

9 March 2021

## Proposals for recognition of transition finance in the EU legislation

### Key points:

- ◆ Despite the attempts to recognize certain transition efforts in the EU Taxonomy, these are not sufficient to support the EU objective to promote the transition of the whole economy. The EU Taxonomy leaves as “non-aligned” a vast majority of the EU economy, **without differentiating between activities/companies that have a credible transitioning path, from other** that have not yet adapted their business strategies.
- ◆ As repeatedly affirmed by financial regulators, notably in the context of the Network for Greening the Financial Sector (NGFS), banks’ contribution to climate-related policies is to **finance the greening of the economy**, and not only the green economy.
- ◆ The EU Taxonomy must be **complemented by an approach which allows assessment of a company alignment with net zero 2050 objectives**. This requires adding to the current EU Taxonomy framework, which defines “what is green”, an additional, forward-looking dimension, defining “what is greening”.
- ◆ Financing for companies that are aligning their activities with the EU climate targets should be considered under the concept of “**transition financing**”. Some key sectors not covered in the EU Taxonomy framework or activities not covered yet should also be considered as “**transition aligned**”.
- ◆ There are **several options** to properly consider the transition in the EU framework. The following options should be considered cumulative or possibly also in combination of several options:

European Banking Federation aisbl

Brussels / Avenue des Arts 56, 1000 Brussels, Belgium / +32 2 508 3711 / info@ebf.eu  
Frankfurt / Weißfrauenstraße 12-16, 60311 Frankfurt, Germany  
EU Transparency Register / ID number: 4722660838-23

  
www.ebf.eu

- ◆ 1) **Extend the current 5-years CAPEX to 10 years**, and tailor it as a function of activities while still comparing with 2050 taxonomy thresholds
  - ◆ 2) When looking at a 5/10y CAPEX programme, **comparing this target with new thresholds calibrated at the 2030 horizon, as an intermediate target**, aligned with the -55% objective set by the Commission by 2030
  - ◆ 3) **Include a reference to 2050 business alignment commitment, according to a methodology duly validated by a third party recognized entity including at company level**
- ◆ Finally, a **simplified and proportional approach** to the EU Taxonomy should be introduced for SMEs.

## Recognition of transition finance in the EU legislation

### 1. General comments

European banks welcome the “Call for Advice” of the European Commission to the Platform with the view of better incorporating the transition dimension in the EU Taxonomy (also referred further as taxonomy). Indeed, banks are committed to contributing to financing a sustainable economy, not only by financing green assets, but also by accompanying their clients in their transition towards a net zero emission economy; a considerable transformation, necessary, to achieve the goals of the Paris Agreement and the targets set by the EU.

Banks support their clients in the ESG transition by providing conditional sustainable financial products such as green bonds, green loans, sustainability-linked loans, social bonds/loans and various types of ESG improvement loans as well as transition plan related capital structuring & advisory services including to SMEs when relevant. Such ESG-related financing structures are becoming increasingly popular, as ESG awareness grows in the corporate, retail and investment universe. It is essential that this development be encouraged by the EU ESG regulatory framework, so that incentives for financial institutions be well aligned with the European and national investment plans to achieve such carbon-neutrality.

Under the current EU Taxonomy framework, investments are typically labelled as “taxonomy-aligned” when they are directed towards economic activities that **already make a substantial positive contribution** to one of the six environmental objectives, as required by the Taxonomy

regulation, while the taxonomy itself covers so far 2 of the six environmental objectives, climate mitigation and climate adaptation.

The EU Taxonomy has been designed to target activities and thresholds that are very demanding, to define “what is green” in a narrow sense, with a view of avoiding greenwashing. As a consequence, it leaves as “non-aligned” a vast majority of the EU (and global) economy, without differentiating between activities/companies that have a credible transitioning path, from other that have not yet adapted their business strategies.

As repeatedly affirmed by financial regulators, notably in the context of NGFS, the Network for **Greening** the Financial Sector, banks’ contribution to climate-related policies is to finance the **greening of the economy, and not only the green economy**.

Therefore, we support the enhancement of the EU Taxonomy by the creation of mechanisms that will incentivize investors and companies in the transition to sustainable and, in particular, low-carbon economy. Such mechanisms need to **acknowledge both the transition needs and the capacity and willingness of companies** that are at different stages of their transitional journey across sectors/geographies, and within sectors/geographies and recognize and support gradual improvements in companies’ climate metrics that are consistent with the ambition of the EU’s net zero emissions objective in 2050.

**While some economic sectors and activities need clearly to be singled out positively for their substantial contribution to sustainability objectives, the ambition of the EU will not be met without recognizing the achievements of firms, both financial and non-financial, in hard-to-abate economic sectors/activities that are successfully transitioning in line with the EU's ambition.**

Similarly, **within activities** currently addressed by the EU Taxonomy, the achievements of firms which are not meeting yet the ambitious thresholds set by the EU Taxonomy but have credible and binding corporate plans to adapt their business models over time, should be recognized. Indeed, those achievements may be the most effective in terms of **impact** -i.e., in terms **of potential of carbon emission reduction**.

This is particularly key, given that the majority of financing in support of the transition towards a more sustainable economy and society will have to be directed towards economic sectors and companies not currently classified as “environmentally sustainable” under the EU Taxonomy framework. As a recent paper by the Climate Bonds Initiative noted, *“green finance frameworks and capital flows have been principally directed at activities which can be considered ‘already green’. There has been significantly less investment into transitioning*

*activities and assets that are associated with the highest carbon emitting industries and businesses.”* Action is urgently needed on decarbonizing those sectors of the real economy that contribute to a large share of global emissions, such as heavy industry, manufacturing and agriculture. There is significant business model innovation taking place in such sectors, which is in urgent need of sustainable finance.

**Not sufficiently recognizing the transition efforts** of certain companies particularly in such high-emitting sectors would effectively lead to the market classifying them as “unsustainable”. This, in turn, might disincentive crucial investments in such “transition capable” companies and economic activities, and therefore slow down, rather than accelerate the transitioning of the EU economy toward net zero emissions.

Transition is fully endogenous to economic policy measures outside the scope of the EU Taxonomy (fiscal, regulatory, reforms of market mechanisms such as ETS, introduction of CBAM, ...) so flexibility and assessment of what could be considered “greening” in real time and depending on the economic policies framework is necessary.

Technology and its development is partly dependent on the above but it is also by definition an unknown that will alter the considerations on what could be considered sustainable but also how to transition to “green”. It can transform the scope of what is hard-to-abate and is the key differentiator between NGFS scenarios for example. Putting efforts into transition requires appropriate incentives.

**The transition must therefore also be supported by governments by** setting clear transition paths and **including fiscal measures such as carbon tax or phasing out fossil fuel subsidies as well as incentives for greening the economy.** This will allow banks to better support their clients to the transformation of the economy and thereby increasing the bankability of sustainable economic activities.

## 2. Recognition of transition efforts in the EU Taxonomy

The considerable work done by the TEG and now the EU Platform for Sustainable Finance should be underlined, and needs to be continued, including further operationalizing of the EU Taxonomy<sup>1</sup>.

---

<sup>1</sup> For recommendations on further enhancements of the EU Taxonomy application please see a joint EBF/UNEP FI report [Testing the application of the EU Taxonomy to core banking products: High level recommendations - EBF](#)

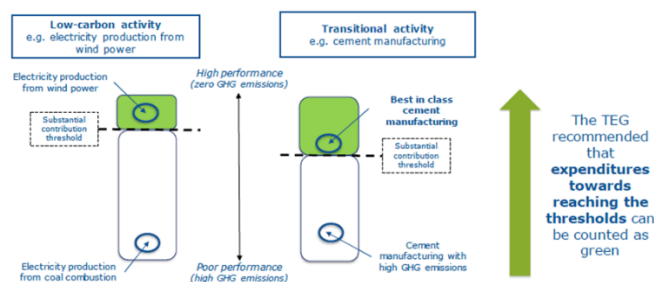
The EU Taxonomy covers about 70 activities representing 80% of carbon, emissions, but only 20% of the EU economy, and clearly its scope will be enlarged as the Platform continues its work.

Based on our understanding, the current EU Taxonomy framework addresses transition efforts in five ways:

i. **Recognising the best available level of performance for these industries**

- a. EBF view: These are referred to in the Taxonomy Regulation as “transitional” criteria. **However, these encompass only a very limited number of activities and should be extended to broader range of economic sectors.**

**Transitional activities - Illustration**



- b.
- ii. **Decreasing the thresholds for some activities from very low to zero** (e.g. car transport)

- a. EBF view: This approach **does not have the** potential to reflect the general question of the transition as the decrease of thresholds in 2025 does not address a long-term transition. In fact, what the private sector (financial and non-financial) describes generally as “transition”, is the fact that a company **may not be aligned on 2050 goals today** but is transitioning towards it. Instead, decreasing threshold over time, while meaningful as technology evolves, has the effect of excluding companies that may be taxonomy-aligned today, if they do not progress fast enough to adjust to the revised and more ambitious threshold to be set in 2025, irrespective of whether they may still be on track to align by 2050 or not.

iii. **Recognizing the investments in innovation.**

- a. Research, development and innovation financing, where it contributes to meeting or exceeding the criteria, can be counted as Taxonomy-aligned. This allows companies to get recognition for investing in the low-carbon solutions their industries need.
  - b. EBF view: while welcoming R&D, it generally represents a **rather small percentage of total expenses** (depending on the sector) and therefore is not sufficient to reflect the reorientation of the business models.
- iv. **Recognizing companies that are engaged in a maximum 5-year plan and trajectory of alignment with the taxonomy targets as “in transition” (strategy made public and validated by the administrative body).**
- a. For activities not meeting the TSC, the financing of improvement measures (Capex and, if relevant, Opex) can be counted as Taxonomy-aligned if they are part of an investment plan to meet the activity threshold over a defined time (TEG recommends a limit of five years for these plans).
  - b. A key role of banks is to discuss with companies their (potential) investment plans (to become low carbon), as well as the corresponding CO2 abatement curve for these investments.
  - c. In the case of climate change adaptation, the investment plan and associated abatement curve should directly respond to the climate risks identified in the assessment required by the adaptation principles.
  - d. The Technical Annex (Updated methodology & Updated Technical Screening Criteria) reflects this in the “principle” underlying many of the technical screening criteria, following a similar formulation: **“Mitigation measures are eligible provided they are incorporated into a single investment plan within a determined time frame that outlines how each of the measures in combination with others will in combination enable the activity to meet the threshold defined below actions”**.
  - e. EBF view: while this approach is welcome it **does not have the potential to mainstream the transition effort as it does not capture the full transitioning path by 2050**. In addition, **it only captures specific projects** which aim at converting an activity/infrastructure and **within a limited timeline**. In any case it would not capture general purpose loan since the capex could only be used in project finance (cf. EBA advice on article 8 of the taxonomy).

- v. **Enabling companies that help others by directly enabling other activities to make a substantial contribution to one or more of those objectives.**
  - a. The EU Taxonomy has also incorporated so-called “enabling activities”, which is one way of enlarging the taxonomy to some activities that are unavoidable during the transition period.
  - b. EBF view: such enabling activities may be further expanded, **however, this does not address the core issue of companies within a sector, that do not yet meet the taxonomy-alignment threshold** set for their activity(ies), but have credible alignment plans.

Despite the above-mentioned attempts to recognize certain transition efforts in the EU Taxonomy, this is not sufficient to support the EU objective to promote the transition of the whole economy.

### **3. Further recognition of transition finance – EBF proposals**

Recognizing improvement measures is a critical issue for corporate and financial users. In order to provide incentives to all companies to improve their environmental performance, the Taxonomy should not only recognize activities that already meet the criteria now or within five years, but also recognize efforts with the purpose of meeting those criteria over a longer period of time.

We have identified several **possibilities for adjustment to the EU Taxonomy framework** and related regulatory acts that could create more appropriate incentives in a practical way and recognize alignment of financial institutions’ portfolios with the goals of the Paris agreement.

**We believe that the EU Taxonomy must be complemented by an approach which will allow the assessment of a company alignment with net zero 2050 objectives. This requires adding to the current taxonomy framework, which defines “what is green”, an additional, forward-looking dimension, defining “what is greening”. In the rest of the document, we call this approach the “transition-aligned” approach.**

## EBF proposals in response to the Commission's questions to the Sustainable Finance Platform

*“Can the EU Taxonomy framework support finance for companies undertaking activities that do not yet meet, or may be unable to meet, the substantial contribution criteria? And how can this be done?”*

*“Can we clearly address the concerns that the taxonomy will be used to prevent financing of transitional activities, while at the same time ensuring that we are not facilitating “greenwashing”?”*

The way that the EU Taxonomy help support finance to companies undertaking activities that do not yet meet the TSC (R&D, CAPEX, enabling activities) is insufficient as it does not properly incorporate the notion of pathway.

We are not proposing to “water down” the current EU Taxonomy, which needs to be preserved in its capacity to define a science-based target consistent with the 2050 objectives. Relaxing taxonomy thresholds may indeed be detrimental to the credibility and usability of the taxonomy, as regards the trust of institutional and retail investors who want to ensure that (a proportion of) their assets is invested in already green assets. This is the main benefit of the taxonomy and it should not be compromised (unless science-based targets evolve over time).

Instead, we need to **add to the current taxonomy a complementary “transition approach”, to measure and incentivize the “greening” of the economy** and orientate the financial flows toward this greening objective. This is what we call **“transition alignment”**. What is essential on this additional “layer” is to avoid “greening -washing”. It should be made very transparent that **“greening assets”, by definition, are not yet green**. And it should be ensured that those assets are really “greening”. Please see our proposals below.

### Options to assess “transition-alignment”

**There are several options that could be considered to reflect transition finance in the EU Framework properly. The options developed below could be cumulative, as for**



example, the option 1 alone could not be sufficient at this stage (only some very specific project finance could be included). Combination of several options could also be considered.

- **Option 1: extend the current 5-year CAPEX to 10 years, and tailor it as a function of activities (while still comparing this 10-year plan with 2050 taxonomy thresholds).**
- **Option 2: when looking at a 5/10y CAPEX programme, comparing this target with new thresholds calibrated on the 2030 horizon, as an intermediate target, aligned with the -55% objective set by the Commission by 2030.**
- **Option 3: include a reference to 2050 business alignment commitment, according to a methodology duly validated by a third party recognized entity.**

### Option 1: Financing investment plans to achieve the TSC within 10 years or more in certain sectors

Transition activities currently captured in the taxonomy have strict starting thresholds and only those companies that are engaged in a maximum 5-year alignment trajectory with the taxonomy targets are considered “in transition” (strategy made public and validated by the administrative body). With its current static and sectoral approach, the taxonomy excludes economic activities with a decarbonization trajectory to reach the EU Taxonomy ‘green thresholds, based on sound Paris-aligned industry transition pathway on a longer term than five years.

Even the capex approach would only capture some specific projects which aim at converting an activity/infrastructure (general purpose loans are excluded). It is important to consider the timeline for implementation of those improvement measures. While five years may be appropriate as an indicative timeline, a more tailored approach on implementation timelines for investment plans is needed by corporate users of the Taxonomy. The timeline for investment plans ought to reflect the needs and complexities of the different types of investments or projects for different industries. A minor renovation plan would require a much shorter implementation timeline compared to a complete retrofit of several plants or the construction of a large infrastructure project.

An explicit recognition that would allow investors to classify “preparatory” investments as transition-aligned, if they can demonstrate credible and binding alignment over time with a substantial contribution to the Taxonomy as defined in the company’s longer term transition

strategy, would support investment in such activities. A trajectory approach would enable the mapping of the activities and corporates that **are in the pathway of 'greening'**. It could be envisaged under different modalities. A credibly demonstrated trajectory paths of e.g. 10 years should therefore be regarded as transition-aligned and the EU Taxonomy should reconsider the timeline-criteria, **with the possibility to deviate with clear objectives depending on the context of the sector.**

### Examples

- A) Long-distance deep-sea shipping (LDDSS) will continue to be needed throughout the transition period. Although greening solutions are already available for short sea coastal shipping and inland shipping, technology which allows LDDSS to reach net zero is not yet developed nor commercialized. Due to the long-term nature of investments in this sector (up to 25 years) transition paths will be needed which do not punish operators who use emission-reduction fuels such as gas, low sulphur marine fuel, or investments in technologies such as closed-loop scrubbers early in the transition period. The infrastructure which supports reduced emission LDDSS should likewise be considered.
- B) Small scale natural gas power plants may be needed in some markets to provide quick start cost-effective balancing of renewable networks and on-demand backup to renewables. These solutions will help quicken the take-up of renewables by ensuring a steady supply of electricity, building public confidence. While it is clear that these plants should not lock in use of natural gas and should eventually transition to green hydrogen beyond a certain date in net-zero 2050 scenarios, they are part of the solution and should not be unduly penalized early on in the transition period.
- C) Long-distance heavy-freight road transportation, fleets with moderate GHG emissions should also receive this label. The current taxonomy approach essentially excludes any transportation except electric and hydrogen – which are not yet commercially viable –, creating disincentives for companies that already want to work with existing technologies such as natural gas to reduce emissions, significantly, while creating a pathway to green hydrogen. The infrastructure which supports reduced emission long-distance heavy freight road transport and a pathway to green hydrogen should likewise be considered.

**While extending the Capex capture to 10 years instead of 5 would be a step in the right direction, it would still fall short of capturing the full horizon, and we would still compare a 10-year step with the 30-year target, which is not consistent.** Extending further the Capex is not necessarily realistic, depending on the sector, as companies do not typically plan specific Capex over more than 3 to 5 years, except in highly capital-intensive sectors. Hence this

approach needs to be complemented with other options. Therefore, while this approach would improve the framework it would not be sufficient on a standalone basis.

### Option 2: Intermediate thresholds at 2030 horizon

One approach could be to define **Intermediary milestones / thresholds** by economic activity for each [x] years period till the final target in 2050. These intermediary milestones / thresholds should be **consistent with EU climate law (2030/2050 reduction objectives) and could be based on recognized scenarios and sectorial standards**. The thresholds / milestones should be incorporated into a credible corporate transition plan and could evolve around:

- a) sectorial orientations of the national low carbon strategies
- b) PACTA
- c) IMPACT Measurement
- d) Commitments and reduction targets
- e) PCAF

Financing activities within these intermediary milestones/thresholds should also be considered” as **transitional activities”** within the current EU Taxonomy framework

### **Option 3: Recognizing full transition pathway of corporates at the 2050 horizon, duly validated by eligible third parties.**

In this scenario, the full transition pathway would be considered to determine whether the company is “transition-aligned”. Such a transition pathway should be made public and be duly validated by a third party. These third parties should submit their assessment methodologies to an EU standard setter (as is the case for ECAIs, who are subject to ESMA authorization), and their methodologies should respect agreed standards: science-based, aligned with the Paris Accord/Net Zero emission strategy/ EU and Member States plans.

The benefit of such an approach is that the KPIs used by those third parties in their transition pathway assessment may be more specific to each sector / company. This would create an alignment between the definition of “greening” in the taxonomy, and the KPIs typically used in sustainability-linked loans and other ESG related solutions.

It would also create an **alignment between the definition of “greening” and the specific pathways defined by Member States**, which could vary depending on their starting point.

All in all, it would provide a definition of greening that would reflect adequately the scope of investments needed to achieve the EU's ambition, and therefore would help channel funding to the right projects and companies.

The respect of the transition pathway by the corporate should be monitored closely by the **third-party evaluator**, and, in case the commitments are not met, the company would lose its "greening" status. This would **avoid any "greening washing"**, a very important aspect to foster trust and accountability.

**To complement the current focus of the EU Taxonomy** that is either on 'use of proceeds' investments or companies active in sectors already classified as "sustainable and to avoid that the remaining universe of companies, (whether they are on track to meeting EU Taxonomy thresholds over time or far off the mark) are effectively treated the same, i.e. "unsustainable", we believe an explicit recognition of investments in a credible transition path at company level should be considered. This will prevent negative incentives for crucial investments in economic activities and/or companies that are willing and able to support the transition to a low-carbon economy and society.

Financial products that create incentives for companies to reduce their emissions, but do not explicitly prescribe the way to do so are very useful in the transition and have a potential to impact, materially, the EU objectives of climate neutrality as they allow companies to innovate and choose their own paths in a most cost-efficient way. We believe that the primary determinant of whether a company is "green" or "sustainable" should shift from its primary industry sector to its "transition preparedness" or "transition capacity".

An explicit recognition of efforts in a credible transition path that would be consistent also with the DNSH principle and minimum social safeguards at company level should therefore be considered **complementary to the EU Taxonomy**. It should also be consistent with the "do no significant harm and minimum social safeguards". For example, a general purpose loan to a company where interest rates are linked to the CO2 performance at the levels required by a net-zero 2050 scenario would be classified as "**transition-aligned**". An added benefit of this recognition is that it could very easily be applied to sectors that are not yet developed in the draft delegated acts for climate change mitigation or adaptation, like textiles, etc. In banking activities this type of financing could be usually covered by a KPI-linked loan (also referred to as "sustainability-linked loan") where targets should be in line with EU climate targets (net zero by 2050).

**We are not proposing that “transition-aligned” means “EU Taxonomy-aligned”** as the EU Taxonomy is clearly defined for those activities that substantially contribute to environmental and social objectives. What **we propose is to consider the financing of companies that are aligning their activities with the EU climate targets under the concept of “transition financing”**. In summary, if all banking clients were performing in line with net zero pathways by 2050, banks would succeed in helping them to achieve EU climate targets.

This means that the EU sustainability framework would **formally recognize corporates’ decarbonization engagement in line with the Paris agreement** providing that some conditions are met:

- **KPI measuring the engagement would be in line with indicators used in the taxonomy** (e.g. Carbon intensity per unit of production for power, transport sectors);
- The decarbonation **trajectory should include intermediate targets** (until 2050) consistent with EU climate law (2030/2050 reduction objectives) and could be based on recognized scenarios and sectorial standards. This could take the form of (i) intermediate threshold or (ii) “reduction target” (EU objective of 55% reduction in 2030) in line with the low carbon plan developed by the EU member’s states and the review of EU sectorial regulation.
- The credibility and robustness of the corporate engagement should be subject to the adoption of recognized approaches. Such approaches should not only **define the targets** at corporate level, but also define / **evaluate realistic and ambitious decarbonation strategies and actions** of the corporates as well as **their alignment to the sectorial strategies consistently with the national decarbonation pathways and the Paris mitigation goals**.
- In order to avoid greenwashing, there must be a **requirement to provide evidence on how this KPI-linked funding contributes to the realization of the investment plan, and a requirement that a company cannot raise more sustainable funding than the amount of sustainable investments that they do (in a certain timeframe)**.

Companies should be encouraged to make their own emissions’ reduction engagement based on scientific targets, for instance through the adoption of objectives **aligned with science-based targets and robust governance**.

The approach based on a recognition of corporates’ decarbonation engagement could **complement the current EU Taxonomy framework** based on the activities. A formal EU recognition of such an approach (including through the use of such an approach as a formal indicator to report) would help investors and credit institutions to reorient capital flows

toward the companies that are effectively engaged into a transition pathway. The approach could be **labelled as “transition aligned financing/investment” and separated from the “taxonomy aligned”**.

***“Can the current EU Taxonomy framework support finance for companies active in sectors that are not covered in the Taxonomy Regulation’s Delegated Act?”***

### **Some key sectors not covered in the EU Taxonomy framework or activities not covered yet should be considered as transition aligned finance/investment.**

Economic activities in certain sectors are expected to be key in the transition to a low carbon economy, yet due to their exclusion from the current iteration of the EU Taxonomy there is no incentive to fund feasible technologies to improve them.

For some sectors, the adoption of a **“transition-critical sectors”** label may be useful and provide more certainty to investors. Two leading examples are gas power plants and heavy-freight transportation equipment.

Small scale natural gas power plants may be needed in some markets to provide cost-effective back up to renewables in substitution of coal plants. While these plants would not operate beyond a certain date in net-zero 2050 scenarios, and should not be used as an excuse to delay the transformation, they should not be unduly penalized in the transition period.

Because at this stage there is limited visibility on the most effective way to decarbonize heavy-freight transportation, fleets with moderate emissions should also receive this label. The current taxonomy approach essentially excludes any transportation but electric and hydrogen and bioethanol – which are not yet commercially viable –, creating disincentives for companies that already want to work with existing technologies that offer improvements on the margin.

In our interpretation, investments in the textile sector, for example, would only be covered to the extent that they can be considered under one of the headings that will be included in the initial versions of the draft Delegated Act (i.e. energy efficiency or renewables), and then with difficulties for documentation, etc. As previously mentioned, we believe the focus needs to be on company level activities and exposures.”

While we expect that the number of activities eligible for the taxonomy will expand over time, a quick way to cover these sectors would be to consider KPI (Key Performance Indicators)-linked loans as mentioned above. An EU standard for KPI or Sustainability-Linked loans and bonds is desirable in terms of transparency, of main characteristics to be respected, and in terms of KPIs for the measurements of the achieved results to avoid greenwashing. A requirement to provide evidence on how this funding contributes to the realization of the investment plan is recommended.

***“Can the current EU Taxonomy framework be used to provide greater support for attracting capital for the transition of companies towards “sustainable” activities, including in ways not yet proposed by the Commission and if so in which ways?”***

### A simplified approach in the EU Taxonomy for SMEs

Small and medium-sized enterprises (SMEs) represent 99% of all businesses<sup>2</sup> in the EU and their external financing is to a large extent dependent on banks. To meet the EU objectives of climate neutrality it is important to support SMEs in the transition. While the above consideration of transition finance could also benefit SMEs, we would suggest that the Platform of Sustainable Finance investigates whether a more proportionate and simplified framework could be envisaged for SMEs to incentivize their participation in the transition. We have been calling for an inclusion of the SMEs in the revised NFRD based on a simplified framework as we do believe a simplified framework could lead to material impact, given the large number of SMEs in Europe that could be discouraged from embarking on the transition journey if the criteria are too strict and considered unachievable in the short to medium term.

A simplified and proportional approach in the EU Taxonomy with alternative screening criteria could be applied to economic activities carried out by SMEs and micro-enterprises. The way to define proportionality would depend on the nature of the indicator in the screening criteria:

- a. quantitative indicators could be relaxed by a certain percentage;
- b. qualitative indicators could be adapted;
- c. specific high emission activities (for example fossil fuel exploration and production, oil, gas, coal that are not covered by the EU Tax) could fall within the regular criteria.

---

<sup>2</sup> [SME definition | Internal Market, Industry, Entrepreneurship and SMEs \(europa.eu\)](#)



## **It should be clearly disclosed when the economic activity of SMEs is aligned with the full EU Taxonomy or with the simplified EU Taxonomy for SMEs.**

To further facilitate the application of the EU Taxonomy for SMEs the following could be considered:

- a) It should be possible to adjust coefficient under the JRC methodology applied on a portfolio basis by maximum of 50 % depending on the outcome of banks' ESG due diligence of SMEs and assessment of portfolios.
- b) DNSH should either be proven, assumed for EU entities, or alternatively, public policy commitment could be published on the corporate website which includes the following three commitments at minimum: 1) net zero scope 1 & 2 GHG emissions by 2040 (i.e. accelerated and well ahead of Paris), 2) adherence to OECD Guidelines for MNEs, and 3) adherence to UNGPs.

These would substitute for further DNSH tests. European SMEs individually are not significant and if they cause harm it is not significant harm. They operate in a highly regulated economic market and collectively employ a lot of people. Policy commitments would embed responsible business conduct and serve as evidence that these companies are aware and acting to exceed core EU DNSH requirements. Policies are easy to implement and can be easily verified by Financial Institutions. This step would also fundamentally improve ESG across global value chains.

### **A simplified approach in the EU Taxonomy also for NON-SMEs**

In order to avoid nearly all activities not being qualified as EU Taxonomy compliant or transition aligned and to alleviate operational constraints, the **DNSH criteria need to be simplified and clearly aligned with the existing or to-be-revised sector specific EU Regulations** (so that extensive due diligence would not be needed in the assessment process), based on finalized methodologies and available data.

It should be ensured that DNSH and Minimum Social Safeguards' criteria are consistently reflected across all relevant laws governing the reporting of corporates and SMEs, in such a way that alignment with DNSH TSC can be expected for EU-based companies and assets (e.g. the activities run in Europe and for counterparts established in Europe).

**Credible remediation plans over a reasonable timeframe (i.e. 5 years) to meet the DNSH criteria should also be accepted in order to qualify the activity aligned with the EU Taxonomy.**



*“What further avenues could be explored to enable financing the transition through development of the taxonomy framework and beyond?”*

## Moving from a target to an impact

So far the taxonomy has focused on defining targets, and the current work on transition should expand it to include a new dimension, taking into account, according to various possible methodology options, the pathways towards the Net Zero economy.

There could be a totally different approach, building on scientific work by many NGOs, which would be to measure “impact”, i.e. measure the **reduction** in CO<sup>2</sup> emissions, and not only its absolute level. At the end of the day, what we are aiming at is to reduce the level of emissions from today to tomorrow.

The concept of “impact investing” has been built initially by philanthropy, emerging in 2007 and coined by the Rockefeller Foundation around this concept. Impact investing refers to investments "made into companies, organizations, and funds with the intention of generating a measurable, beneficial social or environmental impact alongside a financial return". Impact investments provide capital to address social and/or environmental issues, including but not limited to Climate. It could therefore be a relevant concept as the EU starts developing taxonomies on other ESG aspects, such as biodiversity and social.

Impact investors actively seek to place capital in businesses, non-profits, and funds in industries such as renewable energy, basic services including housing, healthcare, and education, micro-finance, and sustainable agriculture. Institutional investors, notably North American and European development finance institutions, pension funds and endowments have played a leading role in the development of impact investing.

Impact investing occurs across asset classes; for example, private equity/venture capital, debt, and fixed income. Impact investments can be made in either emerging or developed markets, and depending on the goals of the investors, can "target a range of returns from below-market to above-market rates". A commitment to measuring social and environmental performance, with the same rigour as that applied to financial performance, is a critical component of impact investing, which can also provide interesting reference for non-financial disclosure, including “ESG accounting” principles.

\*\*\*



### **About EBF**

The European Banking Federation is the voice of the European banking sector, uniting 32 national banking associations in Europe that together represent some 4,500 banks - large and small, wholesale and retail, local and international - employing about 2.1 million people. EBF members represent banks that make available loans to the European economy in excess of €20 trillion and that securely handle more than 300 million payment transactions per day. Launched in 1960, the EBF is committed to creating a single market for financial services in the European Union and to supporting policies that foster economic growth.

**[www.ebf.eu](http://www.ebf.eu) @EBFeu**

For more information contact:

**Name Surname**  
Function  
email@email.com  
+32 2 508 37 32