

ESMA Publishes Final Guidelines for ESG and Sustainability-Related Fund Names

16 May 2024

On 14 May 2024, the European Securities and Markets Authority (“ESMA”) published its [Final Report](#) on the “*Guidelines on funds’ names using ESG or sustainability-related terms*” (the “Final Guidelines”). ESMA initially consulted on the topic in November 2022 (please find a link to our update [here](#)) and subsequently provided an update in December 2023 (please find a link to our update [here](#)). Consistent with the scope of the Sustainable Finance Disclosure Regulation (the “SFDR”), the Final Guidelines should apply not only to EU fund managers but also to non-EU fund managers marketing EU or non-EU funds in the European Economic Area.¹

The Final Guidelines apply to both retail and professional funds and broadly categorise terms used in fund names, as: (i) transition-, social-, and governance-related terms; (ii) environmental- or impact-related terms; (iii) sustainability-related terms; and (iv) a combination of the above. Each category triggers certain minimum requirements for the fund’s investment strategy, as summarised below. Accordingly, the marketing materials and fund documentation will need to comply with the Final Guidelines.

The Final Guidelines will apply three months after the translations in all EU official languages have been published on ESMA’s website (the “Effective Date”) to fund managers of new funds (*i.e.*, funds created after the Effective Date). There are no grandfathering rules. Fund managers of funds *existing* before the Effective Date benefit from an additional transitional period of six months to comply with the Final Guidelines.

We summarise in this Debevoise Update the most important aspects for fund managers to consider as a result of the Final Guidelines.

¹ Note that our update focuses on alternative investment fund managers under the AIFMD; the Final Guidelines will equally apply to UCITS management companies and managers of EuVECA, EuSEF and ELTIFs.

Listed Terms in Fund Names and Related Restrictions. This table contains a non-exhaustive list of terms used in fund names and the corresponding restrictions that are triggered pursuant to the Final Guidelines.

Restricted Fund Names	Restriction
<p>“Environmental” terms in its name (e.g., “green”, “environmental”, “climate”, including “ESG” and “SRI”²)</p>	<ul style="list-style-type: none"> • At least 80% of the fund’s investments must meet (a) the environmental and/or social characteristics promoted by the fund pursuant to Article 8 of the SFDR or (b) sustainable investment objectives of the fund pursuant to Article 9 of the SFDR. • The fund must adhere to the full exclusion list prescribed under the EU Paris-Aligned Benchmarks (the “PAB”).³
<p>“Sustainable” or sustainability-related terms in its name (e.g., “sustainable water”, “sustainable society”)</p>	<ul style="list-style-type: none"> • At least 80% of the fund’s investments must meet (a) the environmental and/or social characteristics promoted by the fund pursuant to Article 8 of the SFDR or (b) sustainable investment objectives of the fund pursuant to Article 9 of the SFDR. • The fund must adhere to the full exclusion list prescribed under the PAB. • The fund must commit to invest meaningfully in SFDR-aligned “sustainable investments”.
<p>“Impact”, or “impact investing” or impact-related terms in its name</p>	<ul style="list-style-type: none"> • At least 80% of the fund’s investments must meet (a) the environmental and/or social characteristics promoted by the fund pursuant to Article 8 of the SFDR or

² Socially Responsible Investing.

³ Article 12(1) (a) to (g) of Commission Delegated Regulation (EU) 2020/1818:

- (a) companies involved in any activities related to controversial weapons;
- (b) companies involved in the cultivation and production of tobacco;
- (c) companies that benchmark administrators find in violation of the United Nations Global Compact (UNGC) principles or the Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises;
- (d) companies that derive 1 % or more of their revenues from exploration, mining, extraction, distribution or refining of hard coal and lignite;
- (e) companies that derive 10 % or more of their revenues from the exploration, extraction, distribution or refining of oil fuels;
- (f) companies that derive 50 % or more of their revenues from the exploration, extraction, manufacturing or distribution of gaseous fuels; and
- (g) companies that derive 50 % or more of their revenues from electricity generation with a GHG intensity of more than 100 g CO₂ e/kWh.

Restricted Fund Names	Restriction
(e.g., “ impacting ” or “ impactful ”).	<p>(b) sustainable investment objectives of the fund pursuant to Article 9 of the SFDR.</p> <ul style="list-style-type: none"> • The fund must adhere to the full exclusion list prescribed under the PAB.
<p>Terms relating to “transition” in its name (e.g., “transitional” or words that derive from “improve”, “progress”, evolution, “transformation” and “net-zero”)</p>	<ul style="list-style-type: none"> • At least 80% of the fund’s investments must meet (a) the environmental and/or social characteristics promoted by the fund pursuant to Article 8 of the SFDR or (b) sustainable investment objectives of the fund pursuant to Article 9 of the SFDR. • The fund must adhere to the exclusion list prescribed under the Climate Transition Benchmark (the “CTB”).⁴ • ESMA recommends that a fund ensures that its investments are on a clear and measurable path to social or environmental transition.
<p>“Social” or “governance” terms in its name (e.g., “equality” or “controversies”)</p>	<ul style="list-style-type: none"> • At least 80% of the fund’s investments must meet (a) the environmental and/or social characteristics promoted by the fund pursuant to Article 8 of the SFDR, or (b) sustainable investment objectives of the fund pursuant to Article 9 of the SFDR. • The fund must adhere to the exclusion list prescribed under the CTB.

Use of Combined Terms. ESMA generally envisages cumulative treatment for funds that use a combination of ESG or sustainability-related terms in their names. For example, this would mean that, a fund combining an environmental- and a social-related term must meet the prescribed 80% asset allocation threshold and also ensure that its investments adhere to the PAB exclusion list.

⁴ Article 12(1) (a) to (c) of Commission Delegated Regulation (EU) 2020/1818:

- (a) companies involved in any activities related to controversial weapons;
- (b) companies involved in the cultivation and production of tobacco;
- (c) companies that benchmark administrators find in violation of the United Nations Global Compact (UNGC) principles or the Organisation for Economic Cooperation and Development (OECD) Guidelines for Multinational Enterprises;

However, to the extent a fund uses ESG- or sustainability-related terms in combination with “transition-related” terms, the fund will only have to fulfil the minimum requirements for transition-related terms as set out above (and, in particular, only comply with the limited exclusion list under the CTB).

Compliance, Reporting and Supervision. The Final Guidelines are addressed to National Competent Authorities (“NCAs”) and financial market participants which “*must make every effort to comply with these*”. However, NCAs must notify ESMA within two months following the Effective Date, of whether or not they intend to comply with the Final Guidelines, on an “explain-or-comply” basis. It remains to be seen if NCAs will opt to comply with the Final Guidelines. Therefore, the Final Guidelines use the term “*should*” when describing the requirements to be met when using ESG- or sustainability-related terms in fund names.

A temporary deviation from the 80% threshold or the applicable exclusion requirement will be considered a passive breach (which may be corrected in the best interests of the investors), so long as such deviation is not intentional. NCAs can investigate and initiate supervisory dialogue if a fund manager fails to comply, or does not “*sufficiently*” meet the minimum requirements, or fails to act honestly and/or fairly while using the restricted fund names. It will be interesting to see how NCAs handle these requirements for private equity funds that naturally have ramp-up periods before they reach the targeted asset allocation disclosed in their SFDR pre-contractual disclosure. If handled too strictly, a disadvantage for private equity funds (and similar asset classes such as private debt) may be the consequence.

Transitional Provisions and Industry Concerns. New funds established after the Effective Date must consider the Final Guidelines from day one. Funds established before the Effective Date will have an additional six months from the Effective Date to comply with the Final Guidelines (the “Transitional Period”). ESMA states it is “*conscious of the efforts in terms of time that existing investment funds may have to go through in order to adapt to the guidelines*” but is also of the view the transitions rules are “*already very generous as the guidelines will start applying 3 months after the publication of the translation and with a further 6-month transitional period for existing funds it will give managers of existing funds a minimum of 9 months’ time to comply, without taking into account the time necessary for the translations*”.

ESMA’s clarification in the Final Report indicates that ESMA makes no distinction between funds in fundraising and funds no longer in fundraising. Even closed-ended funds that were established before the Effective Date and are no longer being offered must adhere to the Final Guidelines after the Transitional Period. Therefore, fund managers should assess whether it is more feasible to change the name of the fund or adjust the investment strategy to retain the name.

Next Steps. Managers of funds containing ESG or sustainability-related terms in their names — including closed-ended funds — should start analysing possible implications of the Final Guidelines on their fund strategies and disclosures. This may entail, *either* (i) changing the name of the fund to bring it outside the scope of the Final Guidelines or (ii) adjusting a fund’s investment strategy to comply with the Final Guidelines, both of which may require changes to the fund’s legal documents, which, in turn, may potentially be subject to certain investor notification or consent rights. Given the fact that professional investors have once been admitted to such a fund while knowing of both the investment strategy and the fund name, these options seem disproportionate and are a disadvantage for private equity funds and similar funds (e.g., private debt funds or infrastructure funds).

* * *

Please do not hesitate to contact us with any questions.



Patricia Volhard
Partner, London, Frankfurt, Paris
+44 20 7786 5505
+49 69 2097 5150
pvolhard@debevoise.com



Jin-Hyuk Jang
International Counsel, Frankfurt
+49 69 2097 5115
jhjang@debevoise.com



John Young
International Counsel, London
+44 20 7786 5459
jyoung@debevoise.com



Harry Just
Associate, Frankfurt
+49 69 2097 5262
hjust@debevoise.com



Eike Björn Weidner
Associate, Frankfurt
+49 69 2097 5220
ebweidner@debevoise.com



Keith Moshe
Corporate Staff Attorney, Frankfurt
+49 69 2097 5123
kmoshe@debevoise.com

This publication is for general information purposes only. It is not intended to provide, nor is it to be used as, a substitute for legal advice. In some jurisdictions it may be considered attorney advertising.