mirova
Investing in sustainability

August 16, 2022

Vanessa A. Countryman

Secretary

U.S. Securities and Exchange Commission

100 F. Street, NE

Washington, DC 20549-1090

Via E-mail: rule-comments@sec.gov

Re: Comments on Proposed Rules regarding Enhanced Disclosures by Certain Investment Advisers and Investment Companies about Environmental, Social, and Governance Investment Practices and Investment Company Names file numbers S7-17-22 and S7-16-22 respectively.

Dear Ms. Countryman:

Mirova US LLC ("Mirova US", "our" or "we") welcomes this opportunity to comment on the Securities and Exchange Commission's (the "SEC" or the "Commission") proposed rules concerning ESG investing.

We hope this letter will aid the Commission in its consideration of the final form of the Enhanced Disclosures by Certain Investment Advisers and Investment Companies About Environmental, Social, and Governance Investment Practices proposed rule (the "Proposed ESG Rule"). As a global asset manager headquartered in Europe and exclusively dedicated to sustainable investing, we have a strong familiarity with the existing regulatory schemes that contemplate sustainable investing throughout the jurisdictions where we conduct business. We also believe our US operations and sponsorship of US funds registered under the US Investment Company Act of 1940 (the "1940 Act") qualify us to comment on the SEC's proposed amendments to Rule 35d-1 under the 1940 Act (the "Proposed Amended Names Rule").

We commend the Commission for addressing these topics. As the Proposed ESG Rule states, the absence of a common disclosure framework makes it difficult for investors to understand how effectively an environmental, social, and/or governance-related ("ESG") or "sustainable" investment strategy is being implemented. We feel strongly that comparable, consistent disclosure with a simple tiered classification, as proposed, will serve to mitigate investor confusion over ESG products.

mirova
Investing in sustainability

I. Overview of Mirova

Mirova US[1] began offering investment advice to US clients in March 2016, but our history with sustainable investing is much longer. Our parent, Mirova[2] ("Mirova France" and, collectively with Mirova US, "Mirova[3]"), began providing sustainable investment advice in France and Europe in the 1990s and became a standalone investment adviser exclusively focused on sustainable investing in 2014. Mirova managed $30.2 Billion Assets Under Management as of March 31, 2022, $9.1 Billion of which is managed by Mirova US and $1.2 Billion of which is exclusively for US investors. All Mirova strategies, including those offered to US clients, are focused on sustainability. Being so focused presents Mirova with unique opportunities to add its voice across various jurisdictions for key topics related to sustainability. Mirova is among the 1%[4] of global asset managers selected to be part of the Principles for Responsible Investing ("PRI") 2020 Leaders' Group[5] on climate reporting. Our participation in key initiatives and programs has included:

- Acting as a member of the High-Level Expert Group on Sustainable Finance that advised the European Union ("EU") Commission in 2017 and 2018 on its sustainable finance action plan, where we actively advocate for sustainable finance regulatory developments;
- Being a founding member of the Green Bond Principles and a member of its Executive Committee;
- Acting as a member of the steering committee of the Science Based Targets Initiative, which provides technical assistance to the Net Zero Asset Owner and Asset Managers Alliances;
- Acting as a member of the Net Zero Asset Managers initiative;
- Actively engaged in the Taskforce on Nature-related Financial Disclosure (TNFD) initiative by participating in the launch and serving as a member of the TNFD Mandate and Governance Working Group;
- Contributing to several global consultations, including consultations led by financial marketplaces and financial regulators such as the EU Commission, the European Securities and Markets Authority (ESMA), Monetary Authority of Singapore (MAS), Hong Kong Stock Exchange, as well as industry-led consultation such as the Task Force on Climate-related Financial Disclosures (TCFD).

[1] Mirova US began offering investment advice in the US originally as a division of Ostrum Asset Management U.S., LLC and spun-out to become a standalone investment adviser in 2019.

[2] Note Mirova France is also a "Participating Affiliate" of Mirova US. Pursuant to this arrangement, certain employees of Mirova France serve as "Associated Persons" of Mirova US within the meaning of Section 202(a)(17) of the Investment Advisers Act of 1940 and, in this capacity, are subject to the oversight of Mirova US and its Chief Compliance Officer. These Associated Persons may, on behalf of Mirova US, participate in providing discretionary and non-discretionary investment management services (including acting as portfolio managers and traders), research and related services to clients of Mirova US.

[3] Mirova France began offering investment advice originally within an affiliate, Ostrum Asset management.

[4] This percentage is representative of total signatories. To find the complete PRI Leaders methodology, please visit the PRI website here: https://www.unpri.org/showcasing-leadership/leaders-group-2020/6524.article.

[5] The PRI Leaders' Group 2020 showcases PRI signatories that, in their responses to the PRI Reporting Framework, demonstrate a breadth of responsible investment excellence, and that excel specifically in this year's theme: climate reporting.

II. General Comment on Proposed ESG Rule

Mirova very much supports the core principle underlying the Commission's proposal – to provide a consistent, comparable, and decision-useful regulatory framework for ESG advisory services and investment companies to inform and protect investors. To this end, we strongly support the adoption and implementation of the Proposed ESG Rule with many of its currently-proposed provisions. However, we respectfully request that the Commission consider several modifications to the proposed framework.

The SEC Should Seek to Align its ESG Regulatory Framework More Closely with Europe

While we applaud the SEC's efforts to propose a consistent, comparable, and decision-useful ESG regulatory framework for ESG advisory services, we believe more work needs to be done to align the proposed framework with existing frameworks in Europe, including with respect to the Sustainable Finance Disclosure Regulation ("SFDR") and the related EU Taxonomy Regulation.

Specifically, the three ESG fund classifications set forth in the Proposed ESG Rule do not align with Article 6, 8, and 9 funds under SFDR as it relates to the scope and level of sustainability ambition (as contemplated for SFDR classification purposes). For instance, certain funds that would be classified as Article 9 under SFDR (the category most aligned with "impact") might not meet the definition of an "impact" fund under the Proposed ESG Rule. While the SFDR categories still pose some interpretative questions, they aim to distinguish 3 levels of "sustainability ambition" (Article 6: none or very limited; Article 8: limited; Article 9: high) and have been so understood by market participants, including investors. Further, the fact that all EU funds must be classified under the SFDR regime has resulted in market participant adoption of the labelling system (although this was not the intent of the regulators), which we believe should be aligned with the Proposed ESG Rule categories. If not, the resulting divergent classification regimes could be misleading and will contribute to increased confusion at the end-investor level on the sustainability nature and ambition of the product that is classified in one category or another. Harmonizing these classifications would also result in greater alignment of disclosures.

Investors Would Benefit from Greater Regulatory Alignment

Many asset managers that consider ESG factors in their investment strategies are global. Likewise, many investors seek to invest globally. The lack of a comparable regulatory framework between the United States and Europe creates a risk that investors investing in (or simply looking at) both regions will not receive consistent, comparable, and reliable information among investment products and advisers (or across products offered by a single adviser) that claim to consider one or more ESG factors. While creating a strong regulatory framework in the United States is helpful, without global consistency investors would not fully benefit from what the ESG Proposed Rule is designed to do, namely help investors (and those who provide advice to investors) make more informed choices regarding ESG investing and better compare funds and investment strategies on the basis of their sustainability goals and level of sustainability ambition.

III. Definition of ESG – Disclosure of Incorporation of ESG Factors

We support requiring funds and advisers to disclose how they incorporate ESG factors into their (1) investment selection processes and (2) significant investment strategies. We, however, believe the SEC also should require funds and fund sponsors to specifically disclose the overall rationale, philosophy or thesis for utilizing ESG factors in such processes and strategies for all "integration" and "focused" funds and strategies.

In our view, such disclosure would better position investors (including prospective investors) to understand the sponsor's ESG investment intent and whether it aligns with such investors' desired investment exposure(s) and ESG philosophy. We believe that such ESG intention – rather than disclosure of the specific use of ESG factors – is what differentiates ESG investing approaches across managers, funds and strategies.

IV. Classification of the 3 Types of Strategies

As an initial matter, we agree with the SEC's conceptual approach in both applicable SEC registration statement forms and Form ADV as well as to tiering the disclosure required based on the nature and extent of ESG factor utilization in a given fund or strategy.

In our view, the most important goals for such a disclosure regime are that (i) any terminology used to discuss the various tiers of ESG funds or strategies is easily understandable and discernible by investors (and notably retail investors) and (ii) the ESG classification regime ultimately adopted can be implemented in a way that (a) delivers consistent results within and across fund complexes, (b) can be adapted to reflect the particularities and practical considerations applicable to individual fund sponsors and (c) delivers meaningful information for investors. As discussed above, we recommend aligning the final framework with the SFDR classification regime.

The Definition of ESG Impact Should Be Broadened

Under the Proposed ESG Rule, "impact" funds or strategies would be those ESG-focused funds, strategies or methods of analysis that seek to achieve a specific ESG impact or impacts. First, we believe impact should be a specific category and not a sub-category of ESG-focused, to enable end-investors to distinguish more "sustainability ambitious" funds, including those investing in listed markets, and so as also to align more closely with the rationale behind SFDR. We also believe broadening or clarifying the definition (or interpretation) of an impact fund or strategy under the Proposed ESG Rule would improve regulatory alignment with the SFDR regime and generally applicable industry and investor standards and would lead to more useful classification for end investors.[6] Within this context, it is our view that there are a significant number of funds with high levels of sustainability ambition (based on the intent to align with a sustainability impact rationale to support the transition to a sustainable economy). However, these funds would not appear to meet the definition of "impact" under the Proposed ESG Rule which, in our view, indicates that the proposed definition of impact funds is too narrow and potentially limits the classification to strategies that invest in unlisted or private markets.

[6] If, upon broadening the impact category as suggested, the SEC wishes to further differentiate the types of impact investing, we would suggest doing so consistent with the recommendations set forth in the July 2022 white paper by Eurosif and the University of Hamburg, "Classification Scheme for Sustainable Investments: Accelerating the just and sustainable transition of the real economy" (pub. avail. at https://www.eurosif.org/wp-content/uploads/2022/07/FINAL-White-Paper-Eurosif-Classification.pdf).

In light of this and as discussed in further detail in the next sub-section, it should be clear in any final regulation that it is not required for an impact strategy to "measure progress toward a specific impact" or to have a "time horizon to analyze progress" to be an impact fund. Rather, we would find it useful for managers to disclose their intention to create impact and/or make impact-aligned investments, to disclose how they measure for such impact, and to report on such impact measures accordingly. Additionally, because of how narrow this classification would be, it essentially leads to the ESG-Focused classification as being a catch-all classification.

Time Horizon Component Excludes Funds with Strong Sustainability Ambition

The time horizon component within the impact classification has the potential to exclude certain funds with strong sustainability ambition. Consider labelled bond (Green, Social, Sustainable, etc) funds – for example, funds that invest in green-labelled bonds, which are issued by a range of public market issuers to finance specific projects with environmental benefit. There is typically no time horizon for such a fund. Active green bond funds do not necessarily buy bonds at issuance and hold them to maturity and, as such, would not be able to disclose "time horizon" impact factors or "progress toward" specific impact factors. However, the fund would be able to disclose, for example, the types of projects financed by the proceeds of the green bonds it holds and the associated environmental benefit.

Current Definition of Impact Funds Creates Global Misalignment of Fund Classifications

As noted above, coherence with other global ESG frameworks such as SFDR is important to fulfil the objective of the Proposed ESG Rule and avoid investor confusion. To illustrate, consider a large cap actively managed equity fund that invests globally in companies that make material contribution to the advancement of the UN Sustainable Development Goals (SDGs). There are products on the market with this sustainability objective that are classified as Article 9 in Europe (i.e., those with high sustainability ambition) but these products would not qualify as impact funds under the Proposed ESG Rule as these strategies are not seeking a specific impact (e.g., affordable housing units) and do not have the ability to measure impact over a specific time horizon. Rather, the above example references investments that are selected by identifying companies whose products and services create a material positive impact on the SDGs with an objective to outperform the index. In terms of measurement and reporting, these types of funds may instead measure and report on the share of assets that are invested in companies that contribute to the various SDGs through their products and services (e.g., % of sales from products/services that contribute to specific SDGs), for example. These types of funds are much more ambitious from a sustainability or impact-aligned perspective in their investment strategies and in their ability to report on sustainability impact than many other types of funds that would be classified as ESG-focused. As mentioned previously, we believe these types of funds should be consistently labelled with the SFDR framework, based on their high sustainability ambition, as "impact funds."

<u>The Definition of ESG-Focused Funds Should Be Revised and Clarified</u>

Clarify the Conditions Precedent to an ESG-Focused Fund Classification

As an initial matter, there is a potential interpretational ambiguity in the proposing release that should be clarified. Specifically, we request that the SEC clarify that a condition precedent to an ESG-focused fund classification is the existence of associated principal investment strategy disclosure pursuant to Item 9(b) of Form N-1A.

Indeed, Proposed Item 4(a)(2)(i)(B) indicates that a fund may classify itself as ESG-focused if the fund focuses on one or more ESG factors by using those factors as a "significant or main" consideration (1)

in selecting investments OR (emphasis added) (2) in its engagement strategies with the companies in which it invests, which may include proxy voting and/or other direct engagement activities. In our view, many asset managers proactively proxy vote and engage directly with management, including on ESG matters. We believe it would be inconsistent with the objectives of the proposal to permit a fund to classify itself as an ESG-focused fund if the fund maintained an ESG voting and engagement program (including a robust program) without a corresponding ESG investment strategy/securities selection process. For example, one fund that simply proactively proxy votes on ESG issues would find itself in the same classification as a strategy that has robust investment selection criteria in addition to thoughtful voting and significant engagement activities. Similarly, the engagement or proxy voting disclosure should not be in the same lines as items related to investment strategies.

Enhance the Disclosures Required of ESG-Focused Funds Based on Proxy Voting & Engagement

Certain ESG-focused funds would be required to disclose pursuant to Proposed Instruction 2(f) to Item 9(b) and Items 27(b)(7)(i)(C)-(D) of Form N-1A quantitative metrics related to proxy voting and engagement activities. This includes, for example, “the percentage of ESG voting matters during the reporting period for which the fund voted in furtherance of the initiative” and “the number or percentage of issuers with which the fund held ESG engagement meetings and total number of ESG engagement meetings.” We believe that the proposed quantitative metrics would not completely capture the holistic picture that is active voting or engagement. Instead, the proposal appears to potentially prioritize disclosure of the volume of engagement over the quality.

In our experience, proxy voting and engagement work hand in hand to push for progress on ESG matters. Therefore, consistent with the theme of ESG “intentionality” discussed elsewhere in this letter, we recommend that any final rulemaking require ESG-focused funds that utilize ESG engagement strategies (including proxy voting) to:

(1) provide narrative information regarding their voting or engagement activity – in addition to the quantitative metrics proposed – that would illustrate *how* and, importantly, *why* they vote or engage consistent with their investment philosophy. This is particularly true for impact funds; and

(2) provide engagement statistics that – unlike the proposal in some respects– are accompanied by a “show your work” type description and include pertinent information such as targets set, progress achieved, and escalation if necessary.

ESG Integration Should only Encompass Funds that Hold themselves out as Using ESG as a Factor in a Material and Consistent Manner

As a general matter, we agree with the SEC’s view that including registration statement (or Form ADV) disclosure for funds that incorporate or “integrate” ESG factors or criteria in the investment process will aid investors in better understanding how funds may incorporate ESG criteria. In our view, such ESG considerations, like any other criteria used to make investment decisions (e.g., profitability, quality of management team, etc.) can be relevant to investors. We further support the SEC in the corresponding Proposed Amended Names Rule in designating materially deceptive and misleading the use of ESG or related terminology in the names of integration funds. As noted below, we believe this could help prevent “greenwashing”—an inherently deceptive practice that frustrates investors’ ability to identify funds that align with their ESG-related investment goals.

However, the current proposed definition[7] of an "integration fund" is overly broad and lacking in specificity. In our view, absent further guidance in the final rulemaking, this approach is likely to cause confusion among investors. It is also unlikely to result in meaningful disclosure for investors because (i) we expect that many funds that do not materially incorporate ESG factors in their investment strategies could qualify as "integration funds" for registration statement disclosure purposes and/or (ii) the required registration statement disclosure could cause fund sponsors to provide undue prominence to ESG strategy disclosure, thus confusing or misleading investors.

We suggest that the SEC, as part of any final rulemaking, modify the definition of an integration fund across SEC forms or provide guidance which provides a materiality qualifier and/or guidance clarifying the anticipated threshold – quantitative or qualitative – that it would expect to trigger the integration classification. Otherwise, the integration fund classification would not allow investors to distinguish between funds that are meaningfully (though not necessarily in a "focused" manner) integrating ESG information and those with less material use of ESG criteria.

V. Proposed Amended Names Rule

We support the SEC's proposal to identify various ESG terms within the scope of the Proposed Amended Names Rule as a means of ensuring that a fund that holds itself out as reflecting certain ESG values in fact invests in accordance with those values. As noted above, we further support the SEC in designating as materially deceptive and misleading the use of ESG or related terminology in the names of integration funds. We believe these proposals could help prevent "greenwashing"—an inherently deceptive practice that frustrates investors' ability to identify funds that align with their ESG-related investment goals.

We also support the proposed codification in the Proposed Amended Names Rule of the view that a fund's name could be materially deceptive or misleading for purposes of section 35(d) of the 1940 Act notwithstanding the fund's compliance with its 80% investment policy if, for example, the fund makes a substantial investment that is antithetical to its investment focus (e.g., a "fossil fuel-free" fund making a substantial investment in an issuer with fossil fuel reserves). However, we respectfully request that the SEC provide confirmation that an investment that a fund's investment adviser deems to be "neutral" (such as cash or securities of a company that neither contributes positively to nor materially subverts the Fund's ESG goal), if held in the fund's 20% basket, would not be considered to be "antithetical" to such fund's investment purpose.

[7] *See* Proposed Item 4(a)(2)(A) to Form N-1A ("a Fund that considers one or more ESG factors alongside other, non-ESG factors in its investment decisions, but those ESG factors are generally no more significant than other factors in the investment selection process, such that ESG factors may not be determinative in deciding to include or exclude any particular investment in the portfolio.").

We appreciate the opportunity to provide comments on the Proposed Amended Names Rule and Proposed ESG Rule and hope that the SEC will move forward to create a comprehensive, mandatory disclosure framework. If you have any questions, please contact me at

Sincerely,

Jens Peers

CEO of Mirova US LLC

cc: The Honorable Gary Gensler

The Honorable Allison Herren Lee

The Honorable Hester M. Peirce

The Honorable Caroline A. Crenshaw