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SEC Enforcement Case Summary
Adviser Fails to Adhere to Investment Criteria for ESG-Marketed Funds

On October 21, 2024, the SEC charged investment adviser, WisdomTree Asset Management Inc., with making misstatements and for compliance failures relating to the execution of an investment strategy that was marketed as incorporating environmental, social, and governance (***ESG***) factors. The adviser agreed to a $4 million civil penalty in the settled case.

According to the SEC's order, from March 2020 until November 2022, WisdomTree represented in prospectuses for three ESG-marketed exchange-traded funds, and to the board of trustees overseeing the funds, that the funds would not invest in companies involved in certain products or activities, including fossil fuels and tobacco. However, the SEC found that the funds invested in companies that were involved in fossil fuels and tobacco, including in coal mining and transportation, natural gas extraction and distribution, and retail sales of tobacco products. In seeking approval to create the ESG Funds as part of a strategy change for three existing funds, WisdomTree represented to the Board that the model it was developing would have the capability to screen out the securities of companies that had "any involvement" in fossil fuels and tobacco. However, the SEC order noted that data WisdomTree purchased from a third-party vendor only identified a subset of companies involved in fossil fuels, and WisdomTree failed to purchase supplemental data that would have identified additional such companies. According to the order, WisdomTree attempted to augment its screening process with additional data from a second third-party vendor, but its investment process was still not removing all securities of companies involved in fossil fuels. WisdomTree was further informed that the vendor data identifying issuers involved in tobacco retail sales had not captured certain retailers who derived less than 10% of their revenues from retail sales of tobacco products. WisdomTree did not promptly inform the Board or revise the ESG Funds' prospectuses concerning these issues with respect to fossil fuels and tobacco screening.

The SEC further charged WisdomTree with failing to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act in connection with the investment process for the ESG Funds, including concerning the manner in which WisdomTree's model excluded the securities of certain companies from the portfolios of the ESG Funds as described in its statements to the Board and the ESG Funds' disclosures. The Firm later updated disclosures and risk factors in the ESG fund prospectuses to address the data the model used and subsequently obtained Board approval to liquidate the ESG funds.

Wisdom Tree was charged with violations under the anti-fraud provisions of the Investment Advisers Act and Investment Company Act as well as compliance rule violations. While ESG rulemaking proposed in 2022 has not been adopted, it is important to keep in mind that the SEC may still bring enforcement actions for misleading disclosures regarding ESG investment criteria or for failing to establish and implement policies and procedures to ensure that advisers adhere to any criteria disclosed with respect to their investment activities.

See Summary – https://www.sec.gov/newsroom/press-releases/2024-173