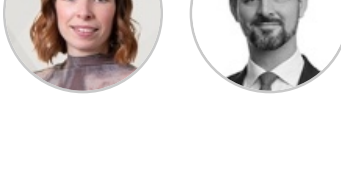


Transition loans explained: What to know about the LMA, APLMA and LSTA Transition Loans Guide

Norton Rose Fulbright



NORTON ROSE FULBRIGHT

United Kingdom | October 31 2025

Introduction

Transition finance has long been a topic of discussion in sustainable finance circles, yet until recently, it lacked a clear and consistent definition – particularly in the context of the loan market.

On 16 October 2025, the Loan Market Association (LMA), in collaboration with the Asia Pacific Loan Market Association (APLMA) and the Loan Syndications and Trading Association (LSTA), published the first official Transition Loan Guide (the Guide). The Guide is in the form of a voluntary, cross-jurisdictional framework and provides the clearest articulation to date of how transition finance should operate in loan markets.

For lenders and borrowers, particularly in high-emitting and hard-to-abate sectors, the Guide offers a pragmatic blueprint for structuring credible, verifiable and transparent financing aligned with net-zero pathways.

Purpose, scope and positioning

In its introduction, the Guide draws a sharp distinction between the economy-wide concept of “financing the transition” and transaction-level “labelled transition finance”. The latter concept, meaning transactions which are explicitly designated and structured to support companies achieve decarbonisation over time, is the subject of the Guide.

Related to this, the Guide sets out where transition loans fit in the wider sustainable finance toolkit. Since the emergence of formal guidance on sustainable finance, certain transactions and activities fall outside traditional ‘green’ classifications but are aligned with credible net-zero pathways and decarbonisation investments that are essential to transitioning high-emitting and hard-to-abate sectors. The Guide now looks to recognise such transactions as ‘transition finance’, plugging the classifications gap.

The Guide applies to two main structures: general corporate financing via sustainability-linked loans (SLLs) calibrated to entity-level decarbonisation outcomes, and use-of-proceeds “transition loans” for asset and project-level investments that drive real-economy emissions reductions. Hybrid structures that combine SLLs and use-of-proceeds elements are explicitly identified, reflecting the reality that borrowers may need both enterprise-level incentives and project-specific capital to execute transition strategies.

Core concepts of transition finance

The Guide specifies the following criteria as the core concepts of transaction finance:

- Must be “objective-aligned” towards an economy-wide transition in line with Paris Agreement-consistent trajectories;
- No lock-in of carbon-intensive assets or asset obsolescence occurs (i.e. do not unnecessarily prolong the life of carbon-intensive assets); and
- Must be benchmarked against science-based pathways where available, referencing sectoral and regional pathways and technology roadmaps.

For use-of-proceeds financing, the following additional safeguards should also be present:

- Transition activities or assets “Do No Significant Harm” (DNSH) to other environmental and social objectives;
- Assets and activities meaningfully contribute to decarbonation targets, quantitatively or qualitatively, over a given timeframe; and
- Financing, assets and activities should be made available in locations where low-carbon alternatives are technically or economically locally feasible, acknowledging the practical feasibility taking account of the specific borrower.

This framing squarely targets decarbonisation levers outside the “already-green” universe and emphasises integrity in both climate and broader sustainability outcomes.

Entity-level credibility: transition plans and indicators

The Guide places entity-level credibility at the centre of any transition financing. Borrowers should evidence a credible transition strategy through either “a transition plan or planning process, aligned with recognised frameworks,” or “a robust set of indicators that demonstrate alignment with science-based pathways”. How such strategy looks will vary from borrower to borrower: multinationals may break their strategy down based by region or sector while investment funds may split by portfolios. Any assets or projects should align with the borrower’s group’s overarching strategy for continuity and consistency.

Any transition plan should be based in the borrower’s factual scenario, including proposed actions and resources available, and cover strategy, implementation, metrics and targets, and governance. These components are referenced in the Transition Planning Taskforce Disclosure Framework which is global and publicly available.

Where a published plan is not available (for example, due to a lack of frameworks applicable to the borrower’s business or industry), evidence from climate disclosures or other suitable documentation can act as indicators. The Guide provides a non-exhaustive list of such indicators, including time-bound phase-out of high-emitting assets or sites; allocation of capital and/or operating expenditure to transition-aligned activities; adoption milestones for low-carbon technologies; Scope 1 and 2 coverage and, where material, Scope 3; and engagement across value chains. Where indicators are being used, the Guide encourages explicit articulation of dependencies and assumptions such as policy support, technology availability and market access.

Each plan and/or any indicators must be contextualised and their practicality assessed, ensuring such items are feasible and commercially possible in the Borrower’s reality and reflect relevant best market practice. As an example, the Guide notes that “shorter-term milestones may be appropriate where long-term detail is not yet feasible,” particularly for SMEs and emerging markets. This pragmatic stance is designed to widen access without diluting integrity, provided the direction of travel is Paris Agreement-aligned and transparently managed.

SLLs as a transition tool for general corporate financing

The role of SLLs as a core instrument for entity-level transition is re-affirmed within the Guide. Properly structured, transition-themed SLLs are an effective transition tool by incentivising delivery against material, ambitious sustainability objectives. Alongside the existing SLL guidance published by the LMA, APLMA and LSTA, the Guide emphasises two further structural imperatives.

Firstly, key performance indicators (KPIs) should specifically target the borrower’s emissions footprint: “KPIs should target material Scope 1, 2, and, where material, Scope 3 emissions, or credible proxies when direct measures are not feasible.” Proxies may include low-carbon capital expenditure or research and development allocations, product or physical carbon intensity, abatement impacts of key measures, and decommissioning timelines for high-emitting assets. KPI selection should consider lock-in risk and be benchmarkable against recognised sectoral pathways and just transition principles.

Secondly, sustainability performance targets (SPTs) must be calibrated with ambition and integrity: as stipulated by the LMA, APLMA and LSTA’s Sustainability-Linked Loan Principles (the SLL Principles), SPTs must go further than “business as usual” and regulatory baselines, be founded in science-based or policy benchmarks and robust governance. Transparent reporting and independent verification, also required under the SLL Principles, are essential to credibility. When underpinned by rigorous KPI selection, ambitious SPTs and robust reporting, SLLs can drive behavioural change and capital reallocation at the enterprise level in sectors that have not historically accessed green use of proceeds financing.

Use-of-proceeds transition loans: the Transition Loan Principles exposure draft

Addressing a critical gap, the Guide publishes an exposure draft of the Transition Loan Principles (the TLP), a dedicated framework for use-of-proceeds transition loans. Transition loans are defined as any loan or contingent facility “where the proceeds or an equivalent amount shall be exclusively applied to finance, re-finance or guarantee, in whole or in part, new and/or existing eligible Transition Projects ... and which are aligned to the five core components of the TLP but do not meet the categories for eligibility for Green Projects.” The TLP mirror the structure of the Green Loan Principles to support familiarity and consistency, while introducing transition-specific features.

The five core components of the TLP are as follows:

- Entity-level transition strategy: Borrowers must evidence a credible plan or indicators “aligned with science-based pathways.” This ensures that project-level financing is not pursued in isolation but “contributes meaningfully to the borrower’s overarching GHG emission reduction strategy”.
 - Use of proceeds: Transition Projects include assets, investments and other related and supporting capital and/or operating expenditures that are “not yet aligned with the goals of the Paris Agreement but contribute meaningfully to the decarbonisation of the real economy.” Projects should have substantial, clear and quantifiable reductions of GHG emissions within a specified timeframe” and may include capital expenditure, operating expenditure, research and development, early decommissioning and replacement. Eligible categories may be identified by reference to credible taxonomies and roadmaps.
 - Process for project evaluation and selection: Borrowers should anchor eligibility of Transition Projects to their sectoral pathways and taxonomies, demonstrate consistency with the borrower’s transition strategy and have robust internal governance. The TLP expects consideration of three tests:
 - first, alignment with recognised pathways and benchmarks, citing the IEA NZE or IPCC scenarios and relevant national roadmaps;
 - second, “absence of low-carbon alternatives” that are technically or economically feasible in the local context; where relevant, R&D for emerging solutions can qualify; and
 - third, environmental and social risk management to ensure DNSH, including biodiversity, water and pollution safeguards and just transition considerations.
- The TLP also requires explicit assessment of carbon lock-in risk, noting that interim lower-emission investments must be “time-bound, pathway-aligned, and justified by regional/technological constraints,” with consideration of asset lifetime, cumulative emissions, retrofit/repurposing potential and end-use emissions. Such assessment would cover the economic, technical, and contractual forces that keep high emitting assets in operation for years or decades, even when lower emission alternatives exist
- Management of proceeds: As with other labelled use-of-proceeds products, proceeds should be credited to a dedicated transition loan account or appropriately tracked by the borrower, with disclosure of any temporary treatment of unallocated balances.
 - Reporting: At least annually, borrowers should disclose allocations and any expected and/or achieved impact of a Transition Project, including methodologies and key assumptions. Forward-looking indicators, such as projected emissions reductions, capital expenditure and research and development allocations, and implementation timelines, are encouraged for longer-tenor loans. Aggregated reporting is acceptable where confidentiality or deal volume limits granularity, and public disclosure is encouraged where feasible. External review is encouraged pre- and, where relevant, post-transaction, leveraging existing disclosures for efficiency.

Interaction of entity and project-level credibility

A core theme of the Guide and the TLP is the reciprocal integrity between entity- and project-level credibility. Projects should be considered within the context of, and as contributors to, the borrower’s overall transition strategy and objectives. Likewise, credible projects serve as evidence of, and help to implement, that strategy, turning stated ambitions into tangible decarbonisation outcomes. This interaction strengthens risk management by reducing the likelihood of financing stranded assets which fail to integrate with company or group-wide level governance, targets and capital allocation.

For market participants, the message is pragmatic: use SLLs to drive entity-level outcomes; use transition loans to finance specific, pathway-aligned investments that measurably bend the emissions curve; and anchor both to transparent, science-based frameworks with robust reporting and independent assurance.

DNSH, just transition and lock-in: practical safeguards

The Guide elevates safeguards that have often been unevenly applied in transition narratives. DNSH requires that Transition Finance transactions do not materially undermine other environmental or social objectives The just transition lens is made explicit through references to labour rights, community health, inclusiveness and energy access/security.

On carbon lock-in, the Guide cautions that proceeds should not entrench high-emitting infrastructure and calls for transparent sunset clauses and phase-out plans where interim steps are unavoidable. These requirements align transition lending with broader sustainability integrity and help lenders manage reputational and policy risks.

Market evolution and next steps

The Transition Loan Principles are published as an exposure draft and are designed to be refined over a 6 to 12 month period based on market feedback prior to being issued in final form.

Implications for lenders and borrowers

For lenders, the Guide provides a defensible structure to scale capital into transition-critical activities while managing integrity risks. It formalises expectations for KPI/SPT design in SLLs, strengthens diligence for use-of-proceeds structures, and integrates DNSH and lock-in assessments into credit and reputation risk considerations.

For borrowers, particularly in emissions-intensive sectors, it offers a pathway to access labelled financing before activities are fully “green,” provided there is a credible plan, measurable impact and transparent reporting.

In short, the Guidance creates a common language and a workable set of guardrails to turn transition intent into investable, auditable financing at both the entity and project level.

Norton Rose Fulbright - Alex Collerton and David Milligan

Filed under

United Kingdom Banking Norton Rose Fulbright

Industries

Financial services banks

Popular articles from this firm

Make Work Pay - Employment Rights Bill consultation papers published.

Consultation on Enhanced Dismissal Protections for Pregnant Women and New Mothers

Government Consultation on Bereavement Leave Including Pregnancy Loss

The use of AI in legal judgments

Third-party funding in arbitration: Guidance from the Chartered Institute of Arbitrators

If you would like to learn how Lexology can drive your content marketing strategy forward, please email enquiries@lexology.com.

Professional development

Running a Real Estate Finance Transaction - From HOTs to Completion - Learn Live

MBL Seminars | 2 CPD hours
Online
5 November 2025

Financial Covenants in Loan Facility Agreements - An Introduction - Live at Your Desk - Learn Live

MBL Seminars | 3 CPD hours
Online
7 November 2025

Board Meetings & Governance - What the FCA Expects

MBL Seminars | 5 CPD hours
London
10 November 2025

View all

Seminars & Events

Lexology Live: Asia 2025

Lexology Live
Regal Hong Kong Hotel
13 November 2025

Navigating IP Frontiers

Liedekerke Wolters Waelbroeck Kirkpatrick
Antwerp, Belgium
21 November 2025

View all

Related practical resources

CHECKLIST

Recently updated

Checklist: Navigating DORA compliance: addressing practical post-implementation steps (EU)

HOW-TO GUIDE

Recently updated

How-to guide: Introduction to the UK financial services regulators (UK)

HOW-TO GUIDE

Recently updated

How-to guide: The general prohibition – beware the consequences of breach (UK)

View all

Related research hubs

United Kingdom

Banking

Resources

Daily newsfeed

Panoramic

Research hubs

Learn

In-Depth

Lexy: AI search

Scanner

Contracts & clauses

Lexology Index

Find an expert

Reports

Research methodology

Submissions

FAQ

Instruct Counsel

Client Choice 2025

More

About us

Legal Influencers

Firms

Blog

Events

Popular

Code of ethics

Lexology Academic

Legal

Terms of use

Cookies

Disclaimer

Privacy policy

Contact

Contact

RSS feeds

Submissions

Search Lexology

Q

Follow on X

Follow on LinkedIn