



REPORT

Green taxonomy in Ukraine

2022

Establishing green finance infrastructure

PREPARED BY
Elina Toteva



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Kyiv
2022

CONTENTS:

- I. INTRODUCTION3
- II. PART I: EXISTING TAXONOMIES FOR GREEN PROJECTS WORLDWIDE8
 - A. The European Union Green Deal package: the path to a more regulated and transparent sustainable finance8
 - B. Russia, China and Singapore: examples of the Eastern European and Asian approaches to green taxonomy 12
 - C. Canada and Mexico: North-American examples for development of taxonomies for sustainable finance 19
 - D. Chile and Columbia: examples of how emerging countries are considering sustainable finance while tackling difficult domestic economic issues24
 - E. South Africa: a transition to an equitable, resilient, low-carbon green economy28
- III. PART II: ANALYSIS OF INVESTMENT CLASSIFICATIONS QUALIFIED AS SUSTAIANBLE FINANCING.....30
 - A. Drivers of ESG factors at investor and company level providing knowledgeable concepts of meaningful investments33
 - 1) ESG factors and the Corporate Social Responsibility (CSR) policies at corporate level: a key element for green growth in capital markets33
 - 2) Greenwashing and sustainability challenges: how to address this phenomenon?36
 - 3) Identification of environmental, social and governance (ESG) factors: material mapping38
 - B. ESG factors for sustainable investing enhanced by international non-governmental guidelines and recommendations and reporting standards41
 - 1) Principles and recommendations for responsible investment developed by investors for investors41
 - 2) International reporting standards: investors are seeking transparency and measurable impact about their sustainable investments45
- IV. PART III: REGULATION (EU) 2020/852 ON SUSTAIANBLE ACTIVITIES AND EU LEGAL ACTS RELATING TO GREEN PROJECTS IMPLEMENTATION.....52
 - A. The European Union acting as a pioneer by establishing a clear and transparent framework for sustainable investments in the financial sector55
 - 1) The EU Taxonomy Regulation55
 - 2) The Sustainable Finance Disclosure Regulation (SFDR).....61
 - B. Other European proposal, recommendations and guidelines relating to sustainable investments within the European Union67
 - 1) EU Green bond standard67

	2) EU Regulation establishing EU Climate-Transition Benchmark	70
	3) Proposal for a new EU Corporate Sustainability Reporting Directive ...	73
V.	PART IV: WORLD BANK RECOMMENDATIONS FOR DEVELOPPING NATIONAL GREEN TAXONOMY	76
	A. General approach in developing national green taxonomy	78
	1) Identification of strategic environmental goals	79
	2) Selection of environmental objectives	79
	3) Identification of sectors and investments that could achieve environmental objectives.....	81
	4) Evaluation and selection of investments supporting environmental objectives	81
	5) Identification of the potential users and beneficiaries of the green taxonomy	82
	6) Identification and clear description of reporting guidelines	82
	B. Identification of key components of the development of a national green taxonomy	83
	1) The role of the users and main actors of a reliable national green taxonomy	84
	2) Key implementation considerations of the World Bank guidelines	85
	3) Principals and processes to be followed when developing national green taxonomy	86
VI.	PART V: RECOMMENDATIONS FOR UKRAINE	88
	A. To designate principals specifically focused on environmental goals consistent and aligned with the Paris Agreement (Country Action Plan for Sustainable economy)	92
	B. To implement a clear and consistent taxonomy legislation embedding realistic future pathways to reach sustainability goals (Ukrainian Green Taxonomy)	94
	C. To implement a clear and consistent regulatory framework providing transparency and disclosures obligations at the company and investors' level (Disclosure of non-financial information).....	95
	D. To ensure that an appropriate national legislation is implemented with regard to financial products relating to sustainable capital markets such as green bonds (Green Bonds Standard)	97
	E. To associate all actors of the financial sector to the implementation of green finance	97
VII.	PART VI: CONCLUSION	99

I.INTRODUCTION

1. Climate change actions and measures are not a new topic for governments and economic sectors. Today, governments are facing challenges in enhancing economic and social development in light of resource constraints and risks set forward by climate change and environmental degradation. The green finance is the path towards an inclusive green economy that achieves resource efficient and climate resilient and sustainable economic development. This is, now, our reality, individuals, corporations and governments do not have any other choice than considering environmental, social and economic factors shifting to sustainable development.
2. This global awareness is not new. The origins of the recognition and consideration of climate change go back several decades from now. The starting point of the climate change consideration could be placed in 1979 with the First World Climate Conference, held in Geneva, Switzerland. This Conference was attended by more than 300 specialists from 53 countries and 24 international organisations from a wide range of disciplines including agriculture, water resources, fisheries, energy, environment, ecology, biology, medicine, sociology and economics.
3. In 1992, at the Earth Summit in Rio de Janeiro, Brazil, the United Nations Framework Convention on Climate Change was opened for signatures. It was followed by the United Nations Convention on biological diversity and the United Nations Convention to combat desertification.
4. In 1995, the first Conference of the Parties (COP1) took place in Berlin, Germany. The Conference did not result in concrete results providing climate protective measures, but the 120 governments present acknowledged the gravity of the situation and the need to reduce greenhouse gas emissions from human activities.
5. The Kyoto Protocol of 1997 was a significant milestone. The carbon dioxide quota systems used in Europe, China, Korea and North America were dedicated tentative to control the carbon dioxide emissions better, but they were not enough. In 2005, the first meeting of the parties to the Kyoto Protocol took place in Montreal, Canada. It is the year of the entry into force of the protocol, which called for reducing the emission of six greenhouse gases in 41 countries. The European Union had to reduce its emissions to 5.2% below 1990 levels during the period from 2008 to 2012. It was widely claimed as the most significant environmental agreement ever negotiated, but finally it did not meet the success of effectiveness that it was promising.

6. In 2010, Cancun Agreements was drafted and largely accepted at COP16. Through the multiple agreements of countries, they made their official pledges for carbon dioxide emission reduction. This was an example of the largest collective effort worldwide to reduce harmful emissions in a mutually accountable way.

7. In 2012 was held the United Nations Conference on Sustainable Development in Rio de Janeiro, Brazil. Unfortunately, it did not have the expected success as the most powerful government leaders could not attend. However, this Conference integrated for the first time the concept of Green Economy and Green Growth. These concepts emphasised the need to integrate the environment and economic growth through channelling 2% of capitals of the global GDP into green investments. As a follow-up of Rio's Conference, the international community met again in New York, the same year, during the United Nations Development Summit to adopt a new development agenda for the period of 2015-2030. The United Nations member states agreed on a new plan called "*2030 Agenda for Sustainable Development*", which consisted in political declarations and strategies, but above all the proclamation of the 17 Sustainable Development Goals (SDGs). This was one of the starting points of referring to SDGs as a target mission while implementing new sustainable development approaches in traditional economies around the world.

8. In 2015, COP21 held in Paris, France was the second biggest achievement on the international scene of climate change consideration. It had the same ambitious goal and allowed to bring together many governments' representatives, who successfully agreed to set ambitious targets for the reduction of carbon dioxide emissions in the atmosphere. However, the efforts of the governments following COP21 were not enough. They were not able to reduce the harmful emissions globally. The main factor of this difficulty was the different stage of economic, social and governance development of the different countries and their economic and political strategies.

9. The first time this happened was in the first semester of 2020 when the world experienced the first shock of the Covid-19 spread worldwide. For a couple of weeks, carbon dioxide emissions went down in a way that nobody could imagine. The historical decrease had a marginal impact on the total volume of carbon dioxide already in the atmosphere generating the global warming, but it was a significant indicator of the human carbon print. What is now important and essential is to learn the lessons from the Covid-19 crisis regarding the reduction of the global warming and to put in place the most concrete actions that will allow governments, corporations and individuals to realise the most important shift within the global community of actors for sustainable development.

10. In 2021, the latest COP26 was held in Glasgow, Ireland, but did not bring a significant achievement in climate change enhanced consideration. Therefore, the ambitions of some countries to further accelerate the climate change adaptation and mitigation process were not met.

11. Nevertheless, a growing number of countries and regional authorities around the world are demonstrating an active approach to climate change awareness and are looking to provide value to the “*Green growth*” in achieving a sustainable economic, environmental and social development. The Green growth is the response to the adverse climate changes and the global warming process around the world. Thus, governments have to implement appropriate Green growth policies and strategies to tackle this important problem. Thus, the green growth is the process of economic and social development based on a more sustainable pathway toward a prosperous, inclusive and climate-resilient future. Accordingly, governments have a choice, either to chart new and more sustainable development of their economies or to keep conventional form of development that deepen today’s environmental and social problems and create ecological debts for the future. On the first path lies the promise and potential of the Green growth, the better and more sustainable future for our and next generations.

12. Today, we have a better understanding of the negative impact of transportation, electricity, and industrial productions. Governments and local authorities understand the relation between productions and carbon dioxide emissions. This knowledge gives them early warnings of needed adjustments and show the direction of the transition to save our planet.

13. The Green growth is also becoming an attractive opportunity for countries around the world to achieve poverty reduction, environmental protection and resource efficiency in an integrated way. Green growth strategies generate policies and programs that deliver these goals within the same framework of actions. They accelerate investment in resource efficient technologies and new industries, while managing costs and risks for corporations, communities and individuals. Likewise, the Green growth is requiring both public and private sectors of a country to mainstream all economic, social and governance activities in a more sustainable way.

14. To better understand the green growth and the transition to a more sustainable development, it is important to understand basic concepts of sustainable finance. Hence, one of the most popular acronyms used while talking about climate finance or green finance is the ESG acronym. It stands for E (Environmental), S (Social) and G (Governance). These are the three letters, but also the three pillars of the sustainable finance leading to a Green growth and a more resilient

future. Currently, ESG considerations are more and more applied in the financial sectors around the world and governments of countries are looking to include ESG considerations in their national classification system giving legal and regulatory framework of their sustainable finance policies. The acronym is globally known but however due to the difficulty to summarise and include all the topics that need to be included, there is no official definition internationally recognised. When it applies to finance, ESG dimensions lead to sustainable finance and entail all the information, disclosure and integration required by the integration of the ESG dimension. The extent, transparency and metrics applied and used have to be accessible to institutional and professional investors to be better prepared to take informed decisions about their current and future investments. In this respect frameworks, standards, and guidelines are increasingly being developed for investors and companies to implement them in their investment strategies and decisions. In other words, sustainable finance, where ESG dimension is applied, can be described as all financial services used to finance the transition of an economy towards a more sustainable and equitable future. Thus, sustainable finance refers to financial decisions that not only seek financial return, but also consider its non-financial impact and the environment, social and governance aspects to achieve green and growth by a sustainable way of investing.

15. Therefore, the ESG can be defined as:

- “E” (environmental) which refers to how the investors can contribute to protecting our planet, providing that their decisions are foreseen to reduce the carbon dioxide emissions, support energy efficiency, fight against water scarcity, tackle illegal deforestation, protect biodiversity or promote circular economy;
- “S” (social) applies to investors, who could create a socially responsible economy, by pursuing protection of human rights, such as no child labour, no forced, bonded or compulsory labour, no human trafficking and many others;
- “G” (governance), refers to how investors can contribute to establishing a fair governance of public and private institutions. They can help improve transparency, disclosure and traceability in the supply chain, promote diverse board structure, support transparent and equitable policies etc.

16. The acronym is now deeply rooted and linked to sustainable finance and even the European Union’s definition of sustainable finance encompasses the ESG dimension:

“Sustainable finance refers to the process of taking environmental, social and governance (ESG) considerations into account when making investment decisions in the financial sector, leading to more long-term investments in sustainable economic activities and projects. Environmental considerations might include climate change mitigation and adaptation, as well as the environment more broadly, for instance the preservation of biodiversity, pollution prevention and

the circular economy. Social considerations could refer to issues of inequality, inclusiveness, labour relations, investment in human capital and communities, as well as human rights issues. The governance of public and private institutions – including management structures, employee relations and executive remuneration – plays a fundamental role in ensuring the inclusion of social and environmental considerations in the decision-making process. In the EU's policy context, sustainable finance is understood as finance to support economic growth while reducing pressures on the environment and taking into account social and governance aspects. Sustainable finance also encompasses transparency when it comes to risks related to ESG factors that may have an impact on the financial system, and the mitigation of such risks through the appropriate governance of financial and corporate actors”¹.

17. This is the reason why the European Union has developed an ambitious program of actions called “*Green Deal*”. This program includes a package of actions and measures meant to be the regulatory input by a top-down approach of the European Union to Member States in order to stimulate and pursue a sustainable development transformation. One of the regulatory measures established by the European Union is a particular tool called taxonomy, which is the current legal basis of all the activities considered as sustainable and compatible with the ESG dimension from European Union’s perspective. Consequently, other countries have already started to develop similar regulatory tools that will help them to guide all sustainable investments in the public and private sectors to more sustainable economies. Therefore, this final report will focus on material findings and recommendations regarding the transition of a green economy and the green recovery of Ukraine. The analysis of the existing taxonomies for green projects worldwide (II) and the investment classifications qualified as sustainable financing (III) will provide for an initial mapping of the regulatory framework used to regulate green projects and sustainable investments by different countries around the world. The EU Regulation (2020/852) (IV) and the World Bank guide will provide useful example and recommendations of how to achieve a robust green taxonomy framework necessary for the transition from traditional to a sustainable economy (V). Ukrainian authorities will be provided with relevant recommendations regarding the future development of their domestic green finance regulatory framework (VI).

¹ https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/overview-sustainable-finance_en

II.PART I: EXISTING TAXONOMIES FOR GREEN PROJECTS WORLDWIDE

A. The European Union Green Deal package: the path to a more regulated and transparent sustainable finance

18. Climate change and environmental degradation are a real threat to Europe and the world. To overcome these challenges, the European Green Deal is intended to transform the European Union into a modern, resource-efficient and competitive economy, ensuring (i) net-zero emissions of greenhouse gases by 2050 and (ii) economic green growth decoupled from resource use. The European Green Deal is also the lifeline out of the Covid-19 pandemic. The European Commission adopted a set of proposals to make the EU's climate, energy, transport and taxation policies fit for reducing net greenhouse gas emissions by at least 55% by 2030, compared to 1990 levels. Thus, sustainable finance has a key role to play in delivering on the policy objectives under the European Green Deal as well as the EU's international commitments on climate and sustainability objectives. This will be supported by channelling public finance and private investments into the transition to a climate-neutral and resilient, resource-efficient and fair economy, as a meaningful step to a next generation sustainable development. Sustainable finance will help to ensure that investments support a resilient economy and a sustainable recovery from the impacts of the Covid-19 crisis. Thus, the European Union strongly supports the transition to a low-carbon, more resource-efficient and sustainable economy and has been at the forefront of efforts to build a financial system that promotes green growth.

19. The response of the ambition of the European Union was the release of the “*Action Plan for Sustainable Growth*” established by the European Commission. It is a major policy initiative and aims to promote sustainable investment across 27 Member States of the European Union. The Action Plan stands for ten reforms in the following fields:

- a) Direct capital flows towards sustainable investments to achieve Green (sustainable and inclusive) growth:
 - Establishing an EU classification system for sustainable activities;
 - Creating standards and labels for sustainable financial products;
 - Fostering investments in sustainable projects;
 - Incorporation sustainability when providing investment advices;
 - Developing sustainability benchmarks;
- b) Mainstreaming sustainability into risk management:
 - Better integrating sustainability in ratings and research;

- Clarifying institutional investors and asset managers' obligations;
- Incorporating sustainability in prudential requirements;
- c) Foster transparency and long-lasting in financial and economic activities:
 - Strengthening sustainability disclosure and accounting rule-making;
 - Fostering sustainable corporate governance and decreasing the volume of short-term investments in capital markets.

20. All these goals have to be put in place to achieve a sustainable shift in the European Union economy. In May 2018, the European Commission adopted a package of measures implementing several key actions announced in its Action Plan on sustainable finance. The package includes:

a) EU Taxonomy for sustainable finance, which is a classification system establishing a list of environmentally sustainable economic activities which enable scaling of sustainable investments. It would also provide appropriate and clear definitions to corporations, investors and policymakers on which economic activities can be considered environmentally sustainable. The EU taxonomy is expected to create security and to reduce the risk for private investors from greenwashing. It will help corporations and investors to plan transactions, mitigate market fragmentation and eventually shift investments in more sustainable activities. Hence, the EU taxonomy is seen as a first step to channel a consistent volume of private sector investments to more sustainable activities;

b) Sustainability related disclosure obligations, which include a proposal for a regulation relating to sustainable investments and risks amending EU Directive 2016/2341. It lays down sustainability disclosure duties for manufacturers of financial products and financial advisers toward end-investors. It does so in relation to the integration of sustainability risks by financial market participants and financial advisers in all investment processes and for financial products that pursue the objective of sustainable investments. In addition, the co-legislators added disclosure obligations regarding the adverse impacts on sustainability matters, investments and financial products. The disclosures obligations also require financial market participants and financial advisers to consider negative externalities on environment and social equity of the investment decisions/advice they perform or provide. The reason is that investment decisions and financial advice might cause, contribute to or be directly linked to negative material effects on environment and society, regardless of whether the investment strategy pursue a sustainable objective or not, such as investments in assets that pollute water or cause coastal erosion, to ensure the sustainability of investments. It consists of

a directly applicable regulation introducing additional disclosure requirements to the existing elements of relevant sectoral legislations through self-standing regulatory provisions providing full harmonisation, cross-sectoral consistency and regulatory neutrality;

c) In May 2018, the European Commission put forward a proposal for a regulation creating two types of low carbon benchmarks, requesting ESG disclosure requirements for benchmarks. The underlying assets for these new benchmarks will have to be selected, weighted and clearly identified in such a manner that the resulting benchmark portfolio is either on a decarbonization trajectory or its carbon emissions are aligned with the objectives of the Paris agreement;

d) The European Green Bond standard was announced in the Green Deal Action Plan by the European Commission. It should establish an EU green bond standard, which will be a voluntary standard to help scale up and raise the environmental ambitions of the green bond market. Once it is adopted by co-legislators, this proposed regulation will set a gold standard for how corporations and public authorities can use green bonds to raise funds on capital markets to finance ambitious large-scale investments, while meeting tough sustainability requirements and protecting investors. This will be useful for both issuers and investors of green bonds. Issuers will have a robust tool to demonstrate that they are funding legitimate green projects aligned with the EU taxonomy. And investors buying the bonds will be able to more easily assess, compare and trust that their investments are truly sustainable, thereby reducing the risks posed by greenwashing. The new green bond standard will be open to any issuer of green bonds, including corporations, public authorities, and also issuers located outside of the European Union. There are four key requirements under the proposed framework:

- Taxonomy-alignment: the funds raised by the bond should be allocated fully to projects that are aligned with the EU taxonomy;
- Transparency: full transparency on how the bond proceeds are allocated through detailed reporting requirements;
- External review: all European green bonds must be checked by an external reviewer to ensure compliance with the Regulation and taxonomy alignment of the funded projects;
- Supervision by the European Securities Markets Authority (ESMA) of reviewers: external reviewers providing services to issuers of European green bonds must be registered with and supervised by the ESMA. This will ensure the quality of their services and the reliability of their reviews to protect investors and ensure market integrity.

21. Consequently, EU Taxonomy paper is one of the most important regulations released by the European Commission with regard to sustainable finance. For quite some time, one of the most pressing issues in sustainable finance was how to define it, as it means different things to different people. The EU Taxonomy is intended at providing solution to this challenge, because it is perceived as a tool at the disposal of investors to understand if an economic activity of a given company is truly sustainable and to what extent it covers one or more sustainable objectives. The EU Taxonomy is also a tool for guiding companies, private and institutional investors to achieving a low carbon economy. Setting a common and clear language between investors, issuers, policymakers, promoters etc. will help investors assessing whether investments are meeting environmental standards and are consistent with high level policy commitments such as the Paris agreement on Climate Change. Ultimately, the EU Taxonomy will help capital flows to be directed towards low-emissions economic activities that will help decarbonise the economies, but most of all to decrease the carbon dioxide emissions on the planet. Such regulation will help the European Union to reach its 2030 climate targets and the ultimate target of net-zero greenhouse gases emissions by 2050.

22. The EU Taxonomy came into force in July 2020² and is establishing a framework of four overarching conditions an economic activity has to meet to qualify as environmentally sustainable:

- It must contribute substantially to at least one of the environmental objectives;
- It must “*do no significant harm*” (DNSH) to any of the other environmental objectives;
- It must be carried out in compliance with minimum social and governance safeguards;
- It must comply with technical screening criteria to be adopted under the regulation.

23. The six environmental objectives in the EU Taxonomy are:

- Climate change mitigation;
- Climate change adaptation;
- The sustainable use and protection of water and marine resources;
- The transition to a circular economy;
- Pollution prevention and control;
- The protection and restoration of biodiversity and ecosystems.

² Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

24. For each of the eligible economic activities, the EU Taxonomy provides detailed technical screening criteria that must be complied with in order to determine that an activity is taxonomy-aligned. This is quite a concert step forward because the financial and capital markets were relying so far on ESG scores that were developed by different companies and agencies based on different criteria without a common framework or a relative coherence. The activity-level focus is something new as it demands a deeper level of granularity to access the eligible activities that companies undertake to invest in. This section will be further developed in a separate report, that will be a part of the present developments.

B. Russia, China and Singapore: examples of the Eastern European and Asian approaches to green taxonomy

1) Russia

25. The national strategy of Russia for medium to long-term growth will be greatly affected by how well its policies integrate environmental and natural resource management into economic planning. Natural resources use is critical for Russia's economic development and is an important source of income. The natural resource management and improvements in environmental sustainability are among the key requisites for economic growth and social progress of Russia.

26. The Government of the Russian Federation has adopted a decree approving the "*Criteria for Green Development Projects in the Russian Federation*"³ (n° 1587 of 21 November 2021). The document defines *criteria for green projects* (taxonomy of green projects), and *criteria for sustainable adaptation projects* (taxonomy of sustainable adaptation projects), The regulatory provisions of the decree are providing criteria for the system of verification of green projects in Russia and the financial instruments for recognising them as financial instruments of sustainable development. The definition of "*green*" and "*sustainable development projects*" is set by the objectives and key thrusts of sustainable (including green) development of Russia and approved by another decree⁴ of 14 June 2021, (n° 1912). This decree also establishes the requirements, conditions and procedures for ascertaining that an investment project is compliant with the criteria of the national taxonomy and the concept of sustainable development. It further establishes the principles of the national infrastructure for responsible investment. Among the priorities are the reduction of activities with negative effect on the environment, in particular by reducing emissions of pollutants and greenhouse gases, increasing resource efficiency and energy storage.

³ <http://static.government.ru/media/files/3hAvrl8rMjp19BApLG2cchmt35YBPH8z.pdf>

⁴ <http://static.government.ru/media/files/sMdcuCaAX4O5j3Vy3b1GQwCKfa9lszW6.pdf>.

27. The Russian taxonomy for transition and sustainable projects is based on national peculiarities and the specifics of the Russian economy. It is meant to encourage corporations, especially those in the energy sector to switch to more environmentally friendly production methods and to invest in new technologies for less polluting activities. When developing the taxonomy, the standard was developed taking into account national priorities and international best practices (ICMA, CBI, IDFC⁵, European Union) to ensure that the Russian taxonomy as a whole meets the EU taxonomy's criteria and components. This approach was followed to ensure that both taxonomies will converge and facilitate European investors to come on the Russian capital market.

28. The Russian taxonomy covers the following sectors: waste management, energy, construction, industry, transport, water supply, public utilities and agriculture. Energy criteria include scientifically grounded electricity production thresholds based on the recommendations of the EU Technical expert group on sustainable finance (TEG) for the EU taxonomy of sustainable operations. A threshold of 100g CO₂e/kWh/year for electricity generation is the cornerstone of the EU taxonomy. Thus, the adoption of this threshold in Russia for gas-fired power generation is a significant step, which could draw the attention of international investors, willing to invest in Russia. It is also a sign that the Russian taxonomy is in line with the global definition of green investments and is not only driven by interests in the production of fossil fuels.

29. The transition taxonomy requires Russian companies to comply with disclosure obligations and to inform their investors on the efforts of the management of climatic risks. It is also demonstrating that the Russian government is willing to develop credible transition pathways to provide guidance to Russian companies on how they can achieve the net-zero greenhouse gas emissions target by 2060 set by the Russian government.

30. The Russian taxonomy is also identifying different categories of projects that are covered by the rules. Such projects could be either green or sustainable projects; The difference is that unlike the green projects the sustainable projects do not need to comply with international instruments agreed by the Russian Federation in the field of climate change adaptation and mitigation. However, the sustainable projects need to comply with the Russian priorities in the field of ecology defined by the objectives of sustainable development in Russia. The Russian taxonomy is also referring to “*other*” projects, considering the fact that social or social-linked projects could be covered under these provisions of the rules. This category of projects will be further developed by the government in a separate piece of rules.

⁵ <https://www.idfc.org/>.

31. However, the Russian taxonomy does not address other aspects of the EU taxonomy for example there is no any provisions relating to "*Do No Significant Harm*" concept developed by the EU taxonomy. It also includes nuclear power, which is not the case of the EU taxonomy at this stage of development.

32. Further, the implementation of green and sustainable projects in Russia will be supported by the establishment of appropriate financial instruments, which should be backed by the Central Bank of Russia. The use of natural gas was a focal point in the development of the Russian taxonomy, because it is one the most important source of income for the country. Accordingly, the Russian government demonstrated the will to coordinate its taxonomy rules with the European Union but this approach found its limits in the particularity of Russia's economic and energy prerogatives.

33. The United Nations international organisation in charge of responsible investing, also known as the Principles for Responsible Investment (PRI), took part in the project published in April 2020⁶ and provided some comments and detailed recommendations⁷. PRI stressed the point that the classification principle proposed in the Russian taxonomy focused on the identification of implementation areas of green and sustainable projects with a variety of sub-industries, while the EU taxonomy classification system is mostly focused on the identification of economic activities.

34. The comments of PRI were also including a point on the implementation the green projects according to the Russian taxonomy, which does not contain a distributional approach with regard to the climate change adaptation and mitigation differentiation. It was also noted that the main focus areas of sustainable projects in the Russian taxonomy do not include technical criteria, metrics and thresholds for projects that can be classified as sustainable in these focus areas. These criteria reduce disadvantages for attracting investment in sustainable development projects on the domestic market, clarify the alignment of investments in sustainable development objectives and create conditions for cross-sector financing. Thus, the lack of technical criteria for the identification of sustainable projects will not allow project and asset managers to provide investors with a clear and meaningful information about how SDGs are met.

2) China

35. China has multiple policies and programmes in the area of green and climate finance. Five pilot areas for green finance innovation were set up in 2017 in Guangdong, Huizhou, Jiangxi,

⁶ <https://xn--90ab5f.xn--p1ai/files/?file=1cc7ffec701762260d130988dafca0cf.pdf>

⁷ https://dwtyzx6upklss.cloudfront.net/Uploads/x/t/o/priconsultationresponse_russiantaxonomy_rusfinal_366932.pdf

Zhejiang and Xinjiang. In other regions, seven regional carbon market areas also were launched in 2013 and 2014, and a national carbon market in 2017. In terms of financial regulation, China has three main frameworks for green finance definitions. The core framework is the “*Guiding catalogue for the green industry*”. Originally established in 2016, it was lastly updated in 2020. China introduced separate definitions for green credit and green bonds. What is often referred to as the “*Chinese taxonomy*” is the Green Bond Endorsed Project Catalogue⁸, a list of projects supported by green bonds, which is a voluntary standard for the Chinese green bond market.

36. China's “*green*” taxonomy refers to the financial contributions made to the economy, with the aim of (i) improving the environment, (ii) considering the climate change and (iii) an appropriate and efficient use of natural and energy. All activities qualifying under this scope should include financing, investments and risk management of projects in areas such as environmental protection, energy conservation, clean energy, green transport and green buildings. The Chinese taxonomy is largely aligned with the EU taxonomy, but unlike the latter, the Chinese taxonomy is applied only to the national assets of green bonds. In terms of compliance, the Chinese taxonomy provides a residual list of activities that meet green and sustainable definitions.

37. Further, the Chinese taxonomy provides a detailed white list of accepted economic activities and projects. A total of 204 types of activities from the following categories are considered as fully compliant with a white list of activities such as activities providing for (i) energy-saving and environmental protection industry, (ii) clean energy and clean industry production and (iii) ecology, new-tech infrastructure together with “green” services. Different thresholds are set on the basis of various national and international standards set by the People's Bank of China.

38. The China banking and insurance regulatory commission issued green lending guidelines in 2012, green credit statistics in 2013 and key performance indicators (KPIs) for the implementation of these guidelines in 2014. Banks are required to report every six months on the balance of loans designated as “*green*” and to report on the impact of these loans on energy savings and reduction of waste and water savings. Green credit sectors are agriculture and forestry, energy and water and nature conservation, environmental rehabilitation and disaster prevention projects, waste recycling, recycling and pollution prevention, clean energy, clean water rural projects, green buildings and green transport. A catalogue of projects supported by green bonds became effective in June 2021 and applies to green bonds issued by financial institutions. This latest update of the catalogue is a significant progress in the unification of domestic green finance standards in China. The latest version of the catalogue has four-tier

⁸ <http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/4236341/index.html>

structure. The first three tiers correspond to the green industry. The fourth tier includes more detailed descriptions of specific economic activities.

39. Thus, the Chinese taxonomy is primarily a tool for regulating the green bond market and safeguarding the environmental benefits of the financing projects and is mandatory for all green bond issuers, including all financial institutions, corporations and state-owned enterprises, third-party appraisal agencies and regulators. The aim is to clearly identify projects eligible for green bonds and reduce the possibility of non-green projects being financed with green bonds, enhance the credibility and reputation of green bonds, and further regulate the domestic market for green bonds with regard to green assets and projects. It is mainly used by financial institutions and corporations to issue green bonds on the Chinese capital market.

40. Finally, the Chinese taxonomy is meant to structure the domestic financial market, but should in the near future also take into consideration other countries' taxonomies, because the Chinese investors are investing in assets under several jurisdictions and thus providing financing to different kind of projects, including international sustainable projects.

3) Singapore

41. In January 2021, the Green Finance Industry Taskforce of Singapore (the "**Taskforce**") published its proposal for a Singaporean taxonomy⁹. The Taskforce is an industry group comprising representatives of Singapore-based financial institutions and is convened by the Monetary Authority of Singapore (MAS). The proposal outlines the key challenges that Singapore financial sector and national economy will face in the near future. These key challenges are (i) the targets of reduction of carbon dioxide emissions agreed in the Paris agreement, that Singapore is a part of, (ii) the transition to a low carbon economy, (iii) the recognition of climate change adverse material impact on the stability of financial markets, (iv) the establishment of national regulatory framework to prevent from greenwashing and (v) the direction of capital flows into the green finance of the country.

42. Following, the core objective of the Singaporean taxonomy is to accelerate investments towards environmental objectives of Singapore, but also of other members of the Association of Southeast Asian Nations (ASEAN) by Singapore-based financial institutions. The proposal acknowledged the role of the taxonomy in spurring the growth of green financial products, preventing greenwashing by clearly defining environmentally sustainable activities and

⁹ Green Finance Industry Taskforce, "*Identifying a Green Taxonomy and Relevant Standards for Singapore and ASEAN*", Communication Paper, January 2021.

developing a common language among domestic and international market participants to facilitate international capital flows. The taxonomy proposal is framed in the context of four primary concerns: (i) international inconsistency, (ii) undue compliance burden, (iii) path dependency and (iv) insufficient coverage of the economy. Given the global nature of capital and market participants on the Singaporean capital market, there is strong emphasis that a Singaporean taxonomy must be internationally consistent and interoperable to prevent capital market fragmentation. The taxonomy should also be coupled to disclosure duties and reporting requirements. The proposal also takes into consideration and will dedicate efforts to minimise compliance burden for financial institutions. There is also a concern that prescribing strict thresholds may create a static instrument incapable of evolving in the time. The proposal recognises that an exclusive focus on “*green*” risks excluding vast majority of the economic activities. This could generate asset pricing bubbles and present systemic risks to financial stability. Finally, the Taskforce recommended designing a Singaporean taxonomy based on the structure and methodology of the EU taxonomy.

43. However, the Singaporean taxonomy should also (i) focus on sectors that are most relevant to ASEAN for economic growth and volume of carbon dioxide emissions generation (including transition activities), (ii) adjust targets and thresholds to those compatible with the growth and development in Singapore and the Asian regions, and (iii) factor in current disclosure practices and data availability in ASEAN.

44. The Taskforce proposal recommended measuring contribution against a set of environmental objectives, namely (i) climate change mitigation, (ii) adaptation, (iii) protecting biodiversity, and (iv) promoting resource resilience. To comply with the proposed taxonomy, financial activities have to demonstrate no significant harm caused to other environmental objectives, adhere to defined social safeguards and not breach any local laws. Projected reliance of ASEAN members on fossil-fuel based power and sectors like steel and aluminium for infrastructure development, imply that there is a need to not only finance technologies and activities that are proved to be green but also those that facilitate a progressive lowering of harmful emissions and negative environmental impact. Transition activities are recognised as those that “*are currently high carbon and critical to the on-going activities of domestic economy but are in transition to less carbon intensive business models*”.

45. The proposal recommends including abated gas as a transition fuel in the taxonomy together with the inclusion of activities enabling the transition, for instance low-carbon technologies in the fossil fuel sector. The proposal identifies five broad sectors to be included in the taxonomy based on their contribution to greenhouse gas emissions and economy at ASEAN level. These include

(i) agriculture and forestry/land use, (ii) construction/real estate, (iii) transportation and fuel, (iv) energy (including upstream), and (v) industry. These sectors together are responsible for 90% of ASEAN emissions and 40% of economic activity. The sectors have been mapped based on the International Standard Industrial Classification System (ISIC) and include those that are green as well as in transition. Additionally, the proposal suggests inclusion of three enabling sectors, namely (i) information and communications technology (ICT), (ii) waste/circular economy and (iii) carbon capture and sequestration (CCS). A non-exhaustive sub-sectoral mapping is included in the taxonomy proposal.

46. Further, the Taskforce recommends implementing the Singaporean taxonomy in a phased manner, acknowledging that quantitative metrics and thresholds could take time to develop. The proposal outlines a 'traffic light' system of classification of activities to commence rollout. This approach allows categorising transition activities distinctly. The classification is largely based on substitutability and implementation of green technologies available for each identified transition sector. From the context of the proposal, transition activities may be understood as those that cannot be substituted by a green alternative and are (i) either on a time-bound transition to becoming green i.e. implementing the green technology available for the sector, or (ii) making efforts to significantly lower carbon dioxide emissions in a manner that will contribute to the objectives of the taxonomy.

47. The proposal clarifies that transition activities are those that are not yet undertaking a transition consistent with a carbon dioxide emission-reduction pathway aligned with the objectives of the proposed taxonomy and Paris agreement. However, there is no clarity in the proposal on what is meant by a carbon dioxide emission-reduction pathway consistent with the objectives of the taxonomy and how the progressive emission reduction and improved environmental footprint from transition activities count towards the objectives of the contemplated taxonomy.

48. Finally, the proposal recommended development of granular quantitative criteria for transition activities to ensure time bound convergence with a well below 2-degree pathway considered as a target goal by Singapore in its path to decarbonisation of domestic economy.

C. Canada and Mexico: North-American examples for development of taxonomies for sustainable finance

1) Canada

49. The Canadian government put forward a plan to underline Canada's wish for transition called "*the Pan-Canadian Framework for Clean Growth and Climate Change*" and begun implementing key policies, the role of financial markets in driving this change has yet to be fully leveraged. The climate change challenge will not be solved by the finance but it has a critical role to play in supporting the real economy through the transition.

50. Thus, the Canadian Standard Group (CSA) is currently leading the development of a transition taxonomy as part of a national standard of Canada for transition finance. This work was initiated based on the recommendations put forward in the Government of Canada's Expert Panel on Sustainable Finance Final Report dated June 2019¹⁰. This new program will include major tasks as (i) development of the Canadian "*green and transition-oriented fixed income taxonomies*" as a national standard of Canada for transition finance, (ii) active role and leadership of Canada in the creation of a global transition finance taxonomy that is relevant for Canadian investors, corporations and policymakers and (iii) development of technical standards for sustainable finance.

51. When the future taxonomy is developed, a number of stakeholder groups in Canada will benefit from transition-related financial products and services. Corporations in Canada seeking capital for transition-oriented activities (e.g. reducing greenhouse gas emissions and their environmental footprint while advancing new technologies) will receive a true answer of their sustainable investment strategies thus preventing them from greenwashing influences. Institutional and retail investors who require transparency as an investments support to be able to securely invest in transition projects contributing to a low-carbon economy. The future transition taxonomy will definitely contribute to support Canadian financial institutions providing credit solutions, advisory services or access to capital markets to enable the transition to a low-carbon economy while also helping investors managing investment risks.

52. Given the importance of natural resources and heavy industry to the Canadian economy, Canada has both an opportunity and a challenge in meeting its own greenhouse gas reduction

¹⁰ Final report of Canada's Expert Panel on sustainable finance, *Mobilizing Finance for Sustainable Growth*, dated June 2019.

targets. It is imperative that Canada's climate change strategy includes transition-related investment opportunities that contribute meaningfully to Canadian and global climate objectives.

53. The CSA standards development process combines rigor with a transparent, balanced consensus-based approach that integrates feedback from a range of stakeholders and draws on the expertise of technical experts. National standards of Canada are developed by a technical committee comprised of a balanced matrix of experts across all relevant interest groups. The committee for the development of these standards includes representatives from Canada's financial sector (including the major banks, pension fund managers, wealth and asset managers, insurance companies, rating agencies), Canada's natural resource sectors, government and related industry stakeholders.

54. The CSA will soon release the first draft of the "*transition taxonomy*," essentially a definition-setting exercise for what kind of projects should qualify for transition financing, that will be further defined as "*sustainable*" financing. Nevertheless, Canadian financial sector remains under increasing pressure to move money away from activities causing the global warming towards those the goals of the Paris agreement allowing to keep global temperature rise well below 2 degrees.

55. Banks and investors are responding by creating billions in financing accessible to green projects, but there isn't consensus on what should qualify. This is where taxonomies come in, to come to agreement on what "*sustainable*" financing means, and also what is "*transition*" financing for projects that are on their way to sustainable but not there yet.

56. In its final report, the Expert Panel argued that the emerging international definitions of sustainable finance would exclude Canadian heavy industry and recommended that Canada creates its own definitions of "*transition*" finance so that it would be able to qualify. Sustainable finance taxonomy is a matter of public policy; therefore, it is requiring open and transparent deliberation accessible to a wide range of national actors. Hence, it appears that it is highly likely that the future Canadian transition taxonomy may sanction what is known as "*carbon lock-in*," when investing in carbon-intensive systems perpetuates or delays the transition to low-carbon alternatives.

57. Canada's current economic and industrial development is highly depending on fossil fuel energy sector. Thus, the proposed taxonomy would grant the "*transition*" label to investments that increase access and use of natural gas to replace coal. But that is not a decarbonisation process. It's merely switching dependency from one fossil fuel to another. The proposed rules

would also allow for the exploration and development of new oil and gas reserves, but no amount of creative accounting or qualification can credibly align financing for new fossil fuel expansion with climate change challenges. Investing in pollution abatement at an oil refinery may reduce carbon dioxide emissions at the refinery itself, but since 70-80% of the emissions occur at the tailpipe, although locking in those latter emissions by requiring a return on the refinery investment rather than investing in switching to low or no emission fuels.

58. It is time for Canada to put in place a reliable domestic transition taxonomy providing certainty and mitigating the risks of greenwashing in the financial sector. Moreover, the Canadian government should take the lead in this action thus providing not only a partial and weakened “transition” taxonomy but rather establishing an overall and detailed sustainable finance taxonomy. Adopting a weakened taxonomy, because of the strong dependency of fossil fuels, could stem financial flows into Canada, as major European investors will lack confidence in Canada’s compliance with international standards. It could also create difficulties for internationally invested Canadian financial institutions.

2) Mexico

59. Regulatory classification systems regarding sustainable finance and green activities are developed around the world. The Latin America countries are also following the lead of the European Union and other countries. Chile, Colombia and the Dominican Republic are currently developing their own taxonomies. The acceleration in development of local taxonomies demonstrates the interest of governments in mobilising capital flows towards sustainable and climate resilient investments.

60. Financial authorities are increasingly fostering the sustainable finance agenda in Mexico, despite having few regulatory measures in place. Most actions have concentrated on raising awareness and developing capacities of financial institutions to integrate sustainability factors in decision-making processes, thus providing investors and corporations with a better advice and reliable sustainable financial products. The Central bank of Mexico developed a good understanding of climate-related risks and their potential impact on financial markets. It is the leading actor in Mexico, which provided the initial input of the recognition of sustainable finance on the Mexican financial market.

61. In 2019, the Central bank of Mexico undertook a study to assess the degree of awareness of Mexican financial institutions regarding climate, environmental, and social related risks, as well as financial institutions’ capacities to assess and manage these risks. More than 25 credit

institutions and more than 35 asset managers and owners were involved, which was a significant share of the financial system. The study covered three main sections such as governance, strategy, and risk management practices relating to climate, environmental, social and governance risks. Results were presented in a final report called “*Climate and Environmental Risks and Opportunities in Mexico's Financial System - from Diagnosis to Action*”¹¹. The report also included a set of drivers and recommendations to better align financial flows with the development of an environmental and socially responsible agenda and low-carbon economy. The report is a call for action in particular for institutional and private investors, asset managers and board directors of financial institutions to (i) incorporate environmental and social risks and opportunities into their risk assessment and investment strategies, (ii) strengthen internal corporate policies and (iii) develop internal competencies to assess transition risks associated with climate change and environmental degradation.

62. In 2020, in line with the main recommendations of the report, the Central bank of Mexico proposed the creation of a sustainable finance committee to be in charge of all matters relating to sustainable finance and green growth of the national economy. All Mexican financial authorities participated as members, and the chairs of the main financial sector associations as observers.

63. The committee was split in groups with the following objectives:

- to develop a sustainable finance taxonomy in line with the SDGs;
- to integrate climate and environmental, social and governance risk factors in supervisory and financial market activities by supporting a wider adoption of environmental risk management systems in financial institutions;
- to improve the amount and quality of disclosures and reporting by non-financial and financial institutions, in line with frameworks and international standards; and
- to increase sustainable capital mobilisation by identifying barriers that limit issuance of sustainability-linked securities and by sharing best practices among market participants.

64. Through these efforts Mexico is looking to align disclosure of climate and environmental information by corporations and financial institutions with forthcoming international sustainability standards and reporting duties. In addition, the country is stepping up in the assessment of the regulatory framework for gradual implementation of ESG material factors. Although there is still progress to be made, establishing a clear institutional framework to foster Mexico’s sustainable finance agenda seems to facilitate communication and send a clear message to market

¹¹ Central bank of Mexico, “*Climate and environmental risks and opportunities in Mexico's financial system from diagnosis to action*”, February 2020.

participants on the road ahead. Thus, the establishment of a clear and well-designed Mexican roadmap for sustainable finance will facilitate market and regulatory best practices at national and even international level.

65. In 2021, as part of a conventional risk management survey, financial institutions were required to provide their opinion about the actions that need to be carried out to manage and mitigate climate risks. About 57% of surveyed institutions confirmed having already analysed their exposures to climate related risks and 18% planned to do so during the following 12 months. Thus, the main methods used to measure risk exposure were scenario analysis and stress testing.

66. A noteworthy development for the support of the sustainable finance agenda was the formal launch of the task force of Mexico Consortium in 2021. This Consortium will initially focus on raising awareness about the importance of financial aspects related to climate change consideration, as well as developing a knowledge basis regarding climate risk in the financial sector.

67. Finally, the review of the context of development of green finance in Mexico, as well as the best national and international practices allowed government and local authorities including financial institutions to understand that the Mexican taxonomy system should focus on three key elements:

- harmonisation with best international practices, which will provide more certainty for investors in search of opportunities in green assets. Mexican taxonomy rules do not need to be the same as the international once, but they do need to be harmonised using comparable methodologies to avoid risks of inconsistency and locking of capital flows;
- engagement in the reality of the Mexican domestic economy and international place within ecosystems, as well as the specific capacities of its financial institutions. The future taxonomy may have a different focus and development, while maintaining a certain degree of comparability to the other existing taxonomies. To that end, transparency about reporting and establishment of technical evaluation criteria seems to be crucial; and
- framing the green finance taxonomy of Mexico within existing initiatives, providing advantage to initiatives that have credibility, legitimacy and dynamism, thus avoiding parallel inefficient and unnecessary structures.

D. Chile and Columbia: examples of how emerging countries are considering sustainable finance while tackling difficult domestic economic issues

1) Chile

68. In 2021, a roadmap for taxonomy development was published in Chile. It was prepared by the International Climate Initiative and the Inter-American Development Bank. Sustainable finance development was expected to start before the end of 2021 under the supervision of the Ministry of Finance and the Green Finance Public-Private Roundtable.

69. In February 2022, Chile issued USD 2 billion in Sustainability-Linked Bonds and became the first country in the world to issue sustainability bonds in such volume. The Ministry of Finance reported that it made its first sovereign issuance of a sustainability-linked bond with remarkable results, despite the difficult times, high volatility and uncertainty in the domestic and global economies and markets. The operation was very successful in several dimensions. First, it achieved a high demand of USD 8.1 billion, 4.1 times the amount placed of USD 2 billion, diversified not only by type of investor but also by geography. This is particularly relevant considering the current difficult global circumstances. This bond issuance demonstrated the confidence in the Chilean economy of the international capital markets, as well as Chile's leadership in green finance, being the first country in the world to issue this type of bond.

70. Over the past years, Chile has strengthened its commitment to climate change mitigation and environmental protection through both domestic and international initiatives. The issuance of this Sustainability-linked bonds seeks to set another milestone in the country's commitment. This milestone is an important step towards the ambitious target of Chile to achieve a net-zero carbon economy by 2050. The Chilean government is actively promoting public-private cooperation and aligning incentives in this direction to show its commitment to move quickly to a more resilient domestic economy.

71. Accordingly, in May 2021, the International Climate Initiative together with Chile's Ministry of Finance developed a roadmap called "*Taxonomy Roadmap for Chile*"¹², which provides an assessment on the most suitable approaches and relevant methodologies for developing a national taxonomy. The government of Chile is fully aware that the establishment of a national green taxonomy will make Chile's economy greener, but also stronger. Establishing clear green

¹² Ministry of Finance in cooperation with the Inter-American Development Bank and the Green Finance Public-Private Roundtable, "*Taxonomy Roadmap for Chile, one more step towards consolidating the local Green Finance Agenda*", May 2021.

definitions could give Chile an advantage compared to other countries in the region to attract international capital flows to domestic sustainable projects. The roadmap also described various applications and users of the taxonomy, as well as opportunities and challenges for sustainable finance. Priority is given to sectors such as energy, transport, buildings and industry, in particular mining. The recommended pathway to follow is to adopt, adapt and lead the sustainable finance and direct most of the capital flows in this direction. There is space for Chile to establish leadership in certain areas, including mining and nature-based solutions. Climate change and other environmental indicators are recommended to be the overarching goals of the Chilean taxonomy. In addition to mitigation, the Chilean taxonomy would also benefit from developing criteria towards adaptation and resilience, considering the climate risks and adverse impacts on various sectors in the country such as water and desertification areas. Chile needs to decarbonise rapidly, and a strong and well-designed national taxonomy can facilitate the capital flows into sustainable investments.

72. Chile has already demonstrated excellent leadership through its international and national commitments to mitigate climate change issues. The country has also implemented several national policies, plans and legislations to achieve this goal. Rising global temperatures also have adverse effects on the ecosystems and population of Chile. It is an opportunity for Chile to lead the initiative to develop the eligibility criteria for activities that primary focus on the mining sector for strategically important minerals that are required for a low carbon transition (e.g., lithium, copper, etc.).

73. Key sectors in Chile, such as construction, energy, transport and mining were analysed as examples to perform a basic gap assessment. Some of the key starting points for assessment and development of the taxonomy could be the energy efficiency law that was approved in January 2021 providing a rating system for all new buildings in Chile. Construction of energy-efficient buildings and implementation of renewable energy for new and existing buildings are important for the transition of this sector towards net-zero emissions and alignment with Chile's climate goals.

74. Chile's government also focused on renewable energy activities such as solar and wind, which should have softened eligibility criteria that will also apply to off-grid electric and small-grid with renewable energy generation. Natural gas could potentially be used for the production of hydrogen and other purposes only as a transition activity subject to the implementation of full carbon capture and storage. To achieve carbon neutrality by 2050 the electrification of end-use technologies is key, both in fixed and mobile sources.

75. Transportation is also a key sector of the Chile's economy. It is one of the most difficult to adapt to climate change challenges. In a constantly and quickly developing country such as Chile, providing reliable and safe transportation is a key factor for economic development and growth. Introducing climate changes requirements for sustainable development is a delicate measure that needs to be properly provided to avoid any adverse effect on the current economic development of the country. Therefore, the energy efficiency law of Chile included efficiency benchmarks for vehicles, provides incentives for electric vehicles and declares hydrogen as a fuel. The law also established benchmarks based on gCO₂ per litre of fuel which should be translated to CO₂/km for new vehicles sold in Chile. Thus, infrastructure required for low-carbon transportation should be included in the taxonomy, as well as net-zero emission micro mobility such as bicycles, electric scooters, etc. The electric and green hydrogen-based equipment should be directly eligible through the taxonomy for all modes of transportation.

76. The future Chilean taxonomy should dedicate a particular attention to the mining sector, which is one of the most important for Chile. The primary goal of this sector should be the mining for strategically important minerals that are required for transition. For example, for copper mining, the goal is to ensure that 94% of the energy consumption for surface mining and 82% of the energy consumption for underground mining will be provided by electricity and green hydrogen by 2050. For non-copper mining, the goal is that by 2050, at least 58% of the energy consumption will be by electricity. Due to the sector's complexity, the criteria should assess options such as life cycle evaluation or environmental impact assessments in addition to emission thresholds.

77. Thus, a sustainable classification system such as a taxonomy set of rules may facilitate the capital flows into sustainable activities and assets and act as guidance for climate-aligned investments and project development. It could also provide an appropriate assessment of climate-related risks for the financial sector. In conclusion, Chile's national taxonomy will help to establish a green investment roadmap and act as a blueprint for the country's transition towards a green economy and green growth. If aligned with international taxonomies, it will also help to increase capital flows into green projects from international investors and will accelerate the economic development of the country.

2) Colombia

78. Colombia began developing its green taxonomy in 2019¹³. The process has been led by the Colombian Financial Regulator, the Ministry of Finance, the Department of Planning, the

¹³ Development of green taxonomy of Colombia (phase 1): <https://www.irc.gov.co/webcenter/portal/TaxonomiaVerdeColombia>

Department of Statistics and the Ministry of Environment and Sustainable development which are all part of a supervisory committee. The Colombian green taxonomy included economic activities and financial products with substantial contribution to the commitment of the country in line with the Paris agreement. The strategy of the Colombian government is to catalyse the capital markets for the development of green financing instruments, thus encouraging green investments.

79. The Colombian green taxonomy will be a classification system for economic activities and assets that contribute to the achievement of the country's environmental objectives and commitments. It should incorporate a set of definitions aimed at supporting different actors in the public and private sector, such as bond issuers, investors, financial institutions, public entities, among others. It will further support the identification and evaluation of investments that could meet environmental objectives and that could be considered green or environmentally sustainable in Colombia. The taxonomy is being developed with a similar architecture to the EU Taxonomy and should focus primarily on climate change mitigation and adaptation components, including *Do No Significant Harm* principles together with *Minimum Social Safeguards*.

80. Thus, the future green taxonomy of Colombia will facilitate the identification of projects with environmental objectives, develop green capital markets, and promote the effective mobilisation of private and public resources towards green investments. This will allow Colombia to meet its commitments with regard to the Paris agreement, but also with regard to the Convention on biological diversity and the SDGs. Further, Colombia has a leading climate action in Latin America and the Caribbean regions. In 2020, the country carried out its update and set more ambitious goals such as to be able to achieve 51% of the reductions in greenhouse gas emissions by 2030. Given the global nature of financial markets and environmental challenges, the best practices of environmental sustainability and other countries' classification systems will be incorporated in the construction process of the technical documents, such as the EU taxonomy, the Climate Bonds Initiative guidelines, the Green Bond Principles and the SDGs. Likewise, the Colombian government recognises that the process of establishment of a national green taxonomy has taken into account existing international taxonomies and guidelines but also considers the challenges, capacities and specific realities of Colombia, which remain the cornerstone of a strong and well-designed domestic classification system relating to sustainable finance and investments.

81. Finally, the Colombian green taxonomy is still in a process of development but according to the initial documents released by the government, it will like other taxonomies in Latin America,

be focused on the most important economic sectors of the Colombian economy such as energy, construction, waste management and emission capture, water supply and treatment, transportation, information and communication technologies, manufacturing, livestock, agriculture and forestry.

E. South Africa: a transition to an equitable, resilient, low-carbon green economy

82. Sustainable finance will be critical for enabling Africa to adapt to the growing impacts of climate change and to ensure that its future development path is consistent with the decrease of the global warming. Africa has contributed little to global emissions so far, but it is already being disproportionately affected by the impacts of climate change adverse effects. How Africa develops will also be critical to future greenhouse gas emissions given the fact that its energy use is projected to grow rapidly to meet its development needs with its share of the world's population projected to increase from 17% to 40% by 2100.

83. A low-carbon, climate-resilient path offers Africa the opportunity to avoid the mistakes of the past and seize the opportunity to leapfrog to a better form of growth that can deliver on both its development and climate goals. It will require, however, a major ramp-up in the scale and quality of investments in three critical areas (i) energy transitions and related investments in sustainable infrastructure, (ii) investments in climate change adaptation and resilience and (iii) restoration of natural capital and biodiversity. Africa will also not be able to finance alone the scale of the investments needed. It will definitely need a significant help from other countries and in particular from international investors.

84. South Africa has a leading role in sustainable finance in Africa. It launched its own platform for energy transition at COP26, that could be adopted by other countries to provide a scaling-up of transformative investments. Thus, all African countries have to make concerted efforts to boost domestic resource mobilisation to ensure the long-term sustainability of green project investments.

85. In May 2020, South Africa's National Treasury published a technical paper called "*Financing a Sustainable Economy*"¹⁴ with the intention to unlock the access to sustainable finance and direct capital flows to support a climate-resilient economy. One of the key recommendations was to develop a national green finance taxonomy for South Africa. The taxonomy project should

¹⁴ South Africa National Treasury, Technical paper May 2020, "*Financing a sustainable economy*".

focus on the adaptation of international best practices to South Africa's economic situation and demographic and social reality. Thus, South Africa's green economy should take into consideration the following activities:

- economic activities that are aligned to or expected to make a substantial contribution to the transition to green economy in South Africa;
- economic activities that presently have significant detrimental environmental impact but are needed as part of the future South African green economy and which will be further improved to reduce their impact on environment and climate in South Africa.

86. In June 2021, the National Treasury of South Africa released the first draft of the "*Draft Green Finance Taxonomy*"¹⁵ and a draft guidance providing useful insight of how to consider the taxonomy rules "*Applying the Green Finance Taxonomy, User Guidance to the Draft Green Finance Taxonomy*"¹⁶. The draft paper is establishing the South Africa's blueprint for future classification of activities as green or sustainable. It defines a matrix of covered sectors and activities and provides mapping of environmental activities. Technical screening criteria are proposed to assess activities that will be falling under the taxonomy framework. These criteria will provide an extensive information on the requirements for each eligible activity, including principals, metrics and thresholds for substantial contribution to climate change adaptation and mitigation. The draft is identifying, like other countries' taxonomies, the critical economic sectors of South Africa, such as Industry, Energy, Water and waste, Transportation, Information technologies and Construction. A particular focus is provided on industry, especially mining and renewable energies. The draft is also including the concept of "*Do No Significant Harm*" together with the one of "*Minimum Social Safeguards*" like the EU Taxonomy. Those concepts are developed with a particular focus on sustainable use of water and marine resources, ecosystem protection and restoration and pollution prevention.

87. Finally, the draft paper is ascertaining that the taxonomy to be put in place in South Africa will (i) help the financial sector with clarity and certainty in selecting green investments in line with international best practices and South Africa's national policies and priorities, (ii) reduce financial risks through enhanced management of environmental and social performance together with disclosure and reporting duties to be further implemented, (iii) reduce the costs associated with labelling and issuing green financial instrument, (iv) unlock significant investment opportunities for South Africa in a range of green and sustainable assets, (v) support regulatory

¹⁵ National Treasury of South Africa, "*Working Draft, Draft Green Finance Taxonomy*" June 2021.

¹⁶ National Treasury of South Africa, "*Applying the Green Finance Taxonomy, User Guidance to the Draft Green Finance Taxonomy*", June 2021.

and supervision oversight of the financial sector with regard to green finance and (vi) provide a basis for regulators to align or reference green financial products in South Africa.

88. The South Africa National Treasury did not provide further information about when the green finance taxonomy is expected to be implemented in domestic legislation, but the process should evolve rapidly and most probably there will be a final version of the Green Taxonomy of South Africa, end of 2022 or in 2023.

III.PART II: ANALYSIS OF INVESTMENT CLASSIFICATIONS QUALIFIED AS SUSTAINABLE FINANCING

89. ESG factors and sustainable investments have been a topic for quite some time, but only few investors were actors in this field and dedicated to responsible investing. However, the last ten years and especially during the Covid-19 crisis the sustainable investments and ESG factors took their place at the international investment scene. Capital markets around the world started to focus on these investments and alongside traditional financial products we have seen the emergence and even the boom of sustainable financial products such as green bonds.

90. The environmental and social awareness evolves and more and more investors and corporations have integrated ESG factors in their processes and new ESG dedicated procedures and products were developed. More importantly, many larger corporations and multinational groups move towards sustainable investing and even in some cases impact investing. The whole industry was pushed forward to sustainable finance to accelerate the move and make it much more concrete. However, many investors and corporations are still navigating in murky waters, as there are no precise definitions, nor clear and concrete rules regarding so-called sustainable investments, nor regarding the integration of ESG factors in the operation and investment decisions of investors and corporations. Thus, it is important not only to seek answers through regulatory taxonomies providing rules based on top-down approach but it is also necessary to see what other choices are provided by international actors dedicated to sustainable finance and ESG investing.

91. It is important to understand what is at stake and what is standing behind the sustainable finance and sustainable investing to better understand the concept of green or sustainable growth and sustainable development. As ESG analysis becomes more and more considered in the investment world, thus providing financial information to capital markets, investors and

corporations, it is important to understand what this means at the level of an investor and at company's level. It has become increasingly critical for investors and companies to discern the real value produced by these assessments. Thus, the concept of materiality analysis is a method to identify the ESG issues that are most important for an investor, companies and shareholders.

92. Accordingly, a materiality analysis is a methodology that investors or companies can use to identify and estimate ESG factors which might affect the business they run or the investment they are going to make. Hence, using the materiality method provides investors and companies with possibility to elaborate a long-term ESG strategy and thus to engage important financial flows in sustainable investing thus decreasing investment risks. To translate sustainability into financial performance, a company or an investor needs to focus on two sides: one which will be guided by the cash flow generated by the investment and the other one will be guided by the costs necessary to perform this investment. Materiality is typically measured both in terms of likelihood and severity of impact providing identification of the cash flows and necessary financial costs for the performance of an investment.

93. Investment strategies about ESG factors are often used and linked to responsible investing or sustainable investing and even to impact investing. To better understand all these concepts, it is important to understand how the spectrum of capital is to be considered while applying ESG factors to capital investments. ESG factors should also be considered at the level of an investor or a company outside of specific countries' regulations to better understand what involvement is required of each capital market actor. Only when all capital market actors decide to direct their investments towards sustainable projects and activities will the global economy be able to make the shift towards a net-zero carbon economy. Investors and companies who primary see ESG factors and their integration as a way to enhance investment processes are likely to focus on ESG issues and consider them as financially material.

94. Therefore, it is essential to clarify and define all terms that are gravitating around the ESG factors for sustainable investing to communicate properly in a clear and meaningful way to investors and companies, thus avoiding misunderstandings and misleading information. Capital markets are influenced by cash flows and investment transactions thus providing capital circulation within the markets. The spectrum of capital is a map aimed at showing how different investment approaches and financial goals are aligning with their sustainability objectives and their impact on people and on the environment. There are five categories of investments in the spectrum of capital:

- Traditional investing: focused on returns and profits only, with limited or no regard for ESG factors;

- Responsible investing: foresees that investment decisions are made following filters based on a particular list of approaches. There could be different types of approaches within this strategy such as (i) negative or exclusionary screening providing exclusion from financing certain economic or industrial sectors or companies based on specific criteria linked to ESG goals; or (ii) positive or best in class screening which implies investments in sectors, companies, projects or activities selected for their positive impact on environment thus providing a positive ESG performance compared to industry peers; or (iii) norm-based screening, which implies the screening of companies, activities or projects against minimum standards of business practices based on international norms, such as those issued for example by the Organisation for Economic Co-operation and Development (OECD), or the International Labour Organisation or the United Nations;
- Sustainable investing: refers to the integration of ESG factors into investment decisions and incorporating of ESG criteria into all management processes within a company to provide transparency on the benefits that an investment is meant to have, mainly when financial products are distributed.
- Impact investing: defines investments explicitly made to generate positive measurable, social and environmental impact alongside a financial return. This type of investing is (i) designed to contribute internationally to a positive social and environmental impact, (ii) built upon evidence and impact data; and (iii) providing impact performances that are managed by the impact investors.
- Philanthropy: focuses only to investments with a positive non-financial impact such as charity or donation activities.

95. Accordingly, designing new tools for sustainable investments directing cash flows to sustainable activities will necessary need to address key elements such as the materiality of ESG factors, their integration in investments decision at corporate and investors levels based not only of taxonomy regulations but also on corporate and social responsibility based on an estimate of positive and negative impacts of a contemplated activities, thus providing more security in investments and reducing the risks of greenwashing (A). ESG factors for sustainable investing should also be seen in international non-governmental guidelines and recommendations, including reporting standards providing investors and companies with a better knowledge and transparency about the sustainable investments they are realizing (B).

A. Drivers of ESG factors at investor and company level providing knowledgeable concepts of meaningful investments

1) *ESG factors and the Corporate Social Responsibility (CSR) policies at corporate level: a key element for green growth in capital markets*

96. Current concept of sustainable development stands for an economic model that covers human beings' needs while enabling future generations to satisfy their needs too. The current definition focuses on resilience and shift from traditional to more sustainable economy as a response to the growing limitation of natural resources on the planet. Internationally, the United Nations have mobilized the international community of actors around the 17 Sustainable Development Goals (SDGs). Accordingly, a key player of the international community of all those concerned by the SDGs is the company and even the United Nations agreed that the most important input in terms of sustainable investments should be handled by the private sector and at corporate and investors' level.

97. The corporate social responsibility (CSR) is the cornerstone of our sustainable development and any future shift to an economy governed by the green growth. Any type of regulatory or legislative development relating to classification such as taxonomies in sustainable investing should consider the central role of the company in a given country's domestic capital market or within the framework of national economic development¹⁷. The CSR covers all of the resources and action that a company commits to its contribution to sustainable development. It also helps companies of the private sector of a given economy to adapt to their economic, social and environmental situation while creating an additional value to global environmental objectives and on national level by supporting the shift to a sustainable domestic economy. It is a voluntary initiative for business conduct which reflects businesses' contributions to sustainable development. The CSR is the corporate commitment of a given company to act responsibly and to reduce negative externalities and thus create a positive impact for the society.

98. Accordingly, companies are acting responsibly when they (i) develop CSR strategy to create additional value and support global environmental objectives, (ii) include key CSR principals in their governance to improve decision-making processes and shareholders active commitments, (iii) create responsible human resource policy providing positive impact on employees' careers and (iv) develop an eco-friendly value chain to increase the efficiency of operations and limit

¹⁷ OECD Guidelines for Multinational Enterprises, edition 2011.

environmental impacts. To ensure it has a long-term future, a company needs to see value creation as a coherent system. Intangible capital, processes and value perceived by customer has to form an integral part of company's policy. Thus, in society the value brought by companies could be presented in a form of four layers: environmental, society's, economic and financial capital. Hence, actions taken by a company with respect to these layers could increase or reduce such capital layers and destroy or create different forms of value in society.

99. This is the reason why it is important to understand the relationship between CSR and ESG criteria. A good CSR strategy requires that a company in conducting its ordinary business activities also impact and contributes to the society and the environment in a positive way. Thus, CSR allows companies to be part of the positive change and to choose what is consistent with current society challenges and not only focus on its own benefits. Accordingly, the CSR makes a company responsible, while ESG criteria make such company's efforts measurable because ESG provides quantifiable indicators to measure the impact of the company's business activities. It also includes the use of various actions going further the baseline settled by laws and regulations to actively improve local and global community well-being, such as for example the EU Directive 2014/95 relating to the disclosure of non-financial and diversity information by certain large undertakings and groups, which should be amended soon¹⁸. Following, the ESG criteria help companies to elaborate different approaches and influence their activities and customers.

100. Today, most of companies and asset managers have a list of activities they consider to be incompatible with responsible investment. Thus, if a company's activities and operations have detrimental impact on society or the environment, exclusion is often a straightforward answer for the asset manager, but it is also a difficulty because different screening approaches deliver quite often different results. Therefore, different types of screening have been developed to better respond to ESG criteria and clearly identify what activity could be considered as truly sustainable, and which activity is actually contributing to the reduction of carbon dioxide emissions as targeted by countries international commitments¹⁹. The most popular types of screening are:

- (i) Negative screening which filters out companies operating in businesses that do not meet sustainability requirements. This implies that several sectors or industries could be excluded from investing such as weapons, tobacco, gambling etc. However, it is difficult to exclude large-scale sector activities from investments, because this may result in imbalanced risks and a much narrower opportunities for business and the investment

¹⁸ EU Directive 2014/95 relating to the disclosure of non-financial and diversity information by certain large undertakings and groups dated 22 October 2014

¹⁹ ESG Investing and Climate transition, market practices, issues and policy considerations, OECD 2021.

universe could be skewed. Thus, it is important for asset managers and companies to exclude only activities and sectors that are truly harmful and irrevocably opposed to their sustainability and financial goals;

(ii) Positive screening, or also known as “*best in class*” approach implies that companies’ activities are ranked according to their compliance with ESG criteria and then the leading company from a particular sector is picked as the best choice for sustainable investment. However, this approach can leave a company with a lower ESG performance in absolute terms, because even the very best oil company producer remains a fossil fuel producer contributing heavily to carbon emissions global spread. Nevertheless, the *best-in-class* approach remains today one of the most popular approaches among investment screening types because it does not exclude a particular sector and it leaves room to engage with companies in all sectors;

(iii) Norm-based screening aims to screen companies that do not comply with international business acceptable behaviour such as human rights and minimum labour standards. Norm-based screening results in either straight exclusions at individual corporate level or the start of engagement with the company. Engagement with a company means entering into dialogue in a way allowing asset managers to put forward their expectations on corporate behaviour and encourage the company to enhance its sustainability performance or governance. Thus, engaging with companies allows asset managers to address and mitigate material sustainability risks, providing competitive advantage for the company increasing the likelihood of being successful in the long run; and

(iv) Active ownership is the consequence of company’s engagement in ESG compliant investment strategy. It aims to provide shareholders with an active role or “*active ownership*” to influence the company’s managing bodies to improve the environmental, social and governance practices in its decision-making processes. Thus, voting and voting rights at general assemblies are the cornerstone of such active ownership shifting the responsibility of a given corporate decision into the hands of all shareholders. Voting exercise should go together with regular dialogue between the shareholders and the margin bodies of a company to build strong relationship to produce “clean” activities or sustainable investment portfolios matching shareholders corporate and investment strategy values.

101. Consequently, appropriate, rigorous and transparent screening approach to ESG compliant investment strategies plays a key role in reducing the risk of greenwashing, thus providing investors with safer investment environment.

2) *Greenwashing and sustainability challenges: how to address this phenomenon?*

102. The Sustainable development has gained huge momentum, especially since the Covid-19 crisis and countries around the world are strengthening their efforts to improve their internal rules and regulatory framework to encourage private sectors actors to engage in sustainable investing. The way our modern economy is organized has dramatically changed our views on sustainability. Today, the goal is clear, no net emissions of green-house gases by 2050, decoupling economic growth from heavy resource use and no one should be left behind. However, such a deep change in economies, especially in circular economies will require a huge amount of funds either from the public and private sectors. Public sector already mobilized an important amount of funds such as 500 billion EUR will be provided by the EU budget and additional 280 billion will be triggered by the European Investment Bank for sustainable investments. But this will not be enough to achieve the transformation into net-zero green-house gases economy. Besides, corporations will have to transform their activities and operational processes and this will require the biggest amount of funds necessary to achieve the 2050 goal. Thus, capital markets will have a key role in channelling capital flows from detrimental activities towards environmentally friendly production, providing positive environmental impact.

103. However, when private capital is coming into play, several investment risks may occur, such as greenwashing. This phenomenon could be described as a practice which consist for a company to provide misleading information regarding its activities, investments and operations making them to appear more environmentally responsible than they really are. In the context of ESG, the greenwashing gained huge importance, as the field is not yet fully regulated and many capital market actors are using this new economic bubble to take advantage of this opportunity. Listed companies could gain importance and attract investments and money inflows using misleading information about their assets' value regarding their sustainability positioning. In financial investment sector, greenwashing has become an issue and being called-out across financial companies with sustainable investment products that may be misleading to actual ESG investments.

104. One of the reasons why greenwashing is gaining importance is that money flows are tied to ESG compliant criteria. The more a company appears to be ESG compliant, better ESG rating will be provided and the more potential money flows could be attracted. Thus, greenwashing has clearly an economic shift. It is important to understand what kind of issue greenwashing could arise from such misleading information. First thing to know, is that greenwashing could be anywhere, even at governmental level so it is always essential to ask the rights questions and to

seek transparency and accuracy in all the information provided about the sustainability of an asset, or an investment.

105. Therefore, it is of necessity to analyse different layers of our society where greenwashing could be a treat for investors and companies:

- at state or government's level: there are many examples of how ESG factors could lead to a misleading information and even worse to a confusing approach while considering an in-depth transformation of an economic system. Thus, the European Union has implemented the Taxonomy rules by excluding the nuclear energy from all those activities considered as truly sustainable. This matter has to be dealt with on a later stage. However, the European Union is going to risk its reputation, because while looking to the energy production and use in Europe, a nuclear production of energy will decrease the green-house gases emissions and that will be a significant step forward to the 2050 goal. But what will happen in case of an accident and even more importantly what is the solution of the nuclear waste which is highly harmful for the nature and we did not find yet an eco-friendly way of treatment and storage of such a waste. Further, there are ongoing discussions about natural gas, to be qualified as a sustainable source of energy, especially since the beginning of the war conflict between Russia and Ukraine, the European Union and other countries strongly dependent on Russian gas have introduced economic sanctions against Russia, without considering the heavy impact of Russian gas flowing around European member states. Some of them refused to ban Russian gas because it is impossible for them to properly handle their energy needs without the regular provisions of Russian gas. Following, natural gas might become an eco-friendly source of energy, thus benefiting from the qualification of sustainable activity. As a consequence, the European Union regulator is risking greenwashing although it is trying to do the best possible effort to achieve the 2050 goal;

- at corporate level: companies need to do the biggest efforts in greening the economy as they are the major actors of it, while producing and delivering goods and services. Thus, more and more companies are engaging in greening their activities and are seeking to market their engagement regarding nature. For example, coffee producer "Nespresso" started to recycle all its capsules to reuse them again, while advertising that most of the aluminium capsules they are using are coming now from recycled materials. But what about removing aluminium capsules and any plastic associated material at all? Because this will call for a deep restructuring of the whole operational model of a company therefore, companies are engaging efforts, but these efforts seem to be surface attempts of sustainability approach arousing more doubt about greenwashing than about greening the activity and operations of a company;

- at asset managers' level: capital markets are playing a huge role in capital flows and economic activities in each country. Therefore, a key role is given to capital markets in directing capital flows to sustainable activities and investments. Since sustainability became a trend, many asset managers are looking to find and propose the most suitable assets providing the highest ESG score thus attracting investors willing to invest in sustainable financial products. The problem is that there is no data or better said, there is no reliable data and no reliable information about sustainable assets or investments. Hence, the European Union regulator gave a first input by implementing the SFDR Regulation (to be defined) providing mandatory duties for all asset managers willing to qualify for sustainable financial products under articles 8 and 9 of the SFDR Regulation. It was no surprise when asset manager started to compete for investors' money trying to label as much as possible assets under articles 8 and 9 of the SFDR Regulation. Here, greenwashing took a huge turn, because many assets initially qualified as green or sustainable were further disavowed through high-profile press announcement that rattled investors.

106. Following, is there a remedy of greenwashing? The current state of play does not provide for, because the risk still exists but what is of crucial importance to fight effectively greenwashing is transparency and reliable information using appropriated reporting standards that give accurate and precise information without undue influence by lobbyists or capital market speculators.

3) Identification of environmental, social and governance (ESG) factors: material mapping

107. The implications of climate change, harmful resource use, biodiversity loss alongside with social inequality and health pandemic situation are deeply influencing the behaviour of businesses and corporations together with consumers and governments. Priorities changed more and more governments are focused on changing current laws, regulations and policies in response to the environmental and social challenges our society is facing, while the demand pattern of businesses and consumers is shifting driven by increased transparency and awareness enabled by the digital age. The latter trend has empowered and catalysed an increased scrutiny to the environmental and social impact and externalities resulting from business activities. Asset managers are more and more keen to offer to their investors financial products that create an added value and enhance long-term financial returns. As such a wide variety of sustainability and ESG consideration of material importance are starting to be included in a large portfolio of investments and decision-making processes.

108. ESG issues are highly contextual in nature, given that what could be relevant for one industry sector, business or geography position might not be of relevance for another country, region or domestic environmental matters. This is the reason why a materiality mapping framework is crucial. It helps investors and investments to identify risks and opportunities while considering pertinent ESG factors to a company, industry sector or a particular region where the investor operates or the investment is to be performed. Thus, this process could be of crucial help for all businesses willing to have a coherent and efficient approach to sustainable investing and ESG factors consideration. Therefore, the materiality mapping is important tool to find out how a sustainable investment could be performed while avoiding risks of greenwashing and investments portfolio depreciation.

109. The materiality mapping could be considered as follows:

- Identify of the most important material issues both on an industry and regional levels;
- Simplify and analyse all identified issues focusing on drivers of materiality and probabilities that this could impact future financial performance of a given investment of company activity;
- Build proprietary and forward-looking frameworks to quantify the issues and look for possible solutions or gather the necessary data to build on fair solutions and analytical capabilities that could be incorporated into financial models that will help to avoid or solve these issues;
- Engage with companies, shareholders and stakeholders to seek possible solutions and to integrate this information in investment research to better understand what stands behind these issues while investing in sustainable financial products.

110. Hence, an increasing number of investors both institutional and retail concerned by the increased impact of ESG challenges on their future returns are using, today ESG portfolio selection and shareholders' engagement to address important economic issues. Following, by choosing to invest using ESG considerations as guidelines for investing, larger asset owners have shown that ESG is the future of investing. Consequently, the ESG integration has been to enable investors to add a sustainable dimension to existing portfolio of investments without any requirement to modify its underlying investment policy or the investment process. Today, the challenge to asset managers is to determine which information is relevant or "material" to a particular investment and to use it in the best possible way to optimize the investment and avoid high investment risks²⁰.

²⁰ Idem.

111. However, the most important input of materiality mapping remains not only to identify all sustainability issues but also to be able to generate impact by identifying the theme of investing and by measuring its impact. Thus, although most of the ESG investing is focused on “Do No Harm” approach i.e. mapping, assessing and mitigating the possible negative impact of an investment may have on the planet and people, only less than 1% focuses on positive or norm-based approach. While only a fraction of global investments is focused on impact investing for now, there are signs that wealth management will transform over time and will shift towards impact-based approaches. For now, impact investing comes often with a trade-off between impact and risk-adjusted financial returns but it also could be in another way, because there are already businesses and opportunities where impact drives valuations of companies without fundamental financial indicators and where the impact narrative is truly compelling that financial returns matter to lesser extent.

112. ESG consideration in the process of investments strategy construction is not only about financial but it is also to consider long-term consequences of actions in both financial and societal fields. Investing sustainably is about understanding the material non-financial factors that impact long-term value of portfolio companies and large-scale corporations. It aims to achieve the (i) integration of ESG factors in the fundamental bottom-up research and security process resulting in a more complete view of the risk-return features of investments; (ii) the understanding of the non-financial impacts of investment decisions on portfolio companies and their broader stakeholders, including employees, suppliers, customers, regulators, and communities; (iii) measurement of the improvements of behaviour of investing companies and large-scale corporations leading capital markets both directly and in collaboration with peers and clients, by leveraging different tools of selection, engagement and voting facilities. Integrating sustainability factors into fundamental bottom-up approach leads to more complete analysis and better-formed investments decisions.

113. Exercising ownership rights and actively engaging with companies in collaboration with other but also with the public sector provide more incentive for companies to raise their ESG standards and to direct financial flows to sustainable activities and investments.

B. ESG factors for sustainable investing enhanced by international non-governmental guidelines and recommendations and reporting standards

1) *Principles and recommendations for responsible investment developed by investors for investors*

a) Principles for responsible investors

114. The Global Reporting Initiative (GRI) is an independent, international organisation that helps businesses and other organisations to take responsibility for their impact investing and sustainable activities, by providing them with the global common guidelines for responsible investments.

115. In 2005, the United Nations Secretary-General Kofi Annan invited a group of the world largest international investors to develop principles for responsible investments that could be used by international investors while investing responsibly. The investors' group was supported by experts from the investment industry inter-governmental organisations and civil society. The group developed a framework of six fundamental principles for responsible investors (PRI). The PRI were launched in April 2006 for signatures and the number of signatories has grown from 100 to close to 4,000 members representing the majority of the world's professionally managed investments. The most important about PRI is the organisation sitting behind the principles. It is the world's leading proponent of responsible investments based on purely voluntary behaviours. It works to understand the investment implications of ESG factors and to support signatory members in the incorporation of these factors into their investment decisions. The PRI encourages investors to use responsible investment to enhance returns and better manage risks of investments, but does not operate for its own profit. It also engages with policy-makers around the world but it is not associated with any government. It is supported by the United Nations but it is not a part of them. PRI acts in a long-terms perspective of its members of the capital markets and from different economies in which they operate. The mission of PRI is "*to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.*"²¹

²¹ Principles for Responsible Investment, an investor initiative in partnership with UNEP finance initiative and the UN Global Compact, 2021.

116. The six principles are the following:

- incorporate ESG issues into investment analysis and decision-making processes;
- be active owners and incorporate ESG issues into our ownership policies and practices;
- seek appropriate disclosure on ESG issues by the entities in which we invest;
- promote acceptance and implementation of the PRI within the investment industry;
- work together to enhance our effectiveness in implementing the PRI;
- report on activities and progress towards implementing the PRI.

117. Accordingly, the incorporation of ESG factors and issues are the core pillars of responsible investing and therefore the work of PRI is to mobilise as many economic actors as possible to achieve real-world sustainability goals and to provide action-shaped outcomes that will feed back financial risks these responsible investing is facing. The challenge if PRI is to deeply embed ESG factors and issues into investors' decisions as a concept of real investment.

118. In its ambitious strategic plan for the period of 2021-2024 PRI already started initiatives to raise awareness and help businesses to engage with climate change mitigation, as the most urgent existential challenge facing society and further with human rights, as both an immediate source of protection for individuals from harm and discrimination, and as a necessary foundation for lasting social equality, stability and productivity²². The priority is given to ESG issues based on their significance and scale and scope for institutional investors. PRI is also focusing on accountability by providing reporting standards and lobbying about transparency in ESG data collection.

119. Following PRI's strategic drivers are leveraging scale by attracting representative by cross-section of the mainstream investment industry, responding to diversity by providing market knowledge approach and tailored solutions to all its members especially newcomers willing to learn from leading investors and enhancing accountability by continuously improving standards and guidelines to efficiently fight against greenwashing and to maintain credibility of members' engagement. This was clearly demonstrated by the drafting of the "*Blueprint for responsible investment*"²³ paper which is showing the ambitions of the PRI organisation and its long-term perspective in providing responsible investors with suitable and safe sustainable markets to achieve a prosperous world for all. Thus, PRI is willing to act as unique platform gathering

²² PRI Strategic plan 2021-2024, building a bridge between financial risk, opportunities and real-world outcomes, April 2021.

²³ PRI Blueprint for Responsible Investment, 2021.

together companies, investors, governments and academics to develop strong links and to build reliable sustainable markets.

120. Therefore, if the efforts of PRI are successful in the coming years, investors will consider ESG factors and issues as a part of their investment decision-making measured by the impact they have on the real economy and the world. ESG issues will be integrated into financial policies and regulations of the core financial markets, and leading financial systems will align incentives and behaviours with sustainability. Investors will use international ESG frameworks, principles and guidelines in their investment activities to align with the 1.5°C target. Progress will be on the way towards a global sustainability system for investors and corporations.

b) Climate Bond Initiative versus International Capital Market Association

121. Another good example of ESG guidelines is the start of green bonds standardisation by the Climate Bonds Initiative (CBI) and the International Capital Market Association. The CBI is an international organisation working to mobilise global capital for climate action and to promote investment in projects and assets necessary for a rapid transition to a low carbon and climate resilient economy. It has developed a set of certification schemes for energy saving projects and sectoral standards for projects in the field of hydro and solar energy, low-carbon public transport and energy-efficient buildings. In addition, sectoral standards have been developed for the issuance of bonds for the implementation of programmes and projects in the field of electricity, tidal energy and geothermal energy. First launched in 2013, the Climate Bonds Taxonomy²⁴ has become a globally recognised tool that provides an overview of green investment opportunities in key sectors of the economy. In 2015, CBI published and updated version of its standards the taxonomy requirements incorporating these standards. The Climate Bonds Taxonomy also relates to the issuance of bonds for the implementation of programmes and projects in the field of bio- and geothermal energy and low-carbon transport, as well as in hydro-energy, agriculture and forestry.

122. In 2014, the International Capital Market Association (ICMA) joined the methodological work in the field of green bonds and launched the process of developing another green bond standard called Green Bond Principles²⁵. Unlike the CBI standards, which focused on technical aspects of green bonds, the Green Bond Principles of ICMA were intended to balance the economic interests of the process participants. During the period of 2015-2016, the two groups

²⁴ Climate Bonds Taxonomy, September 2021.

²⁵ In 2014 a consortium of investment banks from *Bank of America Merrill Lynch, Citi, Crédit Agricole Corporate and Investment Bank, JPMorgan Chase, BNP Paribas, Daiwa, Deutsche Bank, Goldman Sachs, HSBC, Mizuho Securities, Morgan Stanley, Rabobank* and *SEB* first developed the principles for green bonds - *GBP*.

of standard setters (CBI and ICMA) actively worked together to formulate common principles and standards for green bonds. As a result, by the end of 2016 a new set of CBI standards was developed, which fully incorporated the provisions of the ICMA Green Bond Principles.

123. Today, CBI standards were amended for a third time to establish the criteria to be met by projects in the areas of forestry, biodiversity and hydroelectric power, land management, aquaculture, fisheries and waste management, aquaculture and fisheries as well as in the area of waste management funded through green bonds and green credits. The CBI updated standards and taxonomy requirements the building block of the certification scheme CBI for eligible securities.

124. The CBI taxonomy of is broadly aligned with Green Bond Principles of ICMA and is based on the recognition of their contribution to the mitigation or adaptation of the effects of climate change. The CBI taxonomy is a very detailed covering some 165 specific assets in the energy, transport, water, construction, land and marine resources, industry, waste and pollutant control, and ICT sectors. Different screening criteria are developed and can consist of: (i) absolute quantity thresholds, (ii) tolerance thresholds, (iii) quality thresholds, (iv) supply chain conditions, (v) conditions of pre-defined use of the asset, (vi) dynamic benchmarks or even a combination of these criteria.

125. Today, the CBI taxonomy and the ICMA Green Bond Principles are the benchmarks followed by most of the world's green bond issuers. Such benchmark reference ensures that companies are in compliance with the standards for the management of bond proceeds, project selection and reporting to investors.

126. However, CBI's recommendations for compliance go beyond the taxonomy itself, mainly for certification purposes:

- sector criteria: a subset of the CBI taxonomy, which contains detailed criteria for fourteen sectors with non-exhaustive examples of revenue generation. The sectoral criteria call for additional disclosure of information on the assets/projects and outline the issues a company needs to address;
- climate resilience principles: add a level of adaptation to sectoral criteria and helps to cast investments for climate change adaptation, which can be "asset-driven" or "system-driven".

127. The CBI taxonomy is primarily designed to be applied to financial products, especially bonds. However, the latest update of the CBI taxonomy relies more on flexible acceptance of

assets, projects and activities and leads to the inclusion of instruments in the CBI green bond list, which is then used by some index providers to determine the suitability of investments in green bonds for funds and by some stock exchanges to list in old growth segments.

2) *International reporting standards: investors are seeking transparency and measurable impact about their sustainable investments*

a) Global Reporting Initiative

128. The global sustainability landscape is shifting rapidly as climate change communities and businesses disrupt supply chains and governments are rushing to tighten regulations to effectively provide regulatory frameworks to “*ESG type*” of financial investment activity. Nevertheless, the most basic financial behaviour remain the same, investors and business stakeholders are looking to ensure a return on investment while minimising risks but taking into consideration not only the financial but also the environmental, social and governance side of their investments. In turn, the demand for sustainability reporting and disclosures is becoming imperative and crucial because greenwashing treats are everywhere at the capital markets around the world.

129. ESG and sustainability reporting standards are transitioning from voluntary to mandatory as companies begin to compete for sustainability-focused investment capital. Through reporting, an organisation can better understand and manage its impacts on people and the planet while identifying and reducing risks, seizing new opportunities, and taking action towards becoming a responsible and trusted organisation.

130. However, while many companies are likely to boast about the ESG portfolio targets, clear and uniform reporting standards are still in their early stage as regulations and investor preferences evolve. Thus, as the need for data requirements grows, certain reporting standards are beginning to raise as industry leaders truly support the creation of standardised classifications, guidelines and frameworks. One of these leading reporting frameworks is the Global Reporting Initiative (GRI), a non-profit organization that provides businesses with a framework for comprehensive corporate sustainability reporting. The GRI is one of those independent organisations that was one of the first non-governmental organisations dedicated to reporting about sustainable activities and investments. It was founded in 1997 in Boston, United States of America and since then actively working with businesses, investors, policymakers, civil society, labour organisations and other experts to develop the GRI Standards

and promote their use by organisations around the world. GRI created a global common language for organisations to report about their impacts and enabled them to take informed decisions about their investments around the world.

131. GRI reporting is becoming widely accepted around the world as a leader in standardising sustainability reporting in part because of the triple bottom line approach developed by GRI. The GRI Standards help organisations to understand their outward impacts on the economy, environment, and society. The goal of GRI is to create an accountability mechanism that would ensure companies adhere to responsible environmental conduct. As GRI grew, the reporting system was broadened to include ESG factors and issues.

132. Today, GRI reporting helps companies to increase their accountability and provides more transparency about their sustainability goals, efforts, and outcomes. The GRI reporting framework consists of universal and topic standards that organisations can use to prepare and report information that shows their sustainability impacts.

133. GRI reporting approach could be summarised in a five-step process:

- (a) Prepare for reporting: companies, investors and organisations define a vision for the report, create a team, develop a plan of action, and set meetings;
- (b) Connect with others: companies and organisations identify, hold meetings, and set priorities with key stakeholders in order to determine reporting scope and priorities;
- (c) Define reporting approach: the reporting team selects issues for action and reporting as well as decides on the report content;
- (d) Monitor reporting: the reporting team monitors activities and records data, checks processes and systems, ensures quality of information, and follows-up on reporting objectives; and
- (e) Communicate using reporting: companies and organisations choose the best way to communicate, write, finalise, and launch the report publicly.

134. The world is currently focused on reaching the Paris Agreement goal of net-zero emissions by 2050, therefore environmental management sustainability reporting has become particularly important to companies, investors, and customers around the world. In order to determine the weight of greenhouse gas emissions generated on-site, companies have to carefully track their product usage, chemical inventory, and control technologies and many others. GRI reporting standards aim to cover a wide range of ESG factors and issues, from employees' safety and human rights to environmental management at company's level and such

reporting framework requires a deeper knowledge of company processes and supply chains, as well as comprehensive data inputs.

135. Accordingly, GRI standards²⁶ offers thirty environmental performance indicators that could be used as part of environmental sustainability reporting. They are divided into nine primary categories:

- materials, which includes raw materials (natural resources, manufactured chemicals, and materials needed for manufacturing) as well as packaging materials and recycled product content;
- energy, which includes direct and indirect energy consumption, renewable energy amounts used, such as wind, solar, and geothermal, and efforts made to reduce energy requirements through more energy efficient processes;
- water, which covers the total amount of water withdrawn from water sources and company impact on those water sources, as well as the percentage and total volume of water that is recycled or reused;
- biodiversity, which provides information regarding company impact on the biodiversity of nearby protected areas and areas considered to have high biodiversity, as well as company strategies for managing impacts on biodiversity,
- emissions, effluents, waste, which includes total weight of direct and indirect emission of green-house gases, ozone-depleting emissions, and other air emissions by type; total water discharge by quality and destination; total weight of waste generated by type and disposal method; total weight of treated, transported, or imported hazardous waste either as well as the percentage of waste shipped internationally; total volume and number of spills on and off-site;
- products and services, which provides the percentage of products sold and packaging materials that are recycled;
- compliance, which provides the total monetary value of noncompliance fines and number of noncompliance sanctions;
- transport, which describes the impact of transporting your materials and finished products; and
- overall, which provides the total values of environmental protection expenses and investments.

136. To be able to provide information on all of these performance indicators, the GRI reporting standards require clear and concise data. This data is a large reason why GRI reporting

²⁶ Consolidated set of the GRI standards 2021.

standards are held in such high global regard and companies, investors and organisations are keen to use them to produce real and reliable results.

137. Accordingly, ESG materiality assessments and standardisation of data is providing investors with true answers to their questions about sustainable investments, treatment of employees and vendors and dedication to sustainability activities. GRI standards are providing this ESG materiality assessment, which empowers companies and organisations to easily report on their current state and outline future initiatives while taking into consideration business goals and risks.

b) Sustainability Accounting Standards Board

138. The Sustainability Accounting Standards Board (SASB) is an ESG guidance framework that sets standards for the disclosure of financially material sustainability information by companies to their investors. It was founded as a non-profit organisation in 2011 to help businesses, investors and other organisations to develop a common language about the financial impacts of sustainability. SASB Standards enable businesses around the world to identify, manage and communicate financially-material sustainability information to their investors. Over the years, the corporate sustainability disclosure landscape has become very complex. SASB developed a set materiality map including seventy-seven industry standards²⁷. In November 2018, SASB published these standards, providing a complete set of globally applicable industry-specific standards which identify the minimal set of financially material sustainability topics and their associated metrics for the typical company in an industry²⁸.

139. These standards provide specific, detailed with the aim of integrating them into accounting standards and have replicable requirements for what should be reported for each topic, including metrics. They make frameworks actionable, ensuring comparable, consistent, and reliable disclosure of sustainable information²⁹. SASB standards can be used by any global company looking to report on material, environmental, social and governance issues. These standards are intended to make it easier for organisations to provide investors with high-quality information and can be used to understand the sustainability factors and issues that are most likely to add value to a business. SASB considers that an improved transparency will raise investor's awareness of non-financial risks and will result in behaviour change allowing to avoid such risks.

²⁷ <https://www.sasb.org/standards/download/>

²⁸ SASB Implementation Supplement: Greenhouse Gas Emissions and SASB Standards, September 2021.

²⁹ SASB Conceptual framework, September 2021.

140. All standards issued by SASB meet a minimum set of criteria³⁰:

- they are relevant, useful and applicable while being cost effective and comparable;
- the metrics used provide enough information to understand and interpret performance associated with the disclosure topic;
- they are directional and provide clarity about whether an increase/decrease in the numerical value signals changed performance; and
- they are verifiable and can be easily quantified and qualified.

141. However, SASB standards do not represent additional reporting, but they focus on evidence-based information that is already present. The standards integrate sustainability reporting with financial reporting and give companies and investors the tools to identify sustainability areas that are relevant to them and that they can report on and/or are likely to affect their financial performance. These standards are applicable to all investors and provide a model for reporting that is useful to investors when taking investment decisions. SASB standards also offer free comparable sustainability data that is suitable for benchmarking and evaluating sustainability performance which helps investors and companies to make more informed decisions.

142. For example, a health industry company seeking to adopt relevant SASB standards can expect to report about:

- Energy Management
- Waste Management
- Patient Privacy and Electronic Health Records
- Access for Low-Income Patients
- Quality of Care and Patient Satisfaction
- Management of Controlled Substances
- Pricing and Billing Transparency
- Employee Health and Safety
- Employee Recruitment, Development and Retention
- Climate Change Impacts on Human Health and Infrastructure
- Fraud and Unnecessary Procedures

143. There are specific accounting and activity metrics within each of these categories. Accounting metrics are intended to measure performance, while activity metrics quantify the scale of a company's business and are intended to be used with the accounting metrics to facilitate comparison with other companies. The accounting metrics are accompanied by

³⁰ SASB Rules of procedure, February 2021.

technical protocols that provide guidance on definitions, scope, implementation, compilation, and presentation, thus providing useful tool to investors and companies to further communicate and share information about their sustainable activities.

144. SASB standards are also including environmental reporting tool that covers a variety of quantitative metrics within green-house emissions, air quality, energy management, water, wastewater, waste and hazardous materials, and ecological impacts. Each category requires the collection of specific data and is measured on a company-wide portfolio level. Hence, SASB standards is built to support companies in sharing their outward ESG impacts through the language of investors, debt holders, and internal financial stakeholders. ESG performance is now considered a key indicator of business health and long-term financial viability. Increasingly, governments, investors, financial institutions and companies are using ESG reporting standards and frameworks like SASB standards to compare peers and distinguish the ESG leaders from the others.

c) Task Force on Climate-related Financial Disclosures

145. The Task Force on Climate-related Financial Disclosures (TCFD) was created in December 2015 by the Financial Stability Board (FSB) in recognition that climate change presents a significant risk to the global financial sectors and as a part of the finance industry's response to the global financial crisis, with a remit to identify and manage risks to the financial sector. The FSB is an international organisation that aims to protect the global financial system, so the focus on climate-related impacts to the sector is particularly significant. The FSB established a final report in 2017, which included the eleven recommended disclosures which guide TCFD reporting guidelines³¹.

146. TCFD reporting approach is based on eleven recommended disclosures divided into four pillars. The four pillars are:

- governance, which provide information about how a company governance bodies manage, assess, and oversee climate-related risks and opportunities;
- strategy, which provides tangible material impacts of climate-related risks and opportunities on the whole business, including strategy and financial planning;
- risk management, which provide information of how a company or a business defines, assesses, and manages climate-related risks;

³¹ Implementing the recommendations of the TCFD, October 2021.

- metrics and targets, which provide information about the measurements used in assessing material climate-related risks and opportunities.

147. Beyond this core recommended disclosures, in 2021 the TCFD published additional sectoral supplemental guidance for Banks, Insurance Companies, Asset owners and managers, and non-financial groups. Over 1,600 companies and organisations around the world, which represent nearly USD16 trillion in market capitalisation, endorsed or have already adopted TCFD reporting standards. The G7 (United States, France, Germany, United Kingdom and Japan) have agreed to make TCFD-aligned reporting mandatory. In the United Kingdom premium listed companies are required to follow TCFD by April 2022. In addition, the United Nation's PRI has also endorsed TCFD-aligned reporting since 2020.

148. TCFD reporting standards are explicitly designed to address climate risks, falling within the ESG reporting frameworks, but they do not touch on the social and governance pillars composing ESG reporting. The TCFD four pillars of disclosure requirements explicitly focus on climate risks and opportunities. In particular, TCFD is focusing on how governance links with, and guides, organisations' approaches to environmental protection. While TCFD is relatively silent on social and governance components of ESG reporting, TCFD's reporting guidance allows certain flexibility in the way disclosures are provided, so companies could choose to disclose topics such as climate justice or operational resiliency if they desire to do so.

149. Like SASB standards, TCFD reporting is also under the umbrella of ESG guidance framework used by financial stakeholders such as investors, companies, insurers, and stakeholders. However, while, SASB focuses on reporting the outward ESG impacts and risks of a company's performance across different industry standards, TCFD reporting addresses the impacts of climate change on the company's ability to create value. Both TCFD reporting and SASB standards are focused on financial materiality. Where SASB standards provide a backward-looking snapshot of sustainability performance, TCFD reporting is more interested in the company's approach to sustainability and climate change, and in assessing the company's readiness to deal with the associated risks and opportunities. The two frameworks are rather complementary than interchangeable.

150. While the future of global ESG standardisation, currently strongly endorsed, is unclear, ESG reporting frameworks are sure to continue to play a critical role in climate-related disclosures.

IV.PART III: REGULATION (EU) 2020/852 ON SUSTAINABLE ACTIVITIES AND EU LEGAL ACTS RELATING TO GREEN PROJECTS IMPLEMENTATION

151. The European Union's (EU) Regulation 2020/852³² establishing a framework for sustainable investment ("EU Taxonomy"), and amending Regulation (EU) 2019/2088³³ on sustainability-related disclosures in the financial services sector ("SFDR") are the two major pieces of European legislation that constitute the EU's regulatory framework aiming to oversee and regulate the sector of sustainable financing. The EU Taxonomy was developed as a tool to support sustainable investments providing a clear framework of economic activities contributing in meeting EU environmental objectives. These two legislations are within the framework of the EU Green Deal initiative³⁴ and in particular within the lines of the EU Action Plan for financing sustainable growth of 2018³⁵, establishing ten key actions providing for the EU strategy of sustainable growth.

152. The key actions are divided into categories and could be summarised as follows:

- establishing a clear and detailed classification system for sustainable activities (i.e. the EU Taxonomy);
- creating an EU green bond standard and labels for green financial products;
- fostering investment in sustainable projects;
- incorporating sustainability in financial advice;
- developing sustainability benchmarks;
- integrating sustainability in ratings and market research;
- clarifying asset managers' and institutional investors' duties regarding sustainability;
- introducing a 'green supporting factor' in the EU prudential rules for banks and insurance companies;
- strengthening sustainability disclosure and accounting rule-making; and
- fostering sustainable corporate governance and attenuating short-termism in capital markets.

153. All these actions constitute today the EU strategy and long-term policy for sustainable development and sustainable growth. The current and future EU legislation is and will be fully

³² Regulation (EU) 2020/852 of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088.

³³ Regulation (EU) 2019/2088 of 27 November 2019 on sustainability-related disclosures in the financial services sector.

³⁴ European Green Deal Investment Plan of 14 January 2020, European Commission.

³⁵ European Action Plan: Financing Sustainable Growth of 8 March 2018, European Commission.

dedicated to the fight against the climate change adverse effects to people and on the planet within the EU and in close cooperation with international partners. It aims to transform the economies of the EU member states into a low-carbon economies, without reducing prosperity and, at the same time, improving people's quality of life, through cleaner air and water, better health and a prosperous natural world. The initiative also provides for a fair and inclusive economic and social transition of the countries within the EU. It has to focus on people first, and then to regions, industries and workers that will face the greatest challenges of this transition.

154. Accordingly, the EU Taxonomy was designed to ensure a common understanding for businesses and investors to evaluate green activities allowing them to communicate in a reliable way and to empower the sustainable transition. In other words, the EU Taxonomy regulatory framework is a common classification system that relies on technical screening criteria ("TSC") that are science-based criteria to be used to assess various economic activities covered with regard to the EU climate neutrality objectives. The EU Taxonomy is not a mandatory tool for economic activities to invest into but it aims at creating the first "green list" of recognized sustainable activities within the overarching monitoring of the EU institutions. By providing such guidance and such detailed listing of EU criteria, the EU Taxonomy becomes a powerful tool to help companies and investors to plan their climate and environmental transition and investments and raise funds for this transition, while the financial sector can rely on this green list to design credible financial products and direct capital flows into sustainable activities and projects.

155. The EU Taxonomy is designed to be an evolving regulatory framework and there will be future updates of the legislation until it reaches a satisfactory level of implementation according to the changes of investment behaviours on the capital markets. Thus, the EU Taxonomy will remain a living framework and will change over time. Its scope, in terms of economic activities or sustainability objectives will continue to be kept up to date on the International Platform on Sustainable Finance³⁶, which a group of permanent expert group that has been established by article 20 of the EU Taxonomy. It is responsible for assisting the European Commission in developing its sustainable finance policies and to support the further development of the EU Taxonomy. This platform plays also a key role in enabling cooperation between the best expertise on sustainability from the corporate to public sector, from industries as well as academia researchers, a place where civil society and financial industry join forces to achieve a common goal of sustainable transition and the green-house gases net-zero emissions target of 2050.

³⁶ https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/international-platform-sustainable-finance_en.

156. Accordingly, the EU Taxonomy is not meant to be a stand-alone paper, it is also a tool which is a part of a broader sustainable package developed by the European Commission and is linked to the SFDR. The EU Taxonomy directly amends the SFDR by requiring some financial products notably those promoting environmental or social characteristics or those with pure sustainable investment objectives to calculate and disclose their alignment with the EU Taxonomy. A lot of emphasis is given to the categorization of financial products under the SFDR, such as investment funds subject to articles 8 or 9 of the SFDR.

157. However, under the EU Taxonomy, the question is rather around the percentage of sustainable investments or taxonomy-aligned investments in these financial products. This is in line of other regulatory developments, in particular relating to distribution of financial products, which introduce new obligations regarding the assessment of client's sustainability preferences by financial advisors in the context of a sustainability assessment.

158. The SFDR and the EU Taxonomy both need non-financial information to reach their objectives and to produce the expected result. Therefore, the EU Taxonomy will also operate as a transparency tool that will formalise and harmonise the limited non-financial reporting, requiring financial and non-financial undertakings to provide standardised information into EU Taxonomy-aligned reports. In 2019, the EU Commission also worked to amend the EU Climate transition benchmarks and sustainability-related disclosures for benchmarks regarding sustainability and climate-related investing³⁷ to provide a better understanding of benchmark standards and a more transparent path for assessment of ESG factors while channelling capital flows to sustainable investments.

159. Currently, the EU Commission is working on new legislations regarding EU Green Bond Standard and labels for financial products³⁸ and on a new EU Directive of non-financial reporting relating to large-scale corporations and a proposal was already adopted on 21 April 2021 providing a new content of a Corporate sustainability reporting directive ("CSRD")³⁹, which should amend the existing reporting requirements of the EU Directive 2014/95/EU regarding the disclosure of non-financial and diversity information by certain large undertakings and groups ("NFDR")⁴⁰.

³⁷ Regulation (EU) 2019/2089 of 27 November 2019 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks.

³⁸ Proposal for a Regulation (EU) on European Green Bonds of 6 July 2021, European Commission and annexes.

³⁹ Proposal for a Directive (EU) amending Directive (EU) 2013/34/EU, Directive 2004/109/EC, Directive 2006/43/EC and Regulation (EU) 537/2014, as regards corporate sustainability reporting.

⁴⁰ Directive 2014/95/EU of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups.

160. Therefore, acting like an engaged and ambitious actor of the fight against the adverse impact of climate changes, the European Union is settling as a pioneer establishing regulatory and classification frameworks for sustainability-aligned investments and financial products as provided for in the EU Taxonomy, together with a reliable regulatory framework regarding disclosure of non-financial information as provided for in the SFDR setting the initial stand of the EU action to comply with its international commitments with respect to the objectives of the Paris Agreement to significantly reduce the risks and impacts of climate change on people and on the planet. The EU is also providing an active and result-oriented approach to all other relevant fields of the EU members states economies, that are linked to industries, major businesses and capital markets to achieve these objectives as provided for in the Paris Agreement. Such other pieces of legislations are concerning the EU Green bonds standard (1), the EU Regulation establishing EU Climate-Transition Benchmark (2) and the future Corporate Sustainability Directive (3), which is going to guide large-scale businesses to the shift from traditional to sustainable development and direct their investment strategy to sustainable investments and activities. Such panorama of development regarding EU regulatory framework will necessarily lead to useful recommendations for Ukraine.

A. The European Union acting as a pioneer by establishing a clear and transparent framework for sustainable investments in the financial sector

1) *The EU Taxonomy Regulation*

161. The EU Taxonomy, entered into force on 12 July 2020, is a cornerstone of the European Commission Action plan on financing sustainable growth and was designed as a tool to help the financial sector to redirect capital flows towards environmentally sustainable activities. It was not meant to be a mandatory piece of EU legislation for all businesses and investors but it is a requiring transparency exercise for some EU companies that will fall within its scope. The EU Taxonomy should not be seen as a static rule of law but rather as evolving legislation that will take into consideration over the time technological breakthroughs and evolving economic activities.

162. As a consequence, in December 2021⁴¹, the European Commission published a first round of delegated acts completing the EU Taxonomy framework by delivering the first set of TSC providing criteria for activities to be considered as contributing substantially to the major

⁴¹ <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32021R2139>.

climate changes objectives of the EU, the climate change adaptation and climate change mitigation. These delegated acts in a summary form also provided criteria about activities that can be considered as respecting the “*Do No Significant Harm*” principal (“DNSH”), which is one of the fundamental principles of the EU Taxonomy. The EU Taxonomy climate delegated act is quite short and comprised only three provisions while all the detailed information and TSC, all considered economic activities are contained in the annexes relating to climate change mitigation and adaptation. All combined, there are 500 pages of detailed information regarding all the considered activities which should be used when assessing the environmental sustainability of a given economic activity of a potential investment. The delegated act had to apply from 1st January 2022, but as it only covers the first two environmental objectives (i.e. climate change mitigation and adaptation) the European Commission is expected to continue its work providing rules regarding the remaining environmental objectives (i.e. pollution prevention, circular economy, sustainable use of water resource and healthy ecosystems) to be able to implement them as of 1st of January 2023. It should also be mentioned that this process is taking quite some time for businesses and investors, especially with respect to TSC, so the full implementation of all these rules will most probably take more time.

163. The EU Taxonomy covers more than eighty (80) economic activities representing about 40% of the EU-domiciled listed companies, in roughly nine (9) major economic sectors, which are producing almost 80% of direct green gas emissions in Europe. This also means that some other activities are not initially covered by the EU Taxonomy. Therefore, some traditional industry activities or fossil fuel dependent activities should remain outside of the scope of the EU Taxonomy.

164. Clearly, to be eligible as sustainable under the EU Taxonomy, an economic activity followed by a non-financial company has to contribute to one of the sustainability objectives. The EU Taxonomy covers six (6) environmental objectives:

- Climate change mitigation,
- Climate change adaptation,
- Sustainable use and protection of water and marine resources,
- Transition of a circular economy,
- Pollution prevention and control, and
- Protection and restoration of biodiversity and ecosystems.

165. Therefore, other environmental or social objectives are not covered by the EU Taxonomy at this initial stage, but it is expected to see these activities covered by the European Commission while providing further EU legislation relating to the remaining environmental objectives. The use

of the EU Taxonomy in practice will apply directly to non-financial companies required to disclose information about their Taxonomy-aligned sustainable activities but also to financial companies required to report on their sustainable or also ESG (Environmental, Social and Governance) ratio of assets within a portfolio of investments.

166. Accordingly, to be qualified as sustainable, economic activities have to contribute substantially to one of the six environmental objectives, without causing significant harm to any of the other five objectives, while meeting minimum social and governance safeguards.

167. For example, the production of electricity by a hydroelectric plant can be considered a "sustainable" activity if it meets one of the following substantial contribution criteria:

- the power generation facility is a run-of-river plant and does not have an artificial reservoir;
- the power density of the electricity generating facility is greater than 5 W/m²;
- the lifecycle GHG emissions of the electricity generation from a hydroelectric plant are less than 100g CO₂e/kWh.

168. The EU Taxonomy also provides for transitional economic activities, which are those activities for which there is no economically or technologically viable low-carbon alternative, and can be considered to make a substantial contribution to climate change mitigation when these activities:

- have greenhouse gas emission levels that are in line with the best performance of the sector or industry;
- do not impede the development and deployment of low-carbon alternatives;
- do not result in a lock-in of carbon-intensive assets, taking into account the economic life of those assets.

169. Thus, the passenger rail business can be considered sustainable if its direct carbon dioxide emissions are zero (i.e. 100% electric or hydrogen powered trains) and it could also be considered transitional if, its direct carbon dioxide exhaust emissions are zero on a track equipped with the necessary infrastructure, and a conventional engine is used when such infrastructure is not available.

170. Therefore, the initial stage of using EU Taxonomy consists in determining if one, some or all activities performed by a company are covered by the EU Taxonomy and consequently, eligible as possible EU Taxonomy-aligned. The identification stage is very important for all companies and investors because it gives the initial input of all the sustainable activities or

investments that are covered or at stake, which also means falling under the scope of the EU Taxonomy. The identification of eligible economic activities relies on the statistical classification of economic activities in the EU, commonly referred as NACE code. Following, if an activity is not referenced under the NACE and deemed to be under the scope of the EU Taxonomy, it does not mean that it is not sustainable or harmful, but only that it may not be considered as EU Taxonomy-aligned. This is the reason why the climate delegated acts are adopted to add sustainable activities over the time.

171. The following stage, after the identification of activities falling under the scope of the EU Taxonomy, is to assess if the eligible economic activity meets the TSC of substantial contribution, which may include quantitative or qualitative thresholds. This approach ensures that an economic activity either has a substantial positive environmental impact or that it substantially reduces negative impacts on the environment. If, for example, an economic activity is aligned with climate neutrality and contributes to limiting the rise in temperatures, then it could be qualified as EU Taxonomy aligned with regard to the climate change mitigation objective.

172. The third stage requires analysis of the impact of such economic activity with regard to the DNSH principal because an economic activity may pursue an environmental objective but it may at the same time be harmful in its consequences to other sustainable or environmental objectives. Therefore, this is also seen as a double degree of assessment of a given economic activity with regard to its sustainable nature. These analyses are performed through a due-diligence process where a given economic activity is required to comply with TSC of the EU Taxonomy for DNSH. To demonstrate this, companies and investors need to disclose Principle Adverse Impacts (PAI) and set acceptable tolerances against specific indicators for PAI set out by the Regulatory Technical Standards (RTS) of the SFDR. Indicators for PAI are a set of pre-defined mandatory and optional data points such as carbon foot-printing, water and waste metrics and human rights policies, which help companies and investors to align their operational and investment-related data with identifiable technical metrics.

173. The DNSH principal is defined by article 17 of the EU Taxonomy. This article provides for what constitutes “*significant harm*” for the six environmental objectives covered by the EU Taxonomy:

- An activity is considered to do significant harm to climate change mitigation if it leads to significant greenhouse gas (GHG) emissions;
- An activity is considered to do significant harm to climate change adaptation if it leads to an increased adverse impact of the current climate and the expected future climate, on the activity itself or on people, nature or assets;

- An activity is considered to do significant harm to the sustainable use and protection of water and marine resources if it is detrimental to the good status or the good ecological potential of bodies of water, including surface water and groundwater, or to the good environmental status of marine waters;
- An activity is considered to do significant harm to the circular economy, including waste prevention and recycling, if it leads to significant inefficiencies in the use of materials or in the direct or indirect use of natural resources, or if it significantly increases the generation, incineration or disposal of waste, or if the long-term disposal of waste may cause significant and long-term environmental harm;
- An activity is considered to do significant harm to pollution prevention and control if it leads to a significant increase in emissions of pollutants into air, water or land;
- An activity is considered to do significant harm to the protection and restoration of biodiversity and ecosystems if it is significantly detrimental to the good condition and resilience of ecosystems, or detrimental to the conservation status of habitats and species, including those of European Union interest.

174. Therefore, an economic activity needs to prove that it does not fall under one of these indicators to be qualified as not harmful regarding environmental objectives. However, to be considered as EU Taxonomy-aligned, it also needs to demonstrate an assessed availability of and, where feasible uses, equipment and components of high durability and recyclability, easy to dismantle and refurbish at the end of their economic cycle with regard to the DNSH principle.

175. The fourth stage for companies and investors, is to assess if a given eligible economic activity of a non-financial company complies with the minimum social and governance safeguards as set forth in article 18 of the EU Taxonomy. This latest requirement, should be carried out to ensure the company's compliance with the guidelines of the OECD for Multinational Enterprises and the UN guidelines for businesses and human rights.

176. All the foregoing assessments represent the four conditions set by the EU Taxonomy for an economic activity to be recognized as EU Taxonomy-aligned. The final stage consists of calculating the percentage of alignment of an investment or of a non-financial company with the EU Taxonomy on the basis of various Key Performance Indicators ("KPIs") under the CSRD.

177. Further, the EU Taxonomy directly amends the SFDR by requiring some financial products, in particular those promoting environmental and social characteristics (i.e. article 8 products) or those with sustainable investment objectives (i.e. article 9 products) to calculate and disclose their alignment with the EU Taxonomy. Under the Eu Taxonomy, a particular focus is

given not on the categorization of financial products but rather around the percentage of sustainable investments or taxonomy-aligned investments are performed in these financial products.

178. Accordingly, three (3) categories of financial products are outlined in the EU framework to be able to fulfil clients' sustainability preferences:

- Financial products that pursue a minimum proportion of sustainable investments in economic activities that qualify as environmentally sustainable under article 3 of the EU Taxonomy;
- Financial products that pursue a minimum of proportion of sustainable investments as defined in article 2 (17) of the SFDR, where the minimum proportion is determined by a client or a potential client;
- Financial products that consider PAI of their investment decisions on sustainability factors, where elements of demonstrating that consideration are determined by the client or a potential client.

179. Following, financial products that promote environmental and social characteristics, without the promotion of sustainable investments or without the promotion of EU Taxonomy-compliant activities or where they do not consider PAI, will not be eligible for recommendation to clients or potential clients based on their individual sustainability preferences. This is one of the most challenging missions of all asset managers and financial advisors to properly choose the most appropriate sustainable investment for their clients.

180. The EU Taxonomy will have cross-sectoral implementation through other EU regulations and will require some reporting duties over the financial market participants.

181. Article 8 of the EU Taxonomy requires companies subject to the non-financial reporting requirements under the Non-Financial Reporting Directive (NFRD) are public interest entities with more than 500 employees to publish the following information:

- the proportion of their turnover derived from products or services associated with economic activities that can be considered sustainable;
- the share of their capital expenditure (CapEx) and the share of their operating expenditure (OpEx) related to assets or processes associated with economic activities that can be considered sustainable.

182. The EU Taxonomy also requires reporting under Articles 5 to 7, which are referring to the SFDR. Financial products covered by the SFDR will have to publish appropriate reporting. Thus,

financial products with a sustainable investment objective (Article 9 SFDR) and products integrating environmental or social features (Article 8 SFDR), will have to be subject to the following information disclosure:

- Information on the contribution of the investments underlying the financial product to one or more of the six environmental objectives;
- A description of how and to what extent the investments underlying the financial product are made in economic activities that can be considered sustainable, i.e. the share of the portfolio aligned with the EU Taxonomy.

183. Finally, financial products that do not have a sustainable investment objective or integration of environmental or social characteristics (Article 6 SFDR) have to be specifically declared.

184. As a consequence, the EU Taxonomy introduced a clarified and consistent framework that should give an additional comfort to businesses, investors and asset managers alike on their duties and obligations but opportunities to contribute to a more sustainable future and to create long-lasting impact and economic value.

2) *The Sustainable Finance Disclosure Regulation (SFDR)*

185. EU Regulation 2019/2088 on sustainability-related disclosure in the financial services sector, also known as SFDR seeks to provide transparency on sustainability within the financial markets in a standardised way by ensuring comparability and impeding greenwashing. The SFDR requires financial market participants and financial advisors to consider sustainability from a number of perspectives taking into consideration internal (i.e. integration of ESG factors in investment decisions) and external (i.e. assessment of how investments impact ESG factors for sustainability) considerations. The definition given by the SFDR (article 2) to financial market participants is quite broad including inter alia alternative investment fund managers, management companies of investment funds in transferable securities, investment firms which provide portfolio management services, insurance companies providing insurance-based investment product and institutions for occupational retirement provision together with financial advisors, which include different companies providing investment advice.

186. Thus, the SFDR provides specific requirements for financial market participants and advisors to act in the best interest of end investors, including among others, the requirements to conduct adequate due diligence prior to making investments. To be able to comply with such requirements, financial market participants and advisors have to integrate into their internal

processes and assess on continuous basis, not only the financial risks but also relevant sustainability risks that might have a material adverse impact on the financial return of an investment. The SFDR defines the “sustainability risks” as an environment, social and governance event or condition that, if, it occurs, could cause present or potential material adverse impact on the value of an investment. SFDR contains various transparency requirements on sustainability to be disclosed to investors at different levels both at financial market participants and product levels, such as pre-contractual information to be disclosed to investors has to be implemented as of March 2021.

187. According to Article 6(1) and (2) of the SFDR, financial market participants and advisors have to include certain specific descriptions in the pre-contractual information they are required to provide to investors. To be able to comply with the obligation under Article 6 of the SFDR, all financial market participants and advisors have to proceed to an assessment of whether sustainability risks are relevant at the level of each financial product, be it an alternative investment fund or an insurance-based investment product. It should be highlighted that Article 6 of the SFDR applies to all types of products and not only to those promoting environmental and social factors or to those with sustainable objective.

188. Further to such assessment, if the financial market participant of the investment advisor reaches the conclusion that sustainability risks are indeed relevant in respect of a specific product, according to Article 6 of the SFDR, it has to include in the product’s pre-contractual disclosures (a) a description of the manner in which sustainability risks are integrated into the investment decision, or as applicable, into investment or insurance advice, together with (b) an assessment on the likely impact of sustainability risks on the return of the product made available or advised on. A simple declaration that sustainability risks are integrated into the investment decision or investment insurance advice is not sufficient and financial market participants and advisors are expected to describe how much integration is achieved in practice.

189. Therefore, pre-contractual documents have to clearly disclose a qualitative and a quantitative description of the specific material likely impacts to show the likely impact of sustainability risks on a product’s return. If the outcome of such assessment is negative, the financial market participants and advisors are expected to provide a brief and clear explanation on the reasons why the sustainability risks are not relevant. Unless, pertinent reasons can be given for such an outcome for which sustainability factors are not relevant, not considering sustainability risks could be regarded as a breach of the applicable fiduciary duties towards investors.

190. Neither the SFDR, nor the draft level two of regulatory technical standards (“RTS”) issued by the European Supervisory Authorities (“ESA”) in February 2021 provided practical information on the exact form that the pre-contractual disclosures under Article 6 of the SFDR have to be made. Following the ESA has developed templates that have to be used to provide the required information in a standardised way to investors.

191. There are other financial products where sustainability is not only a matter of risk assessment, but rather a criterion for investment or a proper investment objective. Under the terms of the SFDR, Articles 8 and 9 are referring to those kinds of financial products. The difference between financial products from Article 6 (1) category and those falling under Articles 8 and 9 of the SFDR is the fact that sustainability becomes a binding commitment and can even justify an impractical for investment opportunities or even trigger divestment. If the financial product performs well in terms of sustainability or, on the contrary, if it fails to attain the objectives initially set, it may enhance or hinder relationship with investors.

192. Article 8 of the SFDR, also known as “*light green*” reference for financial products are those products promoting environmental and social factors among the full set of criteria that are assessed when considering an investment opportunity or managing assets in an investment portfolio. This sustainable facet aside, financial products will target and invest in companies and businesses that follow “*good governance practices*”. The SFDR does not elaborate much on what “*good governance practices*” are but provides that investee companies have to follow good governance practices in particular regarding sound management structure, employee relations, remuneration of staff and tax compliance to comply with the qualification of “*light green*” financial product. The main difference with Article 9 financial products lies in the fact that sustainability is an investment criterion but not an investment objective. Similar to disclosures to be made pursuant to Article 6 of the SFDR, it is up to the financial market participants and advisors to identify and determine which environmental and social factors they wish to pursue as part of their investment policy. They may choose to disclose only certain environmental vs. social factors or make a combination of both, depending of the specific investment objective of the financial product they are advising or providing to end-investors.

193. The list of sustainable factors is not defined and could be infinite so most of the financial market participants are using concepts such as SDGs of the United Nations or the concept of ESG factors developed by the EU Taxonomy to determine whether an investment is pursuing a sustainable goal. Pre-contractual disclosures pursuant to Article 8 relating to financial products shall provide (a) information how sustainable factors are met and if (b) an index is designated as a reference benchmark, information on whether and how this index is consistent with these

sustainable factors. Article 8 further reads that investment documents should also provide information of the methodology used for the calculation of the index of reference benchmark and where it could be found in pre-contractual disclosures.

194. The choice of an index is not required by the SFDR and shall be decided on a case-by-case basis by financial markets participants in light of the availability of data with respect to specific environmental or social objective and the willingness to provide quantitative and qualitative information to investors on the performance of the financial product. The choice of index is a critical question for financial market participants because there may be cases where the measurement of the impact is not possible due to the specificity of the factor for example in the social sphere. Another aspect to bear in mind is that where an index is designed, it is important to ensure that it is adequate to the features of the financial product and that it provides concise and valuable information to investors on the performance of the financial product.

195. Further, financial market participants and advisors should provide information in response to several questions relating to sustainability requirements and among others:

- Does the financial product invest partially in sustainable investment?
- What environmental and/or social factors are promoted and what indicators are used to measure the achievement of objectives?
- What investment strategy does a financial product follow, including the investment procedure implemented by the portfolio management with respect sustainability and its outcome?
- What is the asset allocation planned for a financial product between a group of assets aligned with sustainable objectives and others?
- Does a financial product take into account PAI on sustainability factors? Etc.

196. Thus, providing a standard template to financial market participants and advisors for all Article 8 financial products proves to be a handy tool for prospective investors interested in having and in-depth view on the sustainable profile of a given financial product without going through hundreds of pages of documents. It also enables the performance of a comparative analysis between financial products on their commitment regarding sustainability, and how sophisticated their procedures, and tools are providing a possible identification of the best candidates for investment.

197. Article 9 of the SFDR or also known as “dark green” provision for financial products that have either (a) sustainable investment or (b) contribute to the reduction of the carbon dioxide emissions. The SFDR defines sustainable investment as “*an investment in an economic activity*

that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance”⁴²

198. Therefore, a financial product may opt for Article 9 if, (a) it targets investments contributing to one of the sustainable objectives (including reduction of carbon dioxide emissions), (b) such investment does not significantly harm any other sustainable objective and (c) good governance practices are followed by invested companies. Under Article 9, financial market participants are required to provide statements in the pre-contractual disclosures on (i) how the designated index is aligned with that objective, (ii) an explanation of how and why this designated index aligned with that objective differs from a broad market index and (iii) where the methodology used for the calculation of the index may be found. Where no index has been settled, the investment documents should include an explanation on how that objective could be achieved. It should be highlighted that financial products having an objective of carbon dioxide emissions reduction, the information to be included should disclose (a) the objective low carbon emission exposure in view of achieving the long-term global warming goal of the Paris Agreement and (ii) where the methodology used for the calculation of the benchmark could be found. Article 9 further provides that where not EU Paris-aligned or EU Climate transition benchmark is available, the documentation shall provide a detailed explanation of how the continued effort of achieving the objective of carbon dioxide emissions reduction is ensured in view of reaching the long-term global warming goal of the Paris Agreement.

199. Thus, financial products compliant with Article 9 of the SFDR should provide information about among others all questions raised under Article 8 of the SFDR and in addition if the financial product has the objective of reduction in carbon dioxide emissions. This provision of the SFDR already requires an accurate and precise information about sustainable investment and deeper analysis from financial market participants regarding financial products.

⁴² Article 2 (17) of the SFDR.

200. The SFDR does not provide for a standardised approach of disclosure of information, thus Articles 8 and 9 are the sum of many factors such as the industry in which financial market participants and financial products are operating, existing and prospective investors targeted, the geographical location and nature of the assets invested in the financial product etc. It is an exercise of transparency because financial market participants are required to disclose what they actually have implemented in respect of a given financial product i.e. a picture of a financial product and not a presentation of an investment plan to be achieved in a certain period of time. For some other products, the strategy is to go further in the integration of sustainability factors by translating them into investment criteria or defining this matter as a focal point of the investment objective of the financial product. In such a case the pre-contractual disclosure should satisfy the requirements set forth under Articles 8 and 9 of the SFDR. The main purpose of the SFDR was to reduce inconsistency in principal agent relationships through the European Union member states, especially where environmental and/or social factors are promoted by investment funds (the so-called "*Article 8 products*"), or sustainable investments are the core objective of such funds (so called "*Article 9 products*"). Instead of simplifying the things from regulatory point of view, the SFDR was subject to many types of interpretation depending of the financial market participant and its market sector and objectives.

201. Hence, in three years, the SFDR was already amended by the EU Taxonomy and further clarifications are required from different European authorities including the European Commission. Thus, the issuance of the RTS by the European supervisory authority was a great challenge regarding the goals targeted by the SFDR taking into consideration of the size of the European market, the multitude of financial market participants and the diversity of financial products offered on the markets within the European Union and abroad and the willingness to protect as much as possible end-investors while stepping-into a booming financial segment. This is one of the first milestones in building a European sustainable investment environment and there is not a particular sanction for the time being on choice or implementation aside the reputational risks and the risk relating to non-compliance by a regulated financial product with respect to its legal and regulatory obligations. The integration of sustainability will certainly shift from a good governance practice to a mandatory rule with adverse financial consequences for financial products and market participants.

202. Accordingly, financial products such as green bonds have become a major and trended sustainable investment opportunity especially on the European internal market.

B. Other European proposal, recommendations and guidelines relating to sustainable investments within the European Union

1) *EU Green bond standard*

203. In 2007, the European Investment Bank (EIB) issued the world's first green bond, branded as a Climate Awareness Bond (CAB). Today, the EIB is the largest supranational issuer and is spearheading application of the EU taxonomy and EU Green bond Standard, championing EU standards globally. The EU is a global leader in green bonds, with 48 % of global issuances in 2020 being denominated in euros and 51 % of the global volume of green bonds being issued in the EU. In terms of volume, in 2020 the US was the top country of issuance, followed by Germany, France, China and the Netherlands; Sweden and Spain were also among the top ten countries worldwide. Europe has pioneered the green bond market, thanks to the world's first green bond issued by the EIB. Green bonds are starting to play an increasingly important role in financing assets needed for the low-carbon transition.

204. However, there is no uniform green bond standard within the EU. Establishing such a standard was a recommendation in the final report of the Commission High-Level Expert Group on sustainable finance. It was then included as an action of the European Commission on financing sustainable growth. Green bonds are becoming more and more popular. The green bond market, both globally and at EU level, grew by an average of 50 % per year in the period 2015-2020. Nevertheless, it represented only 3 to 3.5% of overall bond issuance in 2020. Even though forecasts predict it will reach USD 1 trillion of yearly global issuance in 2023. Consequently, there is a need for more rapid growth of a high-quality green bond market to achieve the targets in the Paris Agreement.

205. In June 2019, the Commission Technical Expert Group on sustainable finance (TEG) provided recommendations in its final report on EU Green Bond Standard⁴³. In March 2020, the TEG published a usability guide for the EU Green Bond Standard.⁴⁴ In the context of the public consultation on the renewed sustainable finance strategy, the European Commission launched a targeted consultation on the establishment of an EU Green Bond standard until 2 October 2020.

⁴³ Report on EU Green Bond Standards, EU Technical expert group on sustainable finance (TEG), June 2019.

⁴⁴ Usability guide on EU Green Bond Standards, TEG, March 2020.

206. On 6 July 2021, the European Commission published a legislative proposal for a regulation on European green bonds (the “EU Green Bond Proposal”)⁴⁵ which is should be the high quality voluntary European Green Bond Standard. Its intention is to use the potential of the single market for achieving the EU’s climate and environmental goals in a more efficient way. Shortly before, the International Capital Market Association (ICMA) updated its Green Bond Principles to reflect the record growth of the market for green bonds. Therefore, the changes that will be brought by the future EU Regulation on green bonds compared to the ICMA Green Bond Principles are of major interest for practitioners. The framework established by the ICMA Green Bond Principles is the set standard for green bonds. The new version of the Green Bond Principles contains further recommendations for even higher transparency requirements at issuer level. Furthermore, the heightened transparency at issuer level shall be achieved by providing information on (a) sustainability strategies and commitments and if applicable on (b) the degree of alignment of projects with official or market-based taxonomies. The latest version of the ICMA Green Bond Principles also expands the eligible green projects in the category “*Climate change adaptation*” to include projects that make infrastructure more resilient to impacts of climate change. In addition, the so-called “blue bonds” with the objective of emphasising the importance of the sustainable use of maritime resources and of the promotion of related sustainable economic activities are also captured as green bonds going forward. The ICMA Green Bonds Principals are the current leading set of rules while considering green bonds issuance around the world.

207. The EU Green Bond Proposal published by the European Commission is also a cornerstone of the European Commission’s Action Plan on financing sustainable growth and is overall closely aligned with the Paris Agreement and the sector specific criteria of the EU Taxonomy. The goal is to simplify the future issuance of green bonds through the alignment of definitions and harmonisation of external review processes. This should result in a faster transition of the European economy to carbon neutral and overall, less polluting technologies and production processes. At the same time, compliance with this EU Regulation would prove that the green projects are aligned with the EU Taxonomy and as a result of the high transparency requirements it would be easier for investors to identify environmentally sustainable investments. This should reduce the risk of greenwashing while ensuring market integrity. Furthermore, a consistent regulation at EU level is should also lead to a risk reduction regarding the fragmentation of the single market for environmentally sustainable bonds and ensure that there are uniform conditions for the issuer of such bonds.

⁴⁵ Idem.

208. The further development of the EU market for high quality green bonds is intended to maximise the potential of the single market for achieving the EU's climate and environmental goals. For this purpose, the EU Green Bond Proposal establishes a new gold standard for European green bonds, consisting of four key requirements that could be used to compare with and to adjust to other market standards:

- a) Taxonomy-alignment: the funds raised by the bonds should be allocated fully to projects that are aligned with the EU Taxonomy;
- b) Transparency: full transparency on how the bond proceeds are allocated through detailed reporting in an EU Green Bond factsheet;
- c) External review: all European green bonds have to be verified by an external reviewer to ensure compliance with the future EU Green bonds Regulation and EU Taxonomy alignment of the funded projects; and
- d) Supervision of reviewers by ESMA: external reviewers providing services to issuers of European green bonds have to be registered with and supervised by the European Securities and Markets Authority (ESMA).

209. Accordingly, the EU Green Bond Proposal sets higher requirements for the sustainability of the funded projects and, through increased transparency, provides stronger protection of investors against greenwashing.

210. Finally, there would be some flexibility for sovereign issuers: (i) public subsidy programmes and tax relief programmes would be exempt from project-by-project assessment, and the external reviewer would need only to assess the alignment of a programme's terms and conditions with the EU Taxonomy; (ii) sovereign issuers would be able to use state auditors as external reviewers, and state auditors would be exempted from the registration system. The EU Green Bond Proposal also contains an international dimension, which should help to promote the EU Green Bond standard. The adoption by the European Commission of an equivalence decision for a third country would allow third country external reviewers to offer their services. Until such a decision is adopted, a third-country external reviewer may provide its services after recognition from ESMA. Furthermore, a registered external reviewer located in the EU may apply to ESMA to endorse the services of a third-country external reviewer on an ongoing basis in the EU, provided that certain conditions are fulfilled. The final aim is to provide incentive to green bond investments and further issuance of EU Green Bonds.

2) **EU Regulation establishing EU Climate-Transition Benchmark**

211. The European Commission Action Plan for financial sustainable growth outlines a number of legislative initiatives, the first package of which includes an EU Taxonomy to determine whether an economic activity is sustainable, disclosure requirements for a range of financial market participants and new measures regarding investment benchmarks. The establishment of EU climate benchmarks has to provide for a harmonised, reliable tool to pursue low-carbon investment strategies by establishing a new category of financial benchmarks. The EU Regulation 2019/2089⁴⁶, known as the “*EU Climate Benchmark Regulation*”, was published in entered into force in December 2019, thus amending EU Regulation 2016/1011 known as the “*Benchmark Regulation*”.

212. The Benchmark Regulation established uniform rules for benchmarks in the EU. It defined a benchmark as “*any index by reference to which the amount payable under a financial instrument or a financial contract, or the value of a financial instrument, is determined, or an index that is used to measure the performance of an investment fund with the purpose of tracking the return of such index or of defining the asset allocation of a portfolio or of computing the performance fees*”.⁴⁷

213. It also provided for three different categories depending on whether one qualifies as a benchmark ‘administrator’, a benchmark ‘contributor’ or a benchmark ‘user’. A benchmark ‘administrator’ is defined as “*a natural or legal person that has control over the provision of a benchmark*” and is subject to several requirements including, but not limited to, the requirement to be registered or authorised by the national competent authority of the member state in which they are located and to have in place robust governance arrangements which include a clear organisational structure, processes to prevent or manage conflicts of interest and transparency.

214. The EU Climate Benchmark Regulation has amended the Benchmark Regulation to ensure the integrity of low-carbon benchmarks by introducing two new types of “*climate benchmark*” (i) the EU Climate Transition Benchmark (“CTB”) and (ii) the EU Paris-Aligned Benchmark (“PAB”).

215. Currently, there are a large number of low-carbon indexes on capital markets, often labelled and marketed in the same way, despite having different financial and operational targets.

⁴⁶ Article 1 (1) of the EU Climate Benchmark Regulation.

⁴⁷ Article 3 (3) of the Benchmark Regulation.

Therefore, clarification on these objectives was considered necessary to respond to growing concerns regarding potential green washing.

216. A CTB is a benchmark where the underlying assets are selected, weighted or excluded in such a way that the resulting benchmark portfolio provides for a “*decarbonisation trajectory*”, which is defined in the EU Climate Benchmark Regulation as a “*measurable, science-based and time-bound movement towards alignment with the objectives of the Paris Agreement*”.

217. A PAB is a benchmark where the underlying assets are selected, weighted or excluded in a way that the resulting benchmark portfolio’s carbon dioxide emissions are aligned with the objectives of the Paris Agreement. It is ambitious in its goals and selects only components which already actively contribute to the attainment of the temperature reduction target set out in the Paris Agreement. This means in essence that the carbon dioxide emissions savings of each underlying asset exceeds its carbon footprint.

218. The EU Climate Benchmark Regulation is intended to provide investors with a user-friendly tool for comparative analysis of low-carbon benchmark methodologies by obliging benchmark administrators to make significant disclosures regarding the methodology used to measure and reconcile ESG factors and low-carbon factors in the composition of CTBs and PABs. The EU Climate Benchmark Regulation requires administrators of all benchmarks or families of benchmarks, save interest rate and currency benchmarks, and subject to an opt-out for those benchmarks not pursuing environmental, social and governance objectives, have to provide certain disclosures:

- ESG methodology disclosures: from 30 April 2020, an explanation of how the key elements of the benchmark methodology reflect ESG factors;
- ESG benchmark statement disclosures: from 30 April 2020, inclusion in the benchmark statement of an explanation of how ESG factors are reflected in each benchmark. For those benchmarks or families of benchmarks that do not pursue ESG objectives, benchmark administrators only need to state clearly in the benchmark statement that they do not pursue such objectives; and
- Paris alignment disclosures: from 31 December 2021, inclusion in the benchmark statement of information on the degree of alignment with the target of carbon emission reductions or attainment of the long-term global warming target of the Paris Agreement.

219. Therefore, while the EU Climate Benchmark Regulation focuses on benchmark administrators, it may have an impact on benchmark users, such as portfolio and asset

managers. Historically, benchmarks incorporating constraints or objectives related to greenhouse gas emissions have lacked consistency and not been tailored to investor needs and constraints. They have also primarily been built around reducing tail risks, for example, that arising from investing in companies exposed to severe weather phenomena. In contrast, investors using the new CTBs and PABs can, at a portfolio level:

- Hedge against a wider array of climate transition risks:
 - o Policy and Legal Risk For example, risks related to changes in the regulatory framework, like carbon pricing mechanisms or those related to litigation claims;
 - o Technology Risk Impact of technological advancement in the transition to a low-carbon economy;
 - o Market Risk Changes in supply and demand for goods and services;
 - o Reputation Risk Arising, for example, through name and shame campaigns or corporate incidents (e.g. Volkswagen);
- Direct investments towards opportunities in the energy transition. These broadly include products and services related to renewable energy and energy efficiency.

220. The EU Climate Benchmark Regulation reinforces the EU's commitment to the transition towards a low-carbon and greener economy, the continuing growth of sustainable finance and the positioning of the financial sector as a leading global destination for investment in green technologies. As mentioned above, the main impact of the amendments to the Benchmark Regulation will be felt by those entities that are administrators of or contributors to benchmarks within the EU. Although non-EU asset managers are unlikely to be administrators of EU benchmarks, they may contribute to sustainable benchmarks. Asset managers that are administrators of CTBs and PABs will need to ensure that they are able to provide information to comply with the requisite disclosures as set out in the EU Climate Benchmark Regulation. They will need to understand the methodologies used to create the benchmarks and the information that administrators need to receive to ensure that information that they provide to administrators enables those administrators to comply with their obligations. Finally, asset managers that use CTBs and PABs will need understand the disclosures introduced by the EU Climate Benchmarks so that they can make meaningful use of the information and determine the extent to which benchmarks are genuinely focussed on ESG consideration.

221. While these are welcome developments, the adoption of the benchmarks may face bumps in the road which delay in implementation. With regards to scope of implemented climate data,

the CTBs and PABs set a new standard, so moving to the new framework will likely result in some disruption. For investors without any form of climate risk management currently, this will be even greater. Furthermore, the objective to meet the new climate benchmark requirements while also abiding by investment policy statements will likely make portfolio construction and investment strategy more complicated. For example, in order to meet a CTB requirement of cutting carbon dioxide emissions by 30%, and annual self-decarbonisation of 7%, while adhering to diversification and risk-adjusted return characteristics requires fairly sophisticated models. This is even more true for the PABs. Index investors, in particular, will have to weigh the benefits of incorporating climate data and the associated complexities with managing portfolio tracking error within limits. These challenges will require investment in employee and system resources to analyse, monitor and report on portfolio characteristics, as well as greater governance and oversight. Finally, some uncertainty exists regarding how investors should measure progress on green share and brown share investments given a lack of consistent definitions and measures.

3) *Proposal for a new EU Corporate Sustainability Reporting Directive*

222. On 21 April 2021, the European Commission adopted a proposal for a Directive on corporate sustainability reporting⁴⁸ (CSRD). The impact of this proposal on companies meeting the required thresholds that are based and operate within the EU is significant, because, for the first time, these companies will have to ensure that human rights and environmental reporting are an integral part of their core business.

223. According to the CSRD, companies have to prepare and take proactive steps to ensure that they have adequate systems of control in place to detect and mitigate potential human rights and environmental abuses within their companies and across global value chains. In addition, they have to demonstrate that they review and strengthen their governance and public reporting obligations.

224. The proposed CSRD applies to both companies based in the EU and companies based outside the EU but operating within the EU. The requirements set forth in the CSRD will apply to EU-based companies if:

- they are limited liability companies with more than 500 employees equivalent to full-time workers and an annual net turnover exceeding EUR 150 million; or
- they are limited liability companies (i) exceeding 250 full-time equivalent employees and an annual net turnover exceeding EUR 40 million and (ii) at least 50% of

⁴⁸ Idem.

that turnover is achieved in one or more of the following sectors: manufacture of textiles, leather and related products; agriculture, forestry, fishing, food processing and trade in agricultural raw materials, animals, food and beverages, extraction of mineral resources (oil, gas, coal, metals, ores and non-metallic minerals), manufacture of metal products, non-metallic mineral products and manufactured metal products (except machinery and equipment); and trade in mineral resources and mineral products (metals, ores, fuels and chemicals).

225. The proposed CSRD will also apply to companies based outside the EU if:
- they have generated a net turnover exceeding EUR 150 million in the EU in the last year; or
 - they had a net turnover exceeding EUR 40 million in the EU in the last year and at least 50% of their worldwide net turnover was generated in one or more of the sectors manufacture of textiles, leather and related products; agriculture, forestry, fishing, food processing and trade in agricultural raw materials, animals, food and beverages, extraction of mineral resources (oil, gas, coal, metals, ores and non-metallic minerals), manufacture of metal products, non-metallic mineral products and manufactured metal products (except machinery and equipment); and trade in mineral resources and mineral products (metals, ores, fuels and chemicals), providing that small and medium-sized enterprises (SMEs) do not fall directly within the scope of this proposal.

226. The future CSRD will further apply to the operations of the companies subject to their subsidiaries, and their value chains carried out by entities with which the company has an "*established business relationship*", defined as a business relationship that is directly or indirectly established, that is long term and that does not "*represent a negligible or merely incidental part of the value chain*".

227. The proposed CSRD also sets out minimum requirements that companies have to comply with to protect human rights and environment from adverse impacts. Human rights "*which directly affect a legally protected interest*" in a number of listed international conventions such as, inter alia, the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the Convention on the Elimination of All Forms of Discrimination against Women, the UN Convention on the Rights of the Child, the Palermo Protocol to Combat Trafficking in Human Beings and the International Covenant on Economic, Social and Cultural Rights, have to be fully protected.

228. Further, EU member states have to ensure that EU-based companies subject to the proposed CSRD "*adopt a plan to ensure that the company's business model and strategy are compatible with the transition to a sustainable economy*" and limit global warming to 1.5°C in accordance with the Paris Agreement. Such plan has to assess whether climate change is a risk to the company's operations and, if it is a primary risk, the company has to put in place specific targets to reduce its carbon dioxide emissions.

229. Companies concerned by the CSRD have to:

- incorporate the duty of care into all company' policies and appoint authorised representatives. Relevant companies have to implement a policy reflecting the company's approach to sustainability reporting, a code of conduct and a description of the procedures for implementing such reporting and ensuring compliance with the code of conduct;
- company executives are required to consider the short, medium and long-term sustainability implications of their decisions in the areas of human rights, climate change and environmental impacts. In addition, the board of directors of the companies concerned should establish and oversee the implementation of sustainability reporting measures and corporate due diligence policies;
- take appropriate measures to identify actual and potential human rights and environmental impacts arising from their activities, those of their subsidiaries and those in their value chain;
- prevent or appropriately mitigate potential adverse impacts and take actions to end actual adverse impacts. Where this is not possible, the company should minimise the adverse impact on human rights or the environment;
- conduct periodic assessments and monitor the effectiveness of their policies and sustainability reporting measures. These assessments should be carried out annually or whenever there is a reason to believe that significant new risks or adverse impacts may arise;
- communicate publicly about the duty of care by publishing the results on the company's website.

230. Moreover, the CSRD will require EU member States to set up a national supervisory authority to monitor and investigate the activities of the companies concerned by the directive, and may impose sanctions in case of infringement. Such a supervisory authority will have the power to:

- require a company to remedy any non-compliance or violation of the CSRD; and

- issue suspensive measures, impose financial penalties based on the company's turnover and require other interim measures to avoid any risk of serious and irreparable harm.

231. Therefore, if a company takes appropriate measures to comply with the requirements imposed by the CSRD, it will not be liable to pay damages for the adverse impact of an indirect partner with which it has an established business relationship. In this case, the company's actions will be a mitigating and potentially exculpatory factor. However, this exclusion does not apply to entities in the direct value chain.

232. The proposed Directive will have a significant impact on EU and non-EU based companies that meet the thresholds, once the requirements are transposed into national laws of EU member states. It will also have a profound impact on SMEs, which are excluded because of the thresholds but wish to continue to do business with companies that fall within the scope of the CSRD. Currently, the majority of companies concerned by the CSRD and based or operating within the EU do not have adequate systems and processes in place to meet the requirements of the proposed EU directive. It is therefore essential that companies act now to be able to comply with the CSRD and to facilitate the implementation of the European Commission Action Plan for financing sustainable growth.

V.PART IV: WORLD BANK RECOMMENDATIONS FOR DEVELOPPING NATIONAL GREEN TAXONOMY

233. In June 2020, the World Bank⁴⁹ published a guide relating to the development of a national green taxonomy providing an initial framework approach to all countries around the world that were already engaged or contemplating to engage into a transition process to a more sustainable and green national economy⁵⁰. The primarily focus of the guide was at regulators in emerging economies seeking to transform their national economies in more sustainable economies. It was prepared on request by the Central Bank of Malaysia. It is intended to offer recommendations for a coherent framework of tools for the financial sector on environmental issues and to support decisions by financial institutions related to climate-related risks in terms of providing sustainable investments and sustainable financial products.

⁴⁹ The World Bank Group consists of nine institutions: the International Bank for Reconstruction and Development, the International Development Association, the International Finance Corporation, the World Investment Guarantee Agency and the International Centre for Settlement of Investment Disputes.

⁵⁰ Developing a National Green Taxonomy: A World Bank Guide, June 2020.

234. This World Bank guide provides an initial insight about the need for clarity and transparency of financial market participants regarding what could qualify as “sustainable” or “green”. Drawing on its experience in shaping the debate on sustainable finance and its understanding of the highly diverse national contexts of developing countries, the World Bank defined several essential principles and methodologies for developing a taxonomy of environmentally sustainable activities and investments.

235. Thus, the World Bank is actively promoting the idea of a well-regulated global sustainable finance market providing excellent investment opportunities and reduced investment risks. It is already well established that a well-defined and structured national taxonomy can support more informed and efficient decision-making and respond to investment opportunities that support the achievement of national environmental objectives. Although, the lack of formally harmonised definitions and appropriate rules regulating national financial markets with regard to sustainable investments will cause market actors to adopt their own definitions, which will be different from one actor to another and thus will result in the absence of reliability and efficiency. Therefore, an appropriate and clear national green taxonomy will be of crucial importance and essential guidance to domestic financial markets, especially in emerging countries. The recommended approach builds on the experience of the World Bank in supporting similar initiatives in Colombia, Malaysia, Mongolia and East Africa and its role worldwide in promoting a positive social and environmental impact and developing a global sustainable market.

236. Therefore, the guide developed by the World Bank could be very useful for Ukraine, willing to develop its own green taxonomy model providing an enhanced and secured financial environment for the development of sustainable activities and attracting international capital flow focused on sustainable investments. The approach of the World Bank set out in the guide will require significant application to the current situation of Ukraine, including its national environmental policy and capacity in the financial sector.

237. It is important to highlight that the World Bank used the ICMA⁵¹ definition of green taxonomy providing the following “*a green taxonomy is a classification system for identifying activities or investments that will move a country toward meeting specific targets related to priority environmental objectives. An identified environmental target is an aggregate result a country wishes to achieve over a defined timeline - for example, a net reduction in emissions or deforestation by a given year*”.

⁵¹ ICMA, May 2021 “*Overview and Recommendations for Sustainable Finance Taxonomies*”.

238. Therefore, the World Bank considers that an efficient and reliable national green taxonomy has to be focused on achieving an environmental objective. It has to establish domestic environmental targets and results to be achieved over time and in line of particular environmental objectives. Following to be able to proceed as recommended by the World Bank, it is essential to define a general approach in developing a national green taxonomy (A) and to identify the key components of the development of a such a taxonomy (B).

A. General approach in developing national green taxonomy

239. The World Bank guidelines establish a general approach in developing national green taxonomy, which is providing for two main concepts relating to strategic development and technical planning of the process of shaping the national green taxonomy. This process will necessarily require a wide range of experts from different fields willing to support this national initiative.

240. An important recommendation of the World Bank is the need for a substantive analysis and research regarding environmental matters to develop a reliable national green taxonomy. It is essential according to the World Bank's recommendations to focus on the highest priorities and to identify the most appropriate economic sectors and categories of investments that would benefit from green labelling. This process of key sector identification will require technical expertise in specialised areas such as climate, environment, energy, forestry, biodiversity and many sectors.

241. Thus, to identify the content and the boundaries of the future national green taxonomy, the guidelines of the World Bank are suggesting to go through six (6) main steps as follows:

1. Identification of environmental strategic goal;
2. Selection of environmental objectives that are aligned with strategic environmental policies and country's long-term economic and environmental development;
3. Identification of all sectors that are expected to achieve these environmental objectives;
4. Evaluation and selection of specific investments in these sectors that support the achievement of the identified environmental objectives; an important indicator in the selection process should be the estimated effectiveness of these investments in relation to the environmental objectives established by the country;
5. Identification of the potential users and beneficiaries of the green taxonomy, their roles and respective responsibilities for the implementation of such green taxonomy;

6. Identification and clear description of the reporting indicators to be provided by the market participants that use green taxonomy parameters.

242. It is clear from these statements that the World Bank guidelines are focusing on the achievement of objectives. This is one of the most important criteria while developing a national green taxonomy. It is essential to understand what stands behind such steps provided in the guidelines.

1) *Identification of strategic environmental goals*

243. The identification process has to be handled on a large-scale including all national economic sectors that are going to be impacted by the framework of the green taxonomy. Such identification will provide initial inputs of the fields and the topics which should be analysed while developing the national green taxonomy. The goal of developing a national green taxonomy is to ensure that the future economy of a given country is environmentally sustainable, providing a suitable and reliable regulatory framework for all sustainable activities and investments. Such national green taxonomy should further focus on developing standardised definitions of green activities and investments, which should lead to achieving national environmental priorities and sustainable development goals. Such initiative will support and enhance the green growth of domestic green financial markets and will increase the number of responsible investors, implementing sustainable investment strategies in the domestic and international markets. Clear and detailed identification of environmental objective will also facilitate the reporting process of all public and private investments dedicated to sustainable development providing technologically sound and aligned with international best practice processes. It will also show all underinvestment sectors that will need to be taken into account while implementing a national green taxonomy.

244. Finally, the identification of the environmental objectives will lead to a better spread of information to end-investors and will enlarge the part of financial markets dedicated to sustainable investments thus shifting the national economy towards achieving environmental objectives.

2) *Selection of environmental objectives*

245. The selection of the national environmental objectives of a given country should rely on the choices of environmental policies pursued by the country. The national green taxonomy

should be shaped in accordance these national environmental policies, which should be in accordance with the sustainable development of the country. The selection of environmental objectives may include the promotion of a climate change adaptation activities, which is one of the main goals pursued by many countries around the world, thus reducing the vulnerability of the country's environment due to the climate change⁵². It could also be clean energy supply, a very sensitive topic, especially for European countries. It could also be the protection of the country's natural resources (water, land, forests) by promoting and facilitation low-carbon activities for the future. This selection of environmental objectives should also be aligned with existing national environmental laws and regulations, including any contractual obligations under international treaties.

246. In addition, the World Bank recommendations are also providing that the development of a national green taxonomy should follow specific environmental objectives such translated into specific targets, e.g. achievement of a specified target-percentage of renewable energy supply for the domestic energy needs of a country, or a particular level of reduction of water pollution or an enhanced treatment of polluted waters, or the implementation of specific climate change adaptation measures as, for example, required under the United Nations Framework Convention on Climate Change. The World Bank guidelines are advising setting national objectives as a minimum level of expectations, which will help directing financial flows to sectors that are not yet able to shift from low to zero carbon yields. Thus, investments that improve such minimum target level should also be included in the national green taxonomy framework.

247. Developing countries face many challenges in achieving environmental objectives and the implementation of a reliable green taxonomy framework often lags behind policy and regulations. The selection of the most suitable environmental objectives considering the particular environmental, geopolitical and social status and ambitions for development will shape the overall goals to be achieved by the national green taxonomy. The primary ambition of a country willing to develop an appropriate green taxonomy will be focused on increasing capital flows towards environmentally sustainable activities. Therefore, countries may choose environmental objectives where financial flows play a key role, thus ensuring a significant and quick progress. If, for example, a given country lacks a clear policy framework and capacity to reduce fossil fuel dependency, it can focus on other environmental objectives where actions are possible and could lead to achievement of environmental objectives.

⁵² Joint Report on Multilateral Development Banks, Climate Finance 2017.

3) Identification of sectors and investments that could achieve environmental objectives

248. The World Bank guidelines are also advising that relevant sectors of national economies should be identified on the basis of their estimated contribution to the achievement of the national environmental objectives. Such identification could be based on existing national sectoral classifications used by national authorities or by international standardised classification systems such as Statistical Classification of Economic Activities in the European Community (NACE). The relevant sectors can also be derived from environmental policies, laws and regulations. For example, air quality standards for urban air pollution are likely to be implemented in the transport, energy and industry sectors. A review of the public sector budget classification, reporting and verification systems used for measuring and reporting on climate finance can also provide useful information. Such identification should also take into consideration the existing green financial products and associated risks in the banking sector could be very useful. Regardless of the initial input, all sectors and related investments suitable to convey sustainable activities and investments in accordance with national environmental objectives should be covered by the national green taxonomy.

4) Evaluation and selection of investments supporting environmental objectives

249. The World Bank guidelines are expressly providing for the selection and evaluation of specific investments within defined sectors and categories of the national economy, because these investments will play a key role in the achievement of national environmental objectives. The main objective in developing a national green taxonomy is to select specific investments within the defined sectors and categories. For example, an appropriate selection and evaluation of specific investments in the context of a national environmental objective relating to climate change mitigation (providing requirements on reduction of CO₂ emissions in a given year) can be determined by whether it meets the defined threshold for carbon intensity (e.g. gCO₂e/unit of production) in terms of compliance to the baseline of national energy standards. In the biodiversity category, activities can be based on their compliance with nationally accepted branding and standards or with, for example, global Standard for the Identification of Key Biodiversity Areas of the World Commission on Protected Areas (IUCN) in association with the IUCN Global Species Programme. Examples of the transport sector in the context of air quality objectives include whether the transportation technology meets certain air emissions standards

and whether the improvement of mass transport meets national or international environmental standards.

250. Therefore, the evaluation and selection of specific investments will guide investment decisions of investors on the financial markets to direct capital flows to those activities that are providing a clear and reliable financial environment for sustainable investments base on safe and predictable standards.

5) *Identification of the potential users and beneficiaries of the green taxonomy*

251. This step is crucial with regard to the development of a national green taxonomy. The World Bank guidelines are recommending a clear identification of the users and beneficiaries of the green taxonomy because, they will play a key role in its implementation. The banks, financial institutions and regulators, bond issuers, asset managers and owners and all potential investors will be the actors of the future green economy of a given country.

252. The green taxonomy should provide clear information of how users and beneficiaries will use the taxonomy at the outset. There should be clear rules regarding, for example, the banks and non-financial institutions of how to assess compliance with the requirements for green financial products. Such identification will provide information of the volume of green products on the capital markets and will define the part of sustainable investments within a given national economy. This will provide a country with an overall view of the percentage of sustainable investments at a given moment but also of the increase of sustainable activities supported by the implementation of a national green taxonomy. It is expected that green taxonomy users and beneficiaries will act in compliance with the requirements and reporting practices, and that standard setters will set the appropriate caveats in line with the green taxonomy.

6) *Identification and clear description of reporting guidelines*

253. The World Bank guidelines are strongly recommending to define appropriate reporting guidelines providing reliable assessment and reporting standards regarding sustainable activities and investments. National authorities that formulate a green taxonomy framework can be encouraged to monitor its effectiveness in directing financial flows towards priority environmental objectives. Such monitoring should provide transparency including mandatory or voluntary assessments to how users and beneficiaries report on the adoption of the green taxonomy.

254. A mandatory assessment will ensure regular and consistent reporting by all relevant market actors, stakeholders, users and beneficiaries, thus, enabling the national regulator to control capital flows directed into sustainable investments to achieve key environmental objectives. Financial regulators could be required, for example, to discourage certain types of stakeholders (i.e. certain energy-intensive industries) using company turnover, revenues, capital expenditures and others as relevant indicators to promote or strengthen their market position compared to environmentally-friendly economic activities supported by other stakeholders in line with national environmental objectives. In such a case, green financial products can be measured using nominal value, market-based accounting and other indicators clearly showing their compliance with a country's environmental policy. Other national green taxonomies may favour financial intermediation, in which case the relevant performance indicators may include the recorded value of green financial products or the return of the average interest rates on loans, among others. According to a voluntary assessment, relevant market actors, users and beneficiaries could be allowed to decide on the volume and frequency of reporting as a part of a requirement for regular disclosure of non-financial information. According to either assessment, the reporting should provide information regarding financing and investment flows and revenue generation (i.e. environmental topic, type of activity, sectors, etc.).

255. Finally, a national green taxonomy framework could also provide useful information for users and beneficiaries interested in disclosure regarding expected environmental outcomes or impacts of their investments, such as reporting required by a given financial instrument (i.e. green bonds). Therefore, the particularities of a given country will shape the establishment of appropriate criteria for reporting and monitoring in the implementation and the outcome of a national green taxonomy.

B. Identification of key components of the development of a national green taxonomy

256. The World Bank guidelines identify several key components of a reliable national green taxonomy such as users and main actors (1), implementation considerations (2) and processes to be followed while developing a national green taxonomy (3).

1) *The role of the users and main actors of a reliable national green taxonomy*

257. The World Bank guidelines are providing useful information and recommendations regarding the potential use of a national green taxonomy with regard to users and main actors of its implementation. The following categories are directly targeted by the World Bank guidelines:

- a) Banks and financial institutions could possibly use the national green taxonomy as a tool to efficiently improve green lending and green financing of economic and investment activities. This should lead to a reduction of transaction costs through a faster identification and verification of accepted assets using the green taxonomy as a reliable green finance classification. The assets covered by the green taxonomy could be used as a guarantee for sustainable investments thus reducing the investment and reputational risks;
- b) Financial regulators should support the greening of a given national economy by providing and supporting regulatory actions based on the provisions of a national green taxonomy to encourage banks and financial institutions to lend and to finance eligible companies providing green investments. They could also measure the growth of capital flows towards national environmental priorities at national and even international level. Financial regulators should support the creation of national reporting guidelines and the implementation of rules regarding the disclosure of non-financial information to be able to properly assess sustainable/green activities and investments. An important role is given to financial regulators regarding risks of greenwashing and mitigation of the reputational risks for companies and private investors;
- c) Investors should be able to use the national green taxonomy to identify their capacities to meet portfolio investments criteria relating to sustainable or impact investing. This will also enhance their skills and understanding of the impact of sustainable investments and the developing of an investment policy in line with end-investors' expectations;
- d) Green bond issuers and other relevant entities such as debt issuers should identify acceptable sustainable activities using the green taxonomy that can be easily financed by means of appropriate contributions in a form of a debt investing; and

258. Politicians and others should be able to support the development of green projects and activities at national level, which are aligned with national environmental objectives. Politicians could also be in charge of the identification of areas of underinvestment and deficit of capital flows on national financial markets. They should also act proactively to develop national

strategies and environmental policies that meet national environmental priorities and international commitments such as the Sustainable Development Goals (SDGs).

259. Therefore, there is a wide range of potential users interested in the existence of a reliable national green taxonomy. Such national regulatory framework will facilitate green activities at national level and will provide direct access to “sustainable/green finance” to all qualifying projects, companies and private investors. A reliable national green taxonomy should also protect users and beneficiaries of the green taxonomy from greenwashing, one of the major risks constantly faced by companies and investors interested in sustainable/green investing. However, the main goals of such an approach remain the achievement of national environmental objectives and direction of investment flows into appropriate sustainable projects.

2) Key implementation considerations of the World Bank guidelines

260. The guidelines of the World Bank provide that the definition of a national green taxonomy should be developed in line with the national environmental goals, laws, regulations and green labelling standards. Countries developing green taxonomy should always focus on providing a technical basis for activities and investments that are considered as green, using a science-based approach to explain the relation between activities and national environmental goals. This approach is consistent with international practice developed by common principals used by other taxonomies such as the EU taxonomy or the Climate Bonds Taxonomy⁵³. The latter provides for a common climate bonds standard based on specific criteria of bonds labelled as green or sustainable evaluated in terms of their alignment with the Paris Agreement and the SDGs.

261. Another important implementation consideration is to address cross-cutting and societal risks. Thus, national green taxonomy could include a section describing a national and sectoral framework addressing potential transfer of risks from one environmental objective to another or across different categories of objectives. A description of risk mitigation systems enshrined in existing national standards, policies or regulations informs users of how these potential risks are addressed. Appropriate reference should be provided to these national and sectoral regulations.

262. The national green taxonomy should be recognised at national level as a formal classification for filtering sustainable investments in both public and private sectors. Countries should also understand and consider lessons learned from other countries that already have national green taxonomies in place. The national green taxonomy should succeed in catalysing

⁵³ *Climate Bonds Taxonomy*, Climate Bonds Initiative, September 2021.

targeted sustainable investments to the extent of the country's ambition with regard to environmental objectives without the support of policy and national regulations. An efficient national green taxonomy should provide dedicated incentives (such as fiscal incentives, soft credit lines, guarantees, etc.) which support and sustain environmentally-friendly activities, including low-carbon and climate-resilient development. Such initiatives could include lower capital or ratio-risk investment requirements for sustainable financial products, the establishment of regulatory criteria and lower refinancing rates based on sound market research.

3) *Principals and processes to be followed when developing national green taxonomy*

263. The World Bank guidelines are supporting some essential implementation principals that should guide countries' decisions and green taxonomy implementation process such as:

- a coherent and easily understandable language allowing to avoid any ambiguity for the financial sector, because the main actors of the implementation of a national green taxonomy are quite often financial users and investment beneficiaries;
- requiring the insights, research and science-based opinions of technical experts willing to participate to the elaboration of a national green taxonomy. Experts from financial and industrial sectors should also be consulted in specific fields, while developing a green taxonomy;
- ensuring consistency of approach with international best practices. Where possible, the suitability approach should be aligned with international best practices to provide harmonisation between different countries' jurisdictions, disclose its scientific background to national and international investors, and enhance market integrity. A national green taxonomy, which is aligned with others at the international capital markets, will support international capital flows and provide a given country with direct access to a growing international pool of green capitals and investments.

264. The national green taxonomy should also be developed jointly by policy makers and financial users, such as investors, in close coordination with national authorities. Thus, it will enhance the country's sustainable development priorities and the support and promotion of environmental protection and climate actions by national authorities. It is strongly recommended by the World Bank to consult national stakeholders in all sectors, including industrial corporations, small- and medium-sized enterprises (SMEs), financial service providers and asset owners, private investors etc. Direct input and participation of relevant stakeholders is a critical component for the establishment of a robust green taxonomy.

265. The World Bank also recommends that a steering committee or working group of key stakeholders and local technical experts is established to facilitate the development of the green taxonomy. Given the fact that a detailed green taxonomy will certainly induce a certain level of complexity, the goal of the working group will be to help ensuring a technically sound processes by providing high-quality technical expertise.

266. The World Bank considers in its guidelines that countries willing to develop strong and reliable green taxonomy could adopt a plan of action including the following steps:

- Establishment of an expert working group to lead and coordinate the development of the green taxonomy which should include Ministry of Finance, Ministry of Natural Resources, Ministries and governmental agencies or organisations responsible for setting national policies on climate change and development and economic planning; Authorities responsible for the supervision and regulation of the banking and insurance sector and the securities market; Financial institutions in general, especially those supporting sustainable investments; investors; stock exchange representative and all other stakeholders that could be concerned;
- Definition of the strategic goals of the national green taxonomy;
- Identification of national environmental objectives;
- Providing mapping of all additional actions to be handled in the country, including existing initiatives, incentives and mechanisms for green finance in relevant beneficiary sectors, as well as existing guidelines and certification schemes for identifying or defining relevant green activities;
- Review and consideration of the lessons learned in comparable jurisdictions at international level, prioritising national environmental objectives and requirements;
- Drafting and implementing a national plan of action;
- Cooperation with local technical experts in the drafting of the national green taxonomy;
- Review of the project of green taxonomy ensuring consistency and compliance with national and sectoral priorities, objectives and requirements for climate and environmentally sustainable development, general market and policy developments in the financial sector of the country and existing tax and other incentives relating to green investments;
- Formal consultation with the relevant stakeholders involved in environmental and regulatory improvement programmes; banks, banking and insurance associations together with asset managers and owners and actors from key sectors of the national economy that would most likely benefit from a green taxonomy; the civil and scientific communities, international organisations and investors;

- Consolidation and incorporation of relevant experts' and stakeholders' opinions and views;
- Planning of the process from the beginning to full implementation of the green taxonomy; and
- Regular update based on new information and changes in technology.

267. All these steps should be used by countries as a roadmap supporting the development and implementation of a reliable national green taxonomy. A third party with significant experience and global knowledge, such as a multilateral development bank, can help coordinate efforts, exchange international knowledge and facilitate the adoption of national green taxonomies around the world.

268. Finally, the guidelines of the World Bank are providing, through its appendix, useful examples of developing taxonomy-eligible activities for clean urban environment and sustainable land use. Such examples could provide appropriate for countries to facilitate their efforts in the choice of the most efficient national approach in developing green taxonomy. The guidelines are also providing an overview of existing taxonomies to better inform countries that are on their way of developing a national green taxonomy about the regulatory frameworks developed in other jurisdictions and the results achieved by these countries.

VI.PART V: RECOMMENDATIONS FOR UKRAINE

269. Ukraine is one of the most polluted and environmentally problematic countries in Eastern Europe. Its level of environmental pollution is several times higher than in other Eastern European countries. Thus, Ukraine has one of the worst ecological records of all the post-Soviet territories. The Ukrainian government, however, wishes to increase the quality of life of its citizens and provide significant efforts in the transition to a climate-resilient economy complying with its Paris agreement commitment. While considering the current state of greenhouse gas emissions in Ukraine, it is crucial to draw attention to the economic sectors that are eminently environmentally unfriendly. Heavy industry, especially mechanical engineering, ferrous metallurgy, and the coal industry make up a large proportion of the structure of Ukrainian industry. Heavy industry accounts for more than 80% of the total value of industrial goods sold. Over the years the electricity and heating sector has been the highest contributor to harmful gas

emissions, being responsible for some 20% of these, followed by the metal-extracting and transformation sector.

270. In March 2014, Ukraine entered into an association agreement with the European Union which provided several opportunities to Ukraine to introduce new environmentally friendly market incentives and political recommendations into its long-term economic strategy. The economic part of the agreement allowed the European Union standards to be embedded in the key sectors of the Ukrainian's economy. The purpose of this agreement was to support the main reforms aimed at regenerating and developing the Ukrainian economy, thus encouraging sectoral cooperation between Ukraine and the European Union in the field of industry, energy, climate change prevention, industry, social development and consumer protection.

271. However, and despite the fact that the European Union is supporting the necessary economic and policy changes in Ukraine, the latter continues to face difficulties in establishing a clear regulatory basis for its future sustainable development. Thus, even if there is a clear increase in environmental awareness over the years in Ukraine, the majority of public and private companies are facing an inability to utilise their resources accordingly. The financial insolvency of many Ukrainian producers makes investments in new-technology equipment not possible. In addition, the armed conflict between Ukraine and the Russian Federation will have a significant impact on the Ukrainian economy, which has already weakened since 2014. Once these problems are resolved, Ukraine will be able to restore its industrial facilities and infrastructural systems. Consequently, most of heavy-industry sectors will continue to generate a larger amount of carbon dioxide emissions.

272. Further and because of the current war with the Russian Federation, Ukraine will need to lower its gas imports and replace them with coal, as the most accessible alternative for the moment. At the same time, it will be required to comply with the Paris agreement objectives and to develop its national energy strategy towards completely abandoning fossil fuels and transitioning to a climate-resilient economy. The shift to coal-fired energy production will make it very difficult to avoid an increase in the carbon dioxide emissions. Therefore, harmful gas emissions in Ukraine are meant to increase and not to reduce by 2030. Following, Ukraine will require not only the mobilisation of domestic climate finance but also an important number of international investments to comply with its obligations under international climate agreements. For that reason, Ukraine's declared goals of reducing harmful emissions do not entail a precise commitment to real emission reductions. Nevertheless, the Ukrainian government is very dedicated to its commitment to shift to a low-carbon and resilient economy in the near future,

because Ukraine's economy is one of the most energy-intensive in the world and the country has considerable potential for saving energy and reducing harmful emissions.

273. Consequently, Ukraine has already established and implemented some domestic legislation with regard to green finance, especially with regard to green bonds issuance on the capital markets. In June 2021, the Ukrainian law on "*Capital Markets and organised Commodity Markets*"⁵⁴ was implemented into national legislation, which established Ukrainian green bonds as a new financial instrument. The law defined the bonds as a type of financial instrument, depending on the purpose of using the borrowed funds, can be ordinary, green or infrastructural. Green bonds are meant to be these bonds whose prospectus determines the use of the received funds solely for the financing of an environmental projects or a particular sustainable activity.

274. Nevertheless, the efforts deployed so far by the Ukrainian government and local authorities are not enough to stimulate the transition to a climate-resilient economy. Different other green financial tools, such as green credit, green stock indices and many more are a part of the green financial system and will need to be taken into consideration. In addition, various other policies, incentives, and projects have supported the efficient implementation of the green financial system, that reduces the number of investments channelled into industries that negatively affect the environment and, in turn, provide much-needed support to green industries investments. This pathway will provide advantages not only for the domestic economy but also for the development of new energy technologies, new energy sources and new environmentally friendly industrial equipment of Ukraine.

275. The successful implementation of a green financial system is not possible without the improvement of financial institutions and markets, alternatively, without developing new financial instruments. Ukrainian government and public regulatory authorities have to create a harmonised green classification system to determine which activity can contribute to the green economy and make finance more sustainable. A standardised roadmap on climate-related practices will simplify the spread of information to investors, thus providing better transparency and more security and certainty while investing in green financial instruments and products. Therefore, the future Ukrainian green taxonomy should provide a significant measure in directing capital flows of green funds into the environmental sector. A competent legislative group should be formed to elaborate the green classification system, as well as a technical group for its adaptation. Such type of regulatory initiative should be accompanied by the creation of disclosure duties and reporting standards to reduce the risks of greenwashing.

⁵⁴ <https://zakon.rada.gov.ua/laws/show/3480-15#n2163>.

276. Accordingly, the following mapping framework could serve as guidelines of how to structure the initial methodological approach of Ukrainian government and public regulatory authorities to create a reliable and solid green finance taxonomy:

- 1) Identify all economic activities and financial instruments that will be concerned and affected by the green finance taxonomy;
- 2) Familiarise with principals of green taxonomy using existing developments in green taxonomy in other jurisdictions;
- 3) Gather not only government representatives but also public and private sector stakeholders, and regulatory authorities, while working on the green finance taxonomy project to ensure that all the opinions and views are taken into consideration in the preliminary stage of the process of drafting;
- 4) Provide clear and precise definitions of economic activities and financial instruments under consideration that substantially contribute to climate change adaptation and mitigation;
- 5) Provide an empirical approach to concept like “*Do No Significant Harm*” and “*Minimum Social Safeguards*” or create proper concepts of defining the impact of economic activities on environment with regard to climate change;
- 6) Establish technical screening criteria enabling a detailed and concrete assessment of an economic activity to be considered as green or sustainable, thus providing taxonomy-aligned financial metrics;
- 7) Set benchmarks to secure the proper functioning of green finance aligned financial instruments;
- 8) Establish disclosure duties and particular reporting standards linked to technical screening criteria to be able to properly ensure the most reliable transparency while investing in green and sustainable projects;
- 9) Ensure that all the international climate-related agreements are taken into consideration while drafting the green finance taxonomy to avoid inconsistency and locking of international capital flows; and
- 10) Foresee an appropriate update and upgrade of the green finance taxonomy regulatory basis with regard to the constantly evolving climate change challenges.

277. Following, Ukrainian authorities could also take into consideration the fact that green finance represents a positive shift in the global economy's transition to sustainability through the financing of public and private green investments. Public policies have to support green initiatives either on domestic but also in international capital markets. Two main tasks of green finance are to consider environmental externalities and the reduction of risk perceptions to encourage investments that provide environmental benefits. The major actors driving the development of green finance include banks, institutional investors and international financial institutions as well as central banks and financial regulators. Some of these actors implement policy and regulatory measures for different asset classes to support the greening of the financial system, such as priority-lending requirements, below-market-rate finance via interest-rate subsidies or preferential central bank refinancing opportunities. This is also the path that should be adopted by the Ukrainian authorities. Therefore, some of the most important recommendations that could be provided to Ukrainian authorities is to start by providing a reliable regulatory, financial and transparency framework for domestic green finance and investments.

A. To designate principals specifically focused on environmental goals consistent and aligned with the Paris Agreement (Country Action Plan for Sustainable economy)

278. Ukrainian authorities should take as example the EU approach to plan and identify a clear, consistent and reliable (feasible) framework of principals that will lead public and private sector to the shift from industry and fossil fuels economy to a more sustainable and green activities further enhancing a future green economy.

279. Ukrainian authorities could, for example, provide incentives in financing of public and private green investments, including preparatory and capital costs, in the following two areas (i) environmental goods and services such as climate change mitigation and adaptation combined with landscape pollution and (ii) prevention, minimisation of and compensation for damage to the environment and to the climate, such as dams or measures for increasing energy efficiency, using clean energy. It is a well-known fact that Ukraine is strongly depending on fossil fuel energy generation, therefore defining a clear domestic policy with respect to clean and renewable energy generation opportunity draw attention and raise funds for green financing of renewable energy projects on the capital markets. Following, Ukrainian authorities could choose to set as a guiding green finance principal, the United Nations SDG (7) aiming to “*ensure access to affordable, reliable, sustainable and modern energy for all*”. Such goal could be combined with SDG (9) “*Build resilient infrastructure, promote inclusive and sustainable industrialization, and foster innovation*” and SDG (13) “*Take urgent action to combat climate change and its impacts by regulating*

emissions and promoting developments in renewable energy". Thus, providing a set of principles that are aligned with the SDGs and Paris Agreement commitment will provide Ukraine with an initial framework or a starting point for shaping the future green finance regulatory and financial framework.

280. Accordingly, Ukrainian authorities could also encourage the implementation of environmental and environmental-damage mitigation or adaptation projects and initiatives, for example feed-in tariffs for renewable energies. The key action for Ukrainian authorities will be to focus on innovation, which is the most important tool to be developed to be able to usefully tackle high pollution and improvement of the quality of the air. Technological innovation is a crucial component of global energy pattern and low-carbon economic development. Innovation contributes to reducing energy consumption, optimising energy structure and helps to reduce emissions by improving energy efficiency. Technological innovation can raise the efficiency of traditional fossil energy, achieve the target of energy conservation and emission reduction by decarbonization in the production process. It also can improve green total factor productivity, hoist technological capability of renewable energy, and accelerate development of clean energy industry. Thus, investments in Research and Development as an effective strategy to reduce carbon emissions due to improve innovation capability and promote sustainable development. The pollution of the air and the necessity to rebuild Ukraine will lead Ukrainian authorities to structure new approaches to economic, social and governance recovery from the war, but it will also help them to rethink how to better structure their economic development after the end of the war.

281. The pollution problem could be mitigated by the implementation of particular domestic policy supported by structural funds to develop the best possible scenario elaborating on reliable structure of renewable energy system that will help Ukraine to decrease its dependency of fossil fuels and to increase its shares in energy resources that have been generated from sources having less carbon-print impact on the environment.

282. Finally, Ukrainian authorities may provide regulatory framework for the implementation of components of the financial system that deal specifically with green investments, such as the green climate fund or financial instruments for green investments, such as green bonds and structured green funds, including their specific legal, economic and institutional framework conditions specifically dedicated to renewable energy development.

B. To implement a clear and consistent taxonomy legislation embedding realistic future pathways to reach sustainability goals (Ukrainian Green Taxonomy)

283. The future Ukrainian Green Taxonomy could possibly be in a form of a classification system for identifying activities or investments that will shift the country's economy toward meeting specific goals such as SDGs as settled initially within the country's Action Plan and will be related to priority environmental objectives. The identified environmental goal would be the result the country wishes to achieve over a defined timeline a net reduction in carbon dioxide emissions or develop clean energy sources in a given year. The key question will be how an activity or a dedicated investment contributes to achieving domestic environmental objectives and meeting associated goals.

284. Thus, green finance and sustainable growth are often seen as the answer of the Covid pandemic situation, which provided a new turn in countries' economies around the world. The pandemic situation showed the weaknesses of our economic models, health and social systems, but also revealed the human activity impact on the environment. The Covid crisis was one of the worst episodes of the last decades, but it is also a challenge pushing our policy-makers and stakeholders to accelerate the shift from fossil-fuel dependant economies to sustainable economies. The Covid crisis has also shown that global problems require a global economy effort to solve. Climate change, inequality, biodiversity, and the many other issues identified in the SDGs are global problems. The pandemic situation has underscored the complexity and interconnectedness of our world in terms of trade, commerce, as well as relationships between people and societies, and how quickly these connections can collapse if not sustainable. This situation could also be seen as an opportunity to refocus on sustainability and responsible investment. There is early evidence suggesting that sustainable investment strategies continue to outperform the broader market in this crisis. Investors should incorporate Covid matters in their stewardship activities, support their portfolio companies in navigating the effects of this crisis and continue to focus on creating long-term value for their beneficiaries.

285. Ukraine has already received more than 4 billion Euros from the EU Commission under the macro-financial assistance (MFA), which was established to support the Covid recovery of Eastern neighbourhood countries and to show the European Union's solidarity with these countries. Ukraine already showed that it is compliant with the EU Commission requirements to receive such "ad-hoc" funding, in particular, because Ukraine has implemented all eight policy commitments relating to public finance management, governance and rule of law, improving the business climate, and sectoral reforms and state-owned enterprises.

286. Therefore, the future Ukrainian environmental and green finance policies would need to elaborate on different sectors, industry activities and business operations to establish a clear and consistent regulatory frameworks and classification systems that will allow corporations, businesses, investors public and private organisations to rely on while directing their capital flows to sustainable investments. The future Ukrainian green taxonomy would aim to help financial actors and others determine which investments can be labelled “*green*” or “*sustainable*” under domestic jurisdiction and which could be advertised of being “*green*” or “*sustainable*” to end-investors. This support for making informed decisions on environmentally friendly investments can encourage the undertaking of projects and activities that help scale up environmentally sustainable economic development and contribute to country’s environmental goals. The EU Taxonomy could be used as example but the Ukrainian authorities could further enhance and adjust the future Ukrainian green taxonomy to the proper specificities of the country, thus providing more consideration to the level of economic development and specific domestic capital markets print. The future Ukrainian green taxonomy should also include provisions on harmful activities and most probably identify green finance concepts such as “*Do No Significant Harm*” principal. It should also provide provisions on technical screening criteria and clear label and benchmark methodologies for sustainable investments.

287. Finally, there will be a need to define frameworks and drive adoption through voluntary measures. of a specific set of ESG indicators are examples of industry-led efforts that are receiving endorsement from a growing number of domestic companies. The advantage of such voluntary efforts is to reflect the convictions of what is material to some industry leaders in domestic economies.

C. To implement a clear and consistent regulatory framework providing transparency and disclosures obligations at the company and investors’ level (Disclosure of non-financial information)

288. There is a crucial point around the efforts to harness the influence of institutional investors and private asset managers as asset allocators and stewards. Their role of asset allocators has to drive improvements in climate-related disclosures. The advantage of these efforts is they work through existing market mechanisms, and over time have the potential to influence the cost of capital of companies that fail to provide quality climate-related disclosures. The establishment of appropriate mechanisms of disclosure of non-financial information enables a nuanced and constructive approach that is tailored to a sector or individual company at country’s level. This increases the chances the data is relevant enough to be useful in informing financing decisions.

Company shareholders, emboldened by recent successful resolutions to compel more transparent climate disclosures, are also increasingly requiring for more information. It is not yet clear whether market-based data disclosure mechanisms alone will be sufficient to drive increases in consistent, comparable non-financial information disclosure rates at the pace needed by financial institutions, but efforts should be done to improve the capital market lack of consistent environmental investment-related information. Thus, a key challenge will be to maintain existing standards of materiality for financial reporting standards, with climate reporting that is material over a longer time frame.

289. Accordingly, Ukrainian authorities should consider that fact of the double-faced materiality of a capital market such as the EU authorities did while implementing the Non-Financial Reporting Directive (NFRD) purporting to financial materiality when considering the development of corporate reporting standards and the impacts of corporate activity on environmental, climate, social issues. It is also reflected in the recent Sustainable Finance Disclosure Regulation (SFDR), which primarily covers the entity and product-level disclosures introduced for asset managers and financial market participants.

290. Therefore, climate disclosure mechanisms should balance the objectives of consistency and flexibility to reflect that materiality is corporate-specific and should reflect decision-relevant information for financing decisions. Ukrainian authorities should consider the prescriptive to pass legislation requiring corporates, financial institutions, or both to provide climate-related disclosures about their investment activities on domestic markets.

291. Ukrainian authorities, acting as a domestic regulator and supervisor should also pay attention to establish appropriate disclosure requirements to reflect the fact that financial institutions, asset managers and security issuers often operate across multiple countries, economic sectors and capital markets and they will need to have disclosure requirements that could be easily harmonized with international frameworks for ESG disclosures and insure better transparency across different countries' capital markets and economic sectors. Ultimately, internationally consistent material disclosures may be needed, taking into consideration of best practices emerging from existing standards and global frameworks to deliver comparable, comprehensive, decision-relevant climate data that is beneficial for the development of a global sustainable investment market.

D. To ensure that an appropriate national legislation is implemented with regard to financial products relating to sustainable capital markets such as green bonds (Green Bonds Standard)

292. Several financial market actors have identified green bonds as a key instrument of climate finance. The bond market, which includes longer-term debt instruments delivered by governments, regions, municipalities and enterprises, is mainly used to change illiquid assets into tradeable assets, backed by securities. Since the issuance of the first green bond by the European Investment Bank (EIB) the green bonds market has continued to grow and during the last ten (10) years it was considered as a booming sector of capital markets. On the one hand, green bonds have several benefits for green projects and investors, because they represent an additional source of financing for green investments and provide long-term financing for green projects and investors. On the other hand, green bonds are associated with some difficulties. Labelling a bond “*green*” incurs costs related to administrative certification, verification and monitoring, which gives rise to “*greenwashing*”.

293. To avoid greenwashing, corporations, businesses and investors need more information than green labels provide; thus, Ukrainian authorities should provide the necessary regulatory framework to give more security and certainty to corporations and investors while investing in long-term investments such as green bonds. Ukrainian Green bonds standards should be elaborated taking into consideration the impact of climate risk on financial resources such as capital, funding, and liquidity of financial instruments. Ukrainian authorities could use EU Green Bonds standards and ICMA, GBPs as starting point for developing domestic legislation relating to green bonds issuance and listing on domestic and international capital markets. Overall, the future Ukrainian green bonds issuance should provide transparent green credentials alongside an investment opportunity to end-investors. They should provide for a clear process and disclosure for issuers, which investors, banks, underwriters, arrangers, placement agents and others may use to understand the characteristics of any given green bond. This will require domestic regulatory provisions ensuring transparency, accuracy and integrity of the information that will be disclosed and reported by issuers to stakeholders.

E. To associate all actors of the financial sector to the implementation of green finance

294. There are a number of crucial financial intermediaries and institutions driving the greening of the financial system, including banks, institutional investors, as well as, private investors. In

addition, regulatory authorities and central banks can have an important impact on the speed at which the greening of the financial system takes place, as the legal and supervisory mechanism in place determines the framework for such financial system.

295. Banks play an important role in domestic and international financial systems, because they represent an important share of global financial assets. In particular, emerging markets and developing countries have established numerous measures to mobilise finance for sustainable development and to mainstream green finance in the banking system. These measures include priority-lending requirements and below-market-rate finance via interest-rate subsidies. However, these measures carry risks because they could also bring about misallocation of financial resources. In addition, these measures could cause fiscal problems. Therefore, when designing such measures, potential investment-related risks have to be taken into account.

296. It is widely acknowledged that a large share of the trillions of USDs needed to finance green investments have to come from institutional investors, including pension funds, sovereign wealth funds and insurances. However, this investor group is constrained by a number of hurdles: green investments are generally not included in the relevant benchmarks of rating agencies as they do not have a sufficient track record to be given a rating. In addition, green investments are usually not possible at scale because of an insufficient number of appropriate green projects. Therefore, mobilising private capital for green investments is crucial to make the shift from traditional and fossil-fuel based economy to a more sustainable one.

297. Sustainable investing becomes more and more popular and ESG ratings are more and more embedded into corporations' investment portfolios and operational processes and activities. Clearly, this presents a risk for the banking sector, because on one hand banks have tricky role in providing financing, as capital flows can shape corporate behaviour and on the other hand, banks also have a responsibility to help corporate clients' transition. Currently, the most popular sustainable financial products are related to sustainable bonds and loans, however this sector is going to evolve and new sustainable financial products should be offered to corporations and investors in the coming years. National banks of all countries should consider the growing sustainable investing sector providing better shaped sustainable financial products that are focused on specific ESG targets ensuring alignment of sustainability approach across the banking sector.

298. Many infrastructures projects, including in Ukraine and especially in the future after-war reconstruction period, will involve financing through bank loans and facilities. Such financing should be qualified as green financing and will require a variety of guarantees of performance, including green bonds, bid bonds, advance payment guarantees and, in some cases, financial

guarantees. Increasingly, such financial products are usually unfunded in nature and are earmarked as green instruments. This is a good approach, albeit unfunded, but such instruments also consume the capital of the bank and by setting aside capital for green projects the bank is making a contribution to sustainable projects.

299. A proper example could be given with the UK Green Investment Bank, the first investment bank in the world dedicated to promoting a green economy by addressing financing issues. Between 2012 and 2015, with a government investment of 3 billion GBP, the UK Green Investment Bank (GIB) has played a pivotal role in addressing market failures that impede green infrastructure projects and further stimulated private investment. In 2015, the GIB identified five priority areas such as offshore wind power, commercial and industrial wastes, conversion of waste into energy, and a green program. Thus, at least eighty percent of investments approved by the GIB have been allocated for these priority areas, while the remaining twenty percent can be used for other green industries such as maritime energy and carbon capture and storage. Hence having this flexible approach in financing through bank facilities enables banks and corporations to work together to develop alternative strategies to create tangible incentives for the reduction of the carbon footprint.

300. Consequently, Ukrainian authorities should associate all financial actors to the future regulatory process of establishment of Ukrainian green finance framework for sustainable investments. Banks, institutional and private investors together with asset managers, end-investors, stakeholders and financial intermediaries should work together to shape the future regulatory and financial framework of domestic green finance.

VII.PART VI: CONCLUSION

301. The establishment of a sustainable economy is the cornerstone of many governments' action plan supporting sustainable growth through a transition process to a more climate-resilient economy. As a tool designed to help the financial sector of each country, it will direct capital flows towards environmentally sustainable activities and investments in view of achieving the long-term climate neutrality objectives of each country committed to act according to the Paris agreement.

302. It is also a mandatory transparency exercise for countries, local authorities, financial regulators, corporations, investors, policy-makers and individuals, because it has to ensure a proper implementation of a clear classification system, prevent from greenwashing and reduce the risks that incur such type of investing.

303. The final goal is not only to reduce the harmful emissions by greening the economic growth, but it also represents a pathway for economic and social development that can be sustainable in the time. By way of consequences, it could also create green economies around the world guided by the green growth and prosperity across society in a world threatened by global environmental risks and resource constraints. Governments in all regions face the challenge of fostering a transition to green economies that enables durable economic growth and social development, while avoiding risks to public goods, natural resources, and social equality, thus seeking to achieve internationally recognised SDGs.

304. Sustainability performance targets are typically set in accordance with a number of considerations. These include alignment with the Paris Agreement, market and stakeholder expectations, the company's starting point, track record of achievement to date and the feasibility of improvement measures, including economic constraints/cost-benefit analyses, and the existence of proven techniques or technologies which deliver the anticipated improvements. With regards to climate change, authoritative scientific analysis has determined the rate of decarbonisation required in the global economy in order to align the various economic activities with those scenarios which imply a Paris Agreement aligned level of warming. Science-based targets are targets that are in line with the scale of reductions required to keep the global temperature increase below 2°C above pre-industrial temperatures. As part of a credible transition proposition, issuers should reference appropriate benchmark, sector-specific decarbonisation trajectories in communicating their strategy in this area. It is likely that an aim to align the business plans with a 1.5°C trajectory will be perceived as most credible to the increasing proportion of market participants.

305. Therefore, issuers of climate strategy and ESG guidelines, frameworks and assessments should reference science-based targets and transition pathways. The planned transition to a more sustainable economy based on sustainable investments and dedicated sustainable activities should (i) be quantitatively measurable (based on a measurement methodology which is consistent over time, such as coherent and evidence-based reporting standards for disclosure of sustainability information); (ii) be aligned with, benchmarked or otherwise referenced to recognised, science-based economic evolution trajectories where such trajectories exist; (iii) be publicly disclosed in mainstream financing filings, including forecasts and interim milestones, and

(iv) be supported by independent assurance or verification of the information thus provided. Only reliable, precise and detailed non-financial information about sustainable investments could provide the necessary transparency on capital markets, thus attracting investors and companies able to engage financial capital into sustainable activities.

306. The increasingly rising demand for sustainable investment opportunities itself can be interpreted as a promising sign to help close the financing gap. However, current levels of green/sustainable investments are far from what is necessary to allow for the required transition towards a sustainable economy. This in turn leads to amplified risks for the financial sector in the future, when climate change impacts and other ESG-related risks materialise at an increasingly severe scale, delayed policy actions are abruptly taken, and social unrest may unfold. It is thus crucial to take immediate action by engaging a transition process of countries' economies to be able to comply with Paris Agreement goals and carbon dioxide emissions reduction by 2050.

307. Prevailing challenges in the attempt to increase the amount of sustainable economies include (i) a clear and universal understanding of which economic activities contribute towards a green/sustainable environment and therefore qualify as sustainable finance, (ii) development of a comprehensive set of stringent and coherent policies and regulations that create a suitable and level playing field for the required transition, (iii) a general lack of investable sustainable projects and (iv) relevant non-financial (ESG factor based) data, forecast and modelling methods that need to be further developed.

308. Policymakers and market participants are starting to embrace green taxonomies as a powerful tool to mobilise green capital for the transition to an environmentally sustainable economy. Many jurisdictions around the world already have green taxonomies in place or are in the process of actively drafting them. Meanwhile, to prevent market fragmentation and avoid barriers to cross-border flows of green capital, further alignments of existing national green taxonomies are needed. While approaches in green taxonomy development tend to differ from country to country, the existing efforts are generally following a common set of principles such as science-based classification approach, incorporating core principals such as "*do no significant harm*" developed in the EU taxonomy, and an emphasis on the regional characteristics and utilisation of existing labels and regulations. Financial regulators realise that a successful green taxonomy needs to strike a careful balance between compatibility with international practices, regional circumstances and national environmental priorities. Green taxonomy rules also need to be dynamic and flexible to integrate future changes in capital markets and technology development. Therefore, developing green taxonomies has to be reasonably practicable to encourage maximum integration. Investors and companies could use green taxonomies to inform

about their activities and investments, address associated risks and disclosure climate related information.

309. However, implementation challenges still remain including adaptation of green taxonomies to the climate goals of various jurisdictions and existing Environmental, Social and Governance (ESG) and other sustainability ratings. There are also variations in the data quality, transparency, comparability, and availability. Therefore, to improve usability, feedback from investors and companies on their experiences of using green taxonomies must be acknowledged and to the extent necessary included in further developments. National green taxonomies should be designed to evolve continuously and to capture emerging scientific consensus and technological advancements. National green taxonomies will be the promoters and the vehicles of the sustainable transition especially with regard to high-emitting economic sectors to be able to achieve the Paris Agreement goals. Decarbonising all national economic sectors has to be the priority of each country that has agreed to act according to the Paris Agreement. Green taxonomies under development are more and more considering the concepts of transition activities which receive growing support for taxonomy expansion to advance other social and environmental objectives such as biodiversity on land and in oceans protection and climate resilience.

310. Sustainable investments as defined by the climate transition of countries worldwide engaged into the process of greening their economies should be the target investments of each and every responsible investor. In a world where, we face the Covid pandemic situation and its consequences, the scarcity of raw materials, the war in Ukraine and the current economic crisis, we realise that even the most rich countries around the world cannot only focus on financial profits, while developing their economies. Investment strategies need to adapt to the transition from financial profits-based to a circular economy and finance innovative solutions to solve sustainability challenges.