

CONSULTATION RESPONSE

EUROPEAN COMMISSION: SUSTAINABLE FINANCE - OBLIGATION FOR CERTAIN COMPANIES TO PUBLISH NON-FINANCIAL INFORMATION

ARTICLE 8 TAXONOMY REGULATION DELEGATED ACT

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This consultation response represents the view of the PRI Association and not necessarily the views of its individual members.

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**United Nations
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INTRODUCTION TO THE PRI

The Principles for Responsible Investment (PRI) is the world's leading initiative on responsible investment. The PRI is now a not-for-profit company with over 4000 signatories (pension funds, insurers, investment managers and service providers) to the PRI's six principles with approximately US \$100 trillion in assets under management.

The PRI supports its international network of signatories in implementing the Principles. As long-term investors acting in the best interests of their beneficiaries and clients, our signatories work to understand the contribution that environmental, social and governance (ESG) factors make to investment performance, the role that investment plays in broader financial markets and the impact that those investments have on the environment and society as a whole.

The PRI works to achieve this sustainable global financial system by encouraging adoption of the Principles and collaboration on their implementation; by fostering good governance, integrity and accountability; and by addressing obstacles to a sustainable financial system that lie within market practices, structures and regulation.

ABOUT THIS CONSULTATION

As of 2022, financial and non-financial undertakings which are required to publish non-financial information pursuant to Article 19a or Article 29a of [Directive 2013/34/EU](#) (NFRD), will need to disclose the extent to which their activities are associated with economic activities that qualify as environmentally sustainable under the Taxonomy regulation. In particular, they must disclose:

- the proportion of their turnover derived from products or services associated with economic activities that qualify as environmentally sustainable; and
- the proportion of their capital expenditure and the proportion of their operating expenditure related to assets or processes associated with economic activities that qualify as environmentally sustainable.

The [draft delegated act](#) published by the European Commission on 7 May 2021 proposes a methodology and template for undertakings to do this. The PRI welcomes the opportunity to respond to the European Commission's consultation.

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INTRODUCTION

The Taxonomy represents a generational shift for responsible investment. It provides a practical tool to bridge the gap between international sustainability goals, like the Paris Agreement, and investment practice. Financial and non-financial undertakings' disclosures under this delegated act will help investors and companies to identify future growth opportunities, R&D needs, and required changes in business models in order to avoid stranded assets and future-proof their businesses. These disclosures will also play a crucial role in supporting Taxonomy disclosures for financial market participants under Articles 5 and 6 of the Taxonomy regulation. Beyond the mandatory disclosures, the Taxonomy provides a practical tool for investors' engagement and stewardship activities with companies by providing a common language to assess companies' transition plans and track environmental performance progress.

Starting in late 2019, over 40 investment managers and asset owners ([PRI Taxonomy Practitioner's Group](#)) worked with the PRI to implement the Taxonomy on a voluntary basis in anticipation of the upcoming regulation. The final report shares insights from the first comprehensive set of case studies around how to use the EU Taxonomy. The investors assessed Taxonomy alignment before many details of the final regulation were in place, and before widespread corporate reporting against the Taxonomy is available. The results highlighted some important implementation challenges, and the need for more guidance from policymakers and supervisors on how the Taxonomy should be implemented for different asset classes. Yet, the case studies demonstrate that the Taxonomy framework can be operationalised today, despite the challenges due to data availability and limited specific asset class guidance. The recommendations in this consultation response draw from these experiences and insights.

KEY RECOMMENDATIONS

The PRI welcomes the draft Article 8 delegated act (DA), as it provides much needed clarity to financial and non-financial undertakings preparing for their disclosures against the Taxonomy. Below are our main recommendations relating to the draft DA:

- **Ensure consistency between disclosure requirements and sustainable finance policies.** The final Article 8 DA must be coherent and aligned with the Article 5 and 6 Taxonomy disclosure requirements, as well as the Sustainable Finance Disclosure Regulation (SFDR) and the proposed new Corporate Sustainability Reporting Directive (CSRD). PRI strongly disagrees with the phase in approach of the draft DA as it is inconsistent with the Article 5 and 6 disclosure requirements and likely to decrease data accessibility for investors and confuse consumers.
- **Use appropriate timelines and avoid ambition drift.** The Commission should consider bringing the timeline of the review clause forward so the treatment of derivatives and other asset classes can be assessed sooner. The review clause must also provide more clarity on how it will enable disclosure requirements to keep up to date with future developments of the Taxonomy as well as other legislations and methodologies. This must be consistent with the approach taken for disclosures under Articles 5 and 6. In addition, the timeline of capex plans must be possible to extend beyond 7 years for certain projects (e.g. large-scale infrastructure) otherwise there is a risk of dis-incentivising investment in any long-term transition projects. To avoid any greenwashing or ambition drift, all non-financial undertakings should be encouraged and supported by the Commission to undertake regular progress reporting during the period of the capex plan. This will give investors more detail and clarity to enable them to also publish targets and more accurately estimate future Taxonomy alignment.

- **Remove unnecessary reporting requirements.** Financial undertakings should not have to report a breakdown of their numerators and denominators as described in Article 8(5) draft DA. This creates an unnecessary reporting burden and forgets the key purpose of the Taxonomy: to clearly and concisely detail alignment with sustainability objectives in order to increase capital flows, and accelerate the transition, towards a sustainable financial system. The PRI recommends a simpler approach for all financial reporting requirements, consistent with those under Articles 5 and 6 of TR. Assuming the final SFDR RTS uses the same approach as the draft proposal, financial undertakings under the Article 8 DA should simply disclose their Taxonomy alignment in the form of a pie chart for turnover, capex and opex.
- **Take a sensible approach to derivatives, sovereigns, and non-NFRD/CSRD activities.** All investments should be included in the denominator of financial undertakings' KPIs, even those that cannot be judged against the Taxonomy (i.e. sovereign bonds). Otherwise, there is a risk that the calculations for products containing a substantial proportion of such instruments become skewed. Investors need clarity that Taxonomy alignment disclosures give a complete and comprehensive picture of sustainability performance. The Commission should also allow voluntary disclosures, to include non-NFRD/CSRD companies in the numerators of financial-undertaking KPIs. Many non-NFRD/CSRD entities can often have Taxonomy aligned activities so in order for investor Taxonomy disclosures to be meaningful, they must be as comprehensive as possible.
- **Provide guidance and assurance.** The Commission should provide more guidance on minimum social safeguards disclosures e.g. by providing an explicit list of social criteria which undertakings can cross reference. Finally, we support the Commission's proposal to ensure that the CSRD has a robust system for assurance of sustainability-related reporting and call on the Co-Legislators to support this provision.

DETAILED RESPONSE

CONSISTENCY WITH OTHER SUSTAINABLE FINANCE POLICIES

The disclosures resulting from this delegated act (DA) must be clear, comparable, and meaningful. This is important to ensure a fully functioning sustainable finance disclosure framework. Financial market participants disclosing under Articles 5 and 6 of the Taxonomy regulation (TR) will rely on these disclosures. Therefore, there must be alignment between the final Article 8 DA and [RTS for investment product disclosures](#). Consistent treatment of asset classes in Taxonomy-alignment calculations will be essential to ensure a workable framework for both investors and corporates.

The Commission must also ensure alignment between sustainable finance initiatives beyond the TR, including the SFDR and proposed new Corporate Sustainability Reporting Directive (CSRD). We encourage EU institutions to continue existing efforts to explain how SFDR, the Taxonomy and current and future related RTSS, as well as the CSRD, will work together as a coherent framework for disclosure of sustainability risks and impact by investors and companies. Coherence between these different pieces of legislation will be crucial to ensuring that the Taxonomy disclosures are consistent and useful for end-investors.

PHASE IN APPROACH

Under the proposed amendments to the SFDR RTS, investors will have to make product-related Taxonomy disclosures relating to climate mitigation and adaptation technical screening criteria (TSC) from 1 January 2022. Investors will rely on the data disclosed by non-financial undertakings to do this. Therefore, the PRI does not support the phase-in approach detailed in Article 11 of the draft DA. Focussing on eligibility rather than alignment in the first year will:

- Make it harder for investors to access the data they need to make accurate and useful Taxonomy assessments.
- Bring confusion to disclosures between the two concepts of eligibility and alignment – eligibility does not indicate whether and activity is aligned with sustainability objectives. Eligible activities are those listed in the climate delegated act. These activities were prioritised because of their high risk of causing environmental harm¹.

Markets do need time to acclimatize to these new reporting requirements, but this phase-approach is not the solution; it brings confusion and inconsistency with reporting requirements under articles 5 and 6 of the TR. Instead, the Commission should take an approach consistent with the disclosure requirements under Articles 5 and 6 of the TR, requiring alignment disclosures from 2022, provided that it is recognised within the supervisory strategies that disclosures in the first few years will be on a best effort basis as data will not be fully available nor easily comparable.

REVIEW CLAUSE

The PRI agrees there is a need for a review clause (Article 10 draft DA), but we have some concerns:

- Delaying the review to 1 January 2025 seems to unnecessarily extend the time during which investors cannot claim sovereign bonds (for example) as green. The treatment of derivatives and other asset classes must also be assessed sooner to bring a more level playing field between investors.
- More clarity is needed on how this clause would enable disclosure requirements to keep up to date with future developments of the Taxonomy (e.g. the Taxonomy related product disclosure RTS, Taxonomy TSC delegated acts – both future climate change and adaptation TSC and TSC for the other 4 environmental objectives, proposed social taxonomy and significant harm taxonomy) as well as other legislations and methodologies (e.g. CSRD, IFRS SSB).

Article 9 of the draft DA states KPIs shall cover only the objectives of climate change mitigation and climate change adaptation until the TSC for the other environmental objectives are defined. Yet, the timeline between the publication of future or revised TSC in the Official Journal and their input into this DA is unclear. In the proposed amendments to the SFDR RTS, it states FMPs will have to consider the remaining 4 environmental objectives from 1 January 2023. Therefore, to ensure a consistent approach, this Article 8 DA must also follow the same timeline.

Finally, it is especially important that the Commission provides as much clarity and guidance as possible on how the TSC are likely to evolve to aid non-financial undertakings who have capex plans defined under the draft DA.

¹ See pages 10-14 of the [Technical Annex to the TEG Final Report on the EU Taxonomy](#), 2020.

KPIS FOR FINANCIAL UNDERTAKINGS

Derivatives and sovereigns

PRI agrees that derivatives should be excluded from the numerator (as stated in Article 8(2) draft DA), until there is further evidence on how they could be judged against the Taxonomy. Without specific guidance on how these financial instruments can be Taxonomy aligned, such disclosures would be too complex and could potentially be misleading to end-investors. We encourage an examination as to how derivative instruments could make a substantial contribution to environmental objectives, as defined by the Taxonomy.

However, we disagree with the Commission's proposal to exclude exposures to central governments and central banks from the denominator of KPIs of financial undertakings in Article 8(1) draft DA. All investments should be included in the denominator, even those that cannot be judged against the Taxonomy (i.e. sovereign bonds). Otherwise, there is a risk that the calculations for products containing a substantial proportion of such instruments become skewed.

We advise the Commission against seeking a compromise on this issue by only having taxonomy-eligible investments in the denominator. Eligibility does not indicate the sustainability of the activity itself (eligible activities are those listed in the climate delegated act. These activities were prioritised because of their high risk of causing environmental harm (see footnote 1)). Consider two investors both with EUR10m in taxonomy aligned activities and a total of EUR100m in AUM. These investors should be considered equally "green", even if investor A has EUR50m in eligible activities while investor B has EUR 20m in eligible activities. By having eligibility as the denominator investor A would have a 20% alignment score while investor B would have alignment of 50%. This is an unfair reflection on investor A.

Investors need clarity that Taxonomy alignment disclosures give a complete and comprehensive picture of sustainability performance. We encourage the Commission to further investigate and provide guidance on how these investments could be judged against the Taxonomy in the future. In terms of sovereign, sub-sovereign, supranational and government agency bonds, this could be developed in the context of a sovereign green bond methodology for the EU Green Bond Standard, but clarification is also needed for the non-use of proceeds bonds.

Overall, and most importantly, there must be consistency between the KPIs for disclosures under Articles 5&6 and Article 8. We recommend that KPI calculation methodologies in the Article 8 Delegated Act are aligned with the methodologies for investment product disclosures under the SFDR.

KPI breakdowns

PRI does not support the breakdown of financial reporting described in Article 8(5) draft DA. It creates an unnecessary reporting burden for financial undertakings and forgets the key purpose of the Taxonomy; to clearly and concisely detail alignment with sustainability objectives in order to increase capital flows, and accelerate the transition, towards a sustainable financial system. Providing a breakdown of NFRD and non-NFRD, derivative and non-derivative, EU and non-EU investments etc. is only likely to overwhelm and confuse consumers while adding little benefit to experts.

Furthermore, this approach has created inconsistencies within the reporting requirements. Despite the exclusion of non-NFRD undertakings from the numerator, under Annex III and IV asset managers will be required to disclose the proportion of Taxonomy alignment of non-NFRD companies (no

specification on how to do this is given on how asset managers could do this). The Commission must correct this and ensure a consistent approach for non-NFRD/CSRD undertakings throughout the DA.

The PRI recommends a simpler approach for all financial reporting requirements, consistent with those under Articles 5 and 6 of TR. Assuming the final SFDR RTS uses the same approach as the draft proposal, financial undertakings under the Article 8 DA should simply disclose their Taxonomy alignment in the form of a pie chart for turnover, capex and opex, delineated by transition and enabling activities and which environmental objective(s) is/are met. Any further breakdown is not recommended.

Non-NFRD/CSRD exclusion

Article 8(3) of the draft DA states KPIs of financial undertakings shall exclude the exposures to undertakings not subject to an obligation to publish non-financial information pursuant to Article 19a or 29a of Directive 2013/34/EU from the numerator. This will be reviewed by 1 January 2025.

The PRI is severely concerned that this means, at least in the short-term, all small, private, or non-EU companies will be discounted from financial undertakings' calculations as a matter of routine. The advantages of this clear-cut approach are outweighed by the negatives it brings for investors:

- Investors with non-EU and non-NFRD/CSRD assets will not be able to fully disclose their Taxonomy alignment. This may result in market disadvantages (e.g. they will also be ineligible for the upcoming Ecolabel)
- The Taxonomy will have less influence on global markets since there will be reduced incentive for dialogue on sustainability matters between investors and corporates beyond the EU. This may hinder the progress of global taxonomy and reporting alignment meaning investors with assets across the globe could struggle with diverging reporting requirements in future.
- Non-EU or non-CSRD companies will have no incentive to report. This will create an uneven playing field for the EU companies and reduce data availability for investors meaning investor decision-making processes will be less well-informed.
- It will introduce inconsistencies between reporting obligations across articles 5, 6 and 8 of the TR for financial market participants.

PRI encourages the Commission to reconsider this exclusion. Many non-NFRD/CSRD undertakings can have Taxonomy aligned activities. Therefore, it is important for investor Taxonomy disclosures to be as comprehensive as possible.

The three ESAs recommended that the Commission develop sector coefficient methodologies as a solution. Although this could be an improvement, it would only work in the case of turnover and it would mean financial undertakings would not be encouraged to actively seek Taxonomy alignment information for SMEs, private companies, or non-EU companies, instead relying on sector averages. We recommend the Commission instead allows voluntary disclosures from non-NFRD/CSRD companies to be included in the numerator of 'estimated alignment' KPIs, provided the financial undertaking gives a justification of the sources and methodologies used for the estimated data. We also encourage the Commission and/or ESAs to formalise a set of criteria and guidelines, as well as mandatory disclosure requirements for financial undertakings who choose to use proxies to ensure such estimations do not lead to greenwashing.

KPIS FOR NON-FINANCIAL UNDERTAKINGS

Capex plans

PRI agrees that the aims of the capex plan of a non-financial undertaking (either to expand the undertakings' Taxonomy-aligned activities or upgrade Taxonomy-eligible economic activities to Taxonomy-alignment) should be achieved within the plan's timeframe. We also welcome the clarity from the Commission that activities which already meet the TSC do not need a plan. However, the Commission should reconsider the 5-7 year timeline. Certain projects (e.g. large-scale infrastructure) may easily exceed 7 years from initial inception to completion, meaning the non-financial undertaking would not be able to claim the project as Taxonomy aligned. This risks dis-incentivising investment in any long-term transition projects and could cause discouragement as the timeline of such projects is often beyond the control of the non-financial undertaking and can easily vary dependent on project type and jurisdiction.

Non-financial undertakings working on such projects should be allowed a longer time period so their efforts to move towards Taxonomy alignment are recognised. To avoid any greenwashing or ambition drift their plans could be accompanied by mandatory mid-term targets. In fact, all non-financial undertakings should be encouraged and supported by the Commission to undertake regular progress reporting during the period of capex plan. Short, medium, and long-term target setting, accompanied by narrative disclosures, will give investors more detail and clarity to enable them to also publish targets and more accurately estimate future Taxonomy alignment. This should also improve dialogue between investors and investees helping forge stronger transition plans.

OVERALL POINTS FOR ALL KPIS

Members of the PRI Taxonomy Practitioner's group requested further guidance on compliance with minimum social safeguards. We recommend the Commission expand the disclosure requirements for minimum social safeguards from a simply yes/no tick box to an explicit list of social criteria which undertakings can cross reference.

The group also recommended the audit or assurance of Taxonomy-alignment corporate data. We support the Commission's proposal to ensure that the CSRD has a robust system for assurance of sustainability-related reporting and call on the Co-Legislators to support this provision.

The PRI has experience of public policy on sustainable finance policies and responsible investment across multiple markets and stands ready to further support the work of the European Commission to in developing effective technical standards for sustainable finance disclosures.

Any question or comments can be sent to policy@unpri.org.