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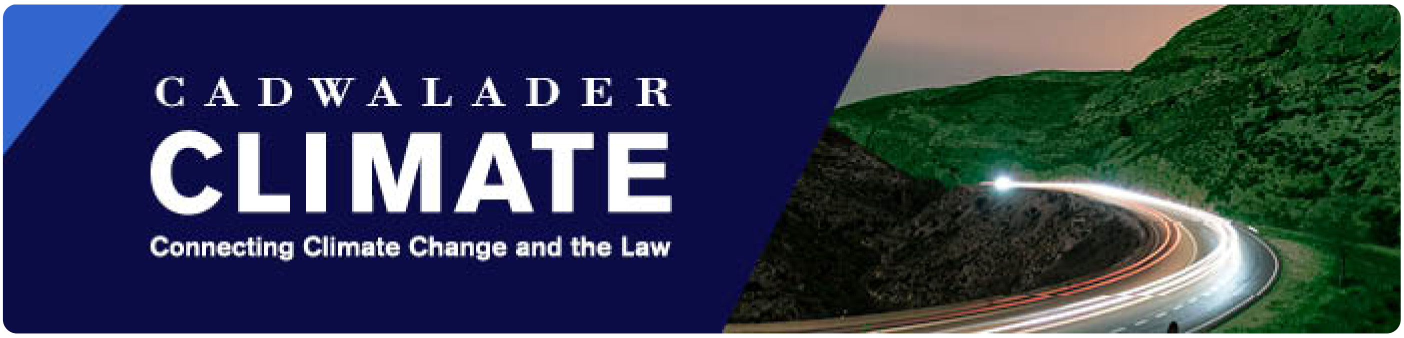
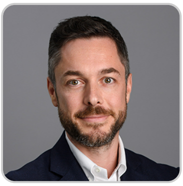


ESMA and NCAs to Assess Disclosures and Sustainability Risks in the Investment Fund Sector

September 5, 2023



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On July 6, 2023, the European Securities and Markets Authority (ESMA), in collaboration with National Competent Authorities (NCAs), **launched the Common Supervisory Action (CSA)** aimed at assessing the compliance of supervised asset managers with various regulations and implementing measures related to sustainable finance.

The primary objective of the CSA is to ensure that asset managers operating within the European Union adhere to the relevant provisions outlined in the Sustainable Finance Disclosure Regulation (SFDR), the Taxonomy Regulation, and applicable "Level 2 measures," including those within the Undertakings for Collective Investment in Transferable Securities (UCITS) and Alternative Investment Fund Managers Directive (AIFMD) implementing acts concerning the integration of sustainability risks.

The CSA aims to achieve several objectives:

- Assessing Adherence to Rules and Standards: The CSA will evaluate whether market participants, particularly asset managers, are complying in practice with applicable rules and standards. This assessment seeks to ensure the transparency and credibility of sustainability-related disclosures.
- Greenwashing Risk Identification: The CSA aims to gather additional information on greenwashing risks in the investment management sector.
- Supervisory and Regulatory Intervention: Based on the findings of the CSA, additional relevant supervisory and regulatory interventions may be identified and implemented to

mitigate the risks associated with incorrect or misleading disclosures and promote the integration of sustainability factors in investment practices.

The CSA is currently underway, having been launched on July 6, 2023, and will continue until September 2024.

Taking the Temperature: Asset managers operating within the EU should be prepared for increased scrutiny of their sustainability-related disclosures and risk integration practices. In line with the new package of measures to build on and strengthen the foundations of the EU sustainable finance framework published in June 2023, the CSA's focus on compliance with the SFDR, Taxonomy Regulation, and related measures underscores the importance of accurately and transparently communicating environmental, social, and governance factors to investors. Asset managers should also be mindful of the risk of greenwashing and take proactive measures to ensure the accuracy and authenticity of their sustainability claims, and as we previously reported, European financial regulators are paying increasing attention to greenwashing. In recent progress reports, regulators have articulated a common, high-level definition of greenwashing and outlined greenwashing risks, impacts, proposed mitigation efforts and challenges for their respective industries. At the same time, however, the European Commission has rejected suggestions that it introduce minimum environmental standards for Article 8 or Article 9 funds under the SFDR on the grounds that it is a disclosure regime, and therefore, it will not set minimum requirements for the key parameters of sustainable investment, such as "do no significant harm" and governance indicators. We also have previously reported on the decision late last year by a large number of asset managers to downgrade ESG funds due to a lack of guidance on how to apply the existing regulatory announcements in distinguishing Article 8 from Article 9 funds. All of which is to say that guidance and market practice in this area remains fluid and likely will continue to be unsettled for the foreseeable future.