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Keynote on greenwashing

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Chair

Introduction

Good afternoon, ladies and gentlemen,

I would like to thank the Danish Investment Association for inviting me today. I will speak about some of the opportunities and challenges ahead of us with regards to the EU sustainable finance agenda. In fact, Sustainable Finance is one of the 5 key areas that will fundamentally drive our work at ESMA in the next 5 years – as reflected in our Strategy for the period 2023-2028, which we published at the end of last year.

For the financial system to be able to facilitate the delivery of the EU's long-term sustainability objectives, the sustainable finance regulatory framework must be effectively and consistently developed and supervised. For the necessary capital flows to be channelled effectively towards sustainability objectives, investors must be able to make informed investment decisions, in line with their sustainability-related objectives.

With that perspective in mind, and in light of ESMA's mandate to protect investors, I would like to stress how transparency and comprehensibility of ESG disclosures, together with their effective supervision, are critical outcomes for ESMA. That is why addressing greenwashing risks is one of our priorities (as also spelled out in the ESMA Sustainable Finance Roadmap).

Promoting transparency and addressing greenwashing

ESG-related financial products and markets have experienced remarkable growth in the EU. With the increasing demand for sustainable investment products, there is a heightened risk of greenwashing. Moreover, as financial market regulators, we face high expectations from stakeholders to step up in ensuring investor protection and market integrity and maintaining a trustworthy environment for sustainable investments.

In May 2022, the European Commission (EC) issued a “Request for input related to greenwashing risks and the supervision of sustainable finance policies” to each of the three European Supervisory Authorities (ESAs), seeking input on:

1. On the definition of greenwashing in the financial sector;
2. On the risks greenwashing poses to investors and financial markets;
3. On the implementation of sustainable finance policies aimed at preventing greenwashing and their supervision, as well as;
4. On the potential improvements to the regulatory framework.

We at ESMA will soon publish a Progress Report on Greenwashing, responding to the Commission’s request for input. This report aims to support a better understanding of greenwashing and to assess which areas of the sustainable investment value chain are more exposed to greenwashing risks. It will also serve as a basis for laying out remediation actions, including regarding the monitoring of greenwashing, and potential future regulatory or supervisory activity.

It is unfortunately too early to give you a full presentation of the findings from this report, as the findings are still under discussion and are only expected to be published towards the end of May / beginning of June, but I would like to give you a little sense of what to expect.

Together with the reports of the other ESAs, the ESMA progress report will lay out the ESAs common high-level understanding of greenwashing. Building on existing references to greenwashing in the EU legislation, we have worked with EIOPA and

EBA to provide a common view of the scope of the greenwashing phenomena across the financial services sectors under our respective remits. This common understanding tries to address the limitations of the references to greenwashing that are currently in the EU legislation. For example, it tries to avoid looking at environmental, social and / or governance aspects in silos, and rather aims to consider sustainability claims across the full ESG spectrum.

One important point, on which we have also convergent views with the other ESAs is the fact that intentionality is not a pre-condition for the characterisation of potential greenwashing cases. Greenwashing can be unintentional and what matters to us as supervisors is whether sustainability claims are misleading or have the potential to mislead consumers and investors. This is in line with our mandates to protect consumers and investors. As supervisors, our view is that, as is usually the case with any other type of misleading information, intentionality can and should, where relevant, be considered as an aggravating factor in the context of supervisory and enforcement actions.

In its progress report, ESMA then identifies areas of the Sustainable Investment Value Chain that seem to be more exposed to greenwashing risks. For this ESMA looks at greenwashing across four key dimensions:

1. ESMA identifies three main roles that can be played by market participants in any given occurrence of greenwashing: trigger (i.e., initiator), spreader and/or (e.g. as an investor) receiver of the misleading claim.
2. Misleading sustainability claims may relate to various sustainability-related topics of relevance for market participants and (retail) investors. What we found is that claims that are more exposed to greenwashing risks are for example those covering real-world impact, how the sustainability strategy fits with the overall business strategy, and claims about ESG performance to date or pledges about future ESG performance.

3. Third, claims may be misleading in various ways, either through the actual provision of misleading information or through the omission of certain information.
4. Fourth, misleading sustainability claims can be communicated through several channels. Marketing materials, labels and product information are generally seen as more exposed to greenwashing risks.

Of course, this mapping of high-risk areas might evolve as market practices improve and the regulatory framework stabilises.

Now that I have covered broadly the mapping of risk areas that we have developed at the cross-sectoral level, let me say a few words about how greenwashing risks exemplify themselves in some key securities markets sectors that we have looked into specifically.

Let me start with the beginning of the sustainable investment value chain – the issuers. Although forthcoming regulatory requirements are expected to further improve the quality of corporate-level sustainability information, several aspects warrant increased attention for issuers. Forward-looking information and in particular pledges about future ESG performance appear to be particularly exposed to greenwashing risk. This feeds into both entity-level sustainability reporting and into the communications associated with the issuances of corporate finance instruments. What seems clear is that enhanced transparency on underlying assumptions and parameters is necessary to help investors make informed decisions, and judge the ambition and the credibility of various commitments. Providing a fair, clear and not misleading view of the sustainability risks and impact of an entity implies clear substantiation and the avoidance of cherry picking and inconsistencies across corporate communications.

On the investment management side, the highest greenwashing risk apply equally to claims regarding funds, and to entity-level claims, about the ESG profile of the asset manager. Specific high-risk areas identified are impact claims, statements about engagement with investee companies, about a fund or asset manager's ESG credentials (such as ESG labels, ESG ratings or ESG certifications), and fund names.

Benchmark administrators can act as triggers, as well as spreaders of misleading information, since benchmarks represent a key channel of transmission of claims produced by issuers and ESG data providers. The high-risk areas identified for benchmarks include for instance issues with impact claims related to EU climate benchmarks or lack of disclosure of methodologies regarding ESG data.

Finally, greenwashing risks in the investment service providers sector stem predominantly from product-level claims. The most notable situations consist of misleading claims on ESG strategy and metrics. Misrepresentation is mostly transmitted in marketing materials, product information or via labels. A high-risk area is the extent to which advice offered to retail investors takes sustainability into account.

As I mentioned earlier, this ESMA report to be published in a few weeks is a 'progress report'. Building on the findings from this progress report, we will work on a final report (due in one year's time, in May 2024), which will provide a stocktake of the supervisory response to greenwashing. It will also cover final recommendations, including on possible changes to the EU regulatory framework.

<u>Consultation on Guidelines for funds names</u>

While conducting the work on greenwashing risks, ESMA is already taking concrete action to support harmonised, comprehensible information for investors. We have recently consulted on draft guidelines on the names of funds using ESG or sustainability-related terms.

A fund's name is one of the most significant identifiers of investment funds for investors, especially retail investors, and a great marketing tool. We are concerned that some funds are using ESG or sustainability-related terms in their names without necessarily living up to the corresponding sustainability features. This could potentially be misleading and give rise to greenwashing.

In our draft guidelines we proposed some quantitative thresholds for the investments of such funds. We received very useful feedback from a broad range of stakeholders covering the financial industry, civil society, and investor representatives. The feedback received confirms the high priority all stakeholders attribute to this topic. The responses however show varying levels of support for what we proposed in the consultation paper.

ESMA is currently digesting the feedback. We are considering the appropriate calibration of the measures together with national competent authorities. We hope to be in a position to communicate publicly about the next steps after the summer.

Sustainability and investment services providers

Looking at the situation from an investor perspective, the integration of ESG considerations adds new layers of complexity to an already complex field. This can be daunting - in particular for retail investors. The few assessments made by now, show that a vast majority of retail investors want their holdings to reflect sustainability preferences. According to a survey run by 2 Degrees Investing in six European countries (Denmark, Estonia, Germany, Greece, Ireland and Romania) in Q4 2021 about households' beliefs and preferences regarding sustainable finance: "60% of retail investors have mixed financial /sustainability goal, paying attention to maximizing financial returns but also to the alignment of savings with personal values and/or the real impact on the society or the environment."[1] However, these surveys also show that sustainability-minded clients did not follow the advice provided as they thought the advice did not match their expectations.[2] We collectively need to improve this situation.

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[1] An AMF study showed that 76% of French people considered environmental impact of their holdings as important

[2] Anlageberatung zu nachhaltigen Produkten: Investoren zurückhaltend – wenig Klarheit in den Vorgaben– Seit dem 2. August 2022 sind Anlageberater aufgefordert, ihre Kunden nach ihren Nachhaltigkeits-Präferenzen zu fragen. Als Ergebnis der bisher erfolgten Beratung geben rund 36 Prozent der privaten Anleger an, dem Rat des Beraters auch gefolgt zu sein; rund 64 Prozent verneinen dies. Mehr als die Hälfte der Befragten gab an, dass die Beratung eher nicht den eigenen Erwartungen entsprochen hat. Sofern private Anleger bereit sind, in nachhaltige Produkte zu investieren, hält annähernd die Hälfte (46,7 Prozent) einen Anteil am eigenen Portfolio von unter 20

To ensure that retail investors trust the advice they are given, we need to ensure that distributors take into account investors' sustainability preferences properly. In this regard, I wish to highlight ESMA's recent revision of its Guidelines related to suitability requirements – with new requirements to collect information from clients on their sustainability preferences and requirements to assess which products fulfil those preferences as well as their other investment objectives. These revised Guidelines also clarify that investment firms need to provide staff with appropriate training on sustainability topics.

ESMA also recently updated its Guidelines on product governance to incorporate new requirements in the area of sustainability. The revised Guidelines explain that firms, when identifying the potential target market for a product, need also to set out any sustainability-related objectives the product is compatible with. This ensures the sustainability features of the products are considered when manufacturing or distributing a product. These two updated guidelines should help to ensure that investors are receiving the right information and advice about products, in a way that properly reflects the product's sustainability features.

Conclusions

I hope my short intervention today allowed me to give you a little insight into the forthcoming report on greenwashing, as well as explain what ESMA is doing in the

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Prozent für sinnvoll. Weitere rund 28 Prozent wollen mindestens zu 20 Prozent in „Grüne Werte" gehen, rund 13 Prozent mit mindestens 40, sieben Prozent mit mindestens 60 und lediglich rund 4 Prozent mit mindestens 80 Prozent. Dies sind Ergebnisse einer Befragung der DSW unter rund 150 privaten Anlagern, durchgeführt im Sommer 2022.

„Auf Anlageberater kommen mit der neuen Vorgabe erhebliche Herausforderungen zu. Sie müssen nicht nur entsprechende Produkte verfügbar haben, sondern auch die jeweiligen Präferenzen und Vorstellungen der Kunden zum Thema kennen. Zudem gibt es noch keine einheitlichen Standards für grüne Produkte oder ein entsprechendes, allgemein gültiges Label. Werden klassische Produkte schlicht umdeklariert, sind wir schnell beim Greenwashing", sagt Jella Benner-Heinacher, stellvertretende Hauptgeschäftsführerin der DSW.

[Source: https://www.dsw-info.de/presse/archiv-pressemitteilungen/pressemitteilungen-2022/anlageberatung-zu-nachhaltigen-produkten-investoren-zurueckhaltend-wenig-klarheit-in-den-vorgaben/]

area of sustainability more broadly. Sustainability will remain top of ESMA's agenda – something we have reconfirmed by making it also an EU wide supervisory priority (so called 'USSP') over the next years. You can rest assured that we will continue to monitor the market and the challenges faced by market participants and National Competent Authorities in the application and supervision of sustainable finance policies. We will identify where additional guidance or regulatory intervention might be needed and do our best to provide it. In the meantime, we count on market participants to do all they can to live up to the high expectations of investors and supervisors alike.

Thank for your attention and I wish you a fruitful rest of the conference!