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Submitted via online survey

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Dear Sir or Madam,

AIMA comments on ESAs' Call for evidence on better understanding greenwashing

The Alternative Investment Management Association (AIMA)¹ welcomes the opportunity to respond to the European Supervisory Authorities' (ESAs) call for evidence on better understanding greenwashing². Given the increasing focus on greenwashing by regulators, we believe it is important to understand the drivers and implications of regulations, where not well-crafted, in potentially increasing greenwashing risks.

ESAs' common section of the CfE

There is currently no industry consensus as to the definition of greenwashing. The core characteristics as set out in the call for evidence (**Q A.1**) are reasonable and comprehensive. However, we would question whether it is necessary to have specific rules or regulatory requirements in respect of greenwashing specifically given that numerous rules already exist that

¹ The Alternative Investment Management Association (AIMA) is the global representative of the alternative investment industry, with around 2,100 corporate members in over 60 countries. AIMA's fund manager members collectively manage more than US\$2.5 trillion in hedge fund and private credit assets. AIMA draws upon the expertise and diversity of its membership to provide leadership in industry initiatives such as advocacy, policy and regulatory engagement, educational programmes and sound practice guides. AIMA works to raise media and public awareness of the value of the industry. AIMA set up the Alternative Credit Council (ACC) to help firms focused in the private credit and direct lending space. The ACC currently represents over 250 members that manage US\$600 billion of private credit assets globally. AIMA is committed to developing skills and education standards and is a co-founder of the Chartered Alternative Investment Analyst designation (CAIA) – the first and only specialised educational standard for alternative investment specialists. AIMA is governed by its Council (Board of Directors). For further information, please visit AIMA's website, www.aima.org.

² https://www.eiopa.europa.eu/sites/default/files/joint-committee/esas_call_for_evidence_on_greenwashing.pdf

address mis-selling. [REDACTED]

While it might be helpful to provide examples of what constitutes greenwashing, there could be risks in developing a regulatory framework that tries to define it exhaustively and in detail, as elements that are not explicitly stated could be missed or not considered greenwashing. For example, 'overstatement of impact' is not expressly covered in the core characteristics as set out in the Call for Evidence, and we would consider this another possible example of greenwashing.

Furthermore, given that regulatory measures relating to sustainable finance are still being implemented, there is not sufficient consensus about their application in order to comprehensively define greenwashing. We note, in particular, that the EU sustainable finance framework (i.e. Taxonomy, Sustainable Finance Disclosure Regulation (SFDR)) is still being developed and there is a lack of clarity over certain concepts (for example, the definition of sustainable investment), with guidance and secondary legislation still expected. Regulations on sustainability disclosures have only recently come into force (e.g. CRSD) and time needs to be given to review the impact of these regulations and how they are working together to address risks.

ESMA Section of CfE

There are a number of drivers of greenwashing risks (Q F.1). One of these being challenges in the application of new rules and inconsistent interpretations of the legal regime. There are many interpretative challenges, and uncertainty in the application of the SFDR that firms will approach differently. For example, the definitions for 'sustainable investment' under Article 2.17 of SFDR (contribution, Do No Significant Harm (DNSH) and good governance) and Taxonomy-alignment, under Article 3 of the Taxonomy Regulation (substantial contribution, DNSH and minimum safeguards), are similar but not aligned. This leads to many cases of looser interpretations of the definition being applied to meet client expectations. Additionally, methodologies for calculating Taxonomy-alignment ratios at entity-level (under Article 8 Delegated Act) and at product-level (under Article 5/6 Taxonomy Regulation and SFDR) are not always aligned with respect to what is included in the numerator and denominator. Key differences relate to the approaches to sovereign bonds, derivatives, and SMEs, which complicates the calculation of Taxonomy alignment for investors.

This illustrates the fact that regulation, if not well crafted, can lead to poorer clarity for investors. If policymakers decide to implement a prescriptive regulatory framework around sustainable finance, it needs to be one that is comprehensive and well designed, otherwise it can force firms to fill in gaps in guidance or rules themselves. If not done in a way which is in line regulators' expectations, this could, under an expansive approach as set out in the Call for Evidence, be considered greenwashing. Intentionality is important to consider as in many cases firms will not be deliberately greenwashing, and it is instead a by-product of unclear or inconsistent regulation.

Firms that are concerned about the implications of falling foul of greenwashing rules may underplay sustainability considerations in their reporting, as they do not want the risk associated with justifying those in the context of regulation. This may work against the aim of a sustainable

finance framework and what it is intending to achieve.

Other drivers of greenwashing relate to the availability, consistency, and transparency of data:

- **Reliance on external ratings:** Greenwashing can occur where firms are reliant on data from ESG data or ratings providers, where there can be a lack of correlation and transparency in how ratings are developed. There are also issues over the timeliness of updates to ESG ratings and from ESG data providers, with updates potentially occurring several months after a company releases an ESG report. Therefore, ensuring quality and accessible corporate disclosures, for example through the work of the ISSB, is important in addressing this risk.
- **Methodological inconsistencies:** Firms do not always have access to consistent, comparable, and reliable ESG information which can increase greenwashing risks. Firms can challenge this data and the methodologies but are often still reliant on it. For example, there is generally consistency over how Scope 1 and 2 emissions are calculated and reported, but there is less consistency in how Scope 3 emissions are calculated, if at all. Data assurance control functions that are either internally or externally (i.e. third-party) assured are not yet harmonised.
- **Asset class considerations:** Certain asset classes and financial products may be more prone to greenwashing risks than others (Q F.5). Whether an asset class is at a higher risk of greenwashing is largely dependent on the availability of data, rather than due to the characteristics of the asset in and of itself. For example, the depth and availability of data tends to be better for equities compared to derivatives. Regulations and regulatory frameworks have also reinforced this, given that they tend to be predominantly designed with a focus on an equity model of ESG and have tended to neglect non-corporate asset classes. This has promoted disclosures within certain asset classes (e.g. equities) compared to other assets. There is a need for regulation and guidance to take into account all asset classes to reduce the risk of greenwashing.
- **Lack of control over index design:** There are particular challenges for managers invested in or emulating index tracker funds as they will largely be reliant on the information and assessments from these providers, with little ability to challenge what is included in the index. Different index providers will make different assessments of the same company; what is considered a 'green' or 'sustainable' company by one provider may not be considered as such by another. One of the risks of greenwashing is simple adherence to a stated index without further work as to the basis of its composition.
- **Manager size and scope to review data:** The level of safeguards in place to address greenwashing risks (Q F.7.3) differs depending on the size of the manager. Larger managers tend to have more internal policies and procedures in place to address risks. Smaller managers may not have the depth and resources available to do extensive reviews of data they receive, from either issuers or third-party data providers.

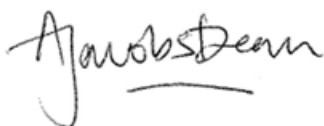
- **Lack of global consistency:** Global consistency at issuer level is important in reducing greenwashing risks, as currently firms find it difficult to gain the level of granularity of data needed. Additionally, there is not a global basis for measuring social factors within ESG. Therefore, policymakers and regulators could help to alleviate greenwashing risks by working with IOSCO to improve global consistency, using TCFD as a framework.

Any future rules around greenwashing (Q F.10) should also differentiate between different audiences and their needs and abilities. Institutional investors should need less support compared to retail investors who may be less sophisticated. Any regulations should also focus on setting out minimum standards rather than attempting to adopt an approach which may not be achievable by all. Setting out minimum standards would make regulations achievable for the smallest firms while not restricting larger firms with the ability to do more.

Additionally, more consistency is needed around the language used in reference to the two perspectives of double materiality. The confusion between ESG integration and the pursuit of impact is one of the causes of greenwashing that could be tackled through a clearer separation, and the use of specific expressions in a consistent manner. Hence, more guidance and methodology on how impact is measured or accounted for could help tackle greenwashing.

We would be happy to elaborate further on any of the points raised in this letter. For further information, please contact Kate Boulden, Associate Director, Governance and Innovation, by email at kboulden@aima.org.

Yours sincerely,



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AIMA