

IRSG UK Green Taxonomy Consultation Response

The IRSG welcomes the opportunity to respond to HMT's consultation on the value and use cases for a UK taxonomy, as part of the UK's wider sustainable finance framework.

The International Regulatory Strategy Group (IRSG) is a joint venture between TheCityUK and the City of London Corporation. Its remit is to provide a cross-sectoral voice to shape the development of a globally coherent regulatory framework that will facilitate open and competitive cross-border financial services. It is comprised of practitioners from the UK-based financial and related professional services industry who provide policy expertise and thought leadership across a broad range of regulatory issues.

Key points

1. **Sustainable finance ambition.** The government has an ambition for the UK to be the world leader in sustainable finance. The government must prioritise measures that will create the enabling conditions for the net zero transition in the real economy and facilitate an increase in sustainable investment. In this context, it is crucial for the government to consider whether proceeding with a UK taxonomy is necessary.
2. **Evolving landscape.** The sustainable finance landscape has evolved significantly since the initial commitment to introduce a UK taxonomy. The government must assess the cumulative impact of sustainable finance policy measures (in place and planned) on market participants and their relative prioritisation.
3. **Diversity of views on a UK taxonomy.** There is a diversity of opinion among IRSG members on the value of a UK taxonomy, within the wider context of government policy on sustainable finance.
 - a. The majority of members do not see a taxonomy as distinctly valuable for achieving the government's stated goals and consider existing regulations and new policy measures to be more effective and important to supporting the UK's net zero transition and unlocking sustainable investment in the real economy.
 - b. A minority of members consider there to be value in a UK taxonomy that is voluntary, proportionate and learns from EU experience, whilst maintaining interoperability.
4. **Key design principles for a UK taxonomy.** Should the government decide to proceed with a UK taxonomy, key considerations include:
 - a. **Interoperability.** With a multitude of taxonomies in development or implementation across the globe, interoperability will be a critical consideration.
 - b. **Alignment with the EU.** Many companies already comply with the EU Taxonomy. Alignment with the EU Taxonomy would embed a baseline of interoperability. However, the UK must learn from the EU experience and incorporate best practices from other jurisdictions.
 - c. **UK context.** A UK taxonomy must be aligned to the UK's transition pathway to net zero and be created in collaboration with sectors from across the economy to ensure cross-sector buy-in and effectiveness as part of the UK's sustainable finance framework.

UK Taxonomy and the Sustainable Finance Policy Landscape

The government has an ambition for the UK to be the world leader in sustainable finance and economic growth is the government's number one mission. It will be important for the government to consider whether proceeding with a UK taxonomy is necessary for the UK to become a world-leading destination for sustainable finance. Alongside this, the government must assess whether introducing a UK taxonomy would maintain and enhance the UK's position as an internationally competitive and attractive destination for companies to invest and do business, which has a fundamental role to play in delivering sustainable economic growth.

It has been four years since the original commitment to introduce a UK taxonomy was made. Since then, sustainable finance regulations have been introduced to the UK market (e.g. FCA anti-greenwashing rule) and the sustainable finance policy landscape has evolved both domestically and across other jurisdictions. For example, the development and adoption of the International Sustainability Standards Board (ISSB) standards, the publication of the Transition Plan Taskforce (TPT) disclosure framework and the introduction of the EU's sustainability reporting and due diligence framework.

The government must prioritise measures that will create the enabling conditions for the net zero transition in the real economy and facilitate an increase in sustainable investment. Priority measures for the government to progress include UK endorsement and implementation of ISSB standards, transition plans, and implementation of the recommendations of the Transition Finance Market Review (TFMR). Alongside this, the government must provide clarity on the industrial strategy and next steps for the National Wealth Fund.

In the Financial Services Growth and Competitiveness Strategy call for evidence, HMT outlines that on sustainable finance "the government's long-term vision is for a streamlined regulatory regime and effective policy framework, that supports innovation and fosters growth of the new markets that will be needed to support the domestic and global transition."¹ The government has committed to introducing a series of sustainable finance measures (such as sustainability reporting standards and transition plans) alongside those already introduced (e.g. the FCA's Sustainability Disclosure Requirements (SDR) and anti-greenwashing rule). The government must assess the cumulative impact of these measures on market participants and their relative prioritisation. This is necessary to identify which measures are most important for the UK at present to support the domestic and global transition to net zero and foster innovation and growth across the UK economy.

¹ HMT, 'Financial Services Growth & Competitiveness Strategy Call for Evidence', see page 25, available at: https://assets.publishing.service.gov.uk/media/6735f4670b168c11ea82311d/Financial_Services_Growth_Competitiveness_Strategy_-_Call_for_Evidence_.pdf

Chapter 2: Assessing Taxonomy Use Cases

- 1. To what extent, within the wider context of government policy, including sustainability disclosures, transition planning, transition finance and market practices, is a UK taxonomy distinctly valuable in supporting the goals of channelling capital and preventing greenwashing?**
 - a. Are there other existing or alternative government policies which would better meet these objectives or the needs of stakeholders?**
 - b. How can activity-level standards or data support decision making and complement other government sustainable finance policies and the use of entity-level data (e.g. as provided by ISSB disclosures or transition plans)?**

To facilitate sustainable investment and mobilise capital into sectors critical for the transition, the government must prioritise measures that create the enabling conditions in the real economy. Last year, the government sponsored the TFMR to examine how the UK, as a global financial hub, could lead in developing norms and practices for transition finance that facilitate an economy-wide shift towards sustainability. We encourage the government to prioritise driving forward policy measures to create favourable conditions in the real economy for sustainable and transition investments, including the recommendations of the TFMR.

When considering a UK taxonomy within the context of existing and alternative government policy on sustainable finance, there is a diversity of opinion across IRSG members on its distinct value. The two opposing positions from IRSG members are set out below.

Position 1. A UK taxonomy would not be distinctly valuable in supporting the government's stated goals

The majority of members do not identify a pressing need for a UK taxonomy and do not consider that it will be distinctly valuable in supporting the government's stated objectives of channelling capital and preventing greenwashing. A combination of existing regulations and new policy measures are identified to be more valuable in supporting the government to meet these aims, such as:

- **FCA anti-greenwashing rule.** The anti-greenwashing rule has created a principle-based approach to prevent companies from greenwashing.
- **Industry-wide classification systems.** Financial institutions already use the Climate Bonds Initiative (CBI), ICMA's Green Bond Principles, the FCA's SDR, the Sustainable Finance Disclosure Regulation (SFDR) and the EU Taxonomy for products and activities.
- **Reporting requirements.** Detailed sustainability disclosures under the UK's Sustainability Reporting Standards (SRS) (aligned with ISSB standards) and the EU's Corporate Sustainability Reporting Directive (CSRD) will improve the availability of sustainability-related information, as well as detailed information on companies' impacts and activities.

- **Transition plans.** The TPT disclosure framework has provided a framework to help companies articulate how they will achieve sustainability objectives and adapt to the net zero transition.

These members do not consider a UK taxonomy to be a necessary and additive measure alongside the other tools and frameworks now in place or planned – such as the anti-greenwashing rule, transition plans and ISSB standards – and the benefits of a taxonomy are not identified to be commensurate with the costs.

There is also concern that introducing a UK taxonomy could promote ‘tick box’ decision-making and undermine the more nuanced judgements that the work of transition plans and climate scenario analysis encourage. For example, as a tool for the government to design incentive schemes, direct public investment towards critical sectors or activities, or identify opportunities to partner with the private sector, a static classification framework could impede action should new technologies become available, or different priorities take precedence.

According to the Green Taxonomy Advisory Group (GTAG), as of 2023 there were 47 taxonomies in development or implementation across the globe. Diverging taxonomies risk market fragmentation and increased transaction costs and could lead to potential greenwashing claims. The introduction of a UK taxonomy has the potential to add to an already fragmented landscape and increase the reporting burden for business. In the absence of any equivalence regime or mutual recognition, many UK companies are likely to default to the EU Taxonomy, which they already comply with. Therefore, it is questioned whether any additional value would be created by the introduction of another taxonomy in the UK.

Furthermore, a UK taxonomy will not cover the majority of economic activities, as they are generally focused on identifying ‘green’ activities. Most corporate financing is provided via general purpose financing and revolving credit facilities, which is not readily accommodated in a taxonomy. In addition, in most taxonomies, SMEs, rightly, are excluded as they do not have the resources to analyse and report on sustainable activities. Therefore, it is likely that a UK taxonomy would not capture a significant portion of the economy.

Whilst a taxonomy can provide clarity on what types of activities are sustainable, without clear government policies, the majority of members do not consider that a taxonomy will in and of itself drive sustainable economic growth or encourage greater capital flows into sustainable activities. These members consider the government should prioritise the development of policy measures that will support an effective real economy transition and the commitments announced at Mansion House on ISSB standards and transition plans. Progress in these areas would be more effective in meeting the government’s stated objectives and better support the financial and related professional services industry in the transition to net zero.

Position 2. A UK taxonomy would be distinctly valuable in supporting the government’s stated goals

However, there is a minority of members who recognise the value and benefits of a UK taxonomy as part of a balanced sustainable finance framework, provided that it is designed effectively and

learns from the EU experience. These members consider that there is an opportunity for the UK to develop a taxonomy that offers improved functionality and usability and addresses the complexities and challenges of the EU Taxonomy, whilst also recognising the need for interoperability. Such a taxonomy could serve as a guiding framework to support sustainable finance initiatives and enable other sustainable finance regulations and policy measures to operate effectively.

A taxonomy is identified to be a useful tool in providing investors, companies and policymakers with a harmonised and uniform approach to identifying sustainable activities. Defining what activities are 'sustainable' and 'transitional' provides clarity and a common understanding to the market. This creates consistency and a more uniform approach to sustainable finance between and across sectors, allowing investors to make informed decisions regarding sustainable investments.

Furthermore, a minority of members consider that, without a clear taxonomy or policy tool from government that defines what is considered a 'sustainable' or 'transitional' activity, it will not be possible for other sustainable finance regulations and policy measures to operate effectively. A taxonomy would provide clarity from government on what is considered 'sustainable' and what is not. This would support existing regulatory and policy measures to function effectively. For example, a taxonomy could support companies with sustainability disclosures under the future UK SRS through providing a common understanding of which activities would be deemed 'sustainable' and would enable greater comparability of sustainability disclosures between and across sectors. A taxonomy could also support in assessing the credibility of transition plans and would enable a more effective comparison of a company's transition plan relative to peers in a particular sector.

A taxonomy is also valued for providing a richer picture of what is happening at an activity level. This enables investors to effectively compare across companies, supporting investor decision making. A taxonomy can also be a useful tool for providing clarity and guidance to companies on the most material risks to their sector, how to consider the impact on the business model, and how to manage their sustainability-related risks and opportunities.

A taxonomy could enable a harmonisation of sustainable financing frameworks across financial institutions. This would streamline requirements for corporates. Instead of having to comply with varying criteria from different institutions, they could adhere to a single set of principles. This would make it easier for companies to secure financing and reduce transaction costs.

A minority of members consider that a UK taxonomy could also facilitate financing and capital formation by providing businesses with more confidence throughout the supply chain in the direction of the UK's pathway towards net zero. Furthermore, demonstrating alignment with a UK taxonomy could send a strong signal to domestic and international investors and help a company attract finance.

For those members who identify value in a UK taxonomy, it will be important for a UK taxonomy to be voluntary, proportionate and underpinned by other parts of the UK sustainable finance

framework. A UK taxonomy that includes mandatory disclosure requirements has the potential to conflict with the government's mission to kickstart economic growth by adding further compliance and reporting burdens.

Nevertheless, while it is recognised that a taxonomy can be helpful for investors in providing clarity on what activities are 'sustainable', this is distinct from encouraging investment into sustainable activities. Clear and long-term government policy is needed to channel capital flows into sustainable and transition activities in the real economy.

2. What are the specific use cases for a UK taxonomy which would contribute to the stated goals? This could include through voluntary use cases or through links to government policy and regulation.

- a. **What are respondents' views on the benefits of the proposed use case (paragraph 2.2)?**
- b. **Are there any other use cases respondents have identified?**
- c. **How does each use case identified link to the stated goals?**
- d. **Under these or other use cases, which types of organisations could benefit from a UK taxonomy?**
- e. **For each use case identified, do respondents have any concerns or views on the practical challenges?**
- f. **What is the role for government within each use case identified, if any (i.e. to provide oversight, responsible for ongoing maintenance, implement legislation, including disclosure requirements)?**

As outlined in response to question 1, there is a diversity of views across IRSG members on the value of a UK taxonomy, and therefore the use cases. The majority of members consider that a UK taxonomy would not be distinctly valuable in contributing to the government's stated goals. However, a minority of members consider that a UK taxonomy would be distinctly valuable and identify several distinct use cases. Many align with those outlined in paragraph 2.2 of the consultation paper.

Such use cases are dependent on a UK taxonomy being simple to use and interoperable with other taxonomies. There have been challenges in using the EU Taxonomy for the use cases identified below, with a recent survey showing that 76% of respondents cannot use the EU Taxonomy to make investment decisions due to complex and ambiguous criteria and data challenges.²

While there is potential for a UK taxonomy to be a useful tool in the government's sustainable finance toolbox, its utility depends on learning lessons from the EU experience and careful consideration of how it is designed and deployed alongside other policy and regulatory measures. This is necessary to maximise usability and interoperability, thereby ensuring a smooth experience for companies using taxonomies across multiple jurisdictions.

²DAI, 'Companies & ESG – transformation or just reporting?', available at: <https://www.dai.de/en/detail/companies-esg-transformation-or-just-reporting>

Specific use cases identified by UK-based financial and related professional services companies include:

- **Providing a common dictionary.** A taxonomy could provide a ‘common dictionary’ for market participants to refer to when developing sustainable products. A commonly shared and coherent definition of what is sustainable would be valuable in ensuring alignment and consistency across the market. It would be particularly beneficial for companies dealing with queries from multiple financial institutions. A taxonomy would enable the market to speak a common language and provide a clear route for information. However, care would need to be taken to ensure alignment with existing taxonomies and classification systems; without this, the concept of a ‘common dictionary’ could be undermined if companies rely on different frameworks.
 - **Labelling of products.** The classification system created by introducing a taxonomy would support consistent labelling and marketing of products. This classification system could support the mobilisation of sustainable investments and ensure consistency with the wider UK sustainable finance framework. For example, financial institutions have adopted the EU Taxonomy to structure sustainable finance products (e.g. green bonds and sustainability-linked loans). As of June 2024, there were more than 500 active bonds from 130 issuers listed on LSEG’s Sustainable Bond Market, equating to more than \$311 billion raised in sustainable debt financing.
 - **Reducing the risk and perception of greenwashing.** The FCA anti-greenwashing rule already provides a principle-based approach to mitigate the risk of greenwashing. A taxonomy could act as a further tool to mitigate the risk and perception of greenwashing. Voluntary classification against a recognised set of criteria of what is ‘green’ and ‘sustainable’ could act as a reference tool or kitemark, to provide confidence to investors.
 - **Useful information for corporates, investors and other financial institutions.** Voluntary reporting on a taxonomy could provide useful data and measurements to help investors and other financial institutions – such as banks and insurers – assess and transact with companies. Data on green capex and green revenues is recognised to be helpful for assessing a company’s commitments and progress towards sustainability, allowing measurements to support investment decisions and the allocation of capital. For example:
 - Measuring what percentage of a bank’s financing or a fund’s Assets Under Management (AUM) is in/to UK taxonomy-aligned activities would support investors in making educated decisions about where to invest.
 - Measuring whether a bond/loan aligns with a UK taxonomy so that it can be classified as a green bond/loan. The EU Taxonomy’s green bond standard is useful for this purpose and is regarded as the gold standard.
 - **Channelling financial flows to sustainable activities.** A UK taxonomy could be useful in providing a defined set of activities that will support the transition to net zero. It could provide the government with a set of guiding principles and market participants with a clear and simple guide on what activities are ‘sustainable’. For example, the EU Taxonomy has helped direct flows to the European Investment Fund which requires a percentage of funds to be aligned with EU Taxonomy activities.
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3. Is a UK taxonomy a useful tool in supporting the allocation of transition finance alongside transition planning? If so, explain how, with reference to any design features which can facilitate this?

The TFMR final report – ‘*Scaling Transition Finance: Findings of the Transition Finance Market Review*’ – recommended the government consult on the use case for a UK taxonomy and identified a taxonomy as a possible reference tool for demonstrating the credibility and integrity of transition-related financial products and strategies. There are taxonomies in other jurisdictions that incorporate transitional elements, such as those used in Singapore and Australia. There is also an opportunity for the UK to learn from the EU experience, which has proven to be overly restrictive and resulted in a limited flow of capital towards transition activities.

If the government decides to proceed with a UK taxonomy, some members consider that it should include transitional elements to encourage investments in activities that support the UK’s transition to net zero. The ability to support transition activities using a traffic light system, as seen in Singapore, could be beneficial for the UK. This approach, along with safeguards such as sunset dates would aid transition efforts while preventing emissions lock-in. Inclusion of transition activities within a UK taxonomy would support the UK’s continued leadership on transition finance internationally and put the UK in a strong position to be seen as the best place to raise transition capital.

However, some members consider that it would be preferable to follow the approach that the EU has taken to transition activities. This is primarily due to the challenges identified in the consultation paper regarding the lack of flexibility to capture the nuances of differing transition pathways within companies and scientific and technological developments.

4. How could the success of a UK taxonomy be evaluated? What measurable KPIs could show that a UK taxonomy is achieving its goals?

Should the government decide to introduce a UK taxonomy, its success could be measured in relation to how it supports the delivery of the government’s stated green and net zero transition outcomes and goals. For example, the deployment level of low-carbon fuels and EV percentage of the total car/lorry fleet, as referenced in Table 7 of the Carbon Budget Delivery Plan.³

The government could also consider evaluating the success of a UK taxonomy at a more granular level by measuring industry adoption and use. For example, the percentage of companies voluntarily using the UK taxonomy as a guiding tool to support sustainable investment decision-making or the capital allocation directed by financial institutions into taxonomy-aligned sustainable activities.

³ Department for Energy Security & Net Zero, ‘Carbon Budget Delivery Plan’, available at: <https://www.gov.uk/government/publications/carbon-budget-delivery-plan/carbon-budget-delivery-plan>

Chapter 3: Key Design Questions

We have responded to the questions below in the context of a decision from the government to proceed with a UK taxonomy. Should the government decide to introduce a UK taxonomy, it will be important to fully consider what ‘good’ looks like for the UK, to ensure it is as effective and value-adding as possible.

A UK taxonomy must reflect lessons learned and best practices of other jurisdictions. It must also be informed by the government’s ambition to be the world leader in sustainable finance, and its mission to deliver economic growth. It must support the objectives of encouraging financial flows towards sustainable activities and an effective transition to net zero and seek to maximise interoperability across companies and markets. It should be created in collaboration with sectors across the economy, to ensure cross-sector buy-in and that it works effectively as part of the UK’s sustainable finance framework.

A significant amount of work on the key design questions outlined in the consultation paper was completed by the GTAG (of which the IRSG was a member), including international interoperability, streamlining the ‘Do No Significant Harm’ (DNSH) principle, and operational considerations for taxonomy reporting. We would encourage the government to look to the work of the GTAG. However, whilst the GTAG’s work is informative and provides a good basis, further consultation will be needed as the GTAG was not necessarily representative of the entire industry nor reflective of current industry positions on a UK taxonomy.

International Interoperability

International interoperability is a critical consideration for a UK taxonomy. The GTAG reported that, as of May 2023 there were 47 taxonomies in development or implementation across the globe. Therefore, it will be important for a UK taxonomy to be as interoperable as possible. This will support the UK as a world-leading financial services hub and reduce the reporting burden for companies operating across multiple jurisdictions.

The GTAG paper on interoperability provides a series of recommendations on how the UK could pursue interoperability without compromising the robustness or science-based nature of a UK taxonomy, whilst also encouraging an increase in ambition globally.⁴ In this report, GTAG outlined the importance of not neglecting local context alongside the pursuit for harmonisation of taxonomies. While international interoperability considerations are important, a UK taxonomy will also need to reflect the locality – that is the specific pathways for the UK to reach net zero by 2050.

There is a notable gap in the international framework for a standard setter for taxonomies, akin to the ISSB. The UK can play a pivotal role in addressing this gap by either joining the Multi-Jurisdiction Common Ground Taxonomy (M-CGT) – that includes the EU, China and Singapore – or

⁴ GTAG, ‘Promoting the international interoperability of a UK Green Taxonomy’, see page 17, available at: <https://www.greenfinanceinstitute.com/wp-content/uploads/2024/06/GFI-GTAG-INTERNATIONAL-INTEROPERABILITY-REPORT.pdf>

advocating for the expansion of the IFRS's mandate to include the development of a high-level international interoperable taxonomy.

The International Organisation of Securities Commission (IOSCO) could also play a role in supporting the international interoperability of taxonomies. IOSCO members regulate more than 95% of the world's securities markets in more than 130 organisations. IOSCO's endorsement decision on ISSB standards sent a strong signal to jurisdictions across the globe that the standards were fit for purpose. IOSCO has called on members to consider ways in which they might adopt, apply or otherwise be informed by ISSB standards to support the development of a global framework for sustainability standards.

5. There are already several sustainable taxonomies in operation in other jurisdictions that UK based companies interact with. How do respondents currently use different taxonomies (both jurisdictional and internal/market-led) to inform decision making?

EU Taxonomy. Many UK-based financial and related professional services companies are already disclosing alignment with the EU Taxonomy under SFDR and CSRD. Bloomberg has reported that, as of 2025, 77% of UK domiciled companies could be expected to report on the EU taxonomy. Furthermore, two-thirds of country-led taxonomies in place or under development use the EU as a benchmark. Therefore, there is limited appetite among members to diverge from the EU approach.⁵

A UK taxonomy that diverges from the EU approach would require companies to respect different standards in different jurisdictions, increasing the cost of compliance or voluntary observance. It would also result in a duplication of data and processes, introducing unnecessary operational costs and frictions for companies operating in multiple jurisdictions.

The GTAG highlighted that divergence from the EU could also cause confusion for companies – for example, whether an activity can be held in a green portfolio if it is classified as green in the EU but not in the UK.⁶ Significant divergence from the EU could act as a disincentive for companies to locate in the UK and could impact the UK's competitiveness as a destination for green and sustainable finance, with implications for the government's growth mission and sustainability objectives. Therefore, there is a strong case for a UK taxonomy to have as much alignment with the EU as possible. This would embed a strong baseline of interoperability into the UK approach, both with the EU and across other jurisdictions.

However, a UK taxonomy must learn the lessons of the EU Taxonomy. Evidence has shown that it is not user-friendly and has become more of a regulatory 'tick box' exercise for financial institutions rather than facilitating green capital flows, due to the challenges set out earlier (see question 2). If the UK were to introduce a taxonomy aligned with the EU Taxonomy, the government

⁵ GTAG, 'Promoting the international interoperability of a UK Green Taxonomy'

⁶ GTAG, 'Advice on the development of a UK Green Taxonomy' available at:

<https://www.greenfinanceinstitute.com/wp-content/uploads/2024/06/GTAG-Advice-on-the-development-of-a-UK-Green-Taxonomy.pdf>

must adapt and improve elements and ensure that it is aligned with the UK's net zero industrial policy.

There is an opportunity for the UK to develop the EU Taxonomy into a more pragmatic, principle-based and voluntary taxonomy. This could serve as a model for other jurisdictions and inform the review of the EU Taxonomy that is planned for 2025 as part of the 'Omnibus Simplification Package' (Omnibus) to simplify and eliminate overlaps in sustainability reporting across multiple EU laws (CSRD, Corporate Sustainability Due Diligence Directive (CS3D) and the EU Taxonomy). The review of the EU Taxonomy under the Omnibus could have a significant impact on interoperability. Therefore, it will be important for the government to monitor developments and the proposals of the Omnibus (expected in February 2025).

Multi-Jurisdiction Common Ground Taxonomy (M-CGT). If the government decides to proceed with a UK taxonomy, and for it to be effective, it needs to be considered a suitable proxy for other international taxonomies. We strongly support the work of the International Platform on Sustainable Finance (IPSF) on the M-CGT and encourage the government to look to this workstream – and the major areas of commonality between the EU, Singapore and China taxonomies – when considering the design of a UK taxonomy.

The findings of the M-CGT mapping exercise show some degree of comparability of green activities across the three jurisdictions. By providing greater clarity and transparency on the commonalities and differences between the jurisdictional taxonomies, the M-CGT will help to reduce cross-border transaction costs and support the mobilisation of green capital flows internationally.⁷

There is an opportunity for the UK to better leverage its seat on the IPSF to promote the harmonisation and interoperability of jurisdictional taxonomies. Work towards developing proxies or compatible metrics across the globe would facilitate taxonomy implementation and improve the accuracy of data.

6. In which areas of the design of a UK taxonomy would interoperability with these existing taxonomies be most helpful? These could include format, structure and naming, or thresholds and metrics.

We recommend government consult the GTAG advice previously referenced on promoting international interoperability of a UK taxonomy when considering where interoperability with existing taxonomies would be most helpful.

⁷ MAS, 'The International Platform on Sustainable Finance presents the Multi-Jurisdiction Common Ground Taxonomy to enhance interoperability of taxonomies across EU, China and Singapore' available at: <https://www.mas.gov.sg/news/media-releases/2024/multi-jurisdiction-common-ground-taxonomy>

7. Are there any lessons learned, or best practice from other jurisdictional taxonomies that a potential UK taxonomy could be informed by?

Lessons learned from the EU Taxonomy. There are several lessons learned from members' experiences of the EU Taxonomy. Some are specific to different sectors within the UK-based financial and related professional services industry.

- For member companies who report on the EU Taxonomy, there is consensus that a UK taxonomy should learn from the experience with mandatory disclosure under the EU Taxonomy, which has imposed a disproportionate reporting burden and cost of compliance for business. There is a strong preference for a UK taxonomy to be informed by this experience and not include a requirement for mandatory disclosure. A UK taxonomy could instead serve as a guiding framework.
- The EU Taxonomy's DNSH requirements for an economic activity to be considered 'environmentally sustainable' make it challenging for companies to assess taxonomy alignment of activities and investors to assess taxonomy alignment of investments. This has limited progress in the net zero transition. A more flexible framework that includes a streamlining and improvement of the DNSH criteria would help support innovation in products that align (in part) with the taxonomy and progress in the transition to net zero.
- The EU Taxonomy requires the classification of activities in line with how a company makes revenue or capital expenditure, this allows companies to map activities in different ways. The lack of standardisation has resulted in inconsistency in approaches to classification and a lack of comparability between companies. There are also similar but slightly different tests included in other pieces of legislation which leads to confusion. Legislation should be as consistent across the board as possible.
- For data providers, the framework of the EU Taxonomy is not retail friendly. For example, the opex and capex alignment metrics are not easy to understand and therefore do not help inform investor decision-making.

As outlined earlier, the EU is currently considering its approach to the EU Taxonomy under the Omnibus in the face of concerns over its complexity, alongside the reporting burden across multiple EU laws. It will be important for the UK to engage with the Omnibus, and the approach the EU is proposing to take to streamline the EU Taxonomy, as this could have an impact on the international interoperability of a UK taxonomy.

Best practice from other jurisdictional taxonomies. There are several best practices from other jurisdictional taxonomies that could inform a UK taxonomy. These include:

- **Approach to transitional activities:**
 - **Singapore.** A taxonomy which combines principle-based criteria and quantifiable thresholds for activities could provide important lessons for a UK taxonomy on how to apply a traffic light system to transitional activities.
 - **ASEAN.** The taxonomy is designed to be an inclusive and science-based classification system to support ASEAN member states transition to a low-carbon and sustainable future. It allows for different starting points in the transition journey and classifies activities as either green, amber (transitional) or red (not aligned).

- **Australia.** The taxonomy is focused on transition categories in addition to green categories, recognising the role that decarbonising sectors will have to play in reducing Australia's national emissions, greening financial portfolios and reducing systemic risk exposure across the economy.⁸
- **Mobilising investment into the UK's net zero transition.** The UK taxonomy could be informed by Canada's approach. The taxonomy aims to mobilise investment in support of Canada's net zero transition by enabling investors to understand and communicate which key activities and investments would deliver a Canadian net zero economy.⁹ Canada's taxonomy is likely to be voluntary and without a requirement for mandatory reporting, based on a single template for the market.

8. What is the preferred scope of a UK taxonomy in terms of sectors?

We recommend that a UK taxonomy take a phased approach to sectoral coverage and scope, with a focus on the top sectors that contribute to the UK's emission profile and therefore priority sectors for decarbonisation to support the UK's net zero transition – such as domestic transport, buildings and homes, industry, electricity supply and agriculture. This would be a pragmatic approach and would ensure that a UK taxonomy is rolled out in a way that is complementary to existing sustainable finance components.

9. What environmental objectives should a UK taxonomy focus on? How should these be prioritised? The list outlined in the consultation is noted to align with those used in other taxonomies globally.

We would encourage the government to consider focusing a UK taxonomy on climate mitigation and adaptation in the first instance, given the recognised impact on the UK economy and target of net zero by 2050. However, in the long term, the environmental objectives of a UK taxonomy should encompass the full spectrum of nature, not solely focus on climate. Since the introduction of the EU Taxonomy, significant progress has been made in understanding nature holistically, incorporating not just climate, but also biodiversity, water scarcity and other critical environmental factors. Whilst the government has established net zero targets, it is increasingly striving to demonstrate its broader commitment to nature conservation and restoration. A comprehensive approach, reflecting the interdependencies of these environmental components, would better align with global efforts and the UK's broader sustainability objectives.

⁸ Australian Sustainable Finance Institute, 'Taxonomy Project', available at: <https://www.asfi.org.au/taxonomy#:~:text=A%20taxonomy%20would%20help%20to,economic%20activities%20will%20need%20to>

⁹ Government of Canada, 'Government advances Made-in-Canada sustainable investment guidelines to accelerate progress to net-zero emissions by 2050', available here: <https://www.canada.ca/en/department-finance/news/2024/10/government-advances-made-in-canada-sustainable-investment-guidelines-to-accelerate-progress-to-net-zero-emissions-by-2050.html>

10. Key metrics to demonstrate alignment. When developing these objectives, what are the key metrics which should be used for companies to demonstrate alignment with a UK taxonomy?

The IRSG will not be responding to this question.

11. What are the key design features and characteristics that would maximise the potential of a UK taxonomy to contribute to the stated goals? Please consider usability for both investors and those seeking investment. This may include but not be limited to the level of detail in the criteria and the type of threshold (e.g. quantitative, qualitative, legislative).

For a UK taxonomy to contribute to the government's stated goals of channelling capital and preventing greenwashing it must be proportionate and pragmatic and focused on the UK's transition pathway to net zero. A taxonomy will not be effective if it introduces unnecessary complexity, cost and burdensome reporting requirements for business, as seen with the EU Taxonomy. Therefore, a UK taxonomy should be designed in a way that facilitates ease of compliance and supports investment in the transition to net zero. A non-legislative (i.e. not fixed in primary legislation) approach would enable the government to introduce a more flexible and dynamic framework, which supports businesses with the transition while not imposing stringent reporting requirements.

It will be important for the government to consider how to approach disclosure requirements under a UK taxonomy. As outlined in response to question 7, there is a strong preference across our industry for the government to learn from the approach taken in the EU and not introduce mandatory disclosure requirements under a UK taxonomy. The benefits of mandatory disclosure are not considered to outweigh the costs.

12. What are respondents' views on how to incorporate a Do No Significant Harm (DNSH) principle, and how could this work?

The EU Taxonomy DNSH criteria as drafted are complicated to follow due to the number of criteria which are inconsistent, overly repetitive and difficult to measure. There is also a lack of clarity on fundamental definitions such as 'significant harm'. This complexity and ambiguity has resulted in reporting that often shows little alignment. Other taxonomies do not feature the EU approach to DNSH due to these challenges.

Should the government decide to introduce a DNSH principle under a UK taxonomy, while the criteria need to be scientific and robust, we recommend a streamlining of the EU criteria and revisions to improve usability and application. The GTAG produced a comprehensive report on '*Streamlining and increasing the usability of the Do No Significant Harm (DNSH) criteria within the UK Green Taxonomy*'. We recommend the government look at the analysis and recommendations when considering how to incorporate DNSH under a UK taxonomy.

13. Is it likely a UK taxonomy would need regular updates, potentially as often as every three years?

- a. Do you agree with this regularity?
- b. Would this pose any practical challenges to users of a UK taxonomy?
- c. Would this timeframe be appropriate for transition plans?

Regular updates will be needed to a UK taxonomy to keep pace with scientific, technological and policy developments. However, this also needs to be balanced with maintaining stability.

Other jurisdictions update their taxonomies every three years. While it may be challenging for companies to keep pace with changes every three years, this frequency would be appropriate to ensure a UK taxonomy is aligned with the latest climate science and changes to technology maturity and adoption, market developments and customer demand.

Whilst regular updates are essential, they could pose practical challenges for users, particularly in terms of compliance and operational adjustments. To mitigate these challenges, it is crucial to incorporate the principle of ‘grandfathering’ into a UK taxonomy. This principle would allow market participants to continue using the taxonomy criteria that were in place at the time of their initial investment or product issuance. This would ensure that users do not have to constantly re-balance or modify their products and portfolios beyond reasonable measures, providing them with the confidence and stability needed to plan and execute long-term sustainable investments.

14. What governance and oversight arrangements should be put in place for ongoing maintenance and updates to accompany a UK taxonomy?

It will be important for the government to have responsibility and accountability for leading the ongoing maintenance and updates to accompany a UK taxonomy. This is necessary to ensure that new policies are developed in line with the standard government policy making process, including formal consultations and undertaking of rigorous cost-benefit analysis.

However, we also assess that it may be necessary for an independent body or committee to have an oversight role and support government with the maintenance of a UK taxonomy to ensure that it is consistent with other UK sustainable finance measures and as internationally interoperable as possible. This is critical to support the government’s growth mission and ambition for the UK to be the world leader in sustainable finance. This independent body should be comprised of subject matter experts and industry representatives and draw from proven academic and scientific inputs, as well as the private sector. The government could also look at the findings and observations from the GTAG report on ‘*Creating an institutional home for the UK Green Taxonomy: exploring options*’ when considering governance and oversight arrangements for a UK taxonomy.¹⁰

¹⁰ GTAG, ‘Creating an institutional home for the UK Green Taxonomy: exploring options’, available at: <https://www.greenfinanceinstitute.com/wp-content/uploads/2024/06/GTAG-Final-Report-on-Institutional-Home.pdf>