Sustainability Blog

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Our Anti-Greenwashing Framework: a preventive approach

Introduction to our Anti-Greenwashing Framework to protect your company from greenwashing risks

In our four-part blog series "Focus on ESG financial products: current market dynamics, SFDR and greenwashing risks", we have already addressed the issue of greenwashing in the financial industry, in particular asset management and looked at the definitions, causes, and options to minimize greenwashing risks. In this article, the question is posed what the financial industry can do to implement preventive measures for enhanced ESG compliance. What options are there to prevent greenwashing risks? What aspects and processes should the internal risk management process focus on? Learn more about our holistic Anti-Greenwashing Framework in order to address greenwashing risks at an early stage.

Sustainability is one of the key issues of our time, as is once more underlined by the current heat wave and forest fires in Europe. As part of the green transformation of the economy, the financial sector has been identified by the European Union as a key player due to its function as loan giver, risk manager, underwriter and asset manager. The EU has published a series of regulations such as the Taxonomy Regulation and the Sustainable Finance Disclosure Regulation aimed at bringing more transparency to sustainable investments and enhancing ESG risk management.

Current challenges and greenwashing risks

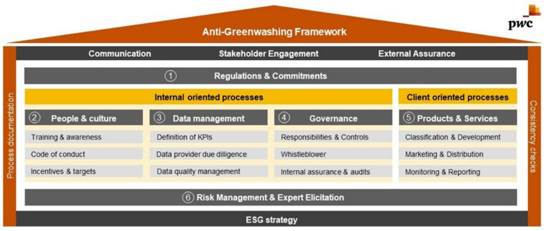
However, as the regulations are step-by-step introduced, the implementation of these regulations is still challenging for financial institutions in the absence of clear definitions and meaningful guidance with regard to the methodologies to be applied. Furthermore, there is still a lack of high-quality ESG data from the counterparties of financial institutions on which they are dependent for their own reporting. This is expected to improve with the entry into force of the Corporate Sustainability Reporting Directive from 2025 onwards which mandates standardized and more comprehensive ESG reporting. Hence, where there is sun, there is also a shadow: The complex and dynamic regulatory landscape proves challenging with regard to interpretation and can lead to mistakes in internal processes and reporting exposing companies to greenwashing risks. Furthermore, there is an increased scrutiny by external stakeholders such as NGOs, the media, and the general public, but also investors and business partners, when it comes to corporate ESG commitments. Companies have to be able to demonstrate how they plan to implement their commitments, e.g. by providing transition pathways with measurable benchmarks in the case of climate commitments, otherwise they risk being exposed for greenwashing.

In a nutshell, so-called “greenwashing” is currently not only a buzz word anymore, but depicts comprehensive reputational, operational and/or legal risks for firms. The increasing number of public greenwashing accusations against various financial market participants, including at senior management level, underlines related risks, which can occur, even if the relevant activity was conducted without false intent.

EU regulators have already begun to address the topic as for example the recently published progress reports on greenwashing by the European Supervisory Authorities have shown. But while specific anti-greenwashing rules are expected to be published by the Financial Conduct Authority in the UK, the EU still has a long way to go in order to properly address greenwashing on a broad basis. Accordingly, so far, no relevant best-practice examples are available on the market, which could assist firms in reducing related risks. So what can companies do in order to minimize the risk of greenwashing accusations? As these questions come up more frequently, PwC Germany has developed a comprehensive approach with its dedicated Anti-Greenwashing Framework which tackles all elements of greenwashing risks in relevant internal processes and functions of a company.

Anti-Greenwashing Framework

Our Anti-Greenwashing Framework provides a holistic guideline to identify the vulnerable processes and functions within a company and to define and implement appropriate countermeasures. Based on recent insights provided in the ESAs progress reports on greenwashing, this framework is designed to strengthen a firm's ESG-related compliance and establish preventive security gates. Due to its flexible structure, the framework is adaptable to the individual product portfolio, company type, location, and risk exposure of a company and therefore each company's specific structures and demands.



The framework consists of various (interrelated) components which are relevant for a sound ESG compliance structure that prevents and manages greenwashing risks. The company's ESG strategy constitutes the foundation of all respective processes, as it sets the ESG objectives depending on the ESG ambition level of the company. A credible ESG communication strategy and active stakeholder engagement are critical for a company's reputation.

Furthermore, external assurance is prescribed by several sustainability regulations, e.g. the Corporate Sustainability Reporting Directive or can be obtained on a voluntary basis to validate claims and commitments. These aspects can hence be seen as a frame, in which a company has to operate and that therefore needs to be taken into account in related internal processes.

Within this frame our framework identifies the regulatory obligations and voluntary commitments as crucial components for effective ESG compliance, as they define the ESG-related policies and actions as well as the scope of ESG reporting. In addition, it is important to integrate ESG risks into the company's risk management procedures. In particular consideration should be given to the evaluation of possible greenwashing events as part of the risk inventory process. Since greenwashing risks are manifold and hard to measure, we recommend the PwC Expert Elicitation as an approach to quantify greenwashing risks.

When assessing specific processes, the framework differentiates between internally oriented and client-oriented processes. While the first focuses on preventing greenwashing risks by establishing a compliance-based corporate culture (e.g. setting relevant incentives), data management structure (e.g. data due diligence), and governance (e.g. integration of ESG-related risks into the three lines of defense), the latter specifically targets the value chain of financial products, including their development as well as corresponding distribution, marketing, and monitoring procedures, which often exhibit a high exposure to greenwashing risks.

Finally, greenwashing risks can be significantly reduced through overarching transparency, granted through comprehensive process documentations as well as consistency checks between all processes and functions.

We recommend an iterative implementation process with three consecutive rounds of checks in order to address issues that can be fixed on a short-term basis, conduct a prioritization based on the highest risk areas and a cost-benefit analyses of relevant measures, as well as, finally, pursue a holistic approach covering all components, processes, and functions defined in the framework.

Next steps

We will provide a further deep dive on our Anti-Greenwashing Framework in a future blog post, including a detailed description of the previously mentioned components of the framework as well as a suggested approach for implementation.

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