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# GFIT Progresses in Developing a Green Taxonomy for Singapore and ASEAN to Facilitate Sustainable Financing

## Introduction

ASEAN countries are highly vulnerable to climate change that is hastening the rising of sea levels and causing more extreme weather events which affect a majority of the ASEAN population that is dependent on fishing and agriculture activities for their livelihood. Singapore, being a low-lying island, is not spared. More capital and funding need to be directed to help businesses reduce carbon emissions to slow down climate change and to support the environmental objectives of Singapore and the ASEAN nations.

Therefore, in Singapore, the Green Finance Industry Taskforce ("**GFIT**") has proposed a Singapore Taxonomy for Singapore-based financial institutions ("**FIs**") with the key objective of encouraging more capital flows towards sustainable activities ("**GFIT Taxonomy**"). A taxonomy helps businesses and investors identify with greater certainty projects and investments that promote sustainability. This improves clarity and transparency in sustainable financing products, boosting investors' confidence.

GFIT consulted on the broad principles and approach for the GFIT Taxonomy in its first consultation paper issued in January 2021 ("**2021 Consultation Paper**").<sup>1</sup> GFIT introduced a traffic light approach to classify an economic activity as green, amber, or red, to differentiate an activity's contribution to one or more of the environmental objectives proposed by GFIT. The 2021 Consultation Paper also sought the views of FIs on, among other things, whether the GFIT Taxonomy would impose additional cost and compliance burden for them and whether businesses could cope with the disclosure requirements required under the GFIT Taxonomy. For more details, please refer to our Client Update on "[\*Sustainability Financing: Taxonomy Proposed for Singapore-based Financial Institutions to Identify "Green" Activities\*](#)".

Following broad-based support for a Singapore Taxonomy, GFIT is now consulting on the second version of the GFIT Taxonomy that has incorporated feedback received on the 2021 Consultation Paper and considered other significant developments in the sustainability space. The second version of the GFIT Taxonomy is set out in GFIT's second consultation paper issued on 12 May 2022 ("**2022 Consultation Paper**").<sup>2</sup>

<sup>1</sup> GFIT Consultation Paper on "*Identifying a Green Taxonomy and Relevant Standards for Singapore and ASEAN*", available [here](#) (on The Association of Banks in Singapore (ABS) website).

<sup>2</sup> Please click [here](#) to view the 2022 Consultation Paper (available on the ABS website).



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This Update provides an overview of the key proposals being consulted on in the 2022 Consultation Paper and highlights the new/revised aspects in the second version of the GFIT Taxonomy.

## Key Proposals in 2022 Consultation Paper

The 2022 Consultation Paper seeks comments on the following selected aspects of the GFIT Taxonomy. The consultation exercise for the 2022 Consultation Paper will end on 23 June 2022. GFIT will consult on other aspects of the GFIT Taxonomy in the later part of 2022, with an aim to finalise the full GFIT Taxonomy in 2023.

### Five Environmental Objectives

The purpose of environmental objectives in the GFIT Taxonomy is to define the types of activities to support the transition to a low-emissions and climate-resilient economy. For an activity to be considered environmentally sustainable, it has to contribute or meet one or more of the environmental objectives.

GFIT proposed that the GFIT Taxonomy covers green and transition activities for five environmental objectives: (1) climate change mitigation; (2) climate change adaptation; (3) protection of healthy ecosystems and biodiversity; (4) promotion of resource resilience and circular economy; (5) prevention and control of pollution.<sup>3</sup>

GFIT has revised the proposed environmental objectives set out in the 2021 Consultation Paper with reference to feedback received on the 2021 Consultation Paper, and the EU Taxonomy (a key reference document), which was then adapted given the local and regional policy contexts in Singapore and ASEAN.

- 1. Climate change mitigation.** This is a focal environmental objective for Singapore and the ASEAN nations as reflected in their nationally determined contributions (NDCs) under the Paris Agreement. An activity meets this objective if it substantially contributes to: (i) avoiding or reducing greenhouse gas ("GHG") emissions;<sup>4</sup> (ii) enabling activities that facilitate low carbon performance or substantial emissions reduction; and/or (iii) enabling activities that are engaged in transitioning to cleaner energies either through renewable power generating sources or via decarbonisation technologies.
- 2. Climate change adaptation.** An economic activity meets this objective if it fulfils one or both of the principles: (i) implements measures to increase its own resilience; and/or (ii) enables other economic activities to adapt to climate change. In addition, the economic activity should not adversely affect adaptation efforts by others, or increase the physical risks posed to others.

<sup>3</sup> In the 2021 Consultation Paper, GFIT proposed that the GFIT Taxonomy cover green and transition activities for four environmental objectives: (1) climate change mitigation; (2) climate change adaptation; (3) protection of biodiversity; (4) promotion of resource resilience. GFIT added promotion of circular economy and a fifth objective: prevention and control of pollution.

<sup>4</sup> Activities that avoid GHG emissions are considered "green" and have very low or near zero emissions. Activities that reduce GHG emissions are transition activities that are currently high carbon and critical to the functioning of the economy but are in transition to less carbon intensive business models.

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- 3. Protection of healthy ecosystem and biodiversity.** Ecosystem restoration is important in reducing the carbon load in the atmosphere, protecting water basins and supporting biodiversity. Ecosystem-based adaptation uses biodiversity and ecosystem services in an overall adaptation strategy. Examples of ecosystem-based adaptation activities include those which: (i) promote protection, restoration and sustainable use of coastal and marine environments that provide essential ecological, economic and social services in the ASEAN region; (ii) establish diverse agroforestry systems to cope with increased risk from changed climatic conditions; or (iii) conserve agrobiodiversity to provide specific gene pools for crop and livestock adaptation to climate change, etc.
- 4. Promotion of resource resilience and circular economy.** Activities that significantly promote resource resilience include those that aim to ensure the safe and secure supply of critical resources like food and water, and to overcome resource constraints by maximising resource productivity.

A circular economy seeks to reduce waste, recover resources at the end of a product's life, and channel them back into production. This is different from the traditional linear economy that follows the take, make, waste route. GFIT is of the view that promoting circular economy strategies will strengthen Singapore's resource resilience and promote environmental sustainability. It will also help Singapore become a regional financing hub for circular economy transition.

- 5. Prevention and control of pollution.** Activities that can contribute significantly to preventing and controlling pollution include activities that: (i) prevent, reduce and/or eliminate direct or indirect pollution of air, water or land; (ii) minimising risks or harmful effects on, or remediate or improve, the state of the environment; and/or (iii) enable the foregoing. In Singapore, due to the dense urban landscape, air pollution is of particular concern and the relevant Singapore governmental authorities have set air quality targets and implemented abatement measures to attain these targets.

In the second version of the GFIT Taxonomy, as a matter of priority, GFIT focuses on developing the criteria and thresholds for economic activities that contribute to addressing climate change mitigation. GFIT will consult on the details for other environmental objectives in the later part of 2022.

### "Do No Significant Harm"

In contributing to at least one of the environmental objectives under the GFIT Taxonomy, an activity should not cause any significant harm to any other environmental objectives - this is generally referred to as the "do no significant harm" ("**DNSH**") principle. In the second version of the GFIT Taxonomy, DNSH requirements are not included in the same way that are in the EU Taxonomy. GFIT recommends that the DNSH criteria should be linked to Singapore's environmental regulations relevant to climate change mitigation and other environmental objectives. For instance, GFIT proposed that the GFIT Taxonomy may include a clause that states that any breach of applicable environmental regulations

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means a non-alignment to the GFIT Taxonomy. GFIT will develop further criteria related to DNSH in subsequent versions of the GFIT Taxonomy.

#### **Eight Selected Sectors**

The GFIT Taxonomy aims to define which economic activities can be considered environmentally sustainable and over time, it has to cover all relevant parts of the economy. As such it is also important to establish a sector framework. GFIT selects eight sectors to be included in the GFIT Taxonomy based on two criteria: (i) contribution to climate change; and (ii) contribution to economic activity in Singapore and ASEAN. These sectors are either enablers or sectors that provide goods and services that allow climate change mitigation.

The eight sectors are: (1) agriculture and forestry/land use; (2) construction/real estate; (3) transportation and fuel; (4) energy (including upstream); (5) industrial; (6) information and communications technology; (7) waste/circular economy; and (8) carbon capture and sequestration. The GFIT Taxonomy retained the originally considered sectors, but the second version of the GFIT Taxonomy consults on the proposed activity-level criteria and thresholds for three of the eight identified sectors: (1) energy; (2) transport; and (3) real estate.

GFIT proposes to use a selection of Industrial Standard Industrial Classification (ISIC) codes within each of these three sectors. This selection is based on the importance to the Singapore and regional economies, the impact of each activity on GHG emissions (and emission reduction) as well as the ASEAN Taxonomy activity selection (which was also based on similar selection criteria pertaining to the region). The ISIC code is chosen due to its wide coverage and usage, thereby supporting one of the key principles underlying the GFIT Taxonomy, namely, interoperability with other taxonomies.

GFIT seeks feedback on the selected sectors, GFIT's approach and data used in identifying the sectors (and sub-sectors). Details are set out in the 2022 Consultation Paper.

#### **Further Details on Traffic Light Classification System for Activities in Energy, Transport and Real Estate Addressing Climate Change Mitigation**

In the 2022 Consultation Paper, GFIT elaborated on the traffic light classification system introduced in the 2021 Consultation Paper which is used to differentiate the impact of an activity on the environment. GFIT focussed on developing more detailed criteria and thresholds for Singapore-based activities based on Singapore's specific decarbonisation pathway for the three focus sectors (energy, transport, real estate) that contribute to one of the environmental objectives (climate change mitigation). In subsequent versions, GFIT will develop the activity-level criteria and thresholds for the remaining sectors and the remaining environmental objectives, and may include activities in other countries.

To be considered aligned with the GFIT Taxonomy, economic activities must meet the technical screening criteria ("TSCs") under each classification which specify requirements for substantial

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contribution to at least one environmental objective and DNSH requirement to other environmental objectives. Under the traffic light classification system, activities classified as:

- **"Green" are those that substantially contribute to climate change mitigation** by operating at net zero, or are on a pathway to net zero by 2050.
- **"Amber" for activities in "transition", i.e. the activities are not currently on a net zero pathway but are either transitioning towards green within a certain time frame, or facilitating significant emissions reductions in the short term.** This means that activities classified as "amber" must show progress or improvement towards green. GFIT highlighted that for certain activities, there will be no amber threshold. This could be due to a few reasons, such as it is not relevant as the technology meets the green threshold, or that the activity covers new assets which have to comply with the green threshold.
- **"Red" are those that are "harmful" and currently incompatible with a net zero trajectory**, and therefore should either be phased out if emissions cannot be reduced or there must be reduction in emissions to be in line with a green transition pathway. GFIT highlighted that not all activities have been assessed, i.e. activities that are not assessed does not necessarily mean they are "red" but that these activities are not yet part of the GFIT Taxonomy.

The 2022 Consultation Paper sets out in detail, among others, GFIT's proposed approach in coming up with the activity thresholds and choice of metrics for each of the three focus sectors (and sub-sectors). In particular, GFIT seeks feedback on the ease of navigation and useability of the proposed approach, and among others, the level of ambition for each criterion, whether the TSCs are clear and/or whether other alternative metrics, policies and documents should be used as reference.

### Practical Application of GFIT Taxonomy and Disclosure Requirements on FIs and Companies

The 2022 Consultation Paper also contains a user guide providing detailed guidance on how to use and apply the GFIT Taxonomy, as well as proposed disclosure requirements on the users of the GFIT Taxonomy.

The primary users of the GFIT Taxonomy will be Singapore-based FIs that provide debt and/or equity capital to companies in ASEAN member states, with the main focus on Singapore. GFIT notes that the ultimate end users would be clients of the Singapore-based FIs (such as asset owners, wealth fund managers and retail investors). Secondary users will include companies, regulators, policymakers and other financial market participants that need to define green activities.

The user guide sets out proposed step-by-step guidance and practices on how FIs and companies can use and apply the GFIT Taxonomy, including, among other things, how to identify which investments/activities are eligible under the GFIT Taxonomy classifications, how to assess the alignment of their investments/activities with the GFIT Taxonomy, and how to report a company's revenue, capital expenditures and operating expenditures that are aligned with the GFIT criteria definitions of these key terms/concepts.

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On disclosures requirements under the GFIT Taxonomy, GFIT's key proposals include:

- **Reporting by Singapore-based FIs on the degree to which their investments, products, or range of transactions are aligned with the GFIT Taxonomy and the environmental objectives to which the investments and activities contribute to from 2023 onwards:** (i) Over the next one to three years, investors should report eligibility and alignment of their investments with the GFIT Taxonomy using the activity classification for eligibility and additional data, where available, for alignment; (ii) over the long term, investors should report both eligibility and alignment of their investments with the GFIT Taxonomy.
- **Reporting by companies of their revenues and/or expenditures that justifies the performance of economic activities it operates in:** GFIT considers an economic activity to be eligible under the GFIT Taxonomy if it is included in the technical annex; an economic activity is aligned with the GFIT Taxonomy if it can demonstrate substantial contribution to one or more of the environmental objectives and the DNSH requirements.

For details, please refer to Section 5 (Taxonomy in Practice) in the 2022 Consultation Paper.

GFIT seeks feedback on: (i) the details and practices proposed in the user guide, such as the transition process from amber to green for economic activities, the aggregation of activities by category at a fund/portfolio level; and (ii) proposed disclosure requirements on Singapore-based FIs and companies.

## Concluding Words

Feedback on the 2022 Consultation Paper may be submitted [here](#); responses by ABS member banks are to be provided through the [ABS Online Feedback Portal](#).

If you would like to discuss any matters raised in the 2022 Consultation Paper, please feel free to contact our team below.

In full support of the Singapore Government's efforts to champion green and sustainability practices in Singapore and the region, Rajah & Tann Singapore has a [Sustainability Practice](#) which comprises multi-disciplinary specialist teams who can advise you on the adaptation of your business to take into account sustainability and ESG (environmental, social and governance) issues.

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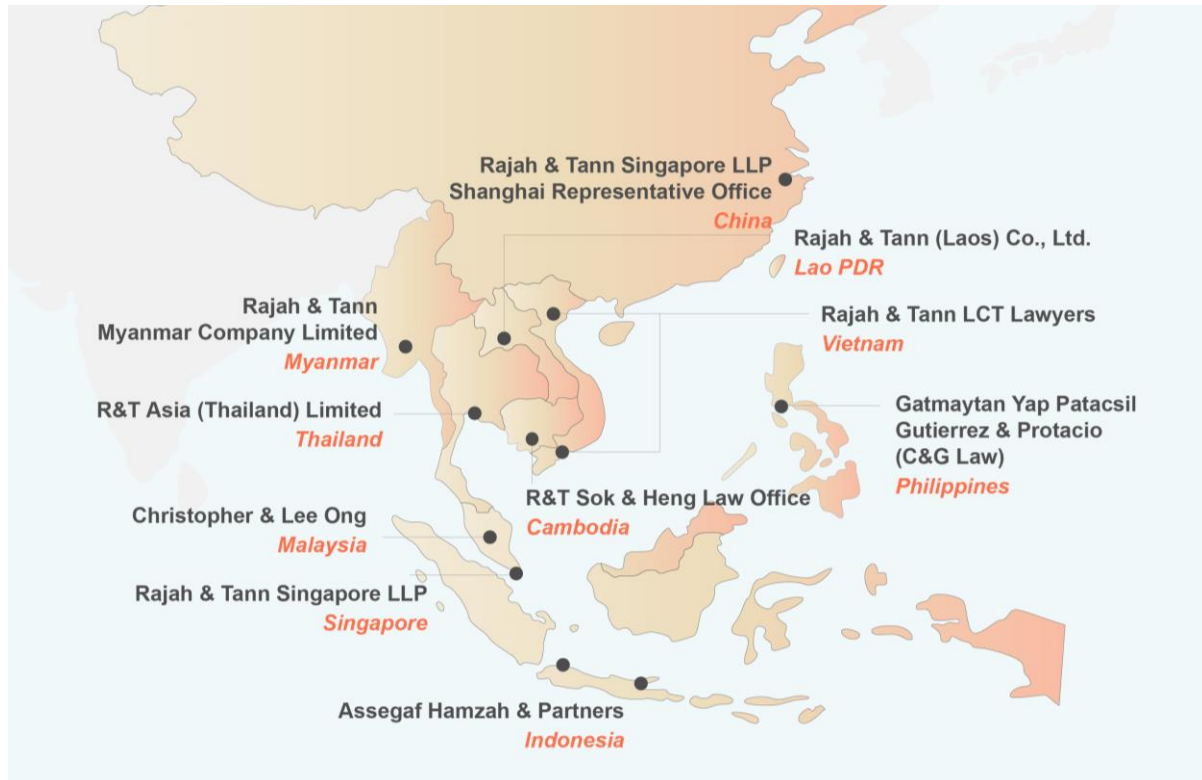
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