

Response of ICMA to the ESAs' Call for Evidence on greenwashing

The International Capital Market Association (ICMA) welcomes the opportunity to provide feedback to the European Supervisory Agencies' (ESA) Call for Evidence on greenwashing. We have not responded to all the questions but to those which are most directly relevant to our area of expertise in the capital markets and in sustainable finance.

ICMA is a membership association, headquartered in Switzerland, committed to serving the needs of its wide range of members. These include private and public sector issuers, financial intermediaries, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others worldwide. ICMA currently has over 600 members located in over 65 jurisdictions. See: www.icmagroup.org. ICMA hosts the [Principles](#) that underpin sustainable bond issuances globally. In 2021, [over 98% of the global sustainable bond issuance volume](#) aligned with the Green, Social, Sustainability, and Sustainability-linked Bond Principles (the Principles).

This feedback is given on behalf of ICMA and its constituencies, and especially the Executive Committee of the Principles and Asset Management and Investors Council (AMIC). The key points in our response to the Call for Evidence (CfE) are summarised below. We also provide in the Appendix an overview of how existing regulations and market standards aim to address the greenwashing concern areas.

Proposed definition of greenwashing for regulatory purposes

The core features as presented in the CfE are excessively broad and therefore unhelpful in the context of developing a regulatory approach to greenwashing. They reflect the current debate around greenwashing that covers a wide range of behaviours from misrepresentation to lack of ambition at both the product level and issuer level. There is also limited allowance for distinguishing between intentional or unintentional behaviour. As it stands, this catch-all approach to greenwashing does not provide a conceptual framework that is either suitable for financial regulation or, arguably for policy making.

Regulators should indeed aim for a clear, fair, calibrated, and actionable definition of greenwashing in the financial sector. A possible definition for consideration could be: *"For financial regulatory purposes, greenwashing is a misrepresentation of the sustainability characteristics of a financial product and/or of the sustainable commitments and/or achievements of an issuer that is either intentional or due to gross negligence."*

Understanding the areas of potential concerns in sustainable finance

It is important to distinguish between the concerns expressed by stakeholders and what could be considered as greenwashing for possible regulatory oversight and enforcement. The areas of concern historically expressed **for sustainable bonds** can be categorised as below.

- 1. Lack of ambition:** For use-of-proceeds (UoPs) bonds, concerns relate to projects or parts of projects which are believed to be insufficiently green or sustainable. For SLBs, it applies when sustainability performance targets are perceived as easy to achieve, if not already realised, or close to a "business as usual" trajectory.
- 2. Mismanagement of wider sustainable risks:** this could occur when an issuer does not have an appropriate process to identify and manage wider environmental/social risks and trade-offs for example when the primary objective of a sustainable project may not score highly or could even conflict with other sustainability criteria.

3. **Strategic inconsistency:** This could occur, for example, where there is a lack of a broader sustainability/environmental strategy accompanying a green bond or a clear inconsistency between the green label and what the issuer does beyond the label.
4. **Actual deception:** This would be, for instance, in the unlikely cases that an issuer did not allocate the proceeds to green projects except due to the reasons beyond its control, or if an issuer manipulated its KPIs or omitted material information.

For fund products, it is understood that the categories for sustainable bonds would also apply when investing in these securities. However, for fund products themselves, we believe that the concerns expressed fall within the categories below.

1. **Vague or ambiguous responsible investment methodologies:** e.g., opacity or inconsistency about the baseline criteria being applied, which leads to criticism if portfolio analysis reveals investments in companies that are not seen as committed to environmental objectives, especially to climate transition, although they may score highly on governance or diversity for example.
2. **Unclear or misleading fund labelling and naming:** e.g., funds labelled as “Transition” or “Impact” where the underlying strategy is focused on disclosure rather than outcomes, or funds labelled as “ESG Leaders” but in fact follow a best-in-class methodology rather than absolute leadership as the name suggests.
3. **Actual deception:** for example, not applying a fund’s advertised processes for rigorous ESG screening at the product level.

The key role of the Principles in ensuring integrity and transparency for sustainable bonds:

In 2021, [over 98% of the global sustainable bond issuance volume](#) aligned with the Principles. Several EU Member States, EIB, the EC issued sustainable bonds aligned with the Principles. The Principles play a key role in ensuring market integrity and transparency. The Principles addressed the concerns expressed by stakeholders in the sustainable bond market as follows:

- **Lack of ambition:** The Principles incorporate environmental objectives and high-level project categories for green and sustainability bonds and focus on transparency provided by issuers (including on green eligibility criteria) for an informed decision by investors. The Principles also offer impact reporting metrics and guidance for all eligible project categories, require allocation reporting, and recommend the disclosure of external taxonomies and exclusion lists. For sustainability-linked bonds (SLBs), targets must go beyond “business as usual”, be externally benchmarked whenever possible, and performance is subject to external verification. The Principles also provide a registry of 300 KPIs for SLBs.
- **Mismanagement of wider sustainable risks:** The Principles require the disclosure of complementary information on processes by which issuers identify and manage perceived risks related to projects. Issuers are also encouraged to identify mitigants to such risks.
- **Strategic inconsistency:** The Principles recommend for green and sustainability bonds that information on underlying projects is communicated “within the context of the issuer’s overarching objectives, strategy, policy and/or processes relating to environmental sustainability”. SLBs are designed to track issuer level commitments, and the SLBP require KPIs to be material and the targets to be ambitious, and as such “strategically consistent at the issuer level”.

Additionally, for all types of sustainable bonds:

- the [Climate Transition Finance Handbook](#) published by ICMA defines transition as alignment with the objectives of the Paris Agreement and recommends the use of science-based targets and the disclosure of climate transition strategy and governance.

- ICMA's [Guidelines for External Reviewers](#) provide voluntary guidance relating to professional and ethical standards for external reviewers, as well as to the organisation, content and disclosure for their reports. In the pre-issuance phase, the external review of the sustainable finance frameworks of issuers typically includes an assessment of the chosen green eligibility criteria, materiality and ambition, environmental/social risk management systems, past controversies, and overarching sustainability strategies while post-issuance review focuses on the verification of allocations, tracking systems, and annual KPI performance.

Finally, the Principles do not make explicit recommendations with respect to “actual deception” as such behaviour would clearly be unlawful under existing securities, civil, tort laws and regulations as well as potentially under criminal legislation.

Prioritising the implementation and usability of existing regulatory initiatives

Regarding the EU's wider sustainability legislative agenda, there are many features of the numerous existing regulatory initiatives that are already relevant in addressing potential greenwashing concerns. The priority should therefore be to consider existing implementation and/or usability challenges, as well as mitigate local fragmentation risk, rather than launch additional initiatives that may lead to duplication or layering.

For **measuring ambition**, the EU Taxonomy represents the most granular effort to date to benchmark sustainability claims. However, it is hampered by considerable usability issues that need to be urgently addressed for its application to the sustainable bond market and more generally to sustainable finance. These have been recognised by the EU PSF (see the EU PSF's [extensive report](#) on the usability issues) and analysed, among other in a dedicated publication called “[Ensuring the usability of the EU Taxonomy](#)” by ICMA. The EU Taxonomy is also seen as providing a binary and EU centric definition of sustainability that is often exclusionary and does not fully integrate transition e.g., by establishing intermediate/SH performance levels. The Corporate Sustainability Due Diligence (CSDD) Directive may also impose a mandatory requirement for entities in scope to adopt transition plans compatible with 1.5 °C objective of the Paris Agreement. A clear definition of transition plans is of paramount importance as it is becoming a key element of regulations.

Regarding **mismanagement of wider sustainable risks**, most taxonomies including the EU Taxonomy incorporate the Do No Significant Harm (DNSH) concept albeit with different levels of granularity and stringency. However, the EU Taxonomy's DNSH is currently seen as the main source of many usability issues as explained in the EU PSF's report and ICMA's publication (mentioned above) while the implementation of Minimum Safeguards is not straightforward and awaits further regulatory guidance. The Corporate Sustainability Reporting Directive (CSRD) / European Sustainability Reporting Standards (ESRS) also cover environmental/social risk management disclosures at entity-level while the CSDD Directive will have compliance obligations on addressing human rights and environment-related risks, going beyond a pure disclosure approach.

On **strategic inconsistency**, disclosures under CSRD/ESRS frameworks at the issuer level are forthcoming and will include Taxonomy alignment, transition plan, and other forward-looking sustainability disclosures. These disclosures will allow investors to assess overarching strategies of entities and what they do beyond the use of labelled products. Their implementation needs to be closely monitored by supervisors as these disclosures will certainly require the development of best practice, and possibly additional guidance.

Regarding **vague or ambiguous responsible investment methodologies and unclear or misleading fund labelling and naming** for sustainable funds, disclosures under SFDR Art.8/9 have become de facto labelling in the asset management industry, even if not formally a labelling scheme. There are reports of diverging practice in terms of the classification criteria applied by asset managers, and the

lack of clear guidance or lack of consistency from national securities regulators has led several investors to reclassify most of their Art.9 funds to Art.8. Additional guidance from the ESAs is already being provided and will very likely need to continue.

It is also important to underline the ongoing work of the UK's Financial Conduct Authority (FCA) on actual sustainable fund labelling which may set an important international precedent. On 25 October 2022, the FCA published a consultation paper (CP22/20) on "[Sustainability Disclosure Requirements \(SDR\) and investment labels](#)". Three sustainable investment labels are being proposed respectively for "Sustainable Focus", "Sustainable Improvers" and "Sustainable Impact" which could provide additional transparency to investors while also explicitly integrating transition.

Our additional recommendations to regulators

With respect to addressing greenwashing risks in the sustainable bond market, several national and international regulatory authorities have integrated the Principles in their regulatory guidance while adding mandatory requirements or supervision. This has involved, among other things, requiring alignment of underlying projects with national or regional taxonomies, providing complementary project guidance, making external reviews mandatory and/or setting professional qualifications for external reviewers (see for example the FCA's [ESG integration in UK capital markets: Feedback to CP21/18](#), [ASEAN Standards for sustainable bonds](#), or the work of [Financial Services Agency](#) in Japan).

With the future EU GBS, the EU is developing an official label based on the Principles, which was originally designed to be a voluntary official "gold" standard for issuers requiring alignment with the EU Taxonomy. As the EU GBS remains in discussion among the co-legislators, there have been calls to incorporate in the legislation measures that would extend mandatory disclosure requirements to all sustainable bonds including their degree of alignment with the Taxonomy and for information on the issuer's transition plans. ICMA has commented extensively on the EU GBS, most recently through a [joint statement](#) with the Principles Executive Committee, cautioning against these proposed mandatory measures that raise usability issues, create duplication with other regulation and increase liability and costs.

More broadly, we would make the following recommendations in relation to additional measures that EU supervisors could take to mitigate greenwashing risks:

1. Call for voluntary adoption of the Principles, including its core components and key recommendation, by issuers in line with existing market practice.
2. Recognise the equivalency and allow the use of other leading official and market taxonomies (see ICMA's publication "[Overview and Recommendations for Sustainable Finance Taxonomies](#)") especially for issuances incorporating international projects (as the EU Taxonomy is not directly usable for these).
3. Call for voluntary alignment of external reviewers with ICMA's [Guidelines for External Reviewers](#) while considering complementary guidance for external reviewers as they play a key role in assessing the ambition, environmental/social risk management systems, and strategic consistency of sustainable bonds. We note that the EU GBS incorporates regulation of external reviewers for the purposes of the EUGB label.

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Appendix – Overview of regulations and market mitigants addressing greenwashing concern areas

For sustainable bonds (use-of-proceeds bonds and sustainability-linked bonds)			
Concern areas	Selected examples	Legislative/regulatory mitigants	Market-based mitigants
Lack of ambition	<ul style="list-style-type: none"> In UoPs bonds, projects or parts of those found insufficiently green or sustainable SLBs with targets seen as easily achievable or close to a “business as usual” trajectory 	<ul style="list-style-type: none"> EU Taxonomy Potential requirement under the CSDD Directive for companies to adopt transition plans compatible with 1.5 °C objective of the Paris Agreement CSRD/ESRS which will include Taxonomy and transition plan disclosures, as well as other forward-looking disclosures related to various areas of sustainability 	<ul style="list-style-type: none"> The Principles’ requirements/recommendations/guidance: (1) for UoPs bonds: on environmental objectives and high-level project categories, disclosure of external taxonomies, green eligibility and exclusion criteria, allocation and impact reporting and relevant guidance, etc.; (2) for SLBs: on ambitiousness of targets which should go beyond business-as-usual, recent KPI registry with 300 KPIs, etc. The Climate Transition Finance Handbook’s recommendation for science-based targets. External review scrutiny and ICMA Guidelines for External Reviews Market-based taxonomies (CBI, MDBs-IDFC, ISO)
Mismanagement of wider sustainable risks	<ul style="list-style-type: none"> Lack of an appropriate process to identify and manage wider environmental/social risks and trade-offs for sustainable projects 	<ul style="list-style-type: none"> The DNSH and Minimum Safeguards concepts in the EU Taxonomy The CSDD Directive’s compliance obligations regarding human rights and environment related risks CSRD/ESRS disclosures on the management of environmental and social risks at an entity-level 	<ul style="list-style-type: none"> The Principles’ requirement to disclose complementary information on processes by which issuers identify and manage perceived environmental and social risks related to projects The Principles’ encouragement to identify mitigants to know material environmental and social risks

<p>Strategic inconsistency</p>	<ul style="list-style-type: none"> • Lack of a broader sustainability/environmental strategy that accompanies a green bond • Clear inconsistency between the green label and what the issuer does beyond the label 	<ul style="list-style-type: none"> • CSRD/ESRS disclosures which will include Taxonomy, transition plan disclosures, and forward-looking disclosures related to various areas of sustainability 	<ul style="list-style-type: none"> • The Principles’ requirements/recommendations/guidance related to: (1) for UoPs bonds: on the communication of overarching objectives, strategy, policy and/or processes on sustainability; (2) for SLBs: requirement for KPIs to be core, material, and relevant and targets to be “strategically consistent at the issuer level”, recent KPI registry with 300 KPIs • The Climate Transition Finance (CTF) Handbook’s recommended disclosures including on climate transition strategy and governance • External review scrutiny and ICMA Guidelines for External Reviews • TCFD and other entity-level sustainability disclosure frameworks
<p>Actual deception</p>	<ul style="list-style-type: none"> • Not allocating the proceeds to green projects in a green bond except due to reasons beyond control • Manipulating KPIs and relevant data • Omitting material information 	<ul style="list-style-type: none"> • Securities and markets regulations • Civil, criminal and regulatory liability, tort law, etc. 	<ul style="list-style-type: none"> • The abidance of market participants to the applicable legal and regulatory framework • Allocation reporting • External review scrutiny and ICMA Guidelines for External Reviews

For fund products

Concern areas	Selected examples	Legislative/regulatory mitigants	Market-based mitigants
<p>Vague or ambiguous responsible investment methodologies</p>	<ul style="list-style-type: none"> • Opacity or inconsistency about the baseline criteria leading to criticism as investment selection may have been based on high governance/diversity scores rather than environment 	<ul style="list-style-type: none"> • SFDR and related existing/upcoming regulatory guidance for implementation • Additional guidance at the Member States level • EU Ecolabel • 	
<p>Unclear or misleading fund labelling/naming</p>	<ul style="list-style-type: none"> • Funds labelled as “Transition” or “Impact” where the underlying strategy is not outcome oriented but focused on disclosure • Funds labelled as “ESG Leaders” which is a best-in class methodology rather than absolute leadership 	<ul style="list-style-type: none"> • SFDR and related existing/upcoming regulatory guidance for implementation • Public sector supported investment labels (e.g., SRI in France) 	<ul style="list-style-type: none"> • National sustainable investment labels (e.g., FNG-Siegel in Austria, Germany, and Switzerland)
<p>Actual deception</p>	<ul style="list-style-type: none"> • Not applying, for example, a fund’s advertised processes for rigorous ESG screening at the product level 	<ul style="list-style-type: none"> • Securities and markets regulations • Civil, criminal and regulatory liability, tort law, etc. 	<ul style="list-style-type: none"> • The abidance of market participants to the applicable legal and regulatory framework