POSITION PAPER

ESBG recommendations on the Corporate Sustainability Due Diligence Directive

ESBG (European Savings and Retail Banking Group)
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ESBG Transparency Register ID 8765978796-80

03 April 2023

ESBG

Savings and retail banks >> strong players in financing the real economy

The European Savings and Retail Banking Group (ESBG) strongly opposes any breaches of human rights or activities that harm the environment. It is rooted at the very core of our identity to act in a socially responsible manner towards our clients, employees, communities and the environment. Moreover, we are playing a crucial role in financing the real economy by actively providing financial services to individuals and their households as well as micro-, small- and medium-sized enterprises and local authorities.

We are taking our vital role very seriously and always act in the best interest not only of the communities we serve, but also of the general public.

We are convinced that a feasible and just framework for corporate sustainability due diligence rules will be essential when it comes to bringing the intention of policy makers effectively to life without doing more harm than help. We believe that regulating such a highly technical matter requires a profound basis and does not allow for any legal weaknesses, as the implications would be tremendous if not designed well.

As negotiations are currently ongoing in the European Parliament, this paper aims to bring further clarity on the role that financial undertakings, and notably savings and retail banks, can play to make this Directive work.

Therefore, ESBG experts propose the below <u>five recommendations</u>.

They are focusing mainly on the role of the financial sector in the proposed Directive, as we understand our capacity in being an integral element when it comes to financing communities in Europe and beyond.

We remain at your disposal (adrien.boudet@wsbi-esbg.org or +32 478 84 34 88) should you have any questions or wish to discuss our recommendations.

Recommendation 1

Reconsidering the scope(s).

Proportionality is a key aspect of making the rules feasible. It is commonly known that a "one size fits all"-approach certainly does not suit the European banking sector. Its particularities need to be factored in when it comes to defining the scope(s) of the proposed Directive.

ESBG supports lifting the employee threshold to 1000. In this regard, it is worth mentioning that the scope is 1000 in the German *Lieferkettengesetz* and 5000 in the French *Loi relative au devoir de vigilance*. Moreover, for competitiveness purposes, ESBG calls to narrow the gap between the suggested thresholds for EU and non-EU companies. This could notably mean to consider the worldwide turnover of non-EU companies instead of the turnover that they are generating in the EU only.

ESBG has also concerns regarding the scope of the "adverse impact." This notion is related to international conventions mentioned in the Annex, part II ("adverse environmental impact") and in the Annex, part I section I and II ("adverse human rights impact"). In total, it will require companies to comply with no less than 33 international conventions. ESBG believes that it cannot be reasonably expected from them to do so and would therefore demand to the Commission to develop guidelines through delegated acts to make sure a proportionate approach is taken.

Finally, ESBG strongly opposes the inclusion of the financial entities in the list of high-risk-sectors.

>> Related provisions: Article 2, Article 3(b) and (c), Annexes.

Recommendation 2

Tailoring the value chain to pivotal parts.

The European Commission's proposal rightly limited the value chain of financial entities to the parts where its activities could cause harm: the financing of companies with harmful practices. Moreover, keeping in mind the objective of making Europe an attractive location for innovation and entrepreneurship, as well as competitiveness in the global scenario, it is indispensable to keep exemptions for small and medium-sized enterprises (SMEs).

Not all financial activities benefit from the same level of control and leverage on their value chain. If a bank providing loan services can have leverage over their clients, it is not the same for investment services and activities that simply consist of buying securities issued by corporates. Investment managers or even retail or professional investors are usually minority shareholders of those issuing companies, hence providing them little to no leverage on their investee companies.

For this reason, we insist on limiting the value chain to the <u>direct customers receiving loans or credits only</u>, not to their subsidiaries or business partners. Also, loans or credits provided to SMEs, natural persons and households should not be covered by the value chain and therefore explicitly excluded in Article 1. Finally, ESBG would like to stress the vagueness of the notion of "other financial services" which should not be mentioned.

>> <u>Related provisions</u>: Article 3(g), Article 1.

Recommendation 3

The need to adopt a risk-based approach when conducting the due diligence for financial undertakings.

The European Commission's proposal took the special role of financial undertakings into account. This equitable treatment in the provisions is key to preserving the well-functioning of key services like loans and credits provided to citizens and companies. As a matter of good due diligence practices, it is essential to differentiate between certain risk profiles of customers. It is therefore fundamental to implement a risk-based approach in the provisions.

ESBG proposes including a differentiation between simplified and enhanced due diligence rules depending on the risk profile of a customer. For instance, it could make sense to prioritize identification of entities established in countries/regions more likely to generate "high adverse impacts". The Commission could define the criteria to identify the aforementioned high risk areas (as an alternative and while the Commission develops them, it would make sense to follow the guidelines from the OECD on this topic) and then, to prioritize the due diligence on the customers located in these zones. A "presumption of conformity" for products and services procured within the European Union could also be a way of introducing more proportionality into the framework.

Regarding the specific role of financial undertakings, ESBG strongly urges to keep the identification obligation limited to <u>before</u> providing loans or credits. Furthermore, terminating a credit or loan contract could have a massive negative impact on financing communities and the economy and thus should be regulated with increased caution. In addition, ESBG would like to ask for more clarity regarding who will be in charge of assessing whether the termination of a contract would "cause substancial prejudice" or "bankrupcy". From a legal perspective, the exact meaning of "substancial prejudice" is also unclear.

Finally, ESBG stresses the need to consider the specific structure of mutualist banking groups. To this end, their banks or regional banks, and generally their affiliates within the meaning of Article 10 of <u>Regulation EU 575/2013</u>, should be considered as subsidiaries. This would allow banking groups to conduct their due diligence at the banking group level.

>> <u>Related provisions</u>: Article 4, Article 5, Article 6(3), Article 7(6), Article 8(7).

Recommendation 4

A coherent frame that makes the rules work.

Various regulatory initiatives in the field of sustainability and corporate governance have been introduced over the past few years. It is of utmost importance to avoid double regulation, align with existing texts and keep a comprehensive overview when designing new acts.

With regard to the transition plan, we cannot be responsible for a company's failure and the need to publish one is already in the CSRD. As a result, ESBG requests the deletion of Article 15.

ESBG also stresses the need for member states to designate already existing national supervisory authorities to supervise the compliance with the obligations of this directive. This will avoid duplication, dispersal of resources and ensure consistency since they have the needed expertise.

Overall, ESBG encourages the legislators to coordinate their progress with other current projects, such as the EU taxonomy, corporate sustainability reporting directive, deforestation regulation and conflict minerals regulation.

>> Related provisions: All the directive, notably Article 15, 17, 18.

Recommendation 5

Ensuring legal certainty is key.

Legal certainty for all parts of society must remain the highest aspiration. Nonetheless, the provisions regarding civil liability as well as how to trigger it seem to go in the opposite direction. ESBG would like to recall that according to general legal principles, liability is always linked to a culpable breach of duty that is causal for the damage. Deviating from this principle can lead to legal uncertainty. **As a consequence, ESBG discourages the inclusion of specific provisions related to civil liability under the proposed Corporate Sustainability Due Diligence Directive, notably because it could lead to a permanent litigation risk.**

ESBG is also of the view that there is no need to establish new corporate directors' duties as they already take long-term sustainability goals into account in their decisions, and they are already obliged to act in the company's interest according to national law. They should not be held accountable for concepts of an undetermined nature that are not completely under their control. **Therefore, ESBG strongly recommends to eliminate Articles 25 and 26 related to the directors' duty of care, as suggested by the Council in its general approach.**

Finally, ESBG recommends that the substantiation of concerns is eliminated alongside all related references and provisions, such as those included in Article 23 on the reporting of breaches and protection of reporting persons.

>> Related provisions: Articles 19, 20, 22, 23, 25 and 26.

About ESBG (European Savings and Retail Banking Group)

ESBG represents the locally focused European banking sector, helping savings and retail banks in 17 European countries strengthen their unique approach that focuses on providing service to local communities and boosting SMEs. An advocate for a proportionate approach to banking rules, ESBG unites at EU level some 900 banks, which together employ 650,000 people driven to innovate at 50,000 outlets. ESBG members have total assets of € 5.7 trillion, provide € 1 trillion in corporate loans, including to SMEs, and serve 163 million Europeans seeking retail banking services. ESBG members commit to further unleash the promise of sustainable, responsible 21st century banking.

Our transparency ID is 8765978796-80.

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Published by ESBG. 29 November 2022.