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2025 UPDATE TO THE SUSTAINABILITY-LINKED LOAN PRINCIPLES

2025 updates to the Sustainability-Linked Loan Principles

On 26 March 2025, following their latest review, the loan market trade associations published updated versions of the Green, Social and Sustainability-Linked Loan Principles (together, the **Loan Principles**) and related guidance[1]. The changes are mostly clarificatory in nature (and more limited than in previous years[2]), but there are some noteworthy points and changes of emphasis for borrowers which use these products or may be considering doing so.

This briefing considers some of the key changes made to the Sustainability-Linked Loan Principles (**SLLP**) and how they might impact current and future transactions. These include:

- **Clearer differentiation between mandatory requirements, recommendations and options**, reflecting feedback from External Review providers. In general, these changes (in terms of requirements that are now expressed clearly as mandatory) are reflective of current market practice, but warrant attention from borrowers with transactions coming up for refinancing.

- **Removal of grandfathering protection for pre-existing and "in flight" transactions**: The grandfathering language which appeared in the previous versions of the SLLP has been deleted. The practical significance of this may be quite limited, but whether the publication of the updated SLLP has implications for transactions structured and originated in line with the previous versions will need to be considered on a case-by-case basis.

- **Refinement of criteria for selection of KPIs and SPTs**: A range of detailed changes bring the criteria for KPI and SPT selection into clearer focus and importantly, underline key contextual factors such as the borrower's broader sustainability strategy and position and geographic considerations.

We have published a separate briefing on the 2025 updates to the Green Loan Principles and Social Loan Principles, available here.

1. Clearer differentiation between mandatory requirements, recommendations and options/possibilities

A new interpretation section at the outset of the SLLP clarifies that "shall" indicates a mandatory requirement and "should" indicates a recommendation. "May" and "can" denote options and possibilities respectively. The language of the SLLP has been reviewed and re-cast accordingly. This change was made in response to calls from external reviewers for the use of more precise language to facilitate their ability to assess whether transactions are aligned with the SLLP.

While in a number of places "shall" replaces the previous "should", the changes largely reflect current practice. For example, the requirement in Core Component 2 that the SPTs be ambitious i.e. represent a material improvement in the respective KPIs, and in Core Component 5, that post-signing verification be conducted by a qualified external reviewer with relevant expertise, have both been updated from "should" to "shall" but were already considered non-negotiables in most instances. Some of the "shall" requirements, however, for example those relating to the frequency of reporting (discussed further at Core Component 4 below), might be viewed as substantive changes, or at least, a change in emphasis.

While "should" indicates a recommendation, it is to be expected that lenders will seek to apply such recommendations where possible, and such features will be deviated from only where there are good reasons why compliance is not possible or practical.

[1] All of the updated material is available from the LMA's Sustainable Lending microsite. Revision marked versions showing the differences between the previous and most recent versions are available. Please contact one of lawyers listed at end of briefing if you would like copies.

[2] The Loan Principles were last revised in February 2023. Please refer to our previous briefing for further details.

2. Removal of grandfathering protection

As part of the 2023 update, grandfathering language was added to the SLLP (and the other Loan Principles), to the effect that transactions completed prior to 9 March 2023 were exempt from following the updated SLLP. The intention was to clarify that for existing transactions and transactions which were "in flight" as the updated SLLP were published, alignment with the version of the SLLP in force when the transaction was originated/completed was sufficient for the purposes of the relevant label.

In the latest version of the SLLP, this grandfathering protection has been removed.

In theory, the removal of the grandfathering language means that "in flight" transactions (i.e. transactions that are being negotiated/finalised but have not yet been completed) may need to be reviewed to ensure alignment with the latest SLLP. The nature of the changes made to the SLLP in this 2025 update may mean that any such review has limited practical impacts on transaction structures and terms. However, it is conceivable that assurances and banks' internal assessments regarding alignment with pre-existing SLLP delivered shortly before publication of the updated SLLP may need to be reissued and/or re-checked to ensure they can be adjusted to confirm alignment with the latest update.

Whether pre-existing sustainability-linked loans (**SLLs**), structured on the basis of a previous version of the SLLP, are affected by the publication of the new SLLP (and the absence of grandfathering language) is likely to depend on the terms of the loan in question. SLLs often contain a "rendezvous" or "sustainability amendment" provision that may (depending on what has been negotiated) enable the terms of the loan to be reopened if the SLLP are updated and/or the lenders believe the loan is no longer aligned with the SLLP as published from time to time.

3. Core Components of an SLL

3.1 Core Component 1 - Selection of KPIs

KPIs may be "internally or externally derived"

The SLLP previously noted that KPIs can be "internal and/or external". The meaning of this was not immediately obvious, but the intention was to note that KPIs do not have to have been internally set or generated within the business. An obvious example of an "external" KPI is an ESG rating. However, reference to ESG ratings was removed from the SLLP Guidance in the 2023 update, leading to confusion as to (1) whether ESG ratings were acceptable as a KPI and (2) what the reference to "external" meant in this context. As part of the latest updates to the SLLP, the reference to "internal and/or external" has been amended to refer instead to KPIs being "internally or externally derived". The guidance on the use of ESG ratings has also been reinstated in the SLLP Guidance (see further below).

Re-emphasis of double materiality

A key requirement of the SLLP is that the KPIs be "material". The SLLP Guidance continues to apply the double materiality principle, requiring borrowers to look at both impact materiality and financial materiality. This approach has, however, now been clarified and emphasised further in the SLLP Guidance.

Additional criteria

The SLLP set out various other criteria that KPIs must meet in addition to materiality. Two new criteria have been added to the list in the latest round of updates, namely that KPIs shall be (1) "*consistent with the borrower's overall sustainability strategy*" and (2) "*where feasible, externally verifiable*".

The first of these new requirements reflects a theme that flows through this latest update to the SLLP, namely that KPIs selected for the purposes of an SLL should be considered in the context of the entity's overall strategy and position.

The second new requirement, while phrased as a mandatory requirement, is expressed to be complied with "where feasible". Our assumption is that this may be intended to acknowledge that some KPIs may not be capable of external verification. KPIs that are not capable of external verification may be relatively few. However, if a KPI is not capable of external verification, it is not clear how this reference to KPIs being verifiable "where feasible", sits alongside the requirement in Core Component 5 that **all SPTs shall** be externally reviewed and verified.

We suspect that, in practice, this discrepancy may be of limited significance given the first of the two new requirements, that KPIs are required to be consistent with the borrower's overall ESG strategy and position. The materiality of KPIs is, and will, increasingly be assessed by reference to (for example) CSRD and ISSB standards. Such KPIs will (by definition) increasingly be the subject of external assurance as a result of regulatory requirements. However, it could be a point that warrants discussion in certain transactions involving KPIs which are particularly unusual and/or have limited application beyond the borrower/business in question.

ESG ratings and "means oriented" KPIs

As mentioned above, express acknowledgment that a third party ESG rating may serve as a KPI has been reinstated in the SLLP Guidance, together with new conditions/considerations around the use of ratings in this way. The SLLP Guidance also now includes a discussion on the use of green capex as a KPI, noting that an SLL may include a KPI related to green capex (presented, for example, as a percentage of overall capex) as a "means oriented" KPI.

Sources to assist with KPI selection

In terms of other KPIs, the SLLP Guidance points users to an expanded range of resources and organisations to assist with KPI selection, and in particular KPI materiality assessments. One such resource is ICMA's KPI Registry, which provides illustrative examples of potential KPIs for sustainability-linked bonds. The KPIs are allocated by sector as well as being classified into core and secondary KPIs. Interestingly, the distinction between core and secondary KPIs, while picked up explicitly in the Sustainability-Linked Bond Principles, has not been included in the latest updates to the SLLP. The general view, supported by the reference to the KPI Registry in the SLLP Guidance, is however that the notion of core vs. secondary KPIs supporting KPI selection is equally applicable to loans as it is bonds.

3.2 Core Component 2 - Calibration of SPTs

Although the fundamental requirements remain unchanged, various clarifications have been made to Core Component 2 of the SLLP which addresses how to set SPTs.

Beyond BAU and regulatory targets

The 2023 update to the SLLP introduced the idea that to be considered "ambitious", SPTs should go beyond both a "business as usual" trajectory and regulatory required targets. This requirement is now clearly framed as mandatory in the SLLP. The practical impact of the tighter language here may be limited (largely reflecting existing market practice), but it may have implications for some borrowers.

Assessment in regional/national context

The statement that SPTs should, where possible, be benchmarked has been redrafted to expressly allow the regional and national context of the borrower to be taken into account. While the SLLP Guidance has, for some time, recognised the importance of taking into account differences in geography in the calibration of SPTs, it is helpful that the point is now expressly made in the SLLP themselves, particularly given differences across geographies in what might be considered an ambitious SPT. (The relevance of the regional context in the KPI materiality assessment has similarly been drawn out in the updated SLLP Guidance.)

Approach to benchmarking

The range of benchmarking approaches identified as relevant to the target setting exercise has been tweaked to make clear that not all approaches e.g. science will be relevant to all KPIs. The range of reference sources has also been expanded to refer specifically to Nationally Determined Contributions and the Kunming-Montreal Global biodiversity framework, the latter acknowledging the growth of nature-based KPIs and associated SPTs.

3.3 Core Component 3 - Loan characteristics

Here, and throughout the latest SLLP, the possibility of a financial and/or "structural" outcome depending on whether the SPTs are met is identified as a key characteristic of an SLL. Previously, the SLLP referred only to an economic outcome - the reference to "structural" outcomes is new.

This change aligns the SLLP with the equivalent provisions of the Sustainability-Linked Bond Principles. In sustainability-linked bonds, in addition to the imposition of a coupon penalty, the issuer's failure to meet the SPTs may have a "structural" impact in that it may trigger redemption rights.

While we are not aware of any UK/European SLLs that link SPTs to "structural outcomes", we understand that it is the potential for regional variations that prompted the new reference to structural outcomes in the latest SLLP. In our experience of SLLs, whether the SPTs are met or not leads solely to an economic outcome, in the form of a margin adjustment. However, the SLLP are intended to be of global application and there may be some SLLs in other regions that link SPT achievement to "structural" consequences (for example, a drawstop).

3.4 Core Component 4 - Reporting

Annual reporting on SPT performance is generally treated as a mandatory requirement in SLLs in practice. This is reflected in the updated SLLP, which now require that borrowers report at least annually - "should" having been changed to "shall".

The new wording "*at least annually and in any case for any date/period relevant for assessing the SPT performance leading to a potential adjustment of the SLL's financial and/or structural characteristics*" potentially raises questions about the frequency of reporting in transactions where SPTs are not set annually. While annual SPTs are intended to be the norm, Core Component 2 permits deviations where there is strong rationale for doing so. Our understanding of the intent of the SLLP here is that annual reporting is still required in those exceptional instances (where SPTs are not annual) to enable lenders to maintain a current picture of the borrower's progress.

3.5 Core Component 5 - Verification

Pre-signing external review of the alignment of an SLL with the SLLP, in the form of a second party opinion for example, is not customary in practice and remains optional (albeit recommended) in the updated SLLP.

Post-signing verification of the borrower's performance against each SPT, on the other hand, remains a mandatory requirement. Unlike reporting which is required at least annually (even where the SPTs are not set annually), clarifications to the SLLP and SLLP Guidance make it clear that post-signing verification is only required for each period for which the SPTs are set which may lead to an adjustment of the SLL's financial or structural characteristics.

Perhaps the most important change to the requirement for post-signing verification is the addition of language to make it clear that where information has already been verified as part of a borrower's annual reporting process or regulatory submissions, separate additional verification is not required for the purposes of the SLLP. Although reflective of what is already happening in practice, it is helpful that the SLLP now acknowledge this point expressly.

4. Other points

4.1 Transition plans and "controversial" issues

The SLLP still make no express mention of transition plans nor their role in the selection of KPIs and calibration of SPTs. This reflects that the approach to the role of, and requirements for, transition plans in most jurisdictions are still developing and the need to ensure the SLLP are capable of global application.

Credible transition plans were highlighted as a key contributor to supporting the integrity of SLLs in the FCA's June 2023 review of the SLL market. Where available, transition plans, outlining how the borrower plans to achieve its goals, are in practice becoming a key factor in SLL lending decisions. The SLLP Guidance acknowledges this, noting that, while SLLs are intended to be accessible to all borrowers, they will be best suited "*to those that already have a sustainability/transition strategy in place*".

Related to this, the SLLP Guidance has been expanded to address in further detail the question of access to the SLL market for those with "controversial sustainability issues", noting that while the SLL market is open to such borrowers, they may be required "*to provide additional transparency, including additional disclosures around the strategic importance of sustainability for the business*". This reflects existing market practice.

4.2 Updated guidance on sleeping SLLs

Sleeping SLLs, being loans which include the SLL mechanics but do not specify the KPIs and/or SPTs which bring those mechanics into operation, continue to be addressed in the SLLP Guidance although the definition of a sleeping structure has now been brought into line with practice to include where KPIs and/or SPTs are not set upfront (rather than just SPTs).

Perhaps also to better reflect market practice, the circumstances in which sleeping SLLs may be used has been somewhat relaxed. Instead of referring to the need for "exceptional instances", the SLLP Guidance now requires the borrower to make every reasonable effort to set the KPIs and SPTs pre-origination, but acknowledges that in "certain circumstances" the parties may agree to a sleeping structure.

The SLLP Guidance does, however, now require that borrowers (1) provide a clear rationale for why the KPIs and SPTs cannot be set pre-origination, (2) disclose their existing sustainability strategy to the lenders and (3) agree on a backstop date by which the KPIs and SPTs shall be agreed (subject to a maximum period of 12 months post-origination, which remains unchanged). The recommendation that the "awakening" of the sleeping SLL should require the consent of all of the lenders also remains unchanged, although further guidance has been provided as to the level at which a lower consent threshold should be set where all lender consent is not practicable.

4.3 Documentation and drafting

The SLLP Guidance has been updated to refer to the publication of the LMA's draft provisions for SLLs in May 2023 (discussed further in our Borrower's Guide to Sustainability-Linked Loan Terms and expected to be reviewed and updated by the LMA to reflect developments in market practice later this year). It also refers to other more recent guidance and documentation produced by the trade associations for the SLL market, including the LMA's and APLMA's template sustainability coordinator mandate letters.

5. Looking ahead

The crafting of globally applicable Loan Principles in support of a developing market requires a balance to be struck between robust guardrails on fundamental issues (and protecting against greenwashing) on the one hand, and sufficient flexibility for the product to adapt to changing technologies and science, as well as developments in the availability of data and impact reporting, on the other. It is also important to recognise that, on certain issues, there remain a range of views. Balancing all this is an ongoing challenge.

There will no doubt be some parties disappointed with the scope of the latest updates to the SLLP (and the other Loan Principles), concerned that particular points of detail have not been added and/or that the changes do not go far enough. With each iteration of the Loan Principles, however, the scaffolding supporting the integrity of the sustainable loan market becomes stronger and better understood. While the demand for further explanation and clarity from individual parties will continue, this year's review further clarifies the requirements of the Loan Principles and explains others, which is a positive step further forward.

We would also observe that in a year where a number of new reporting requirements are starting to land and/or are being adjusted (the EU Omnibus proposals, for example), it is even more important for the industry to tread carefully so as not to de-stabilise further growth in the sustainable loan market.

In the context of SLLs specifically, having updated the SLLP, the industry focus is turning to specific areas where market participants need more support and guidance to facilitate deployment. To this end, the LMA has a number of projects on the slate, perhaps most notably, an intention to produce tailored guidance on the application of the SLLP to SMEs (in the same way as it has done for the fund finance market). Making up 90% of businesses globally, SMEs are vital to global efforts to deliver the net zero transition. Industry-level guidance specifically focussed on the SME market, and the particular challenges SMEs face as compared to their larger counterparts is considered a crucial next step in supporting the growth of the sustainable finance market.

For further information on the matters covered in this briefing please contact one of the lawyers below or your usual Slaughter and May contact.

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