

# The Sustainable Finance Law Review



First Edition

Editor: Anna-Marie Slot, Global ESG Partner of Ashurst LLP

THE SUSTAINABLE  
FINANCE LAW  
REVIEW

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# PREFACE

Sustainable finance is a relative youngster in the world of finance, but it is growing up fast. Public and private financing of sustainable/green projects, or those with provisions in line with borrowers' and issuers' environmental, social and governance (ESG) commitments, has exploded.

Since the signing of the Paris Agreement in 2015, more than 100 countries have committed to net zero emissions targets. Countries have also acted at a national level with ambitious target-setting and nationally determined contributions (NDC) pursuant to the Paris Agreement. They are not alone. By mid-2022, more than one-third of the world's largest publicly traded companies had net zero targets. Financial institutions have also engaged with various policies introduced to enshrine ESG commitments, in terms of both their own lending targets and the carbon emissions linked to those targets. Investors at both retail and institutional levels increasingly look to the financial markets as an important lever in achieving such targets.

For over three decades the United Nations has brought together almost every country on earth for the global climate summits – known as the Conference of the Parties (COP). At COP26 in 2021, private finance showed up in force to play its role in the transformation of the business ecosystem as we know it. Precisely what that role entails is a live debate and the discussions regarding the purpose of sustainable finance cover a wide spectrum of issues – from greenwashing, to the fundamental shift of credit including the risks and opportunities of ESG considerations. We saw that debate play out in real time during COP27.

Notwithstanding ongoing considerations about the purpose of sustainable finance, financial market participants have reacted by creating a wide variety of financial products marketed as sustainable, green or ESG-friendly. The rapid increase in both supply of and demand for sustainable investment products has, at times, resulted in a lack of consistency, transparency and reliability of disclosures and metrics. Governments and regulatory bodies are increasingly focused on imposing guidelines and frameworks to address these issues.

Although sustainable finance continues to elude strict definition at present, significant efforts are being made globally to ensure quality and transparency in the industry, to impose consistent frameworks such as the International Sustainability Standards Board (ISSB) and disclosure requirements such as those of the Task Force on Climate-related Financial Disclosures (TCFD) that support comparability and interoperability among firms and products, and to provide investors with sufficient information to monitor the impact of their investments.

In this inaugural edition we aim to:

- a* provide a snapshot of the current state of sustainable finance and the status of regulatory efforts across multiple jurisdictions; and
- b* track the evolution of sustainable finance and outline key trends for the near future.

I thank all of the contributors for their expertise, hard work and dedication in producing this volume.

**Anna-Marie Slot**

Ashurst LLP

London

December 2022



# UNITED KINGDOM

*Anna-Marie Slot and Eileen Kelly*<sup>1</sup>

## I INTRODUCTION

The United Kingdom (UK) has been an early leader in its commitment to transitioning to a low-carbon economy. In 2019, the UK became the first major economy to commit in law to net zero greenhouse gas emissions by 2050. The government took this commitment further in 2021, setting into law the world's most ambitious climate change target of cutting emissions by 78 per cent compared with 1990 levels by 2035.<sup>2</sup> Achieving these targets will require a transformation of the entire economy, with a significant shift in investment towards sustainable projects and green technology. Demand for such investment is high, with 70 per cent of the UK public wanting their money to go towards making a positive difference to people's lives or the planet.<sup>3</sup>

Although the UK financial markets are beginning to respond to the demand for sustainable investment, raising more than £100 billion in green finance from 2017 to 2021 across bond, equity and loan markets, the levels of investment fell well short of what is required to meet the UK's net zero commitment by 2050.<sup>4</sup> According to the UK Climate Change Committee, approximately £190 billion of green investment annually will be required to meet the UK's net zero goal, or an increase of approximately 450 per cent on green investment levels seen in 2021.<sup>5</sup>

The government has implemented a number of initiatives to highlight the importance of the financial markets supporting the transition to a low-carbon economy and to encourage increased investment towards net zero. In 2019, it published the Green Finance Strategy, which sets out two key lines of effort aimed at aligning UK financial flows with a low-carbon world: 'greening finance', or supporting the financial services sector to align with the UK's net-zero commitment and wider environmental goals; and 'financing green', or mobilising private finance at scale to support clean and resilient growth. The government is now seeking to build on these foundations with a three-phase approach to delivering on the green finance strategy, with an initial focus on addressing the information gap for market participants and ensuring that investors are provided with consistent, meaningful and comparative data

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1 Anna-Marie Slot is a partner and Eileen Kelly is a senior associate at Ashurst LLP.

2 HM government, 'Greening Finance: A Roadmap to Sustainable Investing', October 2021, p. 6.

3 HM government, 'Investing in a Better World: Understanding the UK public's demand for opportunities to invest in the Sustainable Development Goals', p. 7.

4 Christopher Breen, 'A Reality Check on Green Finance in the UK: Analysis of the Size, Growth & Penetration of Green Finance in Capital Markets in the UK', July 2022, p. 5.

5 id.

regarding environmental sustainability. Implementing sustainability disclosure requirements (SDRs) across the economy and developing a UK Green Taxonomy to ensure consistency across sustainability reporting will be central to these efforts.

## II YEAR IN REVIEW

2021 has been the most active year on record for sustainable finance across a number of indicators, with the market responding to the growing climate emergency. The value of green finance raised in the UK financial markets has increased significantly over the past five years to £44 billion in 2021, which represents an increase of more than 500 per cent since 2017.<sup>6</sup> Approximately half of green finance activity comprises issuances of labelled green bonds (that is, bonds with a green use of proceeds, also referred to as use of proceeds bonds). Despite the significant increase in activity, green finance still represents only a small proportion of financial markets activity in the UK, estimated to be just 9 per cent of financial markets activity across bond, equity and loan markets in 2021.<sup>7</sup>

Debt markets, primarily green bonds, account for the vast majority of the market in green finance in the UK. Debt markets accounted for approximately 98 per cent of all green finance in the UK in 2021, comprising roughly 75 per cent green bonds and 25 per cent green loans. In 2021, issuances of labelled green bonds raised approximately £32 billion in the UK, representing a nearly 700 per cent increase on the previous year. A significant portion (more than two-thirds) of the increase is accounted for by the government's debut £19 billion green gilt issuance. Over the past five years, the penetration of green finance has been highest in the bond market, where it represents 12 per cent of all bond issuances in the UK, compared with 7 per cent in the loan market and only 2 per cent in the equity market.<sup>8</sup>

The UK lags behind the European Union (EU) in green finance. Despite representing over 20 per cent of all financial markets activity in Europe over the past five years, UK issuers account for only 14 per cent of all green finance in European financial markets over the same period. Green finance accounted for approximately 5 per cent of all financial markets activity in the UK over the past five years, roughly half of the amount in the EU.<sup>9</sup>

The levels of investment in sustainable finance in 2021 fell well short of the amount required for the government, corporates and financial institutions to meet their net zero targets. The estimated annual investment required to support the UK's net zero commitment is approximately £190 billion, almost twice the amount that has been raised over the past five years.<sup>10</sup> Key elements in scaling up the rate of investment in green finance will include more transparency and clarity about definitions of green finance, use of proceeds and companies' adoption of transition plans, each of which forms part of the initial phase of the government's Greening Finance Strategy.

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6 Breen, p. 3. This figure excludes other categories of ESG financial products such as sustainability, sustainability-linked or social loans and bonds.

7 id.

8 Breen, p. 7.

9 Breen, p. 3.

10 Breen, p. 5.

### III REGULATION AND POLICY

Although the UK is committed in law to achieving net zero by 2050, current frameworks in relation to sustainable finance and ESG reporting are primarily voluntary. The government's Green Finance Strategy, published in 2019, seeks to build a regulatory framework and establish mandatory guidelines for green labelling, sustainability reporting and taxonomies in order to provide investors with more clarity regarding green finance. The Green Finance Strategy will be delivered in three phases:

- a phase 1: focused on addressing the information gap for investors and consumers;
- b phase 2: focused on creating requirements for sustainability information to be incorporated into business and financial decisions; and
- c phase 3: focused on aligning financial flows across the economy with the UK's net zero commitment.

The government is currently focusing on delivering phase 1, with a number of initiatives having been proposed or implemented to address the availability, quality and consistency of information about sustainability for investors. These initiatives include, among others, implementing SDRs across the economy incrementally, and delivering a UK Green Taxonomy that is fit for purpose and useful as a marketing tool.

### IV SUSTAINABLE FINANCE INSTRUMENTS

The term sustainable finance is generally used to refer to a range of financial products connected to ESG-related aims, which include green, social, sustainable and sustainability-linked financial products, as set out below.

#### Types of sustainable finance instruments

<b>Green</b>	Financial instruments whose proceeds are used exclusively to finance or refinance green projects or projects with clear environmental benefits. Also referred to as 'labelled green' products or 'use of proceeds' products.
<b>Social</b>	Financial instruments whose proceeds are used exclusively to finance or refinance eligible social projects, as defined by the relevant international standards.
<b>Sustainable</b>	Financial instruments whose proceeds are used exclusively to finance or refinance any combination of eligible green and social projects, as defined by the relevant international standards.
<b>Sustainability-linked</b>	Forward-looking performance-based financial instruments in which the issuer commits to future improvements in sustainability outcomes within a predefined timeline, in accordance with relevant international standards. These instruments typically include a financial penalty, such as an interest rate step-up, if the issuer fails to meet the sustainability target within the predefined timeline.

Green finance remains the largest area of sustainable finance globally, with green bonds constituting approximately 41 per cent of all sustainability-related bond issuances in 2020, followed by social bonds at 30 per cent and sustainability bonds at 24 per cent. The value of green finance in the UK financial markets rose significantly from 2017 levels to a total value of £44 billion in 2021. A large portion of that activity, approximately £31 billion, comprised labelled green bond issuances, in large part driven by the £19 billion green gilt issuance by the government in 2021. Although the green gilt issuance pushed up the proportion of green finance issued by government entities in 2021, over the past five years corporate issuers have accounted for the majority of green finance, representing an average of 61 per cent of all issuances and reaching a peak of 90 per cent in 2019. Although the share of the market being driven by government and financial sector issuers is increasing, corporate

activity remains the most constant driver of growth in the UK's green finance market.<sup>11</sup> During the same period, £40 billion of sustainability-linked loans were issued in the UK, of which approximately £6 billion could also be considered green finance based on the use of proceeds.<sup>12</sup> The sustainable finance market is continually evolving as new products are developed, including products such as green derivatives and green trade finance.

Green bonds remain the primary instrument for raising green finance in the UK, accounting for nearly £49 billion in issuances over the past five years. Green bond issuances increased by nearly 700 per cent in the UK in 2021, accounting for almost the entirety of the increase in green finance in the UK overall and again driven primarily by the government's green gilt issuance. In January 2021, the London Stock Exchange's Sustainable Bond Market (a sustainable finance platform launched in 2019 and designed to enhance disclosure and increase visibility and access for investors in green, social and sustainability-linked bonds) was home to over 250 bonds.<sup>13</sup> The green loan market raised approximately £11 billion in 2021, a decrease of almost 10 per cent compared with 2020. Prior to 2021, green loan issuance had been the primary capital raising method in the green finance market, yet in 2021 green loans' share of the market fell from nearly three-quarters to only one-quarter. Green equity issuances, which remain a very small proportion of the market, represented approximately £1 billion in issuances in 2021.<sup>14</sup>

Green finance is not solely composed of financing with an explicitly green use of proceeds but also includes any financing raised by companies whose primary activity is addressing climate change or supporting the transition to clean energy and net zero, such as renewable energy firms. Over the past five years, these companies are estimated to have raised an additional £35 billion (adjusted so as not to double-count issuances of labelled green bonds or loans with green use of proceeds), representing approximately 33 per cent of all green finance. Trailing behind these financings are loans with green use of proceeds, which represent approximately 21 per cent of the green financing market over the past five years, or approximately £22 billion. Green venture capital, or investment in smaller companies that are focused on developing clean energy or other activities to address climate change, is the smallest component of the green finance market, representing approximately 1 per cent of green finance over the past five years.<sup>15</sup>

Despite the strong and increasing activity in the green finance market in the UK, green finance still represents a relatively small share of all UK financial markets activity. Green capital raising rose to 9 per cent of all financial markets activity in the UK in 2021, more than doubling the penetration of 4 per cent in 2020. Penetration remains highest in the bond market, where labelled green bonds make up approximately 9 per cent of all corporate bond issuances. Green loans make up approximately 7 per cent of the overall loan market, and green financing in the equity and venture capital markets accounts for only 2 per cent and 1 per cent, respectively.<sup>16</sup> Although penetration of green financing in the overall financial markets

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11 Breen, p. 12.

12 Breen, p. 14.

13 London Stock Exchange Sustainable Bond Market Factsheet, 19 February 2021. The Sustainable Bond Market is not a distinct primary market but a label applied across various segments of the London Stock Exchange's existing primary markets in order to promote visibility of sustainable debt finance instruments.

14 Breen, p. 7.

15 Breen, p. 8.

16 Breen, p. 9.

is increasing, it remains low, signifying that much remains to be done to match companies' stated ambitions to support the transition to a low-carbon economy and to enable the UK to achieve its net zero commitment.

Another way to look at the penetration of green finance in the UK financial markets is to analyse the proportion of capital raised by 'good' and 'bad' companies. In the report 'A Reality Check on Green Finance in the UK: Analysis of the Size, Growth & Penetration of Green Finance in Capital Markets in the UK', Christopher Breen of New Financial LLP demonstrates that the £36 billion raised by good companies (defined as companies whose primary activity is to help address climate change and accelerate the transition to clean energy and net zero) in the UK financial markets over the past five years is dwarfed by the £302 billion raised by bad companies (defined as companies whose main activity plays a significant role in causing the problems of climate change or delaying the transition to clean energy and net zero (including companies in the oil and gas and mining sectors, companies in the Climate Action 100+ list of the largest polluters in the world and companies whose business description includes references to bad activities from a climate perspective)).<sup>17</sup> For much of the past five years, every pound raised by a good company was offset by nearly 10 pounds raised by a bad company, although this ratio decreased to 6:1 in 2021. Overall, green finance represents only 4 per cent of the overall funding of bad companies over the past five years. When considering the types of finance raised by good and bad companies, the differences remain stark: good companies account for over half (55 per cent) of all green financing by UK corporates over the past five years, with bad companies driving only 17 per cent of green financing over the same period. Green finance accounted for only 5 per cent of all financial markets activity by bad companies in 2021.<sup>18</sup> These figures illustrate that significant progress must be made to encourage the most carbon-intensive businesses to reduce their impact on the climate.

## V SUSTAINABLE DISCLOSURE REQUIREMENTS AND TAXONOMY

### i SDRs

Various government and regulatory bodies have already taken steps towards formalising disclosure requirements and guidelines regarding green finance. In November 2020, the Chancellor of the Exchequer announced that the UK intends to make disclosures aligned with the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD) mandatory across the UK economy by 2025. In December 2021, the Financial Conduct Authority (FCA) finalised its TCFD-aligned disclosure rules for UK premium-listed companies, and in June 2021 began consulting on proposals to extend those disclosure rules to standard-listed issuers and to require UK-authorized asset managers, life insurers and pension providers to publish client-focused TCFD-aligned disclosures. In his Mansion House speech in July 2021, the Chancellor of the Exchequer announced new SDRs that will build on the UK's TCFD implementation and will cover three types of disclosure:

- a Corporate disclosure: new requirements will be put in place for companies, including those in the financial sector, to make sustainability disclosures. Subject to consultation, these requirements will comprise reporting under proposed international standards

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<sup>17</sup> Breen, p. 10.

<sup>18</sup> Breen, p. 11.

currently being developed by the International Sustainability Standards Board (ISSB) and reporting of environmental impact using the UK Green Taxonomy (discussed in more detail below).

- b* Asset manager and asset owner disclosure: SDRs will also apply to asset managers and asset owners that manage or administer assets on behalf of clients and consumers, including occupational pension schemes, and will require them to disclose how they take sustainability into account. This disclosure will assist consumers in determining whether their assets are managed in accordance with their sustainability preferences.
- c* Investment product disclosure: SDRs will require the creators of investment products to report on the products' sustainability impact and relevant financial risks and opportunities. This information will form the basis of a new sustainability labelling regime that seeks to simplify classification of investment products for consumers.<sup>19</sup>

The ISSB is currently consulting on a draft climate-related international disclosure standard, which will eventually expand to include broader environmental and sustainability factors. The government expects that the ISSB standards will form a core component of the SDR framework and, to this end, intends to create a mechanism to adopt and endorse ISSB-issued standards for use in the UK. The current expectation is that the standards issued by the ISSB, and therefore integrated into the SDRs, will build on the four pillars of climate-related financial disclosure as developed by the TCFD: governance, strategy, risk management, and metrics and targets. The SDRs will also go further in requiring disclosure against the UK's Green Taxonomy. In particular, asset managers and owners and developers of investment products will be required to substantiate their ESG claims in a way that is accessible to clients and consumers and that allows them to compare one product with another. They will also be required to disclose whether and how they take ESG-related matters into account in their governance arrangements, investment policies and strategies. Additionally, the SDRs will require disclosure against minimum safeguards relating to good business practice.

TCFD-aligned disclosures are required for financial years beginning on or after 1 January 2021 for premium-listed issuers, on or after 1 January 2022 for standard-listed issuers and larger firms (i.e., those with more than £50 billion in assets under management for asset managers, or £25 billion in assets under administration for asset owners) and on or after 1 January 2023 for firms with assets that are under management or administration and that are greater than £5 billion. The UK has committed to make disclosures aligned with TCFD disclosures mandatory across the economy by 2025, with most requirements in place by 2023. In the lead up to mandatory reporting, the government recommends that organisations seeking to report on forward-looking financial risks and opportunities arising from climate change should consider reporting in line with the TCFD recommendations on a voluntary basis. The FCA has a huge focus on transparency and has placed TCFD recommendations at the heart of its work on climate-related disclosures.

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19 Greening Finance, p. 11.

The framework of the UK SDRs

	Corporates	Asset managers/owners	Investment products
<b>Governance</b>	Governance in relation to sustainability-related risks, opportunities and impacts	Governance in relation to sustainability-related risks, opportunities and impacts, and the implications for investment policies, strategies and outcomes	Governance in relation to sustainability-related risks, opportunities and impacts, and the implications for investment products
<b>Strategy</b>	Actual and potential implications of sustainability-related risks, opportunities and impacts for the organisation's businesses, strategy and financial planning	Actual and potential implications of sustainability-related risks, opportunities and impacts for the organisation's investment policies, strategies and outcomes	Actual and potential implications of sustainability-related risks, opportunities and impacts for investment outcomes
<b>Risk management</b>	Processes used to identify, assess and manage sustainability-related risks, opportunities and impacts	Processes used to identify, assess and manage sustainability-related risks, opportunities and impacts, and the implications for the organisation's investment policies, strategies and outcomes	Processes used to identify, assess and manage sustainability-related risks, opportunities and impacts at product level
<b>Metrics and targets</b>	<p>Metrics and targets used to assess and manage relevant sustainability-related risks, opportunities and impacts</p> <p>Performance against targets</p> <p>Taxonomy alignment and relevant supporting information</p>	<p>Metrics and targets used to assess and manage relevant sustainability-related risks, opportunities and impacts, and implications for the organisation's investment policies, strategies and outcomes</p> <p>Performance against targets (where relevant)</p> <p>Taxonomy alignment and relevant supporting information based on underlying investments</p>	<p>Product-level metrics and performance indicators on sustainability-related risks, opportunities and impacts</p> <p>Performance against targets (where relevant)</p> <p>Product-level Taxonomy alignment and relevant supporting information based on underlying investments</p>

Source: Greening Finance, p. 14.

**ii Transition plans**

SDRs will also include disclosures on any published transition plan outlining the actions and targets in a firm's transition to a low-carbon economy. Initially, certain firms in the UK will be required to either publish transition plans that align with the government's net zero commitment or explain why they have not done so. Although no standard template regarding transition plans has yet been adopted, certain guidelines are emerging, such as those provided by the TCFD and groups such as Climate Action 100+ and the Institutional Investors Group on Climate Change, as well as best practice guidance for financial sector transition strategies being developed by the Glasgow Financial Alliance for Net Zero (GFANZ). As additional standards emerge and coalesce, the government and regulators will look to incorporate these standards into UK regulation and strengthen disclosure requirements as appropriate, with a view to encouraging consistency and comparability and supporting more widespread adoption.

**iii UK Green Taxonomy**

To combat greenwashing and provide more consistent and comparative information to support investor decisions, the government is implementing a UK Green Taxonomy (Taxonomy), which will clearly set out the criteria that specific economic activities must meet to be considered environmentally sustainable and therefore Taxonomy-aligned. Reporting against the Taxonomy will form part of the SDRs. Certain companies will be required to

disclose what proportion of their activities is Taxonomy-aligned, and providers of investment funds and products will have to do the same for the assets they invest in. The goals of the Taxonomy are to:

- a* create clarity and consistency for investors: investors will be able to easily compare the environmental performance and impact of companies and investment funds to inform their financial decisions;
- b* improve understanding of companies' environmental impact: Taxonomy disclosures will facilitate an understanding of a company's contribution to environmental sustainability; and
- c* provide a reference point for companies. The Taxonomy will provide companies with an informative performance target. For example, companies can also, on a voluntary basis, use the Taxonomy to develop and communicate their net zero transition and capital investment plans.

The Taxonomy has six environmental objectives:

- a* climate change mitigation;
- b* climate change adaptation;
- c* sustainable use and protection of water and marine resources;
- d* transition to a circular economy;
- e* pollution prevention and control; and
- f* protection and restoration of biodiversity and ecosystems.

Each of these objectives will be underpinned by a detailed set of standards known as technical screening criteria (TSC). Each economic activity included in the Taxonomy will have an individual TSC that identifies how that activity can make a substantial contribution to the environmental objective. To be considered Taxonomy-aligned, an activity must meet three tests:

- a* it makes a substantial contribution to one of the six environmental objectives;
- b* it does no significant harm to the other objectives; and
- c* it meets a set of minimum safeguards.

Taxonomy alignment will be based on reported data, rather than projections, in order to provide a clear picture of the areas in which a company is currently making a substantial contribution to environmental objectives. The Taxonomy also allows for recognition of companies that, while not currently conducting their business in a way that is aligned with net zero ambitions due to technological constraints, are engaged in transitional activities (such as aligning with best-in-sector emissions levels), or are investing capital expenditure in activities that are Taxonomy-aligned, or both. The Taxonomy will also recognise enabling activities, which support contributions to environmental objectives but are not yet sustainable themselves (such as the manufacture of components for wind turbines).

## **VI ESG DATA AND REPORTING**

Despite movement across the UK regulatory structure to implement a suite of reporting requirements regarding ESG, standards in relation to raising green finance remain primarily voluntary. Labelled green bonds and loans are often aligned with the ICMA Green Bond Principles or the Loan Market Association (LMA) Green Loan Principles, as relevant, which



are voluntary standards built upon four pillars: use of proceeds, process for evaluation and selection of eligible projects, management of proceeds and reporting. Similar standards exist for sustainability-linked social and sustainable loans and bonds. Although issuers of green finance often choose to report against these principles, such reporting is not currently mandatory, and investors generally have no recourse against issuers that do not use proceeds as anticipated, fail to achieve sustainability targets or fail to provide a particular level of ongoing disclosure. Many sustainable finance issuers also rely on second party opinions, which are obtained from third-party ESG ratings organisations to confirm the alignment of the issuer's relevant sustainable financing principles with the ICMA or LMA standards, or to confirm the alignment of the particular issuance with the issuer's sustainable financing principles, or both. Currently, these ESG ratings organisations are not regulated, and there are no standard guidelines on the level of diligence required to deliver such opinions. In its Greening Finance sustainability roadmap, the government indicated that it is considering bringing ESG ratings providers within the scope of FCA authorisation and regulation, a proposal that is supported by the FCA. Further detail is expected by the end of 2022.

## **VII SUSTAINABLE FINANCE INCENTIVES**

The FCA is considering regulatory incentives for sustainable finance instruments or for the financing of activities aligned with the Paris Agreement and the UN Sustainable Development Goals.

A market-led transition will require that listed companies and regulated firms have the right incentives, tools and organisational arrangements in place to set and pursue effective ESG strategies, including transition plans aligned with the government's net zero targets. A number of market-led initiatives have developed in the UK to support companies and financial institutions in their independent efforts towards sustainability and to coordinate these efforts across the economy. For instance, the Green Finance Institute (GFI) was established in 2019 as a public and private sector coalition of global financial industry experts that is focused on designing, developing and launching portfolios of scalable financial solutions that accelerate sector-specific transitions to a low-carbon economy. GFANZ was launched in April 2021 to unite net zero financial sector-specific alliances from around the world in one industry-wide strategic alliance and provides a forum for leading financial institutions to accelerate the transition to a net zero global economy. GFANZ currently has more than 450 member firms from across the global financial sector, representing more than US\$130 trillion in assets under management and advice. GFANZ focuses on three core areas: net zero transition planning for financial institutions, mobilising capital towards emerging markets and developing economies and net zero public policy.

## **VIII GREEN TECHNOLOGY**

Data and artificial intelligence have the potential to provide solutions to ESG concerns, from combating greenwashing to expanding access to a wider range of financial products. To this end, the FCA and the City of London Corporation have collaborated to develop the Digital Sandbox, a platform that provides innovators with access to data in the quantity and quality needed to develop algorithms, and it acts as a crossroads bringing together various elements of the financial services ecosystem. The second phase of the Digital Sandbox ran from November 2021 to March 2022 and focused on tech solutions in the area of ESG data

and disclosures, particularly with regard to transparency of sustainability reporting on supply chains, automating and validating ESG data and improving consumers' understanding of a product's ESG characteristics. The UK's efforts to leverage technology to support the growth of the green finance industry is in line with broader G20 efforts through its Sustainable Finance Study Group to explore opportunities to better leverage digital technologies for financing sustainable development.

## IX CLIMATE CHANGE IMPACT

The expansion of ESG regulatory frameworks together with regulators' increasing focus on policing disclosures is likely to result in an increase in the number of firms being pursued for greenwashing claims. The government's Greening Finance roadmap defines greenwashing as 'when misleading or unsubstantiated claims about environmental performance are made by businesses or investment funds about their products or activities'. Greenwashing can make it very difficult for investors to determine the actual impact of their investments, undermining trust in the green finance market and leading to misallocation of capital intended for sustainable investment. According to Schroders Institutional Investor Study 2021, greenwashing was the most frequently cited concern among respondents, with 59 per cent of investors raising it as the biggest challenge to investing sustainably.<sup>20</sup> In July 2021, the FCA published a 'dear chair' letter addressed to authorised fund managers following a number of applications for authorisation of ESG-focused investment funds that the FCA described as 'poor quality' and '[falling] below our expectations'.<sup>21</sup> The dear chair letter provided a number of guiding principles to support the existing regulatory framework in the FCA Handbook (e.g., that communications are clean, fair and not misleading), including the overarching principle that a 'fund's focus on ESG/sustainability should be reflected consistently in its name, stated objectives, its documented investment policy and strategy, and its holdings'.<sup>22</sup> Following the publication of this letter, in December 2021 the FCA published a policy statement (PS21/24) containing final rules and guidance for a climate-related disclosure regime for FCA-authorised asset managers and owners.<sup>23</sup>

The introduction of SDRs and the UK Green Taxonomy are intended in part to address the perception of greenwashing in the green finance market and to reduce the risk arising from misleading statements, and regulatory bodies across the UK have indicated their intention to enforce these and other guidelines. For instance, in the FCA's policy statement published in December 2021, it noted that: '[s]upervision will act reactively where needed and start carrying out work to assess firms' implementation of the rules once the first disclosures are published in 2023. Enforcement could consider taking action if firms failed to make disclosures or if these were misleading/constituted serious misconduct'.<sup>24</sup> Increased regulatory action in other markets provides an indication of what might be expected in the UK once stricter disclosure regimes come into force. For example, in January 2020 Italian

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20 Schroders Institutional Investor Study 2021, available at <https://www.schroders.com/en/uk/pensions/insights/institutional-investor-study-2021/sustainability/>.

21 <https://www.fca.org.uk/news/news-stories/guiding-principles-on-design-delivery-disclosure-esg-sustainable-investment-funds>.

22 id.

23 <https://www.fca.org.uk/publication/policy/ps21-24.pdf>.

24 id.

energy company ENI was fined €5 million by Italian regulatory authorities for false claims related to its ‘green’ diesel, and in the United States the Securities and Exchange Commission has formed the SEC Climate and ESG Task Force to ‘develop initiatives to proactively identify ESG-related misconduct’ and to ‘identify any material gaps or misstatements in issuers’ disclosure of climate risks under existing rules’.<sup>25</sup>

In the UK, ClientEarth (a Shell plc shareholder) is in the process of bringing a claim in the English courts against Shell’s board for its perceived failure to ‘adopt and implement a climate strategy that truly aligns with the Paris Agreement’.<sup>26</sup> The claim is understood to be proceeding as a derivative action. Firms may also find themselves at risk of securities claims under Sections 90 or 90A of the Financial Services and Markets Act 2000 arising from false or misleading ESG-related statements and disclosures. Such claims may become more likely if regulators begin to levy fines against firms with insufficient or misleading ESG disclosures, or if publicity around such enforcement impacts public companies’ share prices and investors are able to demonstrate that they relied on the statements in question and that such statements caused identifiable losses. Other trends in the UK litigation market, such as the rise in collective (or class) actions and the growing availability of third-party litigation funding, may also contribute to a rise in ESG-related litigation.

## X OUTLOOK AND CONCLUSIONS

The timeline below sets out key milestones in the UK’s sustainable finance legislation and regulation.

Date	Action
2022	Government is to publish information about potentially bringing ESG data and ratings providers within the scope of FCA authorisation and regulation
2022	Prudential Regulation Authority (PRA) will switch its supervisory approach on its climate-related supervisory expectations from one of assessing implementation to actively supervising entities’ ongoing progress against such expectations
2022	PRA and Bank of England will begin undertaking work on enhancements to regulatory capital frameworks to support efforts to address climate change
2022	FCA is to: <ul style="list-style-type: none"> <li><i>a</i> engage with stakeholders on transition plans, focusing on governance and the content and disclosure of transition plans</li> <li><i>b</i> focus on and challenge fund managers’ responses to its dear chair letter and its guiding principles for the design, delivery and disclosure of ESG investment products</li> <li><i>c</i> engage with stakeholders on whether its regulatory regime sets the right expectations and incentives across the ESG spectrum</li> <li><i>d</i> engage with stakeholders on developing its policy approach to ESG governance, remuneration, incentives and training in regulated firms</li> </ul>
2022	Government to consult on climate change mitigation and climate change adaptation criteria under the UK Green Taxonomy
Q3/Q4 2022	FCA intends to consult on introducing ESG disclosures for MiFID investment firms as part of the Investment Firms Prudential Regime
Autumn 2022	FCA intends to publish a feedback statement and consultation paper following its discussion paper on the SDRs and product labels
Q4 2022	PRA intends to publish a report on the use of capital and climate change

25 <https://www.sec.gov/news/press-release/2021-42>.

26 <https://www.clientearth.org/latest/press-office/press/clientearth-starts-legal-action-against-shell-s-board-over-mismanagement-of-climate-risk/>.

Date	Action
End 2022	Government intends to legislate on climate change mitigation and climate change adaptation criteria under the UK Green Taxonomy
End 2022	Transition Plan Taskforce to publish a consultation on transition plans, with a view to finalisation in early 2023
End 2022	Updated Green Finance Strategy expected to be published
2023	Government expects firms to start publishing transition plans
Q1 2023	Government to consult on expanding climate criteria and the remaining four environmental objectives under the UK Green Taxonomy
30 June 2023	Deadline for making first public disclosures under FCA's climate-related disclosure regime
End 2023	Government to assess the progress made by the UK's pensions and investment sectors towards stronger stewardship

The key market challenges in the UK include:

- a* Small overall market share: green finance represents a very small proportion of overall UK financial markets activity.
- b* Funds not being used to transition: companies in industries such as fossil fuels are not using raised funds to invest in transition.
- c* Slow transition in the equity markets: the debt markets are becoming greener but the equity markets have been much slower to transition.
- d* Greenwashing: marketing spin that highlights a company's sustainability credentials in a potentially misleading way.
- e* Expectations versus reality: no amount of green financing will solve the problem unless companies, the government and financial institutions are clear about what exactly they are doing to meet their public commitments to reduce their impact and reach net zero.

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Anna-Marie Slot is Ashurst's first global ESG/sustainability partner, appointed in 2019 and global head of high yield debt. She leads the firm's ESG strategy both internally and for clients. She has delivered a number of significant initiatives including establishing the firm's sustainability goals, co-creating Ashurst's first digital product, ESGReady and launching Ashurst's first podcast channel, ESG Matters@Ashurst, and its first series, '30 for Net Zero 30'. Together with Tara Waters, she co-leads the Fintech Legal Labs powered by Ashurst. Anna-Marie was also named the 'Most Innovative Sustainable Lawyer' at the *Financial Times* Innovative Lawyers Europe Awards 2021.

Anna-Marie has over two decades of finance experience acting for investment banks and companies in a wide range of corporate finance and securities transactions, including high yield debt offerings, sustainable finance, liability management including consents and tender offers, refinancings and numerous securities transactions, such as Rule 144A and Regulation S debt offerings, as well as mezzanine debt investments and senior credit facilities.

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