Legal Update

ESAs Progress Reports on Addressing Greenwashing

On 1 June 2023, the ESAs published their progress Reports (“the Reports”) to help define greenwashing and greenwashing practices applicable to regulated firms. The Reports are part of a process to tackle greenwashing and ensure that expectations from stakeholders are met to assist in upholding market integrity and consumer/investor protection.

Background

With sustainable finance being a growing element in the EU Taxonomy, the European Commission requested the input of the European Supervisory Authorities, comprised of the EBA (“European Banking Authority”), EIOPA (“European Insurance and Occupational Pensions Authority”) and ESMA (“European Securities and Markets Authority”) (collectively referred to as “ESA”), to prepare reports giving a high-level understanding of the effects and risks posed by greenwashing in their respective sectors.

Definition of Greenwashing

The ESAs understand greenwashing as, “a practice where sustainability-related statements, declarations, actions, or communications do not clearly and fairly reflect the underlying sustainability profile of an entity, a financial product, or financial services.” Common examples of greenwashing are cited in the Reports and these include, inter alia: deceptive or inaccurate labelling and marketing communications. The inherent risk of greenwashing is that investors can be mislead and inappropriately induced into purchasing/availing of products/services. This also undermines confidence in legitimate related assertions.

ESMA Report Findings

The ESMA progress Report (“ESMA Report”) provides sector-specific assessments for key sectors under ESMA’s remit, such as: issuers, investment managers, benchmark administrators and investment service providers. The salient points from the ESMA Report are that:

•Misleading claims may relate to all key aspects of the sustainability profile of a product or entity, such as governance aspects, sustainability strategy and targets, or claims about sustainability impact.

•Market participants across the sustainable investment value chain (“SIVC”) face challenges implementing the necessary governance processes to support high-quality sustainability disclosures and transition efforts.

•Market participants also face difficulties in producing and accessing relevant, high-quality sustainability data.

•Forward-looking pledges from issuers on environmental, social and governance (“ESG”) future performance are particularly exposed to greenwashing.

•Corporate communications need to avoid cherry-picking, omissions, empty claims, inconsistencies and misleading use of ESG terminology.

•Fund names are exposed to greenwashing risks as they are capable of influencing retail investors’ decisions.

•The fast-moving regulatory framework has created implementation challenges for both market participants as well as National Competent Authorities (“NCAs”), and such a framework needs to better integrate sustainability impact.

•The current impact of greenwashing in funds is estimated at medium or high risk. However, such risk levels are actually expected to increase.

•To pre-emptively tackle greenwashing, the comprehensiveness of sustainability disclosures to retail investors needs to be improved, including by establishing a reliable labelling scheme.

Next Steps

The ESAs note that various challenges remain to ensure that measures are implemented to tackle greenwashing. It is anticipated that Responses to the Call for Evidence on greenwashing will be published on the ESA's websites in the coming weeks. The Final Reports will be issued by the ESAs circa May 2024, and incremental changes to the current position on greenwashing will be taken into consideration when preparing final recommendations.

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