

C L I F F O R D
C H A N C E



LUXEMBOURG PERSPECTIVES SERIES | AUTUMN | EPISODE 3

ESG: FOCUS ON BANKS

THE PLAN

- The EU Sustainable Finance Action Plan launch is part of a wider drive to meet EU climate and energy targets.
- In 2018, the Commission adopted its first action plan on financing sustainable growth. Based on that plan, the EU has put in place the three building blocks for a sustainable financial framework

EU Taxonomy

Taxonomy: The Taxonomy Regulation aims to provide a robust, science-based classification system, allowing non-financial and financial companies to share a common definition of sustainability and thereby providing protection against Greenwashing.

Mandatory disclosure regime for both non-financial and financial companies

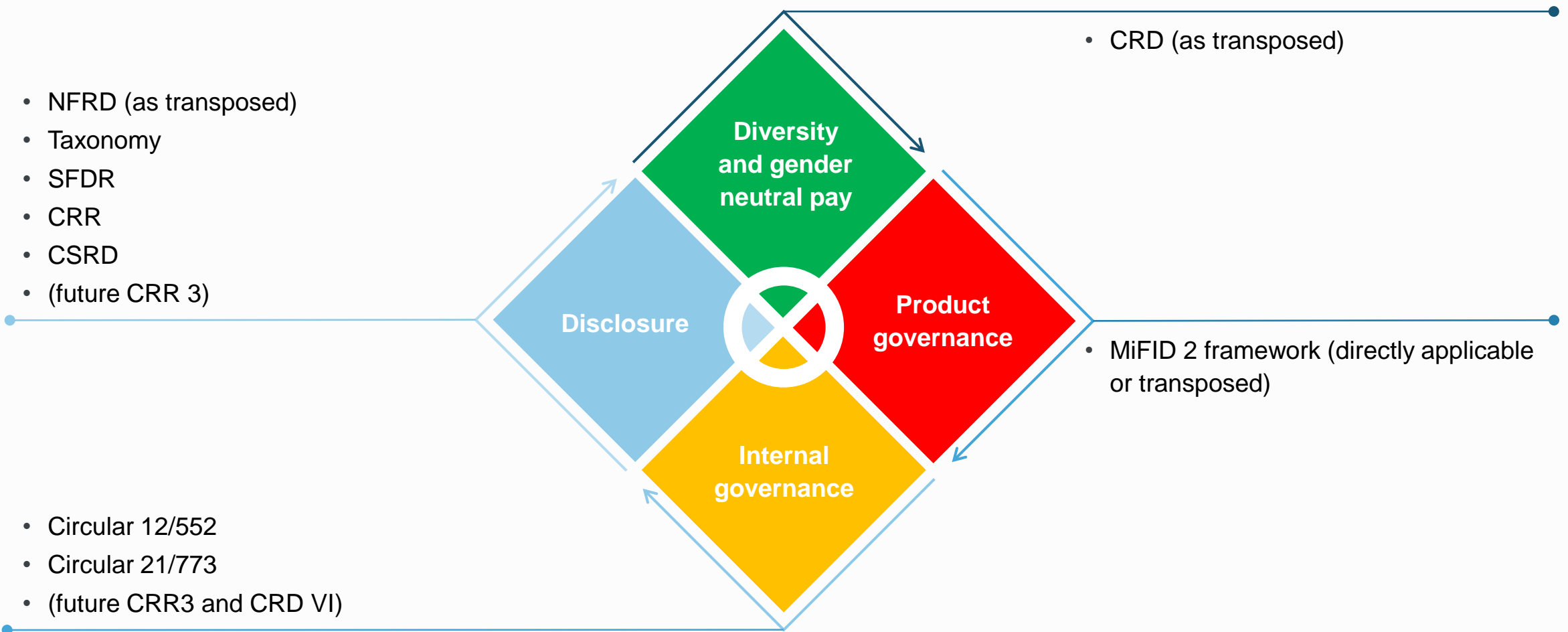
Disclosure: Providing investors with information to make informed sustainable investment decisions.

Investment tools, including benchmarks, standards and labels

Investment tools: These make it easier for financial market participants to align their investment strategies with the EU's climate and environmental goals. They provide greater transparency to market participants.

Source: Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions - Strategy for Financing the Transition to a Sustainable Economy - 6.7.2021

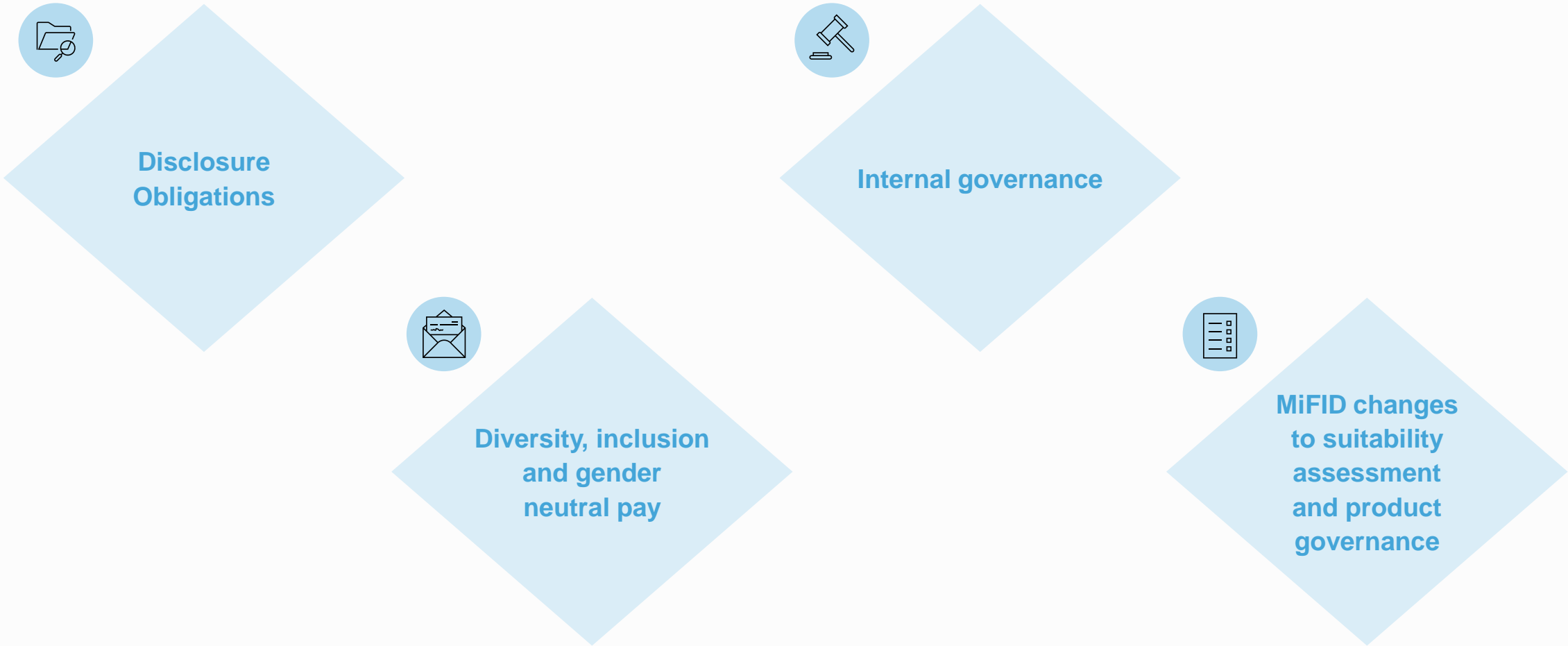
THE LAW



OVERVIEW OF APPLICABLE LEGISLATION

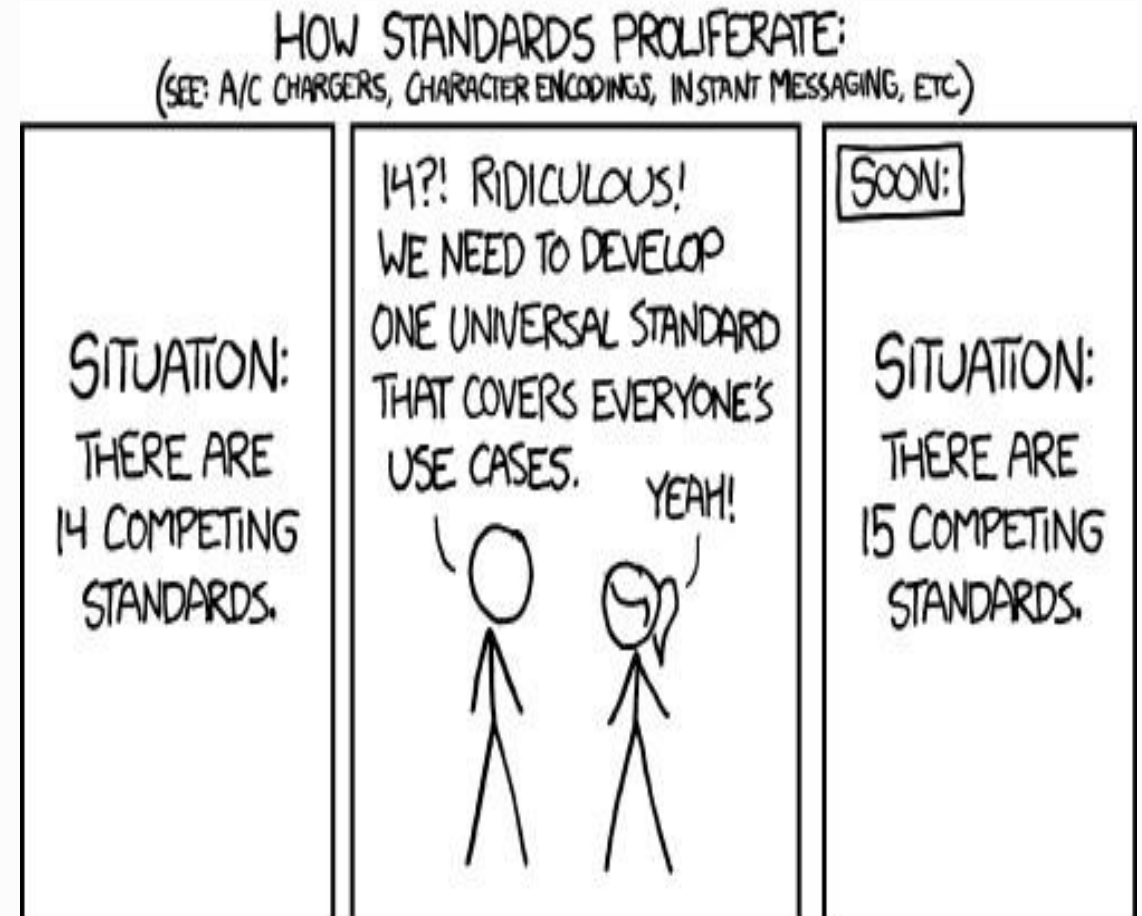
NFRD	CSRD	TAXONOMY	SFDR	Internal Governance	MiFID Framework
<p>Who: primarily large public-interest entities with more than 500 employees. Public-interest entities include credit institutions.</p> <p>What:</p> <ul style="list-style-type: none">Environmental mattersSocial matters and treatment of employeesRespect of human rightsAnti-corruption and briberyDiversity on company boards (age, gender, educational and professional background) <p>Where: in management report or separate report</p> <p>When: in force</p>	<p>Who:</p> <ul style="list-style-type: none">All EU large undertakingsEU SMEs with securities listed on an EU regulated marketNon-EU companies with substantial activity in the EU (with a turnover over €150 million euro in the EU) will also have to comply <p>What: additional disclosure requirements (compared to NFRD):</p> <ul style="list-style-type: none">Company's strategy and targetsRole of the board and managementPrinciple adverse impacts connected to the company, its value chain and intangiblesinformation about the existence of incentive schemes linked to sustainability matters which are offered to members of the administrative, management and supervisory bodies <p>Where: in management report</p> <p>When:</p> <p>On 10 November 2022 the CSRD was adopted by the EU Parliament. The Council is expected to adopt the proposal on 28 November, after which it will be signed and published in the EU Official Journal. The directive will enter into force 20 days after publication. The rules will start applying between 2024 and 2028:</p> <ul style="list-style-type: none">From 1 January 2024 for large public-interest companies (with over 500 employees) already subject to the non-financial reporting directive, with reports due in 2025;From 1 January 2025 for large companies that are not presently subject to the non-financial reporting directive (with more than 250 employees and/or €40 million in turnover and/or €20 million in total assets), with reports due in 2026;From 1 January 2026 for listed SMEs and other undertakings, with reports due in 2027. SMEs can opt-out until 2028.	<p>(ARTICLE 8)</p> <p>Who: Entities subject to the NFRD/CSRD</p> <p>What: financial undertakings to disclose:</p> <p>From 1 January 2022 until 31 December 2023, financial undertakings shall only disclose, among others:</p> <ul style="list-style-type: none">the proportion in their total assets of exposures to Taxonomy non-eligible and Taxonomy-eligible economic activities;Credit institutions shall also disclose the proportion of their trading portfolio and on demand inter-bank loans in their total assets. <p>The key performance indicators of financial undertakings, including any accompanying information to be disclosed pursuant to Annexes III, V, VII, IX, XI to this Regulation, shall be disclosed from 1 January 2024. This would include the green asset ratio (GAR). The GAR shall show the proportion of the of credit institution's assets financing and invested in taxonomy-aligned economic activities as a proportion of total covered assets.</p> <p>Sections 1.2.3 (KPIs on services other than lending – Fees and Commissions (F&C KPI)) and 1.2.4 (Other disclosures in the GAR: GAR for the trading portfolio) of Annex V shall apply from 1 January 2026.</p> <p>Where: in quarterly/annual reports or dedicated CSR report</p> <p>When: see above</p> <p>(ARTICLES 5-7)</p> <p>Who: Financial market participants under SFDR</p> <p>What: requires disclosure of alignment with the environmental sustainability criteria set out in the Taxonomy Regulation</p> <p>Where: Website/pre-contractual/periodic</p> <p>When: RTS expected to apply from 1 January 2023</p>	<p>Who: Financial market participants (e.g. credit institution providing portfolio management) and financial advisers (e.g. a credit institution providing investment advice)</p> <p>What: harmonised rules on disclosure with regard to:</p> <ul style="list-style-type: none">integration of sustainability risks and consideration of adverse sustainability impacts in processesprovision of sustainability-related information on financial products(see slides for more details) <p>Where: website/pre-contractual/periodic</p> <p>When: in force</p>	<p>Circular 12/552</p> <p>Who: This circular applies to all credit institutions and professionals performing lending operations.</p> <p>What: governance rules, inter alia, integration of ESG and diversity in organisational requirements.</p> <p>When: in force</p> <p>Circular 21/773</p> <p>Who: This circular applies to all credit institutions designated as Less Significant Institutions under the Single Supervisory Mechanism and to all branches of non-EU credit institutions.</p> <p>What: climate-related and environmental risks should be assessed as part of the business plan and risk appetite. Institutions are expected to identify and quantify climate-related and environmental risks within their overall process of ensuring capital and liquidity adequacy. The risk identification shall be documented in writing by the Institutions. A high-level summary of this risk identification shall be provided in the ICAAP and ILAAP reports issued each year.</p>	<p>Commission Delegated Regulation 2021/1253</p> <p>Who: credit institutions when providing investment services, with particular rules for investment advisory and discretionary portfolio management services</p> <p>What (among others):</p> <ul style="list-style-type: none">(investment advisory and portfolio management) required to obtain specific information on their clients' preferences regarding sustainable investments and meet such preferences, while also meeting their other investment objectives and taking into account their financial situation and knowledge and experience.Consideration of sustainability related risks as part of general organisational requirement/risk management; <p>When: from 2 August 2022 onwards</p> <p>Commission Delegated Directive (EU) 2021/1269 of 21 April 2021 amending Delegated Directive 2017/593</p> <p>Who: Investment firms (including credit institutions) manufacturing and distributing financial instruments</p> <p>What: Sustainability objectives must be integrated into target market assessments performed by product manufacturers</p> <p>Product distributors must ensure that investment products they offer, recommend or sell are (and remain) compliant with sustainability objectives of the relevant target market</p> <p>When: transposition into national rules and application as of 22 November 2022</p> <p>Luxembourg transposition: Grand-Ducal Regulation of 27 July 2022</p>
<p>CRR</p> <p>Who: certain large credit institutions (EU commission proposal to extend to all institutions)</p> <p>What: information on ESG risks</p> <p>Where: series of tables and templates to be completed</p> <p>When: from June 2022 (annually for the first year, then biannually)</p>			<p>CRD (as amended)</p> <p>Directive (EU) 2019/878</p> <p>Who: among others – credit institutions</p> <p>What: among others – setting rules on gender neutral remuneration policies</p> <p>When: in force and applicable</p> <p>Luxembourg transposition: Law of 20 May 2021, amending the law of 5 April 1993</p>		

HOT TOPICS



DISCLOSURE OBLIGATIONS

- Disclosure obligations are a core part of ESG.
- Rules on disclosure cover a broad scope and are complex.
- They apply in relation to both the business itself and products.
- Not all may be applicable to your business but scoping the ones that apply and the ones that don't is crucial.



DIVERSITY, INCLUSION AND GENDER NEUTRAL PAY

Gender neutral pay

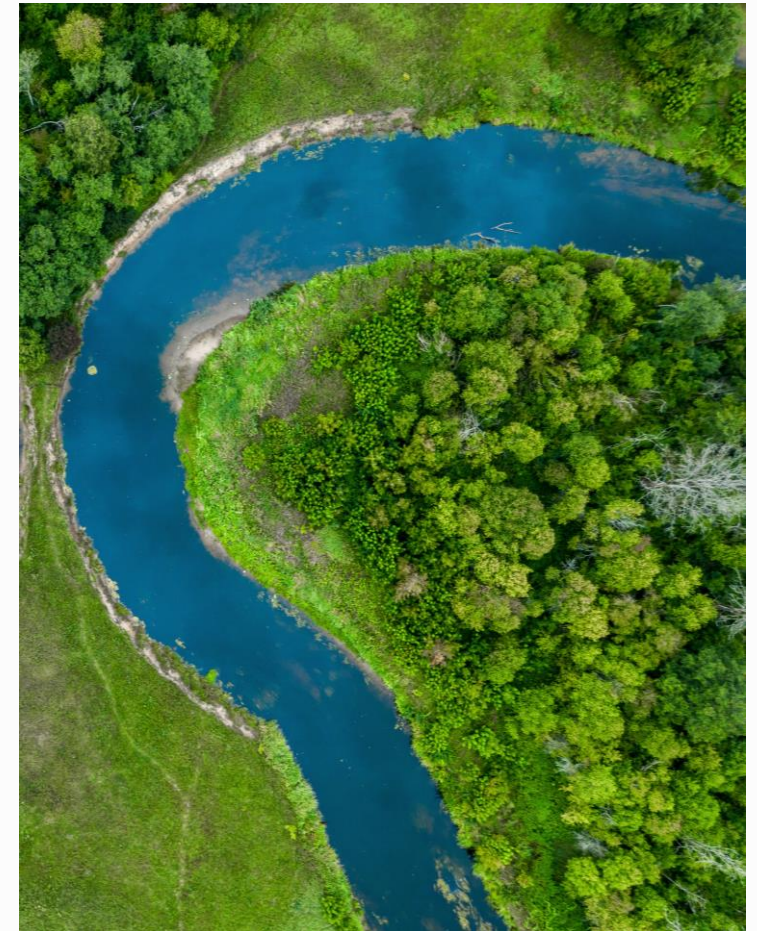
- The remuneration policies should be compliant with a set of principles, including among such principles, the fact that the remuneration policy is a gender neutral remuneration policy (article 38-5 of the law of 5 April 1993 of the financial sector, as amended);
- The CSSF shall collect the information provided by CRR institutions on the gender pay gap and shall use it to benchmark remuneration trends and practices.

Diversity

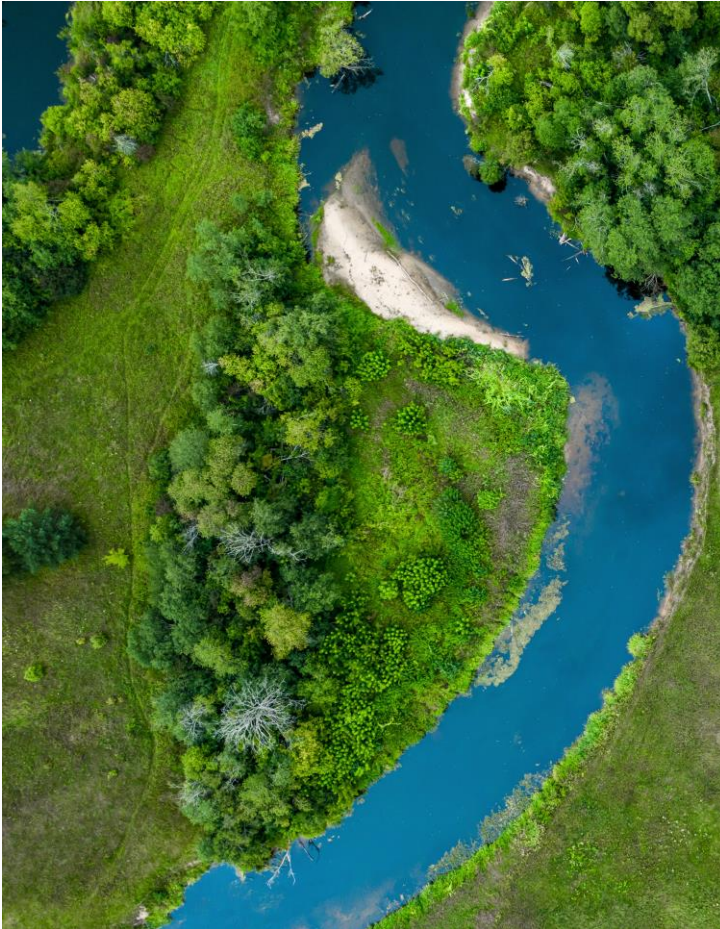
- The CSSF Circular 12/552 on central administration, internal governance and risk management is also relevant as it is one of the core pieces of local legislation on internal governance; among others it embeds ESG and diversity principles in governance.

INTERNAL GOVERNANCE

- Sustainability related risks / climate-related and environmental risks are now relevant for carrying out of business;
- Circular CSSF 21/773 imposes rules on the integration of climate-related and environmental risks in the business model and policies;
- Future proposed changes to CRR3 and CRD VI would further embed ESG risks into the processes, strategies and business of banks.



MIFID – SUITABILITY AND PRODUCT GOVERNANCE



- A scoping exercise should be performed in order to assess which MiFID rules would ultimately apply to the business (e.g. if suitability assessment rules are relevant for business);
- MiFID changes:
 - (from August 2022) the integration of sustainability preferences into suitability assessments (listening to clients) and
 - (from November 2022) the integration of sustainability objectives into product governance (building for clients).

QUESTIONS?



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