The practices to avoid greenwashing through EU regulations and their sustainable impact on the financial sector

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THE PRACTICES TO AVOID GREENWASHING THROUGH EU REGULATIONS AND THEIR SUSTAINABLE IMPACT ON THE FINANCIAL SECTOR

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Abstract

In the face of climate change, our policies must act to prevent an unprecedented crisis. To this end, the European Union is committed to a series of international agreements. The most important of these is the Paris Agreement, which aims to limit global temperature increase to 1.5 degrees Celsius by 2030. To achieve this agreement, public funds are not enough to support the needed investments to make our society more sustainable. Private investors are, therefore, called upon to contribute to the transition of our economy towards a more sustainable model. However, this change in investment flow puts a lot of pressure mostly on polluting companies. Unfortunately, a change of business model is not easy to implement and it leads some of them to lie about their environmental performance. This disruptive phenomenon, also known as greenwashing, hinders the transition of our economy. In response to this issue, the European Union has put in place some regulations known as the SFDR, the European Taxonomy and MiFID II ESG to push companies to disclose more information about their sustainability and limit deceiving investors. Sustainable finance is a necessary asset to reach those objectives. These new green regulations' goal is to focus on reducing carbon emissions into the atmosphere.

Despite the EU's efforts to make finance sustainable, the timeline of its new regulations' enforcement is affecting the market. Therefore, the purpose of the present work is to determine their impacts on greenwashing and on the market players who have to integrate them. Furthermore, this study focuses on the latest law implemented since August 2022, which is called MiFID II ESG. Through a qualitative survey, participants from the financial sector gave us insight regarding their regulatory journey. As a result, we concluded that those regulations are a major step toward sustainable finance despite the presence of possible misinterpretations which may create a build-up of false information and, thus, fuel greenwashing.

Key words:

MiFID II ESG – sustainability preferences – sustainable finance – greenwashing – EU regulations

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Abbreviations

- CSR: Corporate Social Responsibility
- CSRD: Corporate Sustainability Reporting Directive
- EC: European Commission
- EET: European ESG Template
- EP: Environmental Performance
- ESG: Environmental, Social and Governance
- ESMA: European Securities and Markets Authority
- EU: European Union
- GD: Green Deal
- IIA: Index Industry Association
- IPPC: Intergovernmental Panel on Climate Change
- MiFID: Markets in Financial Instruments Directive
- OECD: Organisation for Economic Co-operation and Development
- PCA: Paris Climate Agreement
- Regulation 2019/2088: SFDR
- Regulation 2020/852: European Taxonomy
- Regulation 2021/1253: MiFID II ESG
- SDG: Sustainable Development Goal
- SFDR: Sustainable Finance Disclosure Regulation

CHAPTER 1: INTRODUCTION

1.1. Research Context

Over the past decade, our society's concern about climate change has increased. This issue has put intense pressure on companies to disclose information about their environmental performance in their annual report (de Freitas Netto et al.,2020). According to a study conducted by the Index Industry Association (IIA) (2021), there is significant growth in ESG investments. Eighty-five percent of asset managers interviewed in the survey expect that "ESG will become even more important to their companies in the future" (IIA, 2021). Following these assumptions, the IIA (2022) found in its second annual ESG report that asset managers expect nearly two-thirds of investment portfolios to be more sustainable within ten years through the addition of ESG criteria (IIA, 2022). However, in the absence of clear guidelines and due to the lack of international standards, some entities use this new environmental matter to green market their goods in order to reach stakeholders, even though their products cannot be considered sustainable (de Silva Lokuwaduge et al., 2022). This trend, called greenwashing, destroys investors' trust in ecological values and tarnishes the image of truly sustainable companies (de Freitas Netto et al.,2020). According to a Deloitte (2021) report, entitled "Greenwashing risks in asset management", this phenomenon arises when a company makes misleading or exaggerated claims about the environmental benefits of its products or services in a given situation. Such a scenario destroys stakeholder confidence in the market and ultimately leads to a misallocation of capital towards sustainable investments, as investors buy unsustainable products thinking otherwise (Deloitte, 2021).

For several years, Europe has desired to switch its economy to a more sustainable model (Pizzi et al., 2022). In fact, measures have been taken to increase transparency in non-financial information in order to reduce the information gap between stakeholders and companies (Pizzi et al., 2022). This growing commitment has led many companies to disclose their environmental impacts to comply with legal requirements. According to Pizzi et al. (2022), non-financial reporting has been able to push companies to adopt more sustainable behaviors through the so-called new transparency requirements. However, according to the IIA's 2022 study, companies do not consistently disclose ESG data and information. Indeed, there is a lack of transparency in quantitative and qualitative data, as well as a lack of standardization of data across markets and sectors (IIA, 2022). In response to this, the European Union added a set of green regulations to limit greenwashing and increase green investments (Deloitte, 2022). This package includes the Sustainable Finance Disclosure Regulation (SFDR), the European Taxonomy, the amendments to MiFID II, and finally, the Corporate Sustainability Reporting Directive (CSRD) (European Commission, 2021e). SFDR is the disclosure of information on financial products to increase the transparency of sustainability-related information and their performance concerning sustainability (European Commission, n.d.b). The Taxonomy consists of a classification system for economic activities to determine which activities are considered environmentally sustainable (European Commission, n.d.a). The amendment of MiFID is the integration of ESG criteria when selecting financial instruments in a client's portfolio. Therefore, sustainability preferences are added to the consultant-investor relationship (Regulation (EU) 2021/1253). Finally, the CSRD is a proposal by the Commission to modify the current reporting requirements of the NFRD. Indeed, in addition to setting non-financial reporting requirements, it will increase transparency and information provision while considering ESG criteria to assess companies' performance (European Commission, 2021f; Gueguen, 2022). However, as the CSRD is still a draft legislation, it has not yet entered into force and remains subject to discussion at the commission level, thus, it is a difficult directive to evaluate (Gueguen, 2022). In implementing these new regulations, the EU will ensure that all member states follow uniform criteria for green investment (European Commission, 2021e).

The expanded MiFID II was adopted on the 21st of April 2021 and will be applied from the 2nd of August 2022 (Regulation (EU) 202I/1253). As the last of the four regulations to be implemented this year, it is the least integrated regulation in the business. MiFID II 2021/1253 is changing the entire financial system. Indeed, by incorporating sustainability factors, risks and preferences into specific organizational requirements and operating conditions, investment firms and companies in need of money will have to change their physical structure to meet this new European regulation that is based on both SFDR and Taxonomy (ESMA, 2022a; Regulation (EU) 202I/1253). The objective of this measure is to ensure that sustainability considerations are systematically taken into account in financial product recommendations by advisors to investors (European Commission, 2021e). This is to ensure that everyone can have an impact on the climate through their investments (European Commission, 2021e). As a result, it could help the EU meet its emissions reduction target set by the Paris Climate Agreement by forcing companies to integrate ESG considerations into their organizational requirements in order to redirect private capital to a more sustainable economy (Allen Overy, 2021).

1.2. Main Objective

The world is falling apart. Between catastrophic weather events and a vulnerable population, politicians must take necessary steps to reduce the risk of a crisis (Lahsen & Ribot, 2022). Indeed, always attributing extreme events to climate change is not a solution. The vulnerability of society leads to even more severe crises than expected due to the non-adaptability of the population (Lahsen & Ribot, 2022). According to Lahsen & Ribot (2022), measures must be taken to prepare society for any climate event. Moreover, the government is not the only stakeholder seeking new actions to mitigate the risk of the crisis. Investors, consumers, and financial institutions are increasingly putting pressure on companies to disclose information about their environmental performance (de Freitas Netto et al., 2020). This new demand is supported by the need for corporations to produce in a way that reduces their impact on the climate (de Freitas Netto et al., 2020). However, due to the increased pressure on companies from many market players, a spectrum of forms of greenwashing has emerged (Gatti et al., 2021). Indeed, as greenwashing has multiple facets, there is no single definition of this concept (de Freitas Netto et al., 2020). According to Terrachoice’s survey, a company can deceive its stakeholders in different ways. The problem of greenwashing is, therefore, becoming increasingly difficult to detect, which raises the question of whether MiFID II ESG and the regulations on which it is based really have the potential to reduce it or not.

Before MiFID I, no reliable information was available for fund investors to be aware about the management fees generated by asset managers during the investment process (Liu, 2022). In addition, asset managers also lacked the disaggregated data from brokers to properly track and assess performance and their research costs (Liu, 2022). Financial regulators and the European Commission were, therefore, concerned that the opacity of these exchanges would produce a disadvantage for the investor. With MiFID I and II, regulators sought to address these problems and achieve greater transparency in the market (Liu, 2022). Since the integration of sustainable preferences in MiFID II, the client is now also involved in the allocation of funds that will constitute his investment portfolio. Indeed, for the first time, the client is asked about his values in terms of sustainability (Regulation (EU) 2021/1253). This means that the asset manager will now not only have to take into account the client's risk aversion and desired return, but also the sustainability preferences will have to be in line with the funds the client will own (Regulation (EU) 2021/1253). Sustainable finance has an important role to play in meeting the objectives that the EU has set itself in the context of international climate and sustainability commitments. Furthermore, implementing these new regulations can only improve transparency regarding ESG risks (European Union, n.d.c.). Therefore, it is imperative to study the potential impact that expanded MiFID II ESG could have on the transformation of the investment industry.

The research objectives are twofold: to better understand what the MiFID II amendments bring to the market and the effects of it, as well as the regulations on which it is based to observe their impact on greenwashing. The main research question of this thesis could be formulated as follows: Will the latest EU green regulation limit the risk of greenwashing? Furthermore, how is the MiFID II ESG a step forward in protecting investors? Finally, will these regulations allow the green transition towards which Europe wishes to move?

1.3. Research Motivations

Greenwashing is a common phenomenon in our society. As the pressure on companies to disclose their environmental performance increases, corporations are tempted to use various tricks to please their customers with sustainability values (de Freitas Netto et al., 2020; Gatti et al., 2021). The effects of such a phenomenon are detrimental to the market. The fact that companies make misleading or exaggerated claims about their environmental benefits diverts the flow of capital from the ecological transition towards a model that does not consider sustainability criteria (Deloitte, 2021). According to Parguel et al. (2015), there is a concern coming from some institutional actors, such as the European Community, that greenwashing is not only fooling consumers but also preventing the transition of the economy to a more sustainable model. Indeed, when greenwashing is too prevalent in the market, companies with sustainable goals are discouraged from pursuing their activities. On top of that, sincerely committed stakeholders no longer choose sustainable choices because of the false information given (Parguel et al., 2015). Although companies are greenwashing in the belief to attract their target audience, it has a very bad impact on them when it is discovered. In the long run, it is, thus, also better for them not to deceive the market (Gatti et al., 2021). Therefore, this problem must be addressed by the government through the implementation of regulations and agreements (Terrachoice, 2007).

The green regulations that followed the sustainable agreements to which Europe is committed are numerous but we will only present the most discussed ones. The Taxonomy, the SFDR and the one that we will talk about the most, the expanded MiFID II.

As MiFID II ESG is only released since August 2022, the regulation has not yet been reviewed and is not yet widely discussed in the scientific literature. Fortunately, as the arrival of this amendment will have a considerable impact on the industry, many consulting firms have already written reports. According to Suetens and Nemeth (2022), one thing is sure: this August's new regulation goes further than its predecessor, the SFDR, by focusing on the client and his needs. For this reason, this research is timely and relevant to understanding the difficulties the sector faces in its implementation.

From a managerial perspective, the new regulations that financial actors must implement on a daily basis are a real challenge. In fact, as Suetens and Nemeth assert in discussions with their peers, the concept of sustainability preferences has been poorly understood. They identified five issues that would be problematic in the implementation of the new MiFID. This list of challenges starts with "Lack of uniformity to capture ESG preferences"; "Move beyond the deadline"; "ESG literacy"; "Greenwashing" and finally the "Process of measuring sustainability adequacy" (Suetens & Nemeth, 2022). As the topic is new, the more information managers have about MiFID II ESG, the better they will understand it. In addition, as other regulations fall within the scope of MiFID II, a clear explanation of each element that makes up this new regulation is needed. Therefore, the market's understanding of regulations can help mitigate the risk of greenwashing. According to Zhang et al. (2022), staff training can reduce greenwashing because increased education can help raise awareness of environmental protection. To a lesser extent, it is possible that financial actors may decrease the risk of greenwashing in their company through knowledge.

From an academic perspective, no formal definition of greenwashing has been accepted yet because it can be found in many different forms (de Freitas Netto et al., 2020). As the European Commission takes steps to increase the flow of money to finance the transition to a sustainable economy (European Commission, 2021a), understanding how to limit greenwashing is essential to achieving the goals of the Paris Agreement. Moreover, because these regulations are fairly new, understanding their use is even more important because one of the main goals of all three is to prevent greenwashing by increasing customer protection.

1.4. Contributions

From a managerial point of view, this research aims to provide the financial regulators of each country with a state of the market so that they can report these issues to the European Commission. In addition, as the European Securities and Markets Authority (ESMA) has not yet published all the MifID II ESG guidelines for its implementation, a review of the market perceptions could help them to receive some answers regarding the concerns that have been repeatedly raised (Suetens and Nemeth, 2022). This work could also be useful for advisory firms and financial institutions to understand the MiFID II ESG and how to avoid greenwashing. As the regulation is new and complex, it becomes important to learn how to use it effectively.

From an academic perspective, this work contributes to the existing literature on sustainable finance and follows the path taken by Europe to create MiFID II ESG. Specifically, this research will develop knowledge on greenwashing and the processes and regulations that the EU has put in place to limit this disruptive phenomenon. This will broaden the understanding of new regulations such as the SFDR and the European Taxonomy on which MiFID II ESG is based.
Moreover, as the release date of this regulation was 2nd August 2022, scientific articles on it are scarce. This thesis, therefore, makes predictions about how expanded MiFID II will impact the market. Finally, this study follows Antimiani et al (2016) in showing the risk the European Union could face if other countries fail to follow the green transition.

1.5. Approach

This thesis is divided into six chapters: the introduction that has just been presented, the literature review, the research design, the qualitative survey results, the discussion on the comparison between the literature review and the results obtained in our empirical study and, finally, the conclusion.

The first chapter introduces the context, the motivation, and the contribution of the present work from a managerial and academic perspective.

The second chapter reviews the path of the European Union through sustainable finance. The section begins with the explanation of the greenwashing concept in order to understand what phenomenon is disrupting the market. Then, the main agreements that change the way Europe is taking decisions will be analyzed. Furthermore, the central theme, sustainable finance, will be addressed in order to find out why it has arisen and what effect it has on the economy. Finally, we will go through the regulations that composed MiFID II ESG in order to explain its implementation. A figure will ultimately summarize the literature review in order for the reader to understand the path that the author has taken.

The third chapter presents and explains the methodology used to write this thesis. To collect the data, an interview guide was developed and a list of resource persons was constructed. The four main themes that constitute the interview questions will be addressed in the qualitative investigation. The objective of the study is to understand the impact of the latest European green regulation on the market and on greenwashing.

The fourth chapter presents the results obtained in the interviews in order to understand the individual answers with a broader perspective. The results are discussed further in chapter five to better understand the nuance between papers and what is actually lived by people who are impacted by the law. The questions raised in the first chapter will be answered thanks to the literature review and the qualitative survey. We will underline the advantages, but also the limitations, in order to pave the way to further developments that will make these methods fully satisfactory for the intended purpose, which is to avoid greenwashing to attract investors.

Finally, chapter six reviews the conclusion, the managerial implications, the theoretical implications, the limitations of the present study, and the suggestions for further research.

CHAPTER 2: LITERATURE REVIEW

2.1. Greenwashing

2.1.1. Definition and concept

Over the past decade, our society's concern about climate change has increased. This issue has put intense pressure on companies to disclose information about their environmental performance in their annual report (de Freitas Netto et al.,2020). However, without a clear guideline and the lack of international standards, some of those entities use this new environmental matter to market their goods to reach customers even if their products are not as "green" as they first appear (de Silva Lokuwaduge et al., 2022). This trend, called “greenwashing”, destroys stakeholders' trust in ecological values and tarnishes the image of truly sustainable companies (de Freitas Netto et al.,2020). As a result, this strategy corrupts the green market and makes customers more and more reluctant to buy products to preserve the environment (de Freitas Netto et al.,2020).

Since Jay Westerveld coined for the first time the term "greenwashing" in 1986, it has been used in many different contexts. As a result of its evolution, it is represented by a range of different definitions that capture a spectrum of particular forms of deceptive marketing communication (Lyon and Montgomery, 2015; de Freitas Netto et al.,2020). Yu, Luu, and Chen (p.2, 2020) define companies that greenwash their information as “companies which seem very transparent and publish large quantities of ESG data but perform poorly in ESG aspects.” Environmental, social, and governance (ESG) criteria being specific standards of corporate behavior that allow a socially responsible investor to evaluate potential investments (Investopedia team, 2022a). According to Lyon and Maxwell (2011), greenwash consists in saying only the positive part of a company's information to deceive consumers and investors. For Zhang et al. (2022), the phenomenon of greenwashing is linked to a company's environmental performance. Indeed, a corporation with good environmental performance (EP) tends to reduce greenwashing, while those with poor EP are less willing to disclose their environmental information (Zhang et al., 2022). These different perceptions of greenwashing lead investors to doubt the valid green claims of companies as well as the reliability of any company claiming to be sustainable (de Freitas Netto et al., 2020).

Because of this growing phenomenon, stakeholders find it increasingly difficult to believe in the benefits of spending their money on sustainable products. This problem reduces the financial incentive to invest in green projects and leaves only government regulations as an alternative (Terrachoice, 2007). Therefore, to help stakeholders distinguish one company that practices greenwashing from another, Terrachoice Environmental Marketing Inc. (2007), a company that works in the field of sustainable marketing, decided to conduct a survey to identify key patterns that show when a company is not telling the whole truth about its unsustainable behavior. However, to ensure the accuracy of reported ESG data, this list would not be enough to protect the stakeholders. Thus, regulations on firms' disclosure of ESG data against greenwashing are needed (Yu et al., 2020).

As a result, we can say that greenwashing is a regulatory loophole that has emerged in the market due to the sharp increase in investor demand to implement ESG factors in their investment process and the lack of international standards on ESG-related taxonomy (de Silva Lokuwaduge et al., 2022; Yu et al., 2020).

2.1.2. Types of Greenwashing

In order to tackle this phenomenon that destroys investor confidence, two significant classifications of greenwashing have been emphasized: Claim greenwashing and Executional greenwashing (de Freitas Netto et al.,2020). To help understand why there is no clear definition of this disruptive concept, it is essential to know some significant distinctions to make (de Freitas Netto et al.,2020). Various peer-reviewed articles were evaluated, and specific types of greenwashing were identified.
Moreover, this understanding of the concept may help understand the role that the amendment of the MiFID II law will have on investor trust.

(1) Claim greenwashing

This first classification is the one that has been most studied because it is easier to tackle through government regulation, as it is easier to detect. (Parguel et al., 2015). Indeed, this phenomenon is represented by textual argumentations that refer to a product's or service's ecological benefit to create a misleading environmental claim (de Freitas Netto et al., 2020). Therefore, as those arguments are based on the company's information that can be analyzed, it will be easier for the regulator to limit it. Furthermore, through the textual characteristics, TerraChoice (2007) identifies six types of greenwashing called "sins". These sins result from the fact that the company decides on the rules to adopt in terms of information disclosure (TerraChoice, 2007).

This list helps stakeholders know which green marketing techniques are not to be trusted and thus discourages companies from pretending they are more sustainable than they appear. (de Freitas Netto et al.,2020).

Those six are listed, and will be classified into two categories which are active and passive deception. Indeed, "in the field of communication psychology, deceptive communication can be classified as either active or passive" (Gatti et al., p.3, 2021).

In the **active deception form**, companies deceive their stakeholders by fabricating false information to appear more responsible (Gatti et al., 2021). In this category, we can classify two sins raised by Terrachoice (2007).

1. The sin of no proof:

The lack of certification by a third party is causing this issue. The information released has no right to be there (TerraChoice, 2007).

2. The sin of fibbing

This sin is the least reproduced in greenwashing techniques. It plays on the fact that the company openly lies to its market with false claims (TerraChoice, 2007).

In the **passive deception form**, corporations deceive their stakeholders by failing to disclose compromising information. It involves a strategic selection of information to retain critical information at an advantage, showing only the benefits of a product or procedures used by a company (Gatti et al., 2021). In this category, we can classify four sins raised by Terrachoice (2007).

3. The sin of the hidden trade-off:

This kind of claim is used to make a product greener than it is. The main attributes of a product may be bad for the environment. If one is a little bit better, the company will advertise only on this characteristic to skew the stakeholder (TerraChoice, 2007).

4. The sin of vagueness

A statement cannot be wholly true or false due to its vague nature. The information is not relevant (TerraChoice, 2007).

5. The sin of Irrelevance

When a company makes an environmental statement or action, that may be true even if it is unimportant. As a result, investors who are looking for green products cannot differentiate whether the company is genuinely committed to sustainability or not (TerraChoice, 2007).

6. The sin of Lesser of Two Evils

This greenwashing technique is based on the limited truth of a claim. Indeed, depending on whether the product belongs to a polluting product category, it can be considered sustainable according to this category without actually being sustainable in all product categories (TerraChoice, 2007).

As passive deceptions do not disclose false information but retain the so-called negative information for the environment, they are considered less condemnable than active deceptions (Gatti et al., 2021). This thesis will not go more deeply into the type of claim greenwashing as there are a lot of different kinds on the market, since it is only a means to explain why the UE implements more and more regulations in order to fight this destructive phenomenon.

(2) Executional greenwashing

This second classification is named "executional greenwashing" and is represented by an infinite number of visual elements whose ecological consonance depends on the socio-cultural profile of the target audience. In fact, companies' strategy is not playing with the words but with the design of their ads, using nature-evoking elements, which makes it impossible to create a universal regulation to reduce this type of greenwashing (Parguel et al.,2015). This way of inducing false perceptions of the brand's eco-friendly nature plays on society's naivety in making people think about buying an ecological product even if it does not own any green aspect (de Freitas Netto et al.,2020). However, according to Parguel et al. (2015), that naivety depends on consumers' knowledge about the product's category. Indeed, stakeholders known as "experts" in a specific field are "less likely to rely on and be influenced by the use of advertising executional elements representing nature" (Parguel et al., p.10, 2015). While consumers who are "not experts" would be influenced by "executional greenwashing" and therefore perceive the brand as more responsible if it adds green elements in its advertising (Parguel et al.,2015).

The analysis of these two significant classifications of greenwashing allows us to state that the more stakeholders are informed on the subject, the less impact greenwashing has. It is, therefore, necessary, on the one hand, to educate citizens to recognize forms of greenwashing and, on the other hand, for the government to create laws so that even the ill-informed consumer is protected (de Freitas Netto et al.,2020; TerraChoice, 2007; Parguel et al.,2015).

The following examples will show the internal difficulties of the system, the ineffectiveness of policies, and the steps authorities are taking to eliminate the claims of bogus ESG funds.

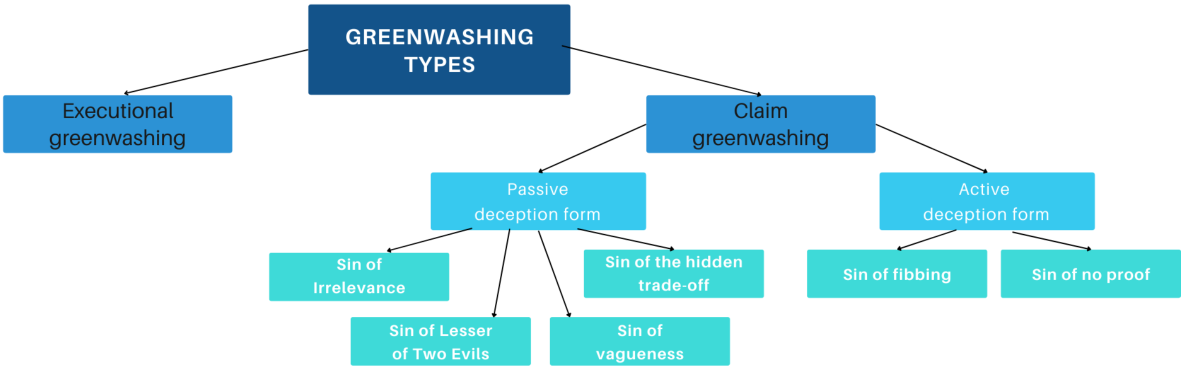


Figure 1: Greenwashing Types

Source: Own work

2.1.3. Examples of greenwashing

Sin of the hidden trade-off

An example of greenwashing at the corporate bank level is the fraudulent claims on DWS[1]' investment products that have been sold as environmentally friendly, whether it was not wholly the case. Indeed, this example shows the technique of "overselling," which consists in highlighting the ecological characteristics of a product to make it greener than it is.

In this recent case, Deutsche Bank's subsidiary is accused of selling funds promoted in prospectuses as “sustainable funds” when “ESG criteria have not been considered in many investments” (Chocron, 2022). As the opacity of the financial sector is a matter that the authorities have not yet managed to resolve, the European Union is working on a legal definition of "greenwashing" to address this marketing tactic better and is attempting to create new regulations to eliminate this lack of transparency (La Libre, 2022).

Knowing that German prosecutors only detected this fraud thanks to a whistleblower, former DWS sustainability manager Desiree Fixler, the U.S. securities regulator SEC has launched an initiative where it said that “it becomes urgent to strengthen the transparency obligations of financial advisors and asset managers concerning investments according to sustainable criteria” (LaLibre, 2022).

Sin of Irrelevance

Corporations that show which green actions they have made, whereas the core of their business is not ecological, are also turning the brand image in the mind of stakeholders in a way to take advantage of their values (Terrachoice, 2007).

As an example of an organization that greenwashes its activity, BNP Paribas is guilty. In fact, one of its numerous ads advertised an exposition on the climate and biodiversity to show that it is committed to the fight against global warming while it is one of the largest investors in fossil fuel financing in Europe (Bon Pote, 2022). Furthermore, five years after the Paris Agreement, 39 billion dollars will be invested in oil and gas in 2020 (Bon Pote, 2022).
Once again, because BNP has a poor EP and the society has evolved to a more valuable market with higher standards, the company is greenwashing its brand image (Zhang et al., 2022). The issue with this is that if the public's environmental awareness is weak, customers will be deceived by the

[1] The DWS Group (Formerly: Deutsche Asset Management) commonly referred to as DWS, is a German asset management company

company. This means that the customers' protection is put at risk and that regulators should take the initiative to protect and punish those behaviors (Terrachoice, 2007).

Following this section, the financial sector framework analysis will be reviewed through the evolution of the different EU regulations.

2.1.4. Greenwashing in the Financial sector

Greenwashing techniques badly impact the financial sector. Indeed, while previous studies have focused primarily on consumers' views on greenwashing, investors are also concerned about climate risk and are beginning to consider it in their investment decisions (Gatti et al.,2021).

Moreover, with growing concerns about climate change, stakeholders' preferences are more and more based on the environmental behaviors of companies. Recognizing this growing demand, environmental activists and the media are increasingly paying attention to how companies respond to this new investor demand, forcing them to be as authentic as possible in their annual self-reporting (de Freitas Netto et al.,2020, Gatti et al.,2021). The pressure to be more sustainable makes companies tend to exaggerate their numbers and greenwash their activities to appeal to potential investors. However, knowing the impact on investors' trust because of greenwashing, the government has to implement international standards to prevent greenwashing (de Silva Lokuwaduge et al., 2022).

According to Gatti et al. (2021), stakeholders' investment is more negatively affected by a company that greenwashes its activities than a company that does not take care of the environment and does not mislead ESG communication. Indeed, being transparent about its activities, even if they are not eco-responsible, gives investors more confidence in the company that is being honest (Gatti et al.,2021). However, Gregory (2021) suggests that there are many other ways in which greenwashing can occur at the corporate level. In fact, greenwashing can find its way into companies in a number of ways. On the one hand, through advertisements aimed at diverting attention from sustainability issues or through non-financial reports claiming to be sustainable without this actually being the case in order to project a positive image of the company. (Gregory, 2021; de Silva Lokuwaduge et Silva, 2022). On the other hand, companies with greater power greenwash their activities by creating subsidiaries that produce sustainable products when they themselves are not green. Or, they also greenwash with the “agreement” of the authorities by influencing regulations or governments through their lobbies in order to gain advantages in the areas of sustainability. Finally, these big corporations can use their power by claiming sustainability achievements that are required by laws and regulations when their entire business is not sustainable (Gregory, 2021; de Silva Lokuwaduge et Silva, 2022).

In an effort to make companies more sustainable and transparent in their reporting, the EU has had to implement a series of regulations in the financial market. Indeed, the EU's implementation of the SFDR and the European taxonomy provide regulatory guidance for the integration of sustainability by all investment intermediaries, both in terms of sustainability and investment performance. As a result, they will have the impact of limiting greenwashing (Chiu, 2022).

Business transparency is, therefore, a solution to prevent greenwashing from corporations (Chiu, 2022).

Following this section, we will now look at the evolution of these different regulations and define how the new MiFID II 2021/1253 will be able to deal with the opacity of the financial market, but also in what way it will help the market to counteract greenwashing.

2.2. The emergence of sustainable finance

The timeline traces the different events that led the European Union to the creation of strict regulations. These events will be explained in this chapter and will show the steps that Europe has taken to make the transition to a more sustainable economy.

Figure 2: Timeline of the agreements on ecological transition

Source: Own work

2.2.1. Paris Climate Agreements

In 2015, years after the Kyoto Protocol, two international agreements were adopted, the UN 2030 Agenda for Sustainable Development with its 17 sustainable development goals (SDG) and the Paris Climate Agreement (PCA). These agendas signaled the beginning of the emergence of sustainable finance that will lead to the transition to a low-carbon world and a climate-resilient sustainable development path (European Commission, 2021). The relationship between these two pacts is significant and must be taken into account to achieve the ultimate goal. Indeed, the implementation of the PCA followed the UN's agenda with its SDG #13, "Climate Action" which aims to take urgent action to fight climate change and its impacts. Moreover, the second agreement will help the United Nations to achieve its goal of limiting global temperature increase to 1.5 degrees Celsius by 2030 (Iacobuţă et al., 2022; Sachs et Sachs, 2021). Therefore, it is easy to see that these two agendas must be considered together when making any decision about either one. Indeed, they will not be as effective as they should be if treated separately (Iacobuţă et al., 2022).

The Paris climate agreement had set some rules that 196 states committed to follow and implement over a five-year cycle to limit global temperature to 1.5 degrees. (UNFCCC, n.d.). Each country enrolled in this program must submit a Nationally Determined Contribution to outline which actions they will take for the next five years (UNFCCC, n.d.). These efforts will need to mobilize enough money to meet the needs of developing countries in reducing greenhouse gas (GHG) emissions from developed countries and increasing their resilience to climate change GHG emissions from developed countries (UNFCCC, n.d.).

This pivotal moment in the financial sector will alter how future legislation will be established and the management of the entire economy (Sachs et Sachs, 2021). In fact, according to the UN, the Paris Agreement provides a durable framework guiding the global effort for decades to come and marks the beginning of a shift toward a net-zero emissions world (European Commission, 2021). These agreements favor our environment but will also create limits for companies that will change how they have always worked. The emission limitation and the ever-increasing transparency requirements might push some companies to adopt wrong behavior, and therefore, more regulations will emerge (de Silva Lokuwaduge et al., 2022).

With the SDGs and Paris Climate Agreement in 2015, aligning corporations with scenarios limiting global warming to 1.5-2 degrees Celsius has been granted considerable attention from companies and their debt and equity investors (Sachs et Sachs, 2021). According to EIT Climate-KIC[2] (2022), investor financial support for corporations is responsible for most of the world's carbon-emitting activities. The explanation of companies' liability is shown in Figure 1. Therefore, the integration of climate risk by the financial sector is no longer a character to be ignored (EIT Climate-KIC, 2022).

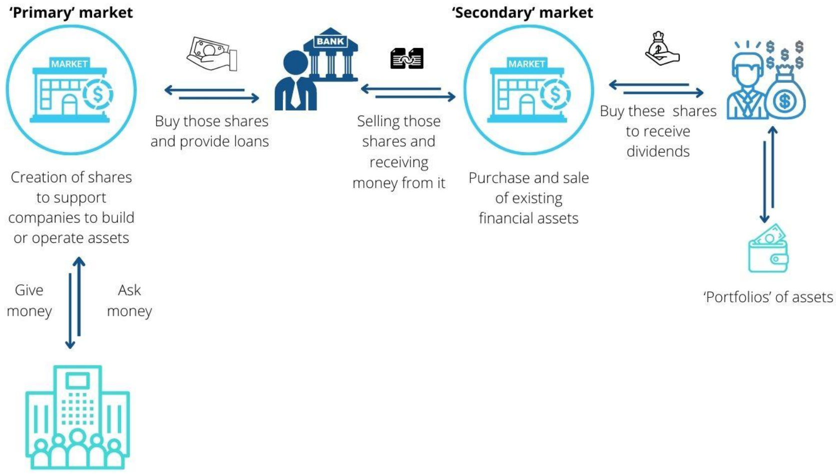


Figure 3: Illustration of investment responsibility chains

Source: own work
Data source: EIT Climate-KIC, 2022

For a company to receive money to finance its operations, it must ask the bank for money. The bank relies on the support of investors in the secondary[3] market when it makes loans in the primary[4] market to help businesses.
So, if investors are no longer willing to finance polluting companies, banks will have no money to lend to companies with a high environmental footprint. As a result, it will push companies to become more sustainable. The power is, therefore, in the hands of the investors (EIT Climate-KIC, 2022).

With this agreement, a concept of asset management has emerged to force companies to become more sustainable. This concept is based on measuring the alignment of an investment portfolio with the Paris agreement (Beacco, 2020). Furthermore, this measure is based on the compatibility of a financial asset with a temperature trajectory (Beacco, 2020). However, aligning one's company with the Paris Agreement is not an easy task, as the concept of investment alignment remains ill-defined (UNFCCC, 2019a). Indeed, several scenarios are in place for a company to claim compliance with the EU targets, but all potential scenarios depend on the decisions made by the company at a specific time (Beacco, 2020). In this context, the scenario we point to is the one named RCP 2.6 presented in Figure

[2] EIT Climate-KIC is a Knowledge and Innovation Community (KIC), working to accelerate the transition to a zero-carbon, climate-resilient society and that is supported by the European Institute of Innovation and Technology

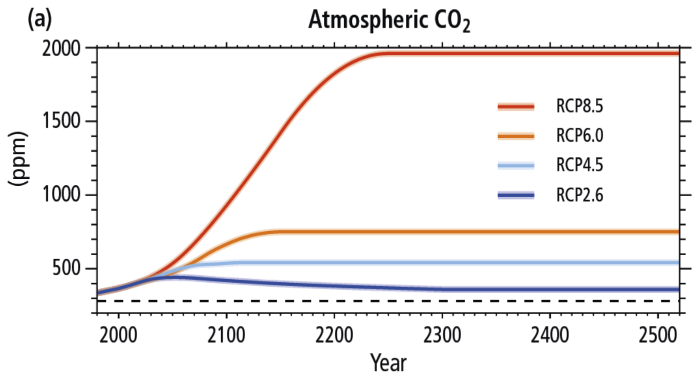
[3] The secondary market is where investors buy and sell securities that already exist and can no longer be found in the primary market (Investopedia team, 2022c).

[4] The primary market is the market where securities are first created to be sold to professional investors such as banks and financial institutions. It allows companies, governments and other organizations to raise capital (Investopedia team, 2022b).

2 which is the one that will limit global warming to 1.5-2 degrees Celsius according to the IPCC[5]. As stated by Beacco (2020), this scenario will be represented in "a top-down form that would say that a portfolio is aligned if, regardless of the emitting companies, the portfolio achieves a percentage of emissions below the determined temperature trajectory."

It is, thus, not easy to certify that a company, and its investments, are in line with the EU targets (UNFCCC, 2019a). In addition, investors do not fully understand how a portfolio should be aligned across different asset classes and sectors (UNFCCC, 2019a), making alignment difficult to enforce. Which is why, this thesis will try to explain why the European Union needed to create clear regulations such as the European Taxonomy, SFDR and MiFID.

In addition to this physical support, the need for a change of mentality is more than necessary. Indeed, "investors and banks continue to prioritize profit over responsibility and see responsible investing as a way to mitigate financial risk and increase long-term profits, rather than a way to mitigate the impact on people and the planet" (Sachs and Sachs, p4, 2021). Therefore, the gap in this agenda needs to be further regulated to be adequately supported.



Graph 1: IPCC scenarios

Source: IPCC; AR5 Synthesis Report: Climate Change 2014

2.2.2. Action Plan on financing sustainable growth

After the 2015 Paris Climate Agreement that signed the beginning of the transition of our economy, the European Commission adopted the action plan on sustainable finance in order to connect finance with sustainability (European Commission, 2018b; High-Level Expert Group on Sustainable Finance, 2018).

This Action Plan, launched in March 2018, was created based on the recommendations of the High-Level Expert Group (HLEG) on Sustainable Finance and encompasses ten key actions that can be divided into three groups (European Commission, 2018a). In terms of the HLEG report, the most important recommendation is to improve green finance for sustainable and inclusive growth by integrating ESG factors into investment decisions in order to meet sustainability needs from a financial advisory perspective. This improvement in the system would ultimately reduce uncertainty in terms of the economy's transition to more environmentally friendly growth (Allen Overy, 2021; PRI, 2018).

[5] Intergovernmental Panel on Climate Change (IPCC) is the United Nations body for assessing the science related to climate change.

Those three groups are composed as follow (European Commission, 2018a) and are represented in figure 3:

- **A. Reorienting capital flows towards a more sustainable economy**
  1. Establishing a clear and detailed EU Taxonomy, a classification system for sustainable activities.
  2. Creating an EU Green Bond Standard and labels for green financial products
  3. Fostering investment in sustainable projects
  4. Incorporating sustainability in financial advice
  5. Developing sustainability benchmarks
- **B. Mainstreaming sustainability into risk management**
  6. Better integrating sustainability in ratings and market research
  7. Clarifying asset managers' and institutional investors' duties regarding sustainability
  8. Introducing a 'green supporting factor' in the EU prudential rules for banks and insurance companies
- **C. Fostering transparency and long-termism**
  9. Strengthening sustainability disclosure and accounting rule-making
  10. Fostering sustainable corporate governance and attenuating short-termism in capital markets

This list is represented by figure 3 and will help to understand how the European Commission set up the new MiFID II 2021/1253 and the steps it has to take to create it.

The HLEG report on which the action plan is based states that sustainable finance is about two urgent imperatives. The first is to improve sustainable finance to meet society's long-term needs and achieve sustainable growth. The second is the strengthening of financial stability through the integration of ESG criteria in investment decisions (European Commission, 2018b). As we will see in the explanation of the new MiFID II, the integration of the ESG preferences on the investment is one of the pillars of the amendment. Therefore, the implementation of ESG-related MiFID is further proof that the EU is following a common thread in order to achieve its ultimate goal of a carbon neutral economy.

The diagram hereunder is the representation of the action plan that the European Commission is trying to implement in order to achieve 3 objectives. This is to ensure that the transition to a more sustainable economy takes place through the reorientation of capital flows (European Commission, 2018a).

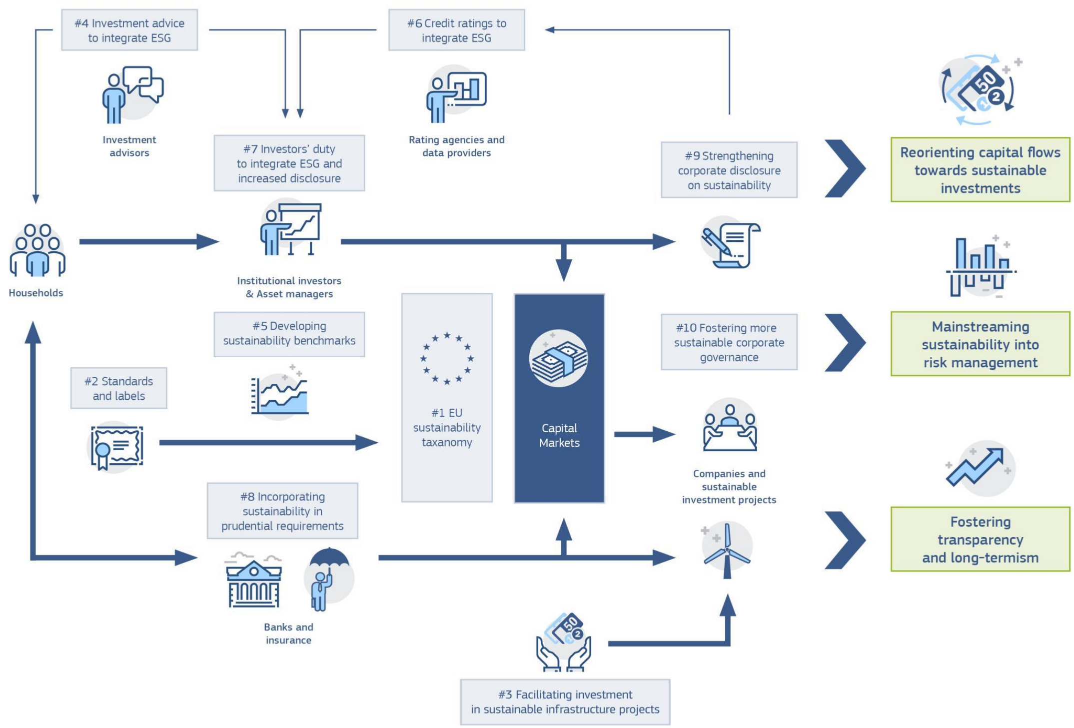


Figure 4: Action Plan Framework

Source: European Commission, 2018b

2.2.3. European Green Deal

As a follow-up to the 2015 Paris Agreement, the EC convened a High-Level Expert Group on Sustainable Finance (HLEG) in December 2016 that raised a series of steps to be implemented. In this list of steps that we have analyzed above, the most important one that has been raised is the creation of a European regulation that would list the so-called sustainable activities and that will be called the "European Taxonomy". This EU initiative marked the beginning of the work undertaken by the EC in the area of sustainable finance (Bruyninckx et al., 2021; Jäger,2022) and will be explained later. It is these various reflections and actions on the part of the EC that led them to the European Green Deal (Eckert and Kovalevska,2021).

The European Green Deal (EGD) has been launched in December 2019 by the European Commission (EC), bringing a series of new rules in order to achieve the objectives for 2030 and 2050. This strategy developed for the EU serves as

> "a roadmap for making the EU's economy sustainable by turning climate and environmental challenges into opportunities across all policy areas and making the transition just and inclusive for all." (European Commission, 2019)

Indeed, following Covid-19 and the Russian-Ukrainian conflict, Europe needs to change the way it operates more than ever. Furthermore, this proposal comes at the right time to overcome this change and move towards a more sustainable and viable economy (European Commission, n.d.a; Delbeke, 2022).

Consequently, the EU Commission's Green Deal proposal is a central strategy for achieving the UN Sustainable Development Goals and carbon neutrality by 2050 (Schunz,2022; Jäger,2022; Bruyninckx et al., 2021).

For the European Union to reach its carbon reduction targets, cooperation between the 27 Member States is necessary (Bruyninckx et al., 2021). That is why the EGD provides general guidance for EU legislation and regional development strategies (Eckert et Kovalevska, 2021). However, the EU needs more than a clear guideline. Indeed, according to Bruyninckx et al. (2021), public and private funds must be directed toward climate and environmental action to finance the green transition as planned. Therefore, strict regulations must be implemented.

Although the public sector has to show the right example to society, the private financial sector is, in the eyes of the EC, the essential element that will contribute to the green transition (Jäger, 2022). For this reason, specific actions need to be taken to stimulate sustainable private finance, such as the four pillars on which sustainable finance is built and especially the amendment of MiFID II 2021/1253, which will be discussed later.

2.3. Sustainable Finance

2.3.1. Concept and definition

In the rush to achieve global SDGs, sustainable finance has started to become popular in both the public and private sectors to channel available assets into more sustainable investments (Cunha et al., 2021). Indeed, according to 2015 United Nations figures, between $5 and $7 trillion per year in public and private investment is needed to achieve the Paris Sustainable Development Goals (Cunha et al., 2021).

Therefore, the EU Commission (n.d.c.) refers to sustainable finance as a "process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects."

However, for Kumar et al. (2022), sustainable finance means more than what the EU stated, limiting sustainable finance to the ESG integration. Indeed, his paper says that this type of finance has a wide range of definitions as it has emerged through the union of finance and the SDGs (Kumar et al., 2022). Thus, Kumar et al. stated that "sustainable finance should encompass all activities and factors that would make finance sustainable and contribute to sustainability" (2022, p.2). With this definition, the integration of the plethora of objectives from different stakeholders, such as "climate finance, carbon and ESG disclosure, green bonds, and socially responsible investing" (p2., 2022) are also part of this broad theme of sustainable finance.

For Swiss Sustainable Finance, the definition of sustainable finance is less oriented towards the view of sustainability but more towards the point of view of the benefits stakeholders can get from it. Indeed, they define it as *"any form of financial service integrating environmental, social and governance (ESG) criteria into the business or investment decisions for the benefit of both clients and society at large"* (in IISD, p4., 2020).

Therefore, sustainable finance can be defined in different ways, but the ultimate goal remains the same. It can support economic growth while reducing pressure on the environment and integrating social and governmental aspects (European Commission, n.d.c).

2.3.2. Company and Investor Relations

A perspective that is important to understand in order to know the implications of the MiFID II 2021/1253 on companies is how investors invest in companies and for what reasons.

Prior to the rise of sustainable finance, the relationship between the investor and his stock portfolio was primarily focused on the profitability that the investment could bring (Liang & Renneboog, 2021). However, since ESG criteria have been taken into account, investors are increasingly paying attention to the non-financial aspects of the companies they decide to invest in (Kim and Li, 2021). As a result, environmental and social aspects are now essential for companies to consider if they want to ensure a sustainable relationship with investors (Liang & Renneboog, 2021).

Traditionally, the Markets in Financial Instruments Directive (MiFID) was intended to make the European Union (EU) financial markets more robust and transparent (Publications Office of the European Union, 2014). It was, therefore, a regulation that provided a new legal framework that better-regulated investment and trading activities in financial markets to enhance investor protection (Publications Office of the European Union, 2014). However, with this growing trend of incorporating ESG criteria into the stock market, banks have to consider non-financial aspects of companies, such as how the company operates about sustainability challenges (Battiston et al., 2021). Companies must prove that sustainability criteria are part of their values and are doing everything possible to meet the market's requirements. For this reason, the need to rank a company's sustainable and unsustainable activities is more than necessary. Through this classification, a company that is transparent about its percentage of unsustainable activity will be able to show its evolution. As a result, it will reward companies that try to integrate more and more ESG criteria in their operational management (Battiston et al., 2021).

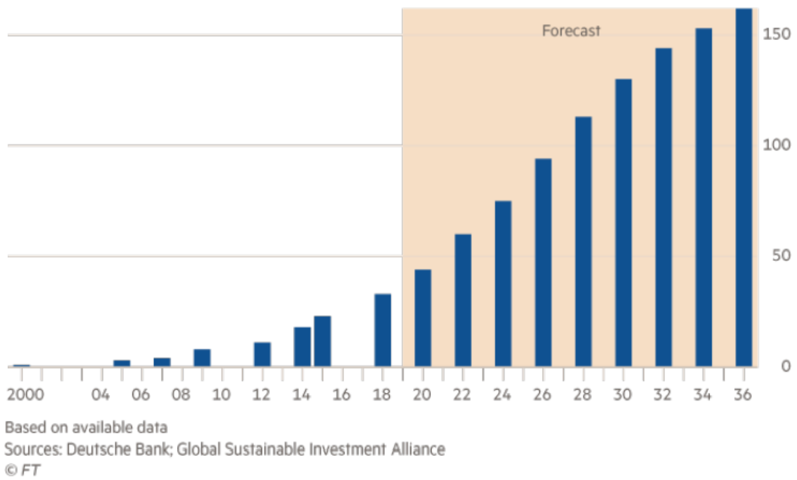
Moreover, companies with good ESG performance are more coveted by investors because they believe that companies with sustainable values are better positioned for the long term, better prepared for uncertainty and, therefore, less risky (Bell, 2021). Corporations have no choice but to set an agenda for climate-resilient growth to ensure long-lasting investor relationships (Bell, 2021).

However, due to the lack of international standards on ESG-related taxonomy, greenwashing continues to grow while stakeholders' confidence declines even if companies want to become greener (De Silva Lokuwaduge et Silva, 2022). In this case, Freitas Netto et al. (2020) suggest that because of the different definitions of greenwashing, a trust issue has arisen as stakeholders have struggled to identify a valid green claim.

2.3.3. Growing demand for sustainable Investments

Sustainable finance is a crucial element of the transition to a low-carbon economy. According to Liang and Renneboog (2021), Europe is the continent where the rise of ESG investing has been strongest, followed by the US which has also seen strong growth in sustainable assets over the years. Moreover, according to them, investors would be willing to give up good financial performance if they were offered more sustainable investments in line with their ESG preference (Liang & Renneboog, 2021).

With the rise of ESG preferences, the number of companies that are increasing their sustainable and socially responsible activities continues to grow in order to be perceived as socially responsible (Liang & Renneboog, 2021). Indeed, an increase in global assets with an ESG mandate can be seen in Figure 1. The graph from Deutsche Bank shows us that assets with an ESG mandate will grow by a little over $100 billion by 2036 as indicated in the forecasts. According to IISD's report, this would mean nearly 100% ESG integration in fund management (ISDD, 2020).



Graph 2: Global assets with an ESG mandate (USD trillion)

Source: Fletcher, 2019 (in IISD, 2020)

Therefore, sustainability investing is increasingly present in investment portfolios, but a lack of specific standards could negatively impact the market in the long run (ISDD, 2020).

Moreover, financial products that claim to be sustainable without any certification may not have the desired result, as the classification of so-called sustainable products has not been made according to pre-established criteria and therefore cannot guarantee that the portfolio generates any positive results (ISDD, 2020). Thus, MiFID II 2021/1253 will have an important role to play in increasing the match between what the client wants and what the asset manager can give him while having the guarantee of transparency in the reporting thanks to SFDR.

With MiFID additional features, such as the consideration of sustainability preferences, the amended regulation will provide a framework to follow in order to obtain an accurate classification of one's stock portfolio, knowing the real impact of every product, given the stock categories that will have been selected according to the client's preferences (ESMA, 2022a).

2.3.4 Lack of Regulation in Sustainable Financial Sector

The SDGs, the PCA, and the European Green Deal are the three principles of European agendas that exist to make a transition to a low carbon economy. Those agendas have common interests and need money in order to be achieved. That is why the European sustainable finance sector is that important nowadays. Together, they aim to create a resilient economy for the future generation to give them the right place to live. (European Commission, 2019; European Commission, 2018b; European Commission, 2021).

However, according to de Freitas Netto et al. (2020), the growing demand for sustainable development in the market drives firms to greenwash their activities in order to highlight their good Corporate Social Responsibility (CSR) to consumers, and this issue slows down the process of raising enough capital to achieve sustainability goals. CSR being a principle that enables a company to adapt to the new expectations of society, such as taking into account climate risk and regulatory issues. (Homer et Gill,2022).

For consumers to regain confidence in investment firms and businesses and, thus, find the funds to achieve their goals, regulations must empower investors to choose where and how they place their money (De Silva Lokuwaduge et Silva, 2022) by allowing them to understand why this type of investment is being made according to their sustainability preferences. With the help of MiFID II 2021/1253, this problem can be solved to make the financial sector more sustainable and resistant to change.

2.4. The four European regulations pillar of the sustainable transition

2.4.1. SFDR

Following numerous European actions for the ecological transition, the Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector also known as the Sustainable Finance Disclosure Regulation (SFDR), was adopted on November 27, 2019, by the European Parliament and the Council of the European Union (Regulation (EU) 2019/2088).
This new regulation has been divided into two levels. The first level has been applied since March 2021 and requires financial market participants to disclose the performance of financial products on ESG aspects (IDS, 2021). While the second level of the SFDR will be applicable in January 2023 and will concern the implementation of the product declaration requirements according to Art. 8/9 SFDR (IDS, 2021). This means that it provides the necessary information for the proper implementation of the SFDR. It will, thus, explain the methodology to be used as well as the content required to ensure that the presentation of the disclosed information according to several articles of the SFDR is correct (Arendt.com, 2022).

The main objective of this new regulation is, as its name indicates, the disclosure of information to be as transparent as possible. Thanks to this new rule, it will be possible to collect detailed information on the impacts of investments on ESG criteria, which will ultimately contribute to improving investor protection and thus, increase the demand of ESG products (Becker et al., 2022). Indeed, according to Beckers et al (2022), in the absence of strict rules, issuers disclose what they want, misleading stakeholders, and so the SFDR incentivizes funds to invest more sustainably through its reporting system. This is why the SFDR regulation will reduce the risk of greenwashing and promote the ecological transition of the financial system (European Commission, n.d.b).

The regulation 2019/2088 specifies in which form to disclose information on financial products in order to increase the transparency of information related to sustainability and to know their performance in relation to it. Moreover, it was enacted to be able to compare these different financial products on the final market (Join Committee, 2021; European Commission, n.d.b). The Sustainable Finance Disclosure Regulation is one of the building blocks of the first action plan on financing sustainable growth that has been issued in March 2018. Indeed, SFDR specifically addresses the integration of sustainability factors into the investment chain and is used to strengthen investor protection against greenwashing (Eurosif, 2022).

As explained before, in order to achieve the ambitious goals that the European Union set for itself in the Paris agreements and the European Green Deal, Europe needs an important legal instrument such as the SFDR (Triodos, 2022). Indeed, as public investments are not substantial enough, the need for private capital is more than necessary. This explains why the SFDR requires financial actors to communicate more transparently on the sustainability of the investment funds they propose (Triodos, 2022).

The transparency criterion imposed by the SFDR leads to a highly specific form of reporting depending on ESG-related products, non-ESG products and their degree of ESG integration (Becker et al., 2022). Although Articles 6, 8 and 9 are referred to as a way of classifying products, it is not a labeling regime (Arendt.com, 2022). A company wishing to promote its sustainability values will have to comply with enhanced transparency rules depending on how it wishes to have its financial products classified (Arendt.com, 2022). Therefore, with this new regulation 2019/2088, a fund can be disclosed depending on 3 different categories which are known as article 6, 8 and 9 (Triodos, 2022).
The first SFDR category is classified under article 6 of the SFDR and is also called "classic" funds category because they do not include any ESG characteristics into the investment decision-making process (Triodos, 2022; Becker et al., 2022). Then, the second category of funds, which is classified under article

8 of the SFDR, includes products that consider ESG characteristics and which invest in sustainable investments (J.P Morgan, 2021). Finally, we have the third and last category of the SFDR, which classifies funds under article 9 of the SFDR and whose main objective is sustainable investment (J.P Morgan, 2021; Regulation (EU) 2019/2088). A "sustainable investment" according to article 2 of the SFDR is defined as "an investment in an economic activity that contributes to an environmental objective, (...), or to a social objective, (...), provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance" (Regulation (EU) 2020/2088).
In summary, the products classified according to article 6 of SFDR are funds that hardly integrate sustainability in their investment process, whereas articles 8 and 9 both consider ESG criteria even if the degree of integration of these criteria differs (Becker et al., 2022). As we will see later on (in 2.4.3. MIFID II 2021/1253), only articles 8 and 9 will be taken into account in category B of MiFID as article 6 does not include sustainability. The European Union is therefore taking a step towards preventing investors from being greenwashed with this new policy approach. The granularity[6] of the pre-contractual information meets the objective of combating greenwashing and the legal documentation will make the suitability of products for investors even more precise (JC, 2021).

However, recognizing that there is always a gap between theory and practice, according to the Eurosif report (2022), some Article 8 and 9 compliant products still have relatively high exposure to non-sustainable activities. Indeed, under the sustainable investment objective requirement and the DNSH (Do Not Significantly Harm) requirement that came from the EU Taxonomy, some claims for Article 9 funds would be inconsistent with reasonable consumer expectations and could give rise to claims of greenwashing (Eurosif, 2022). The DNSH principle considers an activity as not harmful to the environment only if the activity does not harm one of the six objectives of the Taxonomy (European commission, 2021d).

Despite some inconsistency in the regulation, SFDR requires disclosure on principal adverse impacts on sustainability factors (PAI) regarding investment decisions made by a fund manager on sustainability factors. Moreover, an enhanced disclosure in pre-contractual documentation and on websites is necessary for a fund to be classified as Article 8 or Article 9 (Kirkland & Ellis, 2021). The PAI means in other words that financial instruments take into account and reduce the significant negative externalities caused by these investments (European Commission, 2021c). This indicator developed in the SFDR will have an impact on the classification of products in the MiFID II ESG regulation and will therefore be discussed further in section 2.4.3.

Therefore, we can see that the European Union is following a guideline by moving from one step to the other. SFDR focusing on how companies will have to disclose information in order not to deceive investors (Becker et al., 2022).

[6] Granularity means the quality of including a lot of small details

2.4.2. European Taxonomy

The European Taxonomy regulation emerged shortly after the Regulation 2019/2088 and the "Action Plan on financing sustainable growth" based on the 2018 HLEG report. Its purpose is the same as the SFDR which is to finance the transition and reach the objectives of the Paris Climate Agreement and the European Green Deal (European Commission, 2020a) but is stricter than its predecessor. Indeed, the regulation is used as a classification system for economic activities to determine which activities are considered environmentally sustainable (European Commission, n.d.a). As a result, companies will have to meet a list of criteria in order to be considered environmentally sustainable and, thus, the Taxonomy provides security and protection to investors from greenwashing while helping companies to become more climate friendly (European Commission, n.d.a).

Moreover, according to the OECD[7], to meet the goals of the Paris Agreement, we need €6.35 trillion each year until 2030, so private capital will be needed to help the public sector meet this challenge (European Commission, 2020a). Therefore, in the Official Journal of the European Union (L198/13), the European Parliament and the Council of the European Union have adopted the "Regulation (EU) 2020/852 of June 18, 2020, on the establishment of a framework to facilitate sustainable investment", commonly named the "EU Taxonomy Regulation" which has also amended the Regulation (EU) 2019/2088, known as the SFDR.

> *"The adoption of the Taxonomy Regulation marks a milestone in our green agenda. It creates the world's first ever classification system of environmentally sustainable economic activities, which will give a real boost to sustainable investments. It also formally establishes the Platform on Sustainable Finance. This Platform will play a crucial role in the development of the EU Taxonomy and our sustainable finance strategy over the coming years."* said Valdis

Dombrovskis, Executive Vice-President responsible for Financial Stability, Financial Services, and Capital Markets Union in the EU (European Commission, 2020b). The Taxonomy will, therefore, allow investors to redirect their investments towards more sustainable technologies and companies, and thus, enable the EU to become climate neutral by 2050 (European Commission, 2020b).

For the purposes of this Regulation, it has defined in its article 2 twenty-three definitions. In order to understand the main concept of the Taxonomy, this thesis will define only the first concept which is the 'environmentally sustainable investment'. As stated in the regulation, an investment is considered as sustainable only if it is included "in one or several economic activities that qualify as environmentally sustainable under this Regulation" (Regulation (EU) 2020/852). Furthermore, in order for the reader to understand the whole definition, the regulation 2020/852 defines an economic activity as environmentally sustainable when it "contributes substantially to one or more of the environmental objectives" mentioned below. But also, when it "does not significantly harm any of the environmental objectives", "is carried out in compliance with the minimum safeguards" and "complies with technical screening criteria that have been established by the Commission (...)"

We can find in the "Final Report of the Technical Expert Group on Sustainable Finance", that the Taxonomy establishes six environmental objectives, which are:

1. Climate change mitigation
2. Climate change adaptation
3. The sustainable use and protection of water and marine resources
4. The transition to a circular economy
5. Pollution prevention and control
6. The protection and restoration of biodiversity and ecosystems

[7] Organisation for Economic Co-operation and Development

So far, this Taxonomy covers 2 out of 6 environmental objectives that have been cited above, but it does not end there. In fact, a social Taxonomy is also expected soon and its implementation represents a major challenge for the EU as its complexity is high (Neuroprofiler, 2022).

Under the EU Taxonomy Regulation (2020/852), these six targets will be further examined through the climate change mitigation criteria (European Commission, n.d.a). Indeed, according to Article 2 (Regulation (EU) 2020/852), "climate change mitigation" is defined "as the process of holding the increase in the global average temperature to well below 2 degrees Celsius and pursuing efforts to limit it to 1,5 °C above pre-industrial levels, as laid down in the Paris Agreement." which is the number one goal for the European Union.

As explained in Section 2.2.1., portfolio alignment with the Paris Agreement has made investors highly attentive to the impact of their investments in order to be in line with the goals set by the EU (Sachs and Sachs, 2021). Continuing in this direction, alignment with the Taxonomy is very similar.
Indeed, to be aligned with the EU Taxonomy, an activity must make a substantial contribution to one or more of these environmental objectives in one of the following ways; the economic activity must contribute on the basis of its performance or through the provision of its products or services, and it must make a substantial contribution in other activities (European Commission, 2020a). Thus, this alignment is well understood in the financial sector as it defines clearly which sectors are included in the classification of the EU Taxonomy whereas to be aligned with the PCA, the different asset classes and sectors are not fully defined (UNFCCC, 2019a).

Therefore, we can see that the Taxonomy is seen as a way to classify the activities because it is a dictionary of economic activities that determine which activities are considered environmentally sustainable by the EU (European Commission, n.d.a). The European Taxonomy focusing on which activities can be seen as sustainable, it is the second step toward the investor protection (European Commission, n.d.a).

2.4.3. MiFID II 2021/1253

Background

The MiFID regulation, also known as the Markets in Financial Instruments Directive, was introduced in 2007 following the financial crisis. The initial aim of this regulation was to create more competitiveness in the market and harmonize the European financial landscape (European Commission, 2016; European Commission, 2021b). Indeed, this European directive was launched to protect European investors who were increasingly afraid to invest their money (European Commission, 2016).

Then, in January 2018, the amended regulation called MiFID II, offered more transparency through new rules adopted by the European Commission to revise the MiFID framework (European Commission, 2021b). However, some of the principles of MiFID II were insufficient to counteract the problems encountered in the market such as climate risk. As a result, the EC has had to revise it several times in recent years to ensure that it adequately meets market expectations (European Commission, 2016).

MiFID II was, therefore, additional insurance for investors. Indeed, compared to MiFID I, MiFID II has increased the level of information that companies must provide (European Commission, 2016). For example, concerning disclosures, firms will have to provide more fair, transparent, and not misleading information that has been extended to transactions with eligible counterparties (ESMA, 2022b). The EC introduced this additional characteristic in MiFID II to "address concerns that non-professional clients were not always able to understand the risks of investments" (ESMA, 2022b). Consequently, the regulation introduces new disclosure requirements for cross-selling practices and investment advice (ESMA, 2022b).

Integration of sustainability preferences into MiFID II

Following the separate agreements and regulations related to climate change that the EU has put in place, such as the Paris Agreement, the 2018 Action Plan, and also the European Green Plan, the MiFID II Delegated Regulation has been further updated to integrate sustainability factors, risks as well as preferences into specific organizational requirements and operating conditions of investment firms which has led to the Regulation 2021/1253, also known as MiFID II sustainability requirements (ESMA, 2022a ; Regulation (EU) 2021/1253).

According to ESMA, implementing strong guidance on MiFID will reinforce its crucial objective of investor protection. The European Commission's integration of the sustainability theme follows the basic guidelines of the MiFID regulation (ESMA, 2022a). Consistent purposes have been, therefore, set to ensure that the integration of ESG risks will still meet the fundamental objectives of MiFID II after integrating sustainability factors into the regulation (ESMA, 2022a).

Europe, also known as the "old continent", must set an example to other regions of the world in terms of climate commitments (Bruyninckx et al., 2021). In fact, it has always played a leading role in the EU's activities in global policy changes because of its strength on the international scene. Moreover, as one of the most polluting continents on the planet, it must reduce its carbon footprint to meet the targets agreed upon in the Paris Agreement (Bruyninckx et al., 2021).

Therefore, MiFID II 2021/1253 will help the European Commission to redirect private capital towards efforts to "green" the EU. Companies will be forced to integrate ESG considerations into their organizational requirements as of August 2, 2022, if they wish to be financed by green investors (Allen Overy, 2021). Furthermore, it will also try to avoid greenwashing thanks to the inclusion of sustainability preferences in the investor-adviser relationship. Indeed, it serves to prioritize the consideration of ESG risks by the relevant companies and banks in the European Economic Area, thus, the financial system is forced to consider sustainability in its decision making (Allen Overy, 2021).

Although its ambitious policies seem sufficient to save our economy by 2050, Europe absolutely must implement reliable techniques to fully achieve carbon neutrality by the dates set by the IPCC (Bruyninckx et al., 2021). Therefore, the MiFID II 2021/1253 regulation is one of the keys to transforming our financial system into a more sustainable one that considers the climate risks we already face.

What does MiFID II ESG mean in practice?

MiFID II 2021/1253 is changing the whole financial system. Indeed, by integrating sustainability factors, risks, and preferences into specific organizational requirements and operating conditions (ESMA, 2022a), investment firms and corporations that need money will have to change their body structure to please these new EU regulations (ESMA, 2022a).

According to Allen Overy (2021), incorporating the concept of sustainability preference into investor choice requires two steps. To understand what type of financial products an investor requires to have in his portfolio, the asset manager needs to know the degree of sustainability preference of his client and the proportion of each product he will implement in his client's portfolio. This new regulation, thus, encourages the asset manager to customize his service to each of his clients according to their preferences (I. de L., 2022). On top of that, financial institutions will have to implement financial education tools to explain to their clients that the customization of their portfolio comes from the MiFID II regulation which now considers sustainability preferences, and they will have to explain what this term means (I. de L., 2022).

The amended regulation (EU) 202I/1253 has added three new definitions. The “sustainability preferences” which will identify the integration of different financial products according to the client's requirements in terms of sustainability. The “sustainability factors” previously defined in the regulation (EU) 2019/2088 which said that sustainability factors “mean environmental, social and employee matters, respect for human rights, anti-corruption and anti-bribery matters”. And finally, the “sustainability risks” also previously defined in the regulation (EU) 2019/2088 which defines it as “an environmental, social or governance event or condition that, if it occurs, could cause an actual or a potential material negative impact on the value of the investment”. The investor will then know that the portfolio offered to him has been customized according to his sustainability preferences (I. de L., 2022).

These preferences will have an impact on the financial instruments that will make up his investment portfolio (I. de L., 2022). As it is written in the Regulation (EU) 202I/1253, depending on the sustainability preferences of a client, a selection of financial instruments will be integrated in a client’s portfolio. MiFID II ESG classifies four categories of products according to different principles. We will name these categories from A to D (Regulation (EU) 202I/1253; Allen Overy, 2021).

- **Category A:** a financial instrument for which the client determines a minimum proportion shall be invested in environmentally sustainable investments as defined in the European taxonomy.
- **Category B:** a financial instrument for which the client determines that a minimum proportion shall be invested in sustainable investments as defined in the SFDR.
- **Category C:** a financial instrument that considers principal adverse impacts on sustainability factors where qualitative or quantitative elements demonstrating that considerations are determined by the client. In other words, a financial instrument whose investee companies have identified key negative impacts (PAI) on the sustainability factors that will be impacted by its activity.
- **Category D:** this category does not include sustainable preferences. It will be assigned to an investor who says he is not interested in investing his assets in green products.

In order for the reader to understand the different products mentioned above, it is recommended to reread point 2.4.1. for category A and point 2.4.2. for category B and C.

Therefore, MiFID II ESG is the last step toward the investor protection linking his investment choices to his sustainability preferences and the duty of his portfolio manager to give them products in line with his values. However, according to Suetens and Nemeth (2022), financial institutions believe that the lack of information from ESMA makes the regulation flawed. Indeed, the limited information received on the ESG MiFID II directive makes its implementation difficult (Bernal, 2022). In addition, the lack of product data does not allow financial institutions to properly analyze whether a product is truly sustainable. This lack of a regulatory framework leads to deficient information retrieval systems and may have the unintended effect of greenwashing in the short term (Bernal, 2022).

2.4.4. CSRD

The last pillar of sustainable finance that will need the regulation 2021/1253 to be as effective as it is meant to be, is the CSRD also called the Corporate Sustainable Reporting Directive. Indeed, this new directive "aims to fill the ESG data gap" by strengthening and revising disclosure requirements on sustainability-related information (Deloitte Luxembourg, 2021). While the EET that was implemented by Findatex in January 2022 is a valuable tool for obtaining existing data under the new regulations. The uniform standards found in the CSRD are necessary to have "a consistent and comparable baseline against which to compare corporate disclosures across jurisdictions." (Deloitte Luxembourg, 2021; Fefundinfo, 2021).

This new directive goes further than its predecessor released in 2018 under the name “Non-Financial Reporting Directive '' (NFRD). This is because in addition to setting non-financial reporting obligations, it will increase transparency and the delivery of information while taking into account ESG criteria in order to assess company performance (European Commission, 2021f; Guegen, 2022).

Once again, a problem of sequencing of regulations is apparent. Indeed, in order to be applied correctly, the need for data is essential for regulations, such as the Taxonomy, the SFDR and the new MiFID (Sami, 2022). Unfortunately, this contribution can only be fulfilled after the application of this directive, which is scheduled for 2024. Its implementation will involve the transcription of the previous year's data. This means that data collection must start in 2023 (Sami, 2022).

Finally, this timeline proposed by Eurosif was created to show the problem of consistency between the different publication dates of the SFDR, the European Taxonomy and finally the amended MiFID II. According to Eurosif (2021), these inconsistencies will create a risk of confusion among organizations that need to implement these new measures. As a result, the European agenda may have difficulty developing as originally planned.

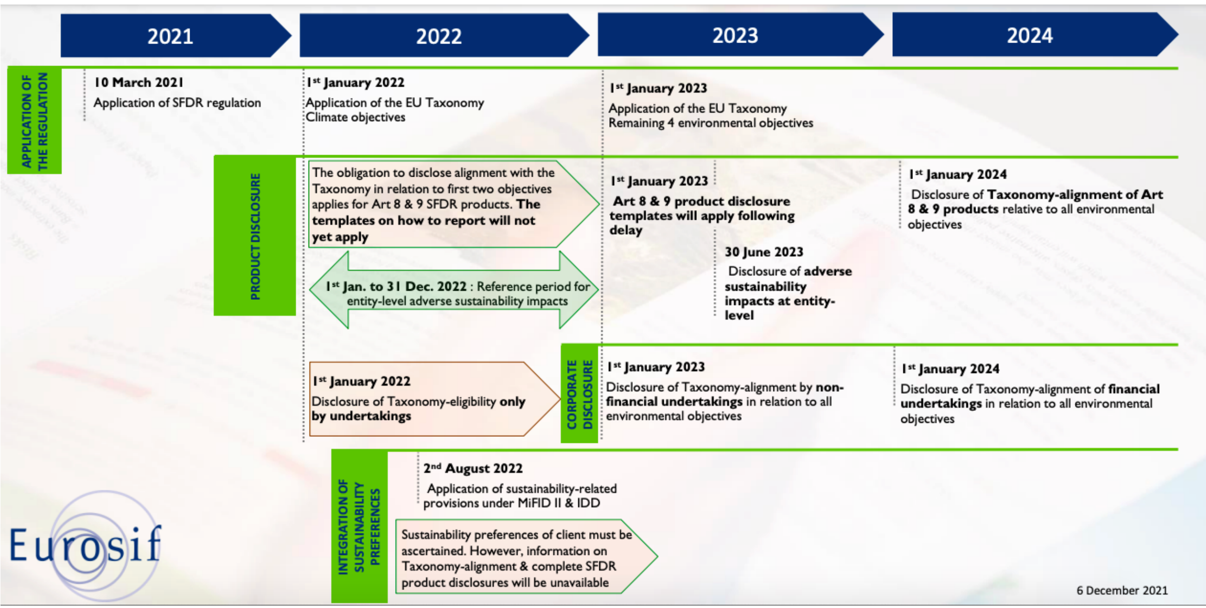


Figure 5: Timeline Chaos

Source : Eurosif, 2021

2.5. Literature review summary

As explained throughout this literature review, greenwashing ultimately comes from the difficulties companies have in adapting to the market. Indeed, as these sustainable values have only existed for a few decades, companies try to meet the needs of the population as they have always done. However, the problem of climate change is urgent and the European Union has decided to intervene to prevent these companies from harming the planet. The EU's goals aim to help the transition to a more sustainable economic model for future generations. Therefore, the implementation of new regulations in the market serves to achieve this ultimate objective and MiFID being the step connecting the investor and the financial advisors, will try to change the core business of companies so that they can still benefit from the private capital of retail clients.

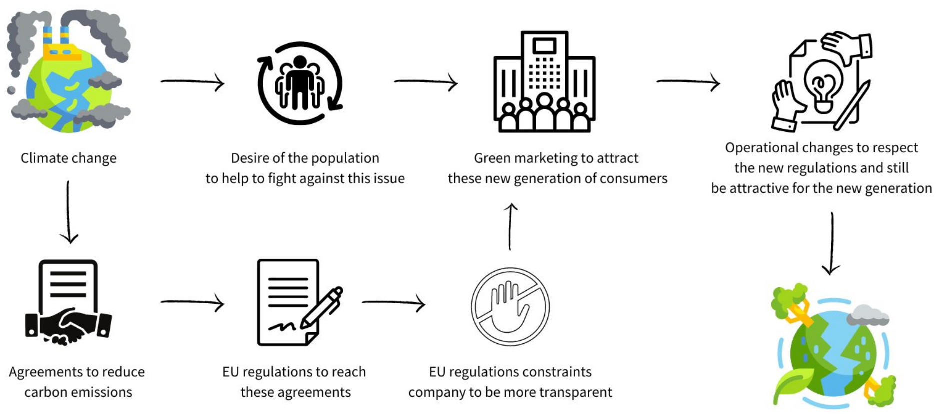


Figure 6: Steps to be taken for Europe's ecological transition

Source: Own work

CHAPTER 3: RESEARCH DESIGN

3.1. Methodology

As mentioned in chapter 2, this work aims to study (1) the evolution of the different European agreements and regulations to finance a more sustainable economy and (2) the impact of the newly implemented MiFID II Sustainability Preferences amendments on greenwashing.

This section will discuss the methodological approach used in this work. First of all, we have established our research questions thanks to the literature devoted to this subject. Indeed, two related factors are greenwashing in the financial sector and the various European regulations favoring companies with strong environmental values. Given the global scope of ESG values and the importance of integrating climate risk in the financial sector, we thought it would be interesting to look at the transition that our economy will undergo in the coming years.

For this purpose, we conducted a qualitative approach to understand how different parts of the financial sector were affected by the arrival of the new European regulations on the market. According to Malhotra, Birks & Nunan (p150, 2017), qualitative research is "An unstructured, primarily exploratory design based on small samples, intended to provide depth, insight, and understanding." Although the qualitative approach does not allow us to have an overall view due to the limited number of participants we can interview, the quantitative method did not seem appropriate for our type of research. Indeed, the quantitative approach would not have allowed us to have a deeper understanding of the subject, therefore, the information retrieved would have been useless for understanding the impacts of the European regulations on the market. Consequently, the qualitative method seemed to be the most appropriate for collecting sufficiently sensitive data to understand the direction in which the financial market is evolving (Malhotra et al., 2017).

Given our research question and its specific field of application due to the ESG criterion, the interview guide seems to be the most appropriate data method. It is relevant to our research question where the actors are still few in number to understand the subject. Indeed, according to O'Dwyer and Edgecliffe-Johnson (2021), large consultancy firms, such as Deloitte, only announced sustainability training plans in 2021.

Therefore, we decided to focus on three types of firms to interview: financial regulators, financial institutions and advisory firms. Our research question aims to understand what the MiFID II amendments, and the regulations on which it is based, can bring to the market in order to observe their impact on greenwashing and consequently on the development of the economic transition towards sustainability.
To this end, we will analyze the changes that these different types of corporations had to take into account during recent months.

3.2. Data Collection

To better understand the sustainable financial sector and the potential and implications of MiFID II 2021/1253 on green investments, we collected our data through multiple interviews based on the inductive approach to better understand the sustainable financial sector. This thesis will, therefore, use the inductive method because, as explained in (Malhotra et al., 2017, p.162), induction is "a form of reasoning that generally involves the inference that an instance or repeated combination of events can be universally generalized." Thus, using the inductive method will allow us to have an approach to primary data to subsequently derive broader concepts based on the link between the preliminary data collected beforehand by an evaluator or researcher during their interviews (Thomas, 2006).

Interviews were conducted with workers working in banks, regulatory entities or in consulting firms in the sustainable finance sector to discuss their perspectives on MiFID II ESG. Given the changing attitudes following the 2019 health crisis, most of the interviews were conducted by video conference as this allowed for greater flexibility in meeting with the participants.

The interviews were recorded in order to obtain transcripts of the answers to the questions asked to facilitate the data sampling process. Furthermore, they were conducted using open-ended questions to get an overall view. Some questions of the questionnaire differ depending on the interviewee's company. Our interview questions were based on four themes identified in the research question: (1) the MiFID regulation and its effects, (2) the effects of unfinished ancillary regulations on the market, (3) the evolution of greenwashing following all these regulations and, (4) summary of MiFID II.

This interview guide can be found in Table 1 and has been based on the literature review. This set of questions is based on the information gathered during the research on sustainable finance and on the three new European regulations that have been analyzed in section 2.4. Moreover, as few scientific articles have been written about the new MiFID regulation, the questions were written by the author based on literature on sustainable finance, greenwashing as well as on articles from consultancy firms talking about MiFID II ESG. The purpose of the answers we had received is to feed the flow of information on the subject.

Table 1: Interview guide

Theme	N°	Company type	Questions
MiFID regulation and its effects	1.	Banks	When the new MiFID II regulation was published in August 2021, how did your firm respond? Did you have to undergo any specific training in order to properly implement the new regulation 2021/1253 which is expected to go into effect in August?
		Consulting firms	When the new MiFID II regulation was published in August 2021, how did your clients react? What are the main tips you have given them to comply with the regulation?
		Regulators	When the new MiFID II regulation was published in August 2021, how did your department react, what did you have to put in place in your territory to comply with the European regulation?
	2.	Banks	How do you see the level of preparation of your company to comply with MiFID II ESG?
		Consulting firms	How do you see the level of preparation of your clients to comply with MiFID II ESG?
		Regulators	How do you rate the level of preparation of firms to comply with MiFID II ESG? How have you helped the industry comply with the new MiFID regulations?
	3.	Banks	If certain aspects of the regulation could not be implemented due to lack of time, how do you think your company will be affected by non-compliance with the regulation? What problems might you encounter as a result?
		Consulting firms	If some of them seem unprepared, how do you think they will be affected by non-compliance with the regulation? What problems might they encounter because of this?
		Regulators	If some companies and financial institutions think that the instructions for complying with this regulation are not clear enough, how do you respond to that? Do you think you could improve the

			implementation problems they are facing and, if so, how? Will there be any sanctions?
	4.	Banks Consulting firms Regulators	In your opinion, what problems could arise with this new law from the point of view of: • Investors: • Financial institutions:
	5.	Banks Consulting firms Regulators	Do you think MiFID II will allow the financial market to have more ESG assets? And do you think that this regulation will have a greater effect on the market than the Taxonomy in terms of the quantity of sustainability assets?
The effects of unfinished ancillary regulations on the market	6.	Banks Consulting firms Regulators	What do you think about adding new green regulations such as the SFDR and the European Taxonomy? Do you see any constraints emerging from these new regulations given their novelty and potential shortcomings? If so, as MiFID II relies on these regulations, how do you think this will affect its effectiveness? Do you see any collateral effects contrary to what the regulation is trying to put in place?
	7.	Banks	Does your company encounter difficulties in obtaining certain types of financial products? For example, MiFID classifies financial products into 4 categories. Is it more difficult for your company to obtain sustainable financial instruments according to the European Taxonomy than sustainable financial instruments according to the SFDR? If so, why?
		Consulting firms	Is it more difficult for your clients to obtain sustainable financial instruments according to the European Taxonomy than sustainable financial instruments according to the SFDR? If so, why? Is it more difficult for your clients to obtain sustainable financial instruments according to the European Taxonomy than sustainable financial instruments according to the SFDR? If so, why?
		Regulators	Are there any difficulties for the market to obtain certain types of financial products? For example, MiFID classifies financial products into 4 categories. Is it more difficult for the market to obtain sustainable financial instruments according to the European Taxonomy than sustainable financial instruments according to the SFDR? If so, why?
The evolution of greenwashing following sustainable regulations	8.	Banks	The pressure that this new regulation will put on companies seeking capital will certainly cause some of them to exaggerate their ESG performance. How can you be sure that the assets you sell to your clients according to their sustainability preferences are not overstated?
		Consulting firms	The pressure this new regulation will put on companies seeking capital will certainly cause some of them to overstate their ESG performance. How can your clients protect themselves to ensure that their clients' assets are not overstated?
		Regulators	The pressure that this new regulation will put on companies seeking capital will certainly cause some of them to exaggerate their ESG performance. How can the market protect itself to ensure that sustainable assets are not overstated?
	9.	Banks Consulting firms Regulators	How do you think MiFID can help mitigate the risk of greenwashing?
	10.	Banks Consulting firms Regulators	MiFID II ESG is likely to be designed to combat the risk of greenwashing. How can you help your clients fully comply with their due diligence and product approval process?

MiFID II ESG opinions	**11.**	Banks Consulting firms Regulators	In your opinion, what are the strengths and weaknesses of the regulations?
	12.	Banks Consulting firms Regulators	If you were the initiator of this regulation and you could change some of its aspects as a whole but also to prevent some companies from greenwashing, what would you do?

3.3. Data Sampling

The interview participants were selected after an in-depth discussion on the topic with Mr. Yves Francis, professor at HEC Liège and independent board director. Indeed, after having understood that the quantitative method was not the right approach to answer my research question, the qualitative method was an evidence. As Mr. Yves Francis has been working for many years in the financial sector, he enabled me to talk to experts in the field. Thanks to the contacts he provided me, I was soon able to extend my research to other experts. After each interview, I asked the participants if they could put me in touch with their colleagues. This technique is sometimes called "snowball sampling" as new participants are recruited through referrals or information given by previous participants (Malhotra et al., 2017). In this way I was able to find people who were open and available to speak about the subject. We also did research through LinkedIn to have more participants. Unfortunately, the search on this social network was not fruitful and only 3 out of 10 people replied to our messages, of which finally only 2 people accepted to be interviewed (see Table 2). However, some weaknesses of the inductive approach must be taken into consideration. Indeed, this research method manages to develop a theory by making links with occurrences that took place during several different interviews. Therefore, the conclusions drawn from this method may be biased due to the small number of financial players interviewed (Malhotra et al., 2017).

Table 2: Interviews information

Name	*Roles*	*Company**	*Country*	*Fields*	*Interview date*	*Interview length*
Jean Benoit Gambet	Chief Executive Officer	Moonshot	France	Consulting company	13.07.2022	43 min
Julien Renkin	Chief Compliance Officer	Sopiad	Belgium	Consulting company	14.07.2022	54 min
Giulia Bruni Roccia	Senior Manager in Sustainability department	Deloitte	Luxembourg	Consulting company	14.07.2022	50 min
Thomas Schoenmakers	Responsible for the development of the Belgian market	Banque de Luxembourg	Luxembourg	Bank	15.07.2022	47 min
Nathalie Dogniez	ESG Leader Partner	PwC	Luxembourg	Consulting company	15.07.2022	81 min
Charles Van Doorslaer	Compliance Officer	NewB	Belgium	Bank	19.07.2022	69 min
Caterina Fuso	Business Project Manager	Credit Suisse	Luxembourg	Consulting company	22.07.2022	45 min
Isabelle Jaspart & Stijn Huysentruyt	Head of Division; Legal Expert	CSSF	Luxembourg	Regulatory entity	27.07.2022	78 min
Emma de Leeuw	Compliance & SFDR Officer	Triodos	Netherlands	Bank	09.08.2022	50 min

*Description of the companies in the appendix 10

3.4. Data Analysis

The qualitative interviews were conducted using an interview guide. Indeed, twelve questions were asked to the ten interviewees and were classified under four different categories. In order to analyze the data from the qualitative study, each interview was recorded with the participants' consent. Then, the transcripts of the interviews, which are in the Appendices, were made. Some participants requested that these interviews be sent to them before being included in this thesis for confidentiality reasons. After data assembly, we proceeded to data reduction. This allowed us to code the information received in order to make more links between the different interviews. The coding of information is used to highlight the answer to our initial question because during an interview some information is less relevant than others (Tessier, 2020).

Then, we encoded these data in an excel file in order to have an overview of the information that had been given to us. The data was sorted by question and the questions were categorized. This step is also called "data display" and as Malhotra et al. (2017, p.247) explained, this process permits "conclusion drawing and action". Finally, in order for the data collected to be perceived as valid, a comparison with the literature review was designed. For this ultimate part also known as "data verification", we used triangulation by contrasting the sources we had collected during the theoretical part with the empirical results in order to enrich our conclusions. Triangulation separately uses interview data and results originally found by previous research and then compares them to validate findings (Valencia, 2020). From there, we highlight the main findings, which allowed us to gain a broader understanding of the potential of EU regulations to reduce the phenomenon of greenwashing and in particular MiFID II ESG. As well as the possible loopholes they contain.

CHAPTER 4: RESULTS

This chapter will only deal with the collection and transcription of the opinions and views of the interviewees. Some observations will be nuanced according to the author's vision. The answers to the questions asked will be analyzed according to the 4 main themes and will allow to have a global hypothesis for each category.

To get a broader view of these four categories, we will first analyze the views of the second link in the regulatory chain (Figure 7), namely the financial regulators. Then, we will look at what intermediaries such as consultancy companies have noticed. Next, we will look at what financial institutions such as banks have to put in place to keep a good contact with their customers. For some questions as well as for some themes, the analysis will be done without distinction of the different institutions. Finally, we will analyze the last theme order to get the pros and cons of the MiFID II ESG.

This research will focus on the institutions in the grey frame (Figure 7).

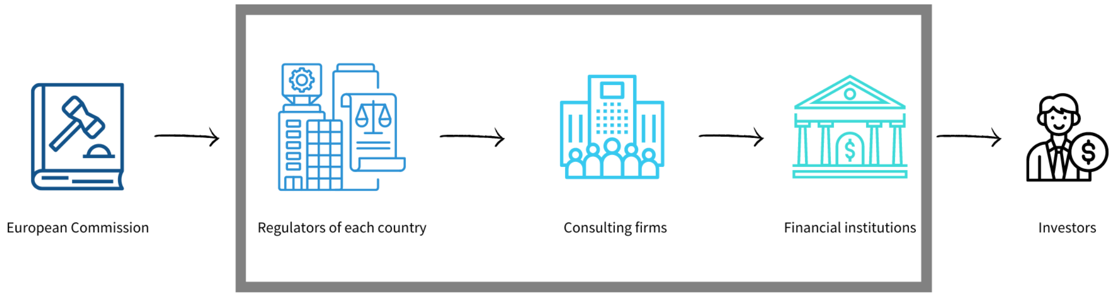


Figure 7: The regulatory chain

Source: Own work

Theme 1: MiFID II ESG regulation and its effects on the market

For this first topic, we will look at the initial impacts of newly implemented MiFID II Sustainability Preferences amendments on the market when it comes into effect and the market's preparation for it.

Financial regulator's opinions

First of all, before getting an overview of what our two legal experts think about market reactions regarding the implementation of Regulation 2021/1253, it is relevant to explain how a law is implemented in a market.

Our two regulatory interlocutors explained that when a European regulation is published, it must be enforced without any difference from one country to another. There is no flexibility for the regulators concerning EU regulations. They can only report any interpretation issues submitted from companies in order to make the European Commission aware of these problems. Then, the EU tries to provide solutions in their guidelines. As a result, the power of financial regulators is limited to the transmission of information between the European Commission and companies. When MiFID II ESG was issued, the Luxembourg regulator did not need to notify the companies because they were already well informed. However, despite the law was already known their regulatory institution felt concerned about it.

The uncertainty in the implementation of the new law comes from the lack of data that companies have in their possession. Yet, for Yves Huysentruyt, "it's not different from other topics or other new laws that have come along (...) they won't be ready in the sense that not everything will be implemented in the IT system(...), but I think that most entities will have something for August and I think that they will have at least made some questionnaires for the customers". From his perspective, MiFID is like any other law and there are no reasons to be anxious.

Regarding the compliance of companies with the new regulation, the legal experts have given their respective opinions. For Yves Huytruyt, one thing is sure, strict controls will not start on August 3rd. However, Isabelle Jaspart has complemented his words by adding "If on August 15 we organize a control on MiFID, we will check if they have put it in place". This allows us to assert that even if controls occur, they will only be for inspection purposes in the first place in order to ensure that companies have started to enforce MiFID II ESG. Therefore, if we use what Mr. Huysentruyt explains, when he talks about the 3 levels of reaction from the CSSF when a company does not respect the rules: "Level 1: Request for correction; Level 2: We can be stricter by sending them a letter of injunction to correct their behavior within a certain date; Level 3: Sending a fine or other type of sanctions". The first level of reaction will be the one mostly used by the CSSF during August's month.

Moreover, as one of our Luxembourg legal experts said about the possible level of sanction that can be carried out this year, the same will apply in the Netherlands. In fact, one of our respondents from the banking sector explained that: "the Dutch regulators are also still trying to figure out how to go about regulating this. So, what we've kind of heard through the grapevine is there is some period of relax, some period of trying your best, implementation time". In other words, companies that do their best to implement the regulation this year will not normally be penalized for their mistakes as the market does not possess enough data to implement it as it should be.

<u>Advisory companies' opinions</u>

From the perspective of intermediate companies, the market is not ready to properly accommodate this new regulation. In fact, the opinions of our four speakers, who came from different consulting firms, coincided. MiFID II ESG is the last sustainable regulation to be implemented this year and is, thus, the one that will be addressed after all the others, namely SFDR and Taxonomy.

The misunderstanding of its implementation seriously affects the market. According to Nathalie Dogniez, the lack of data is one of the major problems encountered by financial institutions. MiFID II ESG coming out before the second level of the SFDR makes no sense. For Giulia Bruni Roccia and Jean-Benoit Gambet, banks will have a questionnaire in place to be in line with the regulation but for Mr. Gambet, it is not because banks have a questionnaire that their employees know how to use it. Giulia added that "In the best-case scenario they will release one, and they will also be able to control it even though it will not be with the perfect process". As a result, we can hypothesize that even for the best prepared companies, its implementation cannot be properly done.

To join the opinion of Isabelle Jaspart, a legal expert at the CSSF, Julien Renkin thinks that "On the average preparation level, (...) everyone is aware, but in relation to the August 2nd deadline, very few people are ready." Therefore, it is clearly expressed that the financial world is aware that this law will shake up the sector but many hope to have more time to be prepared.

Although the general opinion is the same concerning the level of preparation of the companies, the type of sanction expected differs according to interviewees. For Giulia Bruni Roccia and Nathalie Dogniez, financial institutions will be required to report on what they have arranged to comply with MiFID II ESG. The objective is to show their good faith in complying with the rules, even if the measures they have taken are not in line with the whole regulation. Nathalie Dogniez goes further by stating that for those who "look at the topic too late, (...) it is a significant regulatory risk. Indeed, they engage their responsibility if they sell non-sustainable products but also their reputation since it is a thematic that attracts a lot of attention from journalists, NGOs." Contrary to their opinion, Jean-Benoit Gambet and

Julien Renkin assert that sanctions will not be imposed this year. For M. Gambet, this comes from the fact that the big banks, likely to be inspected, have a questionnaire ready while Mr. Renkin qualified by saying that "Not having sanctions in 2022 does not protect against the possibility of receiving sanctions in 2023 for 2022."

Financial institutions' opinions

From a financial institution perspective, the apprehension that one might have expected from the previous answers is not so bad. As stated by Charles Van Doorslaer, "The draft law was already circulating before it was published. (...) There is no single date when banks knew MiFID II ESG was coming out". On this point, Thomas Schoenmakers seems to agree, saying that "the bank had anticipated things well and we had a lot of training programs on the different topics". However, for Mr. Van Doorslaer "MiFID was seen as the regulation that would take longer to be considered" which is in line with the opinion given by the consultants. Furthermore, two of the bank's employees indicated that this law could be problematic because of the different regulations it brings together. In fact, MiFID II ESG requires portfolio advisors to explain sustainability to retail clients when, first, sustainability is a broad topic that institutions have difficulty explaining to their employees and second, sustainability is defined in three different ways under the SFDR, the Taxonomy and finally under MiFID II ESG. Therefore, as the three regulations are not aligned, there is a high probability that the retail customer will no longer understand the information provided to him. The complexity of these laws would become a burden for him who would prefer to let his portfolio manager take care of everything. As a result, this would deviate from the original objectives of MiFID II ESG.
In terms of their company's preparedness, all four participants seemed confident that their companies had done their best. Indeed, employee training programs were integrated early on. However, one of the interviewees points out that with regulations such as the SFDR and Taxonomy to consider, MiFID is not the priority at the moment. Companies are doing their best to comply with expanded MiFID II but they know that there is a lack of data to be perfectly in line with it. Not having information on the level of requirement requested, leads to a market tension. In response to this issue, it is necessary for them to be as transparent as possible in order not to be penalized.

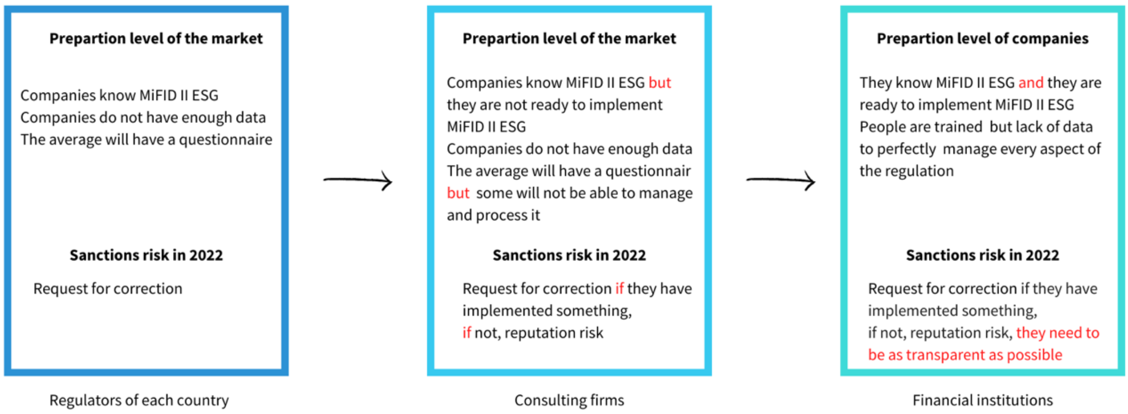


Figure 8: Chain of thought of the different entities on the preparation of market and the possible sanctions that may be incurred for financial companies[8]

Source: Own work

Mixed views on issues that may arise and the effects on ESG funds

For the question related to the problems that investors and financial institutions might face because of MiFID II ESG, we decided to mix the different institutions. Two streams of thought were identified during this question that were not specifically related to the interviewee's entity. The first line of

[8] The transition from one framework to another changes according to the perception of MiFID II ESG in relation to the type of company

thinking is focused on a positive view of regulatory integration and the second is a bit more concerned about market reaction.

For four of our interviewees, the impacts of regulation on investors and financial institutions were not problematic. According to Ms. Bruni Roccia, the regulation itself is not a problem, but it is the lack of data that allows its implementation that makes the situation complicated. However, this concern does not have any impact on the really committed clients. According to her, "If products are not well structured, (...) they will probably continue (...) to invest in the article six product which is the more traditionally financial focused products (...) and just donate to some of their favorite associations from their personal wallet". For Thomas Schoenmakers, this regulation changes the way a manager has learned to manage funds: "A manager knew at the beginning of the year that oil shares were going up (...) but with the new law, he can't buy them. So, he does not respect what his financial analysis would have told him to do", which ultimately will impact the investor's portfolio. For Ms. Fuso, the integration of this new regulation will increase internal training but it will not have a negative impact on companies. Then, she joins the second stream of thinking for investors by stating that "For the investor this regulation and the bad timing will be the possible frustration of not having what they ask when they have to say their sustainability preference". Finally, Ms. Jaspart mainly mentioned that thanks to some of the best companies, others would know how to implement the regulation in a more efficient way.

Regarding the six other interviewees, this law will initially be negatively perceived because of its complexity and bad timing. On the investors' side, there will be frustration. Their expectations will not be met by the market as there are not enough sustainable products. Moreover, the complexity of the information to be understood will be a hindrance to the purpose of the regulation. On the business side, the difficulty of not knowing how to meet customers' expectations will be detrimental to them. Therefore, in the short-term this regulation will only drive the market away from sustainable solutions.

Finally, with regard to the possible impact of the regulation on the quantity of sustainable funds, there is a very mixed view, although the majority thinks that it would allow to generate sustainable products in the long term. According to Mr. Huysentruyt and Ms. Jaspart, "This is the goal" of MiFID II ESG. However, there is an uncertainty about it. Caterina Fuso joins them in this respect, explaining that "(...) it could potentially be the opposite that the products are there, your sustainable products are there, but financial players will not disclose, categorize, market them as so", because "the requirements sets are very strict and not easy to implement at all".
For Ms. Dogniez and Ms. Bruni Roccia, MiFID II ESG will contribute to the increase of the quantity of sustainable funds but not alone. Indeed, the expanded MiFID II being based on other regulations, it will not have a standalone contribution. "Taxonomy is at the management level. SFDR is at the level of reporting on the alignment with the Taxonomy to the end investor and to intermediaries. Finally, MiFID II is about how the intermediary ensures that a financial product is appropriate to the investor's expectations of sustainability." stated Ms. Dogniez. However, Charles Van Doorslaer raises an interesting point. He explains that "as there are currently few ESG securities, there is a possibility of creating a speculative bubble on the few investment funds that meet the standards". Fears could, thus, arise in the market due to an exceeding demand for sustainable funds while supply has not yet followed. For others, the view is uncertain but they would tend to say that in the long run, MiFID II ESG will only have direct and indirect positive impacts on ESG funds. As far as PAIs are concerned, the author of this thesis has the impression from the answers received that it is also quite complicated to have funds following this classification. As a result, the poor sequencing of the various regulations and the lack of understanding of what they actually require is disrupting the financial sector.

Summary of the effects on the market

Ultimately, the effects that MiFID II ESG could have on the market are numerous and difficult to identify. However, we have noted a tendency for the market to think that the legislation will be detrimental in the short-term because of the bad sequencing of each EU green regulations, but in the long term, all are certain that MiFID II ESG is only a good thing for the market and will help the ecological transition.

Theme 2: The effects of unfinished ancillary regulations on the market

For this second topic, we will examine the influences of the SFDR and EU Taxonomy on MiFID II 2021/1253 and the market's understanding of the differences between these three green EU regulations.

Financial regulator's opinions

From a regulatory point of view, Stijn Huysentruyt explains that MiFID II ESG is a regulation that cannot be considered as a standalone. Indeed, for him "the regulation is complicated because it refers to concepts that are not MiFID but come from the SFDR and the Taxonomy". Isabelle Jaspart complemented his statement by saying that the addition of the SFDR and Taxonomy regulations was necessary. As the supply of sustainable products is not enough to answer the future demand, the only way to avoid frustrating the client in terms of obtaining a sustainable product according to the Taxonomy, SFDR or PAI, is to have good communication between advisors and clients. In this way, even if the manager has no product available that best meets the customer's expectations, the investor will have an additional explanation and will remain involved in the process.

This concern about possible miscommunication that could mislead investors was shared by one of our regulatory advisors. Indeed, it was raised that it is important to keep track of initial preferences so that even if the bank does not have the products requested, the market will take them into account to produce more sustainable products. It is about meeting investor expectations later on, not lowering them.

Advisory companies' opinions

From the perspective of intermediate companies, the problem with all these regulations is mainly the question of the implementation timing. In fact, this poor sequencing of regulations will produce various short-term issues in the market. On the one hand, "the fact that we have SFDR, Taxonomy and MiFID II before CSRD may result in calculations and indicators that will not be correct due to the lack of reliable and complete information from the underlying firms" according to Ms. Dogniez. On the other hand, it will lead to additional costs for companies as they will have to implement new training when SFDR and Taxonomy are complete. Finally, getting funds to comply with MiFID II ESG is not easy. All our interviewees explain that aligning a fund to the Taxonomy is very complex from now on.

Financial institutions' opinions

From a financial institution perspective, the addition of all these regulations in a short period of time is very costly for banks from a logistical point of view but also for new customer acquisition. Furthermore, the fact that MiFID relies on unfinished regulations will create even more costs for financial institutions, thus, it will impact the investors' portfolio. Indeed, according to Ms. de Leeuw "It's also a lot of extra work not just for big banks, but even for small medium banks. And it is also really placing a big burden on the banks that are already sustainable". This could lead some companies to

classify a sustainable product as unsustainable due to the much lower number of requirements for an article 6 product under the SFDR compared to the requirements needed for an article 9 product.
Moreover, the lack of data does not allow banks to offer products that meet the customer's sustainable preferences because there are difficulties to "understand what these three types of products entail" stated Ms. Fuso.

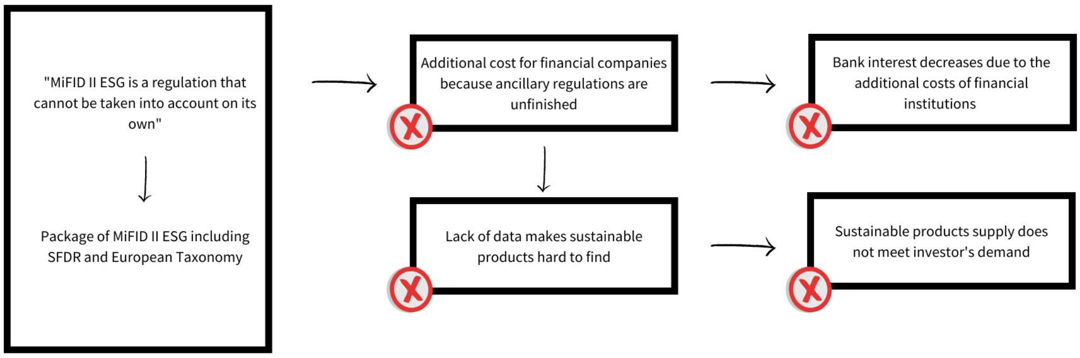


Figure 9: The effects of unfinished ancillary regulations on the market

Source: Own work

In conclusion, unfinished ancillary regulations have negative effects on the market. On the one hand, they produce a gap between demand and supply of sustainable products. On the other hand, they have a negative impact on the cost of financial institutions and, consequently, on investor interest.

Theme 3: The evolution of greenwashing following sustainable regulations

Financial regulator's opinions

For regulators, the only way to ensure that a company does not overstate the ESG criteria of its products and activities is to check the marketing materials. The addition of MiFID II's ESG regulation is an extra layer of verification to be applied. Indeed, the regulation states that "all information given to clients must be clear, correct and not misleading" stated Ms. Jaspart. As MiFID 2021/1253 now incorporates the customer into the fund decision-making process by involving sustainability preferences, it is even more important to verify what companies disclose.

Consultancy companies' opinions

Therefore, the advice from intermediaries to companies in order to protect themselves against possible exaggerations by issuing companies is to add a layer of verification. When a company discloses its non-financial information, it is important that the same information is reviewed by an external auditor. Since this verification is not yet mandatory, it is best to remain "conservative and cautious, (..) in the classification of their products", mentioned Ms. Roccia Bruni.

Financial institutions' opinions

As for financial institutions, M. Van Doorslaer mentions that there is a huge risk of greenwashing when issuing companies disclose information, as there is no mandatory control on non-financial reports at the moment. Yet, for M. Schoemaker, "MiFID will reduce greenwashing through ex-post controls", and banks have no choices than "to rely on what third-party organizations say".
Furthermore, as the SFDR and Taxonomy regulations are not finished yet, there is a risk also in financial institutions. Indeed, "financial institutions can potentially, directly or indirectly, greenwash by

providing too much complex information to their client" leading them to make choices they do not understand, in the view of Ms. de Leeuw. For this reason, Ms. Fuso joins Ms. Roccia Bruni in recommending caution to guard against any risk of greenwashing.

Mixed views on the evolution of greenwashing

MiFID II ESG is a great help in the fight against greenwashing. According to Caterina Fuso, "keeping track of everything is a way to mitigate greenwashing". Indeed, "a portfolio is meant to evolve because it changes every day", explains Ms. Jaspart. It is, therefore, necessary to follow an investor's preferences in order to maintain a portfolio that meets their expectations.
Thus, greenwashing will be mitigated by monitoring the client's requirements but also by intensifying the dialogue between the manager and the investor so that the level of knowledge on the subject increases. According to M. Van Doorslaer "anything that increases knowledge is good for the fight", the more informed a client is, the more difficult it will be to deceive them.

The due diligence system is also a fundamental point in the fight against greenwashing. However, the fact that there is no mandatory external control on non-financial reports reduces its effectiveness. Indeed, consulting companies produce these reports according to the information they are given. This is why banks try to have a high-level of control over the information chain. Using "rigorous screening and selection processes", they assess whether or not a fund qualifies as sustainable. Leading them to take a conservative approach when in doubt, thus classifying a sustainable product as unsustainable.

In conclusion, MiFID II ESG is an additional tool to fight against greenwashing but does not eradicate it completely. Indeed, even if the investor will be protected by a good communication with his manager, there will always be a risk of being misled because of the lack of verification obligation. Consequently, it is important that the EU implements other regulations, such as the requirement for external auditing of non-financial reports.

Theme 4: MiFID II ESG opinions

Regarding the general views on the strengths and weaknesses of MiFID II ESG, many responses came up several times.

On the one hand, the strengths of MiFID that were raised the most were respectively: the inclusion of the sustainability factor in investments; the implementation of this regulation in all European countries; Europe, through MiFID II ESG and its ancillary regulations, is leading the world in terms of sustainability; MiFID II ESG enables the structuring of information on the supply side but also on the market's needs; and finally the fact that it is not a completely new regulation which makes it strong because it solved a lot of past issues.

On the other hand, the weaknesses of MiFID that were most often mentioned were respectively: the timing and sequencing of all the regulations; the complexity of the regulation in terms of implementation; and the lack of a clear guideline.
However, other weaknesses were raised that are more related to the regulatory package. For example, from the point of view of Taxonomy, four of the speakers mentioned the fact that so-called sustainable activities are qualified as such depending on the current political regime. Indeed, if we take the example of nuclear energy or diesel cars, we can see that certain lobbies can change certain activities from polluting to sustainable. This leads to a loss of market confidence in the objectives of the taxonomy and reduces its legitimacy, thus leading to a loss of credibility also for the MiFID ESG. Moreover, all those regulations disrupt the market because they require companies to be more sustainable in order to be attractive for investors. This leads to a decrease of competitiveness for

European companies in the first place, whereas American companies do not have to bother about all these new regulations.

In view of the main answers to the question on the strengths and weaknesses of MiFID II ESG, the possible changes related to the regulation added by the interviewees are consistent.
Indeed, the most raised comment was about the timing, with many preferring a different sequencing between the regulations. The fact that MiFID II ESG is based on unfinished regulations is a real problem for the market. Moreover, the complexity of the regulation makes it so difficult to implement that some believe that, in the short term at least, it will reduce market confidence. This will have the impact of reducing the incentive to move to a greener economy. A more gradual implementation of sustainability in the market would have been more beneficial.

Finally, a last point to note concerns the exit date of the MiFID II ESG regulation. In the course of the interviews, news emerged of a change in the implementation date of MiFID II ESG in France. This news angered many non-French companies who would have liked it to be delayed in their country as well. Therefore, we reached out to the legal experts to obtain information about this issue. Once again, thanks to their insight, it was explained that this regulation has not been understood by the market due to its complexity. Indeed, according to Ms. Jaspart, CSSF employee: "France has not moved the entry into force for investment firms at all". It has only opted for the exemption of certain entities through article 3 but "for investment firms, the date remains 2 August".

CHAPTER 5: DISCUSSION

The literature review of this work elaborates on the path taken by the European Union for the ecological transition and the problems encountered by the market due to the rise of greenwashing. Investors and their investment choices have a pivotal role in the green transition of our economy (EIT Climate-KIC, 2022). It will also examine Europe's progress in sustainability policy, digging into the latest regulation, MiFID II ESG, which considers investors' sustainability preferences and gives them the power to scrutinize what their portfolio manager does with their investments. This section examines the qualitative survey results from the previous chapter and relates them to the literature review. These results should provide a better understanding of what the MiFID II amendments, as well as the regulations on which it is based, could have on greenwashing. They will partially show the effects that MiFID will have on the market and the protection it can provide to investors. Moreover, they allowed us to understand how these regulations could enable Europe's green transition.

The first point we will analyze in this chapter is the eventual limitation of greenwashing through the MiFID II ESG. Based on the literature, the first driver of greenwashing is the lack of clear international standards that would cause companies to exaggerate their ESG performance in order to attract stakeholders (de Silva Lokuwaduge et al., 2022). As we have seen in the explanation of MiFID in point 2.4, this new regulation will give the market strict standards that companies will be constrained to respect. ESMA (2022b) has stated that the information that firms must disclose to the market will have to be fair, transparent, and not misleading. Our survey results confirmed this additional protection offered by the MiFID II ESG. As one of our legal experts commented, the changes to MiFID II provide an additional layer of verification. With regulations now including the customer in the fund decision-making process by bringing in sustainability preferences, it will be even more critical for regulators to verify what companies are disclosing. Therefore, since greenwashing is a regulatory loophole (de Silva Lokuwaduge et al.), MiFID II ESG reduces this loophole by making financial institutions more cautious in classifying sustainable and non-sustainable products.
Furthermore, the results of our interviews allow us to assert that there is a willingness to audit issuing companies. The absence of an audit obligation is deeply regrettable as it could lighten the workload of financial companies and increase the number of sustainable products. It is easier for a non-sustainable product to go through the steps required to be approved as such, compared to a sustainable product. Therefore, financial companies are more eager to classify a product as unsustainable even if there is a possibility for them to be classified as sustainable. Thus, this increase would come from trust and a clear view of the non-financial reports through to a third-party. The requirement made in the first hand would help decrease the number of steps that an institutional company has to go through in order to classify a product as sustainable.

Another driver of greenwashing is the lack of education on sustainability (de Freitas Netto et al.,2020). As expected, this predictor influences investment intention. The literature explains that the more stakeholders are ill-informed on sustainability, the more they can be deceived with false information (de Freitas Netto et al.,2020; TerraChoice, 2007; Parguel et al.,2015). With MiFID II ESG, integrating the concept of sustainable preferences makes investors more aware of their choices (Allen Overy, 2021). This comes from the fact that from August 2022, financial institutions will have to implement financial education tools, to explain to their customers what sustainability is, as well as a questionnaire to collect their customers' preferences regarding the investment of their money (Allen Overy, 2021). However, some problems regarding MiFID 2021/1253 were raised during our investigation. According to M. Van Doorslaer, theory and practice are not always aligned. There are three different definitions according to the SFDR, the Taxonomy, and MiFID II ESG. Although MiFID II ESG requires portfolio managers to educate their clients on sustainability, the concept of sustainability is becoming a

challenge for financial institutions. This becomes an internal obstacle and leads to misinformation of the retail client.
In addition to the difficulty of explaining the concept of sustainability to investors, the lack of a regulatory framework is also a problem in implementing the expanded MiFID II. Whereas the new MiFID is intended to be tougher on investment firms, it is flawed by its reliance on unfinished regulations (Bernal, 2022). According to one of our legal experts, "the regulation is complicated because it refers to concepts that are not in MiFID but come from the SFDR and Taxonomy". Moreover, as sustainable products are not yet available in large quantity on the market, the risk of greenwashing will depend on the communication between the firm and the client. A client who is well informed about what the market offers will not demand a high level of Taxonomy alignment and, in this sense, will not fear being misled.

As a result, the ESG MiFID II can limit greenwashing by preventing it through additional measures in financial institutions. Upstream with the issuing companies and downstream with the customer contact. On the one hand, this regulation reduces greenwashing between companies and financial institutions through the SFDR, which requires companies to disclose their non-financial information transparently (Becker et al., 2022). On the other hand, it prevents the risk of investor deception by requiring their portfolio manager to explain the principle of the regulation and by collecting their information on their sustainability preferences (I. de L., 2022). Finally, as MiFID II ESG is a European regulation that classifies sustainable and non-sustainable products, it meets the international standards that Europe needs to reduce greenwashing (de Silva Lokuwaduge et al., 2022). This is in line with the survey results, which state that one of the strengths of the MiFID II ESG is that it places Europe as a leading continent in sustainability.

The second point we will analyze will be the additional protection for the investors that MiFID II ESG brings to the market. As we have seen in the explanation of the SFDR (section 2.3.1.) and the European Taxonomy (section 2.3.2.), these regulations were made on the one hand to reach the EU's 2030 targets and, on the other hand, to protect the market from greenwashing (European Commission, n.d.a; Eurosif, 2022). Based on Regulation (EU) 202l/1253, we found that MiFID II was linked to these two new regulations in the market while matching the demand for ESG products with the supply efficiently.
One of the points made in our interviews is that MiFID is a regulation that has evolved, always responding to an additional market need. Indeed, when we go back to our literature review, we find that MiFID has been around since 2007 and has always been about helping investors have more confidence in the market (European Commission, 2021b). Although this feature is a real help for market participants who are familiar with the law, our legal experts consider that the length of the texts and their increasing complexity could be a constraint to the proper implementation of MiFID II ESG. Our results from the qualitative survey showed that one of the most significant weaknesses of the regulation is its complexity. This complexity could hurt investor protection. Indeed, one of the advisors interviewed thinks that many companies will not implement MiFID this year. This assumption is due to the lack of understanding of how to implement such regulation, the cost of its implementation, and the lack of data. We can, therefore, assume that MiFID II ESG will not have the desired effect during its first periods of application.

Moreover, although the regulation was made to protect the investor and to include him in the ecological transition, our interviewees all raised the problem of the sequencing of regulations. Indeed, MiFID II is not a stand-alone regulation, and as we have seen in the literature, the Taxonomy is incomplete (Neuroprofiler, 2022), and the SFDR has only published the first level of rules (IDS, 2021). Some respondents, then, pointed out that this lack of consistency of the sequencing between the different regulations weakens MiFID II ESG. A product cannot claim to be sustainable if it does not have the information to prove it. The lack of data has been mentioned several times. This problem disrupts the market because banks cannot offer products that meet clients' sustainable preferences. This leaves investors unsatisfied, and because of this possible pressure on financial institutions, the risk of greenwashing could be increased.

In summary, MiFID II ESG could theoretically increase investor protection, but with the underlying regulations unfinished, it could be said that investor protection will be weakened at the beginning of the application of the expanded MiFID II. We will only see its actual impact on the market in the long term. It is, therefore, tricky for this thesis to make predictions. However, given that the entire sample raised the sequencing issue, we hypothesize that until the underlying regulations are completed, MiFID II ESG will not provide additional protection to investors.

The last point, we will analyze, will be the impact of these regulations on the green transition towards which Europe wishes to move.
Based on the literature review, we have seen that Europe has made great strides in the fight against global warming. After the signing of the Paris Climate Agreement, the European Commission set up the Sustainable Finance Action Plan to connect finance to sustainability (European Commission, 2018b; High-Level Expert Group on Sustainable Finance, 2018). The only way for Europe to reach a temperature well below 2 degrees Celsius is to redirect private capital towards sustainable activities, products, and companies (European Commission, 2020b). However, for some interviewees, even if Europe is the world leader in sustainability thanks to these regulations, its competitiveness will decrease. According to Antimiani et al. (2016), there is a risk to the EU's international competitiveness due to its development of regulations to mitigate climate change. This is because carbon-intensive production sectors export to countries with less stringent regulations for polluting companies. International cooperation is needed to ensure that the EU competitiveness and efforts to reduce the amount of CO_2 in the atmosphere are not compromised. Divergent regulations on climate change are bad for global ecology and the European economy (Antimiani et al., 2016).

Furthermore, regarding the effectiveness of those regulations in increasing the number of ESG products to go to a greener economy, MiFID II ESG is not as effective as we thought it would be. In the literature review, the lack of clear standards and certifications were the only issues that made it difficult to know whether or not a portfolio had a positive impact on the environment (ISDD, 2020). The results showed that even if we implement a regulation to solve this issue, other gaps could arise. As we have noticed throughout our research, the sequencing of regulations is badly made. The SFDR being unfinished, the lack of data implies that many sustainable products cannot be considered as such. In addition, this growing demand for ESG products could eventually create a speculative bubble harmful to the market. Indeed, if supply does not meet demand, serious problems could occur in the market.

CHAPTER 6: CONCLUSION

6.1. Short summary

Given the rise of the sustainable finance movement and the crucial role of private investors in the transition to a more sustainable economy, this thesis investigates how the European Union is putting regulations in place to protect European investors from greenwashing. Specifically, the current study examines the implementation of the latest European green regulation to assess its effects on different market players.

Based on previous research on the development of sustainable finance in the market through international agreements and European green regulations, an explanation of the path Europe has taken has been made. Greenwashing is a disruptive phenomenon and could destroy the European effort to go towards a green economy. Therefore, the implementation of various regulations is essential for the good transition of Europe. A qualitative study was conducted using a questionnaire tailored to each type of institution that would be interviewed, to gather data on how the MiFID II ESG has been received in the market. The survey focused on measuring the collective sentiment on the new European regulation, and ten interviewees from financial institutions, consultancy companies, and financial regulators expressed their opinion on greenwashing and on the newly implemented MiFID II Sustainability Preferences amendments.

After in-depth qualitative analyses of the collected data, results on implementing MiFID II ESG were concluded. Three potential positive impacts of the prevention of greenwashing were found. Firstly, MiFID II ESG obliges portfolio managers to keep records of their clients' sustainability preferences in order to check whether or not the request has been met. Secondly, it provides strict standards and rules for an investment to be considered sustainable, which limits exaggerations in non-financial reporting on the corporations' environmental performance. Finally, as the regulation applies in all EU countries, MiFID II ESG allows European investors to be sure that the environmental information is structured for all EU-sourced products. However, there are three potential consequences that are negatively affecting the prevention of greenwashing. The timing and sequencing of all the regulations means that the market does not have enough data to comply with what the regulations require. Then, the complexity of the regulations in terms of implementation, means that the market may not be able to account for them. Finally, the lack of a clear guideline makes room for misinterpretations.

In conclusion, this regulation is a blessing for the financial sector in its pursuit of sustainability, but some features of MiFID will need to be adjusted to have the desired effect on the market. The European Union will need to consider the public's opinion when developing its Taxonomy so it won't lose its legitimacy. They will need to accelerate the finalization of the other regulations on which MiFID is based. This is necessary to ensure that the transition takes place without destroying stakeholder confidence, which would ultimately be detrimental to Europe's sustainable development.

6.2. Managerial implications

This study aims to help the financial sector to manage the risk of greenwashing thanks to the good knowledge of the new European regulations. The goal is to provide insights to regulatory institutions, in the first place, to understand which issues encounter the market because of MiFID II ESG and its ancillary regulations. In the second place, the present work aims to help financial institutions and advisory firms to implement in the best way possible those regulations thanks to the insight of our interviewees. If they understand the positive and negative aspects of the latest green regulations, financial actors such as banks could adapt their service or product offerings and training strategies to encourage their staff to better understand sustainability. In this way, the regulation will have the desired effect on investors and, thus, reduce the risk of greenwashing.

6.3. Theoretical implications

From a theoretical perspective, this dissertation contributes to the emerging literature about the new European green regulations and understanding the path of the EU to move towards a more sustainable economy. An important contribution is the study of greenwashing in the financial sector. Indeed, duping consumers is often discussed in the literature but investors are also confronted with this phenomenon when investing. Furthermore, this work is the first in the literature review to link the main effects of the new regulation on investor protection as well as on greenwashing, while considering the different problems caused by this regulation on the market participants who have to manage it. The results of this research shed new light on the effects of MiFID II ESG on the market and investor behavior, in particular, in the field of sustainable finance.

Firstly, the results revealed a fear of demand for sustainable investments. The requirement to ask for investors' sustainability preferences will significantly increase demand for ESG funds. The risk that demand will not meet supply could then create adverse market effects such as speculative bubbles in green assets or greenwashing. As greenwashing is the most damaging phenomenon of the European sustainable transition, the present work tries to show the related possible problems to be considered in any investment decision. Then, this dissertation also helps to propose alternatives to creating new regulations so that SFDR, Taxonomy and the expanded MiFID II can have the desired effect when implemented. In addition, the results indicate that investors with a higher level of education would be less likely to be deceived when investing.

6.4. Limitations and suggestions for further research

Although this work provides a better understanding of the new regulations that are affecting the financial sector and their role in the green transition, the results should be interpreted with caution and some limitations should be acknowledged. These limitations should be addressed in future research.

The first limitation lies in the research design of this study. Sustainable finance and especially the regulations put in place for the transition of the sector are little studied topics. For example, it was difficult to formulate interview questions because the MiFID II ESG regulation was new and because its long-term effects on the market are unknown. In addition, the number of employees working in the sustainable finance sector is still low, so it was difficult to find people who were familiar with the expanded MiFID II regulation. As a result, many stakeholders were considered unreliable or not suitable for further questioning. In order to obtain a more in-depth understanding of the effects of the new regulation on the market and on greenwashing it would have been appropriate to conduct broader research in the regulatory field.

Three suggestions for future research emerge from this limitation. Firstly, a qualitative study should be undertaken in the financial regulatory sector to better understand how MiFID II ESG was implemented. Interviewing people working at the European Commission would have provided insight into many complex aspects of the regulation. Such a study would provide a better understanding of the results of the present work. Secondly, a study could be conducted at the level of investors to see how they feel about this sudden change in their portfolio formation. It would also be interesting to know to what extent investors want their investments to be sustainable. For this research, a quantitative study would have been coherent in order to get a maximum of opinions on the sustainable preferences aspects. Finally, it is recommended that the European Commission examine the short-term effects of its new regulations before implementing them. This is to ensure that the consequences are not the opposite of what was originally intended.

Then, the sampling design of this research was chosen because it allows us to collect rich data through the discussion of the subject during the interview, but the transcription and analysis of each response is time consuming. In addition, the qualitative sampling method has important limitations. The results are not representative and cannot be generalized to any population due to the small number of actors interviewed (Malhotra et al., 2017).

Next, the socio-demographic characteristics of the sample in this study are not representative of European workers in the sustainable finance sector and, therefore, limit the generalization of the results. In addition, the participants in the qualitative survey were mainly working in Luxembourg and Wallonia, and secondarily in France and the Netherlands. In future research, it would be interesting to investigate how other EU countries have reacted to these European green regulations. As the languages used in the interviews depended on the interviewees, with the questionnaire guide available in English and French, we can use it for other countries, to have more insight about their situation as well.

Finally, it might be interesting to conduct this research to find out whether regulation over time might have an effect on the returns and costs of sustainable investments. Indeed, in one of our interviews, the discussion was about the price of a sustainable asset compared to a non-sustainable asset given their availability on the market. For this matter, a study in the financial sector should be conducted to add an additional parameter to attract investors to buy sustainable assets.

Appendix 11 - Descriptions of the interviewees' companies

Moonshot

Moonshot is a sustainable investment consultancy that supports management companies, banks, insurance companies and mutuals on a daily basis in order to help them implement certain sustainable constraints and make concrete commitments for the future (Moonshot).

Website : https://www.moonshot.run/

Sopiad

Sopiad is a spin-off that provides services with its SAFIR solution to investment firms, private banks and financial advisors in order to get an overview of what investors want in investment preferences (Sopiad).

Website : https://www.sopiad.com/

Deloitte

Deloitte is a British multinational firm, which specializes in audit, consultancy, financial advices, legal and tax advices (Deloitte).

Website : https://www2.deloitte.com/be/en.html

Banque de Luxembourg

Banque de Luxembourg is a Luxembourg private bank offering responsible wealth management solutions (Banque de Luxembourg).

Website : https://www.banquedeluxembourg.com/fr/bank/bl/homepage

PwC

PwC or PricewaterhouseCoopers is a UK-based global network of firms specializing in audit, accounting and advisory services with a focus on business sectors (PwC).

Website : https://www.pwc.com/

NewB

NewB is a Belgian cooperative bank which still only manages current accounts (NewB).

Website : https://newb.coop/fr

Credit Suisse

Credit Suisse Group is one of the leading banks in private banking and wealth management, with strong investment banking capabilities (Credit Suisse).

Website : https://www.credit-suisse.com/ch/fr.html

CSSF

The Commission de Surveillance du Secteur Financier is a public institution which supervises the professionals and products of the Luxembourg financial sector (CSSF).

Website : https://www.cssf.lu/en/

Triodos

Triodos is a bank whose mission is to contribute to a society that promotes quality of life and puts people at the heart of its concerns. It builds all its activities around 3 main themes: social, environmental and cultural (Triodos).

Website : https://www.triodos.be/

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Executive summary

In the face of climate change, our policies must act to prevent an unprecedented crisis. To this end, the European Union is committed to a series of international agreements. The most important of these is the Paris Agreement, which aims to limit global temperature increase to 1.5 degrees Celsius by 2030. To achieve this agreement, public funds are not enough to support the needed investments to make our society more sustainable. Private investors are, therefore, called upon to contribute to the transition of our economy towards a more sustainable model. However, this change in investment flow puts a lot of pressure mostly on polluting companies. Unfortunately, a change of business model is not easy to implement and it leads some of them to lie about their environmental performance. This disruptive phenomenon, also known as greenwashing, hinders the transition of our economy. In response to this issue, the European Union has put in place some regulations known as the SFDR, the European Taxonomy and MiFID II ESG to push companies to disclose more information about their sustainability and limit deceiving investors. Sustainable finance is a necessary asset to reach those objectives. These new green regulations' goal is to focus on reducing carbon emissions into the atmosphere.

Despite the EU's efforts to make finance sustainable, the timeline of its new regulations' enforcement is affecting the market. Therefore, the purpose of the present work is to determine their impacts on greenwashing and on the market players who have to integrate them. Furthermore, this study focuses on the latest law implemented since August 2022, which is called MiFID II ESG. Through a qualitative survey, participants from the financial sector gave us insight regarding their regulatory journey. As a result, we concluded that those regulations are a major step toward sustainable finance despite the presence of possible misinterpretations which may create a build-up of false information and, thus, fuel greenwashing.

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