by the fund (which is improperly called “collateral”, as these assets are held by the fund, the fund is the direct owner of the fund’s assets, so there is no notion of collateral applicable in this case) follows the asset managers’ Responsible Investment policy (the policy may include different elements as legal exclusions, constraints on coal and fossil fuels linked to the asset manager’s policy, sometimes minimal ESG ratings). In France, AFG has issued guidance on these 2 issues to help asset managers to build their policies:

- AFG, GUIDE TO DEVELOPING A COAL STRATEGY FOR ASSET MANAGEMENT COMPANIES
- AFG, Guide sur l’élaboration d’une stratégie énergies fossiles à destination des sociétés de gestion de portefeuille hors charbon et y compris les énergies fossiles non conventionnelles

For other funds, the approach should depend on the nature of the derivatives instruments and on its related objective within the investment strategy.

<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>

As a general comment, we would like to remind that, a large proportion of “impact funds” are categorized as “article 9” products.

Yes, as investors, notably retail, are sensitive to “impact” terms. To protect them, the use of this particular term should be linked to reality in the fund’s strategy. A level playing field is necessary with all retail products, not only funds and mandates in the SFDR’s scope.

We suggest referring to the 3 following pillars: intentionality, additionality and measurability.

<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>

No, AFG believes that “transition-related” names are covered by “ESG-related” names, and that the latter should be defined as proposed in Q2.

AFG strongly believes that the transition should be part of the SI definition and calibration.

<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>

Yes, most importantly, for level playing field and fair competition reasons, same guidance and consideration should apply:

- to other financial products subject to SFDR,
- to financial instruments as defined in MIF and IDD (as they will be distributed through MIF/IDD sustainability preferences),

- but also to financial instruments not subject to SFDR but claiming ESG or sustainability or impact features in their name (green bonds, notes, derivatives,...). For the latter instruments, guidelines should be adapted as far as references to SFDR definitions and binding information are concerned.

AFG urges ESMA to work closely on the subject with EBA and EIOPA to ensure a level playing field across the financial sector.

<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>

A 6-month transitional period seems too short. AFG suggests at least 12 months. SFDR templates and prospectus changes for the year end had been exhausting stream works within our membership. Authorities should also consider human capital, not only compliance costs, when proposing new requirements. In addition, unlevel playing field among sectors and geographies might have effects on the competitiveness of the European industry and work to the detriment of the best interest of unitholders.

Also, should the EC clarify “sustainable investment” (SI), depending upon their definition, it could involve additional implementation time by the industry. This, combined with these guidelines – all the more if they would rely on a SI threshold -, advocate for an extended period of application of 12 months (minimum).

<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>

We understand from the hearing held on January 23rd that the question is relative to funds closed for subscriptions.

For funds which have terminated their subscription period it is not necessary to extend these naming-related provisions as there will be no new subscriptions. The name of the fund won’t act as a “marketing tool” anymore.

Moreover, this would be in line with the May 2022 SFDR Q&A from the European Commission that indicates that “where a financial product is no longer made available to end investors”, such products must comply with requirements regarding “periodic report” and “websites disclosure” but not with precontractual requirements.

<ESMA\_QUESTION\_FUNA\_14>

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

<ESMA\_QUESTION\_FUNA\_15>

The introduction of the proposed guidelines may have the following effect :

- **Increasing the risk of greenwashing** as the thresholds are based on concept not clearly defined.



- **Increasing the risk of “green-bleaching”** if the constraints imposed are too stringent and inadequate (PAB exclusions for example). Indeed, it may drive some asset managers to stay out of ESG strategies.

In addition, in the light of the SFDR complicated implementation, AFG thinks that authorities should also consider human capital in compliance projects, not only compliance costs, when proposing new requirements. In addition, unlevel playing field among sectors and geographies might have effects on the competitiveness of the European industry and work to the detriment of the best interest of unitholders.

<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>

AFG anticipates significant additional costs first for the compliance of prospectus. It means human resources dedicated for some time. In addition, front office tools will have to be adjusted and asset managers trained. AFG wonders to what extent its members will have to inform investors and how? It should be recalled that teams have had an exhausting compliance exercise for the year end with the SFDR level 2 implementation.

<ESMA\_QUESTION\_FUNA\_16>

**Q17**