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REGULATORY DEVELOPMENTS ON GREEN, SOCIAL AND SUSTAINABLE CAPITAL MARKET INSTRUMENTS

The Capital Markets Board (CMB) had established a detailed framework for sustainable financial instruments with the Guidelines on Green Debt Instruments, Sustainable Debt Instruments, Green Lease Certificates and Sustainable Lease Certificates ("**Guide**") published on 22 September 2022. Recently, in alignment with sustainable development goals, the CMB has made the following initiatives available for public consultation: **(i)** on 6 September 2024, it released the Draft Guidelines on Green, Sustainable and Social Capital Markets Instruments ("**Draft Guide**") to support financing for projects with high environmental and social impact in Türkiye, and **(ii)** to integrate developments in international financial markets into Turkish capital markets and diversify sustainability-themed issuances, it issued a separate Draft Guidelines on Sustainability-Linked Capital Markets Instruments ("**Draft Sustainability-Linked Guide**") based on the International Capital Market Association (ICMA) Sustainability-Linked Bond Principles. Additionally, on 25 September 2024, the Ministry of Environment, Urbanization, and Climate Change of the Republic of Türkiye released the Draft Regulation on Türkiye's Green Taxonomy ("**Draft Taxonomy Regulation**") in alignment with Türkiye's Green Deal Action Plan, published in 2021, and the EU Green Taxonomy. The primary developments envisaged in these regulations are summarized below.

1. New Developments Introduced in the Draft Guide

While the initial Guide focused solely on "green" and "sustainable" debt instruments and lease certificates, the Draft Guide also regulates "social" capital market instruments in addition to "green" and "sustainable" ones. Additionally, the Draft Guide, which includes blue capital market instruments, sets forth provisions for social projects. It addresses domestic and international issuances of green, sustainable, and social capital market instruments, as well as green and social projects, framework documents, reporting, and external evaluation services. It also evaluates the issuance of green, sustainable, and social capital market instruments, such as lease certificates, asset-backed and mortgage-backed securities, asset-based and mortgage-backed securities, project-based securities, and real estate certificates. For capital market instruments to be classified as "green," "sustainable," or "social" under the Draft Guide, they must meet the following

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conditions: **(i)** the issuer must prepare a framework document affirming that the issuance process will comply with the principles in the Draft Guide; **(ii)** funds raised from the issuance must be used exclusively, as specified in the framework document, for financing or refinancing, either partially or fully, new and/or existing green and/or social projects that fit the relevant definitions; and **(iii)** an independent second-party opinion must be obtained to review and assess compliance with the Draft Guide.

Issuers are required to obtain an external evaluation service for this purpose. This service can be provided by institutions listed by organizations such as ICMA and the Climate Bonds Initiative or by public institutions or entities authorized to perform independent audits or ratings in capital markets, specializing in environmental, sustainability, and social areas. The external evaluation process primarily consists of second-party opinion and verification services. Issuers must submit the framework document and the second-party opinion to the CMB, along with other information and documents, during their application for approval of the issuance ceiling prospectus or offering circular.

Funds obtained from the issuance of green, sustainable, and social capital market instruments must be used for green and/or social projects as defined in the Draft Guide as soon as possible, with the designated timeframe stated in the framework document. It is expected that these green and/or social projects will provide clear environmental and/or social benefits, which the issuer will evaluate and present measurably in the framework document. Examples of green project types under the Draft Guide include energy efficiency, pollution prevention and control, clean transportation, and green buildings. A key development differentiating the Draft Guide from the initial Guide is the inclusion of a social project definition. Social projects directly address or aim to mitigate specific social issues and/or target positive social outcomes for a specific group. Expected social project types are accessible infrastructure, affordable housing, employment creation projects and programs, food security and sustainable food systems, and socio-economic progress and empowerment.

Under the Draft Guide, issuers are required to prepare an annual report, at a minimum, detailing the use of funds raised from the issuance. This report must be publicly disclosed on the issuer's website, in line with the CMB's regulations on public disclosure of material events, and if the issuer is a member of the Public Disclosure Platform (PDP), it must also be published on the PDP. Additionally, after all funds raised from issuances under the same issuance ceiling have been fully utilized, issuers must prepare an impact report containing the estimated and/or actual environmental and social impacts and disclose it publicly.

2. New Developments Introduced in the Draft Sustainability-Linked Guide

The Draft Sustainability-Linked Guide covers capital market instruments such as sustainability-linked debt instruments, lease certificates, asset-backed and mortgage-backed securities, asset-based and mortgage-backed securities, project-based securities, and real estate certificates, as well as their issuance. The Draft Sustainability-Linked Guide encourages issuers to set predefined, measurable, and, where possible, comparable sustainability targets monitored on a specific timeline, with key performance indicators whose performance is verified by external evaluation.

The key performance indicators are expected to be fundamental, relevant to the issuer's entire business area, of high strategic importance to the issuer's current and/or future operations, measurable or calculable on a consistent methodological basis, externally verifiable, and

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comparable. Issuers are required to prepare a performance evaluation report, at least annually, containing updates on their progress in achieving sustainability performance targets. This report, which should include information enabling investors to gauge the ambition level of the sustainability performance targets, must be disclosed on the issuer’s website and, if the issuer is a member of the PDP, on the PDP as well. In addition to the performance evaluation report, issuers are required to obtain an independent verification opinion to assess each key performance indicator’s success level against each sustainability performance target.

3. New Developments Introduced in the Draft Taxonomy Regulation

The Draft Taxonomy Regulation is designed to support environmental goals such as reducing greenhouse gas emissions, adapting to climate change, sustainable use and protection of water and marine resources, transitioning to a circular economy, preventing and controlling pollution, and protecting and restoring biodiversity and ecosystems. The Draft Taxonomy Regulation introduces the concept of a “compatible economic activity.” For economic activities to qualify as “compatible economic activity,” they must **(i)** make a substantial contribution to at least one environmental objective, **(ii)** not cause significant harm to any other environmental objective, **(iii)** comply with minimum social safeguards, and **(iv)** meet the technical screening criteria specified for points (i) and (ii). Additionally, economic activities will be assessed according to technical screening criteria, and sustainability reporting will be mandatory for these activities under the Draft Taxonomy Regulation. Institutions and organizations required to conduct sustainability reporting must, in addition to the sustainability reports they submit annually, register verified information regarding their compatible economic activities conducted in the previous year within the Climate Change Directorate’s e-taxonomy system. Although this obligation will enter into force on 1 January 2027, reporting may be submitted on a voluntary basis until 31 December 2026.

These developments enhance investor confidence by aligning capital markets with global sustainability goals and promoting sustainable financing. Türkiye’s alignment with international standards through these regulations facilitates access to sustainable investments and supports the financing of projects in line with environmental, social, and governance (ESG) principles. Combating the climate crisis and transitioning to a low-carbon economy will strengthen Türkiye’s integration with global sustainability targets and provide a crucial pathway to achieving environmental objectives.

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