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Submitted electronically to
consultation-01-2021@iosco.org

Raluca Tircoci-Craciun
International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
Spain

Re: *Public Comment on Recommendations on Sustainability-Related Practices, Policies, Procedures and Disclosure in Asset Management*

Dear Ms. Tircoci-Craciun:

ICI Global[1] appreciates the opportunity to provide feedback to IOSCO on its proposed *Recommendations on Sustainability-Related Practices, Policies, Procedures and Disclosure in Asset Management* (Consultation Paper).[2] The Consultation Paper focuses on asset managers and investor protection issues and aims to improve sustainability-related practices, policies, procedures and disclosures in the asset management industry. We appreciate IOSCO's continued focus on sustainable finance, including challenges asset managers face with respect to the lack of consistency and comparability of corporate ESG data. In general, we support the high-level recommendations proposed in the Consultation Paper but encourage IOSCO's Sustainable Finance Taskforce (SFT) to consider the following suggestions as it works to finalize the details of these recommendations.

[1] ICI Global carries out the international work of the Investment Company Institute, the leading association representing regulated funds globally. ICI's membership includes regulated funds publicly offered to investors in jurisdictions worldwide, with total assets of US$41.1 trillion. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of regulated investment funds, their managers, and investors. ICI Global has offices in London, Brussels, Hong Kong, and Washington, DC.

[2] IOSCO's Proposed Recommendations (June 2021) are available at https://www.iosco.org/library/pubdocs/pdf/IOSCOPD679.pdf

I. Overarching Considerations

Policy Objectives Should Steer Regulatory Outcomes. Regulators around the world are addressing regulatory needs around sustainable finance at different speeds and with some widely varying policy objectives. The European Union's objective for sustainability-related legislation, including the Sustainable Finance Disclosure Regulation (SFDR), is to re-orient flows of capital to fulfill its Green Deal objectives and meet its Paris Agreement commitments.[3] The European Union is using a variety of levers to accomplish these goals, including relying on asset managers to drive change and embedding double materiality into disclosure standards. In contrast, the US Securities and Exchange Commission has announced plans to develop rules for public company disclosures and fund disclosures for the purpose of improving transparency in the capital markets.[4] Similarly, one of the primary objectives of IOSCO is to protect investors. For this reason, IOSCO's recommendations should focus on meaningful disclosures for the protection of investors.

Disclosure of Information Related to Integration of ESG Factors into Investment Processes Should be Proportionate and Distinguished from Disclosure for Sustainability-related Investment Products. The integration of ESG factors into the investment process is a long-standing element of investing that seeks to enhance a fund's financial performance by analyzing material ESG considerations along with other material factors such as credit risk and counterparty risk. For products that integrate ESG factors into the investment process, the ESG factors are among many factors considered. For example, an investment manager may consider a variety attributes when selecting investments for a fund, such as revenues, earnings, cash flows, profitability, leverage, new products, and new management. These funds often do not have sustainability-related strategies. Requiring specific and expanded disclosures relating to the integration of ESG factors would be disproportionate to their role in the investment process and would highlight only one aspect of the investment process that may be confusing and potentially misleading to investors.

Disproportionate disclosure could over-emphasize the relative importance of the ESG factors and provide a misleading picture of the investment process, including security selection. In short, it could confuse investors to focus disclosure on one of many material considerations in the investment

[3] REGULATION (EU) 2019/2088 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 November 2019 on sustainability-related disclosures in the financial services sector, available at https://eurlex.europa.eu/eli/reg/2019/2088/oj.

[4] *See* US SEC Chairman Gary Gensler's Prepared Remarks Before the Principles for Responsible Investment "Climate and Global Financial Markets" Webinar (July 28, 2021) available at https://www.sec.gov/news/speech/gensler-pri-2021-07-28. "Together, I think updates to public company disclosures and to fund disclosures could bring needed transparency to our capital markets. This gets to the heart of the SEC's mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation."

process. IOSCO should distinguish its recommendations on Product Disclosure[5] from any recommendations it makes around disclosures related to the process of integrating ESG risks into investment decisions. IOSCO also should consider how to ensure that new disclosure obligations put in place by member authorities do not have the unintended consequence of signaling to fund investors that ESG factors are more important than other types of investment considerations.

II. Responses to Selected Questions Raised in the Consultation Paper

Question 1: Will the recommendations outlined below sufficiently improve sustainability related practices, policies, procedures and disclosure in the asset management industry and address the issue of greenwashing? Are there other areas of sustainability-related practices, policies, procedures and disclosure in the asset management industry not mentioned in this consultation report that should be addressed as separate recommendations?

In general, we support the high-level recommendations proposed in the Consultation Paper and appreciate IOSCO's efforts to coordinate regulatory efforts across its member jurisdictions. Many ICI members are global firms and, as a general matter, strongly support consistency of regulatory requirements across jurisdictions. As IOSCO considers how to drive forward more consistent sustainability-related disclosure, the experience of the European Union, which has moved ahead on many sustainability standards, provides apt lessons. One of the most important lessons from the EU experience is the need to sequence properly disclosure requirements. The European Union required certain asset managers to disclose sustainability-related information about their investments before requiring companies in which the managers invested to provide sustainability-related disclosure. This approach put asset managers in the position of having to provide information to which they do not have access and even if they are able to obtain the information, methodologies on evaluating and reporting the data are inconsistent.

Proper sequencing is critical to fulfilling regulatory objectives. To ensure that regulated funds have access to consistent, comparable, and reliable data, policymakers should heed the lessons from Europe and focus on public company disclosure before considering fund disclosure. IOSCO should encourage its members to first address regulatory obligations for companies to provide sustainability-related information, which should yield more comparable, consistent, and reliable information for investors.[6]

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[5] *See* Consultation Paper, Recommendation 2: Product Disclosure. Securities regulators and/or policymakers, as applicable, should consider clarifying and/or expanding on existing regulatory requirements or guidance or, if necessary, creating new regulatory requirements or guidance, to improve product-level disclosure in order to help investors better understand: (a) sustainability-related products; and (b) material sustainability-related risks for all products.

[6] *See* ICI response to US SEC request for input on climate-related disclosures (4 June 2021) available at https://www.ici.org/system/files/2021-06/21_ltr_rfi.pdf. In this letter, we encourage the SEC to provide issuers

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Additionally, IOSCO should encourage its members to take a principles-based approach to any regulation related to sustainable finance, which is a rapidly evolving space and one where regulation should be flexible enough to permit asset managers to continue to innovate to meet the evolving objectives of their investors. If policymakers take an overly prescriptive approach to regulating sustainable finance, it could lead to confusing or boilerplate disclosure language that fits the requirements but does not facilitate investor understanding.[7] Additionally, a flexible architecture will ensure policymakers can keep pace with market and technological developments more easily.

Question 4: Should securities regulators and/or policymakers, as applicable, consider setting out different disclosure requirements for products with sustainability-related investment objectives as compared to products that promote sustainability-related characteristics? If so, for which of the different areas of disclosure listed above should the requirements vary, and how should they vary? In addition, if so, should securities regulators and/or policymakers, as applicable, consider specifying thresholds or other criteria for determining whether a product has sustainability-related investment objectives as compared to sustainability-related characteristics, and what should those thresholds or criteria be?

We do not believe that securities regulators and policymakers should draw this line between products with "sustainability-related investment objectives" and those that "promote sustainability-related characteristics." Although the European Union has structured the SFDR and its product disclosure obligations around these two categories, this classification system has created significantly more confusion among asset managers and their clients than clarity. Moreover, because the distinction between these two categories remains unclear, EU Member States have imposed individual requirements across the European Union with respect to marketing and distribution of sustainability-related products.[8] We see no reason for IOSCO to adopt this terminology in its own

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flexibility as related to public company disclosures. We are cognizant of the cost and liability companies may face in providing sustainability related disclosures, and a flexible and practical approach will mitigate these impacts on issuers and encourage more comprehensive corporate disclosures as soon as possible.

[7] For example, consumer testing conducted by ESMA on the content and layout of product-level disclosure templates that will be required to be used under the SFDR revealed that only 1% of consumers tested fully agreed that the templates would be useful. Consumers raised concerns regarding the length, complexity, density, and repetition in the text of the disclosures. It is noteworthy that consumers favored the pie charts in the templates purporting to show the percentage of product holdings invested in "sustainable investments". Given that asset managers may not agree on what constitutes a sustainable investment, the pie charts in practice are likely to give consumers a false sense of comparability a cross products. *See* ESMA Outline of CP and context of hearing (29 April 2021) available at: https://www.esma.europa.eu/sites/default/files/library/open_hearing_on_taxonomy-related_product_disclosures_cp.pdf

[8] *See* French AMF Recommendation DOC-2020-03 (created on 11 March 2020, amended on 27 July 2020) available at https://www.amf-france.org/en/regulation/policy/doc-2020-03 requiring certain minimum standards for products that

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work and instead urge IOSCO to encourage its members to put in place disclosure frameworks for sustainability-related products that are principles-based and aim to promote better disclosure that will help investors determine which products best meet their individual needs. Investors benefit when sustainability-related products provide clear disclosure for an investor to be able to understand the distinctions among different types of strategies so they can choose the strategy that best fits their needs.

With respect to threshold criteria, again we caution against imposing minimum standards that attempt to create "categories" of products for investors rather than providing transparency for investors to make an informed investment choice. Only by empowering investors to make informed choices will the market continue to evolve to meet investor demand for sustainable investing. A diverse spectrum of sustainability-related strategies exists to meet a wide range of client demand, and we are concerned that minimum standards will only limit choice for investors and stifle innovation. We caution that threshold criteria would likely narrow the existing diversity of sustainability-related strategies and reduce investor choice, without improving transparency or investors' understanding of sustainability-related strategies.

Moreover, understanding of sustainability will evolve over time, and regulations should encourage, rather than inhibit, that progression. Investors will benefit from asset managers adapting their own investment processes and product innovation along with the developing landscape. Prescriptive minimum standards that attempt to define what it means to invest sustainably result in confusing

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make non-financial information a key element of product communications. These minimum standards include as an option the reduction of the investment universe by at least 20%. *See also* changes to German distribution rules that require certain exclusions to be met in order to distribute a product that otherwise meets SFDR Art. 8 disclosure requirements as an "ESG" product in Germany. FinDatEx MiFID template EMT v.3.1 available at https://www.findatex.eu/mediaitem/690679db-03ba-4bf6-8a68-9c9f181d33b8/20210129%20-%20FinDatEx%20-%20EMT%20V3.1%20final.xlsx. *See also* German BaFin (Konsultation 13/2021; WA 41-Wp 2100-2019/0002) BaFin is consulting on draft guidelines that would impose minimum standards such as minimum investment in sustainable assets of 75%, a "best-in-class" approach to the entire portfolio, or the replication of a sustainable index in order for a fund to be designated or marketed as sustainable in Germany. (2 August 2021) available at https://www.bafin.de/SharedDocs/Veroeffentlichungen/DE/Konsultation/2021/kon_13_21_WA4_Leitlinien_nachhaltige_Investmentvermoegen.html.

Additionally, the European Commission recently announced that it will consider imposing EU-wide minimum sustainability criteria for financial products that promote environmental or social characteristics to bring clarity and coherence to the financial markets. Commission Communication regarding Strategy for Financing the Transition to a Sustainable Economy (6 July 2021) available at https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52021DC0390&from=EN.

disclosures for investors.[9] Additionally, crowding investors into product categories "created" by regulation with a small investable universe does not further the objective of protecting investors.

Question 5: Should naming permit the product name to reference sustainability only if the investment objectives refer to sustainability?

A product's investment objectives and strategies should be consistent with any product name that suggests a focus on sustainable investing strategies. Although investors should not rely on a product's name as the sole source of information about the investment objective, strategies and risks, a name may communicate important information to an investor. Where a product's name suggests a focus on sustainable investing strategies, that name should be consistent with the fund's investment objectives and principal investment strategies. A broad range of sustainability-related products should be able to reference sustainability in their product names, provided that the product names accurately reflect the relevant investment approaches.

The ability to utilize a product name that references sustainability should not be restricted to only those products whose investment *objectives* refer to sustainability. Frequently the sustainability-related aspects of the product are disclosed in relation to the investment *strategy*.[10] In some jurisdictions, such as the United States, it is common for the investment objective to describe the financial objectives of the fund, and the principal investment strategy to describe the strategies employed, including sustainability-related strategies.[11] IOSCO should be mindful of differences in

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[9] Consider the EU Taxonomy Regulation, which will require certain products to disclose percentage of investments that are in economic activities that qualify as environmentally sustainable. The disclosure is based on technical screening criteria for only environmentally sustainable economic activities, and only one third of the criteria has been fully developed. As the criteria develop further over time, periodic and other reporting to clients of EU asset managers will change in ways that clients are unlikely to understand. This will not be due to the fluctuating investments in the portfolio but changing criteria for what is considered environmentally sustainable. See Articles 5 and 6 of the Taxonomy Regulation (EU) 2020/852 (June 2021) available at https://ec.europa.eu/info/law/sustainable-finance-taxonomy-regulation-eu-2020-852_en.

[10] For this reason, we disagree with the example of greenwashing on p.27 of the Consultation Paper. "A product includes "ESG factors" in its name, but its investment objectives only state that it seeks to provide capital appreciation by investing primarily in global equity securities. A product has the word "sustainable" in its name, but its investment objectives only reference financial performance." In these examples, we do not know the extent to which sustainability-related factors are considered and utilized as part of the investment strategies. The lack of sustainability-related investment objectives alone should not indicate greenwashing.

[11] In the United States, the investment objective of a fund frequently will be either capital appreciation, income, or a combination of the two. The principal strategies of the fund tells investors how the fund intends to achieve its investment objective, including any sustainability-related strategies the fund manager utilizes. These strategies indicate the approach the fund adviser takes in deciding which securities to buy or sell, including sustainability-related selection criteria. See US SEC Investor Alerts and Bulletins "How to Read a Mutual Fund Prospectus (Part 1 of 3: Investment

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regulatory regimes and avoid prescribing where regulatory authorities should mandate specific disclosures.

Moreover, we believe a product whose name includes terms suggesting a sustainable investing focus should define the terms and describe the product's focus on sustainable investing. Many sustainability-related products include terms in their names to communicate their focus on sustainable investing strategies, such as "ESG," "sustainable," "social," and "impact." These products should disclose how the asset manager defines the sustainable investing term. Products with the same terms in their names may have varied investment objectives and strategies. It is, therefore, important that each product define the relevant terms and how it relates to the fund's investment strategies.

Question 10: Should securities regulators and/or policymakers, as applicable, encourage the use of specific metrics or key performance indicators to assess, measure and monitor the sustainability-related product's compliance with its investment objectives and/or characteristics? Should these metrics be subject to self-selection, or should there be a standardised approach?

In considering how data should be used with respect to an investment strategy, IOSCO should encourage regulators to avoid overly prescriptive requirements around what data is appropriate to consider for the design and management of sustainability-related products. Asset managers are well suited to determine the most relevant of the available ESG data within a particular investment universe. Requiring the use of certain key performance indicators (KPIs) will result in asset managers utilizing data that may not be sufficiently reliable or relevant to the manager's investment strategy or client preferences.

Additionally, regulators should avoid outcome-driven reporting where a specific outcome or impact is not a stated design feature of the product. For many sustainability-related products, disclosure should provide transparency around the criteria the asset manager is using to select, or screen out, securities to meet the product's investment objectives and strategies. This would promote investor understanding of how a particular product seeks to achieve its investment objectives and provide investors with the ability to compare among similar products.

Question 13: Are there any sets of standardized sustainability-related terms being developed by international organisations that should be considered by securities regulators and/or policymakers, as applicable?

Objective, Strategies, and Risks)" available at https://www.sec.gov/oiea/investor-alerts-bulletins/ib_mfprospectus1.html.

In July 2020, ICI published a white paper entitled Funds' Use of ESG Integration and Sustainable Investing Strategies: An Introduction (ICI Terminology Paper).[12] The ICI Terminology Paper was developed by a working group of senior executives from ICI member firms who reviewed comprehensively how funds in the United States describe ESG integration and sustainable investing strategies. ICI's working group found that funds were describing similar investing concepts in a variety of ways. To promote the understanding of investors, other market participants, and regulators, the working group agreed that it would be good practice for funds to use consistent terminology to describe ESG strategies in their public communications.

The ICI Terminology Paper sets forth the working group's understanding of the range of those strategies and explains how a fund investor might differentiate among them. It does so by generally discussing the differences among integration and the three common sustainable investing strategies. It then further explains the variations among each of these investment strategies, followed by examples from fund websites and prospectuses that describe how specific funds choose their investments. We encourage IOSCO to leverage the ICI Terminology Paper as a resource when considering coalescence around a set of consistent sustainability-related terms.

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We appreciate the opportunity to provide feedback on the IOSCO Consultation Paper. If you have any questions, please contact me at Jennifer.Choi@ici.org or Elizabeth Lance at Elizabeth.Lance@ici.org.

Sincerely,

/s/Jennifer S. Choi

Chief Counsel
ICI Global

[12] Available at https://www.ici.org/system/files/attachments/20_ppr_esg_integration.pdf.