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The EU Taxonomy and what it might mean for the loan market

A webinar delivered for the Loan Market Association

Sustainable Finance
and Responsible Investment

Summer 2020

Introduction

At CMS we have been active in the field of sustainable finance for some time and a common theme for the investors and lenders and borrowers with which we work is the need for a consistent approach to measuring sustainability. A number of credible benchmarking organisations have emerged in recent years but, to date, there are no industry-standard measures of how to grade the overall sustainability of a business or an investment. The EU Taxonomy has been described as a 'toolkit for determining which economic activities are environmentally sustainable', and it is intended to give clarity to stakeholders across all facets of the financial system as to whether, and how, something contributes to the objective of sustainable growth.

The Taxonomy is wide-ranging and detailed, so this paper breaks it down into three main concepts:

The broader regulatory framework around sustainability:
What is the EU's proposal for a regulation on the establishment of a framework to facilitate sustainable investment (the "**Taxonomy**") and how has it developed?

The application of the Taxonomy and how it is intended to work in practice:
Which entities will be subject to its requirements and how will they be expected to comply?

The implications of the Taxonomy:
What might it mean for the financial sector going forward?

The information we present in this paper is based on a webinar we delivered for the Loan Market Association, so primarily aimed at lenders and borrowers. If you are interested in understanding more about the Taxonomy from another perspective, or discussing its practical applications in the market, please do not hesitate to contact us.

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What is the Taxonomy?

Background

The initial plan for the Taxonomy was developed in the context of the European Commission's 2018 action plan on financing sustainable growth. The plan represents the EU's strategy for implementing a financial system which supports its broader climate and sustainable development agenda. The UK Government, in its Green Finance Strategy, has committed to matching or exceeding the package of sustainability policies set out by the EU in its 2018 plan, and that includes the Taxonomy which is expected to be incorporated into UK policy on sustainable finance going forward.

> The Taxonomy is a toolkit for determining which economic activities are environmentally sustainable.

So how did the EU action plan come about? Broadly speaking, it represents the Commission's response to the realisation that the trajectory of the economy was not consistent with EU's obligations as a signatory to the Paris Agreement. Indeed in 2018 the Commission estimated that there was an investment deficit in the region of EUR 180bn per annum in meeting those climate targets. With the intention of dramatically enhancing the availability and consistency of sustainability-related information in the financial sector, the Commission called for the creation of a taxonomy – essentially to give investors in the European market a clear and comparable picture of the investment opportunities which were in effect scientifically proven to be environmentally sustainable, and therefore aligned with the EU's obligations under the Paris Agreement.

COVID-19 and the EU Commission's new consultation

There has been some concern that the current COVID-19 crisis would side-line the sustainability agenda at European level. However, in late April, the Commission launched its consultation on a renewed sustainable finance strategy which builds on 2018's plan. In introducing the strategy, the Commission made a direct link between the pandemic and the sustainability opportunities posed by a so-called "**green recovery**" with the Taxonomy framework at its core - some commentators have viewed this a clear signal of intent with respect to the priorities of von der Leyen's commission for the remainder of its five year term.

The scope of the proposed strategy is extremely broad and the consultation, which is open until July 2020, covers issues ranging from corporate governance to the introduction of sustainable finance as a subject to be taught at school. The consultation is seeking views, in particular, on whether to require financial advisers to offer sustainable investment products as a default option and, if that were to be adopted as part of the final strategy, the sustainability of those investments would presumably be determined by reference to the Taxonomy. The consultation is also seeking views on whether there are assets that could warrant a more-sensitive treatment in banks' prudential capital requirements, in order to incorporate ESG risks into prudential regulation in a more effective and faster manner. This is a nod to the long discussed "green supporting factor" or perhaps, a punitive factor for carbon intensive activities, which has been mooted since the Taxonomy was first proposed in 2018.

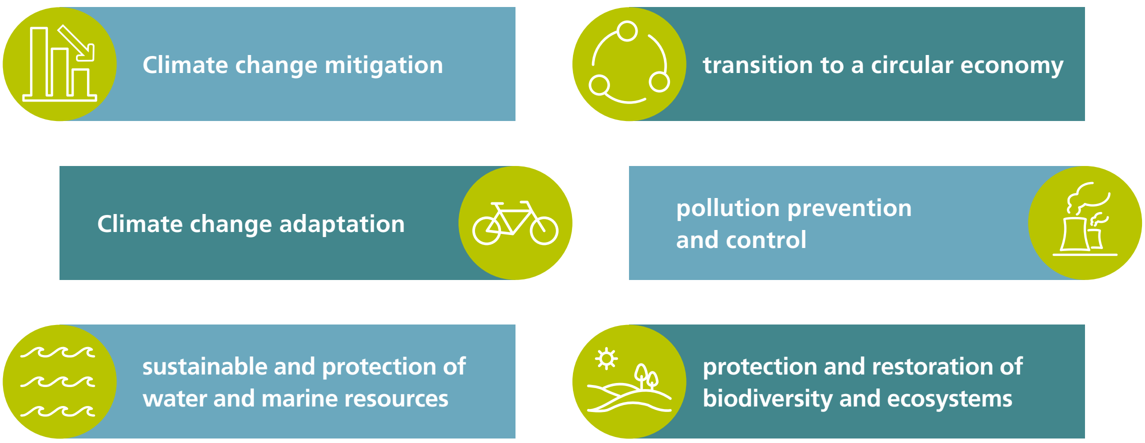
In the context of the European Green Deal, the Commission has also submitted a legislative proposal for a regional climate law which includes a legally binding target of net zero greenhouse gas emissions by 2050 and a 50-55% reduction in present greenhouse gas emissions levels by 2030.

Key elements of the Taxonomy

First of all the Taxonomy identifies an eligible economic activity in accordance with the NACE industrial classification system and then, as shown in Figures 1 and 2 below, it assesses, by reference to technical performance standards, whether that activity meets the following criteria:

Figure 1

Figure 2



1 & 2 EU Technical Expert Group on Sustainable Finance. Technical Report.
Taxonomy: Final report of the Technical Expert Group on Sustainable Finance. March 2020. Page 2

Where is it documented?

These three overarching requirements are set out in the EU's proposed regulation on the establishment of a framework to facilitate sustainable investment ("**Taxonomy Regulation**"), the text of which was adopted by the Council of the European Union at first reading on 15 April 2020. The Taxonomy Regulation now needs to be adopted by the European Parliament at second reading before it is published in the Official Journal of the European Union.

> 20 days after publication in the official journal, the Taxonomy Regulation will come into legal effect.

Given the highly technical nature of the work required to determine what would constitute "substantial contribution" or "significant harm" with respect to each of the EU's environmental objectives, the Commission established a Technical Expert Group ("**TEG**") made up of various experts and stakeholders and gave the group a mandate to, amongst other things, create the performance standards, or **technical screening criteria** as they are known, which would render an eligible economic activity truly sustainable and thus "taxonomy-aligned".

In order to create a usable and consistent framework of reference, the high-level text of the Taxonomy Regulation will be supplemented by delegated acts which will contain the detailed technical screening criteria developed by TEG and which will set out methodologies for measuring what constitutes a **substantial contribution or significant harm** in particular circumstances.

TEG have now created technical screening criteria for the first two of the EU's environmental policy objectives – climate change mitigation and climate change adaptation – and it will hand over to the Platform on Sustainable Finance, a permanent body to be established under the Taxonomy Regulation, to develop equivalent technical screening criteria for the remaining four environmental policy objectives.

Technical Criteria

In terms of the **climate change mitigation** objective, from the 615 categories of economic activity set out in the NACE classification code, TEG identified 67 types of economic activity which could make a substantial contribution to climate change mitigation. The sorts of economic activities foreseen under this objective include those relating to renewable energy, improving energy efficiency and clean mobility.

TEG also identified six so-called "macro-sectors" which were high carbon and therefore a **priority** for climate-mitigation action in order to meet the EU's climate targets. These include agriculture, gas and electricity, financial services and water supplies.

In terms of how one of the 67 economic activities would make a substantial contribution, TEG established **quantitative** criteria, based on the level of reduction of greenhouse gas emissions or increase in greenhouse gas removals either directly caused by or enabled by, the relevant economic activity.

In addition to activities which directly reduce or enable reduction of greenhouse gases, activities for which there are no technologically or economically feasible low-carbon alternatives are also eligible for taxonomy-alignment where those activities:

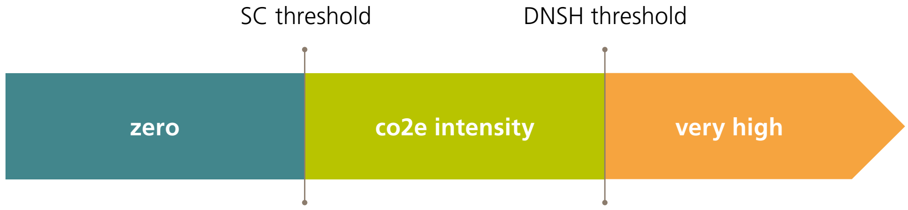
- Support the transition to a climate-neutral economy;
- Have "best in sector" gas emission levels; and
- Do not hamper the development of low carbon alternatives.

The **climate change adaptation** objective includes economic activities which either include adaptation solutions which reduce the impact of climate change on that particular activity or which otherwise provide adaptation solutions for other activities. Due to the context-specific nature of a climate adaptation activity, TEG have not been able to produce an exhaustive list of activities which could be viewed as contributing to adaptation. However, examples of this include the installation of climate resilient transmission lines for the distribution of electricity; the construction of flood protection systems; and the commercialisation of drought-resistant crop varieties.

As noted above, economic activities making a substantial contribution to climate change mitigation or adaptation must be assessed to ensure they do not cause significant hard to all remaining environmental objectives. This assessment ensures that progress against some objectives is not made at the expense of others and recognises the reinforcing relationships between different EU policy goals.

As shown in Figure 3 below, "do no significant harm" criteria in respect of climate change mitigation are based on quantitative, performance-based metrics. Therefore, by example, an economic activity aimed at making a substantial contribution to biodiversity would not be considered taxonomy-aligned if it was achieved using unabated fossil fuel-based technology.

Figure 3
Example of quantitive SC and DNSH criterea



3 EU Technical Expert Group on Sustainable Finance. Technical Report. Taxonomy: Final report of the Technical Expert Group on Sustainable Finance. March 2020. Page 52

With regard to climate change adaptation activities, given the context-specific nature of those, the metrics for measuring significant harm to that objective are more nuanced and based on a qualitative assessment of whether the relevant activity leads to an increased adverse impact of the current and expected climate, on itself or for other people, nature and assets.

Future developments

It is worth noting that when people discuss the "taxonomy" they are referring to both the Taxonomy Regulation and to the delegated acts, which remain a work in progress. It is expected that the delegated acts relating to technical screening criteria in respect of the first two environmental policy objectives will be adopted into EU law by the end of 2020. The full set of technical screening criteria is expected to be in place by the end of 2021.

In the course of the various consultations on the Taxonomy, the key concern raised has been that the framework will be insufficiently flexible to develop alongside climate science and EU policy. The Commission have therefore sought to establish an online stakeholder feedback loop which will be incorporated into the work of the Platform for Sustainable Finance. The idea is that users of the framework will be able to provide feedback on its usability in real time and on a rolling basis. How that will be incorporated into the framework in practice remains to be seen.

The intention is to create a living instrument with the capacity to change and grow with the times.

Taxonomy in practice

To whom does the Taxonomy apply?

Individual Member States

The Taxonomy will apply to individual **Member States**, who will need to apply the Taxonomy criteria in the development of public measures, standards and labels concerning environmentally sustainable economic activities.

Companies and firms within the scope of the Non-Financial Reporting Directive

The Taxonomy Regulation will also apply to **companies and firms within the scope of the Non-Financial Reporting Directive**. For the UK, pursuant to the Companies Act 2006, that includes certain large companies and qualifying partnerships with more than 500 employees, including traded companies, banking companies and insurance companies. Those entities will be required to include analysis of the alignment of their activities with the Taxonomy in their annual non-financial corporate reporting, which will be required to include a description of how, and to what extent, their activities are associated with taxonomy-aligned activities by reference to:

1. the proportion of turnover aligned with the Taxonomy; and
2. capex and, if relevant, opex aligned with the Taxonomy.

Financial Market Participants

In addition to Member States and companies and firms which are subject to the non-financial reporting directive, the Taxonomy will also apply to **"Financial Market Participants" who offer "Financial Products" in the European market.** The definitions Financial Market Participants and Financial Products are taken across from the existing European regulation on sustainability-related disclosures in the financial services sector ("**Disclosure Regulation**") and include funds and investments offered by most pension providers, asset managers and insurance funds.

As a result of the Taxonomy Regulation's interplay with the Disclosure Regulation, Financial Market Participants will be required to provide disclosures in prospectuses, periodic reports and websites as to:

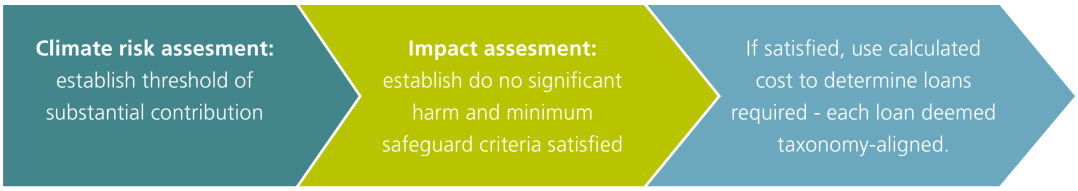
1. how and to what extent they have used the Taxonomy in determining the sustainability of the underlying investments;
2. to what environmental objective(s) the investments contribute; and
3. the proportion of underlying investments that are taxonomy-aligned and that must be expressed as a percentage of the fund and specify both enabling and transition activities

All Financial Market Participants will be required to provide disclosures as to Taxonomy alignment with respect to all Financial Products marketed into or manufactured in the European Union or the Financial Market Participant will need to include a disclaimer on its website, in its prospectus or in its periodic reporting that it has not taken the Taxonomy criteria into account.

How will it work in practice?

Companies and firms within the scope of the Non-Financial Reporting Directive

Take, for example, a software, or service-based company, looking to make its corporate headquarters and certain other facilities resilient to physical risk as a result of climate change. In terms of the EU's six environmental objectives this would fall under the category of **climate change adaptation**. The company would therefore turn to the relevant article of the Taxonomy Regulation which deals with adaptation criteria, as well as the technical screening criteria established by TEG to determine what constitutes substantial contribution to climate change adaptation and significant harm to all of the other EU environmental objectives. The company would also need to carry out suitable diligence to ensure that any action taken would meet minimum social safeguards.



What is the economic activity?

First of all, the company conducts a thorough climate risk assessment, and this establishes that the key potential impacts of climate change on its building are flooding and extreme heat. The company's economic activity in this case would therefore be financing activities aimed at reducing the risk of extreme heat and flooding on the buildings. For example, financing cooling measures and increasing the capacity of drainage systems.

What constitutes a substantial contribution?

As the criteria for establishing what constitutes a substantial contribution to climate change adaptation are "context specific", the fact that a thorough climate risk assessment was carried out would be sufficient in the circumstance to establish that the threshold of "substantial contribution" had been reached in respect of the relevant economic activities.

How can "significant harm" be avoided?

In addition to a climate change risk assessment to establish the relevant actions to be taken which would make a substantial contribution, the company also undertakes an impact assessment to ensure that the measures to be implemented are consistent with local and regional adaptation efforts, and with specific "do no significant harm" criteria for buildings, which will be set out in the delegated acts. By carrying out an impact assessment, the company establishes that the "do no significant harm" criteria have been satisfied and, in this case, also ensure that the threshold for minimum social safeguards are met.

How much of the financing is taxonomy-aligned?

On the basis of calculations set out in the initial climate change risk assessment, the overall cost of the proposed changes will be EUR 50m, and the company seeks several debt instruments over a three-year period to meet this requirement. The company starts its plan by adapting its corporate headquarters, and the cost of that is estimated to be EUR 10m – which is the object of the first loan. This first loan may be followed by other loans or debt instruments, up to an aggregate of EUR 50m.

Each one of those loans will be deemed to be taxonomy-aligned, even if one loan, for example, the initial EUR 10m loan, on its own does not reduce all material physical climate risks to the activity the company conducts; this is because the loans taken together are necessary as part of a broader, time-bound plan to adapt the entire company's facilities.

How might the taxonomy-aligned financing be treated?

— For the purposes of companies and firms which are a subject to the requirements of the non-financial reporting directive, the EUR 50m investment may count as taxonomy-aligned capex which it would report in its annual non-financial statement.
— The company will be able to report EUR 50m of taxonomy aligned investments, which opens the door to it seeking those loans as green loans which would, in turn, allow the lending banks to commercialise the loans as green and 100% taxonomy-aligned.
— a group of green loans might be bundled together and sold to investors as green securities.

Turnover

In terms of calculating taxonomy-aligned turnover on the basis of this example, none of the software company's turnover would count as taxonomy-aligned as a result of the economic activities outlined above. This is because economic activities in respect of their own performance are not yet recognised in the Taxonomy. However, this is expected to change before the Taxonomy comes into force and will have knock on effects for the calculation of taxonomy-aligned investments in equity portfolios.

Financial Market Participants

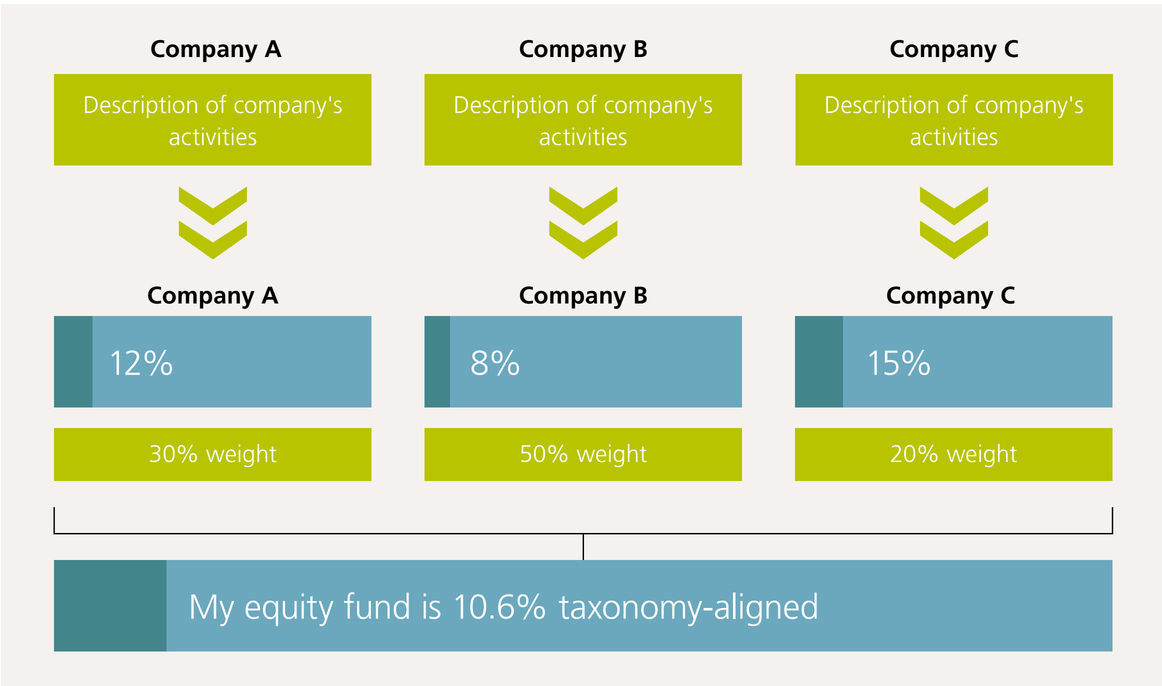
For a Financial Market Participant marketing an equity portfolio in the EU, the level of taxonomy-alignment would be reported by using the turnover of each of the companies as a proxy for equity exposure to taxonomy-aligned activities. An example is set out in Figure 4 below. As noted above, the methodology for including adaptation activities in the calculation of turnover of a company has not yet been developed by TEG, and on that basis Financial Market Participants would not be able to include those activities as part of their disclosures.

TEG has acknowledged that there will be some overlap in reporting obligations for Financial Market Participants who are subject to both the Disclosure Regulation and the Non-Financial Reporting Directive and it is scheduled to issue further guidelines on the scope of the disclosure obligations for affected entities by the end of June 2021.

Loan Facilities

It is worth clarifying that there is no direct obligation pursuant to the Taxonomy Regulation that requires financial institutions to disclose taxonomy-alignment in relation to individual loan facilities. However, investors will need this information when reporting on the portion of taxonomy-alignment of their funds pursuant to the Disclosure Regulation. Banking companies subject to the Non-Financial Reporting Directive will also need to have a record of these activities for the purposes of their non-financial corporate reporting. In addition, the Taxonomy is being applied in the development of new benchmarking and green bond standards, and the expectation is that it will form the basis of future prudential regulation in the European market, as well as future EU policy in the broader sustainable finance sector. As such it is in the interests of financial institutions to develop a clear understanding of its mechanics.

Figure 4



4 EU Technical Expert Group on Sustainable Finance. Technical Report. Taxonomy: Final report of the Technical Expert Group on Sustainable Finance. March 2020. Page 40

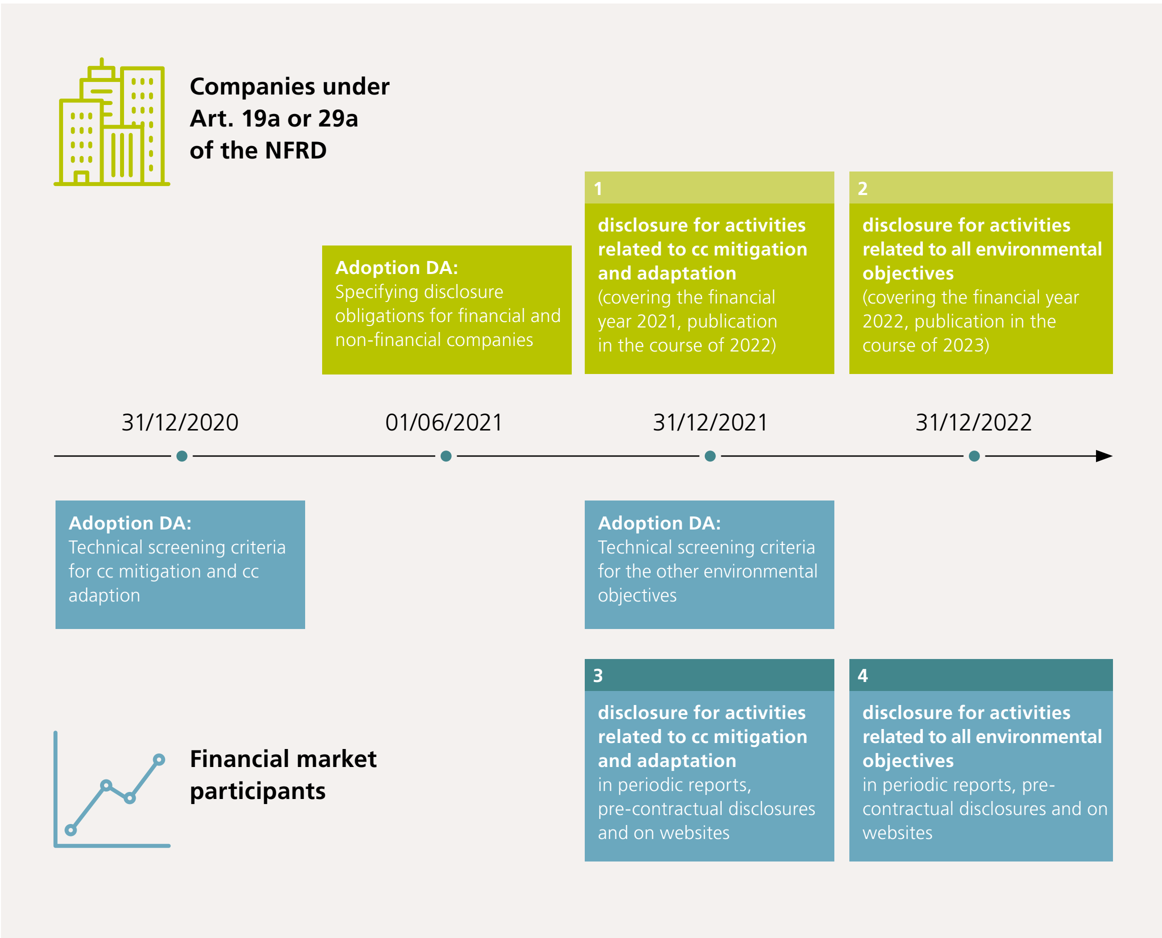
Timeline for Compliance

- Financial Market Participants will be required to complete their first set of disclosures against the Taxonomy, covering activities that substantially contribute to climate change mitigation and/or adaptation, by the **31st of December 2021**
- Firms within the scope of the Non-Financial Reporting Directive will be required to begin reporting on their mitigation and adaptation activities in the course of **2022** with respect to the financial year **2021**.

The Commission has acknowledged that this timing will create a gap in information for the first round of disclosures by Financial Market Participants. It has also acknowledged that since technical screening criteria has only been developed for the first two environmental objectives, the scope of the disclosures will extend only to mitigation and adaptation. As the full set of technical screening criteria is expected to be in place by the end of 2021, disclosures on the full taxonomy of environmentally sustainable economic activity would be expected for the financial year 2022.

TEG has indicated that it would encourage voluntary reporting on the remaining four environmental objectives until such time as full screening criteria are developed.

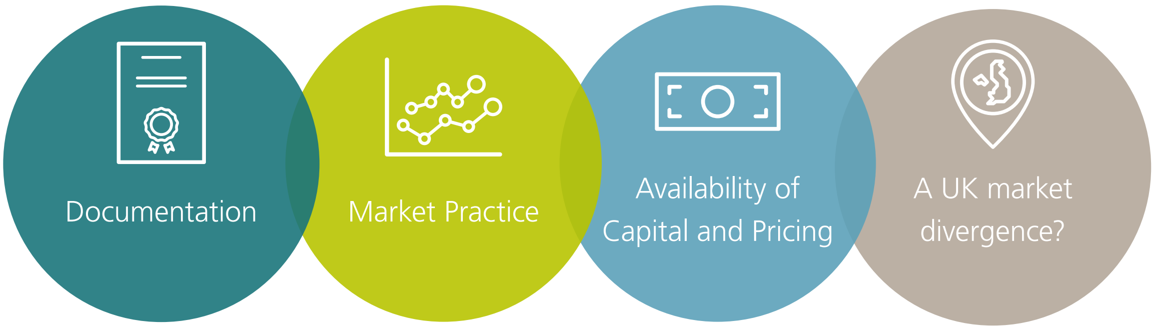
Figure 5



5 EU Technical Expert Group on Sustainable Finance. Technical Report. Taxonomy: Final report of the Technical Expert Group on Sustainable Finance. March 2020. Page 26

Implications, Observations and the New Normal

How might the implementation of the Taxonomy change the loan market?



Documentation

In terms of documentation, we should first consider **Green Loans**. Loans prepared in line with the Green Loan Principles or the Sustainability Linked Loan Principles published by the LMA need to, amongst other things, meet certain requirements in terms of the *Use of Proceeds and Reporting*.

With respect to Use of Proceeds, it is necessary that the loan proceeds are applied to a "green project". Currently the LMA applies the Green Bond Principles' categories of green projects which are "certified" by either the borrower or an independent third party. These categories are broadly framed and do not provide specifics. The Taxonomy differs from this categorisation in two ways:

1. Firstly, it is goal orientated i.e. it was formulated with a view to meeting the Paris Agreement carbon neutral target by 2050
2. Secondly, it sets out the types of technology or standards which are deemed to facilitate that goal.

It would thus be possible to substitute the Taxonomy's "green economic activities" for the Principles' "green projects" thereby providing certainty and potentially obviating "greenwashing" accusations. However, the high standard set by the Taxonomy may not suit all parties.

In relation to reporting, both sets of LMA principles are relatively light on obligations to provide information and leave this up to the parties to negotiate. This is understandable for a voluntary initiative. However, as a result of the disclosure regulations, a significant part of the financial industry will need to start gathering data on green assets within their portfolios. Whilst there will be increased back office requirements to manage this, these information requirements will also land on the companies and borrowers that own or operate the underlying assets. As such, it will not be a surprise if a greater information burden is placed upon borrowers and their advisers in order to satisfy these disclosures. However, if the entire financial sector moves towards this one standard, the reporting burden on borrowers may well reduce over time.

As for **standard loans**, it is possible that we could see the disclosure regulations influencing information covenants and reporting provisions in non-green loan agreements across the board for the same reasons. It is interesting to note that, in theory, a loan asset could be taxonomy-aligned although it does not adhere to the green loan principles. However, in the interest of uniformity and secondary market reasons, we would hope that all taxonomy-aligned loans are documented in line with the LMA's guidance.

Market Practice

As financial institutions are required to report on their compliance with the Taxonomy, they are likely to want to bring certain assets (and reporting on those assets) into line with the Taxonomy. For this reason, we can expect that the Taxonomy and Disclosure Regulations will begin to mould market practice.

In parallel with this, there are a myriad of commitments which have been made by banks to advance green loans and withdraw from markets which have an adverse effect on the environment. These commitments amount to many billions across the loan market, and it is likely that these ring-fenced monies will remain available as the reputational damage of reversing on these commitments would be too great. The Taxonomy could provide a common market standard method of evidencing that institutions have met these objectives and obviate "greenwashing" accusations. Indeed, the ultimate goal of the Taxonomy is to render it unacceptable to call something "green" if it does not meet with its conditions.

Availability of Capital and Pricing

While banks will currently be focused on helping borrowers get through short term issues, as business begins to resume, it will be interesting to see whether there is a rush to secure earmarked green funds by companies seeking capital in a difficult market.

In terms of pricing, one consequence of finalising the Taxonomy is that it can now be used by regulators to differentiate between assets for capital adequacy purposes. This principle has been hotly debated within the EU, with some arguing that there is no evidence to show that applying a lesser capital adequacy requirement to green assets will necessarily result in more of those financial products being generated by financial institutions. Nevertheless, the Bank of England is examining whether to penalise polluting assets if it can be proved that carbon emissions weaken credit quality. It remains to be seen what approach will be taken by regulators and what knock on effect this has on the loan market's modelling of risk. Meanwhile, the pricing debate remains centred on whether financial institutions are, or should be, pricing green loans in a manner that incentivises borrowers to pursue green projects, largely on the basis that they are "better" quality assets.

A UK market divergence?

The UK government has stated that Brexit does not mean that the Taxonomy will not be relevant for the UK. Aside from the fact that there are so many significant European financial players within the UK market which will need to comply with the Taxonomy and related disclosure directives, the government, under the auspices of the Green Finance Strategy, has committed to creating a framework that is at least as stringent as the Taxonomy in order to keep in step with the EU.

Observations

Politics, Business and the Regulatory Landscape

From a political perspective, the Taxonomy sits within a wider framework called the EU Green Deal which seeks to ensure that the EU is carbon neutral by 2050. Pursuant to this, **EUR 1tn in public and private funds is to be invested into climate related activities over the next decade**. This could be seen as a stimulus package aimed at infrastructure, construction and real estate. There is also a circular economy limb to these policies and the European Investment Bank will be using the Taxonomy to identify projects that it can invest into. In the UK, similar carbon neutral commitments have been made which will require a similar stimulus. The Green Finance Strategy points in the direction of a Green New Deal programme to deliver low carbon infrastructure and an energy efficient makeover of housing stock in the medium term.

In terms of regulation, it seems that the Taxonomy is gaining traction beyond regulators in Europe. For example, we understand that Russia's central bank plans to adopt the EU Taxonomy. Many central banks are already working on regulation that treats climate change as a systemic risk to financial systems.

This will mean that corporate governance regulations, rating agencies, banks, insurance companies and asset managers etc and their advisers will also have to integrate the Taxonomy into their analysis frameworks and in that vein, it is worth noting that the "Network for Greening the Financial System" was recently set up by the big 4 accountancy firms.

Turning to business, prompted by and despite recent events, business leaders across the board continue to make commitments to more sustainable business practices. Consider Shell, for example, who at a time of negative oil prices decided to increase its commitments to green initiatives.

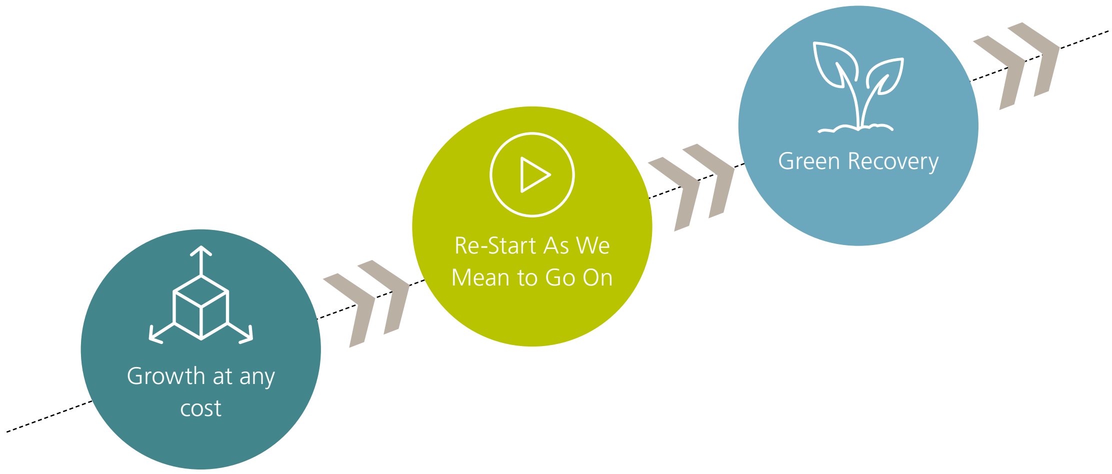
Amazon's Jeff Bezos has committed a whopping USD 10bn to fighting climate change. Accountancy firms and law firms like our own are also making net zero carbon commitments.

Other influences and pressures cement the need for a Taxonomy that facilitates genuine green investments. It is worth noting that Amazon's outsized donation was probably prompted by the Amazon Employees for Climate Justice campaign which last year demanded that Amazon reduce its emissions footprint. Similarly, there are NGOs, individuals and activist shareholders all keen to hold organisations to account for their lack of green or sustainable credentials through social media, direct action and litigation.

The "New Normal"

How might the financial sector respond to the Taxonomy as business resumes?

Here we consider three scenarios, with the first and second encapsulating the "growth v green" debate.



1. Growth at any cost

In this scenario, green initiatives are seen as a "nice to have" in a post pandemic recessionary economy. Globally, there would be fewer commitments and reduced regulatory oversight, given the demands on government resources that need to be dedicated to a post Covid-19 recovery generally. That would be understandable, and there is good evidence to show that following previous economic challenges, industry has tried to ramp up production to catch up for lost time. However, a fly in the ointment here will be the risk of litigation. Furthermore, in a growth at any cost scenario, the Taxonomy does not gain the traction it needs in political and business circles to become an effective mechanism to facilitate a transition to a greener economy, and the Paris Agreement targets aren't met.

2. Green Recovery

On the other end of the spectrum, all the regulatory possibilities outlined in this document at the central bank and policy levels are quickly articulated and come into being in order to facilitate compliance with the Paris Agreement Targets. This gives birth to a new chapter in economic growth. Moving in this direction would involve the public sector re-directing the private sector using the Taxonomy as the reference point to be achieved through a mixture of carrot and stick mechanisms. The private sector would voluntarily opt in to become more sustainable in order to take "control" over the "climate-change related economic shock" that has been predicted.

There have been calls from certain quarters that bail out monies provided to the private sector during this crisis should include "green" conditionality, particularly where state aid rules have been relaxed in order to permit such assistance. Some commentators have also suggested that this might be a "creative destruction" opportunity for governments that allows them to shape a carbon neutral economy of the future. If this approach prevails, the Taxonomy will likely play a key role in setting the targets to be met.

3. "Re-Start As We Mean to Go On"

In this last scenario we continue to see a gradual but definite "mainstreaming" of sustainability (or ESG) principles, and growing interest in sustainable assets across the market generally. Our observation of this sector has shown that the property market, for example, is gradually catching up with the views taken by sustainable property funds that were cutting edge outliers 10 years ago. In short, in this scenario sustainability remains on the agenda informing discussions, and perhaps influencing commercial decisions. After all, lenders want to lend to businesses that are sustainable (in the widest sense) in the long term. If this middle scenario obtains, the Taxonomy will become useful but not necessarily dominate in the market.

Conclusion

The finalisation and implementation of the Taxonomy is important because it can be used to eliminate the confusion that has existed in the market as to exactly "what is green?". However, there are a number of other questions to be addressed by governments, regulators and the financial sector relating to the value and treatment of green or sustainable lending in order to achieve the Taxonomy's ultimate goal of facilitating the transition of our present economy into a carbon neutral one.

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