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WORKING DRAFT
Applying the Green Finance Taxonomy
User Guidance to the Draft Green Finance Taxonomy

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IN PARTNERSHIP WITH

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About South Africa's Green Finance Taxonomy Project

South Africa's National Treasury published the draft Technical Paper on "Financing a Sustainable Economy" in May 2020 with the aim of unlocking access to sustainable finance and stimulating the allocation of capital to support a development-focused and climate-resilient economy.

One of the recommendations of the paper is to "develop or adopt a taxonomy for green, social and sustainable finance initiatives, consistent with international developments, to build credibility, foster investment and enable effective monitoring and disclosure of performance".

A green finance taxonomy is an official classification or catalogue that defines a minimum set of assets, projects, and sectors that are eligible to be defined as "green" in line with international best practice and national priorities. It can be used by investors, issuers, and other financial sector participants to track, monitor, and demonstrate the credentials of their green activities in a more confident and efficient way.

A Steering Committee and Working Groups were established to support the implementation of the Technical Paper recommendations. These include a Taxonomy Working Group chaired by National Treasury and including representatives from South Africa's Department of Forestry, Fisheries and the Environment (DFFE); Department of Monitoring and Evaluation (DPME); the Financial Sector Conduct Authority (FSCA); the Prudential Authority (PA); the Johannesburg Stock Exchange (JSE); Banking Association South Africa (BASA); Batseta (Council of Retirement Funds for South Africa); the Association for Savings and Investment South Africa (ASISA); and representatives from banks and retirement funds.

The initial phase of work for the Taxonomy Working Group is supported by IFC, part of the World Bank Group, through IFC's Green Bond Market Development program in partnership with SECO (Swiss State Secretariat for Economic Affairs) and Sida (Swedish International Development Cooperation Agency). It also benefits from global support from the IFC-facilitated Sustainable Banking Network (SBN).

National Business Initiative and the Carbon Trust were selected to carry out research, stakeholder consultation, and drafting on behalf of the Working Group for the first phase to (i) establish a governance structure and principles for the development and ongoing maintenance of a national sustainable finance taxonomy, and (ii) to develop an initial draft taxonomy for green and climate finance activities, leveraging existing international frameworks.

The **Draft Version** of such a taxonomy for South Africa has been developed through extensive engagement with South African stakeholders over the past year. Presentations, webinars, and other materials are available via the following link: https://sustainablefinanceinitiative.org.za/taxonomy-working-group-oct/

The Taxonomy will have a range of benefits. Among other things, it will

- Help the financial sector with clarity and certainty in selecting green investments in line with international best practice and South Africa's national policies and priorities.
- Reduce financial sector risks through enhanced management of environmental and social performance.
- Reduce the costs associated with labelling and issuing green financial instrument.,
- Unlock significant investment opportunities for South Africa in a broad range of green and climate-friendly assets.
- Support regulatory and supervision oversight of the financial sector.

Purpose of this document

This document presents a working draft of the Green Finance Taxonomy user guidance – i.e. the step-wise guidance concerning how to use the taxonomy to determine taxonomic-alignment as well as guidance to determine financial metrics and related impact metrics.

The document serves to accompany the Green Finance Taxonomy Draft which is a working draft. Updates to the Green Finance Taxonomy Draft are in process.

Acknowledgments

We gratefully acknowledge the tremendous work of the EU Technical Expert Group on Sustainable Finance in developing the landmark final report on the EU taxonomy published in March 2020[1]. We have relied on this report, its taxonomy, and its guidance – as well as ongoing updates, including the EU Taxonomy Climate Delegated Act – as the foundation for the approach of the South African Green Finance Taxonomy Draft. This is in line with consistent recommendations by the project advisors, local stakeholders, and international experts that South Africa should seek to adapt relevant international good practice to the extent appropriate, in order to facilitate alignment and harmonisation for the benefit of users and stakeholders.

Oversight was provided by National Treasury, IFC, and the Taxonomy Working Group. Work was carried out by National Business Initiative (NBI) and Carbon Trust. Lead authors of the Draft Version are Christelle van Vuuren and Marc Coetzee of Carbon Trust. We thank the staff of the oversight organisations for rich input and strategic guidance. They include Sarah McPhail, Lusanda Fani, Kolisang Molukanele (National Treasury); Louise Gardiner, Quyen Thuc Nguyen, Berit Lindholdt Lauridsen, Francisco Avendano, Ben Gaffney, and Karin Ireton (IFC); Steve Nicholls, Reitumetse Molotsoane, Alex McNamara, and Bhavna Deonarain (NBI).

Special thanks go to members of the Taxonomy Working Group, including those from the following organisations: the Johannesburg Stock Exchange (JSE), ABSA, the Development Bank of Southern Africa (DBSA), Batseta (Council of Retirement Funds for South Africa), Old Mutual, the Prudential Authority (PA), BNP Paribas, FirstRand and Rand Merchant Bank (RMB), the Banking Association South Africa (BASA), the Department of Planning, Monitoring and Evaluation (DPME), the Department of Forestry, Fisheries and the Environment (DFFE), the Association for Savings and Investment South Africa (ASISA), Standard Bank, the Industrial Development Corporation of South Africa (IDC), the South African Reserve Bank (SARB) and the Financial Sector Conduct Authority (FSCA).

Valuable inputs were also received during the consultation process. We thank all who participated in the various discussions. In particular, we would like to thank Sean Kidney (Climate Bonds Initiative), and Nicole Martens (PRI) for invaluable insights from international best practice.

[1] Technical Expert Group on Sustainable Finance, 2020. Final Report on EU Taxonomy. [Online] Available at https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy_en.pdf [Accessed October 2020]

1. Introduction

Different taxonomy uses and users

Transitioning South Africa to an equitable, resilient, low-carbon green economy will require the range of economic actors each to act strategically and decidedly towards this, and best in a coordinated manner. A taxonomy provides a common language and agreed methodologies for determining eligibility, which enable different economic actors to identify and respond to investment opportunities and needs that contribute positively to specified objectives - such as the transition to a green economy - and which can support these actors to coordinate their actions. Therefore, the taxonomy can be used as a risk management tool as well as a tool that helps direct and redirect finance to green activities by helping markets manage the impact of climate change.

Table 1 non-exhaustively identifies potential users of a Green Finacne Taxonomy and the functional processes that a Green Finance Taxonomy could be integrated to.

Table 1: Potential users and uses of the taxonomy

User Group	*Example user*	*Typical user applications for the Green Finance Taxonomy* **(World Bank, 2020)**
POLICY MAKERS & GOVERNMENT AGENCIES 	Includes law makers and government departments e.g. DEFF, DPME, SARS, National Treasury, Municipalities	• Develop policy and delegated acts/regulations • Measure and account for aligned financial flows at different economic levels and improve and align tracking systems • Identify areas of underinvestment relative to objectives • Facilitate aligned pipeline development • Align to or reference elements of the taxonomy, such as in the context of setting public measures and standards of labels for green financial products or green bonds and in reporting on economic, NDC and SDG monitoring purposes
FINANCIAL MARKET PARTICIPANTS 	Includes market participants offering financial products e.g. financial institutions, banks, investors, bond issuers, pension providers	• Identify opportunities that align to taxonomy and criteria • Support investee engagement • Evaluate investment portfolios for taxonomic alignment and exposure • Evaluate new investments' taxonomic alignment • Evaluate existing products alignment, and originate and structure aligned new products • Design and shift investment and product policies and strategies • Understand and compile disclosures concerning exposure, in terms of or in addition to regulatory requirements
ASSET OWNERS 	Include non-financial companies and developers with non-financial reporting directives. e.g. mining houses and manufacturers	• Compile disclosures against the taxonomy regarding capital expenditure, operational expenditure and turnover • Support investor and capital markets engagement, to attract financing on the basis of being taxonomically and thematically aligned

Eligibility under the taxonomy should be assessed on a sector, asset and/or project basis within a company. A key part of a Taxonomy assessment includes defining what part of a corporate's activity can be assessed as green. Assessing a company's Taxonomy alignment will require a breakdown by turnover (or revenue, when appropriate), or capex and, if relevant, Opex. Typically, a company will report its turnover across a number of sub-sectors, this concept is illustrated in Figure 1 as follows:

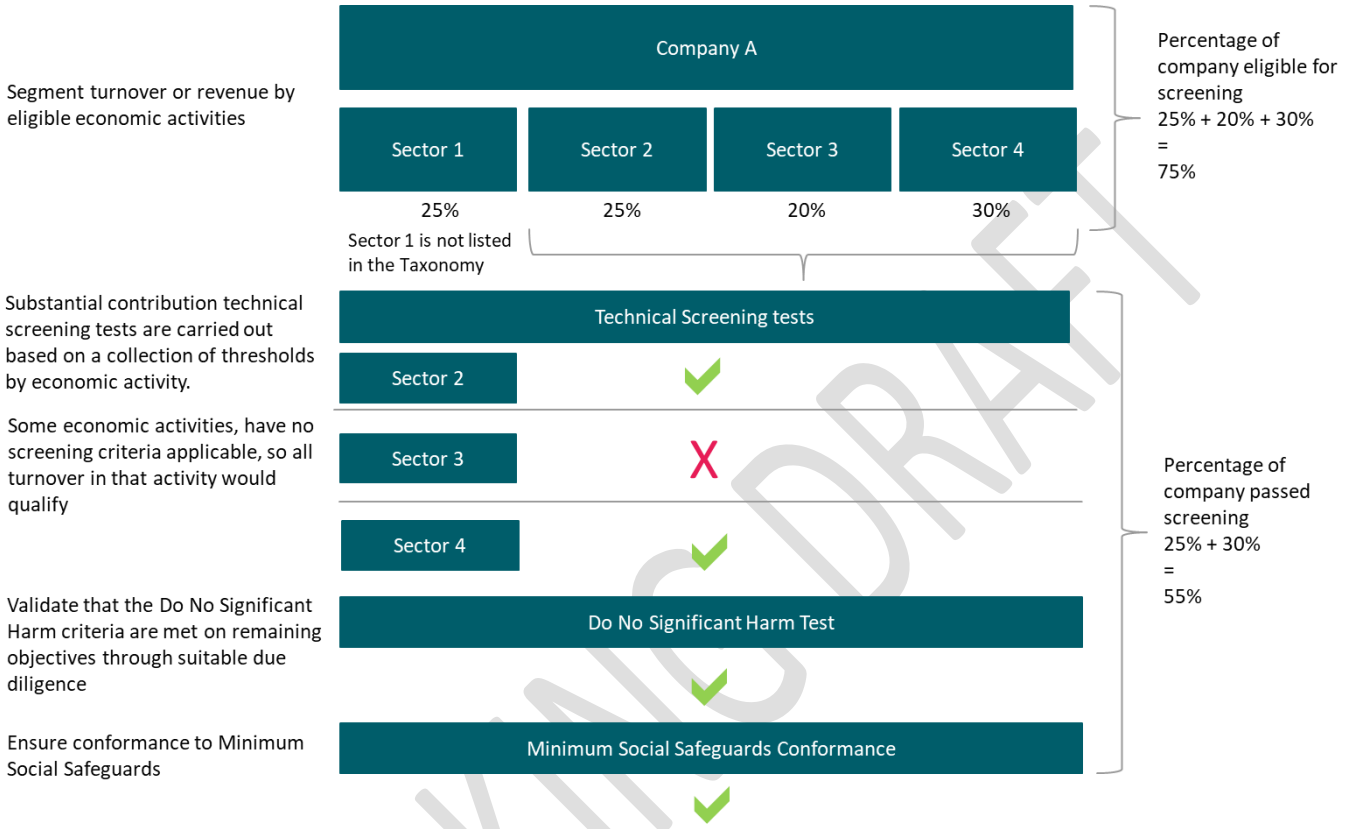


Figure 1: Determining taxonomy aligned finance (UNEP FI, 2021)[2]

In order to assess whether finance is taxonomy aligned, the following sections within this guidance document should be referred to:

- For determining taxonomic-alignment of sectors, assets, and projects – refer to Section 2 Determining Taxonomy alignment
- For financial metrics that could be associated with taxonomically-aligned sectors, assets, and projects – refer to Section 3 Determining taxonomy-aligned finance
- For impact reporting concerning taxonomically-aligned sectors, assets, and projects – refer to Section 4 Sustainable development performance and impact reporting
- For general guidance in overcoming challenges – refer to 5 General challenges and consideration in applying the Taxonomy.

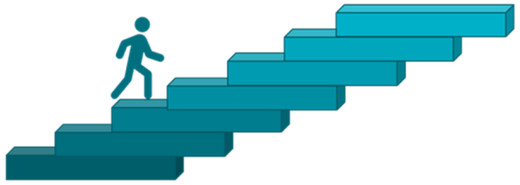
[2] UNEP Finance Initiative, Testing the application of the EU Taxonomy to core banking products: High level recommendations, Online Available at https://www.ebf.eu/events/ebf_unepfi_conference/ [Accessed March 2021]

2. Determining Taxonomy alignment

Process overview for determining an activity, asset or project as green

The seven-step process set out in Figure 1 can be used as guidance that will help determine taxonomic alignment of the economic activity under consideration. The result is binary – either 'taxonomically-aligned' or not. The guidance in this document provides details and suggestions for evaluating alignment with the Taxonomy criteria.

Seven-step approach to determine aliment with the Taxonomy



Step 1 — *Familiarise yourself with all the principles of the taxonomy*

To be taxonomically aligned, users need to meet all four principles

Principle 1: Substantially contribute to at least one of the six objectives of the taxonomy.

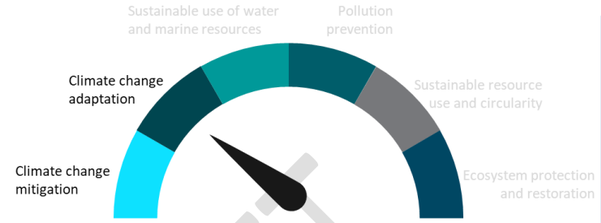
Principle 2: Meet applicable Technical Screening Criteria

Principle 3: Do no significant harm to any of the other objectives

Principle 4: Comply with Minimum Social Safeguards

Step 2 — *Principle 1: Substantially contribute to at least one of the six objectives of the taxonomy*

Identify which objective the economic activity under consideration substantially contributes to



The Taxonomy recognises **two distinct types** of substantial contribution that can be considered Taxonomy-aligned:

1. Activities that make a substantial contribution based on their **own performance**: For example, an economic activity being performed in a way that is environmentally sustainable.
2. **Enabling activities**: Activities that, by provision of their products or services, enable a substantial contribution to be made in other activities. For example, an economic activity that manufactures a component that improves the environmental performance of another activity.

Step 3 — *Principle 2: Meet applicable Technical Screening Criteria*

Identify whether the economic activity under consideration is covered by the current version of the taxonomy

1

Match economic activity under consideration within the taxonomy matrix

Locate the macro-sector that the economic activity under consideration would best relate to and then find the economic activity which best matches that specific economic activity.

2

Refer to the Technical Screening Criteria for the particular economic activity

After a match has been made, **use the referenced section number** provided in the matrix to direct you to where the technical screening criteria related to that specific economic activity under consideration can be found.

If there is **no economic activity** that relates to the economic activity under consideration, this means that the **economic activity does not yet exist** in the current version of taxonomy or that the activity exists in the other taxonomies (transition/social/brown taxonomies). If the economic activity is not found in other taxonomies, it is recommended that **application is made to the designated agency** for consideration and further development of the green finance taxonomy.

Step 4 — *Principle 2: Meet applicable Technical Screening Criteria*

Evaluate performance against technical screening criteria

Refer to make significant contribution criteria section

1 **Refer to the make significant contribution criteria** section of the table in alignment to the objective the economic activity intends to substantially contribute to.

Assess alignment to metrics and thresholds

2 **Assess alignment to metrics and thresholds** to determine whether the economic activity under consideration makes substantial contribution to the intended objective.

Report alignment to metrics and thresholds

3 If the economic activity under consideration meets the metrics and thresholds, this alignment should be **recorded and transparently reported**. If the economic activity under consideration does not meet the metrics and thresholds, the economic activity is not aligned to the taxonomy.

Step 5 — *Principle 3: Do no significant harm to any of the other objectives*

Evaluate performance against Do No Significant Harm Criteria of the other taxonomy objectives

1. **Refer to the Do No Significant Harm assessment** for guidance related to potential significant harm that the economic activity under consideration is associated with.

2. **Assess performance against each of the 5 objective's** Do No Significant Harm Criteria to ensure alignment with the criteria. **Ensure climate resilience of economic activity under consideration is evaluated.** Refer to the climate change vulnerability assessment process for evaluation guidance.

3. If the economic activity under consideration **does not meet** the Do No Significant Harm Criteria, the economic activity is **not aligned to the taxonomy.**

4. If the economic activity under consideration meets the Do No Significant Harm Criteria, the **alignment should be recorded and transparently reported.**

Step 6 — *Principle 4: Comply with Minimum Social Safeguards*

Evaluate compliance with minimum social safeguards

1

Companies and other issuers disclosing against the Taxonomy need to assess their compliance with MSS by ensuring implementation of policies, procedures and governance mechanisms that put into effect alignment with South African labour law and the standards in:

a) International Labour Organisation (ILO) core labour conventions;
b) OECD Guidelines on Multinational Enterprises (MNEs); and
c) UN Guiding Principles on Business and Human Rights

2

Refer to the OECD guidelines and due diligence guidance for Responsible Business Conduct (RBC). If the assessment is positive and compliance with minimum social safeguards is met, this assessment should be recorded and transparently reported.

Step 7 — *Conclude on taxonomic-alignment*

Disclose results

If the economic activity under consideration fully conforms to steps 2 – 6, taxonomic-alignment can be declared.

Declaration should include the final collective result with all supporting assessment results as well as relevant supporting details and impact indicators.

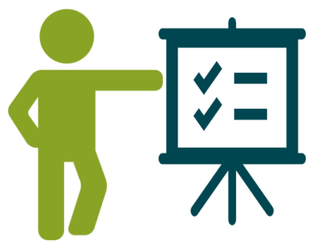


Figure 2: Seven-step approach to determine aliment with the Taxonomy

Step 1: Familiarise yourself with all the principles of the taxonomy

The current focus of the Green Finance Taxonomy is on classifying relevant activities into two fundamental categories: those economic activities that make substantial contribution to climate change mitigation and those which make substantial contributions to climate change adaptation. In order to perform the classification, Taxonomy users are expected to follow the principles provided by the Taxonomy. In its current form, the principles help the assessment to demonstrate that the economic activity under consideration:

1. Contributes substantially towards either Mitigation or Adaptation;
2. Meets the applicable Technical Screening Criteria (TSC);
3. Does no significant harm to any of the other taxonomy objectives; and
4. Meets minimum social standards referred to as 'Minimum Social Safeguards' (MSS).

The concept is illustrated in Figure 3 as follows:

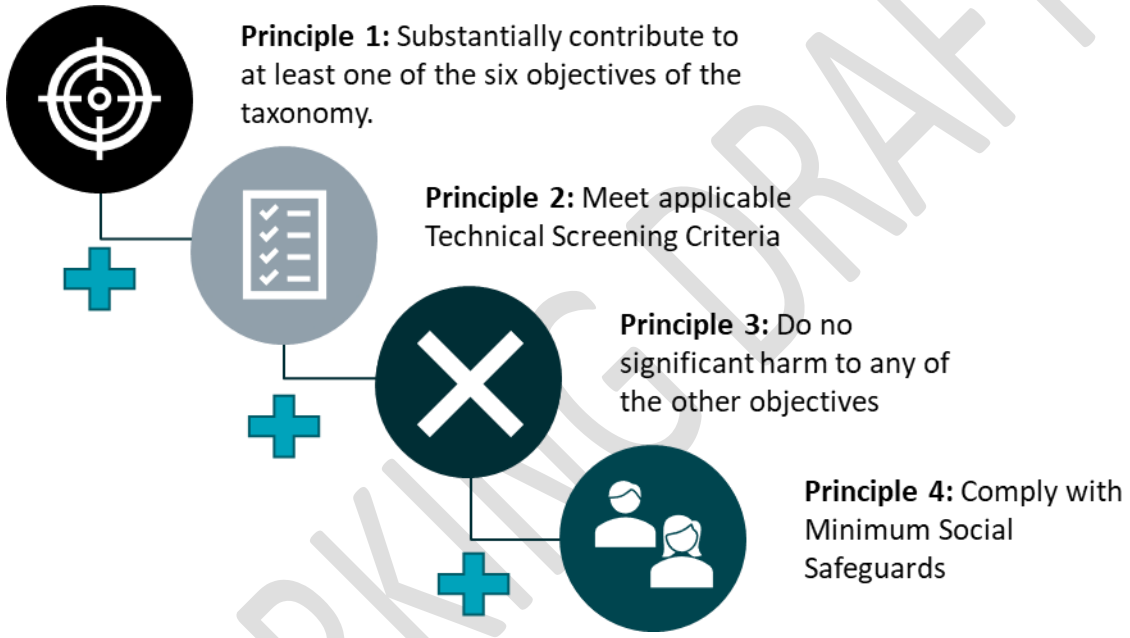


Figure 3: Principles of the Green Finance Taxonomy

In order to demonstrate that an economic activity aligns with the Taxonomy, users need to undertake an assessment against all the principles.

Step 2: Principle 1 - Substantially contribute to at least one of the six objectives of the taxonomy

Identify which objective the economic activity under consideration substantially contributes to

In order to determine whether an economic activity is eligible, Taxonomy users need to evaluate whether the activity contributes substantially to at least one of the six objectives of the Taxonomy. The current Taxonomy provides TSC specific to economic activities which make substantial contribution to climate change mitigation and climate change adaptation. Technical Screening Criteria related to the other taxonomy objectives have not yet been developed, therefore, substantial contribution to these objectives cannot be assessed using the current version of the taxonomy.

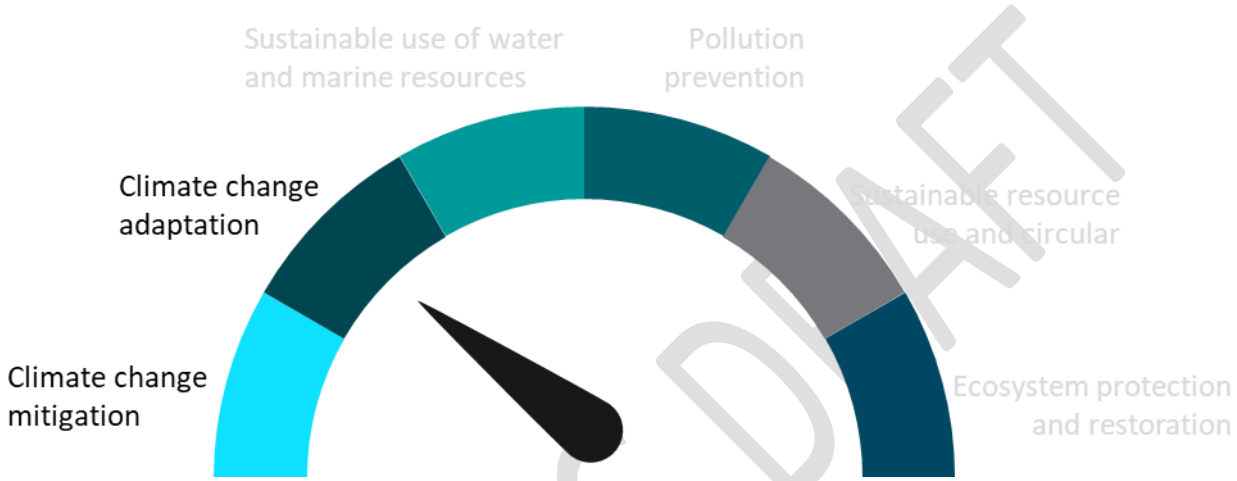


Figure 4: Taxonomy objectives

The Taxonomy recognises two distinct types of substantial contribution applicable across climate change mitigation and climate change adaptation, these different types of Substantial Contribution are reflected in the TSC:

1. Economic activities that make a substantial contribution based on their own performance: For example, an economic activity being performed in a way that is environmentally sustainable.
2. Enabling activities: economic activities that, by provision of their products or services, enable a substantial contribution to be made in other activities. For example, an economic activity that manufactures a component that improves the environmental performance of another activity.

Defining substantial contribution climate change mitigation

An economic activity shall be considered to contribute substantially to the environmental objective of climate change mitigation[3] where that activity substantially contributes to the stabilization of greenhouse gas concentrations in the atmosphere at a level that prevents dangerous anthropogenic interference with the climate system by avoiding or reducing greenhouse gas emissions or enhancing greenhouse gas removals through any of the following means, including through process or product innovation, consistent with the long term temperature goal of the Paris Agreement:

a) Generating, transmitting, storing, distributing or using renewable energy, including through using innovative technology with a potential for significant future savings or through necessary reinforcement or extension of the grid;
b) Improving energy efficiency except for power generation activities;
c) Increasing clean or climate-neutral mobility;
d) Switching to the use of sustainably sourced renewable materials;
e) Increasing the use of environmentally safe carbon capture and utilisation (CCU) and carbon capture and storage (CCS) technologies that deliver a net reduction in greenhouse gas emissions;

f) Strengthening land carbon sinks, including through avoided deforestation and forest degradation, restoration of forests, sustainable management and restoration of croplands, grasslands and wetlands, afforestation, and regenerative agriculture;
g) Establishing energy infrastructure required for enabling the decarbonisation of energy systems;
h) Producing clean and efficient fuels from renewable or carbon-neutral sources; and
i) Enabling any of the above.

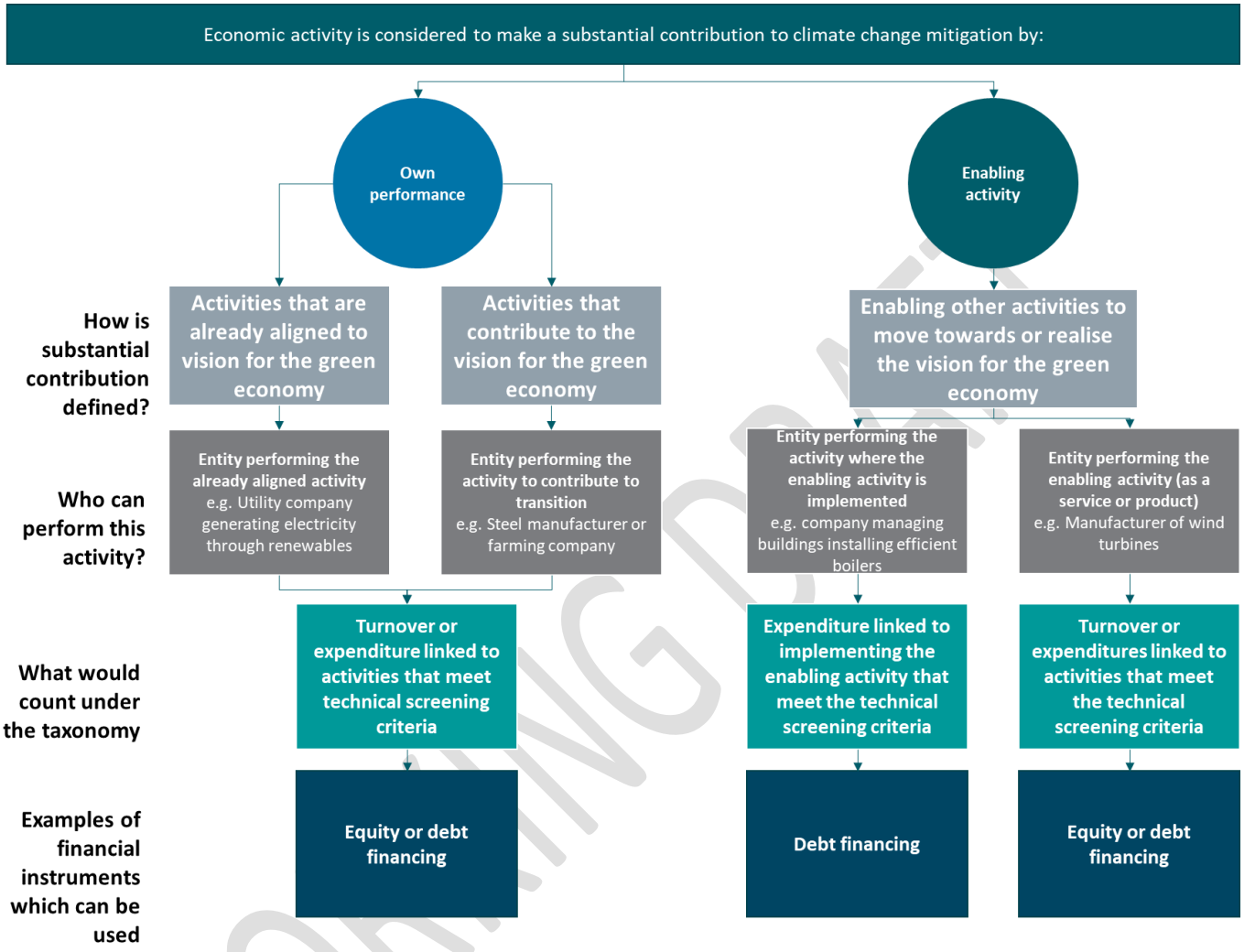


Figure 5: Activities making substantial contribution to climate change mitigation

An economic activity for which there is no technologically and economically feasible low carbon alternative, shall be considered to contribute substantially to climate change mitigation as it supports the transition to a low carbon economy by phasing out greenhouse gas emissions, in particular from solid fossil fuels, where that activity:

a) Has greenhouse gas emission levels that correspond to the best performance in the sector or industry;
b) Does not hamper the development and deployment of low-carbon alternatives; and
c) Does not lead to a lock-in in carbon-intensive assets considering the economic lifetime of those assets.

Defining substantial contribution to climate change adaptation

The starting point for the adaptation is the same as that for climate change mitigation. However, this does not indicate that these activities are more important than any other for climate change adaptation objectives. Below detail establishes a framework for understanding substantial contributions to climate change adaptation objectives. This

definition is broadly consistent with that provided by the Intergovernmental Panel on Climate Change[4]. An economic activity shall be considered to contribute substantially to climate change adaptation where:

a) That economic activity includes adaptation solutions that either substantially reduce the risk of adverse impact or substantially reduces the adverse impact of the current and expected future climate on that economic activity itself without increasing the risk of an adverse impact on other people, nature and assets; or where
b) That economic activity provides adaptation solutions that contribute substantially to preventing or reducing the risk of adverse impact or substantially reduces the adverse impact of the current and expected future climate on other people, nature or assets, without increasing the risk of an adverse impact on other people, nature and assets.

The adaptation solutions referred to in point (a) above shall be assessed and prioritised using the best available climate projections and shall, as a minimum, prevent or reduce:

i. The location-specific and context-specific adverse impact of climate change on the economic activity; or
ii. The adverse impact that climate change may have on the environment within which the economic activity takes place

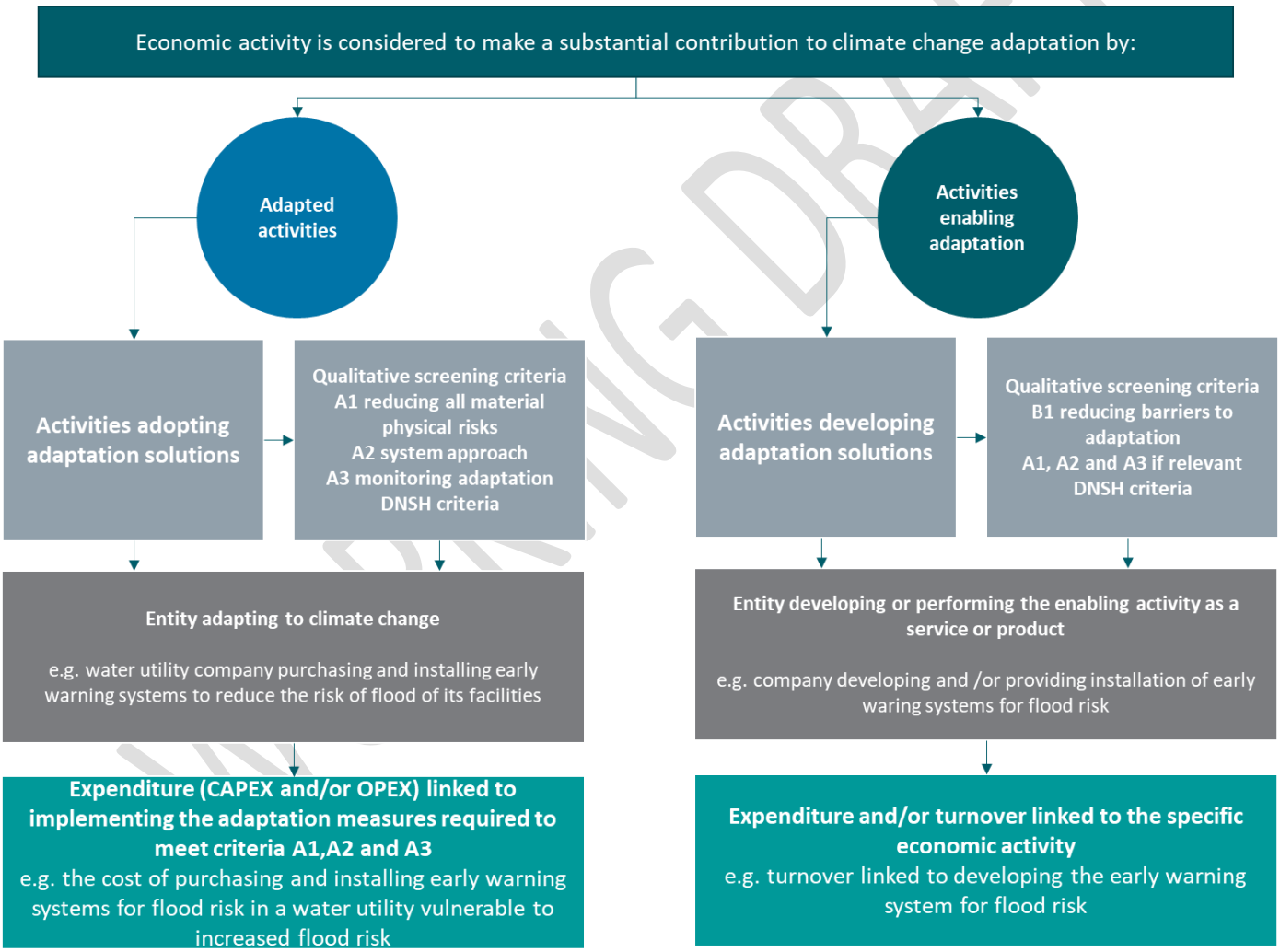


Figure 6: Activities making substantial contribution climate change adaptation

[4] The IPCC provides the following definition of adaptation in their 5th Assessment Report: 'The process of adjustment to actual or expected climate and its effects. In human systems, adaptation seeks to moderate or avoid harm or exploit beneficial opportunities. In some natural systems, human intervention may facilitate adjustment to expected climate and its effects'. IPCC (2014), 'Climate Change 2014: Impacts, Adaptation, and Vulnerability. Part B: Regional Aspects. Contribution of Working Group II to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change', Barros, V.R., C.B. Field, D.J. Dokken, M.D. Mastrandrea, K.J. Mach, T.E. Bilir, M. Chatterjee, K.L. Ebi, Y.O. Estrada, R.C. Genova, B. Girma, E.S. Kissel, A.N. Levy, S.

The adverse impact of climate change considered for the development of the taxonomy include impact resulting from both chronic or slow onset climate-related hazards (such as average temperature increase and sea level rise) and rapid or acute climate related hazards (such as extreme rainfall, storm surges, flooding, and heat waves). Classification of climate related hazards are described under Classification of climate-related hazards section of this report.

Material physical climate risk is the risk of (financial and non-financial) losses occurring due to performance failures, performance delays or incomplete performance of an economic activity resulting from climate-related hazards. With that in mind, climate change adaptation comprises two types of substantial contribution to adaptation objectives:

1. **Adapted activities:** an economic activity is adapted to all material physical climate risks identified for the economic activity to the extent possible and on a best effort basis; and/or
2. **Activities enabling adaptation of an economic activity:** the activity reduces material physical climate risk in other economic activities and/or addresses systemic barriers to adaptation, and is itself also adapted to physical climate risks.

Both types of activities must also meet the criteria for Do No Significant Harm to other environmental objectives and comply with minimum social safeguards established for the Taxonomy. Activities adapted to climate change and activities enabling adaptation of other economic activities provide a positive environmental impact by meeting a set of technical criteria for substantial contribution to adaptation and a set of criteria for doing no harm to other environmental objectives, whilst avoiding adverse impacts to people, asset and nature and preventing a lock-in in activities that undermine long-term environmental goals.

Guidance for substantial contributions to climate change adaptation

The following guidance is proposed to identify an economic activity that substantially contributes to climate change adaptation:

The economic activity reduces all material physical climate risks.

- In the case of an adapted economic activity, the activity integrates measures aimed at reducing all material physical climate risks to that activity as identified through a vulnerability assessment of material risks posed by both current weather variability and expected future climate change. The assessment should take into account chronic and acute climate-related hazards and associated physical climate risks across a range of scenarios, and account for uncertainty. It should consider geographic and temporal scales that are deemed appropriate for the economic activity.
- In the case of an economic activity enabling adaptation, the activity reduces material risks to other economic activities and/or addresses systemic barriers to adaptation, for example through a dedicated asset, technology, service or product, and itself integrates measures aimed at reducing material risks where applicable (e.g. in the case of a dedicated asset).

The economic activity does not adversely affect adaptation efforts by others.

Economic activities and the measures taken to address the material climate risks facing those activities should be consistent with adaptation needs in the applicable sector or region, considering opportunities to build resilience outside of the premises of a single activity. Those measures should also not increase the risk of an adverse impact on other people, nature and assets in terms of hindering adaptation efforts by others for example by shifting impacts faced by others

The economic activity has adaptation-related outcomes that can be defined and measured using adequate indicators.

When possible, the outcomes of adaptation activities should be monitored and measured against defined indicators for adaptation results. If possible, updated assessments of physical climate risks should be undertaken at the appropriate frequency (e.g. every five or ten years) depending on the risks, the context and the availability of new information, technologies or approaches or policies and regulations.

Step 3: Principle 2 - Meet applicable Technical Screening Criteria

Identify whether the economic activity under consideration is covered by the current version of the taxonomy

The Taxonomy matrix (found in the Green Finance Taxonomy Annex document) identifies economic macro-sectors and the associated economic activities within those macro-sectors that are needed as part of the future South African green economy. Using the Taxonomy matrix, users will be able to find the macro-sector that the economic activity under consideration would best relate to and then navigate to the economic activity which best matches that specific economic activity. Another possible way to do this is to identify the SIC code related to the economic activity under consideration (SIC code listing) and match it to the SIC code of the economic activity within the matrix. (SIC codes can cover broad activity and as a result match, a number of activities and, therefore, specific economic activity reference must be referred to when aligning specific economic activities to taxonomy activities). After a match has been made, use the referenced section number provided in the matrix to direct you to where the technical screening criteria related to that specific economic activity under consideration can be found.

The concept is illustrated in Figure 7 as follows:

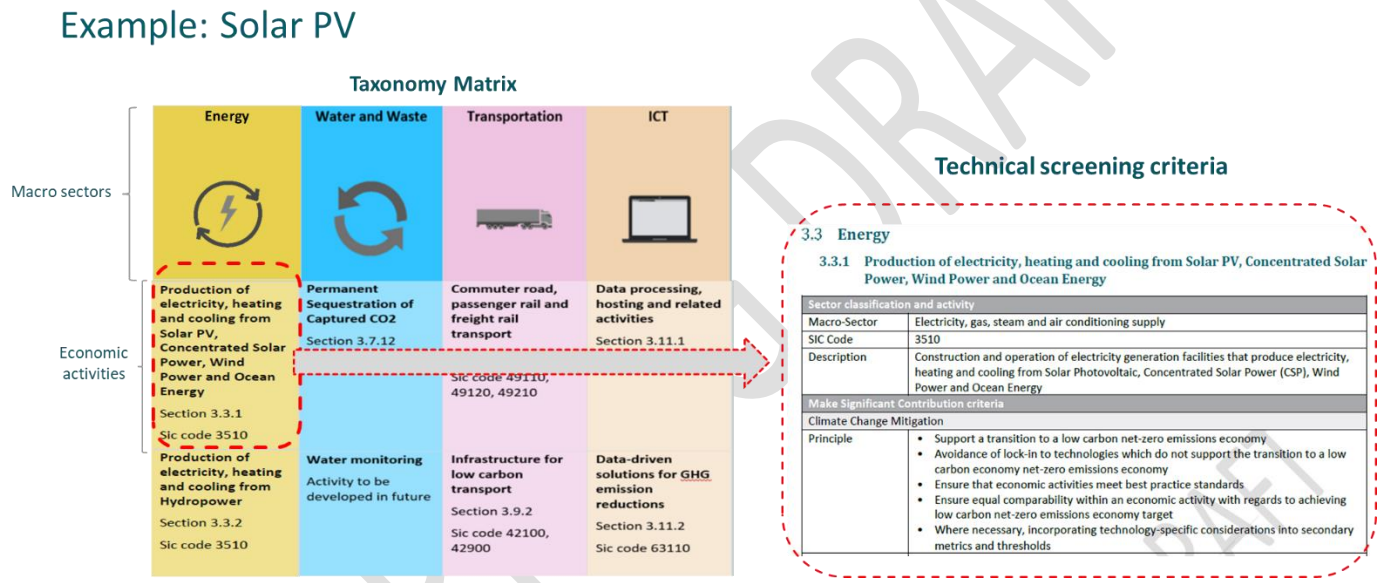


Figure 7: Navigation example using Taxonomy Matrix to identify economic activity under consideration

If there is no economic activity that relates to the economic activity under consideration, this means that the economic activity does not yet exist in the current version of taxonomy. In this case, it is recommended that an application is made to the designated agency (to be determined) for consideration and further development of the green finance taxonomy.

Step 4: Principle 2 - Meet applicable Technical Screening Criteria

Evaluate performance against technical screening criteria

After a match has been made as per Step 3, refer to the make significant contribution criteria section of the table in alignment to the objective the economic activity intends to substantially contribute to. The current version of the taxonomy is limited to technical screening criteria for substantial contribution to climate change mitigation and climate change adaptation.

For each of the activities selected, technical screening criteria have been developed that include:

a) **Principles:** The underlying rationale for how the activity will result in a substantial contribution and/or avoidance of significant harm to the environmental objective in question.
b) **Metrics and Thresholds:** including both metrics and thresholds: The method(s) by which the environmental performance of the economic activity will be measured, including defining the boundary for this measurement and the qualitative or quantitative conditions which must be met to enable the performance of the activity in a way that is considered environmentally sustainable.

The principles, metrics and thresholds can be found under the make significant contribution criteria of each economic activity. The concept is illustrated in Figure 8 as follows:

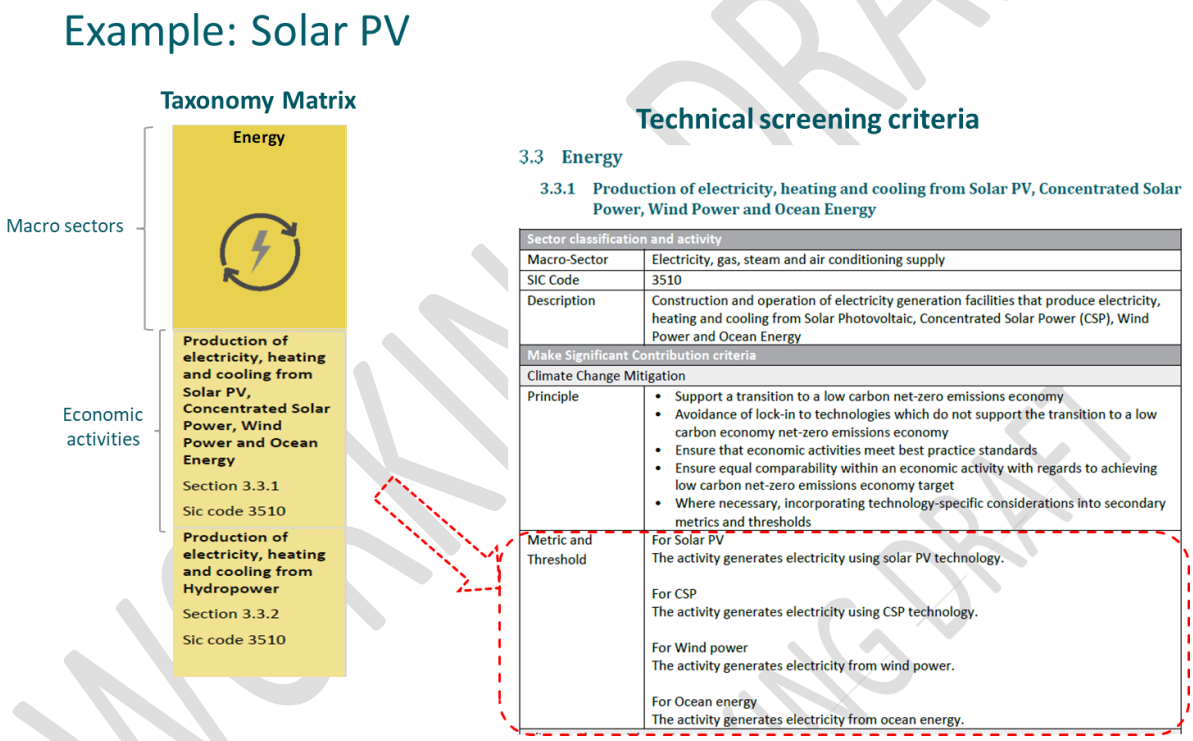


Figure 8: Navigation example illustrating an example of assessing substantial contribution to climate change mitigation

Using the information under this section, assess alignment to metrics and thresholds to determine whether the economic activity under consideration makes substantial contribution to the indented objective.

Testing alignment to the technical screening criteria requires quality and granular data. A combination of third-party data providers together with in-house research can ease the process. Examples include MSCI, ISS, Sustainalytics, FactSet, Trucost S&P, Carbon Delta, GS Sustain Taxonomy mapping tool and RepRisk. (MSCI, ISS, Sustainalytics, FactSet, Trucost, RepRisk)

If the economic activity under consideration meets the metrics and thresholds, this alignment should be reported transparently. If the economic activity under consideration does not meet the metrics and thresholds, the economic activity is not aligned to the taxonomy.

Screening criteria for activities making a substantial contribution to climate change adaptation

The screening criteria are specific characteristics that can be used to determine whether an economic activity provides a substantial contribution to adaptation. These screening criteria vary between 'adapted' activities and activities that enable adaptation.

Criterion	Description
A1: Reducing material physical climate risks	The economic activity must reduce all material physical climate risks to that activity to the extent possible and on a best effort basis.
A1.1	The economic activity integrates physical and non-physical measures aimed at reducing - to the extent possible and on a best effort basis - all material physical climate risks to that activity, which have been identified through a risk assessment.
A1.2	The above-mentioned assessment has the following characteristics: • considers both current weather variability and future climate change, including uncertainty; • is based on robust analysis of available climate data and projections across a range of future scenarios; • is consistent with the expected lifetime of the activity.
A2: Supporting system adaptation	The economic activity and its adaptation measures do not adversely affect the adaptation efforts of other people, nature and assets.
A2.1	The economic activity and its adaptation measures do not increase the risks of an adverse climate impact on other people, nature and assets, or hamper adaptation elsewhere. Consideration should be given to the viability of 'green' or 'nature-based-solutions' over 'grey' measures to address adaptation.
A2.3	The economic activity and its adaptation measures are consistent with sectoral, regional, and/or national adaptation efforts.
A3: Monitoring adaptation results	The reduction of physical climate risks can be measured.
A3.1	Adaptation results can be monitored and measured against defined indicators. Recognising that risk evolves over time, updated assessments of physical climate risks should be undertaken at the appropriate frequency where possible.

The table below describes the screening criteria for economic activities enabling adaptation.

Criterion	Description
B1. Supporting adaptation of other economic activities	The economic activity reduces material physical climate risk in other economic activities and/or addresses systemic barriers to adaptation. Activities enabling adaptation include, but are not limited to, activities that: a) Promote a technology, product, practice, governance process or innovative uses of existing technologies, products or practices (including those related to natural infrastructure); or, b) Remove information, financial, technological and capacity barriers to adaptation by others.
B1.1	The economic activity reduces or facilitates adaptation to physical climate risks beyond the boundaries of the activity itself. The activity will need to demonstrate how it supports adaptation of others through:

	• an assessment of the risks resulting from both current weather variability and future climate change, including uncertainty, that the economic activity will contribute to address based on robust climate data; • an assessment of the effectiveness of the contribution of the economic activity to reducing those risks, considering the scale of exposure and the vulnerability to them
B1.2	In the case of infrastructure linked to an activity enabling adaptation, that infrastructure must also meet the screening criteria A1, A2 and A3.

Classification of climate-related hazards

The climate-related hazards considered are limited to the potential occurrence of a weather and climate-related natural physical event or trend[5]. The climate-related hazard classification comprises four major hazard groups, with hazards related to water, temperature, wind, and mass-movements. All groups include acute (extreme) and chronic (slow-onset) hazards, as adaptation must account for both rapid as well as gradual changes in the weather and climate to take the appropriate adaptation measures and avoid maladaptation[6].

This analysis focusses on the most important or significant hazards and is designed to guide the user to consider the most salient physical risks when mapping the sensitivities of a given sector. All secondary hazards[7] resulting from climate-related hazards (including but not limited to chemical, biological, ecological and epidemiological hazards) are excluded. It is however advisable to assess the risk of such secondary hazards and consider measures to address them for each economic activity.

Table 2: Classification of climate-related hazards

Climate related hazard type	Temperature related	Wind-Related	Water-related	Solid mass- related
Chronic	Changing temperature (air, freshwater, marine water)	Changing wind patterns	Changing precipitation patterns and types (rain, hail, snow/ice)	Coastal erosion
	Heat stress		Precipitation and/or hydrological variability	Soil degradation
	Temperature variability		Ocean acidification	Soil erosion
			Saline intrusion	Solifluction
			Sea level rise	
			Water stress	
Acute	Heat wave	Cyclone, hurricane, typhoon	Drought	Avalanche

[5] IPCC, 2014, Climate Change 2014: Synthesis Report. Contribution of Working Groups I, II and III to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change [Core Writing Team, R.K. Pachauri and L.A. Meyer (eds.)]. IPCC, Geneva, Switzerland, 151 pp (https://www.ipcc.ch/site/assets/uploads/2018/02/SYR_AR5_FINAL_full.pdf, last visit 02/04/2019).

[6] There are clearly linkages with disaster risk reduction in the effort of reducing physical climate risks resulting from extreme climate-related hazards. Geophysical and technological hazards are outside the domain of adaptation to climate change.

[7] As an example, new biological pests or increased prevalence of existing pests can result from changing temperatures. Forests and agriculture are typically sensitive to warmer (minimum) temperatures and, in this example, their effects on pests. In this case, the changing prevalence of pests is a secondary hazard against which adaptation measures may be needed.

	Cold wave/frost	Storm (including dust and sandstorms)	Heavy precipitation (rain, hail, snow/ice)	Landslide
	Wildfire	Tornado	Flood (coastal, fluvial, pluvial, ground water)	Subsidence
			Glacial lake outburst	

Step 5: Principle 3 - Do no significant harm to any of the other objectives

Evaluate performance against Do No Significant Harm Criteria of the other taxonomy objectives

Within the Technical Screening Criteria table of each economic activity, guidance regarding potential significant harm associated with economic activity is provided together with the criteria related to each objective.

The concept is illustrated in Figure 9 as follows:

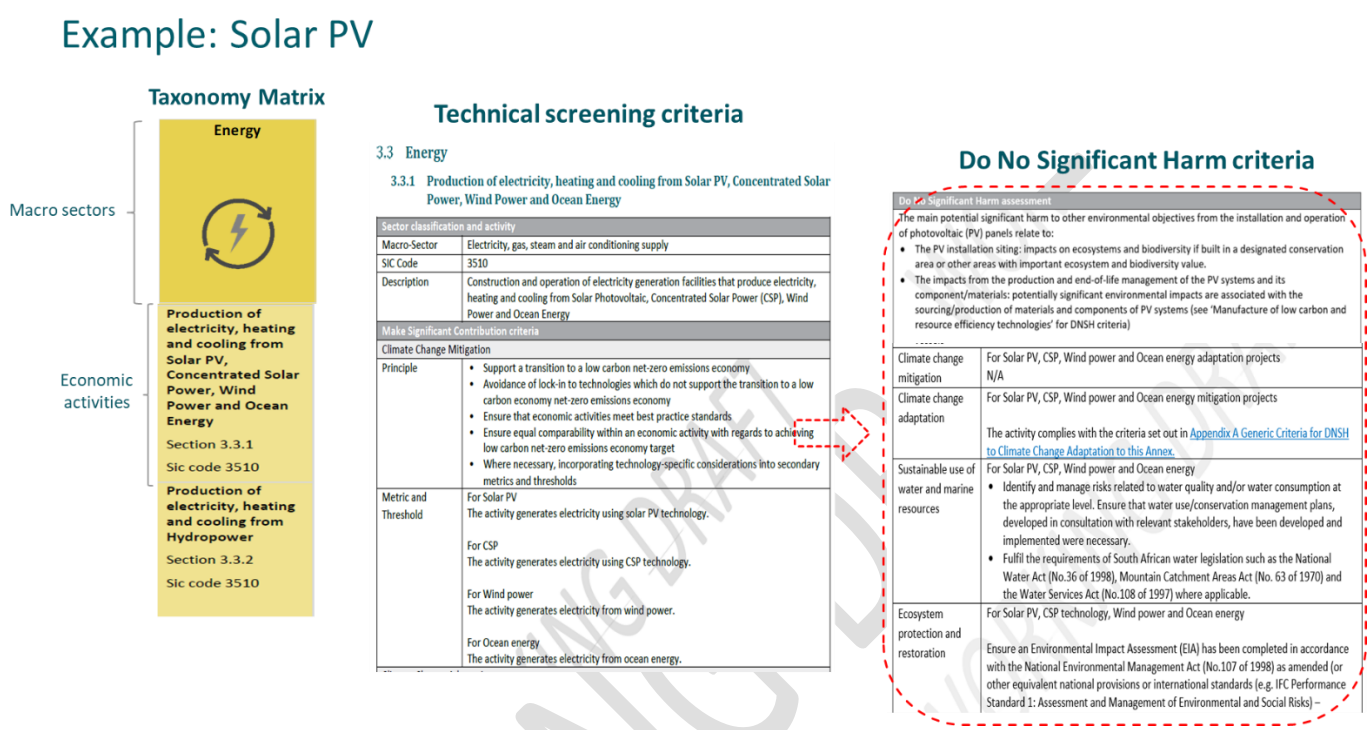


Figure 9: Navigation example illustrating Do No Significant Harm Criteria

Users need to assess performance against each of the 5 objective's Do No Significant Harm Criteria (excluding the objective that the economic activity under consideration intends to substantially contribute to) to be Taxonomy aligned. Additionally, recognition of a economic activity as taxonomically-aligned (and being effective in making its significant contribution) requires the activity to demonstrate climate change resilience. For a new activity and/or activity upgrading or altering existing assets or processes the physical climate risks that are material to the activity need to be identified from those listed within Table 2: Classification of climate-related hazards by performing a robust climate risk and vulnerability assessment. Climate risk hazards under different climate scenarios and for different areas can be identified using the risk tool within the Council for Scientific and Industrial Research's GreenBook (GreenBook)[8]. Figure 10 visually illustrates the climate change vulnerability assessment process to be undertaken. The assessment is required to be proportionate to the scale of the activity and its expected lifespan, such that:

a) For investments into activities with an expected lifespan of less than 10 years, the assessment is performed, at least by using downscaling of climate projections; and
b) For all other activities, the assessment is performed using high resolution, state-of-the-art climate projections across a range of future scenarios consistent with the expected lifetime of the activity, including, at least, 10 to 30 years climate projections scenarios for major investments.

Additionally, the economic operator is required to develop a plan to implement adaptation solutions to reduce material physical climate risks to the activity. Those adaptation solutions must not adversely affect the adaptation efforts or the level of resilience to physical climate risks of other people, of nature, of assets and of other economic activities and are consistent with local, sectoral, regional or national adaptation efforts.

[8] CSIR. 2019. Green Book: *Adapting South African settlements to climate change*. Online Available at: www.greenbook.co.za

For activity upgrading or altering existing assets or processes, the adaptation solutions identified need to be implemented within five years from the start of the activity.

If the economic activity under consideration does not meet the Do No Significant Harm Criteria, the economic activity is not aligned to the taxonomy. If the economic activity under consideration meets the Do No Significant Harm Criteria, this alignment should be transparently disclosed.

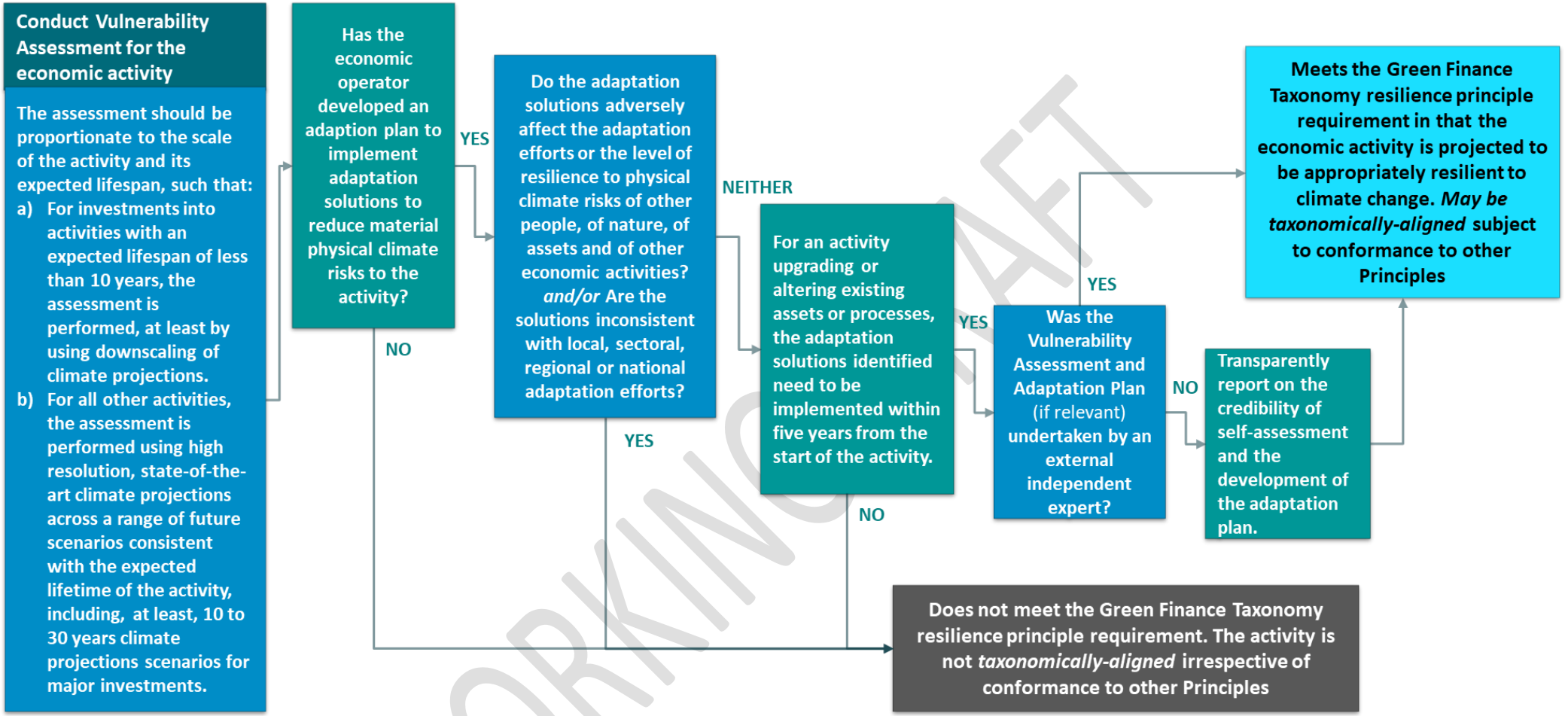


Figure 10: Climate change vulnerability assessment process

Step 6: Principle 4 - Comply with Minimum Social Safeguards

Evaluate compliance with Minimum Social Safeguards (MSS)

Companies and other issuers disclosing against the Taxonomy need to assess their compliance with MSS by ensuring implementation of policies, procedures and governance mechanisms that put into effect alignment with South African labour law and the standards in:

a) International Labour Organisation (ILO) core labour conventions;
b) OECD Guidelines on Multinational Enterprises (MNEs); and
c) UN Guiding Principles on Business and Human Rights

The concept is illustrated in Figure 6 as follows:

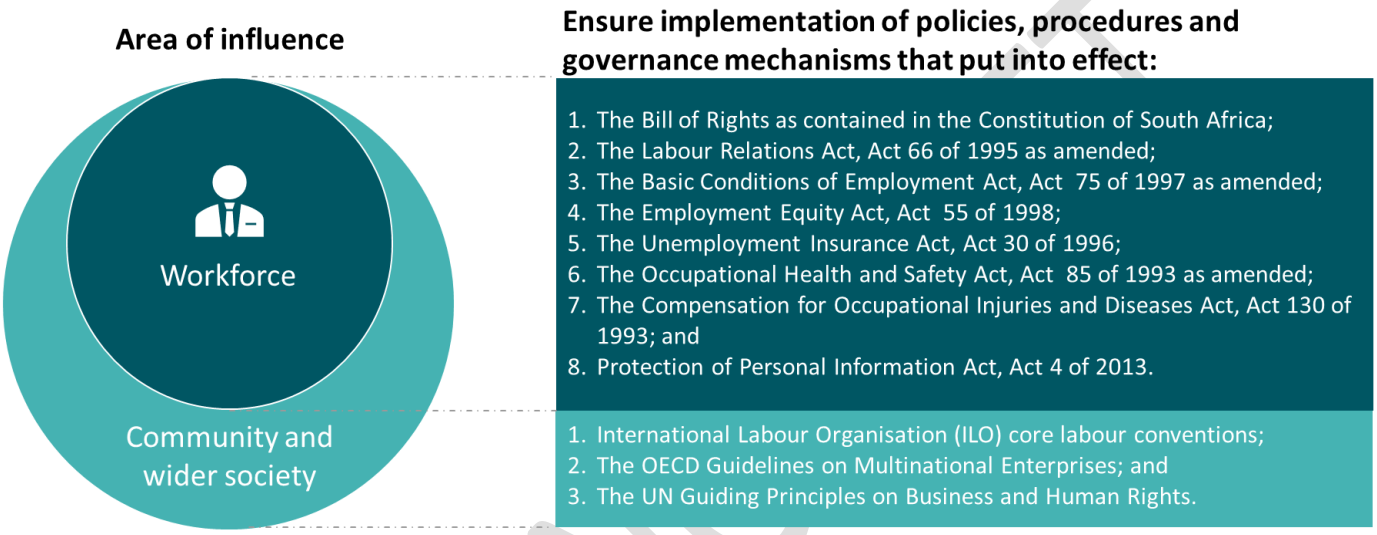


Figure 11: Minimum Social Safeguards

There are two areas of influence that need to be considered when ensuring alignment with policies, procedures and governance mechanisms that put into effect social risk management. The first is that the workforce employed by the company or issuer will need to comply with South African labour law. This includes

1. The Bill of Rights as contained in the Constitution of South Africa;
2. The Labour Relations Act, Act 66 of 1995 as amended;
3. The Basic Conditions of Employment Act, Act 75 of 1997 as amended;
4. The Employment Equity Act, Act 55 of 1998;
5. The Unemployment Insurance Act, Act 30 of 1996;
6. The Occupational Health and Safety Act, Act 85 of 1993 as amended;
7. The Compensation for Occupational Injuries and Diseases Act, Act 130 of 1993;
8. Protection of Personal Information Act, Act 4 of 2013

and should be explicitly included in a formalised policy or procedure documents held by the company or issuer.

Regarding the second area which relates to social impacts concerned with the community and wider society, the process for identification and management of social risks and impacts (those beyond labour, taxation and OHS compliance considerations) would include aspects related to robust social due diligence process. For example, company's and issuers have the responsibility to ensure engagement of service providers and development contractors that manage social risks and impacts sufficiently, and remains exposed if social controls are inadequate – even if the contractor is legally compliant. To note that, although South African legal requirements are comprehensive, social risk and impacts are likely to be beyond that controlled when ensuring legal compliance alone – particularly in the social dimension which may be complex and highly sensitive to the local context. Scrutinising prospective service providers and development contractors for their governance and operational controls is an increasingly mainstream

practice to ensure adequate social risk management. Figure 12 represents six areas related to safeguarding due diligence that companies and issuers can consider.

Figure 12: Safeguard due diligence[9]

There are various guideline materials and frameworks that provide guidance related to assessing social risk and adopting social due diligence process. Some examples of these include:

- OECD guidelines and due diligence guidance for Responsible Business Conduct (RBC);
- The Equator Principle EP4;
- IFC performance Standards

Companies and issuers with such processes in place would be able to provide data that will assist in assessing compliance with the MSS.

Assessments that result in positive compliance with MSS should be transparently disclosed together with the associated supporting evidence.

As part of the first phase of the South African Green Finance Taxonomy development process, it is established that principles and standards for substantially contributing to social objectives is needed. However, at this time, necessary underpinning tools and data are in process of development but not yet suitable for pre-emptive integration. In addition, the project has focused on establishment of the foundational focus areas, with the ambition to expand the Taxonomy for further coverage, given necessary and appropriate resourcing, time, design, development, engagement, testing and coordination.The addition of social objectives and the identification of activities that are more socially conscionable is being developed under a separate project 'Expanding the South African Green Finance Taxonomy and embedding its use' in complementarity to the Green Finance Taxonomy. With the support of UK PACT (Partnering for Accelerated Climate Transitions), this project will undertake the critically important work to expand the Green Finance Taxonomy (GFT) to a Sustainable Finance Taxonomy (SFT);

1. Developing and integrating social aspects and just transition models into the green finance taxonomy,
2. Developing a chapter of the taxonomy specifically addressing transition,
3. Deepening and broadening the catalogue of South African-specific green activities and innovation needs, and
4. Integrating principles and guidance concerning climate-risk and low-carbon incompatible activities.

[9] DFID 2018

The SFT offers a way to tie the financial sector back to the real economy by providing a clear set of definitions for what "counts" towards sustainability in South Africa. Through its contribution to reasonable certainty and to transparency, it places the spotlight on the financial sector to align its activities with sincerity.

The project, lead by National Business Initiative and supported by the Carbon Trust, will continue to work with the financial sector, industry associations, regulators and national and sub-national government throughout. It will also learn from and work bilaterally with others working on similar taxonomy developments across the world, as knowledge and understanding grows and challenges with taxonomies are better understood. The project will also develop roadmaps and provide practical implementation support and knowledge building, to enable the adoption of the resulting SFT by financial actors and non-financial actors, in both the private and the public sectors.

Step 7: Conclude on taxonomic-alignment

Disclose results

If the economic activity under consideration fully conforms to steps 2 – 6, taxonomic-alignment can be declared. A declaration should include the final collective result with all supporting assessment results for each assessment as well as relevant supporting details and impact indicators.

A disclosure template is provided in Appendix A: Disclosure Template.

3. Determining taxonomy-aligned finance

The financial aspects of taxonomy-aligned economic activities may be determined and disclosed. The following sections articulate guidance to do so for the economic activity under consideration, and in aggregate to determine alignment of portfolios. This guidance aligns strongly to that provided by the EU Technical Export Group (TEG) on Sustainable Finance in the TEG March 2020 report to the European Commission.

The taxonomy-alignment must be determined for the economic activity. Thereafter can the specification of the taxonomy-aligned finance be determined, based on the specifics outlined in Section 2 Determining Taxonomy alignment. To note – there are differences in what finance metric may be recognised for different environmental objectives. Aggregate results as set out in Section 3.2 Determining portfolio or aggregate taxonomy-alignment for portfolios of the respective finance metric is done "bottom-up" from the results of the individual economic activity results.

3.1 Determining taxonomy-aligned financial metrics for an economic activity

In determining the taxonomy-aligned finance metrics and performance for an economic activity, the following guidance is pertinent:

- Table 3 provides specification for determining recognition of turnover, capital expenditure and operation expenditure, as well the differentiation in approach between different environmental objectives
- Figure 13 provides an example depiction of how each of these financial metrics may be aggregated from asset level to company level
- In terms of the example demonstrated in Figure 13, if an entity raises debt (bond or loan) for the project (which may be used to cover capital expenditure and/or operational expenditure), the debt would be considered taxonomically-aligned

Where an economic activity makes substantial contribution to more than one environmental objective, the following approach should be applied:

- The reporter is encouraged to assess and disclose the fact economic activities contribute to different objectives.
- The reporter is encouraged to disclose the significance of finance that is taxonomically-aligned, perf environmental objective.
- When the reporter discloses the total taxonomically-aligned finance metrics, there should be no double-accounting. I.e. if an economic activity is taxonomically-aligned – whether making contribution to one or multiple environmental objectives – the financial alignment is counted only once when totals are reported.

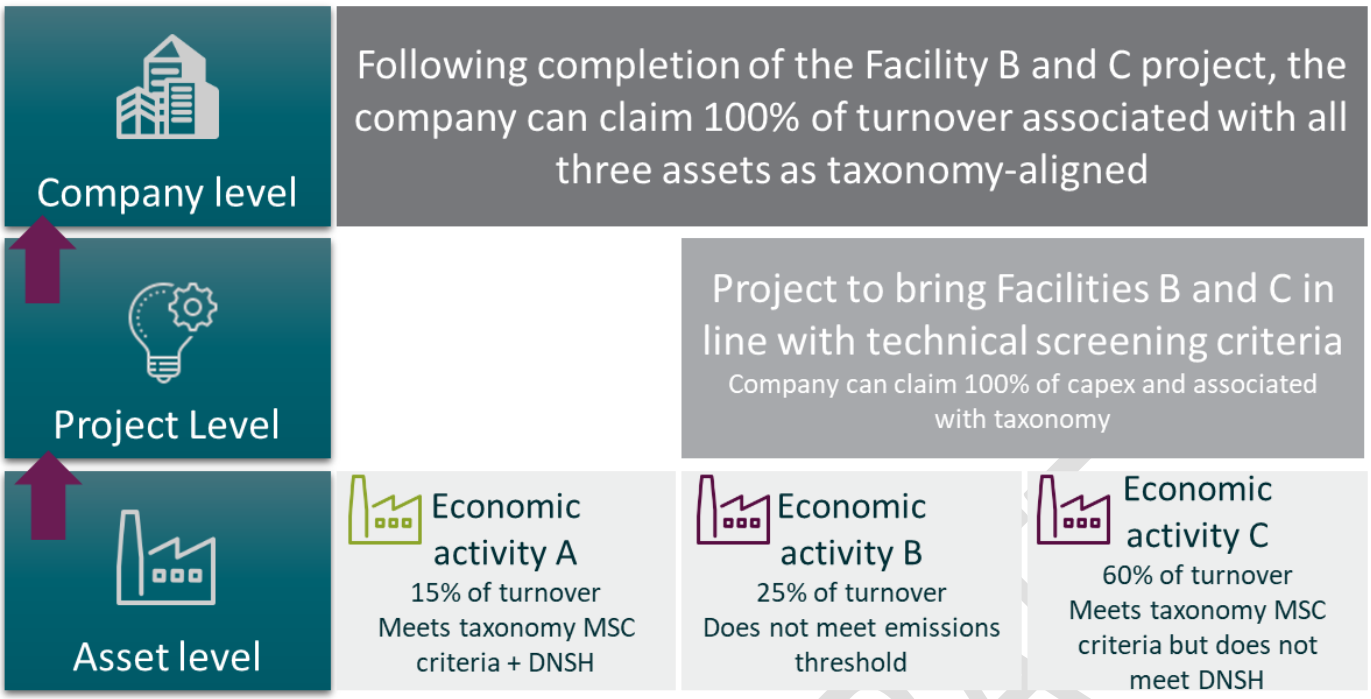


Figure 13: Example of how finance metrics may be determined from asset level to company level, for company level disclosure (EU Technical Expert Group on Sustainable Finance, 2020)

Eligibility under the Taxonomy should be assessed on an activity basis (as described in Section 2 Determining Taxonomy alignment) rather than by entity. However, entity-level taxonomic-aligned operations and finance activity are useful metrics to investors, and guidance for the computation is included in Section 3.2 Determining portfolio or aggregate taxonomy-alignment.

Table 3: Description of financial metrics for disclosure concerning taxonomically-aligned economic activities (EU Technical Expert Group on Sustainable Finance, 2020)

Financial Metric	***Definition***	***Use***	***Calculation approach of environmental objectives***	
			All environmental objectives excluding climate change adaptation	***Climate change adaptation***
Turnover	Net turnover means the amounts derived from the sale of products and the provision of services after deducting sales rebates and value added tax and other taxes directly linked to turnover. Overall turnover is equivalent to an activity's total revenues over some period of time. Turnover ratios are used by financial analysts to understand financial efficiency and profitability based on data found in financial statements.	The primary way of aggregating from an economic activity to a company level. Some companies may need to aggregate from asset to economic activity level. Turnover gives an indication of where a company currently is relative to the taxonomy. Turnover allows investors to report the % of their fund invested in taxonomy-aligned activities.	Can be counted where economic activity is taxonomy-aligned, making substantial contribution to the relevant MSC criteria of the environmental objective (not relevant to climate change adaptation) and relevant DNSH criteria. Turnover from a taxonomy-aligned economic activity can be counted on the basis that it can reach a level of environmental performance that is aligned with envisioned end state of the relevant environmental objective.	Turnover can be recognised only for activities enabling adaptation. Turnover cannot be recognised for adapted activities at this stage. The rationale is that adapting to climate change is an ongoing process that may not be final at any stage. Further guidance on this may be available in future.
Capital Expenditure and *Operational Expenditure*	A capital expenditure (capex) is a payment for goods or services recorded, or capitalised, on the balance sheet instead of expensed on the income statement. Operating expenses (opex) are shorter-term expenses required to meet the ongoing operational costs of running a business.	Capex may provide a sense of a company's direction of travel. Aside from helping investors analyse a company's investment in its existing and new fixed assets, capital expenditures can give an indication of a company's strategy for improving environmental performance and resilience.	Can be counted where costs incurred (capex and, if relevant, opex) are part of a plan to meet taxonomy technical screening criteria for relevant MSC criteria of the environmental objective (not relevant to climate change adaptation) and relevant DNSH criteria.	Can be counted where costs incurred (capex and, if relevant, opex) are part of a plan to meet Taxonomy technical screening criteria for substantial contribution to climate change adaptation and relevant DNSH criteria.

3.2 Determining portfolio or aggregate taxonomy-alignment

Evaluating underlying economic activity taxonomic-alignment and aggregating the results is expected to be especially relevant to financial sector users. The following sections provide a series of graphical examples adapted from the EU Technical Expert Group (EU Technical Expert Group on Sustainable Finance, 2020) as guidance for aggregation considerations and computations for each of:

- Taxonomy-aligned company-level turnover (refer Section 3.2.1 Process to evaluate company-level turnover taxonomy-alignment)
- Taxonomy-aligned equity fund exposure for equity investments in a portfolio (refer Section 3.2.2 Proportion of funds with underlying Taxonomy-aligned constituents – equity investments)
- Taxonomy-aligned debt fund exposure in debt and fixed income investments in a portfolio (refer Section 3.2.3 Proportion of funds with underlying Taxonomy-aligned constituents – fixed income (debt) investments)
- Taxonomy-aligned debt instrument fund constituents (refer Section 3.2.4 Process to evaluate green bond and green loan taxonomy-alignment)

In each application, where an economic activity underlying these computations makes substantial contribution to more than one environmental objective, the same guidance holds for disclosure concerning at the aggregate level, as does disclosure for each economic activity, as noted at the economic-activity level in Section 3.1 Determining taxonomy-aligned financial metrics for an economic activity. Notably:

- The reporter is encouraged to assess and disclose the contribution to different objectives.
- The reporter is encouraged to disclose the significance of finance that is taxonomically-aligned, per environmental objective.
- When the reporter discloses the total taxonomically-aligned finance metrics, there should be no double-accounting.

3.2.1 Process to evaluate company-level turnover taxonomy-alignment

Figure 14 explains the five steps, and example application, to determine investment-level taxonomy-alignment of company turnover.

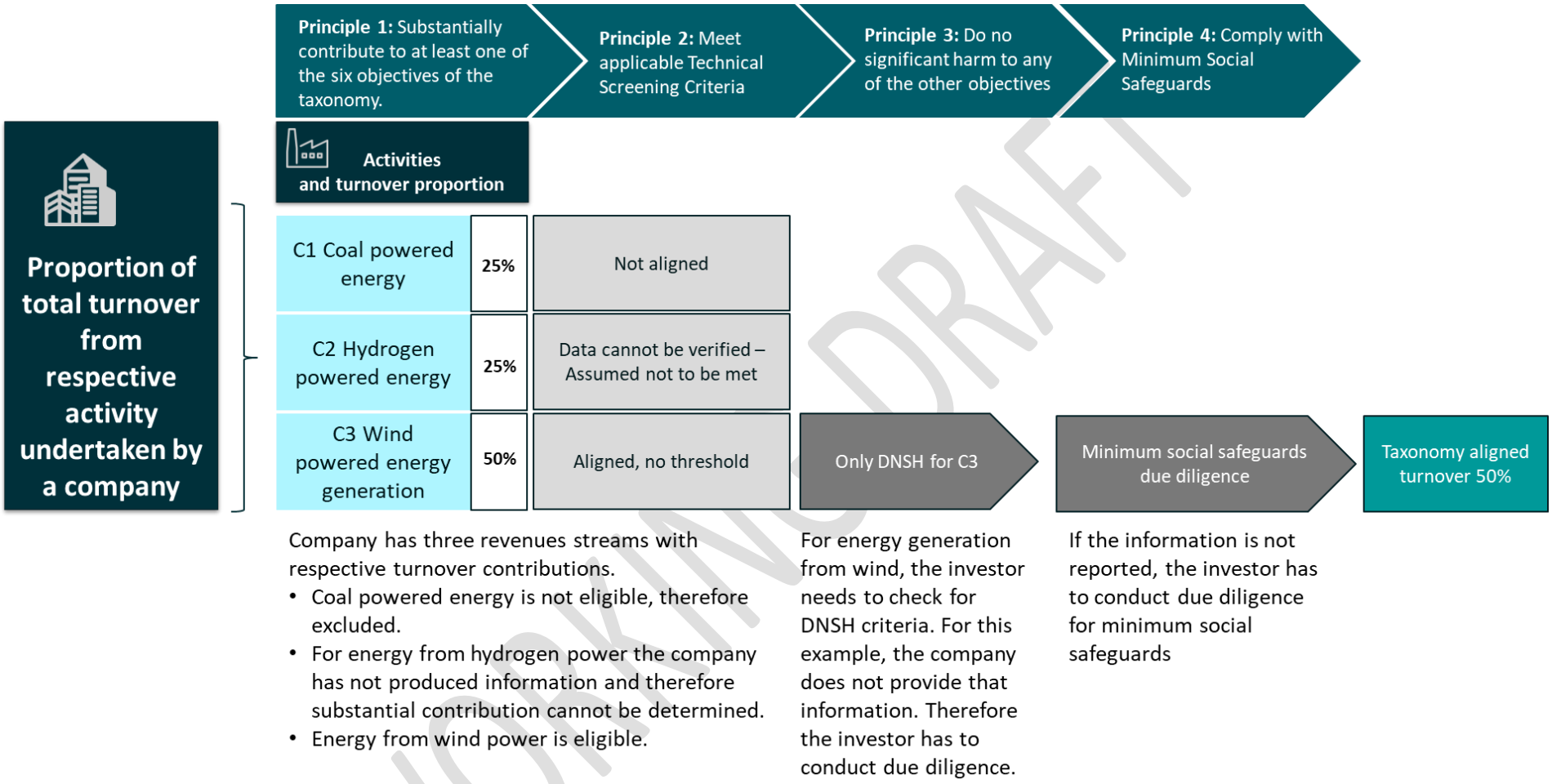


Figure 14: Five steps and example of how investment-level taxonomy-alignment of company turnover may be determined (EU Technical Expert Group on Sustainable Finance, 2020)

3.2.2 Proportion of funds with underlying Taxonomy-aligned constituents – equity investments

Company turnover is applied as the proxy for equity exposure to taxonomy-aligned economic activities in underlying investments.

Figure 15 demonstrates an example of company-level turnover combined with equity share enables computation of equity exposure in a fund to taxonomically-aligned economic activities.

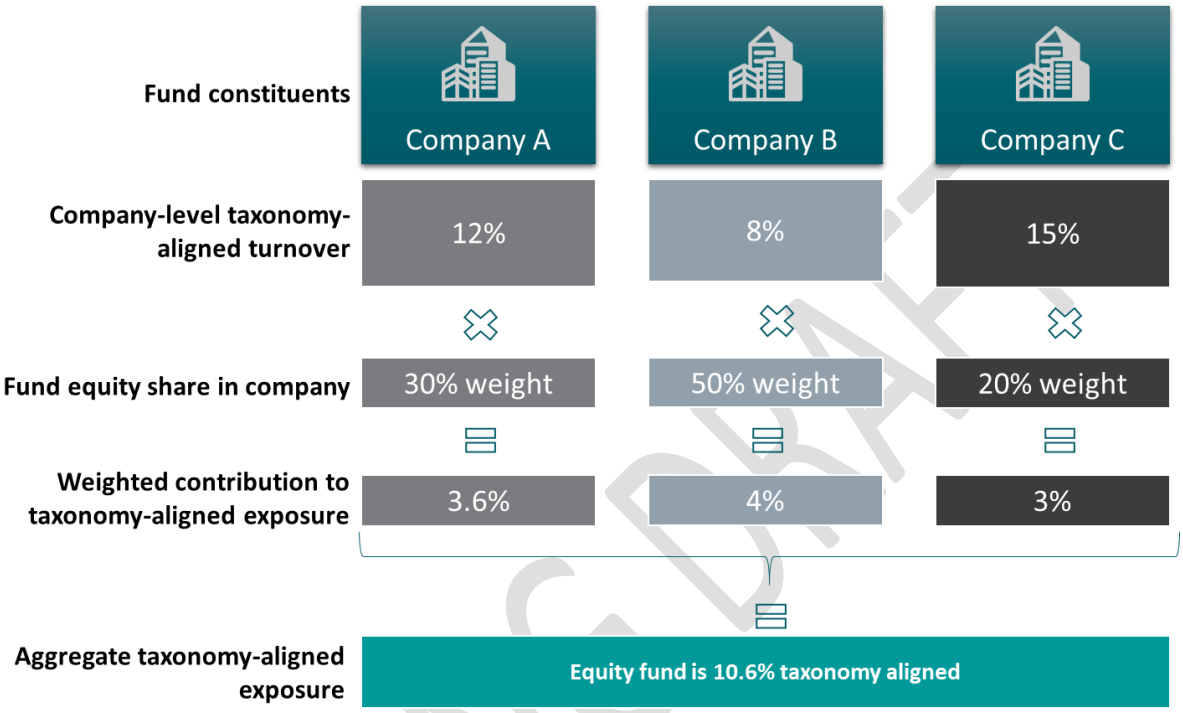


Figure 15: Application of the taxonomy to an equity portfolio from company level turnover and equity share (EU Technical Expert Group on Sustainable Finance, 2020)

While this computation relies on turnover, the EU Technical Expert Group notes that investors may wish to build a forward-looking portfolio and disclose the same information based on capex.

To be clear, taxonomy-alignment of a whole or part of a company requires determination of full-taxonomy alignment, including minimum social safeguards and climate resilience. It is possible that the investor is required to undertake due diligence to determine full taxonomy-alignment, if not disclosed by the investee.

3.2.3 Proportion of funds with underlying Taxonomy-aligned constituents – fixed income (debt) investments

The approach to computing taxonomy-alignment in a fixed income or debt fund takes into account the following:

- Accepted good practice concerning green bonds issuance requires transparency on and accountability regarding the Use of Proceeds. These requirements translate to the ability to determine and ensure taxonomy-alignment of investment to Green Bonds.
    - For the sake of the example, it is identified that 100% of the Green Bonds Use of Proceeds is for Issuer finance of eligible projects' capex or opex for economic activities that are taxonomy-aligned.

- It is possible that the taxonomy does not provide coverage for an economic activity that the Issuer specifies for the bonds Use of Proceeds, in which instance the percentage taxonomy-alignment should be adjusted.
- It is possible that a sustainability bond or similar is issued, and some portion of the Use of Proceeds is taxonomy-aligned environmentally focused projects, in which instance the percentage taxonomy-alignment should be adjusted.
- There is not a distinction made as to whether a green bond issuer is private sector or public sector, provided that the bonds Use of Proceeds is evident.
- It is proposed that the credentials of the bond should be verified as 'green'. Refer Section 3.2.4 Process to evaluate green bond and green loan taxonomy-alignment for further detail regarding green bonds.

- It is possible that a Corporate Issuer issues a vanilla bond and that an activity of the company is taxonomy-aligned. In this instance the computation for taxonomy-aligned turnover may be applied to determine the portion of the corporate bond that is taxonomy aligned. (Refer Section 3.2.1 Process to evaluate company-level turnover taxonomy-alignment.)
- Public sector bonds that are not distinctly identified and verified as green bonds are presently to be computed as zero% taxonomy-aligned contribution, while further work is undertaken to determine an internationally accepted approach. Options noted by the EU Technical Expert Group (March 2020) as under consideration include:
  - "Alignment of national climate change mitigation targets with net zero by 2050, potentially supported via Nationally Defined Contributions (NDCs).
  - The sectoral contribution of Taxonomy-aligned economic activities to national GDP.
  - The sectoral contribution of Taxonomy-aligned economic activities in the form of tax receipts."

  This is an area of potential update for the taxonomy in future.

To be clear, taxonomy-alignment of a whole or part of a debt based instrument requires determination of full-taxonomy alignment, including minimum social safeguards and climate resilience of the underlying constituents. At present, it is not an express requirement to demonstrate climate resilience or minimum social safeguards in order to be verified as a green instrument. It is possible that the investor is required to undertake due diligence to determine full taxonomy-alignment, if not disclosed by the issuer.

The example and detail above applies equally for other forms of green debt, such as green loans.

Disclosure should provide clarity on the distinctions of the fund constituents in terms of proportion of taxonomy-alignment and instrument details, including:

- What part is for verified green debt
- What part is for private sector and public sector debt

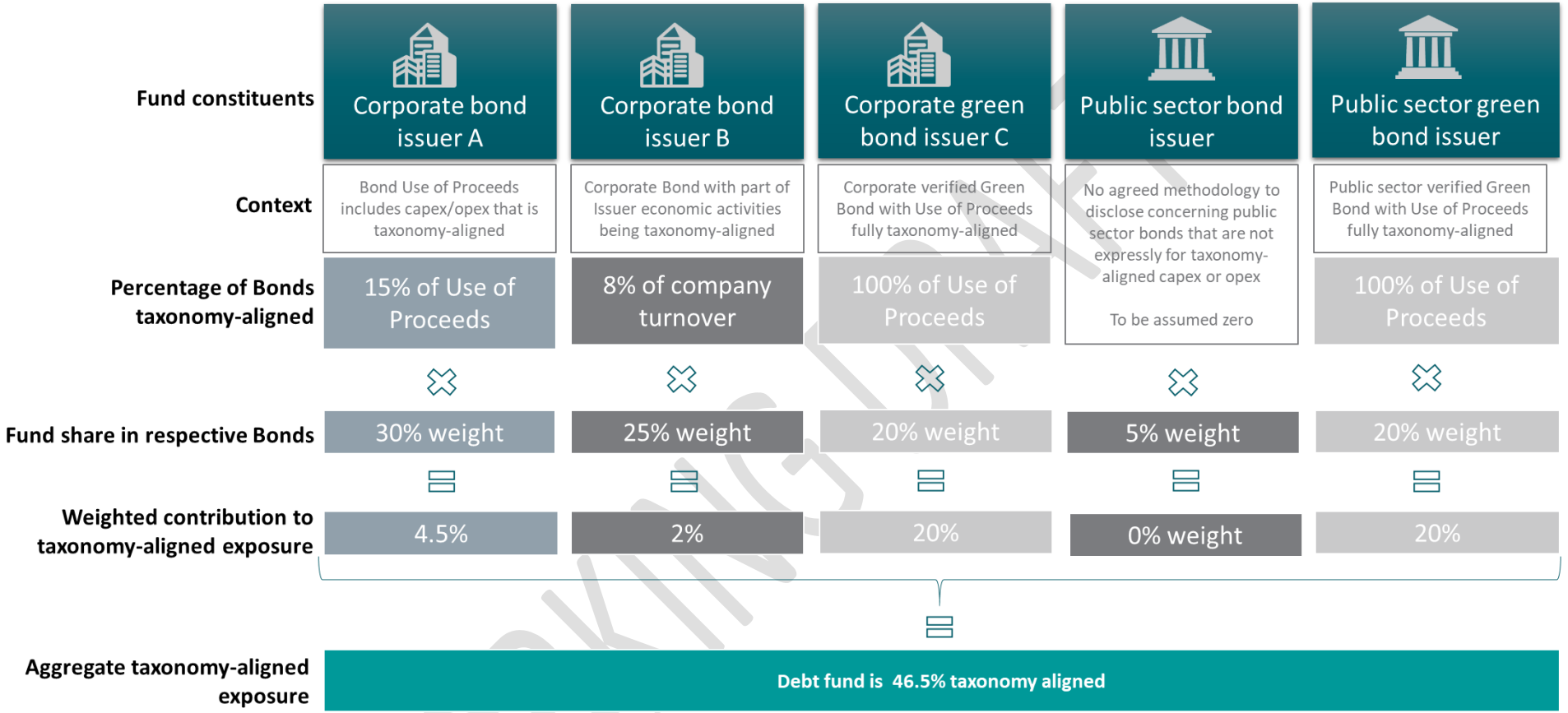


Figure 16: Application of the taxonomy to a debt or fixed income fund from instrument taxonomy-alignment and fund share

3.2.4 Process to evaluate green bond and green loan taxonomy-alignment

There is no present requirement for bond issuers or borrowers to disclose taxonomic-alignment, nor for investors or lenders/financiers. However, this information is expected to be useful to investors looking to understand the alignment for their investments and portfolio composition.

For both green bond issuers and green loan financiers, it is recommended that a process to verify the 'green credentials' of the respective transaction or offering is undertaken. Issuers and loan financiers may consider applying, as relevant for;

- Bonds
  - International Capital Market Association (ICMA) Green Bond Principles (GBP), as updated from time-to-time
  - ICMA Sustainability Bond Guidelines (SBG), as updated from time-to-time
  - ICMA Sustainability-Linked Bond Principles (SLBP), as updated from time-to-time;
- Loans
  - Joint issue by Loan Market Association (LMA), Loan Syndications and Trading Association (LSTA) and Asia Pacific Loan Market Association (APLMA) Green Loan Principles (GLP), as updated from time-to-time
  - Joint issue by Loan Market Association (LMA), Loan Syndications and Trading Association (LSTA) and Asia Pacific Loan Market Association (APLMA) Sustainability Linked Loan Principles (SLLP), as updated from time-to-time.

Other international credible frameworks and standards might also be applied, such as Climate Bond Initiative (CBI) Climate Bonds Standard, as updated from time-to-time.

These frameworks have similarities in expressed market requirements for best practice regarding the following processes, and it is recommended that issuers and loan financiers are aligned with respect:

- Use of Proceeds (refer Table 4 for further recommendations)
- Process for Project Evaluation and Selection (refer Table 4 for further recommendations)
- Management of Proceeds
- Reporting (refer Table 4 for further recommendations)
- Verification – external review and verification are recommended, regarding conformance to a respective framework, taxonomic-alignment and associated environmental and social impact performance (respectively before and after as well as on-going during the term of the instrument).

Table 4: Additional evaluation and disclosure recommendations concerning taxonomic-alignment for debt instruments

Actor	**Investor or Lender**	**Issuer or Borrower**
Considerations concerning Use of Proceeds	The investor or lender should undertake suitable due diligence concerning the transaction to assure themselves of taxonomic-alignment of the underlying economic activity, project or asset	• In order to be taxonomy-aligned as a debt instrument (loan or bonds), the selection of projects should be done using this taxonomy. • Where only a proportion of the bond or loan is taxonomically-aligned, this should be disclosed (both the details of the taxonomically-aligned economic activities and the related finance portion)
Considerations concerning Process Evaluation	The investor or lender should undertake suitable due diligence concerning the transaction with regards the taxonomic-alignment evaluation process,	• The issuer or borrower should apply the taxonomy as detailed in Section 2 for each constituent project, asset or activity relevant to the transaction, to determine taxonomic-alignment

	the associated and the environmental and social impact performance specified.	• The issuer or borrower should clearly inform investors or lenders (respectively) of: o the evaluation process and the assessments to identify and manage potentially significant environmental risks o the taxonomic-alignment result o the associated environmental and social impact performance
Considerations concerning Reporting	• A specific reporting process should outline qualitative and quantitative information about the Use of Proceeds. The key disclosure will be the percentage of expenditures in taxonomically-aligned economic activities – in other words, the percentage of a loan or bonds allocated to taxonomically-aligned projects or assets. • Taxonomic-alignment evaluation should be undertaken ahead of the transaction (ex-ante reporting) and regularly during the term of the loan or bond (ex-post). Green default must be reported to lenders and investors by borrowers and issuers (as relevant) timeously, and proportion of taxonomic-alignment of the transaction must be adjusted. • Regular ex-post reporting of environmental and social impact performance should be incorporated into disclosure.	

The guidance and recommendations of this section are intended to complement any specific requirements expressed by capital markets, regulators and applicable ESG frameworks or commitments, as relevant to products, transactions and participants.

4. Sustainable development performance and impact reporting

In the first instance, taxonomically-aligned economic activities will make a significant contribution to at least one environmental objective. It may also be that a taxonomically-aligned economic activity makes significant contribution to more than one environmental objective and has co-benefits and contributions in terms of multiple sustainable development dimensions.

In addition to disclosure concerning taxonomic-alignment and related finance, reporting on environmental, social and governance performance and impacts of taxonomically-aligned activities is anticipated to provide distinctly useful information to an array of interested stakeholders.

It is **also the intention of this taxonomy to encourage transparency through disclosure, and especially disclosure concerning social impact performance of taxonomically aligned activities**.

This document does not undertake to provide harmonised specification for environmental and social performance and impact indicators that should be disclosed alongside disclosure of taxonomic-alignment and related finance.

However, there are a number of developments referenced and reporters are encouraged to consult these resources to identify material impact indicators. These include the following as inexhaustive options, acknowledging also that different taxonomy users may have different requirements concerning activity-level, company-level and economy-level reporting objectives:

- International Capital Market Association, April 2020 (or as updated) *Harmonized Framework for Impact Reporting* [Online] Available at https://www.icmagroup.org/green-social-and-sustainability-bonds/impact-reporting/
- International Capital Market Association, June 2020 (or as updated) *Social Bonds Working Towards a Harmonized Framework for Impact Reporting* [Online] Available at https://www.icmagroup.org/green-social-and-sustainability-bonds/impact-reporting/
- International Capital Market Association, June 2020 (or as updated) *Green, Social and Sustainability Bonds: A High -Level Mapping to the Sustainable Development Goals* [Online] Available at *https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/June-2020/Mapping-SDGs-to-Green-Social-and-Sustainability-Bonds-2020-June-2020-090620.pdf*
- World Economic Forum (WEF) September 2020 Measuring Stakeholder Capitalism Towards Common Metrics and Consistent Reporting of Sustainable Value Creation, White Paper [Online] Available at http://www3.weforum.org/docs/WEF_IBC_Measuring_Stakeholder_Capitalism_Report_2020.pdf
- Global Reporting Initiative (GRI) Standards, Various [Online] Available at https://www.globalreporting.org/how-to-use-the-gri-standards/resource-center/
- Sustainability Accounting Standards Board (SASB) Materiality Map [Online] Available at https://materiality.sasb.org/
- United Nations Department of Economic and Social Affairs Statistics Division, March 2020 *Global indicator framework for the Sustainable Development Goals and targets of the 2030 Agenda for Sustainable Development* [Online] Available at https://unstats.un.org/sdgs/indicators/indicators-list

There is a wealth of impact analysis tools and frameworks available from different organisations including United Nations Environment Programme Finance Initiative (UNEP FI) and World Business Council for Sustainable Development (WBCSD) amongst others to guide individual project impact evaluation if needed.

Suitable tools and indicator listings should be consulted and further determination undertaken by the taxonomy user to identify the material impact indicators appropriate to be reported regarding the asset, project or activity.

5. General challenges and consideration in applying the Taxonomy

5.1 Taxonomy application challenges

A major challenge in the application of the Taxonomy is related to aligning the types of investment or finance to a specific economic activity as identified by the Taxonomy. Part of this challenge is attributed to unspecified use of proceeds. For example, general credit facilities in the form of general-purpose loans or revolving credit facilities cover diverse corporate expenditures and are not solely related to specific investments, making alignment with taxonomic economic activities challenging. An additional significant challenge is the availability of quality data and information to assess alignment with TSC of the taxonomy. Granular data to evidence alignment with TSC is typically not publicly available data and in many instances can be complex and thereby requires sustainability expertise to adequately assess alignment.

5.2 Taxonomy application considerations

When a client receives financing that spans multiple Taxonomy classification categories, allocating total exposure to sector(s) associated with the Taxonomy becomes difficult and it may not be possible to classify the whole client as taxonomy aligned. In such instances, it is advised to, as far as possible define investment, loan, credit facility or use of proceeds to a specific asset or to project level and thereby split the client's exposure across activities for the purpose of classification. Narrowing down the economic activities that are aligned to the Taxonomy at the beginning of the assessment would be beneficial. This may mean prioritising company activities based on materiality.

When investment, loan, credit facility or use of proceeds is not specified, classify exposure on the basis of clients' business activities. Identify the nature of the intended or existing contribution of the transaction/funds and decide into which Taxonomy category the transaction, activity or company falls. The Taxonomy offers the choice between economic activities which substantially contribute to climate change mitigation or climate change adaptation and acknowledges economic activities which contribute through own performance or as an enabling activity. This helps to provide a specific focus to the assessment and minimises the time needed to carry it out.

Below illustrate three general considerations when applying the taxonomy:

- At first, start simple, by selecting specific investments where quality granular data is readily available. To understand the exact scope of each activity to identify the most suitable match, test on a smaller portion of the investment portfolio or for activities for which KPIs are available/comparable with Taxonomy criteria. This way you will start to become familiar with how the Taxonomy works and gain confidence in applying it to bigger investments;
- The information required by the taxonomy can be complex and it may be useful to involve sustainability expertise to assisting in the interpretation and the assessment of the data. Take a bottom-up approach to fairly assess company alignment with the Taxonomy. Where data is not available or unreliable, adopt a precautionary approach and be clear on data limitations.
- In general, adaptation-related information is more difficult to find than mitigation- related information, as carbon emissions data now have a significant track record. Therefore, projects making substantial contribution to climate change mitigation are more likely to have the data needed to test alignment to the taxonomy.

Appendix A: Disclosure Template

Introduction *Short introductory paragraph on your organisation's perspective on Taxonomy implementation and why it is needed.*
Asset class covered:
Geography covered:
Sector covered:

Which aspects of the Taxonomy do you focus on?

☐ Climate Change Mitigation

☐ Climate change adaptation

☐ Both

Which economic activity do you consider?

☐ All

☐ Several specific activities: *please state*…….

☐ One specific activity: *please state* …….

Provide a description of the process, practice and/or methodology used to assess alignment to the taxonomy's technical screening criteria as outlined below

For substantial contribution to climate change mitigation or climate change adaptation or (both where relevant)	
For Do No Significant Harm Assessment	*Climate change mitigation:*

	Climate change adaptation:
	Sustainable use of water and marine resources:
	Ecosystem protection and restoration
	Pollution prevention:
	Sustainable resource use and circularity:

For Minimum Social Safeguards Assessment	
For proportion Turnover/Capex/Opex alignment with the Taxonomy	
Additional comments*:*	
Main results or outcome in terms of alignment with the Taxonomy	

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