

FBF's answer on the Call for Evidence on « Greenwashing » - 16/01/2023

The French Banking Federation (FBF) welcomes the opportunity to respond to the Call for Evidence (CfE) launched by the European Supervisory Authorities (ESAs) on greenwashing. It is confident that the discussions around the CfE will improve the understanding of this complex subject matter. While acknowledging that the present ESAs' initiative is a response to a request from the European Commission, we wish to underline that greenwashing should be considered from a broader perspective, also including the real economy as greenwashing is not specific to financial services.

The European financial industry has made important voluntary commitments to support the ESG transition and has been involved in several key workstreams that contribute to the enhancement of ESG standards and their practical implementation. Such voluntary commitments and workstreams aim at preventing greenwashing risks through enhanced transparency, the development of common methodologies, and shared best practices. These workstreams cover all stages of ESG projects and their financing, from the underlying data to the distribution of ESG products to end-investors.

Some examples of these contributions notably include:

- The implementation work of the Glasgow Financial Alliance for Net Zero (GFANZ) and its various voluntary alliances, in particular the contribution of banks to the Net-Zero Banking Alliance (NZBA) convened by the UN Environment Program Finance Initiative (UNEP FI).
- Supporting the EFRAG working groups establishing the European Sustainability Reporting Standard (ESRS).
- Working on methodologies to account for transition trajectories (e.g. PACTA methodology).
- Developing best practices in ESG product governance through industry guidelines and data standardization efforts (e.g. Findatex EET templates).
- Working on methodologies for the computation of taxonomy and SFDR alignment for product embedding derivatives (EUSIPA).
- Supporting ESG product labels for funds (e.g. ISR, Greenfin labels) or structured products.
- Working on a practical implementation of the taxonomy on core banking products with the European Banking Federation.
- Working on TNFD pilots and answering to the ongoing consultation.

The transition to a net zero future requires massive investments. The World Economic Forum estimates annual financing needs to be at around \$4 000 bn to \$5 000 bn. McKinsey, based on a broader but not yet exhaustive approach, calculates an annual figure of \$9 200 bn.

Only a vibrant ESG ecosystem will be able to address these needs. All firms that contribute to ESG transition, while complying with existing regulations and acting in good faith with adequate transparency, should be supported and protected from wrongful greenwashing accusations.

To that end, it is essential that any future guidance aiming at tackling greenwashing:

- ensures a clear, stable, and predictable legal environment, and
- considers intentionality and materiality criteria.

In particular, we would like to make the following remarks.

1- Greenwashing is not limited to or specific to financial institutions

First, we would like to highlight that greenwashing is not a matter limited to or specific to the financial sector. Indeed, all industries are likely to generate greenwashing issues and it should therefore be addressed from a cross-cutting perspective.

We understand that a specific focus should be given to greenwashing in the context of financial activities and products. While it is true that the financial industry is often targeted by high-profile greenwashing accusations, we regret that the ESAs' Call for Evidence could contribute to feed the popular stigma associated with financial institutions when it comes to greenwashing, without allowing this issue to be considered in the broader perspective of general corporate communication and commercial practices, irrespective of the sector concerned.

We have reservations regarding some statements underpinning the ESAs' Call for Evidence, such as the idea that greenwashing – which is a cross-cutting concept - should become part of the sectoral regulatory and enforcement framework. If this approach is followed for the financial sector, we would expect it to also include all other activities or industries. In our view, this is not the right way to proceed, as we consider that existing legal and regulatory tools, including those of general application, should prevail to address greenwashing concerns.

2- Although ESG topics are new, and the EU sustainable finance regulatory framework is not yet fully operational, companies already prevent and manage greenwashing

We kindly ask the ESAs to take into account the following contextual elements before submitting their report on greenwashing to the European Commission, and in particular:

- A) ESG topics are not yet mature, and there are pending issues related to the sequencing of sustainable finance regulations, the lack of robust methodologies and data gaps. Many actors must use proxies and/or outsourced and unverified data, therefore exposing themselves to the risk of greenwashing accusations. Safe harbor or similar provisions should be envisaged until the necessary information is fully available and sequencing issues between different pieces of legislation have been resolved. Further guidance (e.g. FAQs) on sustainable finance regulations would also help to ensure that these initiatives are correctly implemented.
- B) The sustainable finance EU regulatory framework is not yet fully entered into application, and complete implementation of this framework – which aims to tackle greenwashing – will require accurate, comprehensive and duly audited data from customers. In particular, we would like to recall that:
 - Level 2 of the Sustainable Finance Disclosure Regulation (SFDR) only applies since January 2023.
 - The first taxonomy-alignment reporting will be published in 2023 by corporates and in 2024 by financial institutions.
 - The Corporate Sustainable Reporting Directive (CSRD) will only enter into application in 2025 for undertakings with more than 500 employees and in 2026 for undertakings with 250 to 500 employees.
 - The European Green Bond Standard (EUGBS) should not enter into force before end 2023.
 - Other pieces of the framework remain to be published, such as the Delegated Acts on activities related to the four remaining environmental objectives of the UE taxonomy and the ESRS standards for CSRD.

- C) Companies already prevent and manage greenwashing as part of their overall reputation risk. In the financial sector, greenwashing is a risk deriving from and strongly enhanced by the fast development of so-called “green” or “sustainable” financial products and services. In that respect, the current legal framework (on sustainable finance, but also more broadly on conduct of business, investor protection and unfair commercial practices, including sanctioning regimes) can already contribute to preventing and addressing greenwashing risk at product level. New initiatives are also underway, that could be relevant in that respect, and should also be adequately considered.¹
- D) Once the sustainable finance legal framework is fully in place, with appropriate guidance and data provisions, its effects should be measured alongside those of existing general legislation on misleading practices and misrepresentation that can be applied to greenwashing. For example, the Unfair Commercial Practices directive (whose 2021 guidance includes a specific section on environmental claims) or the Market Abuse Regulation. This stocktaking should give a clearer idea as to whether further specific regulatory initiatives on greenwashing are necessary.

3- ESAs should support a clear, stable, pragmatic and predictable legal environment.

Legal clarity and legal certainty should be ensured throughout the sustainable finance regulatory framework. Therefore, in addition to the data issues mentioned above, the shortcomings of the current legal framework should be addressed, at least through supervisory guidance. This would help prevent the risk of wrongful greenwashing claims.

If a guidance is finally proposed by the ESAs, it should help companies deal with the shortcomings identified above (nascent methodologies, staggered entry into application of the sustainable finance framework, lack of reliable data).

To do so, we believe that guidance should take into account the following elements:

Adopt high-level internationally harmonized principles

Guidance could be based on the IOSCO definition according to which greenwashing is “a practice of misrepresenting sustainability-related information, practices or features”. These kinds of malpractice are already addressed by the existing and upcoming EU finance and sustainable finance regulatory frameworks which are designed to ensure that market participants provide clear information on financial instruments. Here are a few examples of the texts to which firms would refer in terms of communication requirements:

- Directive 2005/29/EC of the European Parliament and of the Council concerning unfair business-to-consumer commercial practices in the internal market (“Unfair commercial practices are those which: are contrary to the requirements of professional diligence; and are likely to materially distort the purchasing behavior of the average consumer”).
- Market regulations on clear and not misleading communication (MIFID/MIFIR, PRIIPS, UCITS, AIDMD).
- European Commission Proposal for a Directive on empowering consumers for the green transition (March 30, 2022).
- Optional good practices to avoid greenwashing of ISO (ISO 14030-1:21).

¹ ESMA GL on the name of ESG funds, EBA technical work on green loans and mortgages, the CS3D, Commission revision of the Prospectus Regulation including dedicated requirements for ESG-related debt securities, legislative proposal on oversight of ESG Ratings and ESG Data providers (expected in 2023), legislative proposal on empowering consumers for the green transition and a legislative proposal for a Regulation on substantiating environmental claims (expected in 2023).

And specifically in France:

- Art 112-1-1 of the French Consumer Code, and
- Decree No. 2022-539 of April 13, 2022 on « carbon offsetting and carbon neutrality claims in advertising » (*Décret n° 2022-539 du 13 avril 2022 relatif à la compensation carbone et aux allégations de neutralité carbone dans la publicité*)².

As such, we do not need any additional regulatory layers to the existing frameworks which already intend to tackle greenwashing practices as any misleading claims.

Clarify the notion of responsibility in greenwashing

Greenwashing may occur outside financial institutions, though it could then be spread through the investment chain. Rather than splitting greenwashing roles between “trigger” and “spreader receiver”, as suggested in the consultation, it is important to distinguish greenwashing situations that involve a degree of intention or gross negligence on the part of the financial institution, from those where a bank has spread a misrepresentation made by a third party or used data/proxies that are imprecise despite best efforts due diligence and adequate disclosure. We propose that the ESAs’ work on greenwashing focuses on addressing risks arising from situations involving intention or gross negligence, as this would be the most important in ensuring market integrity and confidence in sustainable finance.

Deal with the specific case of “transition” financial products

To date, the only regulation that clearly defines a green financial product is the EU GBS regulation, which covers only green bonds. However, “green” products alone will not be able to meet the EU’s ambitions to decarbonize the economy. “Transition” products, such as sustainability-linked bonds and loans, should be developed without being unduly subjected to greenwashing accusations. In that respect, existing market frameworks should be recognized as fully relevant. In addition, transitioning entities will go through several steps before reaching the targeted optimal situation, so it is necessary to channel funding to transitional activities beyond those that are already sustainable (or so-called “dark green”). Taking into account transition pathways (i.e. decarbonization and other ESG targets) and their related disclosure are key elements in the appreciation of the seriousness of an ESG transition policy.

It is also important to underline that notions used by the European sustainable finance framework are complicated to understand for investors, for example “enabling activities”, “transitional activities” or “transition plans”. Making these notions as clear as possible are key if we want investors to keep supporting and investing in the transition.

Take into account the complete life cycle of ESG investments and deal with the specific case of secondary markets

When referring to ESG investments, the focus is often on the need to provide new funding for the purpose of greening the economy. However, it is equally important not to lose sight of the complete life cycle of ESG investments, spanning both primary and secondary markets. Ensuring a perennial ESG market implies developing an entire ecosystem of players. In this ecosystem, the liquidity-provision function of both intermediaries and market-makers plays a central role. In turn, the long-term

² Link to the decree :

<https://www.legifrance.gouv.fr/jorf/id/JORFTEXT000045570611#:~:text=C2%AB%20Cette%20publication%20est%20tenue%20%C3%A0,signification%20ou%20de%20port%C3%A9e%20%C3%A9quivalente.>

sustainability of their involvement is highly dependent on their capacity to hedge their global-netted positions on derivatives markets (in complement to their no-less sizable hedges on cash markets).

Best-in-class and exclusion strategies represent a dominant share of ESG strategies. While these strategies essentially rely on secondary markets, they indirectly contribute to making primary markets perennial. In addition, these index-based strategies, generally affecting very large portfolios, also tend to have a massive impact on markets and asset valuation. Quite importantly, this impact also includes cash-rich companies. In this regard, best-in-class and exclusion indices constitute a very effective retribution/penalty mechanism for inducing these companies to adopt a greener agenda, notably one in line with the EC taxonomy. Index-tracking strategies that refer to such broad benchmarks are highly dependent on the simultaneous availability of related hedging solutions, whether through OTC swaps or, increasingly, through regulated derivative market products (such as index-futures).

There is a pressing need for an EU sustainable perspective that clearly acknowledges the above-mentioned ESG contribution of derivatives in regulations and guidelines affecting these instruments and structured products. This would avoid financial institutions being exposed to unwarranted greenwashing claims in this area.

Recognize available voluntary market frameworks and firms' internal frameworks

Transparency, based on reliable data and robust methodology, is an important element to consider in greenwashing prevention. Besides the sustainable finance regulatory framework, voluntary market frameworks and firms' internal frameworks contribute to ensuring complementary transparency and should be recognized as such.

4- ESG rating agencies and ESG data providers should be regulated

ESG rating agencies and ESG data providers operate in an EU data market that is excessively concentrated and with insufficient transparency.

The future European Commission proposal on ESG ratings may limit this risk of perceived greenwashing by requiring ESG rating agencies and ESG data providers to be more transparent on the methodologies and criteria they use, in particular to provide ratings. Transparency on methodologies used should help financial market participants offer products that are in turn more transparent and should help investors understand the rationale for products being marketed as sustainable.

Conclusion:

A mature and stable legal sustainable finance framework should be supported by:

- High level principles on use and responsibilities,
- Access to high-quality data,
- Verified/supervised third-party providers,
- "Transition" financial products and services,
- A due consideration of the importance of the transition and secondary markets,
- Harmonization and clarification of ESG disclosure frameworks, regulations, standards and definitions across jurisdictions beyond Europe.

These elements should enable most greenwashing issues relating to the financial sector to be addressed. All this would also help avoid circumstances where fear of being accused of greenwashing adversely impacts firms' inclination to set ambitious sustainability targets, make voluntary commitments or develop innovative sustainable finance products.

However, it is also essential to address the question of greenwashing beyond the financial sector.