PRI RESPONSE

EUROPEAN SUPERVISORY AUTHORITIES CALL FOR EVIDENCE ON BETTER UNDERSTANDING GREENWASHING

January 2023

To inform this briefing, the following investor group has been consulted: PRI EU Policy Reference Group. This consultation is not an endorsement or acknowledgement of the views expressed in this briefing.

INTRODUCTION

The Principles for Responsible Investment (PRI) works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a range of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

The PRI develops policy analysis and recommendations based on signatory views and evidence-based policy research. The PRI welcomes the opportunity to respond to the European Supervisory Authorities' (ESA) call for evidence on better understanding greenwashing.

ABOUT THIS CONSULTATION

The European Commission's 'Strategy on Financing the Transition to a Sustainable Economy' outlined steps to monitor greenwashing risks and assess whether supervisory mandates and powers are effective in addressing these greenwashing risks in cooperation with the European Supervisory Authorities (ESAs). In August 2022 the Commission delivered to the ESAs a mandate to provide evidence of greenwashing risks in the financial sector and identify supervisory actions to address those risks, with a progress report by May 2023 and a final report by May 2024.

This call for evidence sets out the ESAs' initial analysis of the core features of greenwashing and seeks input on potential examples and practices in the EU financial sector (including banking, insurance, and financial markets) relevant to various segments of the sustainable investment value chain and the financial product lifecycle. The deadline to respond is 10 January 2022.

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KEY RECOMMENDATIONS

The PRI welcomes the ESA's and the European Commission's recent focus on greenwashing risks in the financial sector, and the opportunity to provide input via this call for evidence. Overall, the PRI agrees with the ESAs proposed features of greenwashing, which are sufficiently broad and nuanced to capture the evolving nature of sustainability-related practices, claims and client expectations in the financial sector.

We support the actions proposed in ESMA's recent sustainable finance roadmap[1] to address greenwashing risks, notably:

- Working with National Competent Authorities (NCAs) to establish a shared understanding of key concepts (including by relying on existing literature by IOSCO).
- Developing supervisory capacity building and training on sustainable finance issues.
- Providing guidance to the market and NCAs on how to apply various rules in the sustainable finance single rulebook.
- Contributing to further completing the EU single rulebook on sustainable finance while promoting its consistency with international initiatives.

This last action will be particularly important to ensure a clear and coherent policy framework that accounts for sustainability risks and impacts by investors and companies. The development and completion of existing standards and policies to promote further clarity, transparency and accountability will be essential to addressing greenwashing risks within the EU framework.

The PRI's key recommendations for EU policymakers in this area are to:

- Ensure coherence with global approaches to address greenwashing where feasible, notably IOSCO's recent efforts to encourage the use of common sustainable-finance-related terms and definitions in investor reporting.
- Clarify existing sustainable finance-related definitions and concepts within EU investor reporting legislation, notably SFDR. To address greenwashing risks, it will be particularly important to distinguish between reporting on sustainability-related risks/opportunities and sustainability outcomes and clarify the levers and mechanisms for investor contribution to those outcomes within the legislation.
- Strengthen the EU's framework for stewardship with a greater focus on sustainability outcomes[2].

[1] European Securities and Markets Authority (ESMA) – Sustainable Finance Roadmap 2022-2024 (2022). Page 14.

[2] PRI defines sustainability outcomes as the positive and negative effects of investment activities on people and/or the planet. They are understood in the context of global sustainability goals and thresholds.

DETAILED RESPONSE

ESA COMMON SECTION

1. Possible features of greenwashing

1.1. Core features of greenwashing

ESA consultation paper.

This part of the survey enquires about the views of respondents on what can be seen as core characteristics of greenwashing, including:

1) Similarly with the communication of other misleading claims there are several ways in which sustainability-related statements, declarations, actions, omissions or communications may be misleading. On the one hand, communications can be misleading due to the omission of information that consumers or investors would need to take an informed transactional or investment decision (including but not limited to partial, selective, unclear, unintelligible, inconsistent, vague, oversimplistic, ambiguous or untimely information, unsubstantiated statements). On the other hand, communications can be misleading due to the actual provision of information, relevant to an informed transactional or investment decision, that is false, deceives or is likely to deceive consumers or investors (including but not limited to mislabelling, misclassification, mis-targeted marketing);

2) Greenwashing can occur either at entity level (e.g. in relation to an entity's sustainability strategy or performance), at product level (e.g. in relation to products' sustainability characteristics or performance) or at service level including advice and payment services (e.g. in relation to the integration of sustainability-related preferences to the provision of financial advice).

3) Greenwashing can be either intentional or unintentional (e.g. resulting from negligence or from misinterpretation of the sustainable finance regulatory framework requirement).

4) Greenwashing can occur at any point where sustainability-related statements, declarations or communications are made, including at different stages of the cycle of financial products/services (e.g. manufacturing, delivery, marketing, sales, monitoring) or of the investment value chain (e.g. issuer, benchmark/rating provider, investment firms, etc.).

5) Greenwashing may occur in specific disclosures required by the EU sustainable finance regulatory framework (e.g. SFDR Article 9 product-level disclosure requirements). Greenwashing may also occur as a result of non-compliance with general principles – as featured either in general EU financial legislation or more specifically in EU sustainable finance legislation (e.g. the requirement to provide information that is fair, clear and not misleading). In that context, greenwashing may occur in relation to entities that are currently outside of the remit of the EU sustainable finance legislation as it currently stands (e.g. ESG ratings).

6) Greenwashing can be triggered by the entity to which the sustainability communications relate or by the entity responsible for the product, or it can be triggered by third parties (e.g., ESG rating providers or third-party verifiers).

7) If not addressed, greenwashing will undermine trust in sustainable finance markets and policies, regardless of whether immediate damage to individual consumers or investors (in particular through mis-selling) or the gain of an unfair competitive advantage has been ascertained.

Question A.1: Please provide your views on whether the above-mentioned core characteristics of greenwashing reflect your understanding of and/or experience with this phenomenon and whether you have anything to add/amend/remove.

The PRI agrees with the ESAs proposed features of greenwashing, which are sufficiently broad and nuanced to capture the evolving nature of sustainability-related practices, claims and client expectations in the financial sector.

We would encourage the ESAs to consider how other regulatory bodies (notably IOSCO[3]) are conceptualising the phenomenon and how the ESAs' proposed definition aligns with these, notably regarding whether greenwashing can be intentional and/or unintentional (point 3).

While it is unclear to what extent IOSCO's and other definitions[4] include unintentional greenwashing, we believe that an **understanding of the drivers and features of unintentional greenwashing will also be important for supervisors and policymakers** in addressing the wider causes of the issue (including those related to the EU's sustainable finance policy framework). **When applying the definition to enforcement measures (particularly sanctions), regulatory action should focus on instances where greenwashing is deliberate and intentional**.

ESMA rightly states that greenwashing can occur because of the omission of information or due to the actual information itself (point 1). This highlights the need to ensure that mandatory disclosures for financial participants (SFDR) and companies (CSRD) and the underlying data provide the necessary information for end-investors to make an informed assessment of the accuracy of sustainability-related claims.

We therefore particularly welcome the ESAs acknowledgement that greenwashing may occur in specific disclosures required by the EU sustainable finance regulatory framework (point 5). Diverging applications of the definition of "sustainable investment" under SFDR have the potential to create important risks for both institutional and retail investors – particularly over the next few years as data and usability challenges limit the uptake of the EU taxonomy for sustainable activities (see response

[3] In its recent Call to Action on Good Sustainable Finance Practices (2022), IOSCO defined "greenwashing" as "the practice of misrepresenting sustainability-related information, practices or features throughout the investment value chain" (page 1).

[4] See also ASIC's definition of greenwashing as the practice of "misrepresenting the extent to which a financial product or investment strategy is environmentally friendly, sustainable or ethical", in its Information Sheet (INFO 271) on How to avoid greenwashing when offering or promoting sustainability-related products (2022).

to question A.4.1). The development and completion of existing standards and policies to promote further clarity, transparency and accountability will be essential to addressing greenwashing risks within the EU framework.

Within the broader analysis, we would recommend a more detailed focus on the specific claims, objectives, and strategies pursued by sustainability-related financial products and how these can be more accurately labelled or classified based on SFDR disclosures. Specifically, it will be important to distinguish between products that promote the integration of sustainability-related risks/opportunities and those that promote sustainability outcomes, both of which are relevant for many investors. The former can lead to misleading claims on the financial consequences of ESG factors on issuers, while the latter can result in misleading claims about how sustainability performance aligns with relevant sustainability goals.

The PRI agrees that greenwashing, if not addressed, may undermine trust in sustainable finance markets and policies beyond individual actors (point 7). Whilst there is no evidence at this stage that increased scrutiny on greenwashing is affecting demand (institutional or retail) for ESG or sustainability-themed products, there is a risk that insufficient clarity, transparency, and accountability may inhibit the EU's ability to align markets with its sustainability goals.

Question A.2: **Do you have or use a specific definition of greenwashing as part of your activities? If so, please share this definition.**

Whilst PRI does not have or use a specific definition of greenwashing, we find it useful to separate the *green* from the *washing.*

On *green,* there is a need for precision on environmental and social performance relative to science, targets, laws, norms and goals. To avoid greenwashing and provide useful information to the market, any sustainability claim should be verified with reference to an objective benchmark or standard. The development and application of the EU taxonomy with science-based criteria is therefore key to ensuring this within the EU.

On *washing,* arguably the misrepresentation of sustainability claims can be deliberate or unintentional as long as sustainability-related terms and concepts remain open to interpretation. But as information becomes increasingly available – and if the purpose of the *green* or *sustainable* part of the definition is clear enough – then washing will become more of a negligence issue and should become easier for investors and supervisors to identify.

1.2. Dimensions of greenwashing

1.2.1. <u>The potential roles market participants can play in greenwashing</u>

Market participants could potentially play three main different roles (trigger, spreader, receiver) in any given occurrence of greenwashing. For instance, a corporate issuer can trigger greenwashing by understating its carbon emissions. This misleading claim could be communicated to both investment managers, ESG data providers and/or other market participants some of whom might continue to spread the misleading claim to the end investors/consumers, who will be the receiver of greenwashing.

Question A.3.1. Do you agree that market participants could be involved in three different ways in greenwashing, as described above?

a) Yes
b) No

Yes, the above examples are ways that market participants could be involved in greenwashing. In addition to the example provided, it is important to highlight that market participants can play any of these roles in a given occurrence of greenwashing. For example, an investment manager or ESG data provider can trigger greenwashing by making misleading claims about their products.

1.2.2. <u>The topics of sustainability-related claims</u>

Another dimension of greenwashing is the topic of a given sustainability-related claim, which can be grouped into 3 broad topics. These can be applicable to various sectors across the sustainable value chain and can be cross-cutting at entity- and product-level. However, this does not mean that all of these 3 categories necessarily lead to greenwashing in all sectors. Moreover, it is important to note that one given claim can fall under several topics, for instance an entity making claims about targeting positive impact on climate change can be split into its actual strategy around creating positive impact (falling under Topic 2), its governance around monitoring and implementing this strategy including dedicated staff composed of impact analysts (Topic 1), while the actual metrics referenced to measure the impact would fall under Topic 3. Furthermore, greenwashing can occur in relation to an isolated claim about one of the topics listed below or it may relate to a combination of claims which in aggregate constitute greenwashing.

- *<u>Topic 1: Claims about an entity's governance and remuneration around ESG and about an entity or a product's dedicated resources to sustainability matters:</u>*
  - *Board and senior management's role in sustainability*

Topic 1 is mostly relevant for claims made at entity-level. At entity level, topic 1 is meant to cover claims about an organization's governance contribution to sustainability matters (for instance: claims about Board members' sustainability-related expertise and qualifications, claims about the Board's role in sustainability strategy approval, claims about the incorporation of sustainability into senior management performance appraisal or remuneration, etc.). Topic 1 is also meant to cover claims about a product manufacturer's integration of sustainability into firmwide policies and communicated in relation to its products.

  - ESG corporate resources and expertise

For example, claims about dedicated ESG staff, training offered by the entity to the staff, ESG credentials of dedicated ESG staff (certifications held/completed, no. of years of experience in ESG); access to ESG data-various ESG data providers specific to entity and/or to certain products

- <u>*Topic 2: Claims about the sustainability strategy, objectives, characteristics or qualifications of a product, an entity, or a service:*</u>
  - *ESG strategy, objectives, characteristics*

For instance, integration of sustainability in an entity's or product/service's strategy, characteristics, objectives, taking into account clients' sustainability preferences. Some relevant cases in point would be: for funds: current ESG strategies (best in class, exclusions), how financially material ESG factors are identified and integrated in the investment and product design process, environmental and/or social characteristics promoted, sustainable objectives promoted, as well as classifications summarizing the strategy (e.g SFDR Art.6/8/9 , Climate benchmarks), For sustainable products offered under MiFID II like sustainability-linked bonds (SLBs), derivatives (SLDs), sustainability improvement loans (SIls): environmental and/or social characteristics promoted by the KPIs linked to the bond/derivative/loan/security. For products with sustainability features sold under IDD like IBIPs environmental and/or social characteristics promoted by the KPIs linked to the underlying investments and/or the investment strategy of the company. For insurers this, in addition, also includes this includes the business strategy, statements made in transition plans and commitments to aligning their underwriting and investment portfolios with net zero emissions by a certain date, sometimes in conjunction with joining initiatives such as the Net Zero Insurance Alliance. For banks, this includes the business strategy, statements made in transition plans and commitments to aligning their lending and investment portfolios with net zero emissions by a certain date, sometimes in conjunction with joining initiatives such as the Glasgow Financial Alliance for Net Zero (GFANZ).

  - *Sustainability management policies*

For instance, all claims regarding an entity or product's policy on sustainability including the consideration or management of ESG risk or consideration or management of ESG impact these claims can be communicated via any type of channel or document, including in firmwide or product-level policies

  - *ESG qualifications / labels / certificates*

Adherence to (voluntary) reporting frameworks, labels, ratings, awards, certifications; For green bonds: certifications like by specialized organizations with established frameworks for assessing green bonds, ratings by approved green bond verifiers, mentions of inclusion in ESG/green bond benchmarks

  - *Engagement with stakeholders*

Examples would include claims on engagement priorities, what engagement methods are used, active engagement activities at entity or product level, voting on climate and social issues, how engagement is integrated in the investment decision process, etc.

- <u>*Topic 3: Claims about sustainability-related metrics based on historical data or future targets:*</u>
  - *ESG performance to date (including metrics for impact claims)*

Relevant cases in point would be metrics based on backward looking data, in the form of ESG or impact metrics (carbon intensity, gender diversity ratios, SFDR PAIs, ESG ratings, SDG alignment scores, internal impact scores,).

  - *Pledges about future ESG performance (ESG targets, including net-zero commitments; transition plan, taxonomy alignment plans)*

Question A.4. Please indicate the degree to which you consider each topic described above, as prone to the occurrence of greenwashing. Please provide a score from 1 to 5 (where 1 = very low occurrence ; 2 = low occurrence ; 3 = neutral ; 4 = high occurrence ; 5 = very high occurrence).

- Board and senior management's role in sustainability (Topic 1, i) **- 3**
- ESG corporate resources and expertise (Topic 1, ii) **- 3**
- ESG strategy, objectives, characteristics (Topic 2, i) - **4**
- Sustainability management policies (Topic 2, ii) **- 3**
- ESG qualifications / labels / certificates (Topic 2, iii) **- 3**
- Engagement with stakeholders (Topic 2, iv) **- 4**
- ESG performance to date (including metrics for impact claims) (Topic 3, i) **- 4**
- Pledges about future ESG performance (ESG targets, including net-zero commitments; transition plan, taxonomy alignment plans) (Topic 3, ii) **- 4**

Note: we understand "neutral" (3) as "medium occurrence" in this context.

Question A.4.1. Please specify the underlying drivers of greenwashing in relation to the topics you scored higher.

ESG strategy, objectives, and characteristics (topic 2, i)

The lack of clarity surrounding key concepts and definitions within the EU sustainable finance policy framework (notably SFDR) is an important driver of greenwashing risks relating to financial products' strategy, objectives, and characteristics.

Due to uncertainties[5] over the application of the definition of "sustainable investment" under SFDR and expectations for methods of calculating sustainable investments[6], investors subject to SFDR may be exposed to allegations of mis-selling or greenwashing. The requirement for financial products under Article 9 to be constituted almost exclusively of sustainable investments[7] may also create incentives for investors to apply looser interpretations of the definition to meet client expectations for products with a sustainability objective categorised under Article 9 of SFDR.

There is also growing evidence[8] that Article 9 products are being characterised as impact-generating products, which may be misleading under the current sustainable investment definition depending on the type of investments (e.g. asset class/ public or private market) and their ability to achieve impact (e.g. investment and stewardship approach). This is a particular area of concern given the growing

[5] We acknowledge and welcome the ESA's formal request to the European Commission to clarify the definition of "sustainable investments" under SFDR Article 2.17.

[6] For example, it is currently unclear whether sustainable investments should be calculated in a binary way at entity-level or as a percentage of an investee entity's (sustainable) activities.

[7] As clarified in the Commission's 2021 FAQ and Recital 15 of the SFDR Delegated Regulation.

[8] The Impact of Impact Funds – A Global Analysis of Funds with Impact-Claim', Lisa Krombholz, Timo Busch and Johannes Metzler, April 2022.

investor (especially retail/consumer) appetite for impact-oriented financial products[9], which is likely to increase following the integration of client sustainability preferences into financial advice[10].

Additionally, confusion over definitions of "consideration of principal adverse impacts (PAI)" (under Article 7 SFDR) and "promotion of environmental and social characteristics"[11] (under Article 8 SFDR) risk leading to diverging interpretations and expectations among investors across the value chain including (retail and institutional) clients.

Engagement with stakeholders (topic 2, iv)

Engagement/ stewardship[12] is one of the most effective levers investors have at their disposal to contribute to real-world sustainability outcomes. Yet it is often difficult to evaluate the quality of investors' stewardship efforts. Data from the PRI's Reporting & Assessment framework shows that while a majority of asset owners reporting against the framework assess how prospective and existing managers implement a stewardship policy, oversight of specific stewardship actions – such as how the escalation process is deployed, and the levels of involvement in collaborative initiatives – is less common[13]. This partly reflects the lack of clear standards and transparency on best practices when it comes to stewardship[14], which can make it particularly vulnerable to greenwashing risks, particularly when used to demonstrate contribution to sustainability outcomes.

Pledges about future ESG performance (ESG targets, including net-zero commitments; transition plan, taxonomy alignment plans) (Topic 3, ii)

Net zero commitments can be particularly prone to greenwashing risks or allegations given the rapid rise of such pledges by financial institutions over the past few years and the inherent complexity of climate target-setting and portfolio alignment methodologies.

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[9] 2 Degrees Investing – Fighting greenwashing…what do we really need (2022). Page 7.

[10] European Commission Delegated Regulation amending MIFID II as regards the integration of sustainability factors, risks and preferences into certain organisational requirements and operating conditions for investment firms (2021).

[11] For example, environmental and/or social characteristics could be interpreted as characteristics of the investment product (how ESG factors affect investment decisions - exclusion, screening, etc) or the characteristics of the underlying investee companies (sectoral or thematic exposure).

[12] We define stewardship, also referred to as active ownership, as the use of influence by institutional investors to maximise overall long-term value, including the value of common economic, social and environmental assets, on which returns, and clients' and beneficiaries' interests, depend. PRI and World Bank Group (2020), How Policy Makers Can Implement Reforms for a Sustainable Financial System.

[13] Inside PRI Data: Asset owner action (PRI, 2022). "The least common stewardship activities monitored are the degree to which managers take an active role in collaborative stewardship initiatives (ranging from 23% to 64% for all assets, across classes), and how the escalation process is deployed in instances where initial stewardship efforts are unsuccessful (29%-43%)."

[14] PRI is aiming to contribute to greater clarity by including questions about how activities like stewardship are used to contribute to sustainability outcomes, which can be answered on an optional basis, into its Reporting & Assessment framework.

The alliances under the GFANZ[15] umbrella provide important spaces for investors to collaborate on meeting ambitious net zero commitments, and detailed frameworks[16] have been developed to guide common approaches to target-setting. Yet the requirements of the different initiatives can vary in terms of the scope of assets covered by the pledge, for example: partial or full value chain assessment, asset class coverage, the metrics used for target-setting (e.g. carbon intensity or absolute emissions, implied temperature rise, sectoral targets, engagement targets, etc.), approaches to phasing-out of fossil fuel financing, use of voluntary carbon credits, etc. Continued progress on convergence in net-zero target setting methodologies, accountability mechanisms within the alliances and timely implementation of the UN HLEG recommendations for non-state net zero pledges[17] will be important to reduce greenwashing risks related to net zero claims by financial institutions.

Question A.5. For the same list of topics listed in the previous question, please provide a score from 1 to 5 on the potential harm/impact of a misleading claim made on that topic (where 1 = very low impact ; 2 = low impact ; 3 = neutral ; 4 = high impact ; 5 = very high impact).

- Board and senior management's role in sustainability (Topic 1, i) **- 3**
- ESG corporate resources and expertise (Topic 1, ii) **- 3**
- ESG strategy, objectives, characteristics (Topic 2, i) - **4**
- Sustainability management policies (Topic 2, ii) **- 3**
- ESG qualifications / labels / certificates (Topic 2, iii) **- 3**
- Engagement with stakeholders (Topic 2, iv) **- 4**
- ESG performance to date (including metrics for impact claims) (Topic 3, i) **- 4**
- Pledges about future ESG performance (ESG targets, including net-zero commitments; transition plan, taxonomy alignment plans) (Topic 3, ii) **- 4**

Note: we understand “neutral” (3) as “medium occurrence” in this context.

Question A.5.1. Please explain what types of impacts or harm and their consequences you anticipate as a result of greenwashing practices.

Despite clearer global sustainability goals, there is a widening gap between these stated goals and the real-world outcomes being achieved. The growing gap, and a rapidly growing market for sustainable finance, is leading to more scrutiny by market supervisors on financial practices and claims, including prosecutions for egregious failures. A lack of transparency and accountability will

[15] In the financial sector, these pledges are structured at entity level within the Glasgow Financial Alliance for Net Zero (GFANZ), launched in 2021. As of November 2022, the alliances comprised over 550 financial institutions (banks, insurers, asset owners, and asset managers) from a diverse range of 50 countries. GFANZ 2022 Progress Report.

[16] GFANZ – Financial Institution Net Zero Transition Plans (2022). UN-Convened Net Zero Asset Owner Alliance – Target-Setting Protocol (2022).

[17] In November 2022 the UN’s High-Level Expert Group on the Net Zero Emissions Commitments of Non-State Entities published a report with practical recommendations to improve the integrity, transparency and accountability of non-state net zero pledges by establishing clear standards and criteria.

inhibit trust in the financial sector's ability to align investments with sustainability goals and assess their contribution.

Additionally, greenwashing practices can mislead end-investors on the impact or consequence that an investment product can achieve in sustainability terms. This is particularly the case when firms use the same terms to promote sustainability performance, regardless of whether the finance causes, contributes to, or is only linked to sustainability outcomes or impact.

Please see our response to question F.7.2 in the ESMA section for a more detailed analysis of the potential impacts of greenwashing.

Question A.6. In addition to the three topics and eight sub-topics above, do you identify any additional topics which would be relevant to potential greenwashing issues?

- **a) Yes**
- b) No

Several additional sub-topics would be relevant to potential greenwashing issues.

Currently Topic 2 would cover a reporting entity's strategy and objectives related to sustainability issues. However, it should also cover how the strategy has been implemented in practice, and the results of this – such as proxy votes or changes to the risk/return profile of a fund or product.

In addition, to improve clarity, the sub-topic "engagement with stakeholders" under Topic 2 should reference reporting on stewardship (engagement, stewardship outcomes and proxy voting), engagement with other stakeholders, and communication along the investment chain (including reporting on agent-principal and principal-agent communication) – all of which can be subject to greenwashing.

Finally, Topic 3 currently distinguishes between past and future sustainability performance (how the reporting entity's investments affect people and the environment) but should also account for reporting on sustainability-related risks/opportunities and sustainability outcomes, both of which are relevant for many investors. The former can lead to misleading claims on financial consequences of ESG factors on issuers, while the latter can result in misleading claims about how sustainability performance aligns with relevant sustainability goals.

Question A.7: Please indicate below if you have any additional comments regarding the relevance of the above topics on which sustainability-related claims are made in the context of a given sector or entity. (4000 characters).

No PRI response.

1.2.3 The way in which a claim can be misleading

Question A.8. On a scale from 1 (i.e. "not at all relevant") to 5 ("very relevant"), please indicate the extent to which you find each of the misleading qualities of a sustainability-related claim listed below relevant to greenwashing practices.

No PRI response.

1.2.4 Which communication channel

Another dimension of greenwashing is represented by the channels through which sustainability-related claims are communicated to other actors in the sustainable value chain.

These channels include, but are not limited to, the following: (1) Regulatory documents (including Key Investor Documents or Key Information Documents (KIDs), prospectuses, financial statements, management reports, non-financial statements, benchmark statements and methodology documents, insurance—product information documents, pension benefit statements, etc.) or regulatory disclosures, (2) Ratings19/benchmarks/labels, (3) Product information (including internal classifications and internal target market, product testing and distribution strategy related documentation), (4) Intermediary/advice information, (5) Marketing materials (including website, social media), (6) Voluntary reporting, falling outside previous categories as reported on a voluntary basis.

Question A.9. Regarding the above dimension and the list of channels through which misleading claims can be communicated to other segments of the sustainable value chain, please indicate the likelihood that a given channel serves to communicate misleading sustainability claims made at entity level and/or at product/service level. Please score each channel from 1 (rather unlikely) to 5 (very likely):

No PRI response.

Question A.9.1. Please indicate below if you have any comments regarding the communication channels of potentially misleading sustainability-related claims?

No PRI response.

1.2.5 At which stage of the lifecycle and where in the business model/management does greenwashing occur

In addition to the different channels of transmission of claims, greenwashing can also occur at various stages of the product lifecycle, including: the product manufacturing stage (product development, product design, market targeting), the product delivery stage (marketing, product-related disclosure, distribution, sales), the product management stage (product monitoring/review, ongoing product-related disclosure). Beyond the product lifecycle, greenwashing can occur at the entity-level: in the business model (value chains, group structures, innovation and technology, outsourcing) or in the business management (culture, governance arrangements, systems and processes).

Question A.10. For each of the stages of product lifecycle and with regard to the business model and management, please indicate the likelihood of the occurrence of greenwashing. Please provide scores ranging from 1 (rather unlikely) to 5 (very likely):

No PRI response.

1.2.6 Further considerations

Q A.11: Are there any relevant elements or features of greenwashing which have not been referenced in the questions above?

a) Yes

b) No

2. Examples of potential greenwashing

This section of the survey relates to the collection of examples of potential greenwashing practices that you may have encountered that we would like to encourage you to describe below. These examples can be within or outside the current scope of the EU sustainable finance legislation and should refer to the financial sector within the remit of at least one of the ESA's. This CfE does not seek input in relation to sustainability-related claims made regarding entities, products or services not under the scope the ESAs, like sustainability-related claims regarding non-financial products (e.g. consumer goods). Please make sure to provide examples for which you can answer at least some of the below questions. Please provide the details of the described cases to the best of your knowledge.

Please bear in mind that the purpose of this survey is to gather useful and concrete examples that will help the ESAs to better understand greenwashing. Greenwashing cases reported in this CfE are mainly sought for the purpose of informing the advice which the ESAs would provide to the European Commission. Therefore, you may either give full details about the actual names of the entities or products involved in a potential greenwashing practice, or you may refer to them as 'entity X', 'product Y'.

Respondents can provide up to 5 examples of greenwashing in this survey. If you are able to identify more examples of greenwashing, please choose those cases which are the most relevant in your view, and the most likely to occur.

Question A.12. Are you able to identify and characterise at least one example of potential greenwashing practice?

a) Yes, I can provide at least one example of potential greenwashing practice.

b) No, I cannot identify a specific example of potential greenwashing practice.

Question A.12.1: (If no) If you have not identified occurrences of greenwashing, what is the reason for that?

a) There is no specific methodology on how to detect (potential) greenwashing cases

b) As sustainable finance requirements (including definitions and disclosure standards) are new/not in force yet, greenwashing is hard to detect

c) Few or no products with sustainability features are offered in my jurisdiction / entity / area of interest, decreasing the risk of greenwashing

d) I have not encountered any instances of greenwashing.

e) Other, please specify below

ESMA SECTION OF THE CALL FOR EVIDENCE

The ESMA-specific section of the survey below covers questions relevant to entities and products under ESMA's remit.

All financial market participants and issuers under the remit of ESMA are invited to provide answers to this section. Other stakeholders ranging from retail investors and consumers associations to NGOs and academia are also invited to participate to the extent the views and expertise provided are relevant to ESMA's activities.

1. Understanding the drivers and the scale of greenwashing risks

As stated previously, the drivers of greenwashing are multifaceted and better understanding them is critical to addressing the issue.

F.1. Which of the elements listed below, do you consider to be the main driver(s) of greenwashing risks? Please provide a short explanation of your answer: [multiple answers allowed]

a) New / innovative ESG products in rapidly evolving ESG markets

b) Entry of new participants such as issuers of ESG products, ESG rating or data providers, etc.

c) Lack of ESG expertise and skills of market participants

d) A rapidly evolving regulatory framework

e) Differing interpretations of the regulatory framework

f) Desire to exaggerate the sustainability profile at entity/product or service level

g) Competition (wanting to be better than a comparable issuer/product)

h) Lack of reliable data

i) Mismatch between retail investors' expectations and market participants' ability to deliver real-world impact

j) Financial literacy

k) Other, please specify: ___________________________________

Please elaborate briefly on the answer to question F.1

The list of drivers above is exhaustive. We would also add 'attribution of impact or consequence to finance' given the challenge of accurately explaining what an investment product achieves in sustainability terms (e.g. whether the investor is causing, contributing to, or simply linked to a sustainability impact or outcome).

F.2. As stated before, this CfE uses the term greenwashing broadly, covering sustainability-

> *Through the questions below, we seek to better understand which ESG aspect(s), which segment(s) of the sustainable investment value chain, and which asset class(es) or product category(ies) may be more prone to greenwashing risks, in relative terms.*

related claims relating to all aspects of the ESG spectrum. While the sustainable finance legislation gives more prominence to environmental aspects, we would like to understand which aspects of the ESG spectrum may be more prone to greenwashing risks, at this stage? Please rate the three aspects below from 1 to 5 (where 1 = very low occurrence ; 2 = low occurrence ; 3 = medium occurrence ; 4 = high occurrence ; 5 = very high occurrence [multiple choice]

No PRI response.

F.3. Greenwashing may apply to claims at both entity- and/or product-level (including service-related). Based on your experience, we would like to understand which level may be more prone to greenwashing risks in various sectors. For each of the market segments listed below, please select one of the four options, then please provide a short explanation.

No PRI response.

F.4. For market segments which you see as more prone to greenwashing risks, please provide below any quantitative or qualitative data (and relevant links) you may have and that could help inform our understanding of the scale and frequency of potential greenwashing practices. You may also upload files if relevant in the next field.

No PRI response.

F.5. With regards to product-level sustainability-related claims, we want to better understand which asset classes, financial products categories may be more prone to greenwashing risks. For each of the asset classes and/or financial products regarding which your expertise is relevant, please provide a score from 1 to 5 (where 1 = very low occurrence ; 2 = low occurrence ; 3 = medium occurrence ; 4 = high occurrence ; 5 = very high occurrence of greenwashing). [multiple answers allowed]

No PRI response.

F.6. Greenwashing practices can be transmitted over more than one segment of the sustainable finance value chain. Various options are described below representing various greenwashing transmission trajectories of sustainability-related claims, where the first entity is always the trigger with subsequent entities being either in the role of spreader and/or receiver of claims. Based on you experience, we would like to understand which transmission trajectory may be more prone to greenwashing risks. Please provide a score for each transmission trajectory listed below from 1 to 5 (where 1 = very low occurrence; 2 = low occurrence; 3 = medium occurrence; 4 = high occurrence; 5 = very high occurrence [multiple answers allowed] (multiple responses possible)

No PRI response.

2. Consideration of greenwashing risks by financial market participants and issuers

It appears that some industry players already perceive greenwashing as a source of potential risks for their own development and performance and have started to take action with the view to mitigate such risks. The following section seeks to collect insights on how financial market participants and issuers perceive greenwashing and take action to address the issue at their level.

F.7. Does your organisation perceive greenwashing as a potential source of risk?

a) Yes, and we have started developing a structured approach to tackling the issue

b) Yes, but we have not yet developed a structured approach to the issue

c) No

d) Other, if so specify

F.7.1. If you answered a) or b) to Q7: what category of related risks do you anticipate could result from greenwashing issues? [multiple answers allowed]

a) Financial risks

b) Reputational risks

c) Legal risks

d) Other, if so specify

F.7.2. If you answered a) or b) to Q7: what types of potential negative impacts do you anticipate as a result of greenwashing issues?

In addition to the above risks to financial institutions, greenwashing may undermine trust in sustainable finance markets and policies beyond individual actors if not addressed. Whilst there is no evidence at this stage that increased scrutiny surrounding greenwashing is reducing demand (institutional or retail) for sustainability-themed products, there is a risk that insufficient clarity, transparency, and accountability may inhibit the EU's ability to align markets with its sustainability goals.

Climate change and related material risks, impacts, and opportunities have emerged as the most relevant ESG issue for many responsible investors. All material risks for investors – which include physical risks[18], transition risks[19], and systemic risks[20] – are exacerbated by greenwashing due to lack of adequate climate-related risk assessment, reporting, and disclosure.

Assessing, planning, and preparing for such risks in investor decisions requires adequate data, scenario analysis and assessment, and transparent reporting. For example, investor climate action plans and net zero emission targets rely on robust and credible disclosure frameworks, based on science-based targets. Reporting standards or practices which are inconsistent, vague, and do not transparently assess material climate risks may result in an inadequate risk mitigation strategy and delayed action. Greenwashing, unclear reporting standards, and inadequate disclosure all contribute to portfolio risks, less efficient investment decisions, and a potential misallocation of capital.

F.7.3. If you answered a) to Q7: What safeguards / risks mitigants have you (or are you planning to) put in place to address greenwashing risks?

No PRI response.

F.8. Do you know of any industry initiative that could be instrumental in tackling greenwashing?

No PRI response.

F.9. Which do you think are the market mechanisms that can help mitigate greenwashing risks (e.g. reputational issues) and how do you believe supervisors can help in this respect?

No PRI response.

F.10. What could policymakers and regulators do more to alleviate greenwashing risks?

The PRI supports the actions proposed in ESMA's recent sustainable finance roadmap[21] to address greenwashing risks, notably:

- Working with National Competent Authorities to establish a shared understanding of key concepts (including by relying on existing literature by IOSCO).
- Developing supervisory capacity building and training on sustainable finance issues.

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[18] Physical risks manifest as acute natural disasters, e.g., damages from storms, fires, and heat waves, and chronic events, like crop loss due to longer-term droughts or soil erosion.

[19] Transition risks are related to social, economic and financial responses to climate change, for example: new regulations affecting the value chain; shifts in demand, supply or financial conditions due to changing consumer or investor preferences; substitutions in products or services due to new technology and lower-carbon solutions; or reputational damage due to an organization's emissions or effect on natural ecosystems.

[20] Systemic risks arise from ecosystem collapse, and wholesale geographic or sectoral losses; aggregated risks due to physical and transition risks across one or more sectors impacting financial or corporate portfolios; and contagion as difficulties in one or more financial institutions spill over into the financial system as a whole.

[21] European Securities and Markets Authority (ESMA) – Sustainable Finance Roadmap 2022-2024 (2022). Page 14.

- Providing guidance to the market and NCAs on how to apply various rules in the sustainable finance single rulebook.
- Contributing to further completing the EU single rulebook on sustainable finance while promoting its consistency with international initiatives.

This last action will be particularly important to ensure a clear and coherent policy framework that accounts for sustainability risks and impact by investors and companies. The development and completion of existing standards and policies to promote further clarity, transparency and accountability will be essential to addressing greenwashing risks within the EU framework.

The PRI's key recommendations for EU policymakers within this context are to:

- Ensure coherence with global approaches to address greenwashing where feasible, notably IOSCO's recent efforts to encourage the use of common sustainable-finance-related terms and definitions in investor reporting.
- Clarify existing sustainable finance-related definitions and concepts within EU investor reporting legislation, notably SFDR. To address greenwashing risks, it will be particularly important to distinguish between reporting on sustainability-related risks/opportunities and sustainability outcomes and clarify the levers and mechanisms for investor contribution to those outcomes within the legislation.
- Strengthen the EU's framework for stewardship with a greater focus on sustainability outcomes.

Work towards international coherence of investor sustainability reporting frameworks and terminology

The PRI recently conducted a review of ESG reporting requirements facing our signatories, across nine key jurisdictions. Findings are captured in our report: [Review of trends in ESG reporting requirements for investors].

We found that many jurisdictions had adopted approaches to tackling greenwashing, albeit differently across what we refer to as "medium- and high-regulation jurisdictions".

- "Medium-regulation jurisdictions" typically adopt what we refer to as a "tell me" approach – whereby investors are required to report on their policies on ESG issues, their overarching ESG objectives, strategy and how the strategy has been implemented.
- Rules in "high-regulation jurisdictions", such as the SFDR and EU Taxonomy, tend to involve what we have termed a "show me approach" – whereby in addition to the above investors are also required to report on the results of their actions or the sustainability outcomes of investments. This approach provides retail investors and fund members/beneficiaries with greater clarity on what their money is invested in and how investment decisions are made.

In addition, we found that ESG issue-specific reporting is growing. On climate reporting, regulators are starting to require disclosures aligned with recommendations by the Task Force on Climate-related Financial Disclosures (TCFD). Also, there are emerging reporting frameworks on specific ESG issues that are likely to gain traction in the coming years, including the Taskforce on Nature-related Financial Disclosures, and an emerging trend of reporting the risk of modern slavery (and other human rights abuses) in investments and the response to this risk.

The above findings reflect progress made by regional and international policymakers, regulators, and standard setters in addressing greenwashing.

However, they also indicate a growing differentiation in investor regulations targeting greenwashing across jurisdictions. For instance, we recognise there are differences in terms of objectives and scope of such regulations, which may focus on:

- inputs to the investment process (e.g. policies, objectives and/or strategy), the process itself (e.g. implementation and results), and/or outputs (e.g. sustainability performance); and
- different topics, including sustainability-related risks and opportunities, sustainability performance and/or sustainability outcomes.

There is a need for improved regulatory coherence globally to reduce the scope for greenwashing. For instance, product-level disclosure requirements tend to vary across jurisdictions on different types of "sustainable products", meaning investors cannot effectively compare these. There is also a need to harmonise sustainable taxonomies across jurisdictions, including the terminologies, thresholds and sector classifications upon which these are built.

We welcome IOSCO's 2021 recommendations and Call for Action, which provide a sound basis to address these issues by encouraging the use of common sustainable finance-related terms and definitions, and reporting on areas including but not limited to:

- the development and implementation of practices, policies, and procedures relating to material sustainability-related risks and opportunities; and
- a broad range of topics (e.g.. "risk") and processes (e.g. proxy voting and shareholder engagement) related to sustainability-related products, and material sustainability-related risks and opportunities for all products.

Encouraging adoption of IOSCO's recommendations across jurisdictions would help to promote regulatory coherence for investors and thereby address the abovementioned challenges.

Clarify existing definitions, concepts, and levers for investor impact within EU investor reporting legislation

To address greenwashing risks, it will be particularly important to distinguish between reporting on sustainability-related risks/opportunities and sustainability outcomes and clarify the levers and mechanisms for investor contribution to those outcomes within the legislation.

EU policymakers should clarify some of the key components of sustainability-related product categories under SFDR, particularly minimum expectations for the i) promotion of ESG characteristics, ii) the consideration of principal adverse impacts (PAI), and iii) assessment of sustainable investments under SFDR (see response to question A.4.1. for our view on how this uncertainty risks creating a misalignment of expectations across the investment chain).

The SFDR Delegated Regulation[22] states that it is "necessary to address concerns about 'greenwashing', that is, in particular, the practice of gaining an unfair competitive advantage by recommending a financial product as environmentally friendly or sustainable, when in fact that financial product does not meet *basic environmental or other sustainability-related standards*". In line with the European Commission's commitment[23] to develop "minimum sustainability criteria for financial products that promote environmental or social characteristics", there may be a need to define these basic standards, at what level (e.g. investment decision process or investee sector/activity) and on what basis they should be set (e.g. a short list of "always significantly harmful" activities that are incompatible with sustainability objectives, as proposed by the EU Platform on Sustainable Finance[24]).

Policy reforms and guidance should ensure regulatory coherence and seek to accurately reflect the tools investors have to create change. This must entail a move away from the assumption that the impact of an investment strategy is the same as the characteristics of the underlying portfolio, and instead support and develop the full range of tools investors have available to influence real-economy outcomes, including capital allocation, stewardship and real-economy policy engagement.

The Taxonomy and SFDR both set frameworks for understanding the impact of financial products on the environment and society. These regulations affect the same firms and funds and embed similar concepts (such as making a substantial contribution to sustainability objectives while avoiding significant harm). Both also build from the OECD Guidelines on Responsible Business Conduct for Institutional Investors. The ESAs and the European Commission should work towards the development and greater integration of these regulations and frameworks taking inspiration from the recent recommendations of the EU Platform on Sustainable Finance[25]. Where feasible, the upcoming review[26] of the PAI framework under SFDR should seek to:

- reflect the OECD Responsible Business Conduct for Institutional Investors Guidelines framework for understanding investor impact (cause, contribute, or be directly linked to) rather than reflect the characteristics of the underlying investment, and
- contextualise the impact in relation to the EU goals and laws, such as climate neutrality.

Providing more detailed guidance around expectations for investor impact claims will therefore be particularly important, especially at product-level as this is where many clients will express their sustainability preferences. A number of studies and surveys have shown considerable investor

[22] Recital 16 of Commission Delegated Regulation (EU) 2022/1288 (page 12).

[23] "The Commission will propose minimum sustainability criteria, or a combination of criteria for financial products that fall under Art. 8 of the SFDR, in order to guarantee minimum sustainability performance of such products to further strengthen a harmonised application of the Regulation and incentivise transitional efforts.". European Commission Strategy for Financing the Transition to a Sustainable Economy (2021) – action 1(e) page 3.

[24] EU Platform on Sustainable Finance - Recommendations on Data and Usability (2022). "The Platform recommends the European Commission to consider the use of PAIs as the tool to set minimum criteria for Article 8 products. The Platform recommends setting very low maximum tolerance thresholds for the "always principle adverse" indicators, and the rest of PAIs to measure good practice and/or progress over time." page 150.

[25] EU Platform on Sustainable Finance - Recommendations on Data and Usability (2022).

[26] Mandate from European Commission to ESAs on the revision of the Principal Adverse Impact indicators (2022).

(especially retail/consumer) appetite for impact-oriented financial products[27]. ESMA's recent supervisory briefing[28] and proposed fund name guidance[29] state that impact claims in financial products "*should be used only by funds whose investments are made with the intention to generate positive, measurable social and environmental impact alongside a financial return*". Beyond assessment against the EU Taxonomy for environmental objectives, EU policymakers should support the development of guidance and tools[30] to help investors demonstrate how a product is generating "positive, measurable social and environmental impact", and how this impact relates to global sustainability goals.

Strengthen the EU's framework for stewardship with a greater focus on sustainability outcomes

As explored in the response to question A.4.1, stewardship[31] is one of the most effective levers investors have at their disposal to contribute to real-world sustainability outcomes. Yet it is often difficult to evaluate the quality of investors' stewardship efforts where there are no clear standards and transparency requirements. This can make stewardship particularly vulnerable to greenwashing risks as a practice and can create room for mismatches between clients' expectations and investors' actions.

The existing EU legislative framework could go further to incentivise high-quality, outcomes-focused stewardship. The PRI's Strengthening Stewardship in the EU (2021) position paper explores how stewardship could be better integrated into the EU policy framework in greater detail. At investor entity level the EU should prioritise the review of the Shareholders Rights Directive II, as announced in the Commission's Renewed Sustainable Finance Strategy[32], to clarify stewardship standards by recognising best practices in the market. The revision could mandate disclosure of stewardship policies, activities, progress and outcomes (beyond the current comply or explain requirements),

[27] 2 Degrees Investing – Fighting greenwashing…what do we really need (2022). Page 7.

[28] ESMA – Supervisory Briefing – Sustainability risks and disclosures in the area of investment management (2022). "The use of the word "impact" or "impact investing" or any other impact related term should be used only by funds whose investments are made with the intention to generate positive, measurable social and environmental impact alongside a financial return". Page 9-10.

[29] ESMA – Consultation Paper on Guidelines on funds' names using ESG or sustainability-related terms (2022). "Funds using the word "impact" or "impact investing" or any other impact-related term in their name should meet the proposed thresholds and additionally make investments with the intention to generate positive and measurable social or environmental impact alongside a financial return". Page 11.

[30] Based on academic research and building on existing industry frameworks.

[31] We define stewardship, also referred to as active ownership, as the use of influence by institutional investors to maximise overall long-term value, including the value of common economic, social and environmental assets, on which returns, and clients' and beneficiaries' interests, depend. PRI and World Bank Group (2020), How Policy Makers Can Implement Reforms for a Sustainable Financial System.

[32] European Commission Strategy for Financing the Transition to a Sustainable Economy (2021). "The Commission will review relevant frameworks relating to investors' stewardship and engagement activities. In particular, the Commission will explore how the Shareholder Rights Directive II may better reflect EU sustainability goals and align with global best practices in stewardship guidelines". Page 15.

including a clear description of i) the targets pursued[33]; ii) the tools to monitor and evaluate the outcomes[34]; iii) the actions to tackle unsatisfactory outcomes and/or escalation strategies.

To ensure that robust stewardship approaches at product level can gain credibility and address potential greenwashing risks, we would recommend the development of a standard for outcomes-focused stewardship, where efforts are focused on the achievement of outcomes on common goals rather than on the outperformance of individual assets. EU policymakers could take inspiration from existing regulatory or industry standards under development, such as the Financial Reporting Council's newly revised Stewardship Code[35] or the FCA's "Improvers" category for financial products under its proposed Sustainable Disclosure Regulation (SDR)[36].

Such a standard could include at the financial product level:

- The product's sustainability objective (and whether this is aligned with global sustainability goals like the Paris Agreement or the SDGs)
- Stewardship policy – including alignment of engagement and voting activities with the sustainability objective pursued by the product; target-setting (e.g. for capex aligned with the EU taxonomy); how stewardship activities are reasonably expected to contribute to change; and escalation approach within a set timeframe.
- Regular reporting on progress towards meeting individual investees' stewardship objectives (based on an evidence-based environmental/ social benchmark) and activities conducted (including voting if relevant) to pursue objectives - with obligation to give rationale for stewardship activities that appear to contravene the fund's sustainability objective and/or stewardship policy.

It will also be important to ensure that the term "stewardship" and various associated tools and approaches have standard definitions to ensure alignment of expectations. The PRI's definitions (see PRI Reporting & Assessment Glossary) could be taken as a reference.

The PRI has experience of contributing to public policy on sustainable finance and responsible investment across multiple markets and stands ready to support the work of the ESAs further to addressing greenwashing risks in the EU.

Please send any questions or comments to policy@unpri.org.

More information on www.unpri.org

[33] Including whether or not these targets are aligned with international sustainability goals and thresholds (for example the Paris Agreement or the UN Sustainable Development Goals).

[34] For example, alignment with the EU Taxonomy for sustainable activities with regards to environmental targets.

[35] Financial Reporting Council – the UK Stewardship Code 2020.

[36] UK Financial Conduct Authority - Sustainability Disclosure Requirements (SDR) and investment labels (2022). Please see our (upcoming) response to the FCA's consultation for more detail.