

Switzerland to Foster Sustainable Finance and Prevent Greenwashing in Financial Market

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Abstract

The Swiss government published a report identifying four areas for action for a leading sustainable financial centre with 15 measures and a position paper on next steps to be expected regarding the prevention of greenwashing in the financial sector, to consolidate the Swiss financial centre's leading role in sustainable finance.

Introduction

The Swiss financial industry has a long tradition of self-regulation, based on the idea that its flexibility and practical proximity would represent an advantage compared to more state-regulated markets, but also because in recent history, the transfer of regulations from the EU did not have the desired effect.¹ While some self-regulation can be recognised by the Swiss Financial Market Supervisory Authority (FINMA) as a minimum standard in line with art. 7 para. 3 of the Financial Market Supervision Act, with the effect that other market participants would have to follow them, there has been room for voluntary self-regulation, which is only binding for the members of the respective industry association.

Accordingly, also in the field of sustainable finance, industry associations have long paved the way for the implementation of industry standards; the Swiss Bankers Association published guidelines for the integration of ESG considerations into the advisory process of private clients in June 2020 and on the integration of ESG-preferences and risks into investment advice and portfolio management in June 2022 and the Assets Management Association Switzerland together with Swiss Sustainable Finance published guidelines with recommendations to avoid the greenwashing trap.²

Nevertheless, FINMA also published a couple of guidances, closely following international developments,³ to promote sustainable finance and prevent greenwashing, e.g. the FINMA Guidance 05/2021 on preventing and combatting greenwashing in November 2021, the FINMA Guidance 03/2022 on climate risks disclosures in November 2022 and the FINMA Guidance 01/2023 on developments in the management of climate risks in January 2023.⁴

Considering that the measures taken so far were insufficient and with the intention that the Swiss financial centre shall be globally leading in the field of sustainable finance,⁵ the Swiss government, after rather being reluctant,⁶ finally stepped in and published a report identifying four areas for action for a leading sustainable financial centre with 15 measures⁷ and a position paper on next steps to be expected regarding the prevention of greenwashing in the financial sector.⁸

These two publications shall be further analysed hereunder.

Four areas for action with 15 measures to foster sustainable finance

In December 2020, the Swiss government adopted a Swiss financial market strategy, where sustainability was listed as one of the main pillars.⁹ The publication took place half a year upon the publication of the EU's Taxonomy Regulation, which established the overarching conditions that an economic activity has to meet in order to qualify

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¹ For example, the exchange equivalence between the EU and Switzerland, which did not occur, eventually; Thomas Stanat and Susanne Winkler, *Sustainable Finance, Eine praxisorientierte Darstellung der Nachhaltigkeit im Banking* (2022), p. 17.

² Swiss Bankers Association, *Guideline for the integration of ESG considerations into the advisory process of private clients* (June 2020), https://www.swissbanking.ch/Resources/Persistent/5/9/3/b/593b75d1d479dc70ff20a76991deffd9ca4bab/SBA_Guidelines_for_the_integration_of_ESG_considerations_into_the_advisory_process_for_private_clients_EN.pdf; *Guidelines for the financial service providers on the integration of ESG-preferences and ESG risks into investment advice and portfolio management* (June 2022), https://www.swissbanking.ch/Resources/Persistent/a/5/e/0/a5e0845f065a60699df88910ae675b7082e69411/SBA_Guidelines_investment_advice_and_portfolio_management_EN.pdf; Asset Management Association Switzerland and Swiss Sustainable Finance (December 2021), https://www.sustainablefinance.ch/upload/cms/user/RecommendationsforSustainableInvestmentProducts_AMAS_SSF.pdf.

³ Beat Brändli, "Entwicklungen im Bank- und Kapitalmarktrecht" in *Schweizerische Juristen-Zeitung*, SJZ 119/2023, p. 28.

⁴ FINMA, *FINMA Guidance 05/2021* (November 2021), https://www.finma.ch/en/~media/finma/dokumente/dokumentencenter/myfinma/4dokumentation/finma-aufsichtsmittelungen/20211103-finma-aufsichtsmittelung-05-2021.pdf?sc_lang=en&hash=7F911020E829EA5910FF903AF851B2F3; *FINMA Guidance 03/2022* (November 2022), https://www.finma.ch/en/~media/finma/dokumente/dokumentencenter/myfinma/4dokumentation/finma-aufsichtsmittelungen/20221129-finma-aufsichtsmittelung-03-2022.pdf?sc_lang=en&hash=76D53FE0BCE81FEAC2C25077BD69D190; and *FINMA Guidance 01/2023* (January 2023), https://www.finma.ch/en/~media/finma/dokumente/dokumentencenter/myfinma/4dokumentation/finma-aufsichtsmittelungen/20230124-finma-aufsichtsmittelung-01-2023.pdf?sc_lang=en&hash=AE5AC34C3A564F4CF9FBD08557A3D124.

⁵ Brändli, "Entwicklungen im Bank- und Kapitalmarktrecht" in *Schweizerische Juristen-Zeitung*, SJZ 119/2023, p. 29.

⁶ Stanat and Winkler, *Sustainable Finance, Eine praxisorientierte Darstellung der Nachhaltigkeit im Banking* (2022), p. 15.

⁷ The Federal Council, *Sustainable Finance in Switzerland: Areas for action for a leading sustainable financial centre, 2022–2025* (December 2022), <https://www.news.admin.ch/newsd/message/attachments/74562.pdf>.

⁸ The Federal Council, "The Federal Council's position on the prevention of greenwashing in the financial sector" (December 2022), <https://www.news.admin.ch/newsd/message/attachments/74580.pdf>.

⁹ The Federal Council, *Leading worldwide, rooted in Switzerland: Policy for a future-proof Swiss financial centre* (December 2020), <https://www.sif.admin.ch/dam/sif/en/bilder/politik-finanzplatz-schweiz/politik-finanzplatz-schweiz-bericht.pdf.download.pdf/politik-finanzplatz-schweiz-bericht.pdf>.

as environmentally sustainable.¹⁰ Based on the adopted financial market strategy, Switzerland should strengthen its competitiveness as a financial centre by becoming a sustainable finance pioneer, thereby also achieving the United Nations Sustainable Developments Goals.¹¹ Following this strategy, the Swiss government published in December 2022 a report on sustainability for the years 2022–2025, which sets out 15 measures in four defined areas of action, notably aiming at ensuring more and qualitatively better sustainability data from all sectors of the economy and increasing transparency in the financial sector.¹² The measures shall be summarised hereunder.

Area for action 1: sustainability data from all sectors of the economy

Based on the basic principle that the more comparable, accurate and meaningful data¹³ is, and the better it may be integrated into any advice, balance sheets and the financial system, the lower the transaction costs will be for investors, Switzerland makes transparency one of the strategic pillars with regard to climate transition.

In this context, the Ordinance on Climate Disclosures, adopted in November 2022, will enter into force as of 1 January 2024. It is based on the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD), created in 2015 by the Financial Stability Board.¹⁴ Based thereupon, public companies, banks and insurance companies with 500 or more employees and at least CHF 20 million in total assets, or more than CHF 40 million in turnover, will have to report publicly on climate issues. Public reporting involves disclosures not only on the financial risk that a company incurs due to climate-related activities, but also on the impact of the respective company's business activities. Moreover, a company is required to describe the reduction targets it has set for its direct and indirect greenhouse gas emissions, as well as how it plans to implement them.¹⁵ The Ordinance on Climate Disclosures is part of the reporting on environmental matters in relation to the reporting obligation on non-financial matters in line with

art.964b of the Swiss Code of Obligations, which entered into force on 1 January 2022, with a transitional period for implementation until 1 January 2023.

More transparency is then expected for risks associated with the loss of biodiversity and the climate compatibility of Swiss real estate.¹⁶ Finally, in a joint effort with the Green Digital Finance Alliance based in Geneva, a classification system for green fintech applications and their need for sustainability data was published by the Green Fintech Network.¹⁷

Area for action 2: transparency in the financial sector

Financial institutions are encouraged to publish the methodology and the strategies applied to take climate risks into account and to engage in investment stewardship strategies, which shall also be made public by them. Besides regular voluntary climate tests with financial institutions conducted by the Federal Office for the Environment and the Federal Department of Finance, financial institutions are encouraged to apply the selection of indicators embedded in the Swiss Climate Scores,¹⁸ the comparability and incentive of which shall be reviewed by the end of 2023 and refined, where necessary.

Area for action 3: impact investments and green bonds

In this third area for action, the Swiss government intends to promote social impact investing in developing countries. For this purpose, a Sustainable Development Goals Impact Finance Initiative was announced in 2021, aiming to raise CHF 100 million from public and philanthropic stakeholders by 2030. Also, the financial market legislation shall be amended to promote the expansion of impact investments. In the area of green bonds, Switzerland adopted in August 2022 a framework for issuing green Confederation bonds¹⁹ and the Swiss government committed itself to regularly issue such green bonds or reopen green bonds in the future.

¹⁰ Benjamin M. Abdel-Karim and Franz Xaver Kollmer, "Wichtige Punkte: Die Grundlagen" in Benjamin M. Abdel-Karim and Franz Xaver Kollmer (eds), *Sustainable Finance* (2022), p.14; EU Taxonomy Regulation available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32020R0852&from=EN>.

¹¹ For more details on the United Nations Sustainable Developments Goals, see <https://sdgs.un.org/goals>.

¹² The Federal Council, *Sustainable Finance in Switzerland: Areas for action for a leading sustainable financial centre, 2022–2025* (December 2022), <https://www.news.admin.ch/news/message/attachments/74562.pdf>.

¹³ See also regarding the importance of data for the sustainable finance value chain: Benjamin M. Abdel-Karim and Franz Xaver Kollmer, "Money, Money, Money und Daten: Von Daten zur Systematisierung der Sustainable Finance Wertschöpfungskette" in Benjamin M. Abdel-Karim and Franz Xaver Kollmer (eds), *Sustainable Finance* (2022), p.43.

¹⁴ For more information on the TCFD, see <https://www.fsb-tcfid.org/>.

¹⁵ The Federal Council, "Federal Council brings ordinance on mandatory climate disclosures for large companies into force as of 1 January 2024" (23 November 2022), <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-91859.html>.

¹⁶ The Federal Council, *Sustainable Finance in Switzerland: Areas for action for a leading sustainable financial centre, 2022–2025* (December 2022), p.9, <https://www.news.admin.ch/news/message/attachments/74562.pdf>.

¹⁷ Also referred to as the World's First Green Fintech Taxonomy, <https://www.greendigitalfinancealliance.org/news-and-events/the-worlds-first-green-fintech-taxonomy#:~:text=The%20role%20of%20the%20Green,and%20segment%20green%20fintech%20markets>.

¹⁸ The Swiss Climate Scores provides for best practice transparency, to honour the obligations under the Paris Agreement, <https://www.sif.admin.ch/sif/en/home/swiss-climate-scores/brief-summary.html>.

¹⁹ Swiss Confederation, *Green Bond Framework* (July 2022), <https://www.efv.admin.ch/dam/efv/en/dokumente/brennpunkte/rahmenwerk.pdf.download.pdf/Beilage%2001%20Rahmenwerk%20f%C3%BCr%20gr%C3%BCne%20Eidg.%20Anleihen%20EN%20zu%20BRA%20EFD.pdf>.

Area for action 4: pricing pollution

As far as pollution pricing is concerned, Switzerland actively supports multilateral initiatives that promote the establishment of equitable global carbon pricing, particularly the newly established OECD Inclusive Forum for Carbon Mitigation Approaches.²⁰ Also, carbon offsetting in the financial sector will be supported. The Federal Department of the Environment, Transport, Energy and Communications is examining together with the Federal Department of Finance measures which could be taken in this respect.

Prevention of greenwashing in financial market

Greenwashing is generally considered as a public relations method to create a false environmentally friendly and responsible public image.²¹ In the financial sector, which is considered as crucial when it comes to meet sustainability goals due to its international size and its intermediary role,²² greenwashing occurs when e.g. a financial instrument or service is falsely promoted as having sustainable characteristics or pursuing sustainability goals. This has for a long time been deemed as a minor and rather reputational risk for corporates, but times have changed.²³ The Swiss government considered that to ensure the smooth functioning of markets, there is a need for a clear and common understanding when a financial product or service may be labelled as sustainable.²⁴

In the Swiss government's position paper, four main risks are identified in the context of greenwashing:²⁵ (i) clients, investors and insured persons being misled about the sustainability or contribution to sustainability of financial products and services;²⁶ (ii) financial institutions being exposed to legal and reputational risks, due to the missing clarity about what constitutes a sustainable investment; (iii) impairment of the smooth functioning of financial markets and the reputation of the financial centre as well as a lack of credibility as far as Switzerland's desired role as a leading financial centre; and (iv) capital flows are unduly diverted to

non-sustainable activities, which may question the international sustainability goals to which Switzerland adhered.

Financial products or services labelled as sustainable or as having sustainable characteristics shall follow at least one of the following two investment objections: (i) alignment with one or more specific sustainability goals, which should be defined using the widest possible reference framework, such as the Sustainable Development Goals in the United Nations' 2030 Agenda for Sustainable Development; and/or (ii) contribution to achieving one or more of said specific sustainability goals. Financial products and services which are merely intended to reduce ESG risks or optimise performance following entirely financial investments objections should not per se be labelled as sustainable, since these ESG risks should rather be taken into account as part of fiduciary duties.²⁷

As far as the description of the applied sustainability approaches is concerned, the information should be public, easily accessible, transparent and comparable. A service provider shall, therefore, not only describe how the alignment is achieved and measured, but also describe the management process, define the KPI and their monitoring, following the impact investment approach. In line with the active ownership approach, the selection process for the target investments, the coordination with other investors, the influencing process, the escalation procedures as well as the assessment process for the effectiveness of the engagement shall be detailed.²⁸ Accountability, through regular, efficient and appropriate reporting, following recognised indicators like the recommended Swiss Climate Scores, shall be ensured, together with a verification by an independent third party and the enforceability of the rights of clients, investors and insured persons in case of non-compliance with the transparency requirements.²⁹

For this purpose, the Swiss government has instructed the Federal Finance Department's State Secretariat for International Finance to set up a working group, including, among others, FINMA, the affected industries and the civil society. A plan and specific proposals will be submitted by the end of September 2023.

²⁰ The Inclusive Forum on Carbon Mitigation Approaches (IFCMA) is an initiative designed to help improve the global impact of emissions reduction efforts around the world through better data and information sharing, evidence-based mutual learning and inclusive multilateral dialogue, see <https://www.oecd.org/climate-change/inclusive-forum-on-carbon-mitigation-approaches/>.

²¹ Béatrice Hirzel Corte, "Greenwashing" in *Expert Focus*, EF 12/22, p.576.

²² Thomas M.J. Möllers, "Green Deal: Greenwashing, information Overload und der vergessene Good Corporate Citizen als Investor" in *Zeitschrift für das gesamte Handels- und Wirtschaftsrecht*, ZHR 185 (2021), p.883.

²³ Corte, "Greenwashing" in *Expert Focus*, EF 12/22, p.576.

²⁴ The Federal Council, "Federal Council wants to prevent greenwashing in financial market" (16 December 2022), <https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-92279.html>.

²⁵ The Federal Council, "The Federal Council's position on the prevention of greenwashing in the financial sector" (December 2022), p.1, <https://www.news.admin.ch/news/message/attachments/74580.pdf>. But see also: Damian A. Fischer, "Greenwashing-Bekämpfung am Point of Sale" in *Gesellschafts- und Kapitalmarktrecht*, GesKR (2022), p.257.

²⁶ It should nevertheless be noted that even without specific greenwashing provisions, there are general legal requirements which have to be complied with, intended to prevent the deception and misleading of clients, e.g. in the Federal Act against Unfair Competition or the Collective Investment Schemes Act.

²⁷ Climate-related risks (such as regulatory, reputational or liability risks) have to be taken into account as part of the risk management within a regular banking relationship; see also Tamara Teves, Romina Lauper and Martin Eckert, "Nachhaltigkeit und Finanzmarktrecht" in *Gesellschafts- und Kapitalmarktrecht*, GesKR 2020, p.421.

²⁸ The Federal Council, "The Federal Council's position on the prevention of greenwashing in the financial sector" (December 2022), p.3, <https://www.news.admin.ch/news/message/attachments/74580.pdf>.

²⁹ The Federal Council, "The Federal Council's position on the prevention of greenwashing in the financial sector" (December 2022), p.4, <https://www.news.admin.ch/news/message/attachments/74580.pdf>.

Outlook and concluding observations

Switzerland sets out an ambitious agenda to strengthen the Swiss financial centre's position in the area of sustainable finance. Concurrently, in order to avoid misleading labelling, but also underlining the credibility

of the sustainability strategy, greenwashing shall be combatted. It thereby follows international trends and takes into account the investors' needs as well as the political expectations. It remains to be seen whether the related administrative burden may be contained in a reasonable way.