

Case study: Deutsche Bank - Application of the EU Taxonomy to Guarantee Facilities for Exporting Clients

Introduction

This case study has been developed to explore the application of the EU Taxonomy to Trade Finance products for exporting clients. However, the challenges and recommendations outlined in this case study are also relevant for SME clients in the manufacturing sector more generally. Overall, the case study aims to advance the understanding of the assessment methodology defined in the EU Taxonomy and to evaluate its feasibility for this type of transaction.

All parties and related transactions presented in this case study are fictitious and not based on any specific business activities conducted by Deutsche Bank.

Case description

Client

The client is a German equipment manufacturer with subsidiaries in China and the US. The company has an export share of 80%. Its business activities focus on the manufacturing of specialised conveyor belt technology without any inherent climate change adaptation / mitigation-related characteristics. Among other use cases, the conveyor belts are used for baggage handling at airports and bulk materials handling in factories.

Product

Deutsche Bank is part of a banking club consisting of four German banks, providing a guarantee facility with a tenor of five years. The guarantee facility can be drawn and re-drawn for any guarantees (e.g. bid bonds, advance payment guarantees) up to a tenor of five years. Over the past year, guarantees for eight individual transactions have been issued under the facility. Based on the use of the conveyor belts, the following transactions are potentially eligible under the EU Taxonomy:

Transaction	Guarantee Type	End Use	Industry	Project
Guarantee 1	Bid Bond	Materials' handling system for raw materials	Utilities	Harbour project.
Guarantee 2	Bid Bond	Conveyor belt for a recycling plant	Recycling	New mechanical recycling facility to sort and re-use paper waste.
Guarantee 3	Bid Bond	Baggage handling system	Transportation	Regional airport.
Guarantee 4	Advance payment	Materials' handling system for clinker	Cement	Construction of a cement plant.
Guarantee 5	Advance payment	Conveyor belt for a recycling plant	Recycling	Mechanical recycling facility to sort and re-use plastic waste.
Guarantee 6	Performance	Materials' handling system for ore	Iron & Steel	Modernisation of a steel plant (hot iron).
Guarantee 7	Performance	Materials' handling system for waste	Utilities	Construction of a 50 MW waste-to-energy plant.
Guarantee 8	Performance	Materials' handling system for a copper mine	Mining	Modernisation of a copper mine.

Assessment

Technical Screening Criteria

All guarantees are assessed individually against the technical screening criteria outlined in the EU Taxonomy.

Transaction	Eligible activity as per EU Taxonomy	Assessment criteria	Data points provided by client	Outcome
Guarantee 1	No	n/a	n/a	n/a
Guarantee 2*	E38.3.2 Material recovery from non-hazardous waste	>50% of weight converted to secondary raw materials	Client cannot provide required data point	No assessment possible
Guarantee 3	No	n/a	n/a	n/a
Guarantee 4*	C23.5.1 Manufacturing of cement	Emissions < 0.766 tCO2e/t	Client cannot provide required data point	No assessment possible
Guarantee 5*	C20.1.6 Manufacturing of plastics in primary form	The plastics in primary form is manufactured by mechanical recycling	Plant produces plastics by mechanical recycling	EU Taxonomy aligned
Guarantee 6*	C24.5.1 Manufacture of Iron and Steel	Emissions ≤ 1.328 tCO2e/t	Client cannot provide required data point	No assessment possible
Guarantee 7	No	n/a	n/a	n/a
Guarantee 8	No	n/a	n/a	n/a

* Questionable whether the activity can be classified as own performance as opposed to enabling activity which is not foreseen for the respective eligible activity. There is no direct link between emission reduction and the activity (handling of materials).

Thus, only guarantee 5 is potentially aligned with the EU Taxonomy, pending the outcome of further risk assessments.

Do No Significant Harm assessment (DNSH) & Social Safeguards assessment

For Guarantee facilities, it is usually not possible to conduct the DNSH assessment and social safeguards' assessment on a project basis, as Deutsche Bank does not have a direct business relationship with the project owner and thus cannot access the information required to conduct the assessment. To fulfil the DNSH / Social safeguard assessment requirements outlined in the EU Taxonomy, Deutsche Bank has conducted a due diligence regarding the environmental and social performance of its client. Furthermore, a screening of the publicly available data pertaining to the environmental / social performance of importers has been conducted. Both assessments showed no relevant findings.

Challenges

There have been four key challenges in applying the EU Taxonomy for the classification of individual transactions under the Guarantee facility.

- *No leverage to collect data:* the provider of the Guarantee facility has no leverage to collect the data required for the assessment from the importer, as there is no direct business relationship. The direct business relationship is between the bank and the exporter.
- *Data availability:* data required for assessment is not captured by importers / not publicly available due to lack of disclosure requirements for European SMEs and non-European counterparties.
- *High costs for additional risk assessments:* in absence of data disclosures provided by the client and the importer, resource-intensive due diligence processes would be required to conduct the DNSH / Social Safeguards' assessments, leading to disproportionately high administrative costs compared to revenues generated.
- *Narrow scope of enabling activities in the manufacturing sector* which hinder the classification of the delivery of components for an overall sustainable project.

Recommendations

To enable a feasible application of the EU Taxonomy and overcome the challenges outlined above, we propose the following:

- **enhance disclosure requirements** with internationally harmonised criteria to enable a level playing field for all market participants;
- implement a **(semi-)public database with project-level information** to provide transparency on the characteristics of individual projects; as some financial products require a more detailed due diligence (e.g. project financing), the data generated as part of this process could be shared across the industry to enable the classification of related transactions;
- develop a **tiered approach to the DNSH / Social Safeguards' assessment** based on the transaction characteristics (e.g. product, volume) to make the application feasible for products with a high relative cost of due diligence and/or straight-through-processing, small ticket business and SME clients;
- **widen scope of enabling activities in the manufacturing sector** to allow classification of the delivery of components for an overall sustainable project.

As of now, for this type of business (low proximity to the project owner, partly automated, small sizes) it seems to be not pragmatic to apply the EU Taxonomy.