

# **ESG Investments vs. Corporate Social Credit System (CSCS) – How New Governance Models Impact Businesses in Switzerland and in China**

SCCC LEGAL CHAPTER WEBINAR

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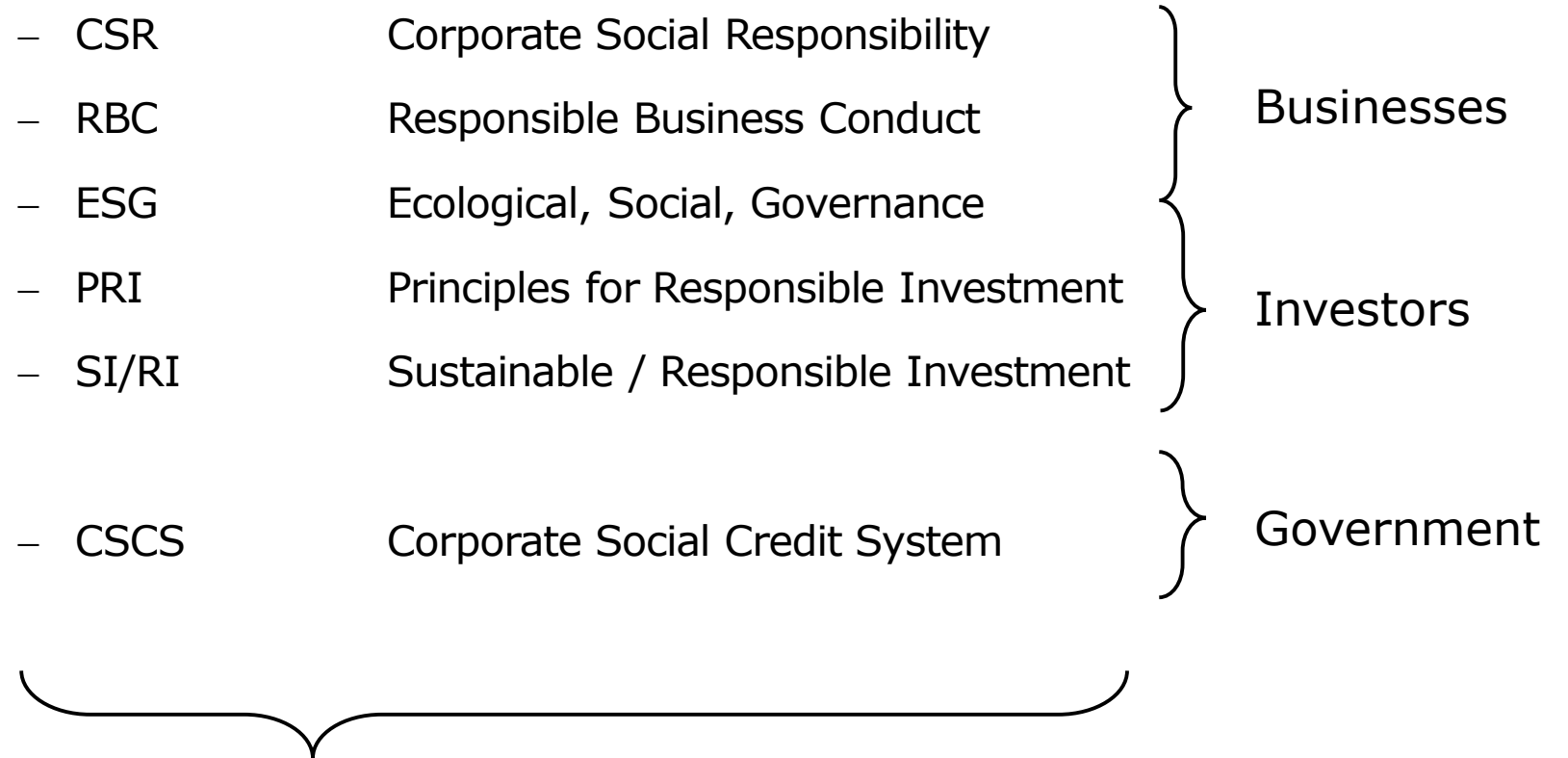
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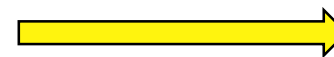
## **PART I – INTRODUCTION**

**I. TERMINOLOGY**

**AN EMERGING FRAMEWORK**

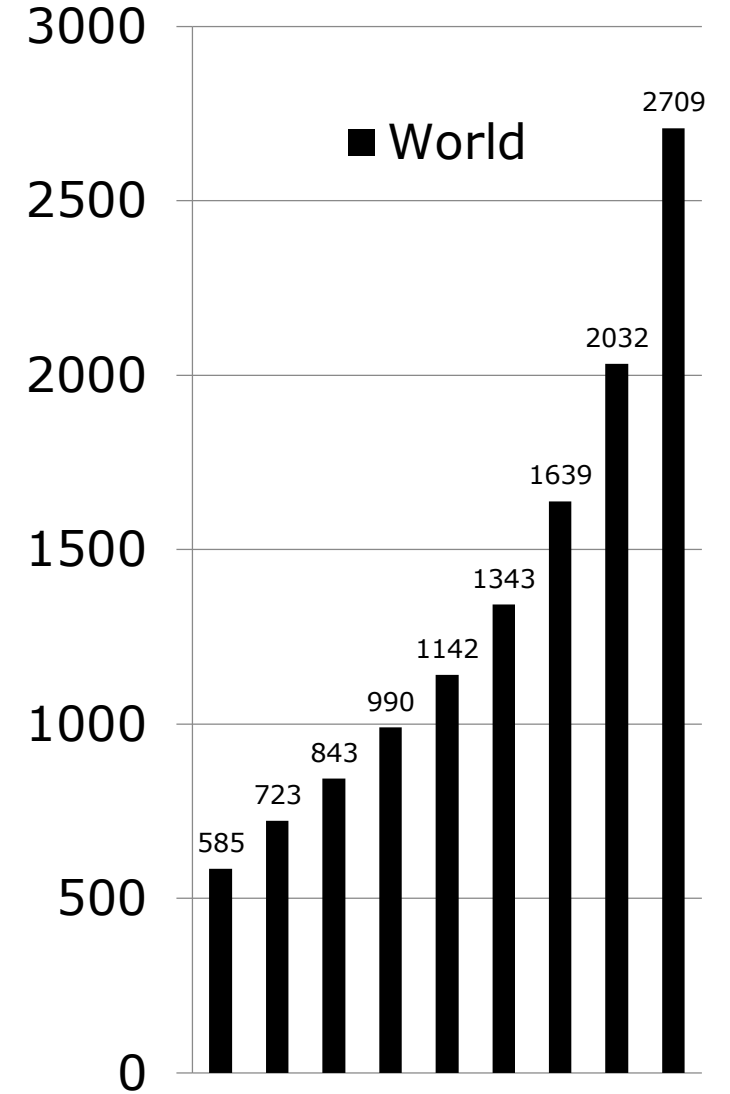
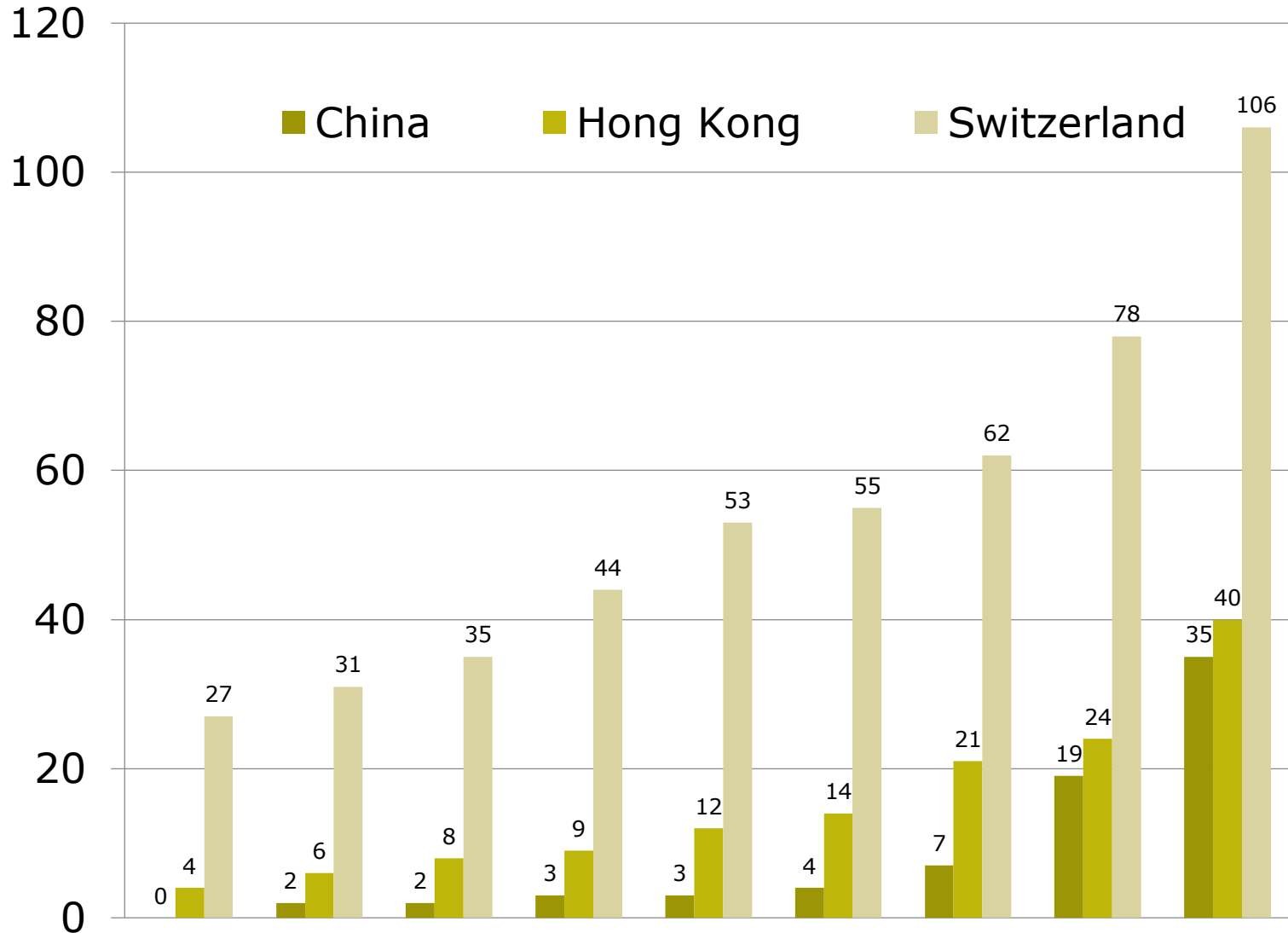


**Governance Tools**  
(used by «principals»)



**Businesses**  
(«agents»)

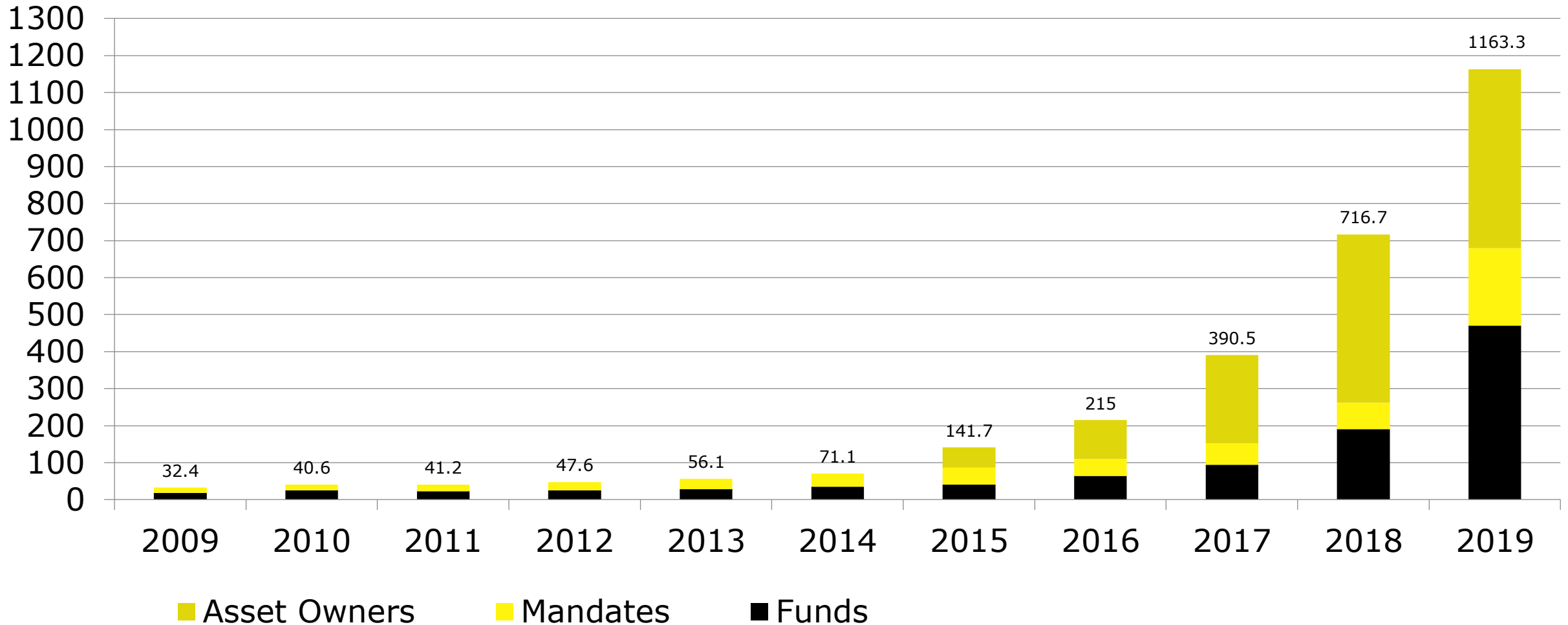
## II. PRI SIGNATORIES 2011 – 2019



Source: <https://www.unpri.org>, signatories directory

## **PART II – ESG IN SWITZERLAND**

### III. DEVELOPMENT OF SI IN SWITZERLAND (IN CHF BN)



Source: SSF/CSP: Swiss Sustainable Investment Market Study 2020, p. 18

## IV. PRACTICAL EXAMPLES

### LARGE COMPANIES



< ESG investing

## ESG investment solutions

+ Share Print

Credit Suisse Asset Management places great importance on sustainability across its investment businesses. We believe that a holistic approach to sustainability induces positive change and is crucial to enabling clients to earn above-average investment returns in the long run.

**coop** Locations Customer Service < Sustainability

Home Sustainability topics Background

**ACTIONS**  
not  
**WORDS**

### INNER DRIVE MEANS ACTIONS, NOT WORDS

We don't just talk, we act: The slogan «Actions, not words» encapsulates our commitment to sustainability on behalf of people, animals and nature. Learn more about our commitment to sustainable consumption and discover our latest actions!



**IV. PRACTICAL EXAMPLES**

STARTUPS

Rank	Ranking	Publisher	Issue
1	 <b>Global Talent Competitiveness Index</b> 	INSEAD, Adecco Group, Tata Communications	<u>2020</u>
1	 <b>World Talent Ranking</b> 	IMD	<u>2019</u>
1	 <b>Global Innovation Index</b> 	Cornell, INSEAD, WIPO	<u>2019</u>
1	 <b>European Innovation Scoreboard</b> 	European Commission	<u>2020</u>
4	<b>Global Competitiveness Report</b>	World Economic Forum (WEF)	<u>2019</u>
3	<b>World Competitiveness Ranking</b>	IMD	<u>2020</u>
5	<b>World Digital Competitiveness</b>	IMD	<u>2019</u>
1	 <b>Change Readiness Index</b> 	KPMG	<u>2019</u>
1	 <b>Best Countries Ranking</b> 	U.S. News, Y&R, BAV, Wharton	<u>2020</u>

**IV. PRACTICAL EXAMPLES**

STARTUPS



## IV. PRACTICAL EXAMPLES

### STARTUPS / PICKWINGS

The screenshot shows the Pickwings website header with a dark blue navigation bar. It includes a menu icon, the Pickwings logo (a stylized bird/wing), the text 'pickwings DAS SCHWEIZER TRANSPORTPORTAL', a 'Menu' label, an 'Online-Beratung' dropdown, a 'Fahre für uns' button, and a 'Registrieren' button. Below the header is a large banner image of a road with a truck, overlaid with the text 'Pickwings reduziert nachhaltig Leerkilometer auf Schweizer Strassen'. Underneath the banner is a grey section titled 'Weniger CO2, NOx und Feinstaub' containing four white boxes with green icons and text: 'Beste Fahrzeugauslastung' (leaf icon), 'Nachhaltige Prozess- und Tourenoptimierung' (truck with leaf icon), 'Aktiver Palettentausch' (pallet icon), and 'Papierlose Logistik' (document with slash icon).

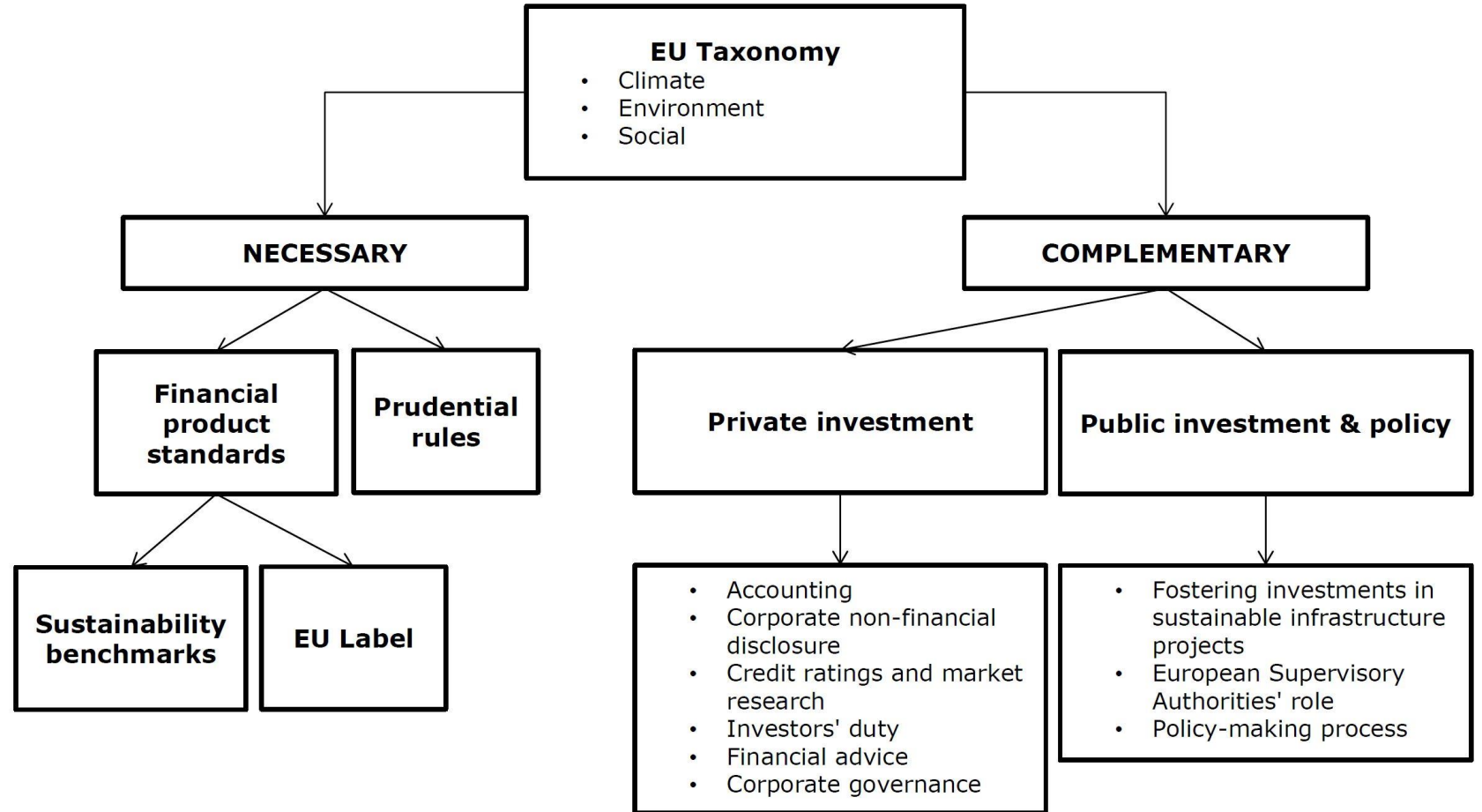
## CODIFICATION OF ESG INVESTMENT OBLIGATIONS?

### V. LEGAL FRAMEWORK

	International	National
hard	<ul style="list-style-type: none"> <li>• Paris Agreement</li> <li>• EU Investment Law</li> <li>• Conventions on individual «E», «S» and «G» issues</li> </ul>	<ul style="list-style-type: none"> <li>• Financial Market laws and regulations</li> <li>• CO2-law</li> <li>• KVI</li> </ul>
soft	<ul style="list-style-type: none"> <li>• UN Sustainable Development Goals</li> <li>• UN Global Compact</li> <li>• RBC</li> <li>• PRI</li> <li>• ISO-Standards (e.g. the "14000 Family")</li> <li>• Sustainability reporting (e.g. SASB and GRI standards)</li> </ul>	

# ROLE OF EU TAXONOMY IN THE EU 2018 ACTION PLAN ON SUSTAINABLE FINANCE

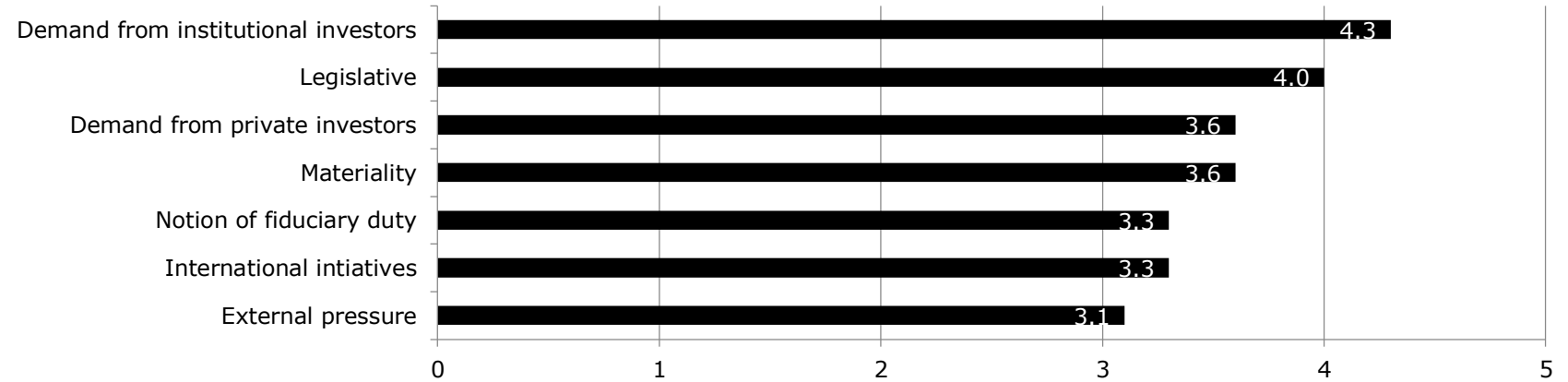
## V. LEGAL FRAMEWORK



Source: EU Action Plan: Financing Sustainable Growth (COM/2018/097), p. 14

## KEY DRIVERS FOR SI IN THE NEXT 3 YEARS

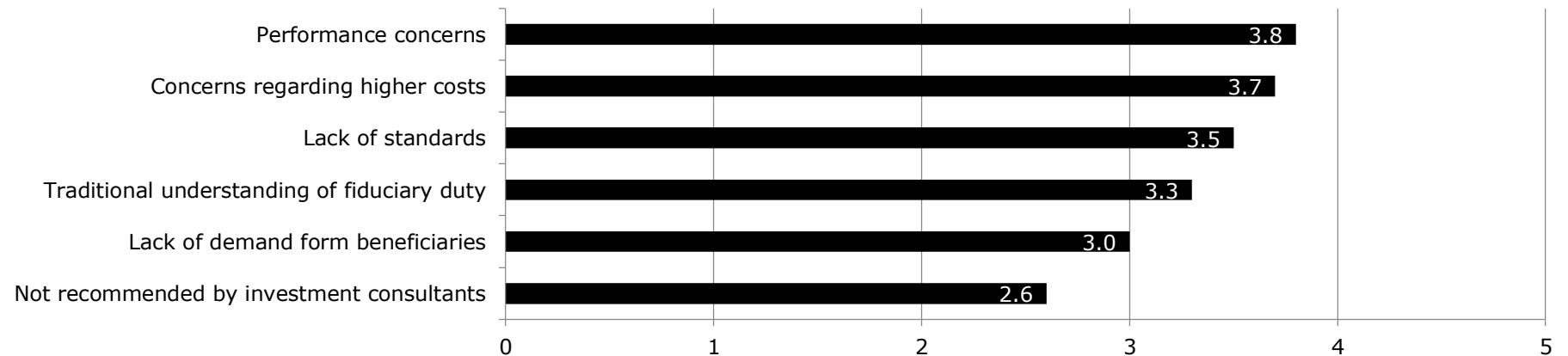
Perception by Asset Managers



0: Not important

5: Very important

## VI. PRACTICAL OUTCOMES



Perception by Asset Owners

## KEY BARRIERS TO SI IN THE NEXT 3 YEARS


Source: SSF/CSP: Swiss Sustainable Investment Market Study 2020, pp. 39, 41

## **PART III: GOVERNANCE MODELS IN CHINA**

## **VII. CORPORATE GOVERNANCE IN CHINA**

### **FOUNDATIONS**

#### **1. Existing Legal Framework**

- From agency questions (SOEs) to the **Company Law**
- New Foreign Investment Law (1.1.2020)
-  Company Law applies to Joint Ventures / Foreign-invested Companies
- Other laws and regulations influencing corporate governance in China, e.g.
  - Environmental laws
  - Stock exchange regulations (Shenzhen / Shanghai / Hong Kong)

#### **2. The emerging framework of the CSCS**

- 2014: State Council announces plan for establishing a social credit system
- Cluster of local / regional regulations and (trial) practices
- No harmonized «CSCS-law» yet – expected entry into force: 2022



## CORPORATE SOCIAL CREDIT SYSTEM – OBJECTIVES

*«Let there be benefits everywhere for the trustworthy,  
and for the untrustworthy restrictions with every step.»*

*Li Keqiang*

### VIII. THE CSCS



**Source:** Picture by Markus Herrmann, Shanghai, IAPM mall in Huangpu District, Nov. 2019

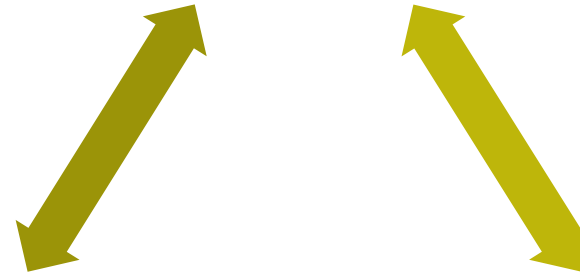
## VIII. THE CSCS

### CORPORATE SOCIAL CREDIT SYSTEM – KEY ELEMENTS

- **Who** is subject to the CSCS?
- **What** fields (e.g. environment, product and work safety, tax, customs)
- **Punishment and reward system**
  - Rating-specific punishments (depending on industry)
  - Joint punishments (MoUs)
- **Internet + Monitoring System** (data transfer, pooling of information)
- Licensed commercial and governmental **rating agencies**



## CORPORATE SOCIAL CREDIT SYSTEM – KEY FUNCTIONS



### Currently:

- No Company Rating on National Level (**yet**).
- Incomplete flow of data.

## VIII. THE CSCS

## CORPORATE SOCIAL CREDIT SYSTEM – PRACTICAL IMPACT ON BUSINESS

➤ Joint **awards**:



- Less inspections (e.g. customs)
- Enhanced access to loans
- Lower taxes
- Fast-track administrative procedures

➤ Joint **sanctions**:



- “black-listing” // “heavily distrusted entity”
- More inspections / targeted audits
- Import / export restrictions
- Restricted access to loans / public procurement
- Key personnel of a company, e.g. travel restrictions



**Source:**

<https://www.nytimes.com/2019/09/22/business/china-social-credit-business.html>

## VIII. THE CSCS

## ESG IN CHINA – CURRENT STATUS

### IX. ESG IN CHINA AND IMPACT OF THE CSCS

2019 green bond issuance (YoY growth)

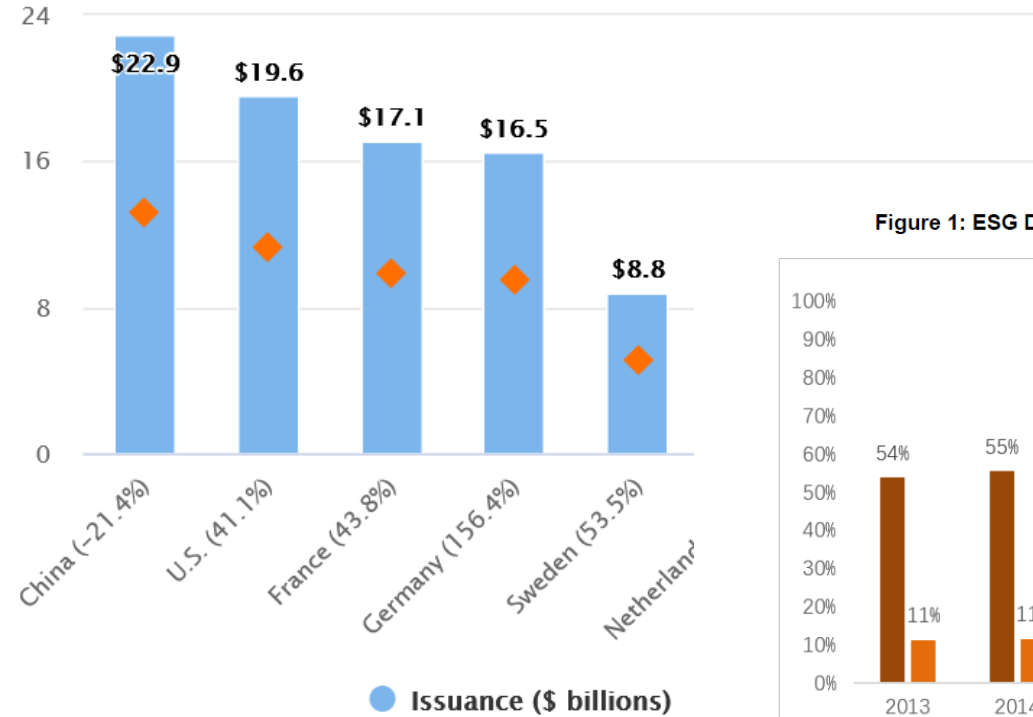
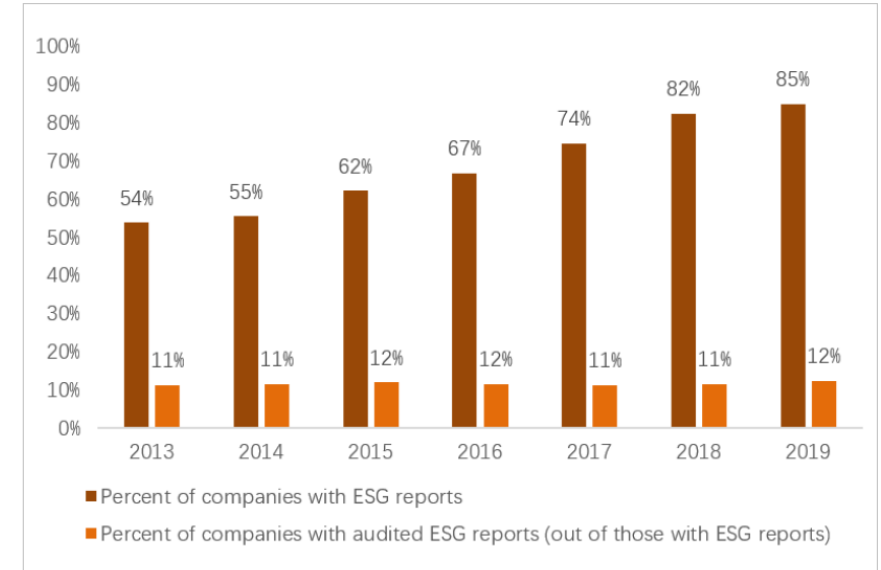


Figure 1: ESG Disclosure Among CSI300 Companies (2013-2019)



Source: Analysis of Wind data

<https://www.pionline.com/interactive/china-leads-green-bonds-others-catching>

[https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKewjak6\\_BrffrAhUnGTQIHXYfChgQFjAEegQIBB&url=http%3A%2F%2Fwww.pingan.cn%2Fapp\\_upload%2Ffile%2Fofficial%2FESGinChina\\_EN.pdf&usq=AOvVaw0p3qVT7TbOExufW3oqXtvz](https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&cad=rja&uact=8&ved=2ahUKewjak6_BrffrAhUnGTQIHXYfChgQFjAEegQIBB&url=http%3A%2F%2Fwww.pingan.cn%2Fapp_upload%2Ffile%2Fofficial%2FESGinChina_EN.pdf&usq=AOvVaw0p3qVT7TbOExufW3oqXtvz)

## **IX. ESG IN CHINA AND IMPACT OF THE CSCS**

### **ESG IN CHINA – IMPACT OF THE CSCS**

#### **1. Increased focus on ESG topics**

- Compulsory provisions on environmental protection, product quality, workplace safety etc.
- New Chinese 5-year plan: focus on sustainability («E»-Factor)

#### **2. CSCS makes non-compliance with ESG-standards transparent and costly**

- Government-backed incentive to comply with ESG-standards
- The «market» will eliminate black sheep
- Monitoring ESG-compliance and taking a pro-active approach are essential
- **Governance 2.0**

## **PART VI: ESG VS. CSCS AND OUTLOOK**

## THE GOVERNMENT AND SOCIETY PERSPECTIVE

Aspect	CSCS	ESG
innovative claim	reaching societal goals without involvement of the judiciary	reaching societal goals without involvement of the legislative
time frame	short term: immediate compliance	long term: working towards a paradigm shift among decision makers
goals	social stability, enhance trust among market participants (producers and customers, businesses, authorities);	sustainability on a global scale (climate change, Covid 19-pandemic)
rationale	<b>comprehensively steer behavior of businesses at low agency costs; internalize external costs</b>	
effectiveness	probably high, immediate sanctions for non-compliance	incremental transition from moral obligations into enforceable legal rights and obligations
implementation	basic idea promulgated first, gradually to be implemented by local and national authorities	basic idea first, gradually to be co-opted by businesses themselves

## X. COMPARISON



## X. COMPARISON

### THE INVESTORS' PERSPECTIVE

Aspect	CSCS	ESG
incentive	extrinsic: hard incentive not to invest in businesses with a bad CSCS rating	intrinsic: align profit seeking with moral values (if possible)
trajectory	inbound (CSCS only applies to businesses active in China)	outbound (e.g. investment in developing countries)
normative vs. descriptive	clearly normative (punishment for non-compliance)	both descriptive (materiality of ESG risks and opportunities) and normative (adoption of binding standards, hard and soft)

## X. COMPARISON

### THE BUSINESS PERSPECTIVE

Aspect	CSCS	ESG
«governor»	the state: lawmaker and its enforcers	primarily investors, but also society, legislator (in response to societal demands)
compliance to	pre-existing and future legal obligations as interpreted by government agencies	aspirational ESG standards
reward for compliance	direct: access to credit; smooth customs service; lower taxes; access to government procurement	indirect: public relations (CSR); expectation of improved risk management and favorable business opportunities
punishment for non-compliance (enforcement)	direct: less access to credit, degraded customs service, higher taxes; loss of business license	indirect (loss of goodwill among the public, affecting business volume and recruitment of talent)
goals	compliance/avoid punishment	ward off legislative pressure / attract investment capital
motivation	long-term survival and profitability of one's business	
challenges	<b>Efficacy of spent efforts difficult to anticipate:</b> uncertainty about the relation/correlation between "wrongdoing" on the one hand and the form and extent of punishment on the other	<b>Efficacy of spent efforts difficult to anticipate:</b> credibility as to the sincerity of one's ESG efforts; materiality of ESG factors difficult to gauge.

## **XI. CHALLENGES**

### **CHALLENGES TO THE CONCEPTS OF ESG AND CSCS**

#### ESG:

- trade-offs with profitability not addressed (yet)
- transparent, internationally recognised evaluation and reporting standards still wanting (most labels apply only sectoral)
- only «hard» law will eventually provide a level playing field for all actors, big and small

#### CSCS:

- «Governance 2.0» has not yet replaced, but continues to rely on, more traditional forms of governance, such as courts and administrative agencies
- co-existence of CSCS and the existing governance apparatus could diminish, rather than foster, legal certainty

## **XII. UNIFIED APPROACH FOR BUSINESSES**

### **SUGGESTED UNIFIED APPROACH TO ESG AND CSCS**

1. Anticipate, identify, and comply with «hard» (legal) obligations
2. Use surplus compliance resources to:
  - identify hitherto unrecognised ESG/CSCS factors in your business model («low-hanging fruit»)
  - leverage existing ESG/CSCS compliance potential to generate optimum cost-benefit outcome, e.g.:
    - implement ESG reporting to attract more investors
    - join one or several labels
    - become «red-listed» under CSCS
3. If pressurized to ESG-conformity: do not accept ESG as a goal in itself; always identify what practical business outcome is to be expected from a certain business move; discuss identified trade-offs with investors, implement solution with best long-term viability

**Q&A**

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**THANK YOU FOR YOUR PARTICIPATION !**

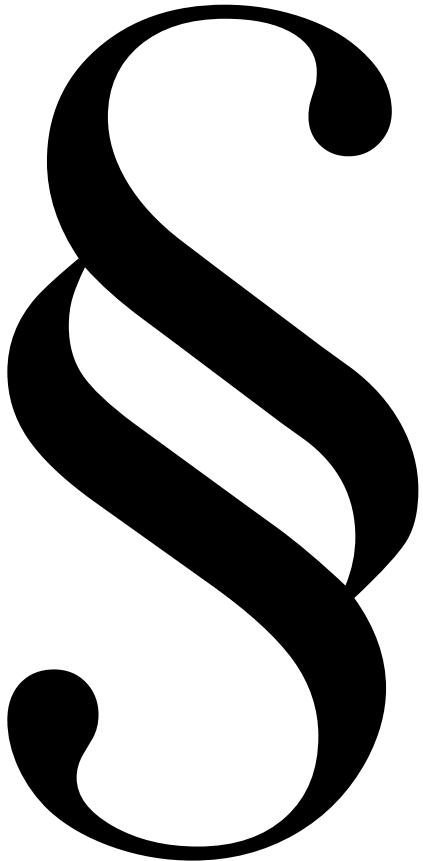


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