

EU Taxonomy

A foundation for an EU disclosure system on sustainability

Teneo Insights / March 2022



The EU Taxonomy represents the backbone of the sustainable finance strategy in Europe. It establishes criteria for green economic activities that should make a substantial contribution to at least one of the EU-defined environmental goals and avoid significant harm to the other goals (climate change mitigation, climate change adaptation, water conservation, pollution prevention, cyclicity and biodiversity).

While the Taxonomy is not a mandatory list and activities not included are not necessarily non-ESG friendly, it will put pressure on companies to ensure that their activities comply with the framework.

EU Taxonomy summary

The Taxonomy is a classification system that entered into force on 12 July 2020, establishing a list of environmentally sustainable economic activities. According to the [Taxonomy Regulation](#), economic activities are qualified as environmentally sustainable if they:

Julia Staunig

Senior Managing Director
Julia.Staunig@teneo.com

Tomasz Krawczyk

Director
Tomasz.Krawczyk@teneo.com

Ramona Visenescu

Consultant
Ramona.Visenescu@teneo.com

- a. Make a substantial contribution to at least one of the following six environmental objectives:
 - Climate change mitigation
 - Sustainable use and protection of water and marine resources
 - Transition to a circular economy
 - Pollution prevention and control
 - Protection and restoration of biodiversity and ecosystems
- b. Do no significant harm (DNSH) to the other environmental objectives
- c. Meet minimum safeguards (e.g., UN Guiding Principles on Business and Human Rights)
- d. Comply with the technical screening criteria that will be established by the European Commission in delegated acts

Specific provisions in the Taxonomy

The technical criteria of the Taxonomy are provided by the Commission through various adjacent legislative initiatives called delegated acts. The Commission has already published two delegated acts on the climate change mitigation and adaptation objectives, and on Article 8 of the Taxonomy (sustainability disclosure). Two more delegated acts have yet to be published: one including nuclear and natural gas as sustainable activities and another on the last four environmental objectives.

I. The Taxonomy delegated act on establishing the technical screening criteria on sustainable activities for climate change adaptation and mitigation objectives (“Climate Taxonomy delegated act”) offers the first set of technical criteria for defining the activities that substantially contribute to climate change mitigation and adaptation. It covers two of the six environmental objectives included in the Taxonomy and represents the economic

activities of roughly 40% of listed companies, which are responsible for almost 80% of direct greenhouse gas (GHG) emissions in Europe. The delegated act was officially approved on 13 December 2021 and entered into force in January 2022.

II. The delegated act related to the content, methodology and presentation of the information to be disclosed by both non-financial and financial undertakings

specifies how certain large companies that are required to publish non-financial information under the current Non-Financial Reporting Directive (NFRD) and the upcoming Corporate Sustainability Reporting Directive (CSRD) should disclose information on how and to what extent their activities are associated with the defined environmentally sustainable economic activities. This includes, in particular, what proportion of a company's total activities are sustainable, which can then be used for translation of environmental performance into financial variables with which to inform investors and the financial markets.

III. On the contentious issue of classifying natural gas and nuclear energy as sustainable economic activities, the Commission put forward the Taxonomy complementary delegated act proposal on 2 February 2022, specifically covering how economic activities in the energy sector contribute to decarbonisation. In this regard, the Commission defines the production of nuclear energy and natural gas activities as Taxonomy aligned (sustainable) if they comply with the technical screening criteria, such as safe nuclear waste disposal or meeting the threshold for lifecycle emissions in case of gas installations.

IV. The Commission should soon publish the delegated act on the other four environmental objectives, although the exact date is still unknown. This delegated act should apply to companies reporting from 1 January 2023 and will offer the set of technical

criteria for defining the activities that contribute substantially to:

- Sustainable use and protection of water and marine resources
- Transition to a circular economy
- Pollution prevention and control
- Protection and restoration of biodiversity and ecosystems

Finally, the Commission is also planning to make a decision this year on whether to adopt a **Social Taxonomy**. The Platform on Sustainable Finance, which advises the Commission on sustainable finance, recently published the Final Report on Social Taxonomy, which will inform the Commission's draft. According to the report, the Social Taxonomy should be built on the foundation of international norms and principles such as the Sustainable Development Goals (SDGs) and the UN Guiding Principles on Business and Human Rights. It should also be built on social objectives such as decent work, inclusive and sustainable communities and affordable healthcare and housing.

The EU Taxonomy Regulation and its interaction with reporting obligations for financial and non-financial sectors

While the EU Taxonomy is primarily a classification tool, it also has other functions such as shaping the EU sustainable finance strategy together with other legislative initiatives. The Taxonomy aims to support economic growth while reducing pressures on the environment and considering social and governance aspects.

In this regard, the EU Taxonomy is intertwined with other EU sustainable finance legislative initiatives, such as the CSRD and the Sustainable Finance Disclosure Regulation (SFDR), creating reporting obligations for companies and financial institutions. Under this legislation, investors marketing funds as

sustainable, as well as corporates required to publish non-financial information, are required to disclose the extent to which they have used the Taxonomy and the percentage invested in Taxonomy-eligible activities.

International developments

In the international arena, various countries have developed their own taxonomies for defining sustainable activities. In order to encourage dialogue and, where appropriate, coordination on the development and harmonisation of taxonomies between its members, the EU has created an International Platform on Sustainable Finance (IPSF). The IPSF was set up in October 2019 by the EU and the relevant authorities of Argentina, Canada, Chile, China, India, Kenya, and Morocco. Since then, Indonesia, Norway, Switzerland, the UK and New Zealand have also joined the IPSF.

The IPSF published the EU and China Common Ground Taxonomy in November 2021, which maps the overlapping 'green' activities identified in their respective taxonomies in detail and assesses the strength of the criteria applied by each. This was described as a milestone in ensuring comparability between the EU and Chinese taxonomies. The IPSF is planning to compare other taxonomies in the future.

Another project under development is the International Organization for Standardization (ISO)'s Taxonomy of green activities. Due to be launched in the first half of 2022, the ISO Taxonomy is a list of activities eligible for green financing. According to an initial draft, the Taxonomy will exclude nuclear energy, while natural gas is likely to be included. This Taxonomy follows the ISO's publication of standards for green bonds and loans in September 2021, which plan to use the Taxonomy to determine the eligibility of use of proceeds.

In September 2021, the Climate Bonds Initiative (CBI) also updated its Climate Bonds Taxonomy, with the aim to identify the assets, activities and projects needed to deliver a low-carbon economy. Its first Climate Bonds Taxonomy was published in 2013 and is regularly updated to remain relevant to the latest technological developments.

Other countries, such as Malaysia, South Africa, Mexico, the UK and Russia, have also developed green taxonomies or are in the process of developing them. Some countries are already looking at the EU Taxonomy as a benchmark to prepare their own.

The UK, for example, joined the IPSF and its UK Green Technical Advisory Group is currently reviewing the EU metrics to ensure they are compatible with the UK market.



Teneo is the global CEO advisory firm.

Teneo helps clients tackle their biggest reputation and business challenges. We work side-by-side with a company's CEO and senior executive team, providing bespoke advice and support based on an on-the-ground understanding of the client's specific business needs.

Our team's multi-faceted skillset and depth of experience offers our clients a level of support that is unmatched by any other advisory firm in the world.

Teneo combines expertise that includes not only corporate strategy, communications, research, crisis management, government and public affairs and investor relations, but also taps into the expertise provided by our other business services capital advisory, management consulting and risk advisory to offer comprehensive advisory to help CEOs run their businesses and solve for their biggest challenges.

Our strategic communications consultants are located across the globe, in 19 offices, spanning six continents, enabling us to offer clients a truly global perspective and on-the-ground support in a variety of locales.

teneo.com