SFC position on the Corporate Sustainability Reporting Directive (CSRD) proposal

A proportionate approach for financial institutions' sustainability reporting

About the Swiss Finance Council (SFC)

The Swiss Finance Council (SFC) engages in dialogue around policy developments in finance at a European and international level. It represents the interests of its Members, Credit Suisse and UBS, who are internationally active Swiss financial institutions and provides a platform to share their experience, expertise and knowledge. We firmly support and advocate for a strong and ambitious response to climate change as demonstrated by our members' commitment to transparency through TCFD aligned disclosures and working with peers to embed sustainability into their business strategy and practice through the Principles for Responsible Banking and Principles for Responsible Investment. SFC Members have committed to align operational and attributable emissions from their portfolios with pathways to net-zero by 2050[1]. More broadly, SFC members are also committed to directing financial flows and supporting clients to invest according to their preferences in a way that also helps achieve the UN Sustainable Development Goals.

Context

Regulatory frameworks for sustainable finance have developed at a great pace across the globe over the last few years, and the EU is by far at the forefront of the requirements globally. Over the past few years, with the Non-Financial Reporting Directive (NFRD), the EU Taxonomy, the Sustainable Finance Disclosure Regulation (SFDR) and more recently with the Corporate Sustainability Reporting Directive (CSRD) proposal, the EU has achieved very important milestones which will pave the way for a greener and more sustainable economy. However, to achieve climate neutrality and a more sustainable world more broadly, global coordination is key: as noted in the recent IPSF report on the *"State and trends of ESG disclosure policy measures"*, 18 jurisdictions, including China, the US, the UK, Japan, India, Singapore and Hong Kong SAR, have some sort of ESG disclosure requirements in place[2].

We hope that the recently established International Sustainability Standards Board (ISSB), which will develop a comprehensive global baseline of sustainability-related disclosure standards, will create a solid and comparable global common ground on which jurisdictions will build upon. The EU has the unprecedented opportunity to provide guidance and global leadership, but to do that it is of utmost importance that while it develops its framework at its preferred pace, it does not prevent other jurisdictions to do the same, under the auspices of the newly created ISSB. As highlighted by Commissioner McGuinness during the EU side event on disclosures at COP26 on 4 November 2021, "*Global processes should be flexible enough to accommodate the need for different countries and jurisdictions to go further according to their own rules and priorities. So two-way cooperation between global and regional standard-setters is critical. We need to ensure coherence between frameworks*"[3].

Against this backdrop of a widely recognised need for regulatory collaboration and coordination in sustainability reporting, the development of requirements which could lead to any forms of "extra-

[1] https://unfccc.int/news/new-financial-alliance-for-net-zero-emissions-launches

[2] https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/211104-ipsf-esg-disclosure-report_en.pdf

[3] https://ec.europa.eu/commission/commissioners/2019-2024/mcguinness/announcements/remarks-and-eu-side-event-disclosures-cop-26-eu-sustainability-reporting-standards-and-future_en

territorial" application should be avoided. However, the CSRD proposal includes an extraterritorial feature which might have unintended consequences, for both the EU and its policy objectives (climate neutrality by 2050 and the Capital Markets Union) and non-EU companies wishing to support the EU economy. According to the CSRD proposal, multinational companies domiciled in the EU and outside the EU – where the latter have any type of security listed on EU regulated markets (including debt securities) – would need to report sustainability information at consolidated level as per the CSRD requirements for their entire group operations, including operations in third countries that will not be subject to the same ESG disclosure requirements as the operations performed within the Union. Financial institutions will be particularly affected as they issue securities in many different jurisdictions to reap the benefits of currency and country diversification.

We have reasons to believe that, were such a requirement to be maintained, it would provide a strong disincentive to companies whose head offices are located outside the Union, to continue to deepen EU capital markets, with potential second-order effects on the EU's ability to take the Capital Markets Union (CMU) to the next level, which is now more urgent than ever. Global financial institutions might decide to move the issuance of debt securities from the EU to other jurisdictions in order to avoid disproportionate CSRD reporting requirements at group level. This situation would harm the CMU objective of stronger and deeper EU capital markets and make global banks less resilient, as an important driver of risk diversification (currency/country) will no longer be available to cushion the impact stemming from global shocks.

In addition, we are concerned that if other jurisdictions follow the same path and design their frameworks with "extraterritorial scope of application", this could lead to a fragmentation of sustainability reporting standards along national lines and the related complexity for companies with a global footprint to report under multiple frameworks. This would result in international companies, including those based in the EU, being obliged to produce several consolidated sustainability reports according to different sets of rules: non-EU entities with securities listed on EU exchanges will need to report under EU rules but also under foreign rules and the same will apply to EU entities that operate outside the Union.

Such an intertwined regulatory framework would represent a significant departure from existing reporting requirements (financial reporting as well as Capital Requirements Regulations' Pillar 3 reporting for banks) and a huge and disproportionate burden on financial institutions, which would ultimately create confusion for investors if they see different sustainability reports produced by the same company under different frameworks, potentially harming the overall decarbonisation efforts.

Lastly, this extraterritorial application of the CSRD seems to be in contradiction with the support expressed by Commissioner Mairead McGuinness at COP 26 for the IFRS Foundation initiative to develop a common global baseline on sustainability reporting and the related commitment to ensure that EU standards are closely aligned with global sustainability reporting standards[4].

Recommendations

We propose that the scope of the CSRD should apply to third country firms with shares listed in the EU, while it should not apply to third country firms with other types of securities (including debt securities) listed in the EU. Our proposal would ensure a more proportionate approach to sustainability reporting and limit unintended negative extraterritorial impacts of the CSRD. On the one hand, EU subsidiaries of non-EU companies would report their activities according to the EU standards at the highest EU consolidated level. On the other hand, the parent company based in a third country

[4]https://ec.europa.eu/commission/commissioners/2019-2024/mcguinness/announcements/remarks-and-eu-side-event-disclosures-cop-26-eu-sustainability-reporting-standards-and-future_en

would be allowed to make a single consolidated sustainability report according to the international standards developed by the International Sustainability Standards Board (ISSB) or according to its home jurisdiction's standards that ensure compliance with the ISSB standards. This principle already applies in the context of Pillar III disclosures under the Capital Requirements Regulation (CRR), which are made at the consolidated level by non-EU financial institutions in their home jurisdiction according to the local framework. Applying EU sustainability reporting rules at global level to non-EU financial institutions that have only a relatively small percentage of their activities in the EU would be disproportionate.

We think it is important to introduce such an adjustment to the CSRD application scope, which should support global financial institutions which need global funding to manage and diversify their balance sheets. Global financial institutions have a diversified balance sheet which requires diversified financing (primarily in the form of debt instruments). Therefore, if the entire pool of "listed securities" is considered to define the scope of CSRD application to non-EU financial institutions, it is more likely that global non-EU financial institutions will be subject to reporting requirements at group level under both EU standards and their home jurisdiction standards (and possibly the standards of other jurisdictions which may retaliate to the EU approach by developing reporting requirements with similar extraterritorial reach). This situation would inevitably create uncertainty and confuse investors which would need to grapple with different reporting requirements / standards for the same issuer. Moreover, our proposal would mitigate the possible negative impacts of the CSRD on the CMU, as global non-EU financial institutions will continue to focus on EU markets to execute their funding plans and would not move their issuances of debt securities from the EU to other jurisdictions in order to avoid CSRD reporting requirements at group level. Similarly, our proposal would help the CSRD to align with the European Commission's objective of making it more attractive for companies to list in the EU[5].

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[5]https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13238-Listing-Act-making-public-capital-markets-more-attractive-for-EU-companies-and-facilitating-access-to-capital-for-SMEs/public-consultation_en