fund-raising in Indonesia and the Philippines.

[34]Terrorism Financing Regional Risk Assessment 2016—South East Asia and Australia, produced by the Australian government, see pg. 16 discussing key features of TF in the region.

[35] http://www.bsp.gov.ph/banking/emi_.pdf. Wirecard e-Money Philippines is still registered as an electronic money issuer.

[36] https://www.coindesk.com/sec-cftc-hit-crypto-app-abra-with-300k-in-penalties-over-illegal-swaps. Coindesk has identified over $50 million in funding to date, including between $350,000 and $1 million in PPP bailout loans.

[37] https://www.congress.gov/107/plaws/publ56/PLAW-107publ56.pdf. Uniting and strengthening America by providing appropriate tools required to intercept and obstruct terrorism (USA Patriot Act) Act of 2001.

[38] https://www.coindesk.com/bitinstant-ceo-charlie-shrem-arrested-silk-road-bitcoin-bust.

EU TAXONOMY REGULATION COMES INTO FORCE

By Mehran Massih and Jason Pratt

Mehran Massih is a counsel in Shearman & Sterling LLP's Environmental practice, advising on all aspects of transactional environmental and social work, including environmental and social review in the financing of major infrastructure and industrial projects. Jason Pratt is a counsel in Shearman & Sterling's Environmental practice, advising companies and financial institutions in the context of mergers, acquisitions, divestitures, financings, real estate transactions, bankruptcy proceedings, regulatory compliance matters, and governmental cleanup programs.
Contact: mmassih@shearman.com or jpratt@shearman.com.

On June 22, 2020, the European Union so-called "Taxonomy Regulation"[1]—touted as the world's "first ever green list"—was published in the EU Official Journal after the final stage of its approval by the European Parliament. This paved the way for the Regulation to come into effect on July 12. The green framework the Regulation establishes will evolve over time well beyond this date and, in practice, may influence financial disclosure practices beyond the European Union, including in the United States.

The Regulation is one part of the European Commission's multi-faceted package of reforms relating to sustainable finance, which in turn is a component of the EU's more ambitious "Green Deal."[2] The Taxonomy Regulation is a significant milestone among these measures because it establishes an EU-wide classification system—in effect, a glossary or "taxonomy"—for determining whether an economic activity is environmentally sustainable for purposes of investment. It purports to provide businesses and investors with a common language to identify which economic activities can be considered "green."

The Taxonomy Regulation amends the "Disclosure Regulation"[3]—which is also part of the EU's sustainable finance reform package—to require new sustainability-related pre-contractual and period reporting disclosures from financial market participants offering EU-regulated financial products, including managers of UCITS funds, alternative investment funds, insurance-based investment products, securitisation, venture capital and private equity funds, and pension products and pension schemes. The disclosures will be mandatory in respect of certain products or offerings that invest in an economic activity that contributes to an environmental objective and (a) have sustainable investment as their objective or (b) promote environmental or social characteristics of the investment. Broadly, the financial market participant offering the relevant product will be required to state: how and to what extent they have used the Taxonomy in determining the sustainability of the underlying investments; to what environmental objective(s) the investments contribute; and the proportion of underlying investments that are Taxonomy-aligned as a percentage of the investment, fund, or portfolio.

Pre-contractual and periodic reporting disclosures in respect of all other financial products must carry a disclaimer that the investment does not take into account the EU criteria for environmentally sustainable investments.

The Taxonomy Regulation also introduces new sustainability-related disclosure obligations for "large public-interest entities" that are already required to publish a non-financial statement under the EU Non-Financial Reporting Directive.[4] This category generally includes EU-listed companies, banks, or insurance companies with more than 500 employees that meet specified balance sheet or turnover thresholds. These entities will be required to disclose in their non-financial statements, such as their annual reports or sustainability reports, how and to what extent their activities are associated with Taxonomy-aligned activities in terms of their proportion of turnover, capex, and, if relevant, opex.

Despite the prescribed scope of the Taxonomy Regulation, the mere fact that a pan-European package of "green" criteria has been published for the first time in a rulemaking instrument will likely give the Taxonomy a much larger life. At least for the time being, the Taxonomy is likely to become the go-to reference point for sustainability criteria in any investment or financing context, potentially regardless of jurisdiction. Given the lack of any equivalent rulemaking in the United States, financial market participants in the U.S. could start to refer to the Taxonomy as a benchmark in so-called "green" offerings and financial products.

What Activities Are "Green"?

In substance, the Taxonomy Regulation is the culmination of final recommendations made in March 2020 by a Technical Expert Group on Sustainable Finance or TEG, a body the European Commission established to further a number of initiatives under the EU action plan on sustainable finance. The Regulation recognizes six broad "environmental objectives":

- Climate change mitigation.
- Climate change adaptation.
- Sustainable use and protection of water and marine resources.
- Transition to a circular economy (*i.e.,* waste prevention, reuse and recycling).
- Pollution prevention and control.
- Protection and restoration of biodiversity and ecosystems.

An economic activity is deemed to be environmentally sustainable if it:

- Contributes substantially to one or more of these environmental objectives, or directly enables other activities to make a substantial contribution to one or more of them.
- Does not significantly harm any other environmental objective.
- Complies with applicable technical screening criteria, which mostly have yet to be developed and are forthcoming pursuant to delegated regulatory authority.
- Complies with certain minimum safeguards (*e.g.,* OECD Guidelines on Multinational Enterprises and the UN Guiding Principles on Business and Human Rights).

The technical screening criteria are the centrepiece of fleshing out the specifics and will be developed in stages. So far, the TEG has developed technical screening criteria for 70 activities in eight economic sectors contributing to climate change mitigation and 68 activities contributing to climate change adaptation. The sectors covered so far include the following:

- Agriculture, forestry, and fishing.
- Manufacturing.
- Electricity, gas, steam and air conditioning supply.

- Water, sewerage, waste, and remediation.
- Transportation and storage.
- Information and communication technologies.
- Construction and real estate.

These criteria are the "flesh and bones" of the Taxonomy—the glossary element that is bound to be referred to repeatedly. The TEG's work so far on these criteria provides the basis for a delegated act that the European Commission intends to adopt by the end of 2020. The TEG's criteria are very much a work in progress, however, and it is possible additional activities will be included as substantially contributing to climate change mitigation or adaptation in the Commission's delegated act. In addition, the Taxonomy Regulation requires the Commission to review regularly the criteria it adopts in line with scientific and technological developments.

As for the other four environmental objectives, the Taxonomy Regulation requires the European Commission to establish technical screening criteria for these objectives by the end of 2021.

"Enabling" and "Transitioning" Activities

Importantly, the Taxonomy Regulation deems economic activities that directly "enable" the six environmental objectives to be environmentally sustainable, as long as they (a) do not lead to a "lock-in" in assets that undermine long-term environmental goals, and (b) have a substantial positive environmental impact based on life-cycle considerations. Enabling activities cover the provision of products or services that make a substantial contribution to activities deemed environmentally sustainable based on their own performance. Examples would include manufacture of low-carbon technologies or their key components, equipment or machinery, information and communications technology for climate change mitigation, and professional, scientific, and technical activities for climate change adaptation.

In addition, TEG recognized that, although some economic activities will not currently meet the Taxonomy's technical screening criteria, the financing or costs of improvement measures can be considered Taxonomy-aligned if they are part of a "transition" plan to meet the criteria over a defined time period.

Future Steps

The Taxonomy will evolve over time as the Commission's delegated acts bring more detail to each of the broad requirements outlined above. One of the key next steps will be the development of additional regulatory technical standards to flesh out the "do no significant harm" principle to an activity being Taxonomy aligned, and its related disclosure requirements. Moreover, as part of its action plan on sustainable finance, the Commission intends further down the line to propose an EU "eco-labelling" scheme for financial products and an EU green bond standard, both of which will rely heavily on the criteria established by the Taxonomy. These are only two of the initiatives planned in a robust EU rulemaking space that is likely to pave the way for similar requirements elsewhere.

ENDNOTES:

[1]Regulation (EU) 2020/852.

[2]The European Green Deal is an overarching framework of actions the European Commission presented in December 2019 to transform the European economy. A key component is a legal commitment for the EU to achieve climate neutrality by 2050. Other core components are strategies on supplying clean and secure energy, biodiversity, zero pollution, a circular economy, and sustainable food production.

[3]Regulation (EU) 2019/2088 on Sustainability-Related Disclosures in the Financial Services Sector.

[4]Directive 2014/95/EU, amending Directive 2013/34/EU.