IRSG

INSURANCE AND REINSURANCE STAKEHOLDER GROUP

Advice on EIOPA's technical advice on greenwashing risks and supervision of sustainable finance policies

IRSG-22/25
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European Insurance and Occupational Pensions Authority

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CfA on Greenwashing – Request for input to the IRSG

Background

On 23 May 2022, EIOPA and the other European Supervisory Authorities (ESMA and EBA), received a Call for Advice (CfA) on Greenwashing from the European Commission. This CfA requests each ESA, separately but in a coordinated manner, to provide input on (1) definition, cases and risks of greenwashing, (2) the supervision of greenwashing and relevant sustainable finance requirements, (3) proposals to improve the regulatory framework. Two deliverables are foreseen in the CfA:

- A progress report expected by May 2023, and
- A final report expected by May 2024.

As presented during the October 2022 IRSG meeting, EIOPA would like to seek the IRSG's input in order to inform its work on the CfA on greenwashing. This request for input will complement stakeholders' input collected in the context of the Call for evidence to stakeholders due to end on 16 January 2023.

Therefore, EIOPA is now sending a request for input to the IRSG with a deadline **by 13 March 2023 COB**. This with a view of seeking more insurance specific inputs and of receiving the IRSG's views as a group rather than Members' specific inputs, which EIOPA highly welcomes via the Call for Evidence.

In case of questions do not hesitate to contact us at Giacomo.barbet@eiopa.europa.eu,Paola.Brenda@eiopa.europa.eu,Marco.traversa@eiopa.europa.eu

Understanding what is greenwashing:

1. Please outline below what the IRSG understands greenwashing to be in the insurance sector - ideally this would be a common understanding that suits all members of the IRSG, and this understanding would be captured in one or two paragraphs maximum. (It should cover some or all elements presented in Annex 1 to this document):

As preliminary comment, it is worth mentioning that in some jurisdictions, the term "greenwashing" is already embedded in the legislation. There are already multiple definitions of greenwashing (EC, UK, Finma). However – these are not consistent. Instead of focusing on creating a "definition", which would in our view, increase complexity and not actually help to combat the problem at hand, the focus should be on describing the conduct or circumstances of concern and on settling/improving the existing ESG legislation, managing the alignment across regulators, definitions and quality of data to reduce the risk of miscommunication/misleading statements.

Greenwashing within the financial sector is the process of intentionally or negligently misrepresenting sustainability-related practices or features of a product, and – as such – not complying with existing regulatory requirements.

Greenwashing can occur either at entity level, delivery, product level or at service level, including advice.

'Intentionally' shall be understood as pursuing the objective of misleading and deceiving the receiver of the sustainability claim into believing that a company's practice or product is (more) sustainable or have a greater ESG impact than it actually does. Gross negligence should also be included under the definition of greenwashing as a company is expected to follow a best-effort approach, i.e. to implement necessary processes e.g. To ensure that sustainability claims are substantiated, and the information given is correct.

On the other hand, the lack of clarity and inconsistencies in the EU Sustainable Finance framework (e.g., Definition of sustainable investment) is creating diverging interpretations which can lead to unintentionally flawed information from financial market participants. Another challenge which may create unintentionally flawed information is the current lack of robust ESG data (or reliable third-party data), mainly due to the lack of reporting by companies and the lack of transparency by ESG data providers and ESG ratings providers on methodologies and assumptions.

Such cases of divergent interpretations and potential flawed information due to lack of ESG data must be clearly differentiated from cases of intentional non-compliance with existing regulatory requirements which may be considered as greenwashing. In the same way, grandfathering should

apply when new guidance is provided by the EC or ESAs and as ESG data reporting is increasing over the years.

Where insurers build on and integrate on other providers' information (e.g., unit-linked products), reliance on prospectus information and other statutory reporting (e.g., periodic reporting of funds) should not be held against insurers if such information would turn out to be incorrect.

The proposed amendments for the Unfair Commercial Practices Directive should be taken into account. In developing a common understanding of "greenwashing", rather the clarification of what is "green" and "sustainable" will help to apply the general rules on unfair commercial practices or misleading communication.

Lastly, the term "greenwashing" gives rise to uncertainty, which undermines and discourages efforts with respect to the necessary change of economic activities towards sustainability. As a consequence, market participants (both in financial markets and real economy) could refrain from starting to act and from contributing to the sustainable transformation. In other words, "greenwashing" risks are becoming a determining factor for reputational risks – beyond legal risks – harming trust of consumers in sustainable financial products. Thus, current and expected market response, such as a series of large asset managers reclassifying Art. 9 funds (to Art. 8 funds), deserves careful consideration.

Occurrence of greenwashing:

2. What should insurance product manufacturers do in order to ensure that their sustainability-related claims do not lead to greenwashing? Inputs are also sought on measures which insurers could put in place to prevent greenwashing spreading from other sectors into the insurance sector.

The insurance industry is highly regulated in relation to sustainability claims, transparency and the implementation of robust processes and controls:

- The **IDD** governs the sale and provision of advice related to all insurance products (life and non-life) by providing robust rules which work well and have had a positive impact on the industry and insurers' customers.
- The **SFDR** increases and standardises transparency towards consumers by requiring insurers to provide a large number of disclosures regarding the financial products that they offer.

- The **CSRD** requires all large and listed insurance companies to report not only on the impacts of ESG factors on their financial statement, but also on the impacts of their activities on ESG factors (so-called 'double materiality').
- Insurance-based investment products are currently in the scope of **Ecolabel** which will be, if well designed, an important tool to ensure that sustainable products meet minimum sustainability criteria, thereby increasing the trust of consumers who want to purchase sustainable products.
- Insurers respect the **Prudent Person Principle** when investing on behalf of their clients and sustainability is a key aspect of how the principle is applied and is central in the insurers' risk management. From a risk management perspective, it is crucial for insurers to have greenwashing under control, also in order to limit negative impacts on their reputation.
- Many insurers are considered to be Public Interest Entities and are therefore subject to extensive audit requirements under the **Audit Directive.** Some insurers even go beyond their legal requirement and have their sustainability disclosures voluntarily audited.
- **Unfair Commercial Practices Directive** provides for effective rules to protect customers from unclear or misleading claims including on sustainability-related characteristics.

If designed correctly and putting aside the data (one of the main sources of concern is the lack of available and/or reliable data on the underlying funds) and timetable or sequencing problems, ultimately, these legislations have the potential to address potential greenwashing triggers. Therefore, for the EU Sustainable Finance framework to deliver on its high ambitions while addressing greenwashing risks, rewriting the existing definitions in regulation is needed to clarify what is meant by 'ESG' and to explain how to achieve material impact. The multiplication of definitions (e.g., sustainable investment) should be avoided. Instead, further clarification, coherence and guidance are needed to deliver on sustainable objectives, improve customers' understanding and facilitate the offering of ESG products. Insurers must be able to offer many sustainable products to match with clients' expectations. Time is also needed to assess the functioning of the current framework (which is not fully in place yet) and to get acquainted with its new concepts and definitions, which are not always straightforward and easy to understand for all market participants. Portfolios are only going to increase and strengthen their sustainable assets in the upcoming years in keeping with the clarification of the framework.

In the meantime, insurers are doing their best to develop their climate and sustainability related policies, reporting and products. Many have been reporting for a number of years under emerging standards such as the Task Force on Climate-Related Financial Disclosures (TCFD); some have sought voluntarily assurance from audit firms on their sustainability disclosures; and all are now complying with elements of the SFDR already in place and preparing for the additional disclosures required from 2023.

In addition, multiple insurers have joined the Net-Zero Insurance Alliance and other initiatives such as the **Net-Zero Asset Owner Alliance**; the Principles for Sustainable Insurance; and the Principles for Responsible Investments, which supports them with guidance via a common standard to adhere to. This helps to reduce the risk of confusion and therefore of greenwashing.

Additional points to consider, partially mentioned above:

- At entity level, insurers should establish their commitments in line with science-based methodology (TCFD/PCAF), irrespective of whether they join voluntary initiatives or not.
- At product level, insurers must interpret SFDR regulation with a conservative best effort approach until more clarification has been provided by regulators.
- The implementation by insurers of a due diligence process for the selection of third-party funds in the insurance portfolio/product and as well as for any delegation of the portfolio management to asset managers could also help in preventing greenwashing spreading.
- Measures to prevent greenwashing spreading from other sectors into the insurance sector: Today, insurers' ability to prevent greenwashing spreading from other sectors into the insurance sector is limited. This is mainly due the fact that the sector-neutral EU sustainability regulation is still under development and that the transitioning into a robust and more mature stage with more granular data availability requires a reasonable level of caution and forbearance. Putting best efforts during such transition phase generally under suspicion of misleading by intent (greenwashing) undermines early efforts of market participants.

3. The revision of the IDD introduced new sustainability requirements as part of the product oversight and governance (POG) process. As part of these requirements, insurance product manufacturers are now also required to take into account the target market's sustainability preferences when designing products. Please provide examples of product testing and other processes (e.g., target market definition) which may be put in place to prevent occurrences of greenwashing.

The IDD framework and the extensive guidance provided by EIOPA are sufficient to prevent occurrences of greenwashing, plus the SFDR increased the level of standardization of sustainability disclosures and thereby improved transparence towards consumers.

Time is needed to assess the functioning of the current framework and to get acquainted with its new concepts and definitions, which are not always straightforward and easy to understand for all market participants.

The main source of concern is the lack of available and/or reliable data on the underlying funds.

Supervisors can be instrumental for ensuring the ESG data sources are made easily available, and their use is regulated, available at a low cost (or free) and in a standardized format.

4. What should insurance distributors do in order to ensure that sustainability-related claims do not lead to greenwashing? In particular, inputs are sought on measures which insurance intermediaries could put in place to prevent greenwashing when sustainability-related claims made by insurance product manufacturers may not be substantiated.

The real problem is that the complex language used in the SFDR templates, the length of the SFDR information and the inconsistencies between the SFDR product categorization and the IDD definition of "sustainability preferences" do not help a smooth advice process.

The "EIOPA Guidance on the integration of sustainability preferences in the suitability assessment under the Insurance Distribution Directive (IDD)" is very detailed and prescriptive, confirming good intent to structure the customer dialogue and embed detailed information as available. Insurance intermediaries have to use and rely on SFDR Annex templates when providing detailed precontractual information. Matching such information with customer preferences should allow for a robust practice and mitigate greenwashing risk effectively.

More concerning is the mandatory structure of the customer conversation as suggested in the EIOPA guidance: the mandatory ask for customer preferences regarding the share of taxonomy aligned / sustainable investments and PAI insinuates that there would be unrealistically high shares of such investments available in the market.

5. What should insurance supervisors do in order to ensure that insurers' and insurance intermediaries' sustainability-related claims do not lead to greenwashing? Please also elaborate on aspects such as which data they should collect, which tool should they use, and challenges thereof.

Supervisors should focus on the proper enforcement of the framework, taking into account the difficulties caused by the lack of available and/or reliable data on the underlying funds, the fragmented and constantly changing legislation, the mismatch in timelines and application dates, the complexity of the new definitions and the short timeframe for the implementation of the new rules.

What should be avoided at this stage is a multiplication of definitions (e.g., definition of sustainable investment), labels or new thresholds. This would not facilitate the offering of ESG products, nor consumers' understanding.

In addition, supervisors should work towards more regulatory clarity and guidance, in particular on SFDR. The current room for interpretation for products disclosing according to Art. 8 and 9 SFDR is too broad to allow financial market participants to confidently and appropriately categorize financial products.

Consumer testing /feedback could be performed to see whether more simplification is needed.

6. EIOPA's thematic review on monetary incentives between asset managers and insurance undertakings highlighted that possible conflict of interest arising because of kick-backs. Do you think these kickbacks can also lead to greenwashing?

The IDD framework already ensures a high level of consumer protection against the risk of conflicts of interest.

It would be more relevant to assess whether difficulties with the data exchange might lead to the situation where certain funds are more offered than others because for these funds the data are more accessible (a certain preference for the funds for which data are available).

Today, there is only a limited number of products with high shares of sustainable / environmentally sustainable investments available on the market. Where no IBIPs meets the customer's sustainability preferences, the customer can decide to adapt his or her sustainability preferences. The process is duly regulated under the IDD, including the record keeping requirements. This would not be greenwashing, as the sustainability features of the products are transparently communicated towards the customer.

7. What should insurance consumers do to protect themselves against potential greenwashing? Do you see any challenges for consumers, for example in terms of information overload and or difficulties in understanding sustainability-related documentation?

Consumer disclosures should include clear accessible information needed to support financial decision making and sustainability preferences. The current SFDR templates go too far away from this, as they are too detailed and complex. For example, the SFDR templates require at least 5 pages of additional pre-contractual documents for a simple ESG fund. This excessive length also makes the accessibility of the templates via digital tools (e.g. a smartphone or tablet) more difficult.

Even the definitions used in the introductory table of the document (e.g. sustainable investment objective, sustainable characteristics) are not so straightforward to understand.

Also, the SFDR periodic disclosures can be very long: for example, for MOPs, there might be a need to provide over 60 pages to clients on top of the Solvency II periodic disclosures, often on paper. There is a need to allow the use of hyperlinks to the existing periodic information of the underlying funds.

Access to professional advice will be important for the clients who need it.

In addition, public education on how sustainability factors can be reflected in financial market products is needed. The new regulatory concepts, terminology and display of information require concise yet effective guidance for consumers to mitigate the risk of misunderstanding and disappointment.

8. What support and/or checks should be in place to ensure that consumers are able to understand sustainability-related documentation?

The use of digital solutions should be encouraged to put consumers in control of the type and amount of information they wish to receive. For example, in the SFDR periodic disclosures, there is a need to allow the use of hyperlinks to the existing periodic information of the underlying funds.

Moreover, disclosures should be simplified, as detailed in question 7.

Further points to be considered:

- The Sustainable Finance Disclosure Regulation requires further clarification. The current room for interpretation of disclosure and transparency requirements under SFDR is perceived to be too broad to allow financial market participants to confidently and appropriately categorize financial products and thus avoid greenwashing risks. We therefore support further regulatory/legal clarification as relevant.
- Provided the condition of final guidance on the definition and calculation method of "sustainable investments" according to Art. 2 (17) SFDR is met, the introduction of quantitative minimum thresholds for products with ESG or sustainability reference in the product name would be useful in order to clarify under which criteria products can be put on the market as "sustainable". However, such thresholds would need to work also for IBIPS and need to consider the special structure and functioning of life insurance products with long term investment characteristics. Therefore, careful consideration is required to make such frameworks feasible for the insurance sector, and to avoid that the multiplication of definitions, labels or new thresholds increases the risk of confusion for both providers and consumers.
- The need for public education as mentioned under Q7.

9. Various insurance undertakings have recently made voluntary net zero commitments, for example via the UN-convened Net-Zero Insurance Alliance (NZIA). In your view, are these commitments prone to potential greenwashing? if possible, provide examples of how greenwashing could emerge from these commitments.

Alliances and initiatives such as the NZIA, the Principles for Sustainable Insurance (PSI) or the Principles for Responsible Investments (PRI) are an important pillar to promote the transition to a net zero economy and support insurers with guidance via a common standard to adhere to (which is regularly reviewed). As such, these voluntary commitments rather reduce the risk of greenwashing instead of giving room to it. Since the regulatory framework is not in place yet, joining such voluntary alliances and initiatives demonstrate the willingness from European insurers to take a step into the right direction, notably to achieve Paris Agreements goals.

10. The concept of consumer redress in the case of IBIPs with sustainability features might be different than for IBIPs without sustainability features. When consumers indicate their preference to invest in a sustainable manner, they show their preference to make a positive impact on the environment or on society. In case of greenwashing, how should consumer be compensated?

The value proposition of a financial product is and remains the coverage of a financial risk and providing financial return. The additional dimension of sustainable features does (only) specify how such financial return is generated. It should be understood as additional restriction for asset allocation. If the asset allocation is performed in line with prospectus (terms & conditions), there should not be room for redress. The real-world impact must be reported for Art. 9/ impact products as a matter of transparency to the customer. However, we should doubt that this forms part of a product liability towards the customer which can give rise to redress.

Intentional greenwashing in this sense would amount to mis-selling, as the indication asset allocation would not match what was indicated to the customer. Issues over what is allocated and clear definitions of how to have material 'ESG' impact are addressed in our response to question 2.

11. The concept of value for money in the case of IBIPs with sustainability features is different than for IBIPs without sustainability features. When consumers indicate their preference to invest in a sustainable manner, they show their preference to make a positive impact on the environment or on society. In line with EIOPA's value for money approach, it is important that IBIPs offer value on the basis of their wider sustainability-related impact beyond the quantification of their individual impact on a particular customer. In this case, how do you think value can be measured (i.e., in terms of societal and environmental impact)? Can greenwashing occur in relation to this?

I think it is important to consider the sustainability features of the product among the non-financial aspects of the value for money assessment, which go beyond value-add for a particular customer and are measured based on their wider impact on society. As such, the impact discussion should be limited to "impact" products (Art.9), not in general to every product that has sustainability features. To assess such wider societal impact, ESG ratings could play an important role, however only after harmonization of regulation of ESG data, ratings and related services to ensure investor protection on the one side and manage reputational risk for the insurance sector on the other. As it stands ESG ratings differ widely in their methodologies, results and are not comparable so cannot be used at this stage. They currently rather create a risk of greenwashing.

In any case, the sustainability features of the product are substantiated and disclosed in the SFDR documentation.

Regulation:

12. If you have identified shortcoming (mishaps, inconsistencies, conflicting concepts or definitions, gaps, etc.) in the EU sustainable finance regulatory framework that might lead to greenwashing in the insurance sector or that might prevent the adequate mitigation of greenwashing in the insurance sector, please share below what these are:

We generally support the existing Sustainable Finance Regulatory framework, which should be further developed and specified to enable the necessary transformation of financial markets and the real economy while minimizing any greenwashing risk.

The unclarity and inconsistency in the regulatory framework is creating diverging interpretations and confusion for both consumers and investors, which can lead to unintentional flawed information on the part of financial market participants which should not be understood as greenwashing. In that context, further guidance e.g., on the application of Articles 8 and 9 of the SFDR is needed. However, the provision of level 3 guidance should not mean that divergent interpretations preceding their publication are automatically considered to be greenwashing.

Another challenge in the application of the EU Sustainable Finance framework which creates confusion and unintentional flawed information is the multiplication and sometimes contradicting definitions of what "green" is (e.g., definition of sustainable investment). The SFDR, the EU Taxonomy, the IDD and MiFID Delegated Acts, the ESMA consultation on funds' names, sustainability preferences and other voluntary frameworks all offer competing definitions.

Furthermore, some key elements of the EU sustainable finance framework are not yet finished and there are challenges with the sequencing that create difficulties for insurers to collect the ESG data they need. Robust ESG data is still very scarce due to the lack of reporting by companies (given that the CSRD is entering into application only from 2025) and the lack of transparency by ESG data providers and ESG ratings providers regarding methodologies and assumptions. This lack of data or lack of reliable third-party data is a source of greenwashing risk. In addition, it must be noted that insurers must currently rely on sustainability data for which, with regards to many ESG topics, methodologies and metrics are only at an early stage of development. Such a lack of maturity on ESG issues and methodologies can lead to the risk of unintentional under- or over-statement, which could create the impression of greenwashing or green bleaching (i.e., underestimating how sustainable a company/product is).

Another issue is the mismatch in timelines and application dates for the various initiatives under the EU sustainable finance framework as it creates a structural legal risk of greenwashing for insurers. For example, the inconsistent application timeline between the Insurance Distribution Directive (IDD) sustainability preferences, SFDR Article 8 and 9 templates (including amendments to disclose exposures to gas and nuclear activities) and Ecolabel regulation creates significant risk of greenwashing.

In addition, the necessary input for SFDR reporting will only be available from 2023 on the basis of the DA on Article 8 Taxonomy and only be available from 2024 on the basis of the new CSRD. Therefore, the financial sector faces a data gap creating very significant compliance and greenwashing challenges.

There are serious concerns and practical difficulties with the preparation and provision of the SFDR periodic disclosures. Firstly, there is a persistent difficulty in collecting the necessary data/underlying option disclosures from asset managers to comply with the SFDR requirements. Secondly, the SFDR periodic disclosures can be very long: for example, for MOPs, there might be a need to provide over 60 pages to clients on top of the Solvency II periodic disclosures. There is a need to allow the use of hyperlinks to existing information on the underlying funds in periodic disclosures, to help both clients and insurers to manage the number of documents.

Life insurance products with long term investment characteristics are particularly suitable for asset allocation that aims at financing the transition into a sustainable economy. They may therefore also use such mid- to long-term ambition to increase the share of sustainable investments as an element of the product description (or naming). Given regulatory diversification requirements for the underlying asset allocation of (certain) financial products, a taxonomy-aligned asset allocation can currently only be achieved to a very limited extent.

Customer information will have to be focused on getting this notion across accordingly as financing needs for the economic transition are tremendous.

For distribution and marketing of financial products, the regulatory framework provided by contract law, prospectus liability regime and marketing regulation (in addition to the specific Sustainable Finance Regulation in SFDR, MiFID II and IDD) is the right and sufficient mechanisms to address the design and the marketing of financial products with sustainability features or objectives.

Another issue could be the use of ETFs as funds in the insurance unit-linked product where these products have strong dependencies on large index providers, on which an increasingly large number of products are built (namely passive products and ETFs, which are also steadily increasing through time). Given the new EU sustainable finance regulations, a lot of products and portfolios depend on how large index provider define sustainability, or Paris alignment and so on. For example, an ETF-only insurance product will somehow need to rely on available investment vehicles in order to implement its sustainability policy. If the insurance provider considers that a revenue threshold of maximum 5% from fossil fuels should be applied to comply with its exclusion policy but that the index provider has defined this threshold to be 10%, and that most of the ETFs available are tracking this index, the insurance provider can't implement its policy. To tailor an index that aligns with the consumer's own investment aptitude is very costly for the insurance provider.

Annex I – Based on the ESAs Joint Call for evidence launched in November 2022:

Potential core characteristics of greenwashing[1]:

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, over simplistic, 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 mislabeling, 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

[1]As noted in the ESAs Joint Call for evidence, this should not be understood as the current view of EIOPA nor of the ESAs.

particular through mis-selling) or the gain of an unfair competitive advantage has been ascertained.

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