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FCA reveals it is pursuing a climate-related investigation

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In a historic first, last month, the Financial Conduct Authority (FCA) confirmed that it had opened a climate-related enforcement investigation against a company. This information was provided in response to a freedom of information request by legal activist organisation ClientEarth. It represents a key milestone on the path to joining regulators in the US, Germany and Australia, in enforcing climate-related obligations.

What do we know?

This is a welcome step, but the exact nature of the investigation is unclear. Information released by ClientEarth indicated nothing more than that the investigation concerns “climate-related issues”.

The FCA has implemented new rules aimed specifically at misconduct connected to products environmental, social and governance (ESG) – its ‘sustainability disclosure and labelling regime’ (widely known as the ‘greenwashing rules’). However, these came into force on 31 May 2024, and its associated guidance only one month earlier. The regulator is likely to give the market time to understand and implement its expectations. Consequently, an investigation concerning a breach of these rules seems unlikely.

A more probable hypothesis is that the FCA is using its wider regulatory tools, such as those concerning mis-selling or systems and controls and aiming them at climate-related misconduct. The regulator has already been active in this area, and has warned the market of possible enforcement action. Most recently, in March 2023, those providing ESG benchmarking were reprimanded over poor disclosure of methodologies following a review and were warned of further action in this area. There have also been similar warnings in respect of the design, and disclosure of information to clients, of ESG and sustainability focussed investments. The market has, therefore, been on notice for some time of potential enforcement action.

It seems unlikely that the FCA will release more information any time soon. According to ClientEarth, it was only following significant delay and a complaint to the Information Commissioner’s Office that the FCA disclosed that it had opened a single climate-related investigation.

This coyness is surprising: the FCA has recently issued a controversial consultation seeking the implementation of broader rules permitting publication of the details of its active investigations. This was on the ground that it would ensure better protection of consumers, increase public confidence and issue timely messages to the market. One might consider that informing the market, and consumers, of climate-related enforcement investigation would fall squarely within those objectives.

The broader context

The regulator has publicly stated its ambitions to make ESG a key focus of its work. At the same time activist organisations are using legal challenges to seek to influence the conduct of government agencies and regulators in relation to ESG issues. Recent examples include legal actions against the National Crime Agency by the World Uyghur Congress, in respect of criminality in supply chains, and ClientEarth's own recent unsuccessful judicial review of the FCA earlier this year, challenging the approval of a listing prospectus of an oil and gas explorer on the ground that it did not adequately describe the climate risks it posed. It seems that the FCA is likely to come under increasing pressure to deliver enforcement actions in this area.

On the other hand, the UK's new Labour government has been elected on a manifesto promising "a pro-business environment, with a competition and regulatory framework, that supports innovation, investment, and high-quality jobs". This sentiment is echoed in the FCA's new listing rules, issued on 11 July 2024 and which present a simplified regime, which designed to attract more listings to London. These have been criticised for reducing corporate governance and the power of shareholders to hold listed companies to account, a key lever for shareholders concerned with ESG issues.

Satisfying those seeking ever-tighter regulation while also fostering an environment for growth is a tricky task. Whether the FCA can ride both horses without accident remains to be seen.

Looking ahead

Global climate-related enforcement will continue to ramp up. As a result, related enforcement risks will be front of mind for larger international multi-regulated companies. This recent announcement concerning the FCA suggests that the same can be expected in the UK. Similarly, it is likely that as the tool available to the regulator increase, so will the volume of enforcement action.

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