July 2023

Newsletter

ESG Update

New Liability Risks from Corporate Sustainability Regulation in Switzerland:

Recent regulation related to corporate sustainability and green claims is significantly impacting Swiss corporate as well as directors & officers (D&O) liability. This newsletter reports on some major findings of a study published this week about (i) the new risks, (ii) preventive measures and (iii) the role of the rule of law in making sustainability regulation effective.

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Swiss corporate and D&O liability in a changing regulatory environment

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The risk of companies being targeted by sustainability-related legal actions is increasing on a global scale and in Switzerland (cf. Walder Wyss ESG Update of 7 July 2023).

Against this background, new regulation on corporate sustainability and green claims is changing the regulatory environment of Swiss corporate and D&O liability:

- the general **Swiss corporate sustainability reporting obligation** of larger listed or FINMA supervised companies, effective since 1 January 2023, still following the former EU-Non-Financial Reporting Directive (NFRD). Alignment with the EU-Corporate Sustainability Reporting Directive (CSRD) is to be expected (cf. Walder Wyss ESG Update of 15 December 2022);
- the **Climate Reporting Ordinance**, specifying the mandatory sustainability reporting on climate issues, relying on the TCFD recommendations on a comply or explain basis, effective as of 1 January 2024;
- Obligations of **transparency and due diligence related to conflict minerals and metals as well as child labour**, effective since 1 January 2023, as specified by a respective **Ordinance of the Federal Council**;
- Obligation of **raw material companies to report on payments to governmental entities**, effective since 1 January 2022;
- **New Swiss regulation against greenwashing**, proposal announced for Q3 of 2023 by the Federal Council in its Position Paper dated 16 December 2022, declaring, among other things, that labelling simple ESG-risk avoidance as "sustainable" is deemed greenwashing.
  It will be interesting to see to which extent the Swiss proposal will follow the EU Green Claims Directive proposed in March 2023;
- Financial Market Supervision:
  - Contribution to sustainable development as one of **FINMA's strategic targets in financial markets supervision 2021–2024**;
  - **Focus of the Swiss National Bank on sustainability-related risks to financial and price stability** according to a report of the Federal Council of 24 February 2022;
  - **FINMA Guidance 05/2021 on preventing and combatting greenwashing by collective investment schemes** dated 3 November 2021;
  - Amendments to the **FINMA Circulars 2016/01-02 on the disclosure of climate risks and their management by banks and insurance companies**, effective since 31 December 2021;
  - **FINMA Guidance 03/2022 on the implementation of the disclosure of climate risks** by banks and insurance companies dated 29 November 2022;
  - **FINMA Guidance 01/2023 on developments in the field of climate risk management** dated 24 January 2023.

The following sections report on some

major findings of a new study published this week about the consequences of the regulatory changes for corporate and D&O liability in Switzerland.[1]

Corporate communication: a liability trigger

The trend towards corporate social responsibility and sustainability tends to establish a "**responsibility for everything**" of companies and the management.

For such universal and indeterminate responsibility, **corporate reporting and communication turn out to be a main regulatory leverage point**. One reason for this is that establishing evidence of breaches and causality turns out to be easier for deviations from communication standards and expectations raised than for complex multi-causal environmental damages. Respective conclusions drawn from a case study on the derivative suites following the Deepwater Horizon oil spill against BP as well as its directors and managers, the last of which was settled in 2021, also hold for Switzerland.

Therefore, the following sections focus on liability for sustainability-related corporate communication. However, further legal grounds for sustainability-related civil liability have been invoked such as the right of personality, the statutory liability of real estate owners or environmental law.

No general Swiss liability for negligent corporate communication – Liability for systematic greenwashing

The study concludes that under Swiss law, there is **no general liability for negligent corporate communication**. This includes breaches of Swiss sustainability reporting obligations or financial market regulation mentioned above as well as sustainability standards such as the UN Guiding Principles, OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, the reporting standards of GRI or the TCFD recommendations. The reason is that the respective provisions and standards do not qualify as "protective provisions" ("Schutznormen") under Swiss tort and corporate law. Under certain conditions, at least theoretically, civil liability claims for public statements are possible in the case of criminal intent, based on a criminal law provision against wrongful public statements of companies.

This result of over 100 years of evolution of civil law appears to be in line with the possible function and functional constraints of civil liability in general. Still, as after any crisis, politics keeps **claiming for enhanced statutory civil liability**. The study adds for consideration that, in practice, this remedy inherited from roman and common law has rarely proven effective in pursuing any of the purposes intended by lawmakers in legal history and proposes more efficacious mechanisms of enforcement.

However, depending on the circumstances, **sustainability communication amounting to systematic anti-competitive behaviour**, e.g. in the case of a large-scale greenwashing scheme causing investors to lose money, may trigger liability claims against corporations and D&O based on the Swiss Unfair Competition Act (UCA), even for negligence.

UCA liability is and must be limited to severe anti-competitive behaviour and must not lead to a liability for any incorrect statement in a public announcement or report. So far, no specific case law exists. Nevertheless, with current endeavours of NGOs and the Swiss State Secretariat for Economic Affairs (SECO) to promote criminal prosecution of false green claims based on the UCA, related civil actions against companies are put into the realm of the possible.

New legal necessity of integrated corporate communication

In today's regulatory environment, **integrated corporate communication is key** also from a legal standpoint. The range of free and mandatory corporate communication to be aligned is ever growing, to think of sustainability reporting, financial reporting, prospectuses, ad hoc announcements of listed companies, advertisement for financial products, general corporate communication and many more.

Discrepancies between various corporate communications of a same company may prompt **auditors' liability, prospectus liability, sanctioning by stock exchanges and, in the case of financial institutions, FINMA intervention.**

New legal requirement to implement and run a sustainability management system

The new Ordinance of the Federal Council on Transparency and Due Diligence Related to Conflict Minerals and Metals as well as Child Labour (see above) breaks with a taboo in the history of corporate law. It **makes the implementation of a supply chain management system an obligation subject to civil and criminal liability**.

Along the way, the Ordinance **redefines the corporate duty of care** as implementing a specific management system, which indicates a progressing juridification of corporate management.

The legislative material states that unlike said Ordinance, the obligation to report on due diligence under general mandatory sustainability reporting does not imply implementing a management system. Still, the Ordinance has breached in a dam, apart from the fact that the **line**

1 Daniel Dedeyan, Haftung für fehlerhafte Unternehmenskommunikation: Neue Risiken im Zuge der Nachhaltigkeitsregulierung («Liability for corporate communication: New risks from corporate sustainability regulation»), in: Peter R. Isler / Rolf Sethe (eds.), Managerhaftung bei Unternehmensrisiken und -zusammenbrüchen, 11. Zürcher Tagung zur Verantwortlichkeit im Unternehmensrecht 2022, Zurich 2023, p. 67–102, available here.
Daniel Dedeyan is also the author of a book on the regulation of corporate communication in corporate and financial market law (Regulierung der Unternehmenskommunikation, Zurich/Baden-Baden 2015).

between reporting obligations and duties of conduct generally proves to be thin.

Sustainability management – a new core responsibility of the board of directors and the management board

Corporate sustainability reporting and management has become **a direct D&O legal responsibility**. The analysis shows that directors and officers may be sued by the corporation, shareholders or at least (theoretically) creditors for breaches of fiduciary duties related to a lack of supervision and sound internal control systems.

This also means that only severe organisational failure and misconduct and **not every incorrect statement in a sustainability report triggers D&O liability**. However, the "business judgment rule" generally protecting well informed and conflict free business decisions fails to protect directors and officers from liability for corporate communication. To prevent liability, group-wide alignment of corporate communication and sustainability management at the top of the organisation is a must.

Damage claims for stock market losses

The study further shows that for reasons ingrained in Swiss case law, sustainability-related D&O liability claims by shareholders or creditors are quite unlikely in bankruptcy events.

By contrast, **D&O liability is more likely outside of bankruptcy for organisational failure in sustainability reporting as well as for large-scale anti-competitive greenwashing** brought up by shareholders who claim for compensation of **losses on the stock price** due to deficient corporate communication. In and outside of bankruptcy, creditors may sue directors and officers for **fraudulent green claims in the context of financing arrangements.**

Damage claims for stock market losses are supported by case law of the Swiss Federal Supreme Court (FSC) **lowering the burden of proof for the causality of information in respect of the stock price and the investor decision** (FSC Decision 132 III 715, related to prospectus liability, stating a "natural assumption" of causality but "no fraud on the market" like reversed burden of proof). Nevertheless, the procedural hurdles for shareholder suits are high in Switzerland.

New factors increasing the risk of liability claims in Switzerland

Swiss liability law is not known as being particularly plaintiff-friendly. Procedural thresholds for liability claims are sometimes prohibitively high (no class actions, heavy burdens proof). However, **new factors potentially increase the liability risks also in Switzerland**. To list just a few:

- ever rising risk and size of potential environmental damages and stock price losses;
- unfair competition liability claims, even triggered by negligent communication and becoming more likely with more specific sustainability reporting standards as well as green claims regulation;
- increasing challenges in terms of measurability and data processing related to sustainability claims which turn out not only to weigh on plaintiffs but sometimes even more on defendants;
- growing portfolio restrictions of institutional investors reducing the "exit" option and pushing them towards "voice" and legal action.

Preventive measures and the role of the rule of law

In addition to the usual preventive measures such as sound risk-management and careful documentation, the changing regulatory environment sets new demands:

- Sustainability management and corporate communication should be integrated at the top level of the organisation and linked to the risk management system as well as the internal control system.
- External audit and certification are increasing in importance in providing comfort, sending a positive signal to the market and mitigating liability, at least to some extent.
- Integrated corporate communication and regular, consistent as well as transparent market communication have become key also from a legal perspective.
- Announced targets and raised expectations must be attainable.
- Quality culture should prevail over box ticking.

Given the complexity and dynamics of the field, the current regulatory wave, unlike the ones in the past, is not likely to be worked off by running through checklists only.

Finally, as to the law, it is time to recognize its task to channel sustainability regulation from an unmanageable "responsibility for everything" towards a realization of its goals.

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