Greenwashing in Investment Management

Comparative Regulatory and Fund Disclosure Responses

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Introduction

Environmental, social, and governance ("ESG")-oriented investing has become highly prominent in asset management as more investors seek sustainable investment vehicles. As investor interest has increased, the number of funds labelled "sustainable" or "ESG" has experienced similar growth.[1] A report by PWC projects that ESG-focused institutional investment will grow 84% from its 2022 levels, reaching $33.9 trillion (USD) in value and comprising 21.5% of global assets under management in 2026.[2] In Canada, the value of assets in "sustainable funds" grew 160% between 2020 and 2021, and the number of funds grew from 105 to 156.[3] In Europe, 27% of funds had been repurposed to include ESG factors by the end of 2021.[4]

The proliferation of ESG investing creates potential for greenwashing, where asset managers label funds as sustainable without undertaking corresponding ESG investment strategies. Early research indicates that corporations have incentives to change their fund names to capitalize on the increasing interest and cash inflow into ESG-labeled financial products. ESG-profiled funds receive higher cash inflows than non-ESG funds for both retail and institutional funds, irrespective of whether the fund was performing well on the Morningstar sustainability ratings.[5] In addition, some fund managers may be using ESG labeling to improve fund capital inflow: one study found that managers are converting their funds to ESG-focused funds when the funds' inflows are lagging behind inflows to other funds.[6]

While securities regulators globally have expressed concerns about this increased potential for greenwashing, regulatory responses have varied considerably.[7] The European Union ("EU") has developed a relatively comprehensive regulatory framework, whereas the Canadian and United States ("US") have adopted less formal approaches thus far. The US has largely addressed greenwashing through enforcement mechanisms, while Canada has offered guidance to fund issuers, with no formal enforcement or changes in disclosure requirements to date.

This paper seeks to evaluate the efficacy of each of these responses at improving the quality of fund's ESG disclosures. This paper will first provide an overview of the law and the different regulatory approaches in the EU, the US, and Canada today. This paper will then analyze the impact of the US and

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[1] https://www.pwc.com/gx/en/news-room/press-releases/2022/awm-revolution-2022-report.html
[2] https://www.pwc.com/gx/en/news-room/press-releases/2022/awm-revolution-2022-report.html#:~:text=London%2C%2010%20October%202022%20%E2%80%93%20Asset,in%20less%20than%205%20years.
[3] https://www.osc.ca/en/securities-law/instruments-rules-policies/8/81-334/csa-staff-notice-81-334-esg-related-investment-fund-disclosure (para beginning with "interest in ESG investing…"
[4] https://corpgov.law.harvard.edu/2022/11/17/exponential-expectations-for-esg/#:~:text=With%20ESG%20AuM%20under%20this,assets%20(21.5%25)%20by%202026.
[5]https://deliverypdf.ssrn.com/delivery.php?ID=114069009009102120024021098084012106004049020088012091073068101111009121067011110024018110017063062049097119014109030120125001008043088026052068106123094089001115105027052007111070122009007119000088088007068099087089101088111088029109120122028083029066&EXT=pdf&INDEX=TRUE
[6]https://deliverypdf.ssrn.com/delivery.php?ID=686112110110065116124031087008078117041064093064074050004007127102127117098113117089057097038029010061121125029122121087003092024002094022065087066094070102004127007064048071008116070003022007089084000019090116101016011002113005007006116097126111071102&EXT=pdf&INDEX=TRUE
[7] https://www.osc.ca/en/securities-law/instruments-rules-policies/8/81-334/csa-staff-notice-81-334-esg-related-investment-fund-disclosure (para beginning with "as the investment fund industry…"

Canadian regulatory responses to the quality of ESG disclosures in fund prospectuses. Finally, this paper concludes by finding that, based on the limited subset of funds analyzed, the Canadian regulatory response has been more effective at improving the quality of ESG disclosures.

Current Law Governing ESG Disclosure

The European Union Regulatory Response:

Of the jurisdictions considered in this paper, the European Union has undertaken the most comprehensive and stringent approach to regulating ESG reporting. In 2019, the EU adopted the Sustainable Finance Disclosure Regulation ("SFDR"), which targets financial market participants and financial advisers.[8][9] The requirements will be phased in gradually and will fully take effect in June 2024.[10] The SFDR was launched alongside the Corporate Sustainability Reporting Directive ("CSRD"), which delineates ESG-reporting requirements for public companies, and the EU Taxonomy Regulation, which clarifies the types of activities that can be classified as sustainable.[11]

The SFDR has extensive reporting requirements. At the firm level, financial institutions must disclose "Sustainability Risks", which include climate and other ESG-related risks that could materially affect the economic value of an investment. Asset managers must additionally disclose their Principal Adverse Impacts ("PAIs"), which include climate and other ESG-related risks.[12][13]

At the fund level, the SFDR requires funds to be classified as Article 6, Article 8, or Article 9 products and imposes tiered ESG reporting requirements in accordance with funds' self-selected classification. Article 6 funds do not undertake ESG-focused investment strategies, though are nonetheless subject to higher ESG reporting requirements than they were prior to the SFDR.[14] Under the new regulation, Article 6 funds must disclose the integration of sustainability risks in their funds. Article 8 and Article 9 funds include funds that integrate ESG considerations into their investment strategies. Any fund that promotes itself as an ESG fund is required to classify as an Article 8 or Article 9 product.[15] To be classified as Article 8, a fund must promote environmental or social characteristics or a combination of both and invest in companies that follow good governance practices.[16][17] Funds classified as Article 9 have sustainable

[8] https://academic.oup.com/cmlj/advance-article/doi/10.1093/cmlj/kmad005/7060045
[9] https://www.simmons-simmons.com/en/publications/ck6tebyfu23b30937xukyszhi/the-eu-disclosures-regulation-key-requirements-for-asset-managers
[10] https://go.factset.com/hubfs/Website/Resources%20Section/Brochures/sfdr-disclosing-principal-adverse-impact-indicators-brochure.pdf
[11] https://nordesg.de/en/eu-sustainable-finance-dislosures-regulation/
[12] https://go.factset.com/hubfs/Website/Resources%20Section/Brochures/sfdr-disclosing-principal-adverse-impact-indicators-brochure.pdf;
[13] https://www.matheson.com/docs/default-source/sustainable-finance/165_sfdr-factsheet--the-principal-adverse-impact-statement.pdf?sfvrsn=e9e0b170_4
[14] https://www2.deloitte.com/ie/en/pages/sustainablity/articles/sustainable-finance-disclosure-regulation.html?id=ie:2sm:3li:4SFDR%20article%20series::6audit:20210324090000::4649336566:5&utm_source=li&utm_campaign=SFDR%20article%20series&utm_content=audit&utm_medium=social&linkId=114217949
[15] https://www.msci.com/documents/1296102/23003857/SFDR_Proposed+Article+6-8-9+Mapping+Framework_Analysis+of+MSCI+ESG+Indexes.pdf (at the introduction)
[16] https://www.msci.com/documents/1296102/23003857/SFDR_Proposed+Article+6-8-9+Mapping+Framew
[17] https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/Audit/IE_SustainableFinanceDisclosureReg_Article8Funds.pdf (at pg 2)

investment or a reduction of carbon emissions as the fund's objective.[18] In practice, the precise parameters that differentiate these classifications are not clearly defined, but Article 8 and Article 9 funds both have heightened reporting requirements. Periodic fund disclosures include defining the ESG-oriented elements of their strategy, the proportion of sustainability-linked investments in the fund, and actions the fund took to meet its ESG goals.[19][20] As of September 2022, Article 8 and Article 9 funds comprised 33.6% and 4.3% of EU Funds respectively.[21]

The United States Regulatory Response

As of April 2023, US securities regulators have relied solely on SEC enforcement to address ESG disclosure concerns. However, numerous proposed rules could, if adopted, add a formal structure to govern ESG disclosure for public companies and investment fund managers.

The United States began its formal response to greenwashing concerns with the launch of the Securities and Exchange Commission ("SEC") Climate and ESG Task Force ("Task Force") in March 2021.[22] The Task Force aimed to proactively identify ESG-related misconduct and set up a whistleblower reporting mechanism to specifically evaluate and review ESG-related complaints.[23] Thus far, the Task Force has charged and settled greenwashing-related disputes with BNY Mellon Investment Advisor for misstatements and omissions about ESG considerations and with Goldman Sachs for policies and procedures failures related to marketing statements that Goldman Sachs made for its ESG funds.[24][25] In both cases, the charge was related to explicit statements about ESG-related policies and procedures that the firms failed to follow in practice. The SEC has yet to pursue cases where the conduct does not amount to a false statement.

The US has not yet officially introduced any regulation or guidance for fund managers; however, the SEC has proposed several changes to its rules that pertain to registered investment advisors, registered investment companies, and business development companies. First, the SEC is proposing three new categories for registered funds that consider ESG factors in their investment strategies. "Integration Funds" would consider ESG factors alongside non-ESG factors when selecting investments and would be required to disclose how ESG factors are incorporated into their investment process. "ESG-Focused Funds" would prioritize ESG factors in their investment strategy and would disclose details surrounding the strategy. Finally, "Impact Funds" seek to achieve particular ESG-related impacts and would be required to disclose

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[18] https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/Audit/IE_SustainableFinanceDisclosureReg_Article9.pdf (at pg 2).
[19] /https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/Audit/IE_SustainableFinanceDisclosureReg_Article8Funds.pdf (at 6,7,8);
[20] https://www2.deloitte.com/content/dam/Deloitte/ie/Documents/Audit/IE_SustainableFinanceDisclosureReg_Article8Funds.pdf (at 6, 7, 8)
[21] https://www.morningstar.co.uk/uk/news/227898/article-8-funds-shed-another-%E2%82%AC287bn.aspx
[22] https://www.sec.gov/news/press-release/2021-42
[23] https://www.sec.gov/news/press-release/2021-42
[24] https://www.sec.gov/news/press-release/2022-209
[25] https://www.sec.gov/news/press-release/2022-86

their objectives and progress.[26] This structure has some similarities to the SFDR's Article 6, Article 8, and Article 9 classification system. More generally, the proposed new disclosure rules would require funds to disclose information about their ESG practices.[27]

Second, the SEC has proposed to amend Rule 35d-1 under the *Investment Company Act of 1940* ("Names Rule") to include ESG.[28][29] The Names Rule aims to ensure that fund names reflects the fund's investments and risk profile, and has historically been applied to funds that state a particular focus on a type of investment, industry or geography, or that indicate distributions are tax-exempt.[30][31][32] It requires funds to have 80% of their investment in assets that reflect the funds' name.[33] The proposal would effectively preclude Integration Funds and non-ESG funds from using ESG terms in the fund name, as doing so would be considered materially deceptive or misleading.[34] Comments on the initial proposal raised concerns that ESG factors are subjective, which would make testing the 80% threshold challenging and that this could disincentivize funds from pursuing ESG strategies.[35]

The announcement of these proposed rules comes only two months after the SEC proposed the rule *The Enhancement and Standardization of Climate-Related Disclosures for Investors* ("Proposed US Framework"), which focuses on climate-related disclosures by public US companies.[36] The Proposed US Framework requirements are less stringent than the EU's CSRD, but would likewise require public companies to disclose their climate risk-management policies. The Proposed US Framework also requires companies to report their direct and indirect greenhouse gas emissions and delineates a scheme for standardizing these disclosures.[37]

The Canadian Regulatory Response

Canada does not have formal regulations on greenwashing or ESG reporting, however, the Canadian Securities Administrators ("CSA") published the non-legally binding *CSA Staff Notice 81-334 – ESG-Related Investment Fund Disclosure* ("CSA Staff Notice") on January 19th, 2022, providing a set of guiding best practices on ESG disclosure and ESG marketing for Canadian investment funds.[38] The CSA Staff Notice includes definitions of commonly-used ESG terms and provides ESG-related disclosure

[26] https://www.sec.gov/files/ia-6034-fact-sheet.pdf
[27] https://www.nortonrosefulbright.com/en/knowledge/publications/915ef285/us-sec-proposes-new-esg-disclosure-rules-for-funds-and-advisers
[28] https://www.sec.gov/news/press-release/2022-91
[29] https://www.sec.gov/files/ic-34593-fact-sheet.pdf
[30] https://www.klgates.com/Registered-Funds-And-The-New-Name-Rule-Proposals-What-You-Need-to-Know-And-Why-You-Need-to-Comment-Now-6-9-2022#:~:text=The%20current%20Names%20Rule%20requires,adopt%20a%20corresponding%2080%25%20Policy.
[31] https://www.sec.gov/files/ic-34593-fact-sheet.pdf (at 1)
[32] https://www.ropesgray.com/en/newsroom/alerts/2022/june/sec-proposes-changes-to-the-fund-names-rule
[33] https://www.ropesgray.com/en/newsroom/alerts/2022/june/sec-proposes-changes-to-the-fund-names-rule
[34] https://www.sec.gov/files/ic-34593-fact-sheet.pdf (at 2)
[35] https://www.ft.com/content/d7ec1fb6-8be6-4350-9526-657b07d4ffa3
[36] https://www.nortonrosefulbright.com/en/knowledge/publications/c8a01926/climate-greenwashing-liability
[37] U.S. Securities and Exchange Commission, "SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors" (March 21 2022), online: *US Securities and Exchange Commission* <www.sec.gov/news/press-release/2022-46>.
[38] https://www.osc.ca/en/securities-law/instruments-rules-policies/8/81-334/csa-staff-notice-81-334-esg-related-investment-fund-disclosure

recommendations on a wide variety of subjects, including fund ratings, ESG strategies, ESG-related risks, and shareholder engagement, among other things. The CSA Staff Notice also indicates that funds that reference ESG or related factors in their names should have the corresponding ESG aspect as a fundamental investment objective.[39]

Takeaways

These different approaches to addressing greenwashing each raise their own novel concerns. Formal classification and disclosure requirements akin to the European approach have been criticized for the ambiguity surrounding ESG terminology. For instance, managers use the definition of "sustainable" investments to classify their funds as Article 8 and Article 9, which could inadvertently lead to greenwashing if funds are improperly classified.[40] However, the definition of sustainable is not yet objectively clear in practice. The US's proposed change to the Names Rule would create similar concerns regarding ESG definitions.[41] However, the US and Canada's current lack of formal regulation raises a separate concern that funds will follow economic incentives to add ESG labelling to their funds without providing adequate protection or recourse to investors against misleading labels. Under this the current regulation structure, the US's private enforcement approach has been limited to penalizing funds whose disclosures amount to untrue statements rather than misleading investment strategies.

Creating incentives for robust and transparent disclosure is one way for securities regulators to promote investor protection against greenwashing as these definitions continue to develop. The following section of this paper assesses the effectiveness of the US and Canadian schemes against this metric.

Methodology

To assess the impact of the Canadian and American responses to greenwashing concerns on the quality of fund ESG disclosures, we analyzed the historical prospectus filings for three ESG-related funds in both the US and Canada. In addition, we analyzed the historical prospectus filings of the two firms sanctioned by the SEC over greenwashing concerns, Goldman Sachs Asset Management and BNY Mellon (collectively, the "Sanctioned Issuers"), to assess any changes in ESG disclosure quality for firms that are directly punished.

Funds were selected through a two-step process. First, the fund issuers were selected by taking the top three issuers in each country by total assets under management. The selected fund issuers also had to

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[39] https://www.osc.ca/en/securities-law/instruments-rules-policies/8/81-334/csa-staff-notice-81-334-esg-related-investment-fund-disclosure (at para beginning with "staff note that the existing requirements")

[40] https://www.intuition.com/european-funds-warn-of-greenwashing-epidemic-amid-confusion-over-sustainability-disclosure-rules/

[41] https://deliverypdf.ssrn.com/delivery.php?ID=178085004002122028001077126111001024060082067020068050097083090005006085095006117071031096111043054039035082102008075119024086022055033035034016115009097074003004069095034064126098065119024074007124113071026001004078074118065101075092007091125064002081&EXT=pdf&INDEX=TRUE

have their list of offered funds available publicly on their website and had to offer one or more actively managed ESG-related funds. For Canada, the selected issuers were TD Asset Management ("TD"), RBC Global Asset Management ("RBC") and CIBC Asset Management ("CIBC").[42] For the United States, the selected issuers were BlackRock, The Vanguard Group ("Vanguard") and Fidelity Investments ("Fidelity"), in addition to the Sanctioned Issuers.[43] Second, funds were selected by taking the top ESG-related fund from each selected issuer in terms of total assets. The selected funds were the TD North American Sustainability Equity Fund, RBC Vision Global Equity Fund, CIBC Sustainable Global Equity Fund, BlackRock Sustainable Advantage Large Cap Core Fund, Vanguard Global ESG Select Stock Fund, Fidelity Sustainable U.S. Equity Fund, Goldman Sachs U.S. Equity ESG Fund and BNY Mellon Sustainable U.S. Equity Fund.

Funds were assessed by comparing the most recent fund prospectus (2022) with the previous year's version (2021). All of the 2022 prospectuses analyzed were published after the CSA Staff Notice and the SEC's first greenwashing charges were released (these were published in March and May 2022, respectively), so the 2022 prospectuses will reflect each fund's behaviour towards these changes in the regulatory landscape. Given the uncertainty of when knowledge of the SEC's investigations into BNY Mellon and Goldman Sachs would have surfaced, the 2020 prospectuses for the US funds were also analyzed and discussed in the Results section of this paper where material differences were discovered.

Changes in the quality of fund ESG disclosures were measured using two criteria: (1) changes in the level of detail about how ESG factors were included in the investment methodology and (2) changes in the level of commitment to following the stated investment methodology. For changes in the level of detail about how ESG factors were included in the investment methodology, the current and historical prospectuses were compared to document discrepancies. For example, this could include changes in the details shared about the fund's processes for company screening, security selection and use of third-party ESG ratings agencies. For changes in the level of commitment to following the investment methodology, the current and historical prospectuses were compared to document if any statements had been added or removed that seek to limit the strength of the fund's commitment to following its stated investment methodology. For each of these criteria, funds were assigned a rating of "Improved", "Neutral" or "Worsened", along with an overall rating for each fund based on the results of these two criteria. Funds with one criteria assessed as Improved and the other as Worsened received an overall rating of Neutral. These criteria were chosen because providing detailed information about the integration of ESG considerations into the investment methodology for funds labelled as ESG or sustainability related is important for investors to be able to determine which funds are best aligned with their preferences.

[42] https://www.td.com/ca/en/asset-management/documents/institutional/pdf/Benefits-Canada-2022.pdf
[43] https://www.swfinstitute.org/fund-manager-rankings

Furthermore, it is important for investors to have confidence that the published investment methodologies are being followed consistently and correctly.

Since this paper seeks to examine the effect of changes to the Canadian and American regulatory landscape following the CSA Staff Notice and the SEC's charges against BNY Mellon and Goldman Sachs, only changes in the quality of the prospectus filings were analyzed, rather than assessing the overall quality of each fund's prospectus.

Results

Canada

TD North American Sustainability Equity Fund

TD was given an Improved rating for the level of detail about the ESG factors considered in its investment methodology when comparing the 2022 and 2021 prospectuses. The 2022 fund prospectus contains a considerable amount of additional detail pertaining to how the fund utilized ESG considerations in security selection, describing a two-stage process. The first stage is to identify the universe of eligible investments through fundamental analysis (non-ESG related), while the second stage is to apply a positive screen for "sustainable leaders", which TD defines as companies who are making positive contributions to the achievement of the United Nations Sustainable Development Goals ("SDGs") based on both product and operational alignment.[44] While the 2021 prospectus refers to selecting issuers who are making positive contributions towards the SDGs, there is no mention of the two-stage selection process or the assessment criteria of product and operational alignment with the SDGs.[45] The 2022 prospectus also states that the fund uses third-party ESG ratings to ensure that the fund's ESG rating was higher than the ESG rating of its reference index.[46] There is no information about the use of third-party ratings in the 2021 prospectus.[47]

TD was given a Neutral rating for the level of commitment to following its investment methodology, as there are no statements added or removed that seek to limit the extent to which TD is expected to consistently follow its stated investment processes. Overall, TD was assessed an Improved rating for its ESG disclosures given the Improved rating for ESG investment methodology details and the Neutral rating for the level of commitment to following its investment methodology.

RBC Vision Global Equity Fund

RBC was given an Improved rating for the level of detail about the ESG factors considered in its investment methodology when comparing the 2022 and 2021 prospectuses. Both the 2021 and 2022

[44] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00049998&issuerType=02&projectNo=03400349&docId=5555088
[45] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00049998&issuerType=02&projectNo=03239468&docId=5285327
[46] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00049998&issuerType=02&projectNo=03400349&docId=5555088
[47] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00049998&issuerType=02&projectNo=03239468&docId=5285327

prospectuses state that RBC partnered with Sustainalytics as part of the screening process, while the 2022 prospectus provides additional details about the nature of this partnership, such as being provided with an exclusion list of ineligible issuers for the fund based on ESG criteria.[48] RBC also states that material ESG factors are included in the second stage of its investment process (security selection after the negative screening obtained from Sustainalytics) in the 2022 prospectus, while there is no mention of ESG factors being included in this stage of security selection in the 2021 prospectus.[49][50]

RBC was given a Neutral rating for the level of commitment to following its investment methodology. There was an additional statement in the 2022 prospectus that was not present in 2021 stating that the fund "may from time to time depart from its exclusion list when RBC GAM has determined that it would be in the best interest of the fund to do so, such as when RBC GAM has identified inaccuracies in the data, or incomplete data due to more recent developments or events, used to produce its exclusion list".[51] RBC was not given a Weakened rating for including this statement because there is a delineation of when the fund can depart from its investment methodology (when it is in the best interest of the fund). Furthermore, the examples provided of where it may be appropriate to depart from the exclusion all relate to data quality, conveying that this statement is likely not intended to broadly weaken the fund's commitment to following its investment methodology. As with TD, RBC was given an overall Improved grade for its 2022 prospectus given the Improved and Neutral grades for the two criteria.

CIBC Sustainable Global Equity Fund

CIBC was given an Improved rating for the level of detail about the ESG factors considered in its investment methodology when comparing the 2022 and 2021 prospectuses. There is a considerable amount of information in the 2022 prospectus about CIBC's ESG investment principles that is not present in the 2021 prospectus. For example, the 2022 prospectus states that the fund excludes issuers based on quantitative and qualitative assessments on business and product involvement with non-ESG friendly topics and companies involved in a severe controversial event, while no such information is provided in the 2021 prospectus.[52] The 2022 prospectus also states that the fund utilizes inclusionary screening that may select funds that have a positive ESG impact, with no such statement present in 2021.[53]

CIBC was given a Neutral rating for the level of commitment to following its investment methodology, as there are no statements added or removed that seek to limit the extent to which CIBC is

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[48] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00025375&issuerType=02&projectNo=03387821&docId=5536380
[49] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00025375&issuerType=02&projectNo=03387821&docId=5536380
[50] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00025375&issuerType=02&projectNo=03226001&docId=5272936
[51] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00025375&issuerType=02&projectNo=03387821&docId=5536380
[52] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00052153&issuerType=02&projectNo=03367469&docId=5512272
[53] https://www.sedar.com/GetFile.do?&lang=EN&docClass=9&issuerNo=00052153&issuerType=02&projectNo=03367469&docId=5512272

expected to consistently follow its stated investment processes. As with TD and RBC, with one Improved rating and one Neutral rating, CIBC was given an overall Improved rating.

United States

BlackRock Sustainable Advantage Large Cap Core Fund

BlackRock was given an Improved rating for the level of detail about the ESG factors considered in its investment methodology when comparing the 2022 and 2021 prospectuses. BlackRock provided further clarity about how it utilizes ESG factors to screen out companies that is not present in the 2021 prospectus. While the 2021 prospectus outlines certain non-ESG friendly industries that BlackRock wishes to screen out, the 2022 prospectus provides quantitative thresholds for what percentage of revenue a company much earn from non-ESG friendly sectors to be screened out, the data for which is provided by third-party ratings agencies.[54][55] BlackRock also includes references to ESG characteristics in the Investment Objective section of the prospectus, stating that the fund seeks to maintain certain ESG characteristics, climate risk exposure and climate opportunities relative to the fund's benchmark.[56] There is no reference to ESG or climate factors in the 2021 prospectus.

BlackRock was given a Worsened rating for the level of commitment to following its investment methodology. The ESG Investing Risk section of the 2022 prospectus contains the following statement: "There is also a risk that BlackRock may not apply the relevant ESG criteria correctly…Neither the Fund nor BlackRock make any representation or warranty, express or implied, with respect to the fairness, correctness, accuracy, reasonableness or completeness of such ESG assessment."[57] Unlike the statement in RBC's 2022 prospectus, which pertained to data quality, this statement is clearly intended to broadly limit the extent to which BlackRock is legally obliged to consistently and correctly follow the ESG portion of its stated investment methodology. No statement of this nature is present in the 2021 prospectus. Since BlackRock was given one Improved rating and one Worsened rating, it has received an overall Neutral fund rating.

Vanguard Global ESG Select Stock Fund

Vanguard was given a Neutral rating for both the level of detail about the ESG factors considered in its investment methodology and for the level of commitment to following its investment methodology as there are no material differences between the 2021 and 2022 prospectuses.[58][59]

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[54] https://www.sec.gov/Archives/edgar/data/844779/000119312522256473/d392410d497k.htm
[55] https://www.sec.gov/Archives/edgar/data/844779/000119312521289451/d165350d497k.htm
[56] https://www.sec.gov/Archives/edgar/data/844779/000119312522256473/d392410d497k.htm
[57] https://www.sec.gov/Archives/edgar/data/844779/000119312522256473/d392410d497k.htm
[58] https://www.sec.gov/Archives/edgar/data/734383/000168386322004845/f12533d1.htm
[59] https://www.sec.gov/Archives/edgar/data/734383/000168386321003791/f9095d1.htm

Fidelity Sustainable U.S. Equity Fund

Fidelity was given an Improved rating for the level of detail about the ESG factors considered in its investment methodology when comparing the 2022 and 2021 prospectuses. The 2022 prospectus contains additional information about the fund employing ESG exclusion criteria to avoid investing in companies that are engaged in non-ESG friendly industries.[60] There is no statement about the fund employing exclusionary criteria in the 2021 prospectus.[61]

Fidelity was given a Neutral rating for the level of commitment to following its investment methodology, as there are no statements added or removed that seek to limit the extent to which Fidelity is expected to follow its stated investment methodology. Fidelity was therefore given an overall Improved rating.

BNY Mellon Sustainable U.S. Equity Fund

BNY Mellon was given an Improved rating for the level of detail about ESG integration into the investment methodology. For example, in the 2022 fund prospectus, BNY Mellon states that the fund employs negative screening criteria to remove companies with material negative ESG issues from the investible universe, while this is not mentioned in the 2021 prospectus.[62][63] BNY Mellon also provided a considerable amount of additional detail on how it implements its ESG quality reviews and sustainable investment criteria in the 2022 prospectus.[64]

BNY Mellon was given a Neutral rating for the level of commitment to following its investment methodology, as there are no statements added or removed that seek to limit the extent to which BNY Mellon is expected to follow its stated investment methodology. There are also no material differences found in the 2020 prospectus in this respect. BNY Mellon was therefore given an overall Improved rating.

Goldman Sachs U.S. Equity ESG Fund

Goldman Sachs was given an Improved rating for the level of detail about how ESG considerations factored into the fund's investment methodology. While there are no changes to the stated investment methodology between the 2022 and 2021 prospectuses, there are material differences compared to the 2020 prospectus. There is a significant amount of additional detail provided in the 2021 and 2022 prospectuses about how the fund screen's out companies from non-ESG friendly sectors. The 2020 prospectus merely states that the fund will use industry classifications from a third-party provider, while the 2021 and 2022

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[60] https://www.sec.gov/Archives/edgar/data/225322/000137949122002881/filing820665801.htm
[61] https://www.sec.gov/Archives/edgar/data/225322/000137949121002550/filing707206642.htm
[62] https://www.sec.gov/Archives/edgar/data/30167/000003016722000010/c0035bnymsusef-0920221.htm
[63] https://www.sec.gov/Archives/edgar/data/30167/000003016721000007/c0035bnymsusef-0920211.htm
[64] https://www.sec.gov/Archives/edgar/data/30167/000003016722000010/c0035bnymsusef-0920221.htm

prospectuses define revenue percentage thresholds from non-ESG friendly sectors that will result in a company being screened out.[65][66]

Goldman Sachs was given a Worsened rating for the level of commitment to following its investment methodology. The fund's investment methodology consists of an initial negative screen to eliminate companies from non-ESG friendly sectors, followed by a "supplemental analysis" of ESG factors alongside traditional fundamental analysis.[67] The 2021 and 2022 prospectuses state that "The Fund may invest in a company prior to completion of the supplemental analysis or without engaging with company management."[68] No statement of this nature is included in the 2020 prospectus. This statement is clearly intended to limit the extent to which Goldman Sachs must consistently follow its stated investment methodology. The addition of this statement to the 2021 and 2022 prospectuses is particularly noteworthy given that the SEC specifically charged Goldman Sachs with not consistently following its written policies and procedures related to the ESG investment process.[69] With one Improved rating and one Worsened rating, Goldman Sachs was given an overall fund rating of Neutral.

Discussion

As shown in Table 1 and Table 2, out of the funds analyzed, the Canadian funds improved to a greater extent than the US funds in terms of the quality of the ESG disclosures in each fund's prospectus. All three of the analyzed Canadian funds improved the quality of their ESG disclosures, while two of the five US funds analyzed improved, including only one of the three non-sanctioned issuers. Given the differing results of the US Sanctioned Issuers, it is not possible to draw a conclusion on the behaviour of sanctioned funds compared to non-sanctioned funds. The lower US results are due to one fund issuer (Vanguard) failing to improve the amount of detail about how ESG factors are woven into the investment methodology and two fund issuers (BlackRock and Goldman Sachs) adding statements to their most recent prospectuses that aim to limit the degree to which they are obligated to consistently follow their stated investment methodologies.

Table 1: Canadian Fund Issuer Results

Fund Issuer	**TD**	**RBC**	**CIBC**
ESG Methodology Detail	Improved	Improved	Improved
Methodology Commitment	Neutral	Neutral	Neutral
Overall	*Improved*	*Improved*	*Improved*

[65] https://www.sec.gov/Archives/edgar/data/822977/000119312522313644/d362857d497k.htm
[66] https://www.sec.gov/Archives/edgar/data/822977/000119312520327949/d28209d497k.htm
[67] https://www.sec.gov/Archives/edgar/data/822977/000119312522313644/d362857d497k.htm
[68] https://www.sec.gov/Archives/edgar/data/822977/000119312522313644/d362857d497k.htm
[69] https://www.sec.gov/litigation/admin/2022/ia-6189.pdf

Table 2: American Fund Issuer Results

Category	*Non-Sanctioned Issuers*			*Sanctioned Issuers*	
Fund Issuer	**BlackRock**	**Vanguard**	**Fidelity**	**BNY Mellon**	**Goldman Sachs**
ESG Methodology Detail	Improved	Neutral	Improved	Improved	Improved
Methodology Commitment	Worsened	Neutral	Neutral	Neutral	Worsened
Overall	*Neutral*	*Neutral*	*Improved*	*Improved*	*Neutral*

This discrepancy could possibly be explained by the differing regulatory responses to greenwashing in Canada and the US. With the CSA Staff Notice, the Canadian regulatory response has been to provide issuers with detailed guidance on what information is expected to be disclosed in fund prospectuses, with no enforcement from securities regulators to date. In contrast, the US regulatory response has been for the SEC to punish issuers who provide misleading representations of their ESG investment practices, while not providing the same level of guidance as the CSA, though this is currently in progress. It is possible that the SEC's enforcement of greenwashing cases has caused some issuers to become concerned about potential liability if they do not apply their ESG methodologies consistently, thus explaining the new statements found in the BlackRock and Goldman Sachs prospectuses. Furthermore, the lack of formal guidance offered to US issuers, compared to Canadian issuers, could explain the differing levels of additional detail on the ESG investment methodology found in the sample of US funds analyzed.

Conclusion

This paper has provided an overview of the regulatory responses in the EU, US and Canada to rising concerns of greenwashing in investment management. While the EU has taken a comprehensive regulatory approach through the formation of the SFDR, this has not yet been followed in Canada and the US. Without a formal regulatory structure in place, Canadian and American securities regulators have responded to greenwashing concerns in very different ways. In the US, the SEC has addressed greenwashing concerns by charging fund issuers who provide misleading information about the methodologies of integrating ESG into the investment process. In Canada, the CSA has published detailed guidance on how fund issuers should disclose their ESG investment practices, while there has been no enforcement to date.

Given the differing regulatory responses in Canada and the US, this paper explored which response has been more effective through analyzing changes in the quality of ESG disclosures in fund prospectuses before and after the respective changes in the regulatory environment. From the funds analyzed, the Canadian regulatory response has been more effective at improving the quality of ESG disclosures. While all of the Canadian funds improved the level of detail offered about how ESG factors are integrated in the fund's investment methodology, improvements in this area were less consistent in the US and some issuers have added additional statements seeking to limit the degree to which they are required to consistently follow their ESG methodologies. It is important to note that the sample of funds analyzed in this paper is relatively small. Further research on a larger sample size of funds is recommended to verify these results.