Greenwashing: What Happens When Competition And Securities Laws Intersect?

Public companies have long developed best practices and legal expertise in drafting compliant securities disclosure documents. With the increase in required and voluntary disclosure by public companies regarding environmental, social and governance ("ESG") matters, disclosure has become more difficult to navigate, particularly disclosure around green claims such as carbon emissions reduction targets and net-zero commitments.

For over 14 years[1], the Canadian Securities Administrators have provided guidance on how to best disclose such information effectively while avoiding misleading investors.

The introduction of specific greenwashing provisions under the *Competition Act* last year, and the private rights of action thereunder which will come into force in June of this year, have increased the complexity of considerations regarding ESG disclosures.

To assist, we highlight certain key differences between securities laws and competition laws as they relate to greenwashing issues.

Same Goal but Different Perspectives

Generally, in the context of greenwashing, securities and competition laws have the same objective: preventing false, misleading or unsubstantiated environmental representations.

Securities laws consider greenwashing from the investors' perspective, while competition laws focus on consumer protection and maintaining fair competition. As a result, when determining whether a representation may contravene competition or securities laws, the thresholds are quite different.

- The test under the general "catch-all" provisions of the *Competition Act* is whether the representation is materially false or conveys a misleading general impression from the perspective of a credulous and inexperienced average consumer.
- The test under securities laws is more objective given that there will be a misrepresentation only if there has been an untrue statement of a material fact or an omission to state a material fact. This materiality threshold is met if a reasonable investor's decision to buy, sell or hold securities of the issuer would likely be influenced or changed because of such information or omission.

The CSA applied this test to the disclosure of climate-related risks in CSA Staff Notice 51-354, stating that "[t]he assessment should be based on whether a reasonable investor's decision to buy, sell or hold securities of an issuer would likely be influenced or changed by the knowledge that a particular risk exists for the issuer and would have material impact on the issuer's business if it were to crystallize".

The New Anti-Greenwashing Provisions

The difference of perspective between securities and competition laws has been exacerbated by the June 2024 amendments to the *Competition Act*. The amendments added two civil provisions intended to address unsubstantiated environmental claims.

- **Representations Relating to Product**: This provision prohibits a person from making a representation to the public in the form of a statement, warranty or guarantee of a product's benefits for protecting or restoring the environment or mitigating the environmental, social and ecological causes or effects of climate change *that is not based on an adequate and proper test, the proof of which lies on the person making the representation*.
- **Representations Relating to Business or Business Activity**: This provision prohibits a person from making a representation to the public with respect to the benefits of a business or business activity for protecting or restoring the environment or mitigating the environmental and ecological causes or effects of climate change *that is not based on adequate and proper substantiation in accordance with internationally recognized methodology, the proof of which lies on the person making the representation*.

These shifting substantiation onuses impose a burden on public companies analyzing their environmental disclosure. In other words, a statement that may have been considered appropriate under securities laws might be inadequately substantiated under the *Competition Act*.

The Competition Bureau (the "Bureau") released draft guidance regarding these greenwashing provisions, including on what may be considered an "internationally recognized methodology" from the Bureau's perspective. The draft guidance only provides general direction, defining 'substantiation' as "establishing by proof or competent evidence" (but does not necessarily involve testing) and 'methodology' as "a procedure used to determine something". It goes on to indicate that the Bureau will likely consider a methodology to be internationally recognized if it is “recognized in two or more countries”, although not necessarily by governments in those countries. The draft guidance emphasizes that the chosen methodology must also be shown to be “adequate and proper” substantiation of the claim, as that term has been interpreted by prior jurisprudence.

The draft guidance also notes that statements in regulatory filings are not the Bureau’s focus of the new amendments. Concerns were raised during the public consultation regarding the reach of the new provisions, including the application of these provisions to statements made in various regulatory filings, such as securities filings, which are technically public. The draft guidelines confirm that, regardless of whether regulatory filings could be captured under the deceptive marketing provisions of the *Act*, the Bureau is focused on marketing and/or promotional representations. However, if information in regulatory filings is used by businesses in promotional materials, the draft guidance is clear that the Bureau will consider the representations to be marketing representations. Given that the term “promotional material” is not defined in the legislation, we would benefit from further guidance from the Bureau on this.

Treatment of Disclaimers: An Elephant in the Room?

Issuers are used to employing disclaimers in their disclosure documents by following securities laws principles. Companies use disclaimers in regard to various disclosures, such as disclosures of forward-looking information (“FLI”), non-GAAP measures (Generally Accepted Accounting Principals), and information obtained from third party sources. Companies also might provide extensive risk factors in their disclosure documents, including in prospectuses and offering memoranda used in relation to sales of the companies’ securities and in various continuous disclosure documents.

For example, when disclosing carbon emissions targets or net-zero commitments, issuers should follow the securities law requirements applicable to FLI, considering that the CSA have confirmed that "this type of statement will typically constitute FLI" (CSA Staff Notice 51-364). As such, the issuer must not only have a reasonable basis for the FLI but it must also provide, among other things, cautionary language identifying the material risk factors that could cause actual results to differ materially from the information disclosed (see National Instrument 51-102 *Continuous Disclosure Obligations*, parts 4A and 4B). For convenience purposes, such information is often provided in the form of a disclaimer in the document.

The Bureau, however, has expressed an aversion to the use of disclaimers, particularly disclaimers used to restrict, contradict or somehow negate the message to which it relates. In the Bureau's view, if the main body of the advertisement conveys a misleading general impression, before any reference is made to a disclaimer, then the disclaimer may not alter the general impression in a way that ensures that consumers will not be misled.

Accordingly, when examining where to include a disclaimer in relation to environmental claims, the questions of how a disclaimer may be written and labelled and how a disclaimer may be brought to the attention of the reader are important for issuers to consider under both securities and competition laws.

Damages or No Damages: Does It Matter?

Under securities laws, private plaintiffs that bring claims for misrepresentation generally are seeking to be compensated for damages incurred in relation to the misrepresentation.

For example, under the *Securities Act* (Québec), the *Securities Act* (Ontario) and the *Securities Act* (British Columbia), if:

- an investor purchased securities from the issuer through a prospectus offering (i.e., in the primary market) or on a stock exchange (i.e., in the secondary market),
- there is a misrepresentation in the prospectus or in the company's continuous disclosure, and
- the price of the companies' securities decreases, the investor has incurred a loss for which damages may be sought.

Under the *Competition Act*'s private right of actions that will be in force in June 2025, however, the basis for relief will not be based on the traditional damage-based claims. Where representations to the public are found to be materially false or misleading, an applicant can seek "an amount, not exceeding the total of the amounts paid to the [advertiser] for the products in respect of which the conduct was engaged in, to be distributed among the persons to whom the products were sold… in any manner that the court considers appropriate". This choice of language is akin to restitution.

The remedial powers of Canada's Competition Tribunal (the "Tribunal") also include a prohibition order (i.e., an order stopping the alleged conduct), the imposition of a corrective notice and an order to pay an administrative monetary penalty the greater of (i) $10 million, or (ii) three times the value of the benefit derived from the deceptive conduct, or, if that amount cannot be reasonably determined, 3% of the corporation's annual worldwide gross revenues.

In addition, in order for private parties to bring a private right of action before the Tribunal, they must first apply for and obtain leave. In particular, the Tribunal may grant leave if satisfied that it is in the public interest to do so. This new leave test has yet to be judicially interpreted by the Tribunal.

Can Directors and Officers Be Liable?

Directors and officers can be captured by both securities and competition legislation.

First, the *Securities Act* (Québec), the *Securities Act* (Ontario) and the *Securities Act* (British Columbia) indicate that directors and, in some instances, officers can be liable for misrepresentations made in primary or continuous disclosure documents (prospectus, MD&A, AIF, circular, etc.) or other voluntary disclosure (referred to as non-core in Québec).

Second, there are specific provisions under securities laws which provide a defence to claims if the directors or officers acted reasonably and with diligence.

Similarly, the *Competition Act* has a due diligence defence, which provides that if a person (which would include directors and officers) establishes that the person exercised due diligence to prevent a reviewable conduct (including a misrepresentation from occurring), the only remedy available is a prohibition order. In determining whether the person has exercised due diligence, the Tribunal would – as a general matter – consider, despite such person's impugned conduct, whether such person (1) took all reasonable steps appropriate to prevent the commission of the impugned conduct or (2) reasonably believed in a mistaken set of facts that, if true, would render the act or omission innocent. The respondent person bears the burden of proof to demonstrate due diligence.

Is It Safe to Look Forward?

In addition to the complex intersections between competition and securities laws, public companies also face the challenge of relying on securities laws when it comes to forward-looking environmental disclosure (e.g., net-zero commitments).

In order to disclose a financial outlook under securities laws, the information must be based on reasonable assumptions and limited to a time period for which the information can be reasonably estimated. It is unclear how this standard can reasonably be applied in the context of forward-looking environmental disclosure, considering the level of uncertainty and subjectivity associated with climate change and any commitments to reduce carbon emissions (direct and indirect) and the timelines typically used to assess such matters, which far exceed the timelines typically applied to financial disclosures.

Other jurisdictions have implemented safe harbours from private liability for certain climate-related disclosures. Are we ripe for such provisions in Canada? To know more, read our bulletin on the issue: [How Safe Are Safe Harbours for Climate-Related Disclosure in Canada?]

Footnote

1. CSA Staff Notice 51-333 – [i]Environmental Reporting Guidance[/i] (October 2010); CSA Staff Notice 51-354 – [i]Report on Climate Change-related Disclosure Project[/i] (April 2018); CSA Staff Notice 51-358 – [i]Reporting of Climate Change-related Risks[/i] (August 2019); CSA Staff Notice 51-364 – [i]Continuous Disclosure Review Program Activities for the fiscal years ended March 31, 2022 and March 31, 2021[/i] (November 2022); CSA Staff Notice 51-365 – [i]Continuous Disclosure Review Program Activities for the Fiscal Years Ended March 31, 2024 and March 31, 2023[/i] (November 2024).

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

Authors: Marie-Christine Valois, Stephen Erlichman, Antonio Di Domenico, Martin Ferreira Pinho, Melanie Beland

Fasken