# Exploring the potential for undermining effects of greenwashing on the relationship between transparency and accountability in the context of the Sustainable Finance Disclosure Regulation

*By Giacomo Bauer*

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# Abstract

Within the field of global environmental governance, there has been an ongoing debate challenging the assumption that increased transparency will lead to increased accountability. However, transparency's transformative potential has not consistently generated effective accountability mechanisms across contexts.  A potential undermining effect for this relationship is greenwashing, whereby actors selectively present information to appear transparent while deceiving the accountability mechanism intended to hold them to account. The Sustainable Finance Disclosure Regulation requires information disclosure from financial institutions, to allow investors to make decisions that align with their sustainability preferences. Greenwashing poses a potential risk to the relationship between transparency and accountability within this context. Hence, the research objective is to examine the potential for transparency and accountability to be undermined by greenwashing opportunities within the SFDR. Using a case-study approach, a document analysis of the SFDR and interviews with sustainable finance experts were conducted. The results from the document analysis illustrate the expected greenwashing possibilities, with the interview analysis providing insight into the implemented greenwashing possibilities. A comparative cross-analysis illustrated that greenwashing mechanisms are able to shape transparency, through information disclosure, in a way that undermines the efficacy of the accountability mechanisms within the SFDR. Transparency is insufficiently developed within the framework and accountability mechanisms are not *meaningfully* present. The consequential prevalence of selective disclosure and decoupling practiced by financial institutions indicates the extent to which the link between transparency and accountability remains *assumed* rather than *existent*. Greenwashing mechanisms are therefore able to shape transparency, through information disclosure, in a way that undermines the efficacy of the accountability mechanisms within the SFDR.

# Introduction

Our modern economic paradigm has placed our planet's climate and resources in a paralyzing state of crisis. As the critical enabler for economic activity, finance plays a pivotal role in the development of our climate crisis. To avoid it, transitioning to a more sustainable financial industry has been at the forefront of the industry's development. Sustainable finance has emerged as a solution for the transition and has grown exponentially in recent years. It aims to make finance sustainable by integrating environmental, social, and governance (ESG) factors into financial decision-making. The market for sustainable finance products has seen significant diversification and growth, with many products proposing novel ways of promoting sustainability. Coincidentally, there has been a rise in ESG funds, which are investment products that evaluate companies on their management of ESG issues. Substantial monetary inflows have illustrated the investment shifts that favor sustainable products. The industry has ballooned drastically in recent years, allowing the titans of investment management to claim that up to $35trn in assets are monitored using ESG methods (The Economist, 2022). The proliferation of products and funds has also been accompanied by supporting industries such as ESG data analytics companies. Their services allow investors to be more informed about their investment choices. The growth of the sustainable finance industry has necessitated supporting action from governments. By providing subsidies, tax incentives, or grants to encourage investments in sustainable projects, governments can make sustainable finance more economically viable. European governments have attempted to support the transition to sustainable finance through their regulatory bodies, leveraging their power to create frameworks for this novel type of investment.

In order to support the transition, the EU has published the EU Action Plan on Financing Sustainable Growth, a comprehensive set of policies aimed at leveraging financial markets for sustainable growth (Möslein, 2018). The plan outlines a number of measures to encourage the development of sustainable financial products, as well as including sustainability considerations in investment decisions (Möslein, 2018). Integrating ESG factors in investment decisions leverages private finance to achieve key European policy objectives. The main objectives include (1) reorienting capital flows towards a more sustainable economy (2) mainstreaming sustainability into risk management (3) fostering transparency and long-termism (Gonzalez, 2021). Meeting these objectives is proposed to occur through the establishment of three key regulations: the EU Taxonomy Regulation, the Corporate Sustainability Reporting Directive (CSRD), and the Sustainable Finance Disclosures Regulation (SFDR). Combined, these aim to engage various actors within the sustainable finance space to achieve the policy objectives. The SFDR requires financial market participants and advisers to disclose information on how ESG risks and opportunities are integrated into their investment processes and decision-making (Brühl, 2021). Its fundamental aim is to increase transparency on ESG issues to ensure that

financial market participants are able to fund sustainable growth (Bengo, Boni and Sancino, 2022).

Yet the implementation of the transition, despite the attempts of investors, financial institutions, and regulators' intentions for finance to become more sustainable, has faced significant barriers. Investors require reliable and consistent data on the ESG performance of companies (Whelan et al., 2021). However, unlike credit scores, ESG scoring of the same company varies widely among different providers (Rogge and Ohnesorge, 2022). This is in part driven by an insufficient amount of companies disclosing ESG data, and those that do lack consistency in their reporting practices. Unsurprisingly, investors struggle to make reliable decisions based on a lack of information, reducing the efficacy of the transition. ESG data is not widely available, as there is a lack of regulation to necessitate companies to disclose any information regarding ESG issues. Without any commonly accepted standards and metrics, to delineate what constitutes 'sustainable' practices or investments, the transition faces a further significant barrier. The lack of comparability and consistency in information leaves investors without a solid foundation to justify investment decisions. Furthermore, inconsistent information provides an opportunity for greenwashing within sustainable finance products. Institutions selling sustainable finance products would in the most basic definition of greenwashing be communicating a position or achievement on environmentalism without fulfilling the basic environmental criteria to substantiate their claim.

To mitigate the risk of this process occurring, investors and activists have been continuing calls for transparency and accountability. A common argument to validate the call for transparency is that an increase in information allows for more aligned decision-making with the values of the decision-maker. In this case, a higher degree of transparency allows investors, consumers, and regulators to leverage the data they need to assess a financial institutions sustainability performance accurately. Financial institutions that provide information allow investors who intend on purchasing sustainable finance products to decide with more clarity what products to acquire (European Union, 2021). Being able to compare is essential for stakeholders in sustainable finance because it allows for better-informed decisions, ultimately redirecting capital toward the desired sustainable practices. The practice of disclosing information regarding their sustainability performance leaves financial institutions open to the scrutiny of end investors. This could be described as an accountability mechanism, as it provides end investors leverage through the use of information. Transparency therefore offers the possibility for accountability to place consequences on environmentally damaging financial institutions. Accountability is meant to ensure that the institutions face consequences for their actions, particularly when these actions have negative impacts on society or the environment. Mechanisms of accountability, such as enforcement by regulators, are meant to encourage companies to improve their sustainability performance in order to not face consequences.

**Problem statement**

Despite the calls for transparency, its effectiveness as a mechanism to change sustainability behavior is still a matter of debate within academic literature (Mason, 2008; Schleifer, Fiorini and Auld, 2019). While there is a plurality of viewpoints on the wider debate, the key positions can be umbrellaed under two positions. On the one hand, transparency is viewed as having transformative potential, whereby information alone drives changes in the behavior of stakeholders. As a result, through the disclosure of information, stakeholders can be held to account for the environmental outcomes they generate. On the other, transparency is viewed as contextually constrained. The underlying mechanisms of transparency are not value-neutral and are influenced by the context in which the stakeholders engage.

Proponents of transparency transformative potential view transparency through information disclosure as a functional tool, since there is a persuasive assumption that more information on sustainability issues allows for improved decision-making (Gupta, 2010). Within this assumption is the conceptualization of information in a value-neutral way, moving the point of focus away from who and why information is disclosed to what information is being disclosed. Expanding information is therefore seen as an effective way of achieving sustainability goals since the information itself should be sufficient motivation for actors to change their behavior. Applying this to the context of organizations; using disclosed information effectively would allow stakeholders to make more informed decisions, applying context-based strategies to change the behavior of the disclosing organization where necessary (Dingwerth and Eichinger, 2010). It is hypothesized that information disclosure on sustainability data can change internal behavior at the disclosing organization, improve how markets function, and identify regulation gaps for governments (Clarkson et al., 2006). There is some experimental evidence to show that this is the case. The results of a scenario-based experiment testing how financial, unlinked financial and nonfinancial, and integrated information affect the outcomes of investment decisions found that an integrated information basis leads to decisions that generate higher sustainable value creation (Esch, Schnellbächer and Wald, 2019). Disclosed information prepared for external communication can help companies establish sustainable decision behavior for internal purposes (Esch, Schnellbächer and Wald, 2019).

This neutral view of transparency's potential is challenged by scholars who view the underlying mechanisms of transparency as influenced by their contextual variables. In a seminal introduction to the debate on transparency in global governance, Aarti Gupta concludes that transparency is a defining feature of current and future politics and remains a central site of political conflict and power struggles (Gupta, 2010). Whether or not transparency can be used to transcend these issues depends on the context in which the mechanism is situated (Mason, 2008). This conceptualization is meant to reflect that transparency in and of itself is insufficient for changing the outcomes of political conflict and power struggles. It can range from being a tool that simply reflects power structures to being a lever for behavioral change, depending on the

context in which it is applied (Gupta, 2010). Within European environmental governance, transparency has increasingly been considered a default choice to handle environmental issues, leading to direct implications as to whose and which objectives are achieved (Gupta, 2010).

The debate surrounding transparency and accountability is increasingly important, as more policies are being enacted by the EU to reach their environmental targets. While there are a variety of factors that influence the relationship, there has been a lack of research into the effect of a particular factor: greenwashing. Taking an essentialist definition of greenwashing, the concept is commonly defined as the difference between an actor's symbolic actions and their substantive actions within their self-defined sustainability approach (Siano et al., 2017). In other words, actors communicate a position or achievement on environmentalism without fulfilling the basic environmental criteria to substantiate their claim. Greenwashing can conceptually be seen as opposite to forms of transparency, while still appearing to fulfill the requirements of accountability. Since actors communicate a position or achievement on environmentalism without fulfilling the basic environmental criteria to substantiate their claim, they falsely claim accountability benefits yet actively undermine the concept of transparency. As described above, when actors misunderstand demands and selectively communicate information they undermine transparency and consequently accountability. Hence greenwashing can be viewed as a tool for actors to be perceived as accountable while manipulating the contextual variables of transparency in their favor.

In what contexts transparency leads to accountability and the role that greenwashing has with respect to both concepts remains a gap in academic literature. So far transparency and accountability have been studied in a variety of contexts within environmental governance. The focus within the context of sustainable finance has been on evaluating the efficacy of transparency and accountability mechanisms on voluntary ESG disclosure mechanisms (McBrayer, 2018). However, given the introduction of mandatory regulations such as the SFDR, there is an absence of research on the transparency and accountability mechanisms of mandatory ESG disclosure mechanisms. Furthermore, the link between transparency and accountability is not as straightforward as suggested in current discourse (Gupta, 2010). A possible factor that can influence the relationship within the context of sustainable finance is the phenomenon of greenwashing. The extent to which greenwashing is able to undermine the capacity for transparency to lead to accountability has not been studied within the context of sustainable finance. By developing a comprehensive set of standards, the EU can leverage regulation to establish robust frameworks to embed transparency and accountability in sustainable finance. With the emergence of the SFDR to combat greenwashing through transparency mechanisms, the novel EU regulation is well-placed as a starting point to examine the relationship within the context of sustainable finance.

**Research objective**

As sustainable finance regulation is emerging within the European union, it becomes increasingly important to understand factors that influence its aims. One of the central aims of sustainable finance regulation is fostering transparency and long-termism, leveraging the increase in disclosed information to evaluate stakeholders' sustainability performance. Yet the link between transparency and accountability is mostly assumed and has not been systematically studied within the context of sustainable finance. As a variety of factors influence this relationship, building an understanding of how specific ones influence the outcomes is necessary. A concurrent trend to the increase in regulation is the proliferation of sustainable finance products and funds. As investors lack clarity on what products are truly sustainable, the opportunity for greenwashing has drastically increased. Greenwashing can be conceptualized as appearing to be accountable while avoiding transparency. Hence understanding its influence on the relationship between transparency and accountability within sustainable finance is necessary. This thesis will therefore examine the role of a mandatory measure, such as the SFDR, in promoting transparency and mitigating greenwashing. The research objective of this thesis is to examine the potential for transparency and accountability to be undermined by greenwashing opportunities within the SFDR. Bridging the knowledge gaps identified in the literature will be done by attempting to answer the following research question:

*"How is the potential of transparency and accountability undermined by greenwashing opportunities within the SFDR?"*

This research will utilize a case study approach using interviews with sustainable finance experts to answer the research question. Using a case study approach was chosen, as it is particularly well adapted to investigate complex phenomena within their real-world context. The approach is beneficial when the boundaries between the phenomena and the context are not clearly evident, which is the case for the SFDR within the context of sustainable finance. Furthermore, using a case study approach allows for an in-depth understanding of the situation and meaning for the stakeholders involved. Given that prior research upon which to build a theoretical foundation has not been systematically built, using a case study approach is most fitting. This research will take an exploratory approach as the interplay between transparency, accountability, and greenwashing in the context of sustainable finance has not been previously examined. Through the case study approaches flexibility, developing an understanding of the dynamics present within previously unexamined contexts becomes feasible.

Following this introduction, the thesis is structured into several chapters that are dedicated to specific aspects of the research. Chapter 2 discusses the theoretical framework, which extensively reviews the literature on transparency, accountability and greenwashing. It also further examines the links between the concepts to explore the plethora of understandings. Chapter 3 discusses the methodology applied for the research to examine the topic through the

lens of sustainable finance experts. Chapter 4 discusses the current state of sustainable finance and its regulation within the European Union. It delves into its development path and specifically analyses the components of the SFDR. Chapter 5 reviews the evidence and provides a discussion and analysis of the interviews. Chapter 6 concludes the findings and provides a synthesis of the thesis to answer the research question. Further avenues for research are also presented. Combined, these chapters aim to provide a nuanced understanding of the relationship between transparency, greenwashing, and sustainable finance in the European context.

# Theoretical framework

## Introduction

In this chapter, we delve into the theoretical framework that connects the concepts of transparency, accountability, and greenwashing. Transparency, which involves increasing the availability and flow of information to the appropriate destinations, is a multifaceted concept that operates within relational and normative contexts. The mechanisms of transparency are only as effective as the context in which it is used, particularly in relation to both other concepts. Accountability is a complex concept that is rooted in normative and relational aspects and involves making judgments about behavior and imposing sanctions or consequences. As a mechanism, accountability arises from the obligations between two actors, where judgments and consequences come into play. To symbolically fulfill accountability requirements, actors can choose to engage in deceptive practices. Known as greenwashing, this practice refers to the dissonance between an actor's symbolic actions and their substantive actions within their self-defined sustainability approach. It involves selectively disclosing less harmful environmental impacts to create an impression of transparency while withholding information about more damaging aspects. At its core, greenwashing entails falsely presenting the fulfillment of normative environmental standards. This chapter will explore the definitions and interconnections among transparency, accountability, and greenwashing, Understanding the complexities and challenges surrounding transparency, accountability, and greenwashing is essential for effective environmental governance and understanding the contexts in which they emerge.

## Transparency

The paragraphs below will be subdivided into two sections. Firstly, they will deal with the theoretical foundations of transparency and the contested nature of its definitions that have challenged that transparency is a value-neutral concept. Secondly, the mechanisms behind transparency, i.e. in which ways information disclosure is thought to be effective, will be looked at.

### Theoretical Foundations

Transparency within environmental governance is increasingly seen as part of the solution for complex challenges in the integrated fields of economics, politics, and ethics (Gupta and Mason, 2014). The bountiful transformative effects that transparency is meant to produce come from the privileged position it holds within societal discourse. Gupta (2008) identifies that transparency has become a predominant method in global environmental governance, emerging in information disclosure-based methods such as reporting initiatives. Similarly, information disclosure is viewed in this thesis as the operationalization of transparency, albeit that transparency has a plurality of forms in which it emerges. Often associated with openness and reduced secrecy, transparency is thought of increasing the availability and flow of information to the right destinations (Florini, 2002). Reducing these information asymmetries through transparency is particularly timely, as we are currently living through what many consider the "information age", where access to information is abundant. This embeds current discourse on the multiple perceived benefits of transparency, including the empowerment of weaker actors and reduced informational asymmetries between powerful and less powerful actors (Gupta and Mason, 2014). Within environmental governance, these perceived benefits can be seen in the disclosures that companies or states make on their environmental performance. For example, companies and states frequently set net-zero targets whereby they lay out plans for achieving sustainability objectives. This allows weaker actors to scrutinize their performance through access to information (Rogelj et al., 2021). Companies also use increased information disclosure within supply chain reporting mechanisms, which should empower external actors to evaluate companies' environmental performance (Searcy et al., 2022). These examples reflect the liberal institutionalist approach to environmental governance. From this perspective, institutions are able to solve environmental problems through cooperation between actors and *institutionalization* of norms to change actors' behaviors (Mason, 2008). Transparency slots easily into the discourse of liberal institutionalism, as exchanging information becomes a lever to overcome barriers in environmental governance (Mason, 2008). Underpinned by a rational-choice theory of actors' behavior and decision-making, liberal institutionalism assesses environmental problems to suffer from a lack of transparency, whereby improved information disclosure would lead to rational actors changing their behavior. Yet, despite the substantial increase of information on environmental problems, and actors' access thereto, few substantial gains have been made through increased transparency. So does transparency live up to its ideal?

Defining transparency within environmental governance becomes complicated, as it remains a contested concept with different meanings in different contexts (Gupta & Mason, 2014; Ball, 2009; Fox, 2007). In its most basic sense, transparency is the reduction of secrecy and generation of openness, which etymologically signifies the *rendering visible* and seeing through of something (Florini, 2002; Michener and Bersch, 2013). In these definitions lies hidden a dual understanding of transparency; as both a process and a value. In other words, transparency can be understood as the process of rendering something visible, where the onus lies on the *something*. It can also be understood as an end in itself, where the onus lies on the *transparency* of the something being rendered visible. Emblematic of this distinction is a *call for transparency*, where there is not a call for specific information on a given issue but for *the process* of information on a specific issue to be rendered visible. Transparency continues to be a contested concept, as essentialist definitions miss a core conceptual element. The relational and normative dimensions of the given issue, *what* is being made transparent, as well as for *whom*, and *how* reflect the extent to which transparency can only be understood through the context in which it emerges (Gupta & Mason, 2014).

By viewing transparency through the liberal institutionalist approach to environmental governance, one would be unable to include contextual factors in the efficacy of transparency to fulfill its potential. Inadequacies in the effectiveness of disclosure would be more readily attributed to institutional design or bureaucratic capacity of actors, implying that transparency itself had not reached what it is capable of doing (Gupta & Mason, 2014). A contextually embedded understanding of transparency acknowledges the normative and political context in which information disclosure occurs. Labeled as the *critical transparency studies* perspective, this theoretical groundwork includes approaches that (1) problematize transparency and governance by disclosure, (2) account for the historicity and sociopolitical embedding of transparency and disclosure practices and (3) acknowledge the unavoidable normativity of transparency and disclosure (Gupta & Mason, 2014). Analysis that takes these approaches reveals how transparency arrangements, like voluntary disclosure initiatives, are embedded in a neoliberal understanding of environmental governance (Gupta, Boas and Oosterveer, 2020). By broadening the analytical scope and questioning key assumptions, a critical perspective suggests that contextual factors play a central role in understanding whether and why transparency's transformative potential is realized.

The underlying relational and normative dimensions to transparency reflected in this perspective consist of central elements which characterize the contextual nature of transparency which are; who is to be transparent, to whom, about what, and to what end. The first two elements reflect the inherently relational dimension of transparency (Fox, 2007, Mason, 2019). Transparency contains a leading assumption that one actor obliges another to render visible information on a given issue. This relational dimension has previously been identified within the political context

of global environmental governance. Here, transparency is viewed as information that is disclosed between two state-based actors. Hence, transparency becomes part of a political process influencing the relational dimensions between the actors involved. Which falls in line with the growing body of literature on multilevel environmental governance (Yi et al., 2019). With a focus on multiple types of actors, such as civil society, non-governmental organizations, businesses, and governments, the relational dimension of transparency reflects the complexities of current global governance. Who demands and supplies transparency has therefore become multi-directional, going beyond institutionalized actors such as nation-states (Michener and Bersch, 2011). This increased complexity places more onus on actors to disclose information with multiple actors in mind, requiring more nuanced conceptualizations of actors' information demands (Mason, 2019). To whom one feels obliged to be transparent on what is therefore a novel area of political contestation. Managing these expectations becomes a strategic process of power relations. This further solidifies that transparency is not a value-neutral, but rather relationally value-laden, ground for political contestation (Mason, 2019).

Given the strategic process by which actors relationally manage issues that oblige transparency, it becomes further relevant to assess the motivations behind actors' disclosures. Tienhaara (2019) outlines a typology that encapsulates the rationales and agendas which underpin actors' usage of transparency. Motivations can vary drastically regarding why actors disclose information. The typology outlined by Tienhaara suggests multiple types of transparency; conventional, deliberative technocratic, disciplinary, and disruptive transparency. These are briefly outlined here.

**Table 1.** Varieties of transparency.

| Type of Transparency | Ideological Underpinnings | Transparency for Whom? | Mechanism | Transparency to What Ends? |
|---|---|---|---|---|
| Conventional | Liberalism | Citizens | Facilitate accountability of decision-makers | Better/less corrupt governance |
| Deliberative | Liberalism | Citizens | Facilitate deliberation and participation in decision-making | Better/more legitimate governance |
| Technocratic | Rationalism | Experts | Increase efficiency & effectiveness of decision-making | Better governance |
| Disciplinary | Neoliberalism | Market actors | Facilitate market transactions (consumption, investment and trade) | Capital accumulation |
| Disruptive | (Cyber-) Anarchism | Citizens | Obstruct secretive communication amongst the powerful | Abolition of hierarchy |

Source: Tienhaara (2020)

First, conventional transparency assumes that some actors have the right to hold others to a set of standards, whereby the relationship between transparency and accountability would be self-evident. Supporters of conventional transparency view the disclosure of information as empowering the weakest members of society, leveraging the opportunities that transparency provides to create accountability. Second, deliberative transparency encapsulates the notion that deliberation, i.e. the exchange of information, leads to (democratic) outcomes. In the context of transparency, information disclosure should lead to improved deliberation which in turn leads to higher accountability between relevant actors. Third, technocratic transparency is based on the

idea that policymakers must provide experts with access to information to enhance the efficiency and effectiveness of governance outcomes. Fourth, disciplinary transparency involves information disclosure for market actors to facilitate market transactions and discipline the disclosing actors to the demands of the market. It empowers market actors such as consumers, producers, or investors and occurs for example through product labeling. Finally, disruptive transparency is information disclosure strategically intended to interrupt the secret information of powerful institutions to disrupt political realms.

Similar to the typology outlined by Tienhaara, which encapsulates the rationales and agendas which underpin actors' usage of transparency, Gupta and Mason (2016), offer a typology of their own. Through their lens engaging with transparency, or information disclosure, could follow one of four different rationals. First, a democratization rationale, with transparency intending to create accountability and democratic participation, based on the right to know. Second, a marketization rationale, where transparency engages market norms and transactions to trade the economic value of environmental services. Third, a technocratization rationale, similar to Tienhaara, whereby scientific information is leveraged to enhance (policy) decision-making. Fourth, the privatization rationale, that has the underlying aim of maximizing private power and material gains through selective disclosure. The aforementioned rationales limit access to the potential of transparency to deliver on its ‘promise’.

Transparency is characterized by normative and relational elements, which are emblematic of its contextual nature. A further element is *about what* actors are transparent, in other words, what the nature of the information itself is which gets disclosed. A primary barrier to the ability of actors to disclose information is the extent to which the information is available. So if information exists and is possible to access by actors, then actors can be transparent on a given issue. If this information is difficult to collect, as disclosing actors may be unable to be transparent about issues that their counterparties might want insight on. Inherently, this dynamic offers actors the opportunity to be selective about the information they disclose. If there is Information that the general public is unaware of, and actors would prefer to remain secret, can be disguised as unavailable to deflect counterparty inquiries. A further barrier to transparency involves the framing of information. Information can be presented which is factually accurate but does not reflect the significant elements which required disclosure. When information is disseminated which does not reveal how actors behave or take decisions then actors may claim transparency all the while only divulging information nominally (Fox, 2007). This can be referred to as opaque or fuzzy transparency, reflecting the inaccuracy of disclosed information. Therefore, understanding *about what* actors are meant to be transparent about further delineates the contextual nature of information disclosure.

**Mechanisms**

Asymmetric information refers to a situation where one actor in a transaction has more or better information than another (Singhania and Saini, 2021). This can result in negative consequences for the actor with less information since they decide with less information than they might need to make an informed decision. A possible negative consequence is a moral hazard, which occurs when the actor with less information takes on more risk because they are not fully aware of the risks involved (Igawa and Kanatas, 1990). Thereby disclosing more information allows for an improved risk assessment of the actor to whom information is disclosed. Therefore, actors can take improved decisions and thereby leverage the power of transparency to be clearer on the potential consequences. This is related to a further mechanism by which the potential of transparency can create change; that improved disclosure of information can lead to a fuller understanding of potential consequences. Actors who require disclosed information from a counterparty might be actively acting in ways contrary to their interests. They might be drawing conclusions based on the available information that is contrary to their interests, where additional information would have changed their perception of a decision (Mitchell, 2011). Hence, improved information disclosure can allow actors to reassess their understanding of the potential consequences involved and lead to a change in their behavior or approach. This mechanism works both ways, as disclosing actors might be forced to collect information they would otherwise deem unnecessary, thereby becoming aware of the potential consequences they are facing. With both mechanisms, information disclosure creates the capacity for actors to change their behavior or outcomes with the inclusion of novel information. A further mechanism beyond information itself is the social context that disclosure policies establish. The normative forces that information disclosure brings about establish the social context and in turn lead to dynamics of social pressure on actors. If the information disclosed implies specific behaviors, then actors will face implicit or explicit pressure to account for this behavior. Therefore, reducing asymmetric information, enhancing understanding about consequences, and establishing a social context are some of the mechanisms by which transparency's potential for change is realized.

While the above relates to mechanisms of transparency itself, there are also critical differences in the ways in which information disclosure is operationalized on a policy level. An ongoing debate on whether or not information disclosure should be mandatory or voluntary. Voluntary disclosure allows for agents to disclose information that they choose. Consequently, agents would disclose information *selectively* which undermines transparency on a conceptual level. On the other hand mandatory disclosure policies have allowed for the monitoring of environmental performance indicators by NGOs and investors, potentially succeeding at changing firms' internal reporting mechanisms (Delmas and Cuerel Burbano, 2011). However, even if disclosure would be mandatory, it could lead to nominal disclosure, whereby the information itself is not truly measuring what would fulfill the theoretical requirements for transparency. Furthermore, mandatory disclosure requires enforcement, i.e. an actor who decides if the information disclosed is valid and sufficient. Therefore transparency becomes subject to the expertise and motivations

of external actors, who might also have ulterior motives and influences. Both mandatory and voluntary disclosure mechanisms have their benefits, which influence the nature of actors' disclosure patterns. This means that the effectiveness of the information disclosure mechanisms is understood based on how others can utilize the information provided and their accuracy perceived through the institutionalization of the mechanisms.

Information disclosure is seen and conceptualized as effective based on how the information is used. So if the mechanisms of information disclosure are characterized by normative and relational elements and the effectiveness of actors' ability to leverage the information provided, then information disclosure should lead to normatively preconceived outcomes. In the case of environmental governance, these could be both sustainability outcomes or changes in actors' behaviors. Principally, transparency should lead to outcomes that can be umbrellaed under the concept of accountability. The relationship between transparency and accountable governance is far from straightforward.

## Accountability

The following section will first look at accountability and its theoretical foundations. It will identify normative and relational elements that affect the concept of accountability. Furthermore, the link between accountability and transparency will be further explored.

### Theoretical foundations

Accountability and transparency share the common feature that their meanings are multidimensional, whereby both conceptually mean different things to different actors. In even the most narrow definitions of either accountability or transparency, there are both normative and relational elements. The fundamental elements which constitute accountability are structured according to Biermann & Gupta (2011) in four key concepts: a normative, relational, decision, and behavioral element. These need to all be sufficiently present to consider any accountability relationship as meaningful. First, the normative element, which is a standard of behavior defined with sufficient precision. Second, the relational element, which links those who are held accountable to those who have the right to hold them to account. Third, the decision element, which involves a judgment of those actors who may hold other actors accountable about whether the expected standard of behavior has been met. Finally, the behavioral element allows the governing actor to sanction the deviant behavior of those held accountable. However, despite there being elements that are sufficient conditions for accountability as a concept, its analytical operationalization remains elusive. 'Accountability' is used as a synonym for many loosely defined political desiderata including transparency, which creates substantial confusion in the process of operationalization. To bridge the conceptual gaps, Bovens (2010) conceives meanings of accountability where transparency is either a virtue or a mechanism, through which agents answer to their principals. Accountability as a virtue refers to substantive norms for the behavior of actors. It is an active sense of virtuous behavior that is easily used but very hard to define substantively. There is no consensus about the standards for accountable behavior, and because these standards differ, depending on role, institutional context, era, and political perspective. A way of distinguishing accountability as a virtue is in its colloquial use as an adjective. For example; *We want public officials to be accountable* or *accountable environmental governance*. Trying to distinguish what can be considered accountable behavior and what cannot is particularly challenging with a vaguely defined concept. As a virtue, accountability therefore provides a weak basis to create a conceptual framework.

On the other hand, viewing accountability as a mechanism is more operational, as one can analyze the structures which generate accountability within the relationship between actors. The defining element of accountability as a mechanism is the underlying relational dimension. Approached from this perspective there is a specific social relation or mechanism developed when actors are held to account, which involves the obligation to explain or justify behavior. These obligations are created between two actors, one actor who is the *accounter* and one that is

the *accountee*. Accountees allow accounters to take decisions and act on their behalf on a predefined issue, expecting the latter to behave according to expectations and in the best interest of the former. Behavior is justified to the accountee by the accounter, whose behavior is observed and judged. How this behavior is assessed involves a dynamic interplay of provisions of information and performance, which usually includes the possibility for the accountee to contest the accounters provision (Bovens, 2010). Consequences are attached to the outcomes of the provisions, embedding power relations into the accountability dynamics. Hence the relationship between actors and the consequences which accountees can impose on accounters for deviating from expected behaviors define the mechanism by which accountability occurs. Therefore, accountability as a mechanism refers to an institutional relation or arrangement in which an actor can be held to another. It is a narrower, descriptive sense of accountability that focuses on the way in which these institutional arrangements operate. Bovens (2007) outlines the methodology by which these institutional arrangements operate by expressing it through three stages: Stage 1 (*information phase*): The accounter is obliged to inform the accountee about his or her conduct; Stage 2 (*debating phase*): The accountee can question the adequacy of the information or the legitimacy of the conduct by the accounter; Stage 3 (*consequences phase*): The accountee may pass judgment on the conduct of the accounter.

Given the obfuscation of accountability as a concept for the purposes of this thesis accountability is defined on the terms of Mason (2008) where it is: "*broadly understood as holding authoritative actors both answerable for their actions and also subject to evaluation and redress by those affected by them"*. This definition principally avoids viewing accountability as a virtue in and of itself, focusing rather on the mechanism which accountability provides within social relations. Furthermore it alludes to the implicit influence of power within the accountability relations without specifying the directionality of power relations between actors. It does however specify that actors who are answerable for their answers are authoritative within the dynamic, which highlights that accounters take decisions on behalf of accountees. Mason's definition therefore offers a workable and critical understanding of accountability, which principally looks at accountability as a mechanism, while still encompassing the normative elements which underpin it.

**Accountability mechanisms**

Accountability mechanisms do not exist in a vacuum but emerge based on the demands of an actor within a given context. The nature of accountability mechanisms is, similar to transparency, contextually determined through their underlying relational and normative dimensions. These dimensions include, *who* is to be accountable *to whom*, about *what* and in *what manner* and *to what end/with what goal* one is being held to account for. The following paragraphs outline this in more detail.

A primary relational dimension of accountability mechanisms is *who* is to be accountable. As previously mentioned the actors who are accountable can be referred to as the *accounters*. They hold authority and make decisions that have specific impacts. For example; voters delegate authority to governments to make decisions on political issues and accept the impacts on wider society which are the result of those decisions. Accounters can be actors from any segment of society such as private or public (Mashaw, 2006). Hence, accounters do not necessarily need to be powerful actors, as long as they hold some decision-making capacity over a given issue that they are being held to account for (Backstrand, 2006). Two examples illustrate that accountability claims are multidirectional and can be issued from either top-down or bottom-up; i.e. from powerful actors to non-powerful actors and vice versa. The relationship between a company and its suppliers illustrates top-down accountability, as suppliers can be held to account for environmentally damaging behavior such as excessive waste or polluting activities. Here, the powerful actor is the company, which demands accountability from the supplier, which in turn has authority over the decisions it takes in the production process. Conversely, the relationship between NGOs and governments exemplifies the bottom-up directionality of accountability claims. NGOs might hold governments to account through reports which scrutinize their actions over which they had decision-making authority. Both examples also illustrate the underlying relational dimension of *who* is accountable, as mechanisms inherently involve *other* actors.

To *whom* actors are accountable is a further underlying relational and normative dimension of accountability mechanisms. These actors can be termed the *accountee* in accountability relations. For example these can be political communities, shareholders, consumers or social networks (Kramarz & Park, 2016). In a broader definition, onc could also include the environment itself as an accountee, although accountees are mostly understood to be embodied by representatives of the environment. For example, a NGO that is concerned with how ocean plastics affect marine life can be a representative of marine life, and by vocalizing concerns for the impacts can become an accountee of the environment. Different accountees have varying capacities to exert consequences onto the accounter, given their social position relative to each other. For example, consumers can demand both accountability from companies or governments. While the demand may be similar, like stopping pollution in a lake, the mechanism might vary. For companies, consumers may choose to boycott, while for governments they may choose to protest or engage in other political action. Hence *to whom* actors are accountable changes accountability mechanisms based on the expected consequences which accountees may exert on accounters. The relationship between the two becomes more complicated with closer analysis. The rise of governance beyond national borders has evolved accountability relations, whereby “simple” one-dimensional models such as principal-agent conceptions no longer reflect current dynamics (Arnold, 2020). Consequently, who is accountable to whom becomes complex and confusing, as involving multiple stakeholders in mechanisms obfuscates responsibility. This diffusion of accountability relations is closely tied to modern forms of environmental governance such as hybrid governance. Hereby different actors and institutions, both state and non-state, work

together on a given environmental issue (Colona & Jaffe, 2016). Accountability mechanisms within hybrid governance are diffused, as multiple actors are collectively responsible for the outcomes. Assessing who is responsible for specific outcomes introduces complexity and reduces the certainty with which actors can attribute consequences (Bäckstrand, 2006). As a consequence the relationship between accounter and accountee becomes more nuanced as plural interconnected accountees influence the context which accounters take in mind while making decisions. Conceptually these changes are closely linked to increased input accountability, an obligation of decision-makers to seek and consider input from various stakeholders, including the public, civil society organizations, and experts, in the development and implementation of environmental policies (Kramarz & Park, 2016). Through this process there has been a proliferation of accountability mechanisms that engage a plurality of stakeholders, changing the underlying relational dimension of accountability mechanisms.

These relational changes in the underlying dimensions of accountability mechanisms influence *what* accounters need to be accountable for. These can be observed by the changes in output accountability, which is the demand that those authoritative over decisions be held to account for delivering, or failing to deliver, on their aim to mitigate the human impact on the biosphere (Kramarz & Park, 2016). In other words, output accountability becomes the "oversight of operations, or accounting for results or impacts", which uses environmental outcomes as leverage to attribute consequences onto actors for their actions (Davenport and Low, 2013). For example, elected officials can be held to account for serving the public interest by reviewing and judging the legislation they pass. Similarly, companies (or producers) can be held to account for maximizing social welfare in their operations by comparing their performance to social and environmental benchmarks (Kramarz & Park, 2016). What accounters are accountable for remains a challenge because of how insights on outputs are developed and the method by which consequences are enacted. Attaching direct consequences to actors' behavior becomes a contested process, as actors often contribute to environmental problems but are not solely responsible for their existence (Schoenefeld and Jordan, 2020). Biodiversity loss is difficult to attribute to specific actors as it has multiple complex causes such as habitat loss, over-exploitation, agricultural expansion, and invasive species (Caro et al., 2022). Agricultural expansion can, for example, lead to species loss in a specific region. Other losses in biodiversity which occur due to unintended consequences are however difficult to reattribute to the same producers. Accountability for unintended or unmeasurable consequences is difficult to attribute, resulting in less clarity on *what* accounters need to be accountable for.

In *what manner* actors are held accountable involves accounters applying strategies to maintain answerability to avoid enforceability of the accountee. Answerability is the responsibility of accounters to provide information and justification about their actions, while enforceability is the possibility of receiving consequences for failing accountability standards (Anne Marie Goetz and Jenkins, 2005). Accountees demand information and justification for accounters actions and can

attribute consequences for accounters being unable to fulfill these requirements. Hence the relationship between the two frames in what manner accounters are held accountable. For example; voters can hold governments to account for their actions, such as policies treaties, or results of independent evaluations through removal from office or legal actions through courts (Kramarz & Park, 2016). Investors or consumers can hold companies to account for failing social or environmental benchmarks by reducing their access to capital or buying less of the product, which can lead to firms collapsing (Kramarz & Park, 2016). Hence accounters need to find strategies to mitigate the potential consequences which accountees can place on them. Two general ways in which accounters can do this are by information disclosure and creating visibility of desired behaviors. Accounters can benefit from disclosing information as a strategy to keep accountees at bay. Information disclosure is expected to assist in the political mobilization of affected parties, allowing them to apply actor-specific consequences (Mason, 2019). A further strategy that actors can employ is by publicly amplifying their 'prosocial' behavior to strategically manage their image (Benabou and Tirole, 2009). Accounters are therefore able to manage the perception that accountees have of their behavior. If this strategy is successful, then accounters can predict accountees consequences more effectively. Through both strategies accounters apply strategies to maintain answerability to avoid enforceability of the accountee.

Finally, it is critical to understand *to what end* or *with what goal* accounters are intending to be held to account to. Kramarz and Park (2016) make the case that those holding the authority to govern the environment are guided by varying goals that determine to whom and for what to account, and this influences the framing of environmental priorities and how accountability is measured. In other words, differing motivations influence the nature of the accountability relationship which accounters intend to uphold. Furthermore, Kramarz and Park (2016) propose a framework, arguing that public, private, voluntary, and hybrid governance institutions prioritize differing goals to execute respective accountability mechanisms. For example, producers would have the goal in mind to profitably generate goods and services and strategically would choose to demonstrate environmental accountability through social and environmental benchmarks, rather than through government monitoring. Viewed through this lens, *to what end* accounters want to be held to account to determine the subsequent process by which accountability mechanisms exist.

### Link between accountability and transparency

Transparency and accountability are often seen as linked concepts, but the relationship between them is complex and uncertain. Transparency is supposed to generate accountability, but the nature of this relationship can be influenced by contextual factors which can influence the expected effects (Mason, 2019). The relationship between transparency and accountability is

therefore contextually shaped. Kolstad and Wiig (2009) and Archon Fung, Graham and Weil (2010) suggest that greater accountability may not be achieved by transparent information alone, but may require media competition, citizen capacity to process the information, and the resources to act on it. The timing of transparency also affects accountability (Heald, 2012). Transparency in retrospect, compared to transparency in real-time, closes the accountability window after a certain period of time, reducing the possibility for accountees to institute consequences. The modulating effects of the context determine the relationship between transparency and accountability.

Conceptually speaking, transparency is often assumed to be a necessary if not sufficient condition of accountability. As mentioned before, accountability is broadly understood as holding authoritative actors both answerable for their actions and also subject to evaluation and redress by those affected by them (Bäckstrand, 2008; Florini, 2007; Grant and Keohane, 2005). However, transparency alone is not enough to ensure accountability, as information alone does not enact consequences for misaligned behavior. It is therefore more accurate to suggest that certain types of transparency can generate certain types of accountability under certain conditions (Fox, 2007). Therefore, accountability mechanisms such as monitoring, compliance, and sanctions are also necessary to hold those in power responsible for their actions, with information disclosure being a tool to facilitate these occurrences (Kramarz and Park, 2016).

The relationship between transparency and accountability is also considered complex because both concepts are inherently relational. Since the terms transparency and accountability are malleable and can mean different things to different people, how actors interpret either concept determines their effectiveness (Fox, 2007). In other words, the effectiveness of transparency in generating accountability depends on who is being transparent to whom and who is being held accountable by whom (Fox, 2007). The complexity of the relationship between transparency and accountability is illustrated by the reporting mechanisms of the Paris climate agreement. Biennial transparency reports are generated by nation-states, providing information on their greenhouse gas emissions and their progress toward achieving nationally determined contributions. Reports are generated on the basis of the Enhanced Transparency Framework, a set of rules and guidelines for nation-states to provide information in a consistent and comparable manner. By disclosing information to other nation-states, these mechanisms generate “transparency”. The Paris climate agreement does not provide accountability mechanisms with strict enforcement mechanisms or penalties for countries that fail to meet their commitments. Its effectiveness depends on how actors interpret the various information disclosed in order to appropriately apply consequences on each other.

The relationship between both concepts encounters at least three major challenges. One is the implication that information is not only disclosed but also processed well and fully understood (Mabillard and Zumofen, 2016). If the information is given in a format that is not

understandable, then actors will not be able to use it. For example, if emissions data is disclosed without any analysis, it will be difficult for laypeople to interpret the result. An additional challenge is that transparency rarely leads to consequences for institutions or administrations which disclose information (Mabillard and Zumofen, 2016). If actors are not powerful enough to place consequences on the accounter, then the behavior is unlikely to change. For example, if voters are unable to challenge government actions until the next election, then they might forget about behavior by the next election cycle, reducing the political consequences of environmentally unfriendly actions. Finally, transparency mechanisms are subject to manipulation or selective disclosure, which can undermine their credibility and effectiveness (Mason, 2019). A common example of this might be greenwashing. If producers selectively disclose information about their policies, then they might benefit from reputational gains without changing their behavior.

## Greenwashing

Greenwashing emerged as a concept in the early 1980s, coined by environmentalist Jay Westerveld who used the term "greenwashing" to describe the practice of making false or misleading claims about the environmental benefits of a product or service to appeal to environmentally conscious consumers (Gil-Cordero et al., 2021). The term has evolved and been used to describe a wide range of practices, from companies exacerbating their environmental performance to outright deception about the environmental impact of their products or services (Wood, 2010). Greenwashing has become an increasing concern in recent years, as there has been a surge in consumers looking for environmentally friendly products and services. Companies are looking to cater to this trend by producing more environmentally friendly products, however, they additionally have increasingly made misleading claims about the company's overall environmental impact. (Lashitew, 2021).

As a concept, greenwashing can be most clearly defined as the difference between an actor's symbolic actions and their substantive actions within their self-defined sustainability approach (Siano et al., 2017). In other words, actors communicate a position or achievement on environmentalism without fulfilling the basic environmental criteria to substantiate their claim. This difference allows actors to reap reputational or economic benefits while simultaneously misrepresenting environmental progress and/or actively damaging the environment (Alessandro Rizzello, 2022). Greenwashing can additionally be defined as the selective disclosure of less harmful environmental impacts to create an impression of transparency while withholding information that is more environmentally damaging (Grewal, Richardson and Wang, 2022). What this alternative definition highlights is the further extent to which greenwashing involves an attempt at creating an impression. For example, companies might want to create an impression of environmentally conscious production, while their fundamental business practices are unsustainable. What this definition further highlights is that symbolic actions are not neutral, but informed by an actor's purpose. Similar to the definitions of transparency and accountability addressed above, greenwashing involves inherently normative and relational concepts. At its core, greenwashing is the claim by an actor that another has failed normative standards of environmental performance, while falsely presenting the standards as being fulfilled. Hence substantive actions are not defined independently of the actors involved in the standard-setting process.

Literature on what constitutes greenwashing is fragmented and does not provide succinct theoretical frameworks which allow for analytical operationalization. For the purposes of this thesis, the theoretical framework of greenwashing is self-developed and thought only to highlight the relational and normative elements of greenwashing and not as an all-encompassing theoretical construct of greenwashing. Taking inspiration from the conceptualizations of transparency and accountability, here too the framework will look at who is greenwashing, to whom, about what, and to what end. Who is greenwashing will be the actor that is engaging in

both the symbolic and substantive action, as per Siano's definition of the concept. To whom greenwashing occurs are the actors receiving the symbolic action as well as further stakeholders who might suffer adverse consequences of the action. About what will be the content that is selectively presented? If we look at a fashion brand that presents a sustainable clothing line, which makes up only a small portion of the total output, then the greenwashing content will be about the production process of the company. The consumer receives the illusion of environmental responsibility while the company continues unsustainable practices overall. To what end an actor engages in greenwashing is the most complicated element of the theoretical framework. Motivations are notoriously difficult to identify and isolate, yet I would suggest that all cases involve a perceived benefit that the actor engaging in the behavior sees in creating a discrepancy between the symbolic and substantive action. Yet these motivations (or perceived benefits) are highly varied and could be reputational, monetary, economical, legal, or political. Combined these elements provide the building blocks for understanding the relational and normative elements of greenwashing.

The relational and normative elements of greenwashing reflect that greenwashing can only occur in a given context. The contextual factors which bring about greenwashing by actors are the actors' motivations, their opportunity to greenwash, and the actors, often beneficial, expected consequences. Motivation for actors to greenwash can depend on their initial position towards greenwashing. According to Delmas and Burbano (2011) if there is an increase in perceived consumer and investor pressure for environmentally friendly firms, the more likely a brown firm is to greenwash. Hence if two firms operate in the same industry, the brown firm is more likely to greenwash to keep up with their more environmentally competent peers.

Furthermore, there are structural factors that make the opportunities for actors to greenwash more accessible. Firstly, a lack of regulation and transparency in environmental reporting leads to higher levels of greenwashing (de Silva Lokuwaduge and De Silva, 2022). Without clear guidelines and standards for companies to follow, there is a greater opportunity for them to mislead consumers and investors by exaggerating their environmental efforts. This follows into the second point, that a lack of an external verification process by third parties increases the possibility for actors to greenwash (Perego and Kolk, 2012). The absence of any verification process leaves room for actors to engage in deceptive practices regarding their environmental performance. Even if mandatory disclosure would be in place, monitoring the truthfulness of reporting could lead to incentives for firms to lie about or exaggerate their environmental performance (Delmas and Cuerel Burbano, 2011). Verification through for example auditing of reporting would be a necessary complement to any regulatory methods. Delmas and Burbano (2011) furthermore contend that if a verification process were made publicly accessible, consumers and the public would have greater confidence in the reported information. This in turn would accordingly reduce the capacity for actors to engage in greenwashing practices. Thirdly, a source for the lack of regulation could potentially be the lack of a clear legal definition of

greenwashing. Since standards are not universal, governments might struggle to clearly delineate greenwashing as a concept and subsequently impose clear consequences for deviating actors. A lack of universality in standards also makes a global framework for the substantive actions that actors ought to abide by implausible, further complicating the capacity of state actors to impose effective regulation. Actors consequently have further opportunities to greenwash in the absence of regulation and clear normative principles that underlie the standards to be adhered to.

The consequences of greenwashing can be wide-ranging and affect key actors within the governance framework. With a focus on private market dynamics, greenwashing can have consequences on a wide array of actors, such as investors, consumers, and companies. Greenwashing by companies can negatively affect investor confidence in environmentally friendly firms, eroding the socially responsible investing capital market (Delmas and Cuerel Burbano, 2011). When companies make misleading claims about their environmental performance, investors may become skeptical and lose confidence in the company's commitment to sustainability. As a result, investors can decrease investment in those companies. The outcomes for the environment can be either positive or negative. Specifically, they may be positive in the event of polluting companies stopping their operations, but conversely, negative if a company that previously implemented environmental safeguards is replaced by one which further degrades the environment. Additionally, greenwashing can have significant consequences for consumers, specifically in terms of the provision of misleading information and the misallocation of resources. Exaggerated claims regarding a company's environmental performance can systematically mislead consumers and undermine their ability to make informed decisions about their purchases. Additionally, greenwashing can lead to the inefficient use of resources and the exacerbation of environmental harm through the consumption of products with few environmental benefits. Consequently, consumers' actions may have a negligible environmental impact, while falsely believing their actions are improving the environment.

What most definitions of greenwashing have in common, is the concept that greenwashing involves some sort of practice or action to be fulfilled. This points to a fundamental element of greenwashing, which is that greenwashing involves a mechanism to be fulfilled. Various authors have tried to classify these processes taxonomically. The most important mechanisms are described below, which have been summarized by Lyon and Montgomery as mechanisms of misleading behavior.

Firstly, there is the mechanism of decoupling, which is the disconnect between the activities and the structures of an organization. For example, if an organization creates a sustainability department that is understaffed and has little power, yet leverages its establishment for reputational gains to external stakeholders. Secondly, means/ends decoupling, which can be described as the disconnect between the actions and goals of an organization. For example,

adopting electric vehicles as company vehicles, yet not disclosing what energy sources are used to power them. A further strategy is symbolic management, which can be defined as the disconnect between promises and actions. An example would be when companies pledge to go net-zero, yet do not have any concrete plans laid out to achieve this goal. Another strategy is commonly referred to as pooling, which is when actors engage in the same umbrella activities as more sustainable actors to appear identical. An example would be when companies join larger collectives (such as the United Nations Principles for Responsible Investment), yet do not change their investment behavior. One of the most important mechanisms is selective disclosure whereby actors disclose positive information while withholding negative information. Actors hereby engage in greenwashing by purposefully disclosing information they believe will be beneficial to their image. For example, an airline company might disclose that their flights have a reduced $CO_2$ impact of 6%, while not disclosing that they have increased their overall short-haul flight routes, which are notoriously carbon intensive.

While the mechanisms above are general mechanisms of greenwashing that can occur in various dimensions of global environmental governance, there are a few which are less generalizable. To adequately cover the concept of greenwashing concerning sustainable finance regulation, the section below will outline more specific mechanisms,

De Silva Lokuwaduge and De Silva (2022) specifically look at firm-level greenwashing, which are greenwashing mechanisms used by companies. The first mechanism they mention is having an inherently unsustainable business, yet promoting sustainable practices or products. For example, while a fast-fashion brand could reduce water usage during manufacturing to improve its sustainable practices, it would not fundamentally change its business model relying on a wasteful production and consumption cycle. Another mechanism mentioned diverting attention from sustainable issues through the use of advertising and promoted research. An example would be fossil fuel companies advertising their investments in renewables, while not changing their extraction practices. A further mechanism would be companies affecting regulations or governments to obtain benefits in areas of sustainability. An illustration of this would be the aviation industry influencing governments to look at sustainable aviation fuel as the solution, instead of reducing the amount of flight routes. A further mechanism would be when companies proclaim sustainability accomplishments, while their disclosure was mandated by laws and regulations. Banks proclaiming that they have adequate systems to prevent money laundering would for example be a sustainability objective which is required by most financial regulatory bodies. And finally, companies could take advantage of sustainability reports to project an environmentally positive image of themselves. The example here would be companies proclaiming the achievement of emissions reductions in their products while having simply shifted the emissions to another entity.

## Integration of concepts

As mentioned above, transparency, accountability, and greenwashing are all concepts that are contextually defined. Who, to whom, and for what are core elements of all three concepts, which means that the context in which they are assessed shapes the nature of how the concepts are interpreted. Unsurprisingly, their meanings and implications vary depending on the specific circumstances in which they occur. Understanding the causal mechanisms which underpin these concepts remains a challenge, as their definitions do not allow for empirical clarity on how the concepts are causally linked. While transparency can be best understood as a necessary and sufficient condition of accountability, the causal relationship between the two concepts remains more assumed than explored. Transparency only leads to accountability in specific circumstances. So while it might be a necessary condition for accountability, it may not be clear in what way and to what extent its influence emerges. The normative and relational factors which shape the circumstances represent the interconnectedness between the concepts of transparency, accountability, and greenwashing. These factors demonstrate the normative expectations and the consequences of failing to adhere to standards. An illustrative example of these factors is the context of corporate sustainability reporting. Here, transparency, accountability, and greenwashing take on distinct meanings. A company may choose to disclose its environmental practices and impacts through sustainability reports, demonstrating transparency by providing environmental information. The validity of this transparency is shaped by the stakeholders, such as investors, interpretations of the information. The company's accountability, in this case, is determined by how well it demonstrates that its actions are aligned with the disclosed information. By selectively disclosing positive environmental impacts while neglecting to disclose harmful practices, it engages in greenwashing, misleading stakeholders by creating a false impression of transparency and responsible environmental performance. The normative and relational aspects of transparency, accountability, and greenwashing come into play as stakeholders hold the company to certain predefined expectations leveraging their ability to place consequences on the company if actions concerning sustainability have not been upheld. This case reflects the interconnected nature between transparency, accountability, and greenwashing is shaped by normative expectations and the consequences associated with them.

Transparency is, as previously mentioned, operationalized as information disclosure and plays a pivotal role in effecting accountability and greenwashing. Who holds and discloses what information is a critical component of both concepts. When actors hold more information than others, as mentioned above as information asymmetry, then this can have an influence. Specifically, this could hinder the effectiveness of accountability mechanisms and conversely improve the effectiveness of greenwashing mechanisms. When one party possesses more information than others, accountability processes can be manipulated. In the case of greenwashing, selective disclosure of less harmful environmental impacts creates an impression of transparency while withholding information about more damaging aspects. This strategic use of information disclosure is emblematic of the deceptive practices of greenwashing, undermining

both transparency and accountability. For example, if an energy company selectively discloses positive aspects of its operations while hiding non-renewable energy sources, it engages in greenwashing through selective disclosure. This undermines its environmental accountability to investors and the public. The information asymmetry between the company and stakeholders is key, as incomplete disclosure reduces the stakeholders' capacity to enact consequences for poor environmental performance.

There is a complex relationship between accountability and greenwashing. By engaging in greenwashing, actors attempt to fulfill accountability requirements from other actors through symbolic actions and yet differ in their substantive actions. A key link between accountability and greenwashing lies in the judgment and consequences associated with the obligations of responsible actors. Accountability entails the assessment of behavior and the imposition of sanctions or consequences. However, in the realm of greenwashing, the lack of consequences for institutions or administrations that engage in deceptive practices poses challenges to accountability. This process intertwines with the selective use of information. Selective disclosure of information undermines accountability, by selectively revealing only favorable information. By concealing detrimental elements, actors can avoid accountability for their true environmental impacts. This manipulation of disclosure erodes the credibility and effectiveness of transparency mechanisms and raises questions about the enforcement of consequences for greenwashing practices. For example, a multinational company can engage in tree planting projects which could be limited and not independently verified. Despite the misleading claims about the project's effectiveness, the company faces minimal consequences for its greenwashing practices. By selectively disclosing information to create an illusion of transparency, the company could avoid implementing substantial emission reduction measures. Through this process, its accountability requirements towards other actors could be fulfilled, despite the environmental degradation continuing.

Overall, understanding the contextual nature of transparency, accountability, and greenwashing is crucial for comprehending their roles within environmental governance. In key ways, information disclosure acts as a double-edged sword, since it serves as a component of accountability while also being manipulated in strategies such as greenwashing. Challenges in managing the obligations set between actors thereby arise due to selective disclosure and the lack of repercussions for deceptive practices. By exploring these interconnections and considering real-world cases, a more nuanced understanding of the complexities of transparency, accountability, and greenwashing can be developed.

# Methodology

## Introduction

This chapter explains the research design and the rationale behind why a certain methodology has been chosen to answer the research question. This will be done with the following structure; The research design will be introduced that illustrates why certain methodologies were chosen, followed by how the data was collected and analyzed. Finally, ethical considerations and limitations to the study's validity and reliability will be discussed.

## Research Design

To answer the question: "How is the potential of transparency and accountability undermined by greenwashing opportunities within the SFDR?" the method chosen is the case study approach. This approach allows for more depth in exploring the issue, is applicable to exploring a real-world context, and allows for interpretation through multiple perspectives. Case study approaches are able to capture nuances and provide a rich and detailed understanding of phenomena (Yin, 2014). This depth comes from an ontological appreciation for the complexity of issues, which is necessary in the case of the context of sustainable finance and the SFDR. Case studies are used when a researcher's aim is to fully understand a phenomenon (Yin, 2014). Developing this understanding through a holistic empirical approach offers richer insights into phenomena compared to a reductionist approach (Easton, 2010). Furthermore, using a case study methodology allows for the exploration of real-world phenomena within their context (Rashid et al., 2019). This is ideally suited for understanding greenwashing within sustainable finance, as using a case study methodology incorporates the interplay of regulatory provisions, behaviors of stakeholders, and the broader political and environmental context. Case study methods also acknowledge the complexity of phenomena and the multiple perspectives which they contain (Ogawa and Malen, 1991). By incorporating multiple perspectives, the various stakeholders with a view on the SFDR are able to transmit their understanding. A more comprehensive understanding of the potential for greenwashing within sustainable finance and the SFDR regulation can be generated through this approach.

The research conducted here is exploratory in its nature. Since few quantitative studies exist in the field, there is not enough development in the research methodology to use a different research methodology. Using a case study approach as the starting point to develop an exploratory understanding of the phenomena is most suitable. By gathering contextual and in-depth data in a holistic manner, this research could provide a wider and richer understanding of the phenomena. This can therefore lead to more quantitative and comparative research, that are currently still unfeasible.

There are a variety of advantages to using the case study methodology, including the development of a holistic understanding, in-depth insights, and flexibility. Answering this research question involves multiple elements such as regulatory measures, FMPs and FAs actions, environmental objectives, and the interplay between these factors. A case study allows for a holistic exploration that acknowledges the inherent complexity (Harrison et al., 2019). A further advantage is the generation of in-depth insights into a phenomenon through a detailed examination of when the phenomena occur in contexts (Harrison et al., 2019). Specific ways in which greenwashing emerges in the SFDR can be explored through this method. Utilizing a case study approach allows for enough flexibility to discover new or unexpected information (Meyer, 2001). This flexibility is advantageous to incorporate the evolving nature of sustainable finance regulation in developing an understanding of the phenomenon. As a method, the case study can accommodate unexpected findings and shifts in the interview discourse.

The aim of this research is to examine the potential of transparency and accountability being undermined by greenwashing opportunities within SFDR. This requires an exploration of the real-world elements within the context of the European financial sector's sustainability practices. A case study approach is perfect as it is designed to examine specific instances or scenarios in great depth, assessing the intricate dynamics of a complex issue such as the SFDR. The case study approach is therefore connected to the research question as it allows for a comprehensive, context-sensitive, and perspective-based exploration of the issue.

Implementing the case study design involves defining the case, setting up the research framework, and clarifying the data collection and analysis methods. The case to be scrutinized in this research is the implementation of the Sustainable Finance Disclosure Regulation (SFDR) within the European financial sector. The core of the case study involves exploring the strategies and processes of financial institutions engaging with the SFDR. The focus lies on the contextual intricacies and mechanisms of transparency and accountability within these institutions, through which potential greenwashing practices can be identified. This involves developing an in-depth understanding of the financial institutions' products, processes, and motivations to engage with the SFDR, thereby systematically identifying potential areas for a lack of transparency and accountability which could potentially lead to greenwashing. The framework for this case examines specific mechanisms within the SFDR structure and how financial institutions engage with them. These include disclosure requirements, accountability procedures, and ESG metrics. How these indicators of greenwashing and mechanisms of transparency and accountability are implemented by financial institutions is explored. It places particular importance on indicators of greenwashing, such as the mechanism of decoupling, selective disclosure or strategically affecting regulation. This multifaceted framework provides a comprehensive understanding of transparency, accountability, and greenwashing in the SFDR context.

## Data collection and analysis

To collect the data, semi-structured interviews were conducted with the chosen sustainable finance experts. Their selection was made based on several considerations. All of the interviewees were employed by European financial institutions. These institutions provide products on the European financial market. Through their work, these experts have comprehensive exposure to the consequences of implementing the SFDR. Their understanding of investor behavior, market trends, and stakeholder dynamics within financial markets, give them a nuanced understanding of the underlying dynamics present in the regulation. Second, through their positions, experts can have an influence on policy-making, offering insights into the interactions with policymakers on the topic. They have the capability to advocate the limitations to policymakers, offering crucial information about the financial institutions' capacity to operationalize the regulation. Finally, their direct experience in the field of sustainable finance equips them with in-depth knowledge that is integral for answering the research question. This population provided valuable insights as their firsthand knowledge and experience in sustainable finance operations were closely linked to the case. Their perspectives shed light on the intricate implications of SFDR implementation, the potential for greenwashing, and the challenges in achieving transparency and accountability. Engaging with these experts explored and developed further depth in the understanding of the SFDR, allowing for a nuanced analysis of the intricacies involved in disclosure mechanisms. Their current roles and years of experience are listed below.

| Interviewee | Current Role | Years of Experience |
|---|---|---|
| Interviewee 1 | Product offering manager | 6 |
| Interviewee 2 | Advisor for responsible investments | 13 |
| Interviewee 3 | Legal specialist from product management | 3 |
| Interviewee 4 | Strategic sustainability advisor | 15 |
| Interviewee 5 | Sustainable finance analyst | 3 |

*Table 1. List of interviewees and their respective roles and years of experience.*

Using the semi-structured interview method allows for a detailed exploration of their experiences and perceptions about the SFDR, accountability, transparency, and greenwashing. Using a semi-structured approach, whereby structured and unstructured elements are integrated in the interview style, provided the necessary flexibility to examine the experiences, attitudes, and insights of the sustainable finance experts. The steps taken for the data collection process included setting up an interview schedule, contacting the participants, and consequently conducting the interviews. The interviews were primarily conducted through video calls due to their practicality and efficiency. These took roughly thirty minutes, allowing for enough time to

get into the topic, without requesting too much time from participants. Given the semi-structured nature, interviews consisted of initially general and open-ended questions. The questions focused on their experience with the SFDR, their understanding of transparency and accountability, and their insights on the prevalence and nature of greenwashing. An interview guide is provided in the Annex. This was subsequently followed up with ad-hoc questions, enabling a more nuanced and specified understanding of the issues through the lens of the expert. This added flexibility was offered through the semi-structured approach.

Interviews were chosen to not be recorded for several reasons. Information given by participants could be compromising for their role within the company, which means that any formal record of their statements could impact their work. By not recording, participants are more comfortable and less reluctant to disclose potentially compromising details. By respecting their confidentiality through non-recording and anonymity, participants face fewer ethical dilemmas with disclosing sensitive information. To capture the information as accurately as possible detailed notes were taken throughout the conversations to capture the key points. While this offers less direct accuracy, it is a chosen trade-off. Immediately following each interview, these notes were transcribed and summarized into a more detailed narrative form while the details of the conversation were more salient.

Interview notes were prepared from these interviews and were analyzed using the method of qualitative content analysis. By identifying themes and patterns related to the research question in a systematic way qualitative content analysis allows for a deeper understanding of a phenomenon in a conceptual form. During the analysis this was done through reviewing the interview notes and identifying any concepts or pattern of concepts that related to any given topic. These were then organized according to overarching categories that were developed on the basis of the raw data. For example, identifying any concept or pattern that is related to transparency. These would then be reorganized into overarching categories. This enabled a more comprehensive understanding of the SFDR's impact and the possibilities of greenwashing within it. With an inherently exploratory research question that seeks to understand a multifaceted issue, the most applicable analysis method is thematic content analysis. As a method, it allows for the identification and analysis of themes within qualitative data, which is useful for broad ranges of questions around the three main topics (Castleberry and Nolen, 2018). Understanding such a complex and context-specific issue requires an understanding of the intersection of the experiences, views, and interpretations of sustainable finance experts. Using interviews as a methodology provides rich and complicated data. Thematic content analysis provides an adequate tool for interpreting and assessing the data, as it can capture the complexity of various narratives, allowing for an assessment of the broader implications of their views and experiences. It also provides a flexible approach to research, blending well with the multi-faceted data provided by the semi-structured interview format. This added flexibility allows for a more nuanced and in-depth analysis to answer the research question. Since the research is exploratory

and the themes of transparency, accountability, and greenwashing are complex, data can be interpreted in an inductive way using thematic content analysis. Thereby, the interpretations can emerge from the data provided by the experts, rather than being framed by the predetermined theories of existing research.

To expand on the data collected through the semi-structured interview method, this research includes a document analysis of the SFDR document as a method to delve deeper into its context, meaning, and effects. Document analysis provides a text-focused perspective, allowing for the identification of potential areas of themes and assumptions present in the concepts in the text (Bowen, 2009). Using a document analysis can allow for a deep understanding of the context in which a regulation was created (Bowen, 2009). By pairing a deeper contextual understanding with a more nuanced exploration of the assumptions present within the text, the underlying intentions that might not have been explicitly stated can be uncovered through a document analysis. This allows for a more critical later assessment of the effectiveness of the regulation, whereby the intentions of the regulation can be evaluated in comparison to its outcomes. A document analysis alone will unlikely provide these comparisons but can be paired with other methodologies to provide clearer insights. Including a document analysis further expands the research design by capturing the textual intricacies of the SFDR thereby enriching the holistic understanding gained through the case study approach. Evaluating the intentions identified in the SFDR regulation through a document analysis and then comparing these to the outcomes identified in the interview analysis provides for a more holistic evaluation of the case.

The document analysis will follow a step-by-step process. First, the SFDR legislation was selected as the primary data source. To identify the key themes and assumptions within the text a coding scheme was developed. This coding scheme was based on the theoretical framework developed for transparency, accountability, and greenwashing, ensuring the inclusion of relevant analytical features. Using the coding scheme, the text was analyzed to identify concepts and patterns and the relationships between these concepts. Subsequently, these were categorized according to the themes that were drawn out of the analysis.

## Ethical considerations

The study was conducted adhering to the inherent ethical considerations within research. Considerable effort was placed on ensuring that the rights and well-being of all participants were safeguarded, and did not impede on the integrity of the research process. Effectively managing the interviews in a sensitive and respectful manner should have minimized any potential negative impact on participants. Many of the ethical considerations have been taken from Allmark et al. (2009), based on their extensive review of ethical complications of in-depth interviews.

To begin with, informed consent was obtained from each participant before any interviews started. This was done through an informed consent form that was sent to participants prior to the interview. Each interview started with a brief introduction to explain the purpose of the research and reminded participants that this process was entirely voluntary. Participants were explicitly informed about the purpose and nature of the research. Their decision to take part in the study was autonomous without any pressure to participate. Without this, the integrity of the research would be compromised. All elements of the study were explained to the participants, including the methods, expected outcomes, and how the results were intended to be used. This was done in order for participants to understand and be comfortable with their involvement in the study. It was repeatedly emphasized that their participation was entirely voluntary and that withdrawing was an option at any stage of the research.

Given the sensitive nature of the topic and the reputational backlash that participants could face by disclosing their positions on greenwashing, the anonymity of participants was critically important. Considering the professional roles of the participants and the consequences of information breaching the non-disclosure agreements of their contracts, confidentiality was critically important. This was maintained throughout the study with various measures in order to ensure the confidentiality of the participants. Their identities were not disclosed or recorded at any point during the research process or its subsequent publication, safeguarding their personal information. Information disclosed in the email contact was subsequently removed from the researchers' servers. This privacy extended to other elements of communication since interviews were conducted over video calls. Any possible measures were taken to ensure the security and privacy of the communication platform used, thereby minimizing any risk of unauthorized access.

Given the severity of these measures, care was taken to prevent the feeling of exploitation for the participants. Since this information could be leveraged against them, they were assured that the information they shared would be used strictly for research purposes and not used in any manner outside of this thesis. These assurances hopefully furthered participants' feelings of comfort in disclosing information, since accurately representing their views in the findings is both ethically necessary and critical for the purpose of the research.

## Methodological limitations

There are a variety of limitations that impact both the validity and reliability of the research. These inherent limitations arise due to any research being inherently limited through its design and methodological choices. The following issues represent validity issues within the study.

The research study depended heavily on the researchers' interpretation of the interview responses from sustainable finance experts. Given the inherent subjectivity of qualitative analysis, there's an unavoidable risk that the researchers' biases or preconceptions could have influenced the responses. This extends to the analysis of the data. Despite reasonable protocols being employed to enhance reflexivity and minimize the subjective influence on the interpretation, its potential remains an inherent limitation of the study.

**Validity**

The research used a case study approach to specifically focus on the SFDR within the European financial sector in order to provide in-depth insights into this particular context. Prioritizing depth generates the opposite challenge, which is the generalizability of the findings. The insights and tacit conclusions drawn from the research aren't suitable to reapply directly to other sectors or geographical regions. Consequently, the generalizability of the research findings will be limited to similar regulatory environments within the realm of sustainable finance. This can only be avoided through novel research, which either prioritizes other regions or looks at the topic through methods that offer more generalizability. Central to the lack of generalisability is the chosen sample population. Insights drawn from sustainable finance experts represent a small section of the broad array of stakeholders involved in the SFDR's interpretation and subsequent implementation. Further complexities and differing viewpoints present in the broader sustainable finance community are not present in the analysis. While generalizing the findings would be difficult across novel contexts, generalizing the analytical capacity from this thesis could be beneficial. Given the case study design, further research could compare the case to novel cases, generating analytical generalizability.

Furthermore, due to the subjective elements inherent in qualitative research replicating the study to achieve identical results is not possible. Given the emerging nature of the topic in European environmental politics, the research findings are subject to the specific conditions and timing of the research and to the particular perspectives of the participants. While the insights from this study are valuable for understanding the SFDR's context and potential for greenwashing, they are unable to be replicated in other contexts and are unable to be reproduced by the same participants.

**Reliability**

Social desirability bias, whereby interviewees may unconsciously seek to provide answers they believe the interviewer wants to hear, could have played an effect on the study (Kaushal, 2014). Given that participants knew the purpose of the study, this might have primed them to respond in

a more critical way than how the phenomena are truly presented in the world. The mere presence of the interviewer and the knowledge of the purpose could therefore subtly influence participant responses. Leading questions during interviews influencing the outcomes is another potential limitation. Its effect emerges similarly to the social desirability bias. Despite the intention to ask neutral and open-ended questions, some questions might inadvertently have led participants toward certain responses. The construct validity of the data could be compromised, as it might not accurately reflect participants' perspectives within the context, but rather their initial reactions to the questions.

Given the study's primarily qualitative approach, objective measurement of certain variables is limited which presents another limitation of the study. Although qualitative data can provide in-depth and nuanced insights, the data does not have the precision and replicability of quantitative data. This could affect the reliability of the conclusions drawn. Without quantitative data, it's unlikely that the findings could predict how the dynamics would apply to different contexts. An over-reliance on self-reported data can also impact the reliability of the study. The accuracy of the study findings is contingent on the ability of participants to accurately describe their experiences. There might be discrepancies between participants' self-reported experiences and actual practices, especially if participants struggle to present themselves or their organizations critically. While the design choices support participants being able to be critical, verifying self-reported data represents an intrinsic limitation of this research method.

A further limitation is a potential sampling bias of the interviewees who participated in the study. The sample of interviewees may not have been representative of the broader population. Consequently, this could affect the reliability of the generalizations made, as other interviewees might have a different perception of the SFDR. This effect interacts with the sampling strategy. Since the interviews are voluntary, they rely on interviewees being interested in doing the interview. As a consequence, those who might have a critical perspective of the effects of the SFDR could have been more likely to respond to the request and therefore also be more critical than the average. Hence they would be less representative of the broader population.

Finally, the design of the research provides a critical limitation in terms of how the data has been collected. Given the lack of recording, interview data cannot be transcribed accurately and verified sufficiently. Data was dependent on the immediate transcriptions and notes made during the interviews, making the selection of valuable information highly dependent on the researcher. Many nuances may have been misinterpreted, as the schema evoked by the information presented by the interviewee will differ from researcher to researcher. As these interviews have been conducted online, subtle non-verbal cues will have also been missed.

# Sustainable Finance

## Introduction

The European Union defines sustainable finance as the process of taking environmental, social, and governance (ESG) considerations into account when making investment decisions (European Commission, 2022). The aim of sustainable finance is to increase longer-term investments into sustainable economic activities and projects by prioritizing businesses that help the environment. Some key focus points include inclusion and ethical business standards and support for fair and sustainable labor practices (Bakken, 2021). Sustainable finance does have multiple definitions. While the EU's definition focuses on ESG and green growth, other definitions look at the set of financial regulations, standards, norms, and products that pursue an environmental objective and allow the financial system to connect with the economy (Soundarrajan and Vivek, 2016). The difference between these definitions lies in the specific focus, whereby some look more closely at ESG factors, environmental objectives, social goals, and sustainable growth. There are some common elements to the definitions which can be roughly grouped into principles of sustainable finance, whose aim is to promote sustainable economic activities. Some of the most prominent principles are promoting long-term value creation, considering ESG risks and opportunities, and aligning financial flows with sustainable objectives (Schoenmaker and Schramade, 2019). These also involve promoting transparency, accountability, and stakeholder engagement in the financial sector (Schoenmaker and Schramade, 2019b). A fundamental component of sustainable finance is that investors and bankers can steer funding to sustainable companies and projects without sacrificing return. As a consequence, sustainable finance merges an expanding economy with environmental protection to speed up the transition to a sustainable economy.

To achieve the goals set out by sustainable finance, the implementation of disclosure practices plays a vital role. Disclosure practices are theorized to promote transparency, accountability, and responsible investment decisions. There are three key subtypes of ESG disclosure practices, each focusing on one of the three elements of ESG. Environmental disclosure encompasses the reporting and disclosure of an organization's environmental impact, including its carbon emissions, energy consumption, and waste management practices (Hassan and Ibrahim, 2011; Cho and Patten, 2007). Social disclosure focuses on disclosing information related to an organization's social impacts, such as labor practices, employee welfare, community engagement, and social initiatives (Newson and Deegan, 2002). Governance disclosure involves disclosing information about an organization's governance structure, including board composition, executive compensation, and ethical policies (Harvey, Maclean and Price, 2019).

By engaging and standardizing the disclosure areas, sustainable finance attempts to provide investors and stakeholders with key information which they can use to make informed decisions about investments (Busch, 2018). Consequently disclosing this information ought to encourage responsible business practices which would in return foster the transition to a more sustainable and equitable economy. Transparent and standardized disclosure practices play a critical role in sustainable finance by providing essential information to stakeholders. Through increased transparency and the disclosure of non-financial information, the expectation is that the private sector will be incentivized to shift toward a sustainable economy (Schütze and Stede, 2021). By making information available to stakeholders, it is expected that two forces come into effect. Firstly, making companies collect environmental information for disclosure enables companies to become more aware of their environmental impact, prompting them to assess and disclose relevant environmental practices. This self-awareness allows companies to identify areas for improvement and make transitions to sustainable practices more concrete (Dagestani and Qing, 2022). Secondly, transparent and standardized disclosure practices empower investors to make informed decisions by providing them with comprehensive and reliable data. Investors can evaluate companies more rigorously based on this information and consider their environmental performance in investment decisions (Sugianto et al., 2022). This two-pronged approach ensures that both companies and investors can leverage disclosed information to create more sustainable outcomes.

The types of disclosure practices which are necessary to achieve the goals set out by sustainable finance differ, based on the types of sustainable finance products that financial market participants (FMP's) provide. Some of the key types of sustainable finance products are green bonds, social impact bonds, and sustainability-linked loans. Green bonds are used by companies or governments to raise capital for projects that provide environmental benefits. Investors can support a transition to a sustainable economy by purchasing green bonds from the entity, which then exclusively allocates the money to projects such as renewable energy or sustainable agriculture. For example, the State Bank of India issued $650 million from the green bond market to finance renewable energy projects in 2018 (Verma and Agarwal, 2020). Social impact bonds are another form of a sustainable finance product. They involve collaborating investors providing upfront capital to fund interventions for social outcomes and if the outcomes are achieved receive a return from the government (Rizzello and Kabli, 2020). This leverages private sector capital to drive social change. Education or homelessness programs are some examples of this process, whereby the private sector is involved to encourage efficiency and effectiveness in the delivery of social services. These bonds are increasingly being used in the UK and in the US to raise funds to finance government projects (Faia, 2014). A further type of sustainable finance product is sustainability-linked loans. With this product, the borrower's interest rate is linked to their sustainability performance. So when issuers give out loans, they encourage borrowers to improve their ESG practices, thereby leveraging capital to improve ESG outcomes. Since the interest rate is adjusted, borrowers can conversely also be penalized for failing their

sustainability targets. An example would be the sustainability-linked revolving credit signed by the Italian energy company Enel, which was funded by a group of European banks (Versal and Sholoiko, 2022). By linking the interest rate of the loan to the achievement of Enel's sustainability targets, the expectation is that Enel will be incentivized to increase renewable energy capacity and reduce greenhouse gas emissions.

The key actors involved in sustainable finance include financial institutions, investors, regulators, and policymakers. Financial institutions have embraced sustainable finance as a business opportunity, but there is a gap in the way sustainability has permeated primary and secondary markets. Investors are driving demand for sustainable assets, and regulators and policymakers are incentivizing financial intermediaries to offer more sustainable investment products. The European Union has developed a Sustainable Finance Strategy to enhance transparency for investors, avoid greenwashing, and channel more capital into sustainable economic activities. The strategy provides the regulatory framework for sustainable finance in the EU. Green bonds are an example of a financial product that uses its proceeds in environmentally friendly projects and signifies socially responsible investing through investing in energy efficiency, green infrastructure, renewable energy, and water improvement

The key actors involved in sustainable finance include financial institutions, investors, regulators, non-governmental organizations, and policymakers (Versal and Sholoiko, 2022). Combined, these actors create the key components of the sustainable finance ecosystem. Some actors are grouped under the term financial market participants. They are defined as investment firms, such as asset managers, pension providers, insurance-based investors, and some venture capital and social entrepreneurship entities who qualify (Humphreys, 2021). All the aforementioned actors are considered financial institutions. These financial institutions are instrumental as they shape investment decisions and drive the allocation of capital toward environmentally and socially responsible initiatives (Yang et al., 2022). They achieve this by providing funding, investment products, and financial services (Ziolo, Bak and Cheba, 2020). Financial institutions are funded by investors, who similarly have their impact through the investment decisions they make, as this changes the demand for sustainable finance products. These choices result in different allocations of capital to financial companies, who as a result finance companies and projects that prioritize environmental and social considerations (Kawabata, 2019). Pressure from investors is theorized to result in a change in corporate behavior (Falcone, 2020). Which possibilities are given to investors is determined by the regulatory context in which they find themselves. Regulators are able to steer sustainable finance by establishing frameworks, standards, and laws which shape financial institutions and investors' decisions (Campiglio et al., 2018). Their aim often involves promoting transparency and accountability through information disclosure practices on ESG issues (Holland, 2011). NGOs advocate for ESG issues by raising awareness and influencing both regulators and FMPs to adjust their investment decision-making (Awiti and Macheru, 2022). This often comes in the form of information, through expertise or research, which is expected to be incorporated into

financial decision-making. Just like financial regulators, policymakers are instrumental in achieving the objectives set out in the field of sustainable finance. They develop the directives which shape regulations and frameworks. Additionally, they provide incentives, for example, economic ones, which encourage responsible business practices and can reshape countries' economies to become more sustainable (Ioannou and Serafeim, 2012). These actors create the sustainable finance ecosystem, whose combined efforts are directed at addressing social and environmental challenges.

The importance of sustainable finance to address environmental challenges comes from their capacity to mobilize capital towards environmentally sustainable projects and to contribute to a transition to a sustainable economy. To what extent sustainable finance will be capable of addressing these challenges remains an unanswered question. The debate around the role of sustainable finance broadly concerns two positions, (1) the positive environmental impact that it can have and (2) the uncertainties and lack of availability to address the challenges. Financial actors are expected to be able to mitigate climate risks by investing in technology adaptation and mitigation efforts, which would improve the risk-adjusted returns that investors look for (Jin, 2020). Furthermore, long-term value creation, enhanced brand reputation, and access to a growing market are all drivers for investors to generate positive environmental impact through engaging with principles of sustainable finance (Zumente and Bistrova, 2021). Notably, the financial sector changes in response to regulations which is imposed by governments (Oyegunle and Weber, 2014). These are some of the drivers that motivate investors and financial institutions to have a positive environmental impact. On the other hand, there are also significant challenges for sustainable finance to mobilize capital towards environmentally sustainable projects. Some key challenges include the limited availability of capital and high upfront costs of investing in projects (Soundarrajan and Vivek, 2016). This disincentivizes investors and financial institutions from allocating capital. Projects in sustainable finance are also characterized by uncertainties in financial returns, market volatility, and regulatory changes, which decrease the risk-return and consequently negatively affect investor confidence in projects (Hafner et al., 2020; Migliorelli, 2021). Another key challenge to mobilizing capital is greenwashing risks (Berensmann and Lindenberg, 2016). At the corporate level, the financial sector engages more pronouncedly in greenwashing than others, further reducing investor confidence in the sustainable finance products they acquire (Baldi and Pandimiglio, 2022). The role of sustainable finance in mobilizing capital becomes impeded through these challenges. As a whole, the financial industry already faces legitimacy challenges. The financialised global economy has been continuously causing growing social inequality and environmental destruction (Ahlström and Monciardini, 2021). Sustainable finance proposes itself as a remedy to the ails which the finance industry itself has been causing and encounters significant legitimacy challenges. There are some key methods in which sustainable finance contributes to the transition to a sustainable economy. By providing financial support for carbon-reducing projects and by divesting from carbon intensive industries, the sustainable finance industry can use decarbonization to face environmental challenges (Liebel, 2021). Investing in renewable energy sources and divesting from fossil-fuel energy

sources would be an illustrative example. A further method would be the adoption of sustainable practices in industries. Through providing incentives and guidance, financial institutions can encourage sustainable business practices in the companies they invest in (Oh, Park and Ghauri, 2013). Access to cheaper capital, business networks for sustainable development, and consulting services are some methods through which impact can be achieved. Additionally, sustainable finance can stimulate economic growth and job creation within sustainable industries. By investing in industries such as wind energy, supporting industries are created and supported. Increased demands for goods and services in the surrounding area as well as increased demand for maintenance engineering skills can have widespread economic benefits. Hence, the argument is that by integrating sustainability criteria into financial decision-making long-term economic benefits are generated. These allow for improved environmental benefits if the projects that are invested in contribute to environmental protection.

## European Union's Approach to Sustainable Finance

The EU first introduced regulations that required companies to disclose non-financial information such as environmental and social aspects in the early 2000s (European Parliament, 2021). By pioneering the field of sustainable finance, the EU aimed at promoting sustainable investment practices. To achieve this they established the European Sustainable and Responsible Investment Forum (EUROSIF, 2021). On the progress of the forum, the EU launched an action plan for the Capital Markets Union, which aimed to boost funding for the real economy and sustainable finance. To further increase the attention on sustainable finance the EU established the High-Level Expert Group (HLEG) on sustainable finance to provide recommendations on how to integrate sustainability considerations into the EU's financial system (finance.ec.europa.eu, 2016). Their final report proposed a range of measures to promote sustainable finance, including the establishment of a taxonomy for sustainable activities, the development of sustainability standards, and the creation of a sustainable finance label (finance.ec.europa.eu, 2016). Subsequently, the EU developed the Action Plan on Financing Sustainable Growth. Its aim was to complete the objectives of the Paris Agreement on climate change and the United Nations' Sustainable Development Goals (SDGs) (Möslein, 2018). The SDGs have also been instrumental in shaping the evolution of European sustainable finance. As a framework for sustainable development, covering a range of issues including poverty, health, education, and climate change, the SDGs inform strategic targets which sustainable finance can work towards (Morton, Pencheon and Squires, 2017). As a consequence of these events and frameworks, various measures have been implemented to promote sustainable finance. The Paris Agreement on climate change also played a significant role in the evolution of sustainable finance (Migliorelli, 2021). It set a global target of limiting the increase in the average global temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the increase to 1.5°C. By setting the target, economies required significant investment in renewable energy, energy efficiency, and low-carbon infrastructure. To achieve these targets, the EU established the European Green Deal, which includes a number of initiatives aimed at promoting sustainable finance.

The European Green Deal and its Action Plan set out a roadmap for a sustainable financial system and included a range of measures aimed at promoting sustainable finance. These focus on various sectors, including energy, transport, agriculture, and industry, in order to promote clean and renewable energy sources, increase energy efficiency, foster circular economy practices, protect biodiversity, and ensure a just and inclusive transition.

### The European Green Deal

The European Green Deal aims to solidify the EU’s position as a global leader in the fight against climate change (Zeben, 2020). The plan outlines a number of measures to encourage the

development of sustainable financial products, as well as including sustainability considerations in investment decisions (Möslein, 2018). These sustainability considerations are referred to as Environmental, social and governance (ESG) factors. For example, carbon emissions, air and water pollution, deforestation, and ethics in social media could be included in investment decision-making (Parker, 2021). Including these ESG factors in investment decisions leverages private finance to achieve key European policy objectives. The main objectives include (1) reorienting capital flows towards a more sustainable economy (2) mainstreaming sustainability into risk management (3) fostering transparency and long-termism (Gonzalez, 2021). To achieve these objectives, the proposals included the creation of a classification system for sustainable activities, the development of sustainability benchmarks, and the promotion of transparency and disclosure of ESG information (European Commission, 2019). This led to the establishment of three key regulations: the EU Taxonomy Regulation, the Corporate Sustainability Reporting Directive (CSRD), and the Sustainable Finance Disclosures Regulation (SFDR) (European Commission, 2019). Combined, these aim to engage various actors within the sustainable finance space to achieve the policy objectives. These regulations aim to integrate sustainability considerations into financial markets through the following mechanisms.

The EU Taxonomy is designed as a standardized and comprehensive classification system for sustainable economic activities. By classifying which activities are sustainable and which ones are not, it acts as a guide for investment decisions (Schütze and Stede, 2021). The activities cover up to 80% of the greenhouse gas emissions in the EU and by classifying these activities the taxonomy can play an important role in channeling investments into low-carbon technologies by helping investors to make informed decisions (Schütze and Stede, 2021). The CSRD on the other hand aims to integrate sustainability considerations into financial markets to enhance transparency through standardizing reporting practices for environmental, social, and governance (ESG) information. Through expanding the reporting obligations of companies to disclose comprehensive and consistent ESG information, the CSRD attempts to improve the quality, comparability, and relevance of sustainability reporting. By further widening the range of companies that are mandated to disclose information, the directive enables stakeholders to assess a broader set of a company's sustainability performance (Zetzsche, Bodellini and Consiglio, 2022). Through mandated reporting, sustainability factors are integrated into business strategies, operations, and decision-making processes (Zetzsche, Bodellini and Consiglio, 2022). The key contribution of the CSRD is providing investors with reliable information to make informed decisions (Busch, 2023). Improved quality and quantity of information is theorized to affect behavioral change within investors, who would now be more capable of aligning their investments with sustainable objectives. Leveraging information to improve decision-making is the same mechanism used by the SFDR to integrate sustainability considerations into financial markets (finance.ec.europa.eu, 2019). This is achieved by generating transparency by providing comprehensive information on the sustainability characteristics of investment products (finance.ec.europa.eu, 2019). Financial market participants are required to disclose their

integration of sustainability risks and factors into their investment decision-making processes (Busch, 2023). By mandating this disclosure, the SFDR generates comparable information for investors and additionally provides regulatory agencies with leverage for enforcing environmental compliance (Busch, 2023).

**Challenges**

There are some key challenges that the European sustainable finance agenda faces. Some challenges are pragmatic and implementation based, while others are more ideological or principle challenges. Key ideological challenges regard the difficulty in shifting economic priorities and definitions of what counts towards sustainability. Sustainable finance inherently comes with a challenge to current economic thought. Current business models and investment priorities become less compatible with the changes proposed by European legislation. As a consequence, the efficacy of the European sustainable finance agenda relies on overcoming these challenges.

A key challenge is balancing the economic and financial aspects of sustainable finance with social and environmental objectives (Kumar et al., 2022). Profit motives by companies need to be balanced with sustainable practices which are complete social and environmental objectives (Kumar et al., 2022). A further challenge is overcoming the reluctance of some businesses to disclose any ESG information (Bartels and Schramade, 2022). For some businesses within industries, it is disadvantageous to disclose information that could undermine its business model. Therefore they might engage in selective disclosure practices, undermining the sustainable finance agenda (Dando, 2003). Investors can struggle to identify which companies are truly sustainable as a result. By investing according to the principles of sustainable finance, investors and financial institutions would be prioritizing long-term sustainability over short-term returns (Richardson, 2008). Challenges include incentivizing investors to do so and maintaining the motivation of investors who already engage in sustainable practices. A further implementation challenge lies in striking a delicate balance between the imperative of standardized reporting and the accommodation of diverse business models and sectors (Chiu, 2022). Achieving comparability in sustainability impacts across businesses is critical to optimize resource allocation (Ioannou and Serafeim, 2017). This requires the development of reporting frameworks that capture the nuances of varying industries while ensuring the comparability of information. On a political level, the key challenge would be to harmonize and develop consistency in sustainability definitions and standards across the member states of the European Union (Acreman and Ferguson, 2010; Harnesk, Brogaard and Peck, 2017). For example, the EU Taxonomy Regulation requires consistent interpretation and application of the taxonomy criteria across member states (Siri and Zhu, 2019). This requires collaboration among EU member states to establish unified sustainability definitions and standards, which can be difficult to achieve. France and Germany have recently clashed due to differing definitions of what a sustainable

energy mix entails. While France favors a nuclear solution, Germany has had a longstanding commitment to decommissioning nuclear power plants (Schmitz, 2022). Consequently, including nuclear energy in the taxonomy would be disadvantageous to Germany, while France would highly favor it. Political challenges such as these need to be overcome to maintain the momentum of the European sustainable finance agenda.

Furthermore, there are pragmatic and implementation challenges to the sustainable finance agenda. A challenge is ensuring consistent interpretation and implementation of sustainable finance policies across member states to achieve cohesive sustainable finance practices throughout the EU (Siri and Zhu, 2019). Additionally, sustainability considerations are complex and require integration into financial products and services (Tuyon et al., 2022). By developing innovative tools and methodologies that capture and measure environmental and social impacts accurately, such as standardized metrics which assess the carbon footprint of financial portfolios, sustainability considerations can be more consistently integrated. Implementing robust risk assessment tools to overcome the challenges of assessing and managing sustainability risks face similar difficulties (Tuyon et al., 2022). Conducting comprehensive environmental and social due diligence to identify potential risks and opportunities associated with investments remains a challenge within sustainable finance. Finally, a critical pragmatic challenge is the limited availability of reliable and standardized ESG data which complicates investment decision-making (Grim and Berkowitz, 2020; Sakis Kotsantonis, Pinney and Serafeim, 2016). To overcome this, efforts are being made to enhance data collection and disclosure practices and develop common ESG reporting standards. For instance, various initiatives such as the Global Reporting Initiative (GRI) and Sustainability Accounting Standards Board (SASB) aim to standardize global ESG reporting and improve the quality and comparability of data. These would also apply within the EU but are likely to be supplemented with mandatory disclosure regulation.

The sustainable finance agenda in the EU faces several potential obstacles, including the lack of harmonized standards, the inherent contradictions and limitations of sustainable finance, and the insufficient quality of sustainability reporting. A key obstacle is the lack of harmonized standards. This is exemplified in agriculture by the limitations of harmonizing a European system due to geographical diversity, crops, and processes for biomass and bioenergy (van Dam and Junginger, 2011). Developing a common understanding of sustainability criteria would promote consistent sustainability practices across different regions and sectors. Additional work is also required in the financial sector, where sustainability metrics development is needed to inform the investment sector about sustainable performance in companies (Chiu, 2022). Another obstacle is the perceived inherent contradictions and limitations of sustainable finance. While integrating sustainability considerations could be a potential antidote to fight financialization and short-term focus, this has not yet materialized. Its adoption has shown limited effects and may paradoxically promote further financialization (Ahlström and Monciardini, 2021). This might delegitimize efforts in the environmental movement, which reveals the complexities of

reconciling sustainable finance objectives with dominant economic ones (Ahlström and Monciardini, 2021). Insufficient quality of sustainability reporting is another obstacle faced by the sustainable finance agenda. Various methods and significant gaps in reporting practices exist which hinder the comparability and reliability of sustainability information (Oprean-Stan et al., 2020). However, integrated reporting has been found to have a strong relationship with a company's reputation, generating further support for comprehensive and standardized reporting practices (Landau et al., 2020). Companies might be incentivised to do so, as studies have shown that the quality of disclosure and the publication of non-financial statements positively impact investor perceptions and company value (Oprean-Stan et al., 2020). The sustainable finance agenda in the EU faces these potential obstacles and will require regulation to prevent them.

## The Sustainable Financial Disclosure Regulation (SFDR)

### Overview and Objectives of the SFDR

European Green Deal and its Action Plan set to promote sustainable finance through the establishment of three key regulations: the EU Taxonomy Regulation, the Corporate Sustainability Reporting Directive (CSRD), and the Sustainable Finance Disclosures Regulation (SFDR). Under the SFDR financial services participants such as asset managers and investment funds, are required to define their strategic positioning with respect to sustainability (Bengo, Boni and Sancino, 2022). Financial market participants (FMP's) and financial advisors (FA's) are obliged to disclose to end-investors the integration of sustainability risks into all investment processes and for financial products that pursue the objective of sustainable investment (finance.ec.europa.eu, 2019). Disclosure obligations regard adverse impacts on sustainability matters at entity and financial products levels. Therefore, financial market participants and financial advisers are required to disclose if they consider negative externalities on environment and social justice of the investment decisions/advice (finance.ec.europa.eu, 2019). If this is the case they are obliged to indicate how this is reflected at the product level. What makes a sustainable investment according to the SFDR is defined by the following:

*" … an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, 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."*

The SFDR represents a significant European regulatory development with the aim of reshaping the financial industry's approach to ESG factors. Its aim is to leverage ESG disclosure and reporting obligations in order for sustainability to become an integral part of investment decision-making processes (Cremasco and Boni, 2022). According to the EU, investment decisions and financial advice might cause or contribute to negative material effects on the environment and society, which necessitates disclosure (finance.ec.europa.eu, 2019). By mandating these disclosures, it provides additional disclosure requirements to the existing elements of relevant financial sectoral legislation (finance.ec.europa.eu, 2019). The purpose of the SFDR specifically is to require financial players to formally declare their degree of compliance to ESG disclosure and reporting obligations, in an effort to prevent greenwashing by leveraging transparency as a methodology (Cremasco and Boni, 2022). This purpose is reflected in article 1 of the SFDR which states that:

*"this Regulation lays down harmonised rules for financial market participants and financial advisers on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes and the provision of sustainability-related information with respect to financial products"*

Within article 1 of the SFDR it is clearly stated that the objective is to enhance transparency within the financial industry by promoting consistent and comparable disclosure of ESG information. As it is a regulation aimed at end investors, the SFDR attempts to generate transparency for investors, as it allows them to assess the environmental and social impact of their investments. Furthermore, they are able to evaluate the sustainability performance of companies and make informed decisions aligned with their values and objectives. By mandating clear and standardized disclosure requirements, information is generated that enables investors to evaluate the sustainability credentials of financial products more effectively.

Another key objective of the SFDR is to prevent greenwashing through leveraging information disclosure and clarifying the meaning of sustainable finance (Barbet, 2023). Greenwashing can mislead investors who seek genuine sustainability in their investment choices and undermine the capacity of sustainable finance to drive change. One of the key mechanisms employed by the SFDR to prevent greenwashing is through information disclosure. The regulation requires that market participants provide transparent and accurate information about the sustainability characteristics and impacts of their financial products (finance.ec.europa.eu, 2019). This occurs at both the product and entity levels. By leveraging the disclosed information, the SFDR seeks to

ensure that investors have access to reliable and consistent data, allowing them to make informed decisions aligned with their sustainability goals.

This plays into the achievement of a further goal. The SFDR attempts to achieve the harmonization and standardization of criteria and definitions (finance.ec.europa.eu, 2019). Establishing clear criteria and definitions of sustainable investments and activities through a standardized framework allows the regulation to prevent confusion in the assessment of sustainability in finance. By clarifying the complexities surrounding definitions, investors and market participants can more readily identify genuinely sustainable financial products from ones that are labeled as sustainable, while underperforming on environmental criteria (Bengo, Boni and Sancino, 2022). By establishing a common understanding of sustainable investments, the SFDR additionally enhances comparability and consistency across different jurisdictions and financial institutions (Barbet, 2023).

**Scope and applicability of the SFDR**

As a regulation within the EU, the SFDR primarily applies to the financial institutions operating in the EU, such as banks, insurers, asset managers, and investment businesses. It also applies to all financial market participants (FMP's) and financial advisers based in the EU, as well as investment managers or advisers based outside of the EU who market their products to clients in the EU. The SFDR came into effect on March 10, 2021, and takes the form of comprehensive sustainability disclosure requirements covering a broad range of ESG metrics at both entity and product-level to FMP's through websites, prospectuses, and quarterly reports. Disclosure is required with regard to the integration of sustainability risks and the inclusion of adverse impact considerations, both in the processes of FMP's and in the provision of sustainability-related information with respect to their financial products (Busch, 2023). Financial intermediaries are required to provide transparency about sustainability information pre-contractually. They are required to do so on their website, in periodic reports, in promotional material at both entity level and product level (Busch, 2023).

The entities obliged to report by the SFDR are the financial institutions mentioned above. On the other hand, the financial products which are affected by the SFDR include investment funds, such as UCITS (Undertakings for Collective Investment in Transferable Securities) and AIFs (Alternative Investment Funds), as well as pension funds, insurance-based investment products (IBIPs), portfolio management services, and financial advisory services. All of these financial products are involved in the management and investment of funds on behalf of investors. Various regulatory requirements apply to these funds in order to protect investors' interests and ensure market integrity. The SFDR covers these products because they play a significant role in the financial industry, as the most commonly used products, and can have a substantial impact on

sustainability (Brühl, 2021). These financial products are therefore critical in mobilizing capital towards environmentally sustainable projects. By adhering to sustainable finance principles and disclosing relevant information to investors, it is expected that the SFDR can have a positive environmental impact. Furthermore, the SFDR also includes a wide range of environmental, social, and governance (ESG) metrics at both entity- and product-level, to provide a more integrated approach (Bengo, Boni and Sancino, 2022). These metrics include but are not limited to carbon emissions, water usage, biodiversity impact, labor standards, human rights, and board diversity. By including these ESG metrics, the SFDR aims to address key sustainability concerns and encourage FMP's to consider the broader social and environmental impacts of their investments. This information should widen the financial considerations and include factors that are non-financial but essential for a sustainable and responsible financial system.

**Key provisions and requirements of the SFDR**

The SFDR has specific provisions for both entity and product-level disclosures. Combined these provisions provide the framework of the disclosure requirements for any financial institutions operating in the EU and covered under the SFDR. The regulation has a variety of articles that detail these provisions. The articles provide insight into how the disclosure requirements are meant to concretely achieve the objectives set out by the SFDR. All the articles can be found in the regulation itself (finance.ec.europa.eu, 2019).

At the entity level, the disclosures are regulated under Articles 3, 4, and 5 of the SFDR. Article 3 requires financial market participants to publish information on their websites about their policies related to how sustainability risks are considered in their investment decisions. This is similar for financial advisers, as they are required to disclose on their website the policies on how sustainability risks are considered when giving advice. Article 4 defines the obligations at the entity level for disclosures on the adverse sustainability impacts. FMPs are required to publish information on their website where they explain the principal adverse impacts (PAI) on sustainability factors within their investment decisions. The regulation is not applied equally to all FMPs, as those under 500 employees are not mandated to disclose. However, those FMPs not affected are required to follow the "comply or explain" principle. The comply or explain principle means that FMPs and FAs must either comply with the SFDR's requirements or explain why they are not complying. When they do comply, the information published is required to include the due diligence processes regarding PAI. Investors must be informed on how investments have a negative impact on sustainability indicators and what kind of method is used to arrive at the conclusions. Financial market participants and financial advisors are required to publish information, even if they are not considering PAIs. If this is the case, they are required to provide a clear explanation of why they are not including PAI considerations in their decision-making. Disclosures within Article 5 regarding how remuneration policies are

structured with the consideration of sustainability factors. FMPs and FAs are required to include an explanation within their remuneration policies on how these are consistent with the integration of sustainability risks. The information required to be disclosed in all of the articles above is required to be published on the website of the FMPs and FAs. Entity-level information is required to be published irrespective of the extent to which the financial products provided by the FMP are sustainable.

At the product level, the SFDR mandates disclosure to explain the extent to which products are sustainable. Within the regulation, there are three categories of investments that allow investors to more readily differentiate products. The disclosure obligations depend on where FMPs want to position their products. Under the first category, which mandates disclosure under Article 6, financial products are only required to take into account sustainability risks in their investment decisions. This is the least sustainable option according to the SFDR. Article 8 covers products that promote environmental and social characteristics. The second category is therefore reserved for products that are somewhat but are not exclusively sustainable. Under the final category, which is covered by Article 9, financial products are inherently designed for sustainable investment. This category is considered the gold standard under the SFDR. Classification according to these categories has implications for what financial products can contain and how FMPs are allowed to market them. For example, the name of the investment fund and the use of words such as sustainability or ESG is exclusively limited to products that disclose information required by Articles 8 and 9. A possible way of interpreting this categorization is therefore that Article 6 mandates disclosure for any product which does not attempt at being sustainable, while Articles 8 and 9 represent sustainable products.

Article 6 mandates that FMPs must include pre-contractual information on how sustainability risk is considered in their investment decisions, and if not, an explanation for why this is the case. Sustainability risks could be analyzed through an understanding of ESG factors and their impact on the investment decision. If there are any events or processes which might have an impact on the company, this would be included in the description. For example, the FMP could disclose its waste management processes as a sustainability risk. FMPs are also obliged to disclose how the sustainability risk can impact the value of the company. To extend the example, if the waste management process requires processing through incineration, which might become more expensive in the future, this would have an impact on the company's fixed cost and therefore its overall value. If FMPs do not consider sustainability risks in their products, they are obligated to explain why sustainability risks are not being considered.

Article 8 sets in place disclosure obligations for financial products which promote environmental or social characteristics. FMPs provide an explanation for how these characteristics are included in the product and by what method they achieve the objectives set out. They are not required to comply with a certain product design, such as the investment composition or financing structure. For example, FMPs whose fund invests in renewable energy companies would not be required to

disclose how the fund is structured but would be required to disclose how the companies are contributing to the reduction of greenhouse gas emissions. Additionally, pre-contractual information on good governance practices within the companies which compose the financial product is mandated.

Article 9 places disclosure requirements for products that aim to be sustainable investments as defined above. Any FMP which wants to sell a financial product under Article 9 is obliged to clearly define, pre-contractually, how the product fulfills the definition. Additional to all the disclosure requirements of Article 8, Article 9 also requires an explanation for the metrics and methods used to achieve the objective of sustainable investment. The design of such financial products, concerning the composition or strategy, is not mandated by Article 9. However, unlike Article 8, financial market participants are obliged to indicate how the chosen mix aligns with the sustainable investment objectives of the product. For instance, a financial product that targets renewable energy infrastructure development needs to clarify how the investment contributes to an environmental objective such as greenhouse gas reduction. If the fund includes other assets for improved liquidity or reduced risk, then the fund has to explain how these assets are consistent with the overall environmental objectives of the financial product. By doing so, the investment can be considered sustainable.

Initially, the SFDR came into effect on March 10, 2021, and mandated the comprehensive sustainability disclosure requirements discussed above. specific provisions for both entity and product-level disclosures exist, however, missing some key details. Level 2 of the SFDR was introduced in January 2023, with key features which enhance the already existing disclosure requirements. Product and entity-level disclosure requirements have become more detailed, covering a broader range of ESG metrics at both levels. To report more effectively, the SFDR introduced Regulatory Technical Standards (RTS), which provide mandatory templates to be used in the information disclosure process. These templates cover a broad range of ESG metrics and require financial institutions to disclose information on the most applicable articles of the SFDR. Information on how sustainability risks are integrated into the investment decision-making process, how the principal adverse sustainability impacts of investment decisions are considered, and how the sustainability characteristics of investment products are disclosed is now also required to be disclosed periodically. This allows for a more continuous assessment of the sustainability impacts of any fund. The most critical change with level 2 is the stricter requirements for financial institutions. Specifically, the requirement to identify any harmful impact made by investee companies. By doing so, financial institutions are obliged to understand with more depth the ESG impacts of their activities. With these novel changes, Level 2 is considered a critical development in the EU's Sustainable Finance agenda. Through the added depth it aims to improve the transparency and comparability of sustainability information for investors.

**SFDR's effectiveness in promoting transparency, accountability, and reducing greenwashing**

The development of these provisions for financial institutions under the SFDR has significant implications for the operations and considerations of FMPs and FAs. While the implications are widespread, some of the key implications involve developing transparency and accountability, as well as mitigating greenwashing.

As a fundamental aim of the SFDR, increasing transparency with these provisions would occur through the pre-contractual information provided, improved understanding of sustainability risks, and more periodic disclosures. The two-pronged approach of FMPs increasing their own understanding and investors increasing their understanding and scrutiny allows for a clearer integration of sustainability risk in the decision-making process. Investors are thereby able to leverage their sustainability preferences to hold financial institutions to account. By mandating periodic disclosures the SFDR further promotes a consistent flow of sustainability-related information. This periodicity of reporting ensures that the disclosed data remains current and relevant. Additionally, it enables ongoing monitoring of sustainability considerations in investment practices. Transparency is therefore thought to be improved through the method by which information is disclosed.

A further implication of the establishment of the SFDR is an enhancement of accountability, which is exemplified through the "comply or explain" approach. FMPs not only are required to consider the sustainability risks within their operations but also to clearly convey the reasoning behind their decisions. FMPs that do not comply face substantial consequences, further increasing a collective sense of responsibility to adhere to the disclosure requirements. Theoretically, this increased information should shift industry norms through further awareness of who and how is damaging the environment. By mandating that the link between environmental performance and remuneration policies is explained, managers face greater accountability and personal consequences for the environmental consequences of their decisions. Furthermore, having a continuous flow of relevant information reinforces this accountability, ensuring firms consistently uphold their commitment to sustainable practices. By including these consequences, the SFDR enhances the accountability of FMPs and FAs towards the environmental outcomes that they contribute to.

A further implication as a consequence of the provisions is how greenwashing is approached. Several strategies are applied to reduce the risk of greenwashing by FMPs and FAs. Firstly, by establishing a product categorization framework according to articles 6, 8, and 9, the SFDR clearly delineates investment products according to their sustainability. This structured approach enhances clarity and comparability amongst the financial products that FMPs and FAs provide. Secondly, it imposes augmented reporting requirements for sustainable products. This ensures a more rigorous and consistent disclosure of relevant data. Thirdly, it requires an explanation of the

methodologies employed to assess the sustainability of any investment, deepening the understanding for both financial institutions and investors of the decision-making process behind sustainability investments. This offers an added layer of transparency and should theoretically increase scrutiny on unsupported claims of sustainability. Finally, the SFDR attempts to reduce misleading claims by mandating disclosure templates under Level 2. By standardizing the forms, sustainability-related information is delivered in a comparable and consistent manner. Misleading claims are harder to make when the information required to be disclosed is less ambiguous  The multipronged approach taken by the SFDR develops some methods to reduce the risk of greenwashing.

# Results & Discussion

## Introduction

The following chapter evaluates the results from the conducted research, providing insight into the intertwined concepts of transparency, accountability, and greenwashing, their multifaceted meanings and applications within the intricate context of the Sustainable Finance Disclosure Regulation. Recognizing that these notions are not merely standalone ideas but part of a broader narrative that is profoundly shaped by the contextual specifics of each concept, the *who, to whom, about what,* and *to what ends/in what manner.* The chapter attempts a document analysis of the SFDR, aimed at unveiling the underlying assumptions and frames that subtly, yet critically, define the approach to sustainable finance which the SFDR takes. The complex nature of the stakeholders and their interaction with the SFDR shape their potential influence on how transparency, accountability, and greenwashing are perceived and enacted. This in-depth examination is followed by a detailed exploration of major themes derived from interview data, assessing the contextual implications these concepts embody within the framework of sustainable finance. Following the interview analysis, the chapter leads into a cross-analysis, juxtaposing the themes emerging from the interview data with the findings from the SFDR document analysis. By cross-examining results, connections and contrasts emerge that shed light on the nuanced dynamics between the concepts of transparency, accountability, and greenwashing. This explicitly compares the expectations and possibilities of the SFDR to achieve its aims through the document analysis with the current interpretations by professionals who are currently engaged with its implementation through the interview analysis. The chapter concludes with an assessment of conceptual limitations which shape the confines of this research.

Before delving into the analysis, a brief recap of the key concepts within the theoretical framework will be presented. The theoretical framework is subdivided by the three core concepts, transparency, accountability and greenwashing. Each concept is shaped by its contextual specifics, the *who, to whom, about what* and *to what ends/in what manner.* These normative and relational components of each concept differ slightly in how they emerge, as specified in the theoretical framework. The key typologies of each concept are as follows. For transparency there are two typologies, Tienhaara's multiple types and the four rationales as described by Gupta and Mason. Tienhaara suggests multiple types of transparency; conventional, deliberative technocratic, disciplinary, and disruptive transparency. Gupta and Mason (2016), offer a typology of their own, where transparency, or information disclosure, could follow one of four different rationals; democratization rationale, marketization rationale, technocratization rationale and privatization rationale.

Accountability can be viewed through the following typology. The fundamental elements which constitute accountability are structured according to Biermann & Gupta (2011) in four key concepts: a normative, relational, decision, and behavioral element. These need to all be sufficiently present to consider any accountability relationship as meaningful. Unlike transparency and accountability, greenwashing does not have sufficient literature where a typology as such has been presented. As a concept, greenwashing can be most clearly defined as the difference between an actor's symbolic actions and their substantive actions within their self-defined sustainability approach (Siano et al., 2017). In other words, actors communicate a position or achievement on environmentalism without fulfilling the basic environmental criteria to substantiate their claim. Mechanisms of greenwashing have been classified in the literature, with the most prominent ones being Lyon and Montgomery's mechanisms of misleading behavior and De Silva Lokuwaduge and De Silva's firm-level greenwashing. Two examples from Lyon and Montgomery's mechanisms would be *decoupling*, which is the disconnect between the activities and the structures of an organization and *selective disclosure*, whereby actors disclose positive information while withholding negative information. Two examples from firm-level greenwashing, would be companies having an inherently unsustainable business, yet promoting sustainable practices or products and companies affecting regulations or governments to obtain benefits in areas of sustainability.

## Document analysis

### Introduction

Each concept is shaped by key normative and relational components, the *who, to whom, about what* and *to what ends/in what manner*, which differ slightly in how they emerge, as specified in the theoretical framework. During the document analysis, these key components were identified and have been summarized in *Table 2*. The regulation proposes that financial market participants (FMPs) and financial advisers (FAs) need to disclose information for the benefit of end investors. As such FMPs and FAs can be identified as the *who* component, since they are the actors who are meant to be transparent and accountable towards others, and are also the actors capable of engaging in greenwashing. The primary relationship present here is between the financial institutions and their end investors. Within the regulation it is described that its objectives are to "*strengthen protection for end investors and improve disclosures to them*", which makes them the clear receivers of whatever information gets disclosed (finance.ec.europa.eu, 2019). While there are other stakeholders who can make use of the information, it is most apt to describe end investors as the *to whom* across the three concepts. Other potential stakeholders could be either regulators or activists, who can make use of the information for alternative purposes than investment decisions.

The normative dynamics which emerged from the document analysis varied across the three concepts. Identifying *about what* financial institutions should be transparent is specified in the regulation. FMPs and FAs are required to identify and disclose sustainability risks and impacts, how such risks are integrated into investment decisions and disclose sustainability-related information with respect to financial products. *About what* financial institutions can be held to account by investors are the methods by which they integrate sustainability risks into their processes and consider adverse sustainability impacts of their investments. For the concept of greenwashing this normative component differs. The SFDR does not directly mention greenwashing. If FMPs and FAs want to engage in greenwashing they are only able to manipulate the information which they disclose. Therefore, *about what* they greenwash is hidden in the selective choice they make on what information related to sustainability characteristics of financial products they disclose and how they characterize the potential for negative impacts on sustainability factors due to investment decisions. What remains common between all three concepts is that financial institutions use and present information in some shape or form. The *nature of information* is the lining which ties all three concepts together.

The final normative dynamic is the *in what manner* component, which reflects how the actors identified as *who* and *to whom* interact on the content of *about what*. Transparency is demonstrated through information disclosure in pre-contractual information, periodic reports, and through maintaining information about these policies on their websites. This indicates that for this normative dynamic there exists some level of periodic interaction between FMPs/FAs

and end investors, based on the accessible disclosure documents and periodically updated information. Accountability is demonstrated through the development of risk management policies and the integration of sustainability risks in decision-making procedures. These can be reviewed and compared by end investors. The SFDR does not directly address greenwashing. Hence for this analysis *in what manner* greenwashing occurs is less about the actions taken and more about the actions potentially avoided or misrepresented. Greenwashing would therefore be characterized by the potential manipulation or omission of sustainability-related information in disclosures and reports. Just as every concept is shaped by the normative and relational components which exist in the SFDR, each concept has its own assumptions and implicit meanings which emerged from the document analysis.

| | **Transparency** | **Accountability** | **Greenwashing** |
|---|---|---|---|
| **Who** | Financial market participants and financial advisers | Financial market participants and financial advisers | Financial market participants and financial advisers |
| **To Whom** | End investors and potentially regulators or activists | End investors and potentially regulators or activists | End investors and potentially regulators or activists |
| **About What** | (1) Sustainability risks and impacts<br><br>(2) How sustainability risks are integrated into investment decisions<br><br>(3) Sustainability-related information with respect to financial products | (1) Integration of sustainability risks into their processes<br><br>(2) Consideration of adverse sustainability impacts | (1) Information related to sustainability characteristics of financial products<br><br>(2) Potential for negative impacts on sustainability factors due to investment decisions |
| **In What Manner** | Through disclosures in pre-contractual information, periodic reports, and maintaining information about these policies on their websites | (1) Through the development of risk management policies<br><br>(2) Through the integration of sustainability risks in decision-making procedures | Through the potential manipulation or omission of sustainability-related information in disclosures and reports |

*Table 2. Normative and relational components identified in the document analysis.*

**Transparency**
Transparency's implicit meaning within the SFDR is shaped by the concept of information and the practices of this information. Part of the regulation's objective is to "achieve more transparency", which is operationalised through sustainability information being available to end investors (finance.ec.europa.eu, 2019). The implicit meaning of transparency is therefore *information disclosure*, with more disclosure meaning more transparency. The second element of the implicit meaning of transparency is the practice or presentation of this information in a specific form. So when transparency is enhanced there should be more information disclosed, but also disclosed in a particular manner. In the case of the SFDR this is in pre-contractual information which is periodically maintained. Information is therefore required without any compensation from end investors. This formulation of transparency allows for some assumptions about what transparency is and what effects it would have to emerge. The key assumptions about transparency present in the text of the SFDR is that transparency enhances accountability, informs investment decisions, encourages better sustainability practices, can prevent greenwashing, requires standardization, and requires periodic updates.

The assumption present in the SFDR is that transparency enhances accountability by requiring financial market participants to provide detailed disclosures regarding their consideration of sustainability risks, principal adverse impacts and due diligence policies. By requiring pre-contractual information the regulation assumes that FMPs and FAs will factually present sustainability information, since doing otherwise will incur consequences. These consequences are most notably directed at what end investors are able to do, which could be criticism or divestment from the financial institution. This directly relates to a further assumption the SFDR makes, which is that transparency is only effective if ongoing. By providing pre-contractual disclosures and periodic reports, the SFDR necessitates timely information for the mechanism of transparency to be effective. This inherently recognizes the changing nature of sustainability practices and recognizes that investment decisions rely on accurate and timely information. These concepts are underpinned by the assumption within the regulation that providing information about the integration of sustainability risks into investment decisions and their impact on returns will improve investors' decision-making capacity. Transparency, or information disclosure, would allow investors to compare the sustainability risk profiles and estimated returns between financial products and evaluate how those risks are managed. It is supposed that through this capacity, sustainable investment practices will be increased.

There are also other mechanisms through which the SFDR implies that transparency could be a driver for improved sustainability practices. By requiring financial market participants to disclose how they consider the principal adverse impacts of investment decisions on sustainability factors, the regulation highlights knowledge internally, increasing the likelihood that information will be used in the decision-making process. Furthermore, if knowledge is

available to stakeholders outside of the FMP, then behaving unsustainably could incur reputational damages. Consequently FMPs will not want to disclose poor sustainability practices, leading them to improve these practices to avoid negative disclosures and reputational damages. Furthermore, the SFDR emphasizes the need for standardization for effective transparency, implying that without it, the information provided might not enable meaningful comparisons. Information disclosed needs to be standardized to be comparable, which is why the SFDR prescribes specific requirements for the types of information that should be disclosed and how it should be presented. By requiring mandatory standardized disclosure about sustainability practices, the SFDR assumes that greenwashing can be prevented. Information being disclosed in a standardized format is assumed to impede the capacity of financial institutions to make vague or misleading claims about their sustainability efforts. Since FMPs and FAs are required to present information in the same way as others do, they are reduced in their ability to selectively disclose what might frame them in a positive "green" light. This further allows for meaningful comparison by investors, which increases the pressure to engage in positive environmental action to avoid reputational or investment consequences. The assumptions about transparency that emerge from the analysis of the SFDR, are best reflected by two components of the theoretical framework, the *technocratization* and *privatization* rationales by Gupta and Mason.

Gupta and Mason propose that actors might promote transparency to rationalize and improve decision-making, relying on expert drive technical information to gain validity and reduce information asymmetries between actors (Gupta and Mason, 2016). The assumptions about transparency identified in the SFDR fit with the technocratization rationale, as they view transparency as able to inform investment decisions through information disclosure and apply complicated rules and guidelines to achieve this objective. Information disclosure is thought to reduce information asymmetries between end investors and financial institutions. This is explained in the regulation as follows: *"This Regulation aims to reduce information asymmetries in principal‐agent relationships with regard to the integration of sustainability risks, the consideration of adverse sustainability impacts, the promotion of environmental or social characteristics, and sustainable investment, by requiring financial market participants and financial advisers to make pre‐contractual and ongoing disclosures to end investors when they act as agents of those end investors (principals)."* (finance.ec.europa.eu, 2019). Giving end investors access to sustainability information is assumed to improve their decision making ability. The sustainability information provided by financial institutions is technocratic as the methodology to validate the information is complicated. A lack of input from non-financial actors onto the information is also indicative of a marketization rationale behind disclosing information. What speaks against the technocratization rationale being the most applicable is that there is no mandated change in the decision making. End investors are still able to choose unsustainable financial products and are not mandated to act on any information that financial institutions provide. Financial institutions' provision of technical information doesn't necessitate

the source of the information to come from sustainability experts. This limits the extent to which the technocratization rationale is applicable.

A further component of the theoretical framework that is reflected in the assumptions about transparency analyzed in the SFDR is the privatization rationale by Gupta and Mason. This rationale suggests that private actors could be motivated to disclose as much information as possible in order to further corporate sustainability goals, improve their public image, and/or avoid more stringent government regulation. Financial actors under the SFDR could be doing the same, disclosing more information than necessary to avoid further government regulations and demonstrate their sustainability commitment to investors. Given that there is some flexibility in what financial market participants want to disclose about their own sustainability practices, the assumptions fit well with the privatization rationale. What limits the validity of this rationale in explaining the motivation for FMPs to disclose information is that the disclosure in and of itself is not voluntary but mandatory. The privatization rationale however presupposes voluntary disclosure. Furthermore, there are some guidelines by which disclosure needs to occur. If FMPs do not follow it they will face regulatory consequences with further scrutiny from end investors. So while they have some flexibility, they do not have full choice over which information to disclose.

Transparency is therefore conceptualized within the SFDR as information disclosure. Through ongoing and standardized disclosure of information transparency's potential is unlocked. This ought to affect the accountability relationship between stakeholders, most notably FMPs and end investors, by reducing information asymmetries. The reduction in information asymmetries is in turn confounded by the complexity of information, suggesting that transparency to end investors might not be the objective of the regulation. Transparency's potential is captured within the SFDR through the information disclosure mechanism, suggesting it can be realized to the extent to which end investors are interested in sustainability information. Since financial institutions are required to disclose sustainability information pre-contractually, there are few barriers to accessing this information, generating transparency's transformative potential.

**Accountability**

Accountability's implicit meaning within the SFDR is the normative consequences that stakeholders can place on financial institutions based on the way in which they have been transparent about sustainability information. The key stakeholder that can enact consequences is identified in the text as end investors. The regulation says the following: "*Disclosures to end investors on the integration of sustainability risks, on the consideration of adverse sustainability impacts, on sustainable investment objectives, or on the promotion of environmental or social characteristics, in investment decision‑making and in advisory processes, are insufficiently developed because such disclosures are not yet subject to harmonized requirements*." Harmonizing disclosure requirements allows for financial products to be more comparable.

Information provided to end investors through the disclosure mechanism allows them to make decisions that compare financial products on “equal” information, which according to the SFDR would allow for more accountability of financial institutions. Since the information is comparable it motivates financial institutions to align with the norm on how to disclose information. Leveraging the disclosure of sustainability information for end investors to make more informed and scrutinizable decisions is the implicit meaning of accountability in the SFDR. The key assumptions that underpin the concept of accountability in the SFDR are that accountability is enhanced by transparency, can improve sustainability practices, is enhanced through periodic disclosure, requires clarity in policies and procedures, and prevents greenwashing.

As mentioned above, the SFDR assumes that making financial market participants disclose their sustainability practices and impacts will hold them accountable for those practices and impacts. Providing information to end investors and regulators provides them with the tools to scrutinize the behavior of financial institutions, incentivizing them to ensure their policies and objectives are aligned. Disinvestment by end investors and reputational damage are the potential consequences that FMPs might face, providing the sustained motivation to divulge their sustainability practices. The alignment between policies and objectives is assumed to hold FMPs on a path of improvement in their sustainability practices and impacts. Since financial institutions will want to avoid negative disclosures and the subsequent divestment or reputational consequences that might arise from them, they are encouraged to improve their sustainability practices in line with the market. Just like the assumptions present for transparency, the regulation assumed that these disclosures are required periodically in order to generate accountability in an effective manner. Financial market participants are required to provide both pre-contractual disclosures and periodic reports, demonstrating that they are continuously considering sustainability factors in their decision-making processes. Additionally, this information demonstrates that they are achieving the sustainability objectives outlined in their financial products. This perception could stem from the continuously changing nature of financial markets and sustainability information.

There is a clear reliance on information as a lever for accountability in the SFDR. Information is meant to reflect the internal practices of financial institutions. The regulation therefore assumes that for financial market participants to be held accountable, they need to have clear policies and procedures in place that reflect their practices. By requiring them to disclose information about their policies related to the integration of sustainability risks the SFDR tries to ensure that these policies and procedures are clearly defined and implemented. Hence clear and detailed information would represent this internal behavior. This mechanism also reflects the assumption that accountability can prevent greenwashing. If companies are required to provide detailed disclosures on their sustainability practices, impacts, and objectives, the regulation leaves little room for FMPs to maneuver. More, and accurate, information provides a baseline for

accountability claims, as financial institutions will be less able to make misleading or unsubstantiated claims. Yet this crucially relies on the regulation covering the instances where misleading and unsubstantiated claims would be possible, whereby the substantive actions of financial institutions would differ from their symbolic ones. The assumptions about accountability that emerge from the analysis of the SFDR, are best reflected by the following components of the theoretical framework, the *four elements* by Bierman and Gupta and the *three stages* by Bovens.

According to Biermann and Gupta, in essence, accountability has four elements: a normative, relational, decision, and behavioral element. These need to all be sufficiently present to consider any accountability relationship as meaningful. Within the context of the SFDR, the normative element is best expressed through the disclosure standards set. For example, the pre-contractual disclosures on the financial institutions' website would be a standard of behavior defined with sufficient precision. The relational element, whereby those who are held accountable to those who have the right to hold to account are linked, is best expressed through the relationship between end investors and financial institutions. Outside of the SFDR these have a clear dynamic, whereby end investors apply consequences of divestment, if the financial institution does not sufficiently perform the behavior expected from end investors. End investors therefore have the right to hold financial institutions to account. This also verifies the decision element, where the judgment of the end investors on if a standard has been met. The judgment takes the form of the evaluation of the sustainability information provided by the financial institution. Consequences of disinvestment are theorized to rely on the information provided. When a financial institution underperforms on their sustainability risk management and discloses negatively, the assumption is that end investors would sanction their behavior with disinvestment. Conclusive evidence to suggest this behavior occurring has however not been demonstrated. There are also assumptions about the efficacy of the decision and behavioral elements that need to be put in question. Principally the following logical conundrum remains unanswered: It is assumed that end investors have a sufficient understanding themselves of what makes an investment sustainable. Yet sustainability information from financial institutions is required in order for end investors to adequately assess the sustainability of their investment. This leads the question as to why end investors did not require this information *a priori* to the investment open.

Bovens (2010) on the other hand outlines the methodology by which these institutional arrangements operate by expressing it through three stages: *the information phase*, *the debating phase* and *the consequences phase*. Within the SFDR the provided text would suggest that accountability occurs through the following process. Sustainability information from financial institutions is presented in the pre-contractual disclosures in stage 1. This is followed by end investors or regulators questioning the adequacy and legitimacy of the information provided in step 2. If the information is insufficient this would lead to judgment and consequences imposed

by the end investor or other stakeholders in step 3. These indicate that the SFDR in its context provides a tool for the information phase that leads to the other stages being possible.

Leveraging disclosure of sustainability information for end investors to make more informed and scrutinizable decisions is the implicit meaning of accountability in the SFDR. Transparency, *i.e. information disclosure,* is leveraged to generate accountability through end investor scrutiny and internal adjustments due to higher awareness of sustainability risks. Accountability mechanisms are therefore provisioned within the SFDR which rely on the sustained maintenance of periodic information by financial institutions and sustained scrutiny by end investors.

**Greenwashing**

Greenwashings implicit meaning within the SFDR is hidden, as the text does not explicitly address greenwashing. While the intention behind the SFDR is to prevent greenwashing, there is no explicit information illustrating what mechanisms are going to be used to achieve this objective (Barbet, 2023). Within the broader European legal framework, greenwashing is represented a few times, whereby the Sustainable Finance Disclosure Regulation is seen as a tool to tackle greenwashing practices (Bodellini, 2023). Actors within the framework, such as the European Insurance and Occupational Pensions Authority (EIOPA), have expressed that greenwashing is a barrier to a green transition. They also view the SFDR as a tool to avoid trust being eroded through greenwashing practices within the sustainable finance industry (Barbet, 2023). They explicitly indicate that due to the constantly evolving nature of the regulatory framework, the sustainability credentials presented by financial institutions could be intentionally misleading. This practice of greenwashing can create reputational and regulatory risks for financial institutions, which might reduce their sustainable products for fear of being accused of greenwashing (Barbet, 2023). Hence while there is no explicit definition of what greenwashing might constitute within the SFDR, reading between the lines of the text allows some inference as to how greenwashing is being tackled. By requiring substantial sustainability disclosure requirements, the SFDR promotes financial market participants to provide reliable information about their sustainability practices and the impacts of their products. This means that information about sustainability claims will be made in a particular manner. Greenwashing relies on the ability to make misleading or unsubstantiated claims. The SFDR limits this practice by requiring information in a standardized manner, reducing the ability for financial institutions to make misleading claims. What exactly constitutes a 'misleading' claim is not specified within the text. There are some key assumptions which underpin the concept of greenwashing in the SFDR. The ones identified by the document analysis is that greenwashing can be curbed with information disclosure, can be mitigated through regular reporting, is prevented through standardization, undermines investor relationships and involves omission and commission. These are discussed in more detail in the paragraphs below.

The regulation assumes that the risk of greenwashing can be reduced if financial market participants are required to provide detailed information disclosures regarding their sustainability practices and impacts. Reducing the risk of greenwashing occurs through the increased information disclosure burden on financial institutions. Comparable information on how they consider sustainability risks and the principal adverse impacts of their investment decisions on sustainability factors reduces their capacity to make misleading or unsubstantiated claims. The SFDR assumes that greenwashing can be mitigated by requiring periodic disclosures from financial market participants. The requirement means that FMPs must consistently validate their sustainability claims over time, which can help reduce their capacity to make short-term, unsubstantiated claims about their sustainability practices and impacts.

The SFDR requires FMPs to classify their financial products based on three articles, those which do not promote environmental or social characteristics, those who do, and those who have an explicit sustainability objective. If financial products promote environmental or social characteristics, or have a sustainability objective, then the SFDR requires FMPs to disclose whether and how a designated index is aligned with sustainability characteristics or objectives. This requirement reflects the assumption that using standards can help prevent greenwashing through providing a measurable reference against which claims can be validated. Through standardization, it is assumed that greenwashing can be prevented. What is further not explicitly stated is that greenwashing can harm investor trust. By aiming the outcomes of the regulation at protecting end investors, the implicit question "protect investors from what?" is answered with greenwashing practices. Since information is meant to improve investors ability to discern what investments are sustainable and why this is the case, a misrepresentation of said information would require some protection mechanism. Furthermore the SFDR assumes that greenwashing involves both the misrepresentation of sustainability practices (commission) and the failure to disclose adverse sustainability impacts (omission). This is expressed through the requirement for disclosures of sustainability practices and principal adverse impacts. Greenwashing can involve either mechanism according to the SFDR, which sets disclosure requirements in place to prevent greenwashing from occurring. The assumptions about greenwashing that emerge from the analysis of the SFDR, are best reflected by the following components of the theoretical framework, *decoupling* and *selective disclosure* by Lyon and Montgomery and *companies affecting regulations* by De Silva Lokuwaduge and De Silva.

Firstly, there is the mechanism of decoupling, which is the disconnect between the activities and the structures of an organization. Under SFDR, financial institutions are required to disclose how they integrate sustainability factors into their risk processes. While this regulation makes it more challenging for financial institutions to engage in decoupling, it doesn't make it impossible. Financial institutions could still reduce their efforts and simply adhere to the minimum requirements of the regulation. For example, they may disclose some sustainability risks but understate their impact, or they may provide information that is technically enough yet vaguely

formulated, making it difficult for investors to understand their true impact. Furthermore, financial institutions could engage in selective disclosure as a greenwashing mechanism. Selective disclosure is where actors disclose positive information while withholding negative information. Actors hereby engage in greenwashing by purposefully disclosing information they believe will be beneficial to their image. By disclosing very accurately the sustainability impacts which financial products have, but by vaguely explaining the risks of unsustainable products, this mechanism could still occur under the SFDR. Financial institutions are obliged to disclose their principal adverse impacts. However, there might not be adequate data to answer the question, which ‘excuses’ them from providing a concrete answer. They are not obliged to disclose how they searched for this data and can thereby greenwash through not following their commitments with actions. Finally, companies affecting regulations involve the use of lobbying or power to change the nature of a regulation. Financial institutions are invited for consultations on the draft text and take part in discussions, explaining the extent to which they are able to disclose certain information. It is unclear to what extent this occurs in the SFDR from the document analysis, yet an absence of explicit requirements is indicative of some influence by companies on the text itself.

Greenwashing within the document analysis of the SFDR does not provide a clear indication as to what extent it is prevented through the regulation. While the intention behind the SFDR is to prevent greenwashing, there is no explicit information illustrating what mechanisms are going to be used to achieve this objective. By requiring standardized information, the SFDR has the potential to reduce the vagueness of sustainability claims by institutions and also makes the disclosed information comparable for end investors. Through these mechanisms, greenwashing can be reduced, as end investors would have a clearer and more comparable picture of sustainability practices. Nevertheless, the extent to which financial institutions could engage in greenwashing practices through selective disclosure is not clear. As the SFDR does not convincingly address greenwashing, it remains a risk to the relationship between transparency and accountability.

## Interview analysis

**Introduction**
While the document analysis has looked at the underlying themes and assumptions that frame the intentions of the SFDR, the interview analysis looks at the underlying themes and assumptions that are present in the implementation of the SFDR. Within the interview analysis, each of the three concepts, transparency, accountability, and greenwashing, is shaped by key normative and relational components. These are the *who, to whom, about what* and *to what ends/in what manner*, which differ slightly in how they emerge, as specified in the theoretical framework. During the interview analysis, these key components were identified and have been summarized in *Table 3*. Each concept is shaped by key normative and relational components, the *who, to whom, about what* and *to what ends/in what manner*, which differ slightly in how they emerge, as specified in the theoretical framework. The key components are identified and have been summarized in *Table 3*. The interviewees have identified financial market participants (FMPs) and financial advisers (FAs) as those who need to disclose information. As such FMPs and FAs can be identified as the *who* component, since they are the actors who are meant to be transparent and accountable towards others, and are also the actors capable of engaging in greenwashing. These results are similar to those of the document analysis. A difference is that the interview analysis also suggests that regulators are the *who* for accountability, as regulators can be accountable for ensuring enforcement of SFDR requirements. Yet the main relationship identified also by the interviewees is between the financial institutions and their end investors. Two quotes: "*Companies can be more precise in what they offer*" (Interviewee 1) and "*Investors can express sustainability preferences*" (Interviewee 1) illustrate the relationship quite clearly. Interviewees did also point to other stakeholders such as regulators or activists, who can make use of the information for alternative purposes than investment decisions. These were also particularly important in the question of greenwashing.

Similar to the document analysis, the normative dynamics which emerged from the document analysis varied across the three concepts. Identifying *about what* financial institutions should be transparent was indicated by the interviewees as the disclosure of sustainability information, PAIs (Principle Adverse Impact Indicators) and product classifications (Article 6, 8, 9) under the SFDR. Interviewees seemed particularly focused on the latter two, as these are the most salient disclosure aspects. *About what* financial institutions can be held to account by investors seemed less about metrics and more about aligning sustainable investment claims and actual practices according to the SFDR framework. Interpreting “correctly” what the SFDR intends and matching the investment practice accordingly seemed most important. *About what* financial institutions could greenwash leads somewhat directly from the accountability concepts. By misrepresenting or overstating their sustainability credentials of an investment product they are misaligned in their claim and practice, reflecting the most basic definition of greenwashing. Misclassifying and “labeling” their products as sustainable through an article 9 classification, *“aggressively”*

(Interviewee 2) including companies into article 9 funds directly undermines the intention of the transparency mechanism. Finally, lacking complete disclosure by only partially disclosing information seems indicative of a strategy which goes against the intentions of the SFDR.

The final normative dynamic is the *in what manner* component, which reflects how the actors identified as *who* and *to whom* interact on the content of *about what*. Transparency is demonstrated through complex documents like EETs with many data points and by product classifications (Article 6, 8, 9). This indicates that more and complicated data demonstrates some commitment to providing complete information. Accountability is demonstrated through regular auditing of disclosure reports, and through scrutiny from end investors, regulators and activists. This indicates that for this normative dynamic there exists some level of periodic interaction between FMPs/FAs and other stakeholders, based on the accessible disclosure documents and periodically updated information. Greenwashing is demonstrated through a variety of potential practices in which stakeholders would engage. Principally, the interviewees identified vague or misleading language, lack of standardization in sustainability definitions, the use of labeling schemes, and non-disclosure or selective disclosure of certain information. These all relate directly to the *about what* component for greenwashing, as they are the *manipulation of information* in both its *nature* and its *presentation.*

| | **Transparency** | **Accountability** | **Greenwashing** |
|---|---|---|---|
| **Who** | Financial market participants and financial advisers | Financial market participants, financial advisers and regulators | Financial market participants and financial advisers |
| **To Whom** | End investors and potentially regulators or activists | End investors and potentially regulators or activists | End investors and potentially regulators or activists |
| **About What** | Disclosure of sustainability information, PAIs (Principle Adverse Impact Indicators) and product classifications (Article 6, 8, 9) under the SFDR | Sustainable investment claims and actual practices match to correctly apply SFDR standards | Misrepresentation or overstatement of the sustainability credentials of an investment product, including misleading labeling or a lack of complete disclosure |

| **In What Manner** | Through complex documents like EETs with many data points and by product classifications (Article 6, 8, 9) under the SFDR | Regular auditing of disclosure reports, and through scrutiny from end investors, regulators and activists | Vague or misleading language, lack of standardization in sustainability definitions, the use of labeling schemes, and non-disclosure or selective disclosure of certain information |
|---|---|---|---|

*Table 3. Normative and relational components identified in the interview analysis.*

The next three sections are the thematic content analysis which illustrate the key themes of the interviews. They have been subdivided into themes which separately most relate to transparency, accountability and greenwashing.

**Transparency**

Transparency related themes identified in the interview analysis were the following five; complexity of information, inadequate simplification, misinterpretation of labels, lack of standardization and data gaps.

According to the interviews, a common theme was the complexity of information provided under the SFDR. Interviewees identified this as a significant barrier to transparency. Since the amount of information available to investors has drastically increased, it is assumed that this availability allows investors to better identify the sustainability risks of investments and express their sustainability preferences in investments. In practice the increased complexity of the amount of information available to investors has proved to be a barrier to understanding. The complexity of the information could therefore hinder the aims of the SFDR by assuming that more information disclosure is equal to more transparency. If however, the information is not understood, then it would unlikely lead to transparency as intended, but rather to information overload for investors. For example, the European ESG Template (EET) provides investors with a wealth of information. This standard template for information disclosure has been highlighted in an interview as a barrier to investor engagement. According to an interviewee, the "*EET (standard European template) so complex that the end investors can't interact with them*" (Interviewee 1). If investors can't properly interact with information, then it is unlikely that transparent information disclosure is occuring. Therefore the *complexity of information*, while intended to increase transparency, may actually be hindering it by making the information less accessible and understandable to investors.

A similar theme identified from the interview is the need for simplicity. As mentioned above, the intention of SFDR was to simplify information for investors, yet the complexity of information renders subsequent end investor engagement more difficult. Hence, the complexity of

information required from documents such as the EET can make it difficult for investors to understand. By consequence, this suggests that further simplification and accessible formats of information disclosure would render the SFDR more transparent. This was suggested by the interviewees, and is exemplified with the following quotes: "*Investors don't have the time to study a complex EET*" (Interviewee 1), "*Giving more simplistic clarity*" (Interviewee 1). Just like the complexity of information, the lack of adequate simplification of information can hinder transparency, rendering it more difficult for investors to understand the information provided.

The SFDR sets forth classifications which are incorrectly be viewed as labels, leading to frequent misinterpretation and oversimplification. In order to provide clear and standardized information about the sustainability of different investments the SFDR classifications of products into Article 6, 8, 9. FMPs are expected to self-categorize their investments according to their own definitions and provide methodologies for arriving at these conclusions. However, these classifications are often viewed as labels, which can lead to misinterpretation and oversimplification, as end investors believe that the classification arrived due to some standards being achieved from the EU. End investors can thereby be motivated to purchase a fund classified as Article 9, falsely believing there to be some legitimation from the EU. Consequently, classification being misunderstood as labeling can undermine the transparency and subsequent accountability that the SFDR aims to promote. This was suggested by the interviewees, and is exemplified with the following quotes: "*It is viewed as a label even though its not that way*" (Interviewee 1), "*The market has taken this as a 8 is green and 9 is greener*" (Interviewee 1). This misinterpretation of a classification as a label can undermine transparency by influencing the perception of information by end investors, leading to a misunderstanding of the sustainability of different investments.

Transparency is further hindered by the lack of standardized definitions of sustainability under the SFDR. Funds are difficult to compare, if the underlying definitions of what constitutes a sustainable investment differ. While the SFDR puts forward a definition, according to the interviewees, there is a lack of standardization to the extent that interpretations differ drastically. Hence, the lack of standardization could undermine transparency, as the information presented is not equal. Investors would consequently be unable to make informed decisions and compare adequately between different investments. Interviewees illustrated this with the following quotes: "*Lack of definition means every manager comes up with own definition of sustainable*" (Interviewee 4), "*Several points unclear*" (Interviewee 2). Definitional differences make it difficult for transparency to occur, if the information itself is not presented in a similar way. So hypothetically, two funds could classify the same product under different articles yet contain the same underlying asset. Hence, the information presented to end investors differs based on the classification of the products. This lack of standardization of classifications and information can undermine transparency by the comparability of the sustainability of different investments.

Finally, there are some limitations to the *nature of information* available for FMPs and FAs to fulfill the disclosure requirements of the SFDR, most notably the lack of robust data for reporting. The SFDR requires financial institutions to disclose a significant amount of sustainability related information. Various interviewees have noted that significant data gaps exist in sustainability information, which makes it challenging for institutions to comply with the SFDR requirements. This has also been noted within wider academic research, where a lack of general and quantifiable sustainability data is often cited as a limitation (Och, 2020). Since the SFDR requires that principal adverse impacts (PAI) are adequately considered, facing the multifaceted potential impacts with inadequate data sources renders the information disclosed considerably limited. Challenges in data would thereby hinder transparency and make it difficult for end investors to make informed decisions. According to the interviewees this topic is fairly prevalent: "*The data is not yet very developed - Not a lot of coverage*" (Interviewee 2), "*Lack of data around EU taxonomy*" (Interviewee 3). Therefore a lack of sustainability information can hinder transparency by making it difficult for institutions to fully comply with the SFDR requirements and consequently make end investors informed decisions more challenging.

The interview analysis suggests that transparency's transformative potential is limited through the nature in which information is presented to stakeholders. Through a lack of clear definitions and a high level of complexity in how the information is presented, stakeholders are less able to access the information. By incorrectly perceiving the classification system of the SFDR as labels, end investors are misusing the simplified information to inform their sustainability perspective. This systematic misunderstanding of information undermines transparency's potential as the information disclosed is less capable of fulfilling its intended purposes.

**Accountability**

Accountability related themes identified in the interview analysis were the following; regulatory compliance, end investor scrutiny, standardized data, and information overload.

Complying to the regulatory standards and these being enforced by the supervisory authority which regulates the financial institutions was a common theme identified by the interviewees that would lead to enhanced accountability. By requiring FMPs to provide pre-contractual information, the regulatory authorities have the capacity to check whether or not the methodologies provided by the FMP match the definitions within the SFDR. Furthermore, being able to require the information in a specific format enhances the ability of regulators to understand what information is missing and how it can be enhanced, leading to better accountability mechanisms in the future. According to one of the interviewees, *"Strictness makes it consistent"*, which can be interpreted that requiring specific formats for the information to be disclosed makes the disclosure process consistent and allow the accountability mechanism to function better. Regulatory compliance is critical for accountability, as the enforcement mechanism provides financial institutions with the incentive to abide by the regulation.

End investor scrutiny is a further accountability mechanism that incentivizes financial market participants to disclose information and provides a basis for their behavior to be evaluated. End investors are able to change their investment from FMPs by divesting and moving their money elsewhere. FMPs do not want this to occur and therefore would be incentivized to provide end investors with the information they require. Being seen as 'unsustainable' or unable to manage sustainability risk is likely to demotivate end investors to keep their money at the FMP. Hence the main accountability mechanism occurs through the relational leverage that end investors have over FMPs. This accountability mechanism assumes that end investors are motivated to divest in the case that the information disclosure is inadequate. Examining this claim on the basis of the interview data renders mixed results. There is a split between customers who are interested and motivated to include their sustainability preferences in their investment decision-making and those who are not. Multiple interviewees mentioned that customers are overwhelmed with the information presented, which is illustrated for example in this quote; "*mostly overwhelmed clients*" (Interviewee 2). Yet this depends on the exact type of customer. *Retail investors*, who are tendentially smaller and private clients are typically those who are less capable of leveraging the SFDR for their interests. According to the interviews, these customers are not interested in expressing sustainability preferences, since they do not know what they want. When the question arises, if sustainability preferences should be included in the investment strategy, these customers refer the question back to the financial advisor. This is well represented by the following quote: "*Customers expect no harm and dont want to read anything*", which leads to a "*Big mismatch what customers think is sustainable and what the industry thinks*" (Interviewee 3). Viewing end investor scrutiny as an accountability mechanism would therefore be unlikely for these investors. This quote about customer preferences is indicative of the level of scrutiny; *"99% cases customer says whatever you do is fine*" (Interviewee 3). Without end investor scrutiny, the accountability mechanism of the SFDR becomes limited. On the other hand, larger *institutional investors*, who professionally invest are more focused on the sustainability impact of their investments. These have explicit sustainability goals and can leverage the information in the SFDR to purchase funds that adequately allow the institutional investor to reach their goal. According to the interviews "*Institutional investors have a different approach*", "*With them the goal is to grow the aritcle 9 share of portfolio"* (Interviewee 4). Given their explicit interest in growing their portfolios with companies that the FMPs have classified as article 9, the institutional investors seem willing to include sustainability criteria in their investment decisions. The scenario described by the interviewee however explicitly refers to the onboarding or initial purchasing process. As an accountability mechanism, the lack of clarity on post purchase decision making by institutional investors provides a caveat. Since There is an ongoing disclosure process, institutional investors might hesitate from directly divesting when there are unexpectedly negative disclosures by funds. Given the lack of information provided by interviewees, this presents a gap in the research. As an accountability mechanism, end investor scrutiny presents a mixed picture, as on the one hand some investors do not express a

sustainability preference, making the mechanism redundant. On the other hand, others are explicitly interested in including sustainability preferences, which can act as an accountability mechanism.

A further theme regarding accountability mechanisms identified in the interviews was that of standardized data. According to the interviewees, standardized data can be a valuable mechanism for accountability, but its current complexity, coverage issues, and diverse interpretation reduce its effectiveness. Just as the SFDR intends, interviewees mentioned that standardizing data can help to make clear comparisons and evaluations. By providing more complete data, this enhances accountability as every FMP is required to disclose similar information. However, interviewees identified that the evolving nature of data and particularly the lack of coverage for sustainability issues rendered the current data unworkable as an accountability mechanism. The efficacy of the accountability mechanism is further reduced by financial institutions varying in their interpretations of which data and methods are valid, complicating the capacity for comparability and standardization. Without consistent data being used, comparisons of products in funds become less directly comparable in terms of their sustainability performance. Direct quotes from the interviewees indicate these complexities: *"Data still evolving, lacks coverage, different interpretations", "Lack of standardized data, hinders comparison of products and funds"* (Interviewee 5). The challenges associated with the current level of standardization within the data limit the effectiveness of standardized data as an accountability mechanism, despite its potential.

A key challenge for the efficacy of accountability mechanisms is the overload of information presented to end investors in the SFDR. Interviewees identified that information overload could challenge and overwhelm investors which in practice results in a decreased understanding of the sustainability preferences they are able to express. Hence, a decrease in accountability would be likely, as fewer preferences would be expressed in practice. Simplifying information however, also provides a trade-off with the effectiveness of sustainability preferences. If end investors are unable to express their preferences in detail, then the objectives of the SFDR could also be undermined. This challenge is expressed by interviewees with this quote: "*Information overload, clients often ask for simplification*" (Interviewee 5). Information overload could represent a significant challenge to the accountability mechanisms, as end investors' comprehension could be undermined.

The interview analysis suggests that the underlying accountability mechanisms are inadequate at leveraging transparency’s transformative potential. The SFDR proposes that accountability mechanisms such as end investor scrutiny on the basis of comparative information would work through information disclosure. Interview data suggests that these accountability mechanisms are unable to provide meaningful accountability as end investors are not consistently motivated to engage in sustainability discourse and therefore unable to scrutinize financial institutions.

Furthermore, the inadequate comparability of information disclosed under the SFDR poses a significant challenge to the remaining investors that do scrutinize financial institutions. The link between transparency and accountability in the SFDR would therefore fall short of its assumed strength.

**Greenwashing**

Greenwashing related themes identified in the interview analysis were the following; vague definitions, misclassification of products, and reputational risk.

Vague definitions of terms within the SFDR relating to sustainability can enable greenwashing practices by FMPs and FAs. Individual managers are able to come up with their own definition of which investment practices fall under sustainable, rendering a more fragmented landscape of investment products. By defining sustainability according to what the financial institutions believe is sustainable, 'sustainably' labeled funds are difficult to compare. A lack of standardization in the definition allows financial institutions to present themselves as more sustainable than they actually are since they might choose a definition that is favorable to their existing products and institutional structures. A pragmatic example could be the inclusion of companies into investment products, where the company has a net-zero pledge, yet has not made any concrete plans to decarbonize their production. While some FMPs might not consider this sufficient to be labeled sustainable, others could include it, if their definition of sustainability is broader. Hence, end investors would struggle to compare the performance of these two products, if the definitions and their implications are not clarified priorly. This concept is illustrated through the following quotes by the interviewees; "*Lack of definition means every manager comes up with own definition of sustainable*" (Interviewee 4), "*Have seen very broad definitions*"(Interviewee 2). Vague definitions of sustainability can enable greenwashing, as financial institutions are able to appear more sustainable than their counterparts, despite their definitions of sustainability not being comparable. This in turn undermines the fundamental aim of the SFDR to provide comparability for products.

The misclassification of products under the SFDR can enable greenwashing, by signaling a deeper contribution to sustainability than the products would otherwise contain. The SFDR provides classification options for institutions to self-select the level of disclosures of sustainability information, whereby products can be either classified under Articles 6, 8, or 9. As the definitions of sustainability in products are not standardized, products can be misclassified. Hence what one financial institution might consider a product that could only be classified under article 6, another might ascribe to article 8. Through the complexity of the regulations and the lack of clarity on the implications of financial institutions' definitions, this process potentially enables greenwashing. Product classification therefore becomes about providing sufficient justification for why a product fits the definition of sustainability that financial institutions have

developed. Taking article 8 as an example, it is clear that FMPs have some space in how they interpret the "environmental or social characteristics" that are required for the fund (finance.ec.europa.eu, 2019). Since FMPs decide themselves what belongs to an "environmental or social characteristic" they are able to include unverified technology and business models into the fund, while promoting its "green" credentials. According to the interviewee's this practice is fairly obviously indicative of greenwashing; "*The market has taken this as a 8 is green and 9 is greener*" (Interviewee 1) "*Different standards on article 9 - Was way quicker an article 9 then what they would say*" (Interviewee 2). Misclassification of products under the SFDR can enable the greenwashing practice of financial institutions by allowing them to self-select their definition of sustainability to appear more sustainable than they actually are. This practice can only be undermined with a clearer definition of what sustainability means across institutions, whereby standardized definitions can be leveraged to achieve the goals of the SFDR.

One of the most central topics that were addressed within the interviews was the risk of reputational damage through being perceived as greenwashers. Financial institutions have a significant concern for reputational damage, as this might compromise their ability to attract investment from larger end investors. The networked consequences that can arise from reputation damage could be customer withdrawals, increased amounts of lawsuits, and employee pushback against plans. Reduced trust and increased costs to fight off legal claims and reinstate their reputation are undesirable results for financial institutions, who are therefore motivated to engage in actions to reduce the risk of greenwashing. According to the interviewees, financial institutions are taking concrete action to avoid the perception of greenwashing, such as renaming funds, to maintain their reputation. The interviewees illustrated this through the following quotes: "*Main risk is reputational risk*" (Interviewee 3) "*Renamed a lot of funds so that there is no perception of greenwashing*" (Interviewee 4). Reputational damage acts not only as a topic related to greenwashing but is also tied in with accountability mechanisms. By providing a deterrent for certain actions, stakeholders who accuse financial institutions of greenwashing have a limited capacity to hold them to account. The precautionary steps taken by financial institutions reflect the capacity for accountability present in the stakeholders that can accuse them of greenwashing. A key challenge for how greenwashing is understood in the SFDR, is the lack of explicit consequences introduced into the regulation, which limits its capacity to enact direct change. Hence, these informal behavioral changes by financial institutions provide an indication of the nature of the accountability mechanisms that reputational risk provides. The risk of reputation damage through the accusation of greenwashing is therefore a central topic for financial institutions, who are including this consideration in their classification process for their financial products.

The interview analysis suggests that transparency's relationship with accountability is impacted through the presence of greenwashing within the practice of the SFDR. While the intention from the EU will have been to reduce the occurrence of greenwashing, the themes identified in the

interview analysis suggest that through mechanisms such as vague definitions, misclassification of products, and reputational risk, greenwashing remains possible. Transparency's potential to generate accountability is reduced through greenwashing, as the greenwashed information disclosed leads to a 'false' sense of transparency occurring. This 'false' information is not corrected through the accountability mechanism, suggesting that greenwashing impedes the effectiveness of accountability mechanisms in the context of the SFDR.

**Theoretical Framework**

The themes above have emerged from the interview analysis, yet have not been placed into the context of the theoretical framework. The following paragraphs illustrate the overlap between the conceptualizations of transparency, accountability and greenwashing from the interviews with the theories presented in the framework.

According to how the interviewees conceptualized transparency it overlaps most with the *technocratic transparency* from Tienhaara and the *privatization rationale* from Gupta and Mason. Tienhaara describes technocratic transparency as emerging from scientific rationalism and premised on the notion that experts and policymakers need disclosed information to feed into policy processes, thereby ensuring efficient and effective governance outcomes. The intention for information disclosure is not to provide accountability, but to improve governance through expert advice, increasing the efficiency and effectiveness of a specific policy program. Interviewees highlighted the difficulty for end investors to use the complex information that is presented in the EET. If the explicit aim of the SFDR is to enhance accountability through the mechanism of end investor scrutiny, it seems unlikely that complex information would facilitate those efforts, if end investors are unable to interact with the information effectively. Furthermore, interviewees illustrated the technical nature of the information provided. The following quotes show this; *"Hard to translate the information - Very detailed and technical.", "More difficult to implement the information within the calls."* (Interviewee 2). These quotes illustrate the complexity and technical nature of the information being disclosed, indicating that transparency in this context is tailored more toward experts and policymakers rather than the end investors. Hence this would conceptually align most with the technocratic transparency concept.

Furthermore, the privatization rationale by Gupta and Mason aligns well with the conceptualisation of transparency presented by the interviewees. Interviewees mentioned the flexibility that FMPs and FAs have in their application of the SFDR rules through self-selecting the classification of products and defining sustainability according to their own conceptualisations. These indicate that financial institutions might voluntarily embrace transparency to further their own sustainability aims while reducing scrutiny on their public image. Through their influence on the disclosure process, financial institutions may also be able to reduce the pressure from governments to provide detailed sustainability information. One of

the interviewees best summarized it in the following quote: "*This is the issue with the regulation : Lack of definition means every manager comes up with own definition of sustainable - Level of sustainable is not something you can use to compare between funds.*" (Interviewee 4). By being able to define sustainability themselves, financial institutions are able to further their own sustainability aims while reducing scrutiny of their public image. Since they are able to position products as sustainable, they are incentivized to disclose information that aligns with their own definition. Therefore the privatization rationale seems the most adequate.

Accountability within the theoretical framework is conceptualized through the work of Biermann and Gupta, that the interview analysis indicates is insufficiently present within the context of the SFDR. According to Biermann and Gupta, accountability has four elements: a normative, relational, decision, and behavioral element. These need to all be sufficiently present to consider any accountability relationship as meaningful. Within the context of the SFDR, the normative element is best expressed through the disclosure standards set. For example the pre-contractual disclosures on the financial institutions' website would be a standard of behavior defined with sufficient precision. The normative element is defined within the disclosure standard of the SFDR. While there is a sufficient standard present on a theoretical level, in practice the disclosure can vary widely. Hence, when individual managers are able to define sustainability themselves, the standards are not defined with sufficient precision. The following quote illustrates this; *"Reporting requirements [...] - Depends on fund manager."* (Interviewee 4). However the relational element, where those who are held accountable to those who have the right to hold to account is sufficiently present according to the interview data. It was never questioned that end investors are not able to divest from financial institutions on the basis that they were unable to provide sufficient sustainability in their products. Interviewees had only questioned the capacity for end investors to make these choices due to their own insufficient understanding. The same goes for the decision element, where end investors are able to make a judgment of those financial institutions about whether the expected standard of behavior has been met. Interviewees were skeptical of the capacity of end investors to comprehend the complex information present, yet there are no barriers to end investors enacting an accountability mechanism. Similarly, the behavioral element is also present, as end investors are not limited in their enactment of consequences. The interview analysis does however indicate that not all four elements are sufficiently present within the context of the SFDR. From the perspective of the theoretical framework, the SFDR does not provide accountability, as the flexibility in providing their own definition for sustainability inadequately holds financial institutions to account.

Greenwashing is represented through a variety of mechanisms within the theoretical framework. The interview analysis indicates that greenwashing does occur within the SFDR, mostly through the mechanisms identified by Lyon & Montgomery of decoupling, selective disclosure; and the absence of clarity on what is considered an inherently unsustainable business by De Silva Lokuwaduge and De Silva. Interviewees expressed concern about decoupling occurring within

the SFDR, whereby financial institutions classify their products differently from one another. Here, financial institutions are able to present a product as more sustainable than it actually is, since end investors interpret classifications as labels. Hence, the regulations of the SFDR are insufficient to prevent this mechanism of greenwashing from occurring. Furthermore, firms are able to engage in selective disclosure. Since they are able to reclassify their products according to their own definitions, they are able to "downgrade" their own disclosure requirements. There are more requirements for Article 9 products that can be avoided through the selective reclassification of products to Article 8. This avoids the necessity to disclose information while still being considered sustainable as these products contain an environmental or social characteristic. The following quote illustrates this; *"You can call anything a sustainable investment. Biggest flaw. Most discussion is about article 9 - how much should it be. The market has products with less. Repetitional risk make changes as article 8."* (Interviewee 3). Finally, there is a notable absence of definitions on what is considered an inherently unsustainable business. While FMPs and FAs need to justify their classification choices, there are no consequences to misclassification. Through an absence of clear definitions on what is considered unsustainable, the interview data suggests that the SFDR insufficiently prevents the inclusion of what sustainability experts might consider unsustainable businesses. Just as illustrated in the quote above, the problem of undefined and unenforced standards in the SFDR allows for potential greenwashing by allowing financial institutions to self-define what they consider part of their sustainable investments.

## Cross-analysis

There are similarities and differences in the results from both the interview analysis and the document analysis. The following paragraph will cross-analyze the results to identify these and illustrate a more holistic picture. Similarities and differences between these two analyses shed light on the expectations and possibilities of the SFDR to achieve its aims and the current interpretations by professionals who are currently engaged with its implementation.

### Transparency

Transparency is conceptualized similarly in both the interview analysis and the document analysis, by illustrating the technocratization and privatization rationales by Gupta and Mason, as well as Tienhaara. Both analyses align transparency with the technocratization rationale by Gupta and Mason and *technocratic transparency* from Tienhaara, suggesting that disclosed information feeds into decision-making processes by experts and policymakers. Information disclosed is not necessarily disclosed to enhance accountability, but rather for improving governance effectiveness and efficiency. The document analysis and interview analysis both highlight the complexity and technical nature of the sustainability information disclosed, suggesting the information is more accessible to experts rather than end investors. Both analyses also suggest that, for the concept of transparency, the privatization rationale from Gupta and

Mason would hold explanatory power. Financial institutions could be motivated to voluntarily embrace transparency to further their own sustainability goals while reducing scrutiny on their public image. Both analyses identified that financial institutions have significant flexibility in self-defining sustainability and classifying their financial products, indicating that the degree to which they disclose could be motivated by their desire to further their own sustainability goals. Transparency is however also conceptualized differently in both the interview analysis and the document analysis. The interview analysis illustrated the complexity of the information being disclosed and the inability of end investors to effectively deal with the complex information.One of the interviewees mentioned the difficulty for end investors to use complex information presented in the EET for holding financial institutions accountable. How the disclosed information is used, i.e. what transparency is for, is not discussed in the SFDR.

### Accountability

Accountability in both the document analysis and the interview analysis is conceptualized through the four elements identified by Biermann and Gupta: normative, relational, decision, and behavioral. According to the interview analysis these elements are not sufficiently present within the context of the SFDR. Critically, the flexibility given to financial institutions in defining sustainability undermines the normative element. This insufficiency results in a lack of *meaningful* accountability since not all elements are present. Within the document analysis, these elements are seen through the relationship between financial institutions and end investors. It focuses primarily on this relationship and the norms set through disclosure standards. Whether accountability can be effectively enforced is questioned, as there are inconsistencies in the conceptualization. While end investors are assumed to be knowledgeable about sustainability, they still require extensive information from financial institutions to assess the sustainability of their investments. Within the interview analysis, there is a similar skepticism. End investors are considered capable of enforcing consequences, but there's skepticism about their ability to understand the complex information presented. Both interview and document analysis, therefore, question the link between transparency and accountability, given the lack of conclusive evidence that accountability relations are sufficiently present. The results from both analyses indicate that the SFDR is ineffective at ensuring meaningful accountability, mostly due to the flexibility given to financial institutions in defining sustainability.

### Greenwashing

Greenwashing is conceptualized similarly in both the interview analysis and the document analysis, identified as occurring through greenwashing mechanisms such as decoupling and selective disclosure and aided by a lack of clear definition of what constitutes an inherently unsustainable business. There are concerns in both analyses that financial institutions are able to

classify their products according to their own definitions of sustainability, which allows for the potential for greenwashing. Given this flexibility, they are able to generate a favorable definition of sustainability to match the products that already exist in their financial portfolio. Both analyses further identify greenwashing mechanisms such as decoupling or selective discourse. Financial institutions are therefore able to present their products as more sustainable than they actually are through changing their definitions (decoupling), or selectively reclassifying their products to lesser articles in order to avoid stricter disclosure requirements (selective disclosure). Finally, both analyses indicate an absence of clear definitions, especially on what constitutes an inherently unsustainable business. Financial institutions are therefore not faced with direct consequences for including unsustainable business models in their products if they can find adequate methodologies for considering them sustainable. There are differences in what the interview analysis highlighted compared to the document analysis. The interview analysis suggests more clearly that greenwashing occurs in practice within the SFDR. Multiple interviewees indicate the various methods through which financial products are potentially greenwashed. The document analysis suggests methods, yet does not conclusively prove the occurrence of greenwashing within the context of the SFDR. According to the document analysis, financial institutions could still engage in selective disclosure or decoupling, yet the SFDR does pose a significant challenge for them to do so. Finally, the document analysis suggests the possibility of financial institutions influencing the regulations to their advantage, which is only mentioned through the capacity to influence definitions in the interview analysis.

## Theoretical reflection

That transparency's transformative potential is supposedly meant to lead to accountability is put into question through the results of the analyses above, as the technocratization and privatization rationales more closely explain the motivations for financial institutions to disclose information.

According to the results of the analysis financial institutions are most likely motivated to disclose information primarily to further their own sustainability aims while reducing scrutiny on their public image. Rather than providing end investors with information in a manner that is simple to understand, the information disclosure process under the SFDR is complex and technocratic. Accountability is therefore difficult to achieve through the scrutiny by end investors, which suggests that financial institutions might voluntarily embrace transparency not because they wish to be held to account, but because disclosing is convenient for their reputation. By additionally being able to self-defining sustainability and classifying their financial products, accountability mechanisms are insufficiently effective. Accountability is not facilitated through the structures of the SFDR, since contextual factors such as a varying level of desire by end investors to leverage sustainability information and an absence of direct consequences for poor disclosure practices are not conducive to meaningful accountability. The consequential prevalence of selective disclosure and decoupling practiced by financial institutions indicates the extent to which the link between transparency and accountability remains *assumed* rather than *existent*.

There are conceptual implications on the relationship between transparency and accountability when viewing greenwashing through the case of the SFDR. On a conceptual level, greenwashing can be defined as the selective disclosure of less harmful environmental impacts to create an impression of transparency while withholding information that is more environmentally damaging (Grewal, Richardson and Wang, 2022). Accountability mechanisms in the SFDR are shaped by the effective application of transparency through information disclosure. Greenwashing mechanisms undermine this process through financial institutions selectively disclosing information and classifying products strategically according to their own definition of sustainability. Financial institutions are therefore more capable of generating an impression through transparency, generating the risk of greenwashing. This process reveals some conceptual limitations of the concept of greenwashing, through introducing the normative effects into its definition. Greenwashing is possible through the nature of accountability relations. Effective accountability mechanisms should make greenwashing implausible and are achieved through the sustained motivation of those holding others to account (Gatti, Seele and Rademacher, 2019; Nemes et al., 2022). Furthermore, greenwashing is conceptually extended by suggesting that not only external verification processes generate accountability, but also the internal verification processes. Research has previously identified that a lack of an external verification process by third parties increases the possibility for actors to greenwash (Perego and Kolk, 2012). In the case of the SFDR, the accountability relationship lies primarily between financial institutions and end investors, without a third party that externally verifies the credibility of sustainability claims by financial institutions. End investors are therefore the primary actor able to pass judgment, limiting the effectiveness of the SFDR as a tool to end investors' capacities to comprehend sustainability claims. Bovens (2007) indicates that the third phase of accountability involves the adequate application of consequences on the actor being held to account. In the case of the SFDR these consequences are only as strong as the scrutiny of end investors. This indicates that greenwashing fundamentally involves a normative element and is limited to the capabilities of those trying to undermine its existence.

## Conceptual limitations

One of the key limitations of this research is the lack of available data on what financial institutions themselves have disclosed. Both the regulation and the interviews provided perspective on what was meant to be disclosed in pre-contractual information by FMPs and FAs. They however do not provide insight into the quality of this information. How information is disclosed in practice could provide deeper insight into how transparency and accountability can be undermined by greenwashing within the context of the SFDR. This would be the case, since the information disclosed in pre-contractual information could reveal further greenwashing mechanisms that are not accounted for in the perspectives shared by the regulation and interview analysis.

A similar limitation is the lack of direct evaluation of the standards and principal adverse impact indicators themselves to identify possible methods for greenwashing to undermine the potential for transparency to lead to accountability. While the document of the SFDR was analyzed, the methodologies undertaken by FMPs and FAs to disclose their principal adverse indicators were not looked at. Neither were the auxiliary guidelines of the EU reviewed to identify potential methodological limitations and the subsequent possibilities for these to be exploited for greenwashing. Similar as above, a richer understanding of how information is disclosed in practice could provide deeper insight into how transparency and accountability can be undermined by greenwashing within the context of the SFDR. Without directly evaluating the standards and principal adverse indicators for their methodological rigidity the perspectives provided by the document analysis remain limited.

A further conceptual limitation is the *a priori* understanding of the key concepts that interviewees will have had. It is reasonable to assume that the understanding of greenwashing, for example, would have differed between the interviewees. These pre-conceptions are important to understand as they shape what interviewees would or would not assess as greenwashing practices by financial institutions. These differences are not sufficiently captured through the research methodology and are only attempted to be discerned *post-interview*.

Finally, a key limitation is the lack of quantifiability for the amount of greenwashing occurrences that have occurred since the introduction of the SFDR. While interviewees did identify that greenwashing was possible within the context, they mentioned relatively few methods through which this occurred and did not give an indication for the frequency. By sharing that selective disclosure practices through intentional misclassification occurred, the interviewees assessed that greenwashing occurred but did not give insight into the implications. Recently, many funds have been reclassified from article 9 to article 8 (Scheitza and Busch, 2023). Yet the implications for previously classifying funds as article 9 in terms of potential greenwashing were not discussed, despite the reclassification being indicative of some greenwashing having occurred. Part of the reason for why it is challenging to identify the frequency of greenwashing occurrences is the wide-ranging definition of greenwashing. Interviewees will have had different conceptualizations of what greenwashing meant to them. Therefore discussing the frequencies or more complex ways in which greenwashing occurs would not have been possible, as interviewees would have been unable to identify these. Being unable to do so also reduces the quality of the research, as interviewees are able to identify limited greenwashing processes and are unable to identify a wide range of greenwashing practices and their frequency.

# Conclusion

The results of the research provide an in-depth analysis of the Sustainable Finance Disclosure Regulation (SFDR) by examining the underlying assumptions and frames that shape the SFDR's approach to transparency, accountability, and greenwashing. Answering the research question identified that the potential of transparency and accountability is undermined by greenwashing opportunities within the SFDR can occur to a considerable extent through selective disclosure and decoupling. The comparative cross-analysis of the document analysis and interview analysis provide insight into the themes and assumptions of the three concepts, transparency, accountability and greenwashing. Through the comparison, the differences between the intended and actual outcomes of the SFDR have been highlighted.

Transparency's potential to transform the outcomes of environmental policy by providing accountability has been a widely held assumption throughout the political realm. Yet as scholars have uncovered, the link between transparency and accountability remains a flawed endeavor. While any transparency is integral to accountability mechanisms, its presence is not a guarantee for the efficacy of accountability mechanism themselves. Within the theoretical framework provided, transparency has a plurality of rationales that motivate actors to disclose information. Since these motivations have diverging influences on the efficacy of accountability mechanisms, analyzing the rationales behind disclosure in a given context becomes a prerequisite for understanding the efficacy of the accountability mechanisms present. Within the context of the SFDR, the main rationales identified in the analyses have been the the technocratization and privatization rationales by Gupta and Mason and technocratic transparency by Tienhaara. Combined these illustrate that the motivations for financial institutions to disclose information are primarily to further their own sustainability aims while reducing scrutiny on their public image. Information disclosure occurs in a complex and technocratic manner, that lends itself to the decision-making process by experts and policymakers, rather than end investors. The additional intention for information disclosure under the SFDR is therefore not to provide accountability, but to improve governance through expert advice, increasing the efficiency and effectiveness of a specific policy program. These indicate that financial institutions might voluntarily embrace transparency not because they wish to be held to account, but because disclosing is convenient for their reputation. Through significant flexibility in self-defining sustainability and classifying their financial products, financial institutions could be motivated to for reasons most aligned with the privatization rationale. Accountability is therefore not promoted through the information disclosed, yet given the context it might still be prevalent.

Accountability in the theoretical framework is conceptualized through the four elements identified by Biermann and Gupta: normative, relational, decision, and behavioral. These elements are insufficients present in the context of the SFDR, resulting in a lack of *meaningful* accountability. Given the context of the SFDR and the influence that end investors have through

their scrutiny, it is possible that information disclosed under the SFDR leads to changes in their investment patterns. Nevertheless, both analyses identified critical issues with the prevalence of accountability mechanisms, identifying limitations to the implementation of the four elements. Transparencys' potential to enhance accountability is therefore limited by contextual factors, such as the desire from end investors to leverage sustainability information and the complexity of information that is demanded under the disclosure requirements. Accountability is not facilitated through the structures of the SFDR, reducing the efficacy of its mechanisms. Most importantly, there are a lack of clear and direct consequences for misaligned behavior by financial institutions within the SFDR. While stakeholders will be able to criticize the information disclosed pre-contractually, there are no significant mechanisms present to systematically identify and scrutinize the disclosed information. As a consequence two funds could classify differently as either article 8 or 9 while containing the same products, yet would be required to disclose different information. The opportunities for greenwashing are therefore clearly present within the context. Most importantly, decoupling and selective disclosure are prevalent within the SFDR, allowing financial institutions to exert influence on how they present themselves.

Greenwashing mechanisms are able to shape transparency, through information disclosure, in a way that undermines the efficacy of the accountability mechanisms within the SFDR. In both analyses greenwashing is conceptualized similarly, where greenwashing mechanisms such as decoupling and selective disclosure are principally identified. Both analyses are critical of financial institutions' ability to classify their products according to their own definitions of sustainability. Given this flexibility, they are able to generate a favorable definition of sustainability to match the products that already exist in their financial portfolio, increasing the possibilities for greenwashing. Financial institutions are able to present their products as more sustainable than they actually are through changing their definitions (decoupling), or selectively reclassifying their products to lesser articles in order to avoid stricter disclosure requirements (selective disclosure). By selectively disclosing information and classifying products strategically according to their own definition of sustainability, financial institutions are able to present themselves as more sustainable than how they ought to be interpreted. Hence, the SFDR poses a greenwashing risk to financial institutions, because following the guidelines without careful consideration of the reputational implications of statements do not guarantee them protection from greenwashing accusations. The potential for greenwashing to exist influences transparency by shaping how disclosed information is perceived and therefore limits the efficacy of accountability mechanisms. End investors who are overwhelmed by complex information may make decisions based on little evidence, with any shifts in perception undermining the key accountability mechanisms of end investor scrutiny.

Answering the research question based on these results suggests that the potential of transparency and accountability is undermined by greenwashing opportunities within the SFDR

through mechanisms such as selective disclosure and decoupling. Transparency's potential to transform the outcomes of environmental policy by providing accountability has been a widely held assumption, however, the link between transparency and accountability remains flawed. While any transparency is integral to accountability mechanisms, its presence is not a guarantee for the efficacy of accountability mechanisms themselves. Furthermore, transparency's potential to enhance accountability is further limited by contextual factors of the SFDR, such as the desire from end investors to leverage sustainability information and the complexity of information that is demanded under the disclosure requirements. These complex structures are ineffective and reduce the capacity for accountability to occur. Given that end investor scrutiny has been identified as the most impactful accountability mechanism, equitable accountability cannot occur as the SFDR does not provide clear and direct consequences for misaligned behavior by financial institutions within the SFDR. While stakeholders will be able to criticize the information disclosed pre-contractually, there are no significant mechanisms present to systematically identify and scrutinize the disclosed information. Given the complexity of the information required to be disclosed, the potential for greenwashing mechanisms are prevalent. By selectively disclosing information and classifying products strategically according to their own definition of sustainability, financial institutions are able to present themselves as more sustainable than how they ought to be interpreted. Greenwashing mechanisms are able to shape transparency, through information disclosure, in a way that undermines the efficacy of the accountability mechanisms within the SFDR. As a consequence, end investors who are overwhelmed by complex information may make decisions based on little evidence, with any shift in perception undermining the key accountability mechanisms of end investor scrutiny.

**Future research directions**

This research has been exploratory in nature and leaves open various novel avenues for future research. Primarily, research could continue to evaluate the mechanisms by which greenwashing can undermine the relationship between transparency and accountability. This could be achieved through novel contexts, whereby research could specifically focus on the normative and relational elements of all three concepts. Within the context of the SFDR, research could attempt at quantifying the extent to which greenwashing undermines the relationship between transparency and accountability through evaluating the information disclosure quality and comparing it to the intended outcomes of the SFDR. Future research could also expand on this exploratory research by assessing more effective mechanisms for information disclosure. Given the findings on transparency, future research could consider ways to simplify complex sustainability information, making it more accessible to end investors. It could also examine the contextual variables necessary to ensure information is not only disclosed to enhance governance effectiveness but also to improve accountability. Furthermore, future research could consider identifying more robust accountability measures to eliminate the insufficiencies from the four elements of accountability. Studying how these elements could be more comprehensively

incorporated into the SFDR would allow for more effective and meaningful accountability mechanisms and improve the capacity for end investors to divest from unsustainable financial institutions. Finally, the results of this research identified the potential for greenwashing within the SFDR, mainly due to selective disclosure and decoupling. Future research could look at how to reduce these greenwashing opportunities, through the development and incorporation of clear definitions of sustainability and unsustainable businesses into the SFDR. Research on how to create stricter regulations on the disclosure and classification of financial products, or developing a labeling scheme, could further reduce the current greenwashing opportunities. Such research could contribute to enhancing the credibility of financial institutions' sustainability claims.

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