

23 June 2022

ICMA Response to the second GFIT Taxonomy consultation paper

The International Capital Market Association (ICMA) welcomes the opportunity to provide feedback on the second GFIT Taxonomy consultation paper.

ICMA is a global membership association committed to serving the needs of its wide range of members. These include private and public sector issuers, financial intermediaries, asset managers and other investors, capital market infrastructure providers, central banks, law firms and others worldwide. ICMA currently has around 600 members active in all segments of international debt capital markets in 65 jurisdictions globally (www.icmagroup.org).

Through its work with the Green, Social and Sustainability-Linked Bond Principles, the globally recognised framework for issuance of sustainable bonds, and in its key advisory role in other sustainable finance initiatives (including the ASEAN Green and Social Bond Standards and the EU Platform on Sustainable Finance), ICMA is at the forefront of the financial industry's contribution to the development of sustainable finance.

We at ICMA would welcome any enquiries and opportunity to discuss further with GFIT and the MAS on any of the issues explained below. Please contact Mushtaq Kapasi, Managing Director, Chief Representative, Asia Pacific at Mushtaq.Kapasi@icmagroup.org.

In our response to the first consultation paper on a GFIT taxonomy, we drew on our paper [Overview and Recommendations for Sustainable Finance Taxonomies](#) published in May 2021 and commented on “measures of success”. We acknowledge and appreciate that the GFIT has taken them into account and suggest continuing to integrate our recommendations that taxonomies should be:

1. Targeted in their purpose and objectives.
2. Additional in relation to existing international frameworks.
3. Usable by the market for all intended purposes.
4. Open and compatible with complementary approaches and initiatives.
5. Transition-enabled incorporating trajectories and pathways.

Based on our experience with the EU Taxonomy, we would also like to bring to your attention the ICMA paper on the usability challenges and recommendations for the EU Taxonomy (<https://www.icmagroup.org/assets/documents/Sustainable-finance/ICMA-EU-Taxonomy-brochure.pdf>). The paper highlights a few important usability issues (summarised below) that may have relevance for other taxonomies outside the EU context. We suggest the GFIT and the MAS consider and reference the usability challenges identified for the EU Taxonomy to help facilitate a practical design and implementation of the Singapore Taxonomy. These usability challenges include:

- i. requirement for highly granular data for Technical Screening Criteria (TSC) purposes;
- ii. application of the taxonomy in extraterritorial markets for global investments;
- iii. inconsistency in the use of estimates and third-party data;
- iv. the need for proportional arrangements for smaller companies and projects;
- v. dynamic TSC for substantial contributions where the change over time gives rise to the need for grandfathering; and,
- vi. the use of an economic activity-based classification system (ISIC) for complex projects.

Please find our responses to the specific questions of the consultation paper below.

Question 1 – The Workstream seeks general feedback on the environmental objectives identified.

No response.

Question 2 – The workstream seeks general feedback on the sectors identified.

We acknowledge and welcome GFIT’s approach to prescribe green and amber thresholds for each sector (and where appropriate differentiate new projects and transitioning of existing infrastructure) when classifying an activity/project into green, amber and red categories. This approach may avoid the problems caused by what could be otherwise a binary design that builds on niche greenness thresholds that could reduce the taxonomy’s relevance for the current economy and transition.

We would also like to point out the classification result should not be automatically determined by the ISIC code of the sector or the economic activity, especially considering that the green and sustainability bond market functions with a project-based approach.

Question 3 – The Workstream seeks feedback on this proposed approach – ease of navigation and usability.

In our earlier response to the consultation of the EU Platform on Sustainable Finance on the extension of the EU Taxonomy (see [here](#), p.8), we highlighted both the potential advantages and disadvantages of an extended taxonomy including amber and red levels of performance. While we are supportive, there may be a risk that FIs may become reluctant to provide financing to companies in the red category, thus hindering capital to flow to where funding for transition is needed. This could possibly be alleviated with the introduction of other regulatory and supervision measures beyond the design of a taxonomy.

With respect to usability, we would like to recommend ICMA’s paper [Ensuring the usability of the EU Taxonomy](#) as a helpful reference for policymakers to develop and implement a taxonomy. It identifies challenges for the financial and corporate sector in providing information on the alignment of their activities with the EU Taxonomy. Several of the recommendations we make to the EU policy makers could also be relevant to the development and usability of the Singapore Taxonomy. Adjusting our recommendations to the Singapore context, these would be:

1. Allow flexibility on alignment with the Do No Significant Harm and Minimum Safeguards in all cases;
2. Enable Technical Screening Criteria adaptation to function both across ASEAN and internationally to facilitate international usability;
3. Allow estimates and third-party data based on a common methodology to assess Taxonomy alignment;
4. Simplify ISIC classification for complex green and sustainability projects; and
5. Grandfather the Taxonomy alignment of the legacy green bond market for regulatory reporting purposes.

We appreciate that the GFIT provides a step-by-step guide for Taxonomy assessment, which serves as a helpful reference to educate the market and enhance the usability of the taxonomy. To further facilitate the applicability and usability of the taxonomy, we would appreciate if the GFIT and the guide could address the following specific questions:

- Minimum Social Safeguard (MSS) requirement: The figure 3 on p.112 of the second consultation paper illustrates the assessment process but it does not appear to explain how the MSS requirement is applied in the process and affects the classification result. **We would like to seek clarification from GFIT whether “not meeting MSS requirements” would result in an activity being classified as red.**
- Monitoring and grandfathering for amber activities/projects:

- **As amber activities/projects are required to demonstrate that they are in the process of improvement and reach green criteria by the sunset date, is monitoring on amber activities/projects needed every year?**
- **Would an activity or project lose its amber status and fall into the red category, if it fails to meet declining thresholds in one particular year after the project started but before the sunset date?**

Question 4 – The Workstream seeks feedback on the level of ambition for each criterion, whether TSC are clear, usable, or any other alternative metrics, policies and documents should be used as reference?

ICMA as an association does not intend to comment on the ambition level of specific green/amber thresholds, but in general encourages consistency in taxonomies. ICMA welcomes that the proposed Singapore Taxonomy uses the same or equivalent metrics as the EU Taxonomy and considers the EU Taxonomy criteria as a first option for “green” criteria. This will greatly promote interoperability and consistency between the Singapore Taxonomy and other national and regional taxonomies. However, we note that the green thresholds proposed in the consultation paper seem to be static until 2035. Considering that the transitional activities under the EU Taxonomy are expected to tighten every 3 years, it will be important to international market participants to know whether the Singapore Taxonomy will follow and adjust the green thresholds along with the pace of the EU Taxonomy.

Question 5 – The Workstream seeks feedback on the proposed practice, including:

- a) the transition process from amber to green for economic activities**
- b) the aggregation of activities by category at a fund/portfolio level,**
- c) the requirements for disclosure from both companies and financial institutions, and**
- d) any other feedback on the proposals contained within this section.**

Our response to this question is focused on the User Guide included in the second consultation paper, and its implications for disclosure and the sustainable bond market.

Specifically, ICMA and our members are concerned about the application of the proposed Singapore Taxonomy on:

- Sustainable bonds – market standards and regulation:
 - Whether the use of the green criteria of the Singapore Taxonomy will be mandatory or voluntary for green bonds that are aligned with the ASEAN Green Bond Standards. If the application of a national/regional taxonomy is made mandatory, we recommend keeping the ASEAN Green Bond Standards as a voluntary label. This would allow issuers the flexibility to finance projects that are not yet covered by the proposed taxonomy but that would still be considered green by the international markets, using existing global standards for green bonds such as the Green Bond Principles.

- Whether labelled bonds aligned with the technical screening criteria (TSC) at the time of issuance will be grandfathered as “Taxonomy aligned” for the life of the bonds, while the criteria in the Taxonomy may be updated over time. A dynamic update of the Taxonomy is necessary and welcome, as it reflects the need to adjust the TSC to both technological and scientific developments, as well as to the economy’s actual progress towards its sustainability objectives. It creates, however, a problem for green and sustainability bonds that are either providing information on their Taxonomy alignment or are designed to be fully aligned with it. Changing TSCs potentially create a risk of “taxonomy downgrade” when new TSCs are released that could lead to potential related sell-offs by investors, market volatility and damage to the attractiveness and valuation of green and sustainability bonds. The remedy to this problem is to allow Taxonomy “grandfathering”. In other words, the Taxonomy information available at the time of the issuance of the bond would be considered and maintained for the life of the security.
 - How the bond market would evolve with and make use of the “amber” criteria in the proposed taxonomy. We suggest that the GFIT and the Singapore regulators exercise caution if they consider integrating the use of amber criteria into labelled bond regulations or standards. The ongoing, dynamically transitioning nature of the amber category and the need for demonstration of such improvement could work for issuer-level transition strategy and disclosure, but may pose a challenge for use-of-proceeds bonds, especially considering that the “amber” category will either migrate to green or fall into red by the sunset date. Having said that, the amber category could be a useful reference for issuers of a sustainability-linked bond or issuers disclosing their corporate-level transition strategy (e.g. applying the [Climate Transition Finance Handbook](#) published by ICMA in 2020). The current market understanding on best practices of transition themed bonds emphasises an issuer’s continuous efforts towards sustainability at entity-level, beyond a single bond instrument.
- Disclosure regulation:
- Whether the reporting by corporates and by financial institutions (FIs) on Taxonomy alignment and eligibility is mandatory or recommended. While the detailed DNSH criteria and Minimum Safeguard requirements are yet to be developed by GFIT, we at ICMA would like to refer to our experience with the EU Taxonomy and emphasise the challenge on data needed for assessing taxonomy alignment. Assessing alignment against taxonomy criteria and requirements requires granular data that in many cases may prove to be unavailable. Depending on the data requirements, it is also likely that the assessment of outstanding investments (e.g. legacy green bonds) could face data shortfalls. Besides, where the taxonomy criteria refer to and apply local legislation/certification without providing international equivalents, Singapore corporates and FIs may find it difficult to assess and classify their international exposures. FIs may encounter difficulties to obtain sufficient quality data to classify the elements of their portfolios. We suggest at the first phase allowing FIs to classify and report taxonomy eligibility/alignment on a voluntary or reasonable efforts basis.
 - When introducing requirements on corporate reporting and FI reporting, the authority should plan the sequencing so that requirements of corporate reporting should come into effect earlier than the requirements on reporting by FIs. It is an

important sequencing consideration to ensure sufficient data will be available to the financial institutions to meet their reporting obligations on taxonomy requirements. If financial institutions are asked to make mandatory disclosure first, they will be left in a vulnerable position, as they need to report against mandatory sustainability KPIs at either product or entity level but cannot rely on data published by issuers. Mandatory reporting requirements will accentuate this problem. It will make the reporting by FIs costly, less accurate and potentially leave asset managers exposed to litigation risk. The proposal on p.105 of the consultation paper that FIs start reporting on taxonomy alignment before companies are required to report on alignment with TSC will create challenges for FIs.

As per the feedback from our members, if regulations on FI reporting will be introduced, any announcement in advance on the reporting timeline, the period of data in scope for the first reporting timeline, any specific formats or templates to be used for such reporting would be very helpful for financial institutions to have sufficient time to plan and adapt their systems, policies and procedures of their lending and investment operations.

- If disclosure against Taxonomy alignment is made mandatory, we suggest that the reporting requirements integrate proportionality to avoid excessive assessment and implementation challenges by businesses and/or financial entities in the context of Taxonomy disclosures. Depending on how granularity of the criteria in the Taxonomy and data required to make such assessments, smaller companies and FIs, who may lack the in-house expertise and resources, may have to deal with implementation challenges and consequent costs and thus become particularly disadvantaged. Absence of a proportionality approach will also make it more expensive to assess smaller green projects, making market conditions unattractive and hindering further growth for green financings for SMEs. Thresholds for company, project or investment size may be introduced to factor in proportionality. Context of operations, severity of adverse impacts and risk profile are also relevant considerations.
- We recommend grandfathering legacy green and sustainability bonds in FIs' portfolios for taxonomy alignment. It is common in the green bond market that reporting of allocation and impact is made on a portfolio basis and in an aggregated manner, and thus breakdowns per project type or technology do not easily allow a line-by-line Substantial Contribution (SC) assessment. Also, it may not be feasible to satisfy some of the SC TSC retrospectively. As sufficiently granular information to assess the Taxonomy alignment for these legacy green and sustainability securities will not be available, we recommend that a method be agreed to grandfather them. This can be achieved by: Either recognising the degree of Taxonomy alignment of legacy green and sustainability bonds in a wholesale manner, or by providing or endorsing a flexible and common methodology for the purposes of FI reporting.