

**Kellerhals
Carrard (ed.)**

**Adoption of a
New Paradigm
through
Regulatory
Change and
Innovation**

orell füssli
Juristische Medien

Sustainable Finance in Switzerland

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Foreword

The words *Environment, Social and Governance (ESG)* and *sustainable finance* are on everyone's minds. They are key strategic topics not only for society at large, *but* also for the entire business community. At the same time, they address everybody's co-responsibility for political and legal developments. The 17 UN Sustainable Development Goals (SDGs) were adopted by the heads of state and government of the 193 UN member states on behalf of their people. It is widely accepted that the business community should accept its responsibility and contribute to the realization of these ambitious political goals.

Kellerhals Carrard (KC) is one of the largest and oldest leading law firms in Switzerland. KC was the first Swiss law firm to launch a dedicated ESG-Desk to coordinate its firm-wide expertise regarding the interdisciplinary topics ESG and sustainable finance. This publication is primarily shaped by the KC Practice Group Banking, Finance & Fintech, one of the firm's focus areas, and supported by the ESG-Desk as well as various other KC Practice Groups.

This publication is the result of teamwork by over 30 KC lawyers across KC's various sites in Switzerland and provides a lean and comprehensive summary of the most recent regulatory and legal developments in ESG and sustainable finance with a focus on regulatory change and innovation.

Accordingly, the publication focuses on the regulatory and case law developments in Switzerland until April 2024. However, ESG and sustainable finance regulation or self-regulation are a moving target and further developments can be expected. We are looking forward to continuing to monitor the evolution of the legislation and other regulations in these areas.

2024, Zurich, Luca Bianchi/Isabelle Romy/Cornelia Stengel

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Authors

Roman Aus der Au

Dr. iur., Attorney at Law, M.A. HSG
in Law and Economics

Christoph Bauer

PD Dr. iur., Attorney at Law

Thomas Bauer

Dr. iur., Attorney at Law

Sémia Bey

lic. iur., Lawyer, LL.M.

Luca Bianchi

lic. iur., Attorney at Law, LL.M.,
MBA, MAS UZH in Finance

Manuel Brogli

MLaw, Attorney at Law

Jean-Luc Chenaux

Prof. Dr. iur., Attorney at Law

Vincent Cottier

MLaw & BA in International
Relations

Shima Gennari

MLaw, Attorney at Law

Dzeneta Hrustic

MLaw, Attorney at Law

Roman Huber

Dr. iur., Attorney at Law, LL.M.

Michael Kremer

lic. iur., Attorney at Law, LL.M.

Armin Kühne

Dr. iur., Attorney at Law

Daniel Lengauer

Dr. iur., Attorney at Law, LL.M.

Gaspard Loderer

MLaw, Attorney at Law, LL.M.

Karim Maizar

Dr. iur., Attorney at Law

Nicolas Mosimann

Dr. iur., Attorney at Law, LL.M.

Sarah Mostafa

lic. iur., Attorney at Law, LL.M.

Dominik Oberholzer

Dr. iur., Attorney at Law, LL.M.

Henry Peter

Prof. Dr. iur., Attorney at Law

Ines Pöschel

lic. iur., Attorney at Law

Christophe Rapin

lic. iur., DEA in European Law,
Attorney at Law, registered
at the bar in Geneva and
Brussels

Isabelle Romy

Prof. Dr. iur., Attorney at Law

Lea Ruckstuhl

MLaw, Attorney at Law

Reto Schumacher

Dr. iur., Attorney at Law, LL.M.

Jessica Sommer

Dr. iur., Attorney at Law

Cornelia Stengel

Prof. Dr. iur., Attorney at Law

Noémie Weill

MLaw, Attorney at Law

Ksenia Wess

Dr. iur., MLaw

Denise Wohlwend

Dr. iur., Attorney at Law

Rim Zaouia

MLaw, Attorney at Law, LL.M.



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**B. Regulatory Change
and Innovation: A Shift
to a New Paradigm**

A. Origin and Importance of ESG and Sustainability for the Economy and the Financial Sector

1. Notions

The acronym ESG stands for Environment, Social, and Governance and refers to criteria used to evaluate companies and measure their impact in these areas beyond a sole focus on shareholders' returns. Sustainability is a broader concept that aims to reconcile the economic, social and environmental dimensions of a development that meets the needs of the present generation without compromising the ability of *future generations* to meet their own needs¹. In the financial sector, these terms – often used as synonyms even though they have a slightly different meaning – are generally referred to as sustainable finance².

2. Origin

These terms have been gaining in importance for the financial world and the business community at large since early 2000, when the former UN General Secretary Kofi Annan launched a corporate responsibility initiative with the primary goal of implementing universal principles in business. Under the auspices of the UN Global Compact and with the funding of the Swiss government, leading financial institutions were invited to develop guidelines and recommendations on how to integrate environmental, social, and governance issues more effectively. The report “Who Cares Wins”, published in 2004, is the result of their joint effort and collaboration³. The report contains recommendations for a large array of actors, including financial institutions, analysts, companies, regulators, and NGOs, with the overall goals of contributing

1 World Commission on Environment and Development (WCED), 1987, “Our common future”, also known as “Brundtland Report”, available at: <<https://www.are.admin.ch/are/en/home/media/publications/sustainable-development/brundtland-report.html>>, 37.

2 There is no generally accepted definition of sustainable finance. According to the Swiss Federal Council, sustainable finance requires financial market participants to take the three ESG criteria of sustainability into account: see Sustainable Finance Guidelines, 26 June 2020, available at: <<https://www.news.admin.ch/newsd/message/attachments/61909.pdf>>; see also section II (p. 43 et seqq.).

3 UN Global Compact, Who Cares Wins, i.

to more resilient investment markets, as well as to the sustainable development of societies⁴.

3. International Initiatives and Frameworks

Subsequently, several initiatives were launched by various organizations to integrate ESG criteria and factors into the financial market, investment process, and risk management more effectively. For example, the United Nations Environment Program Finance Initiative commissioned the so-called “Freshfield Report”, published in 2005⁵, which concluded that the links between ESG factors and financial performance were increasingly being recognized and that integrating ESG considerations into an investment analysis so as to predict financial performance more reliably was clearly permissible and was arguably required in all jurisdictions under review. The “Who Cares Wins” and the Freshfield reports later formed the basis for the launch of the Principles for Responsible Investment (PRI) at the New York Stock Exchange in 2006 and the launch of the Sustainable Stock Exchange Initiative (SSEI) in 2007.

In the last decade, the view that companies are more likely to generate growth and robust performance if they create value for all stakeholders, and include ESG factors in their business strategy, has permeated the business and financial world and is ex-

pressed in a variety of treaties, guidelines, and principles set forth by governmental bodies, private associations, and NGOs. For instance, the 2030 Agenda for Sustainable Development⁶ and its 17 Sustainable Development Goals (SDGs) stimulate action in areas of critical importance for humanity and the planet, while balancing the three dimensions of sustainable development, i.e., the economic, social, and environmental dimensions.

The Paris Agreement on Climate Change adopted in 2015⁷ expressly provides in its Art. 2 (1) (c) that one of its goals is to make finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development. The OECD Guidelines for Multinational Enterprises of 2010, revised on 8 June 2023, provide voluntary principles and standards for responsible business conduct consistent with applicable laws and internationally recognized standards. The Task Force on Climate-related Financial Disclosures was created in 2017 by the Financial Stability Board (FSB) to develop recommendations on the type of information that companies should disclose to support investors, lenders, and insurance underwriters in appropriately assessing and pricing climate change risks. The TCFD was discontinued following the release of the Task Force 2023 Status Report, at the request of the FSB, which has asked the IFRS Foundation to take over the monitoring of the progress of companies' climate-related disclosures.

⁴ UN Global Compact, *Who Cares Wins*, i-ii.

⁵ UNEP Finance Initiative, *A Legal Framework for the Integration of Environmental, Social and Governance Issues into Institutional Investment*, October 2005.

⁶ UN, Resolution A/RES/70/1.

⁷ The Paris Agreement was adopted by 196 Parties during the UN Climate Change Conference (COP 21) held in Paris, France, on 12 December 2015. Switzerland ratified it on 6 October 2017, AS 2017 5733.

The Taskforce on Nature-related Financial Disclosures (TNFD) was launched in 2021. It is a market-led and science-based initiative supported by national governments, businesses, and financial institutions worldwide. The TNFD developed a set of disclosure recommendations and guidance that enable businesses and finance to integrate nature into decision making.

4. Swiss National Initiatives and Frameworks

Switzerland has ratified numerous international treaties that expressly embody the principle of sustainable development, including the Paris Agreement (2015) in 2017, and has aligned its sustainable development strategy with the 2030 Agenda. The Swiss Federal Council regularly publishes action plans and reports on its policies, goals, and areas for action for the implementation of the 2030 Agenda⁸.

The Swiss legislature has enacted or amended various statutes to implement Switzerland's international obligations into

domestic law (see section III.A., p. 60). Furthermore, in line with other jurisdictions and the EU, Switzerland has enacted statutory transparency and reporting obligations, according to which companies – including financial institutions – must provide social, governance, and environmental information, in particular on their climate transition plans, to ensure that investors and other stakeholders have access to the information they need to assess investment risks arising from climate change and other sustainability issues⁹.

Besides the enactment of new legislation, the Federal Council has repeatedly expressed its clear expectations of the private sector, which it intends to see contribute to the objectives of the 2030 Agenda. Thus, it expects companies headquartered or operating in Switzerland to respect international standards and principles of corporate social responsibility, and to implement human rights due diligence as a “general standard of conduct expected of all companies wherever they operate”¹⁰.

The Federal Council considers that the real economy is the main lever for moving towards a sustainable economy, as it has a direct influence on the various aspects of sustainable development through its production and consumption of goods and services. As to the financial sector, it plays a key role in supporting the transition towards a more sustainable economy¹¹.

⁸ See for instance Voluntary National Review of Switzerland 2022, available at: <<https://www.eda.admin.ch/agenda2030/en/home/strategie/nationale-berichterstattung.html>>.

⁹ See sections III.A. and III.B.3 (p. 60 and 81).

¹⁰ UN Guiding Principles on Business and Human Rights, Swiss National Action Plan 2020–2023, January 2020, available at: <https://www.nap-bhr.admin.ch/napbhr/de/home/nap/nationaler_aktionsplan1.html>, 22.

¹¹ Federal Council, Report 2022, 3.



5. Role of the Swiss Financial Center

Sustainability is a key focus of Switzerland's financial market strategy. The Swiss Federal Council recognized in 2020 that sustainable finance is a great opportunity for the Swiss financial center and a relevant competitive factor in sustainable growth and expressed the view that *"The Swiss financial centre should be a leading global location for sustainable financial services"*¹².

It set forth the broad outlines of its policy to implement this objective in the following reports:

-
- Federal Council Report "Sustainability in Switzerland's financial sector", published in June 2020
-
- Federal Council Report "Leading world-wide, rooted in Switzerland", published in December 2020
-
- Federal Council Report "How can Switzerland make financial flows climate-compatible?", published in November 2021
-
- Federal Council Report "Sustainable finance in Switzerland", published on 16 December 2022
-

The 2022 Report on Sustainable finance in Switzerland outlines 15 measures planned for the period 2022 to 2025. The aim is to solidify Switzerland's position as a global leader in sustainable finance. Sustainability is a key pillar of the Swiss financial market strategy, and Switzerland seeks to enhance its competitiveness as a financial hub while aligning with the UN SDGs. The report emphasizes the importance of credibility and preventing greenwashing to maintain international competitiveness in sustainable finance¹³.

The measures focus on various areas, including improving sustainability data across all sectors of the economy, promoting transparency in the financial sector, and encouraging financial institutions to disclose their engagement with sustainability goals. Additionally, the Federal Council aims to support investments that generate positive social and environmental impacts alongside financial returns. The measures are also intended to contribute to the transition to a sustainable economy through active participation in international bodies and backing global initiatives for carbon pricing¹⁴.

¹² Federal Council, Report 2020, 4.

¹³ Federal Council, Report 2022, 3.

¹⁴ Idem.

B. Regulatory Change and Innovation: A Shift to a New Paradigm

Regulatory change and innovation have been the “hot topics” in the financial industry in Switzerland over the last decade. In the aftermath of the financial crisis of 2008 a completely new set of regulations for the financial markets was elaborated and implemented. In addition, the strong digitalization trend radically changed the financial markets. New players, business models, and financial products challenged established market players.

Developments in ESG and sustainable finance in Switzerland reflect a global so-

ciocultural, economic and legal megatrend and represent a paradigm shift¹⁵ with implications for regulation. New regulations and innovations in the area of ESG and sustainable finance¹⁶ are emerging rapidly and represent a fast-evolving new chapter in the regulation of Swiss financial services.

In addition, a broader adoption of innovative ESG and sustainable financial services and products will support the importance of conducting business in a sustainable and compliant manner.

¹⁵ FRIEDMAN, 1 et seq.

¹⁶ Idem.



II. ESG and Sustainable Finance: Criteria and Definitions

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**B. Environment, Social,
Governance (ESG)**

A. Introduction

In recent years, Environmental, Social, and Governance (ESG) criteria have gained tremendous importance as key factors in evaluating companies' sustainability and ethical practices. It is becoming crucial for them, and is increasingly mandated by law, to

consider ESG criteria when making business decisions. This section provides an overview of the most important ESG issues for the economy and the financial sector as well as a definition of sustainable finance.



Photo: iStock, Eric Bergeri

B. Environment, Social, Governance (ESG)

1. The “E”

“E” for Environment refers to the impact of a company’s operations on the environment or, inversely, the impact of the environment on the company’s operations. While it is generally accepted that the E factors relate to climate change (e.g., carbon footprint), use of natural resources (e.g., energy efficiency), pollution and waste (e.g., toxic emissions and waste management), and protection of biodiversity, there is no overall definition of the environmental elements covered thereby, and they vary depending on the industry or business sector and the applicable regulations.

In addition to the Paris Agreement (2015), which brought climate protection to the forefront of the “E” concerns, a wide range of global, regional, and national legal and non-legal (soft law) instruments specify the environmental elements and resources that fall within their field of application and thus give concrete expression to the scope of the “E”. At the global level, they include, but are not limited to, the UN SDGs, the Rio Declaration on Environment and Development (1992), the Agenda 21 (1992), the United Nations Framework Convention on Climate Change (UNFCCC, 1992), the Convention on Biological Diversity (1992), the Kunming-Montreal Global Biodiversity Framework (GBF) (2022), the United Nations Convention to Combat Desertification in those Countries Experienc-

ing Serious Drought and/or Desertification, Particularly in Africa (1994), the ISO Standard 14001 on Environmental Management Systems (2015), the Environmental and Social Performance Standards (2012/1) of the International Finance Corporation (IFC), as well as the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD).

For instance, the UN SDGs that focus on the environmental dimensions of sustainability include SDG 6 (Ensure availability and sustainable management of water and sanitation for all), SDG 7 (Ensure access to affordable, reliable, sustainable and modern energy for all), SDG 12 (Ensure sustainable consumption and production patterns), SDG 13 (Take urgent action to combat climate change and its impacts), SDG 14 (Conserve and sustainably use the oceans, seas and marine resources for sustainable development), and SDG 15 (Protect, restore and promote sustainable use of terrestrial ecosystems, sustainably manage forests, combat desertification, and halt and reverse land degradation and halt biodiversity loss)¹⁷.

The OECD Guidelines refer expressly to climate change mitigation and adaptation; conservation, restoration, and sustainable use of biological diversity; sustainable, efficient, and lawful use of land, resources, and energy; sustainable consumption and production including through promotion of

¹⁷ UN, Resolution A/RES/70/1.

circular economy approaches, and prevention, reduction, and control of pollution¹⁸.

The relevant legal framework at the Swiss level includes *inter alia* the Federal Act on the Protection of the Environment (EPA) and its ordinances, the Federal Act on the Reduction of CO₂ Emissions (CO₂ Act) and its ordinance, the Federal Act on Climate Protection Goals, Innovation and Strengthening Energy Security of 30 September 2022 (Climate Act), which will come into force on 1 January 2025, as well as individual legal provisions, such as Art. 964a et seq. CO and its ordinances, in particular the Ordinance on Climate Disclosures, which is in line with the TCFD recommendations¹⁹.

While all aspects of the “E” are relevant for the finance sector²⁰, the Swiss Federal Council has recently focused its sustainable finance efforts on climate and biodiversity and has expressly considered that in order for the financial center to support the achievement of sustainability goals optimally, and to take sustainability risks appropriately into account, it is reliant on sustainability data from all sectors of the economy²¹. The new disclosure provisions inserted in the Code of Obligations in 2022 and the Ordinance on Climate Disclosures in particular will allow for more transparency on the environmental and climate impacts of Swiss companies. According to the Federal Council, *“the more comparable, accurate and mean-*

*ingful this data is, the better it can be integrated into advice, financial institutions’ balance sheets and the financial system as a whole, and the lower the transaction costs will be for international and national investors. Ideally, this will also help broaden the investor base and lower capital costs for the companies that provide high-quality sustainability data, thus optimally satisfying investor demand”*²².

The Federal Council further follows the work performed by the private sector-led international Taskforce on Nature-related Financial Disclosures (TNFD), which in September 2023 issued a framework for disclosures on biodiversity risks and impacts that closely mirrors the TCFD recommendations.

2. The “S”

While the “E” and “G” components of ESG have received considerable attention and are becoming well-established in the corporate world, the social component is still often overlooked or misunderstood. The “S” part of ESG focuses on corporations’ impact on society, and encompasses fundamental factors in that context, whose significance and implications for businesses, their management, investors, and society are briefly described below.

18 OECD Guidelines, 33. See, similarly, UNPRI, Environmental Issues, available at: <<https://www.unpri.org/sustainability-is-issues/environmental-social-and-governance-issues/environmental-issues>>; IMF, Global Financial Stability Report, 82.

19 See sections III.A.2 and IX.I.2 (p. 63 and p. 181).

20 See for instance SSF, Glossary, “Environmental Factors (E of ESG)”, available at: <<https://www.sustainablefinance.ch/en/resources/what-sustainable-finance/glossary.html>>.

21 Federal Council, Report 2022, 3.

22 Federal Council, Report 2022, 7.

2.1 Labor Practices

A critical social factor is tied to labor practices. Businesses must prioritize fair employment conditions, including fair wages, reasonable working hours, decent and safe work environments, and non-discrimination policies for employees. Compliance with labor laws and regulations is essential to protect workers' rights, prevent exploitation, and promote social justice.

In Switzerland, required labor-related standards are mainly governed by Art. 8 al. 3, 23, 27 al. 2, 28, and 41 al. 1 lit. d of the Swiss Federal Constitution²³, and Art. 319-362 of the CO. Internationally, the Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy (the ILO MNE Declaration, last revised in 2022) guides corporations on responsible, inclusive and sustainable workplace practices.

Corporations must ensure that their employment contracts, policies, and procedures are in compliance with national laws and international labor standards. Prioritizing labor rights avoids running legal and reputational risks associated with labor law violations and the potentially severe direct and indirect sanctions deriving from the possible materialization of these risks. In addition, companies that prioritize these values are more likely to attract and retain top talents, leading to increased productivity and profitability.

2.2 Gender-Related Issues

Achieving gender equality is another fundamental societal goal and a critical element of the "S" component. Gender equality encompasses equal pay, equal opportunities for career advancement, and the prevention of workplace discrimination and harassment regardless of one's gender.

In Switzerland, progress has been made in addressing gender-related issues through regulations such as Art. 8 al. 2 of the Swiss Federal Constitution and the Federal Act on Gender Equality²⁴. These laws aim to ensure equal rights and opportunities for people in various areas of life. The recent introduction of gender quotas in the new Swiss CO to be implemented by public limited companies (Art. 734f CO) has been controversial but will contribute to promoting gender balance and representation in corporate leadership positions. Internationally, milestone documents such as the Universal Declaration of Human Rights (UDHR), the Convention on the Elimination of All Forms of Discrimination Against Women, and the UN Guiding Principles on Business and Human Rights (UNGPs) provide guidelines and standards for gender equality and women's rights.

While improvements are underway, challenges and disparities remain in achieving gender equality. Efforts are ongoing across countries, including Switzerland, to foster gender equality and create a more inclusive and diverse working environment and society.

²³ Federal Constitution of the Swiss Confederation of 18 April 1999, SR 101.

²⁴ SR 151.1.

2.3 Human Rights

The respect for and protection of human rights is a pillar of responsible business conduct. This includes protecting the rights of workers, suppliers, and communities impacted by a company's operations and avoiding any activity or, more generally, factor which may contribute to human rights abuses.

Companies are expected to ensure that their policies and practices are in line with international human rights standards such as the International Covenant on Civil and Political Rights, the UDHR, and the UNGPs. At a national level, Art. 54 of the Swiss Federal Constitution explicitly states that Switzerland must promote respect for human rights and democracy in its foreign relations. The Federal Act on Measures pertaining to Civil Peace Support and the Promotion of Human Rights of 19 December 2003²⁵, further reinforces this commitment.

By prioritizing human rights and fair treatment of employees, suppliers, and customers, corporations can enhance trust on the part of stakeholders and mitigate legal and reputational risks.

2.4 Community Engagement

Engaging with local communities consists of building positive relationships with neighboring entities and stakeholders and contributing to their economic and social development. Companies that engage with local communities or organizations can often obtain valuable insights, build goodwill, and foster sustainable development.

The concept of “*Social License to Operate*” (SLO) is often referred to in that regard. Inspired by Rousseau’s “*Contrat Social*”, the idea underlying the SLO is that companies

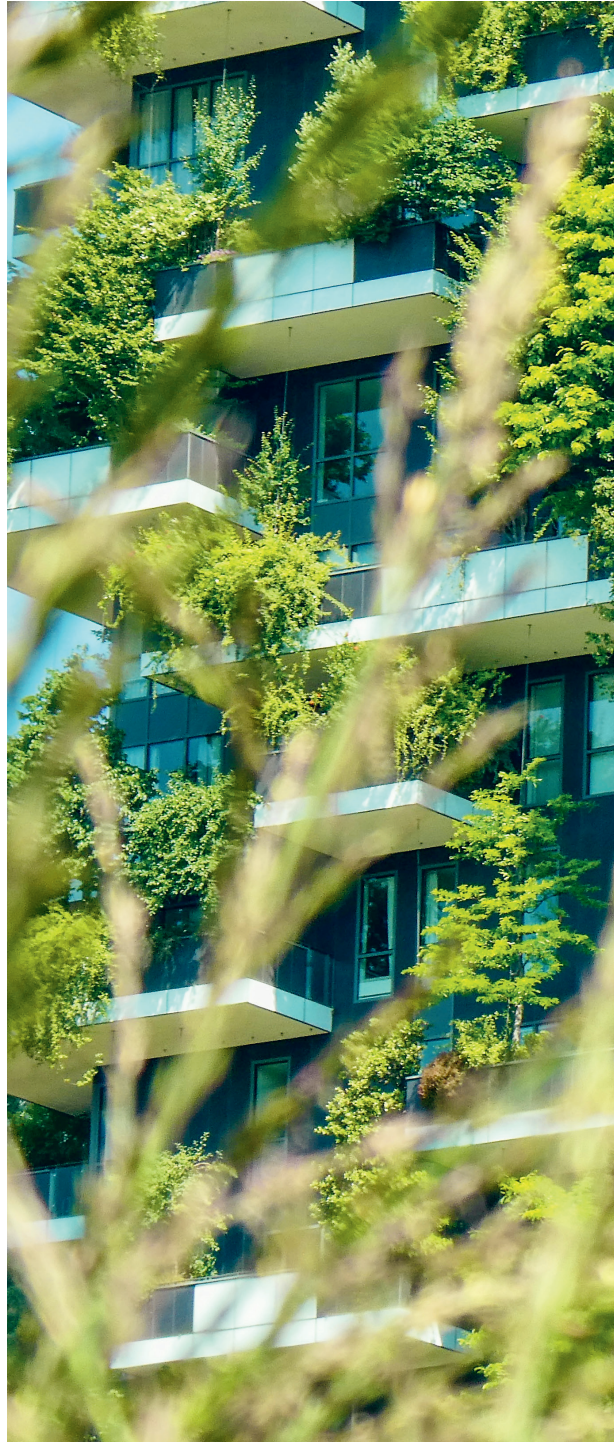




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