# (Non-) Financial Reporting 2.0 for banks and insurers

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## Key takeaways

- **In December 2023, FINMA announced its new circular on nature-related financial risks. FINMA, thus, is looking to specify the risk management requirements for financial institutions regarding climate and other nature-related financial risks.**
- **This initiative is well established in ongoing Swiss legislation on climate change.**
- **As of 1 January 2024, large Swiss companies of all sectors (not just banks or insurers) must implement new mandatory climate disclosures. These disclosures shall comprise, in particular: i) quantitative CO2 targets and, where necessary, targets for other greenhouse gases; ii) the disclosure of all greenhouse gas emissions; iii) quantitative information, as well as the disclosure of the main baseline assumptions for comparison purposes and for the methods and standards used.**

## Introduction

Numbers are vital for so many business functions. This view is evident to anyone active in financial accounting and reporting. Financial reports are primarily intended to present the economic situation of the company so that third parties can form a reliable opinion. Since 2022, certain companies of public interest are required to report on non-financial matters, pursuant to Art. 964a - 964c of the Swiss Code of Obligations (CO). The purpose of this non-financial reporting is to provide accountability on environmental, social, and employee matters; respect for human rights; and the fight against corruption. These provisions come together with Art. 964j - 964l CO concerning due diligence obligations and transparency regarding minerals and metals from conflict areas and child labour.

For financial institutions, the Swiss Financial Market Supervisory Authority (FINMA), taking up the trend in international regulations, started to issue specific rules on the reporting of climate risks in 2021. FINMA announced their new circular on nature-related financial risks in December 2024. Reporting on climate and nature-related financial risks will include both qualitative and quantitative input. The vital importance of numbers will continue to rule. FINMA, thus, seeks to specify the risk management requirements for financial institutions where climate and other nature-related financial risks are relevant.

## Disclosures of climate and nature-related financial risks

### Background: Climate legislation in Switzerland

Under the Paris Agreement, Switzerland implemented its obligations by means of the CO2 Act of 23 December 2011, which came into force on 1 January 2013 (replacing an earlier version of 1999 responding to the Kyoto Protocol). This CO2 Act includes a wide range of specific measures to achieve the reduction targets for greenhouse gas (GHG) emissions. On 18 June 2023, the Swiss voters approved the Climate and Innovation Act (KIG): The KIG codifies a net zero target by 2050 as a binding obligation for Switzerland. In particular, the Confederation shall ensure that the Swiss financial centre effectively contributes to low-emission development that is resilient to climate change. The government shall take measures to reduce the climate impact of national and international financial flows.

The Swiss Parliament is currently debating another revision of the CO2 Act. This draft act includes a mandate for FINMA to review the climate-related financial risks for supervised institutions on a regular basis. FINMA shall regularly publish a report on the results.

### Regulatory activities by FINMA

In May 2021, FINMA included transparency obligations in two disclosure circulars regarding climate-related financial risks for large banks and insurers: FINMA circulars 2016/1 for banks and 2016/2 for insurers, respectively. These two circulars require large banks and insurance companies to disclose information in their annual or regulatory reports on their management of climate-related financial risks. In particular, not only must these reports provide information on their risk management structures and processes to identify, evaluate, and manage climate-related financial risks, but also they must include quantitative information (targets and key data) on climate-related financial risks along with the methodology used.

As of 1 January 2024, numerous banks and insurance companies in Switzerland must implement the new ordinance on mandatory climate disclosures for large companies, which is based on the general Art. 964a CO and applies to all industries. According to art. 3 of the ordinance, climate disclosures shall comprise, in particular: i) quantitative CO2 targets and, where necessary, targets for other GHG; ii) the disclosure of all GHG emissions; iii) quantitative information, as well as the disclosure of the main baseline assumptions for comparison purposes and for the methods and standards used.

By its own statement, FINMA is neither responsible for monitoring compliance nor enforcing the civil law obligations of supervised entities. FINMA considers, however, systematic compliance with the relevant obligations under civil law when assessing a supervised entity's proper business conduct (Gewähr für eine ordentliche Geschäftsführung).

These civil law requirements are in some cases more extensive than the requirements contained in the circulars referred to above (e.g., the obligation to disclose transition plans). Taking up recommendations of the Network for Greening the Financial System (NGFS), of which FINMA is a member, FINMA is preparing a new circular on environmental risk management. Environmental risks not only cover climate risks but also biodiversity loss. Climate change is a major driver of biodiversity erosion, and loss of biodiversity also accelerates climate change processes as the capacity of degraded ecosystems to assimilate and store CO2 tends to decrease (Unesco). A major impact of climate change on biodiversity is the increase in the intensity and frequency of fires, storms, or periods of drought (Royal Society).

To be able to fulfil its upcoming new reporting obligation on climate risks, under the revised CO2 Act, FINMA is building up a database. Data will be sourced for the first time in 2024 and only from larger institutions (supervisory categories 1 to 3).

**The importance of numbers for climate financial risks disclosures**

Like traditional financial accounts, climate financial risk disclosures are heavily dependent on numbers. Climate-related metrics are used to assess and manage both climate-related risks and opportunities.

Calculating the carbon dioxide (CO2) impact of a bank's financing activities involves assessing the emissions associated with the projects and entities the bank finances. This process is part of measuring the carbon footprint of the bank's lending and investment portfolio. The bank will have to categorize financed activities into sectors (e.g., energy, transportation, industry) and identify the types of projects involved (e.g., fossil fuel extraction, renewable energy, construction). Then, it must differentiate between direct emissions (Scope 1), indirect emissions from purchased energy (Scope 2), and other indirect emissions (Scope 3) associated with the financed activities. The bank must obtain financial data related to its lending and investment portfolio as well as its industry-specific emission factors to estimate the CO2 emissions associated with each financed activity. Important to note is that methodologies may evolve, and collaborating with experts in environmental accounting and sustainability can enhance both the accuracy and the credibility of the calculations.

The Task Force on Climate-related Financial Disclosures (TCFD) recommends that organizations disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material. The TCFD defines effective climate-related metrics as those that are: i) decision-useful; ii) clear and understandable; iii) reliable, verifiable, and objective; and iv) consistent over time. The TCFD has identified seven categories of metrics that all organizations should disclose to facilitate comparisons within and across industries:

1. Emissions: Scope 1, Scope 2, and, if appropriate, Scope 3 GHG emissions, and the related risks.

2. Physical risks: Risks associated with climate-related events such as extreme weather conditions, sea-level rise, and wildfires.
3. Opportunities: Opportunities arising from the transition to a low-carbon economy, such as revenue from products and services designed for a low-carbon economy.
4. Transition risks: Risks associated with the transition to a low-carbon economy, such as changes in policy, technology, and market conditions.
5. Resilience: Resilience of the organization’s strategy, taking into account different climate-related scenarios.
6. Metrics: Key metrics used to measure and manage climate-related risks and opportunities.
7. Targets: Targets used by the organization to manage climate-related risks as well as opportunities and performance against targets.

Along these lines, the Basel Committee on Banking Supervision (BCBS), in its 23 November 2023 consultative document on climate financial risk disclosures, proposes that organizations provide certain key metrics used to measure and manage climate-related risks and opportunities, as well as metrics consistent with certain cross-industry, climate-related metric categories. These metrics to be provided for historical periods thus allow for trend analysis. Where appropriate, organizations should consider providing forward-looking metrics for the cross-industry, climate-related metric categories consistent with their business or strategic planning time horizons. In addition, where not readily apparent, organizations should provide a description of the methodologies used to calculate or to estimate climate-related metrics.

**Legal basis for FINMA**

Art. 7 of the Financial Market Supervision Act (FINMASA) dealing with principles of regulation explicitly empowers FINMA to issue circulars to the extent deemed appropriate for supervision. In doing so, it shall also consider international minimum standards. The NGFS recommendations are legally non-binding. Together, with the requirements and guidelines of international standard-setting bodies, such as the BCBS and the International Association of Insurance Supervisors (IAIS), they qualify as international standards.

## Next steps

FINMA will initiate a public consultation on the new circular in the first quarter of 2024. In 2024, FINMA will also review whether a revision of the current FINMA disclosure requirements is necessary due to the many developments in the area of climate and sustainability reporting.

See our earlier legal updates: " News on the CO2 Act: Standstill or departure for new shores?" and " Climate Protection in Switzerland and in the EU."

Author: Markus Winkler (Counsel)

**No legal or tax advice**

This legal update provides a high-level overview and does not claim to be comprehensive. It does not represent legal or tax advice. If you have any questions relating to this legal update or would like to have advice concerning your particular circumstances, please get in touch with your contact at Pestalozzi Attorneys at Law Ltd. or one of the contact persons mentioned in this legal update.



## Markus Winkler

Counsel
Attorney at law, Dr. iur., Dr. sc. math. ETH

Pestalozzi Attorneys at Law Ltd
Feldeggstrasse 4
8008 Zurich
Switzerland
T +41 44 217 92 59
markus.winkler@pestalozzilaw.com