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The UK FCA's anti-greenwashing rule: ignore it at your peril

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As the demand for sustainable products and services grows, so does the risk of "greenwashing" – where firms make misleading sustainability-related claims about their products or services. The Financial Conduct Authority's (FCA) anti-greenwashing rule (AGR), which came into force on 31 May 2024, aims to combat this. Firms should understand the way the AGR interplays with existing FCA requirements, and should be mindful of certain aspects of the rule to ensure proper compliance with it. They should also be aware that, with the AGR, comes new risks of litigation and regulatory enforcement action.

A recap of the AGR

The AGR can be found in the new Chapter 4.3 of the Environmental, Social and Governance Sourcebook (ESG) in the FCA Handbook. We summarised the rule in a previous article but, to recap, the new rule (ESG 4.3.1R) will require any FCA-authorised firm that:

- communicates with a client in the UK in relation to a product or service; or
- communicates a financial promotion to, or approves a financial promotion for communication to, a person in the UK,

to ensure that any reference to the sustainability characteristics of a product or service is:

- consistent with the sustainability characteristics of the product or service; and
- fair, clear and not misleading.

In its accompanying guidance (FG24/3) the FCA makes clear that it expects firms to ensure that any communications they make which include sustainability-related claims must be:

- correct and capable of being substantiated;
- clear and presented in a way that can be understood;
- complete (in that they should not omit or hide important information and should consider the full life cycle of the product or service); and
- be fair and meaningful in relation to any comparisons to other products or services.

How does the AGR interplay with existing regulatory rules?

The FCA points out that various sections of its Handbook already require most firms to ensure the information they communicate is "fair, clear and not misleading". This includes the Principles for Business - specifically Principle 7 (a firm must pay due regard to the information needs of its clients and communicates information in a way which is clear, fair and not misleading) - that apply, in whole or in part, to most firms. There are other requirements in the Handbook which elaborate on what "fair, clear and not misleading" means in specific contexts: for example, COBS 4.2 adds further prescription around financial promotions for investments, and CONC 3.3 adds detail for consumer credit. Firms subject to the Consumer Duty, Principle 12 (a firm must act to deliver good outcomes for retail customers), will also need to consider the Duty – specifically the Consumer Duty outcome relating to "consumer understanding" (PRIN 2A.5).

As to how these existing rules interplay with the new AGR, in its guidance the FCA expressly says that the AGR is intended to "complement and be consistent with these rules", and "is not a substitute for, and is not intended to override, any other rules in the Handbook" (para 2.11 of FG24/3).

In addition, other regulatory bodies in the UK, such as the Advertising Standards Authority (ASA) and the Competition Markets Authority (CMA), already have guidance on greenwashing and green claims being made about a product or service. The FCA has collaborated with the CMA and ASA to ensure that its guidance is consistent with theirs. And firms are also subject to other legislation and guidance that may be applicable, such as existing consumer protection laws.

Aspects of the AGR of which firms should be particularly mindful

Firms should pay particular regard to the following aspects of the AGR:

- *The AGR covers social-washing, as well as greenwashing*: In its guidance the FCA clarifies that the reference to "sustainability characteristic" in the AGR refers to both the environmental and/or the social characteristics of a product or service, so both greenwashing and "social-washing" (i.e. when firms make misleading claims about their social responsibilities) are within scope of the rule (para 2.2 of FG24/3). (The FCA further explains that the "G" of ESG – "Governance" – is not covered as the FCA considers governance to be an enabler of environmental and/or social outcomes, rather than an end in itself (para 2.2 of FG24/3)).

- *The AGR covers images, as well as words. It's the overall impression that matters*: The FCA clarifies that communications which are caught by the AGR include statements, assertions, strategies, targets, policies, information and images relating to a product or service (para 2.7 of FG24/3). Therefore, as well as the words they use, firms should be careful about the images they employ, and the overall impression that is being conveyed. In the guidance the FCA gives the example of a firm which has a picture of a rainforest on its webpage about savings with the words "sustainable savings" – but only one of the savings products listed is a "green savings account". The FCA says that the image coupled with the text may give consumers the overall impression that *all* savings products support sustainable outcomes (example 4 on page 10 of FG24/3).

- *Claims the firm makes about itself may form part of the representative picture of a product or service*: The FCA points out in FG24/3 that while the AGR relates to products and services, it reminds firms that the CMA and ASA's guidance, and FCA Principles 6 and 7 or, as relevant, the Consumer Duty (Principle 12 and the rules in PRIN 2A), apply to sustainability-related claims that a firm may make about itself as a firm (para 2.15 of FG24/3). That said, the FCA points out that firms should consider whether information about the firm itself may be considered part of the "representative picture" of a product or service, and to ensure that the overall picture being conveyed is fair, clear and not misleading (para 2.32 of FG24/3).

- *Firms should not take a cookie-cutter approach to communications*: The FCA says that firms should consider whether the information they are providing is useful for the intended audience. Where a claim is being communicated to a professional client, firms may not need to include the same information or present it in the same way as they would for a communication addressed to a retail client (para 2.23 of FG24/3). In short, firms need to adapt their communications to suit their audience.

- *Third party due-diligence may be required*: Where firms rely on third parties for information, the FCA says they should consider the appropriateness of relying on data, research, analytical resources and other information provided by third parties to substantiate the claims they are making (page 15 of FG24/3). They may want to undertake some due diligence on this information.

- *Compliance with the AGR is not a one-off obligation*: The FCA makes clear that firms should ensure that their sustainability-related claims remain compliant with the AGR on an ongoing basis, for the full life cycle of the product or service (paras 2.20 and 2.31 of FG24/3).

- *There remains uncertainty over exempt promotions*: It is not clear whether the AGR will apply to financial promotions which are exempt under the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005.

What are the regulatory enforcement and litigation risks of greenwashing?

Firms have hitherto been exposed to the risk of regulatory enforcement action and litigation for greenwashing under existing regulatory and legal frameworks. The AGR has provided an additional, explicit line of attack.

Regulatory enforcement risk

- Whilst, as set out above, the FCA already has rules in place which it can use to bring enforcement action for greenwashing, the AGR provides - in the FCA's own words - an "explicit rule on which to challenge firms if we consider they are making misleading sustainability-related claims about their products or services and, if appropriate, take further action" (para 1.4 of FG24/3). The FCA may therefore bring enforcement action against firms who breach the AGR and any other FCA Rules and Principles that require information to be fair, clear and not misleading - plus, where relevant, the Consumer Duty. The FCA can impose fines, suspensions, restrictions or prohibitions, or require the firm to withdraw or amend any misleading claims.

- In circumstances where the misleading statement is made knowingly or recklessly, the FCA could employ its criminal enforcement powers under the Financial Services Act 2012 against the firm and its directors.

- The FCA can impose an industry-wide redress scheme on firms who have failed to comply with the AGR, causing loss or damage to consumers. (The FCA can only use this power where the consumers have a private right of action under section 138D of the Financial Services and Markets Act 2000 (FSMA) – see below).

Litigation risk

- There may be claims by private persons (in broad terms, individuals or other non-corporate persons) who suffer loss as a result of breach of the AGR under section 138D FSMA, which can be brought alongside other causes of action (such as misrepresentation or breach of contract – see below). Both COBS 4.2 and CONC 3.3 provide a "reasonable steps" defence to an action for damages under section 138D based on their contravention. There is no similar defence in the AGR but given the FCA has said that the AGR "is not a substitute for, and is not intended to override, any other rules in the Handbook where firms may be subject to fair, clear and not misleading rules in specific circumstances" (para 2.11 of FG24/3) it would seem arguable that, where COBS and CONC are also engaged, this defence may still apply.

- And, of course, greenwashing litigation may also arise where misleading sustainability-related claims are included:

    - in a prospectus or listing particulars for securities - or in information reported by issuers of securities, such as annual reports. Investors may bring litigation under section 90 FSMA or section 90A FSMA, respectively.

    - in a contract, which may precipitate litigation by contractual counterparties for breach of contract.

    - in other statements, which may lead to litigation by investors, consumers or shareholders for misrepresentation or negligent misstatement.

    - in directors' reports, which may prompt litigation by companies (or derivative actions by shareholders on behalf of companies) against directors under section 463 of the Companies Act 2006.

What is the FCA's enforcement approach likely to be?

Given firms should already be ensuring any sustainability-related claims they make about a product or service are "fair, clear and not misleading" - and given implementation of the AGR was delayed (it was originally intended to apply when the Policy Statement on Sustainability Disclosure Requirements was published in late November 2023) - the FCA is likely to have little patience for any firm found to be committing greenwashing or social-washing, and is therefore likely to be proactive in terms of enforcement.

If you would like to discuss any of the issues raised in this article, please feel free to get in touch with any of the contacts listed.

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