

Legal Update

Tackling Greenwashing: ESMA publishes its Sustainable Finance Roadmap for 2022-2024

On 11 February, the European Securities and Markets Authority (“**ESMA**”) published its Sustainable Finance Roadmap for 2022-2024 (the “**Roadmap**”).

The Roadmap builds on ESMA’s 2020 Strategy for Sustainable Finance and will be of interest to those in the EU and beyond looking to understand the focus and ambition of the EU’s securities market regulator in this area.

The Roadmap identifies three main priorities:

- Tackling greenwashing and promoting transparency
- Building both National Competent Authorities’ (“NCAs”) and ESMA’s capacities in the sustainable finance field
- Monitoring, assessing and analysing ESG markets and risks

The continued focus on greenwashing is notable and reflects a concern shared by a number of regulators globally. In March 2021, the U.S. Securities and Exchange Commission announced an enforcement task force focussed on ESG-related misconduct. Similarly, the UK Financial Conduct Authority have cited addressing greenwashing as a ‘key committed action’ of its ESG strategy. ESMA further reiterated greenwashing as a core risk to its objectives in a Trends, Risks and Vulnerabilities report published on 15 February 2022.

A summary of the key actions of the Roadmap is set out in “Key Areas of Focus and Action” below. Further more detailed information, including indicative timings, can also be found in the Annex to the Roadmap.

1. Tackling greenwashing and promoting transparency.

In ESMA’s view, the combination of growing demand for ESG investments and rapidly evolving markets creates the potential for greenwashing and poses consequential risks to investors.

ESMA’s priority in this area is to investigate the nature and causes of greenwashing, define its fundamental features and ultimately address it with coordinated action.

Whilst ESMA notes that ‘intuitively’ greenwashing refers “to market practices whereby the publicly disclosed sustainability profile of an issuer and the characteristics and/or objectives of a financial instrument or a financial product and the related processes do not properly reflect the underlying sustainability risks and impacts” it intends to take a broad approach to investigating the issue with the aim of understanding its direct (e.g. misrepresentation, wrongful disclosure, poor labelling) and indirect (e.g. availability and quality of data) causes.

The Roadmap contains a useful discussion of National Competent Authorities' ("NCAs") current perceptions of greenwashing risk in the spheres of asset management, investment services, corporate disclosure and benchmarks, summarised below:

Focus	Identified greenwashing risk
<i>Asset Management</i>	<ul style="list-style-type: none"> • Unequal understanding of the type of products which are subject to Articles 8 and 9 of the Sustainable Finance Disclosure Regulation ("SFDR") leading to inconsistent disclosure • Lack of information on limitations related to methodology or data used in ESG disclosures • Mismatch between the emphasis placed on ESG characteristics in the presentation of an investment product and the strategy that is actually implemented
<i>Investment Services</i>	<ul style="list-style-type: none"> • Application of conduct of business rules such as suitability/product governance and information requirements when selling ESG products¹ • Insufficient investor education to ensure that product offerings related to ESG investing are properly understood
<i>Corporate Disclosure</i>	<ul style="list-style-type: none"> • Incorrect or omitted information in non-financial statements and prospectuses • Lack of transparency on the limitations of the methodologies and data used to prepare disclosures • Limited harmonisation in sustainability reporting practices by the Non-Financial Reporting Directive ("NFRD") triggering issues across the entire investment chain • Insufficient scope of Issuers covered by NFRD • Overreliance on ESG ratings and data providers to determine the sustainability profile of issuers
<i>Benchmarks</i>	<ul style="list-style-type: none"> • Disclosures made by benchmark administrators about the impact of their ESG indices, when these are either just applying exclusions or constructed using ESG ratings • Creation of benchmarks which are very close to those envisaged by legislation, such as the Paris-aligned benchmarks, but which fall outside these legally recognised categories while still giving the impression of a strong ESG profile

¹ On 27 January 2022, ESMA also [published](#) a Consultation Paper on draft ESMA guidelines relating to suitability following adoption of amendments to the MiFID II Delegated Regulation to integrate sustainability factors, risk and preferences. ESMA has also announced that a separate consultation relating to amendments made to the product governance and sustainability regime will be conducted in the near future.

The Roadmap also sets out an indicative plan of action for tackling greenwashing. This includes arriving at a definition of greenwashing to drive supervisory work in a coordinated and efficient manner across sectors and ensuring consistent application of the EU rulebook through convergence tools such as Q&As and Guidelines.

Finally, ESMA observes that whilst, in an ideal scenario, greenwashing would be tackled based on a complete and fully applicable legislative regime there is now a real need to address greenwashing without delay, even if all the legislative elements are not fully in place yet.

2. Building both NCAs' and ESMA's capacities in the sustainable finance field.

The Roadmap also recognises that the regulation of sustainable finance requires supervisory authorities to go through a 'learning curve' to ensure that the implications of sustainable finance legislation, as well as the basics of the sustainability transition, are well understood and become mainstream within NCAs and ESMA.

The Roadmap notes the 'peculiar' nature of sustainable finance that requires NCAs to attain not only knowledge of the relevant legislation but also a good understanding of the intersection between sustainability matters and finance.

ESMA intends to implement a range of practical measures to build capacity and expertise for NCA and ESMA staff through various knowledge exchange and training programmes and the development of common supervisory standards on ESG-related matters.

3. Monitoring, assessing and analysing ESG markets and risks.

The Roadmap is clear that whilst ESG markets create new investment opportunities they also bring new risks to investor protection, orderly markets and financial stability. In particular, ESG markets and products (such as investment funds and sustainable bonds), climate change and EU carbon markets are cited as requiring close supervision. Insufficient and poor quality data are also seen as impediments to proper risk monitoring and assessment along with the need for further work in relation to green FinTech and climate risk assessments.

To address these requirements the Roadmap proposes the following actions:

- Supporting single rulebook and convergence initiatives to contribute to a complete and clear set of rules and powers in the EU.
- Continuing the work on climate change scenario analysis and further structuring the dialogue in this area with the other European Supervisory Authorities ("ESAs"), the European Central Bank ("ECB") and the European Environment Agency, including on EU-wide stress testing of the financial system.
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- Better understanding the interaction between digital innovation and sustainability.
- Engaging with the relevant international fora to benefit from synergies and promote globally consistent approaches.

KEY AREAS OF FOCUS AND ACTION

Alongside the three priorities, ESMA has also identified seven sectors and targeted actions where ESG-related risks are currently perceived as having the highest potential impact, as well as a variety of cross sectoral measures:

Sector	Actions
<i>Investment management</i>	<ul style="list-style-type: none"> • Contribute to EC's work on minimum sustainability criteria for SFDR Article 8 products • Review SFDR regulatory technical standards • Contribute to consistent implementation of new requirements through supervisory convergence actions • Undertake work on climate change scenario analysis
<i>Investment services</i>	<ul style="list-style-type: none"> • Contribute to consistent implementation of new/existing requirements related to manufacturing and design of ESG products, information provided on ESG products as well as their marketing and distribution • Promote financial education • Consider implications for ESMA of the EC's plans on sustainable finance related data under the European Data Strategy to support SMEs and retail investors • Collect data on distribution of ESG products
<i>Issuers' disclosure and governance</i>	<ul style="list-style-type: none"> • Contribute to EU and international sustainability reporting standards • Contribute to prospectus requirements for green, social and sustainable securities • Contribute to legislative process on sustainable corporate governance and Shareholder Rights Directive II • Contribute to guidance on stewardship not to impede collaborative engagement by investors on sustainability goals • Contribute to assessment of how IFRS reflect sustainability risks • Provide guidance on Taxonomy Regulation Article 8 Delegated Act • Prepare for supervisory powers over external reviewers for green bonds issuances
<i>Benchmarks</i>	<ul style="list-style-type: none"> • Contribute to EC's work on aligning Climate Transition Benchmarks and Paris-Aligned Benchmarks with EU Taxonomy • Contribute to EC's assessment of possibility to create ESG benchmark label • Monitor trends in the use of EU climate benchmarks • Build supervisory capacities on ESG compliance of critical/third country benchmark administrators
<i>Ratings (credit ratings and ESG ratings)</i>	<ul style="list-style-type: none"> • Support EC in improving reliability and comparability of ESG ratings • Assess how CRAs incorporate ESG factors in their methodologies
<i>Trading and post-trading</i>	<ul style="list-style-type: none"> • Undertake work to consider impact of climate change in central counterparty stress testing • Build analytical tools for monitoring EU carbon markets • Contribute to consistent implementation of new requirements
<i>Financial innovation</i>	<ul style="list-style-type: none"> • Identify use cases of innovative technologies that could help the transition to a greener economy ('green FinTech') • Collect evidence on recent trends and interactions in relation to green FinTech and sandboxes

Sector	Actions
Cross sectoral	<ul style="list-style-type: none"> • Assess greenwashing market practices • Conduct supervisory case discussions on greenwashing among NCAs • Map NCAs' supervisory role, especially on greenwashing • Contribute to consistency of sustainable finance legislation • Contribute to EC's efforts to develop EU-wide labels for sustainable finance products • Establish Consultative Working Group for Coordination Network on Sustainability

Further detailed information on the ESMAs planned actions, including indicative timings, can be found in the Annex to the Roadmap. Notable objectives for the remainder of 2022 include a review of the regulatory technical standards in relation to 'principal adverse impacts' under SFDR and developing guidance to NCAs and market participants on Article 8 of the Taxonomy Regulation.

Noting the fast-evolving nature of ESG markets and of the EU regulatory framework, ESMA has said that it will keep the Roadmap, including the identified priorities and the sectors of focus, under review during the entire implementation period of 2022 to 2024.

If you would like any further information on any of the cases summarised above, please do not hesitate to get in touch.

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