Principles for Responsible Investment

INVESTOR BRIEFING

EU TAXONOMY

UPDATED APRIL 2022

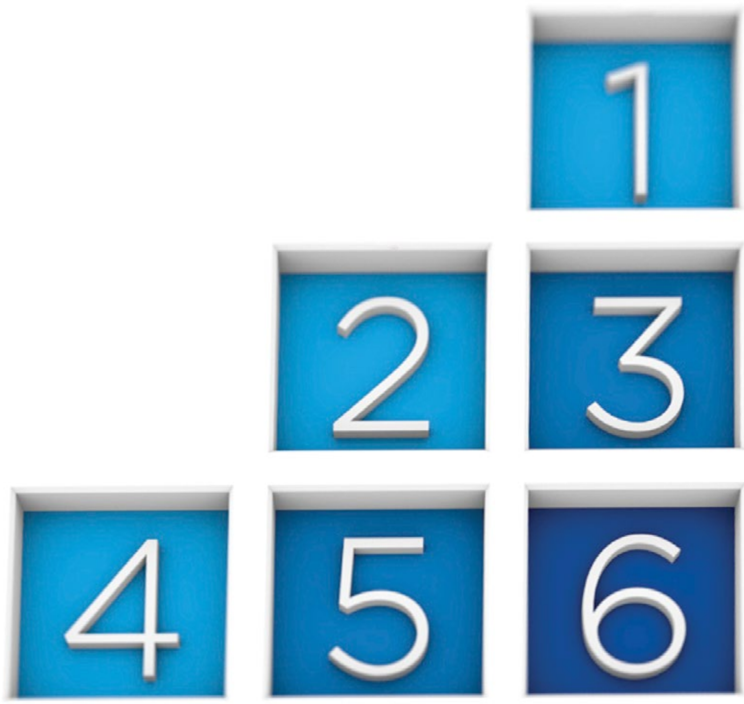
An investor initiative in partnership with UNEP Finance Initiative and UN Global Compact

THE SIX PRINCIPLES

PREAMBLE TO THE PRINCIPLES

As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:

1. We will incorporate ESG issues into investment analysis and decision-making processes.
2. We will be active owners and incorporate ESG issues into our ownership policies and practices.
3. We will seek appropriate disclosure on ESG issues by the entities in which we invest.
4. We will promote acceptance and implementation of the Principles within the investment industry.
5. We will work together to enhance our effectiveness in implementing the Principles.
6. We will each report on our activities and progress towards implementing the Principles.



PRI's MISSION

We believe that an economically efficient, sustainable global financial system is a necessity for long-term value creation. Such a system will reward long-term, responsible investment and benefit the environment and society as a whole.

The PRI will work 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 BRIEFING

This investor briefing is updated on a regular basis – please check the PRI briefings page for the most recent version.

This briefing provides:

- an introduction to sustainable taxonomies, which includes a definition of a sustainable taxonomy, explains its purpose and gives an overview of developments in sustainable taxonomies around the world;
- an overview of the architecture of the EU taxonomy for sustainable economic activities, covering its key components (such as scope and technical screening criteria) and functioning (conditions for being recognised as aligned with the taxonomy, related legislation etc);
- an outline of the state of play in the implementation of the taxonomy's provisions, including the development of the technical screening criteria (e.g., the adoption of the Climate Delegated Act and the recently proposed Complementary Climate Delegated Act covering gas and nuclear energy), disclosure requirements (e.g., those set out in the Disclosures Delegated Act and developments regarding the disclosure methodology for financial products) and the next steps in policy development.

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SUSTAINABLE TAXONOMIES: AN INTRODUCTION

This section provides a definition of a sustainable taxonomy, explains its purpose and outlines developments in sustainable taxonomies around the world.

DEFINITION AND PURPOSE

As defined in the PRI's and the World Bank's policy toolkit, a sustainable taxonomy is one of five[1] priority areas for sustainable investment policy.

BOX 1: DEFINITION AND PURPOSE OF A SUSTAINABLE TAXONOMY

A sustainable taxonomy is a classification system to help investors understand whether an economic activity is environmentally or socially sustainable and navigate the transition to a low-carbon, inclusive economy.

The purpose of a sustainable taxonomy is to set a common language between investors, issuers, project promoters and policy makers, and to help investors assess whether investments meet robust sustainability standards and are aligned with high-level policy commitments.

Sustainable taxonomies generally comprise:

- **Objectives**, which define the aims of the taxonomy.
- **Activity lists**, which detail eligible economic activities (i.e., those activities that can make a positive contribution to the objectives of the taxonomy). Taxonomies may also move beyond sustainable economic activities and include, for instance, economic activities that are needed to enable a transition towards social or environmental goals, or they may include economic activities that are inherently harmful: in such cases, the taxonomy should always maintain a clear distinction between the different types of economic activities.
- **Performance criteria**, which determine whether the eligible activities are aligned with the objectives of the taxonomy. Criteria should be defined for how economic activities can significantly contribute to the objectives of the sustainable taxonomy, as well as for ensuring that economic activities do no significant harm to any of its objectives. To be aligned with a sustainable taxonomy, an economic activity must significantly contribute to one its objectives, while doing no significant harm to any of the other objectives. The EU taxonomy framework includes such technical screening criteria.

Sustainable taxonomies provide a practical tool to bridge the gap between international sustainability goals, like the Paris Agreement, and investment practice:

- They enable investors to identify if, and to what extent, companies are engaged in sustainable activities and, through disclosure obligations and incentives, encourage investors to redirect capital flows towards such activities.

[1] The other four are corporate ESG disclosures; stewardship (engagement and voting); investors' duties to incorporate ESG-related considerations in their investment decision-making, to provide sustainability-related disclosures and to report on their ESG incorporation policies and performance targets; and national/regional sustainable finance strategies that encourage and enable the low-carbon transition and the delivery of the Sustainable Development Goals. For more information, see the PRI's and the World Bank's policy toolkit: How policy makers can implement reforms for a sustainable financial system.

- They help investors and companies identify future growth opportunities, R&D needs and changes in business models necessary to avoid owning stranded assets and to future-proof their businesses.
- They are a useful tool to support stewardship efforts. Investors and companies can use sustainable taxonomies to plan and report on their contribution to the transition to a low-carbon, inclusive economy.

SUSTAINABLE TAXONOMIES WORLDWIDE

The UN Department of Economic and Social Affairs and the International Platform on Sustainable Finance[2] have found that **over 20 jurisdictions have developed, are developing or are discussing the development of sustainable taxonomies. This briefing focuses only on the EU taxonomy of sustainable activities**. As sustainable taxonomies are developed worldwide, the PRI encourages convergence in their architecture at the international level to maximise their impact, considering the global nature of financial markets.

Local differences in performance thresholds may still exist as countries and regions face different challenges and transition pathways. In this context, it is essential that any sustainable taxonomy clearly defines its sustainability goals.

BOX 2: COMMON GROUND TAXONOMY

The International Platform on Sustainable Finance (IPSF) has a dedicated working group on taxonomies. This group, chaired by the EU and China, aims to harmonise the sustainable taxonomies currently used by its members. On 4 November 2021, the IPSF published a "Common Ground Taxonomy" (CGT) package consisting of:

- an overview of the methodology for identifying the commonalities and differences between the approaches of the EU taxonomy and the China Green Bond Endorsed Projects Catalogue;
- a CGT table, which provides activity-by-activity mapping and a high-level comparison of the detailed criteria in the EU taxonomy and in the China Green Bond Endorsed Projects Catalogue;
- a call for feedback – the PRI responded to this call, concluding that the CGT could be a useful tool for increasing the interoperability of taxonomies, on the condition that clarifications and improvements are made regarding its purpose, scientific basis, methodology and presentation of criteria.

[2] The International Platform on Sustainable Finance (IPSF) was set up by the European Commission in 2019. Its objective is to "scale up the mobilisation of private capital towards environmentally sustainable investments". The IPSF "therefore offers a multilateral forum of dialogue between policy makers that are in charge of developing sustainable finance regulatory measures to help investors identify and seize sustainable investment opportunities that truly contribute to climate and environmental objectives". The IPSF should not be confused with the Platform on Sustainable Finance, whose objective is to advise the European Commission on sustainable finance policies (see Box 4 for more information).

THE EU TAXONOMY ARCHITECTURE

This section outlines the key components (scope, technical screening criteria etc) and the functioning (conditions for being recognised as aligned with the taxonomy, related legislation etc) of the EU taxonomy. For more information about the implementation of the taxonomy's provisions, please see the "Implementation" chapter.

SCOPE OF THE EU TAXONOMY

The EU regulation on the establishment of a framework to facilitate sustainable investment, known as the Taxonomy Regulation, applies to:

- **Financial market participants** offering financial products in the EU (including occupational pension providers). Financial products subject to the Taxonomy Regulation are defined in the Sustainable Finance Disclosure Regulation as: a portfolio managed in accordance with Article 4(1) of Directive 2014/65/EU (MiFID II); an Alternative Investment Fund; an Insurance-based Investment Product; a pension product; a pension scheme; a UCITS fund (a mutual fund); or a Pan-European Personal Pension Product.
- **Large financial and non-financial undertakings** that are already required to provide a non-financial statement under the Non-Financial Reporting Directive (NFRD). Additional companies will be brought into scope via the proposed Corporate Sustainability Reporting Directive[3] amending the NFRD once it is approved by the European Council and the European Parliament. A dedicated delegated act has been adopted to detail disclosure requirements for large companies (see the "Recent developments" section lower down).
- **The EU and member states**. They are required to use the EU taxonomy when setting out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable.

Reporting requirements for financial market participants and large companies have applied since 1 January 2022. For more details regarding these requirements, please see the "Implementation" chapter of this briefing.

ECONOMIC ACTIVITIES ALIGNED WITH THE EU TAXONOMY

The EU taxonomy identifies sustainable economic activities. To be recognised as "taxonomy-aligned", an economic activity (referred to under NACE, the EU classification of economic activities) must meet three conditions:

- make a **substantial contribution to at least one of the six environmental objectives** identified in the EU Taxonomy Regulation: climate change mitigation; climate change adaptation; sustainable use and protection of water and marine resources; transition to a

[3] The Corporate Sustainability Reporting Directive, as the revised Non-Financial Reporting Directive (NFRD) is called, was proposed by the European Commission in April 2021 as an amendment to the existing corporate reporting requirements under the NFRD. This was the first step in the legislative process, and the proposal is now in the hands of the European Parliament and the European Council: both have adopted their respective positions, and negotiations to find a compromise between the two positions are ongoing. Once an agreement is reached between the institutions, which is expected in June at the earliest, the legislation will be published in the Official Journal – at which point it will enter into force. The application date for the new reporting requirements is still being negotiated.

circular economy; pollution prevention and control; and protection and restoration of biodiversity and ecosystems;

- do **no significant harm to any of the other environmental objectives**;
- **meet minimum social safeguards** consistent with the Guidelines for Multinational Enterprises from the Organisation for Economic Co-operation and Development and UN Guiding Principles on Business and Human Rights, including core International Labour Organization conventions.

TYPES OF ECONOMIC ACTIVITIES

The EU Taxonomy Regulation distinguishes between three different types of economic activities that contribute to one of the six environmental objectives:

- **"Substantial contribution" economic activities** – those that make a substantial contribution based on their own performance (e.g., renewable energy activities, which result in a low impact on the environment and have the potential to replace high-impact activities);
- **"Enabling" economic activities** – those that enable other activities to make a substantial contribution through their products or services (e.g., manufacturing of renewable energy hardware and installation of energy-efficient features in buildings)[4];
- **"Transitional" economic activities** – those for which low-carbon alternatives are not yet available and which have greenhouse gas emission levels that correspond to the best environmental performance in the sector or industry (e.g., best-in-class cement manufacturing)[5].

TECHNICAL SCREENING CRITERIA

The Taxonomy Regulation tasks the European Commission with developing delegated acts setting out "technical screening criteria" for determining which economic activities "significantly contribute" to one environmental objective while not doing "significant harm" to any of the other five environmental objectives.

[4] Under Article 16 of the Taxonomy Regulation, an enabling activity is one that enables other activities to make a substantial contribution to one or more of the six environmental objectives, provided that such enabling economic activity:

a) does not lead to a lock-in of assets that undermine long-term environmental goals, considering the economic lifetime of those assets;
b) has a substantial positive environmental impact, on the basis of life-cycle considerations.

[5] Under Article 10(2) of the Taxonomy Regulation, transitional activity is an economic activity for which there is no technologically and economically feasible low-carbon alternative and which supports the transition to a climate-neutral economy consistent with limiting the global temperature increase to 1.5°C above pre-industrial levels, including by phasing out greenhouse gas emissions, in particular emissions from solid fossil fuels, and where that activity:

a) has greenhouse gas emission levels that correspond to the best performance in the sector or industry;
b) does not hamper the development and deployment of low-carbon alternatives;
c) does not lead to a lock-in of carbon-intensive assets, considering the economic lifetime of those assets.

BOX 3: Adoption of delegated acts under the EU Taxonomy Regulation

Once an EU law is passed, it can be necessary to provide further details to ensure it is implemented as intended. In order to do this, the European Parliament and European Council can authorise the European Commission to adopt delegated acts.

Delegated acts are proposed by the Commission and are subject to a four-to-six-month scrutiny period during which the European Parliament and European Council can assess the proposal and decide to approve or reject it. Only when the European Parliament and European Council have both approved the delegated act does it enter into force through its publication in the Official Journal.

In December 2021, the EU adopted a delegated act for the climate mitigation and climate adaptation objectives of the EU taxonomy. Additional delegated acts are under development. For more details regarding these, see the "Implementation" chapter of this briefing.

THE BROADER ROLE OF THE EU TAXONOMY

The purpose of the EU taxonomy is to help investors identify and finance environmentally sustainable activities, as well as to report on the levels of those investments. Uncertainty over and concerns about implementing the EU taxonomy may often originate from misunderstandings about this. Notably:

- The EU taxonomy does not prohibit investment in any activity. It is a tool for identifying sustainable economic activities and directing financial flows towards these, but it is not prescriptive. In an FAQ on the taxonomy, the European Commission says: "Investors are free to choose what to invest in."
- As the Commission also says, if an economic activity is not addressed in a delegated act, that does not necessarily mean it is environmentally "unsustainable". At a later stage, the Commission will consider additional economic activities for inclusion in the taxonomy (e.g., agriculture and certain manufacturing activities). New activities, including transitional and enabling activities, may be added to the scope by amending delegated acts.
- The EU taxonomy is a living document that will be updated over time. The technical screening criteria will be subject to regular review[6].

The EU taxonomy does not contain investing requirements for investors – instead, through disclosure obligations, it is aimed at stimulating investment into sustainable economic activities and encouraging engagement with investees to facilitate the transition to a low-carbon economy. In the short term, investors will continue to finance all kinds of companies, including allocating capital to harmful economic activities if they wish to do so.

[6] As per Article 26(1) of the EU Taxonomy Regulation, the Commission is required to publish a report at least every three years evaluating the effectiveness of the application of the technical screening criteria for all the economic activities covered in delegated acts (substantial contribution, enabling and transitional), and the need for their revision. Article 19(5) adds a requirement for transitional activities: the Commission must review these at least every three years to ensure they "remain on a credible pathway consistent with a climate-neutral economy".

BOX 4: The Platform on Sustainable Finance

The Platform on Sustainable Finance is a permanent expert group established under Article 20 of the EU Taxonomy Regulation. It is currently chaired by Nathan Fabian (the PRI's Chief Responsible Investment Officer) and consists of 57 members and 11 observers drawn from financial market participants, businesses, academia and civil society.

The Platform on Sustainable Finance assists the Commission with the development of its sustainable finance policies, notably the further development of the EU taxonomy. Based on the mandate of Article 20 of the Taxonomy Regulation, the members and observers have four main tasks:

- advising the Commission on the technical screening criteria for the EU taxonomy, including on the usability of the criteria;
- advising the Commission on reviewing the Taxonomy Regulation and on covering other sustainability objectives, including social objectives, and activities that significantly harm the environment;
- monitoring and reporting on capital flows towards sustainable activities;
- advising the Commission on sustainable finance policy more broadly.

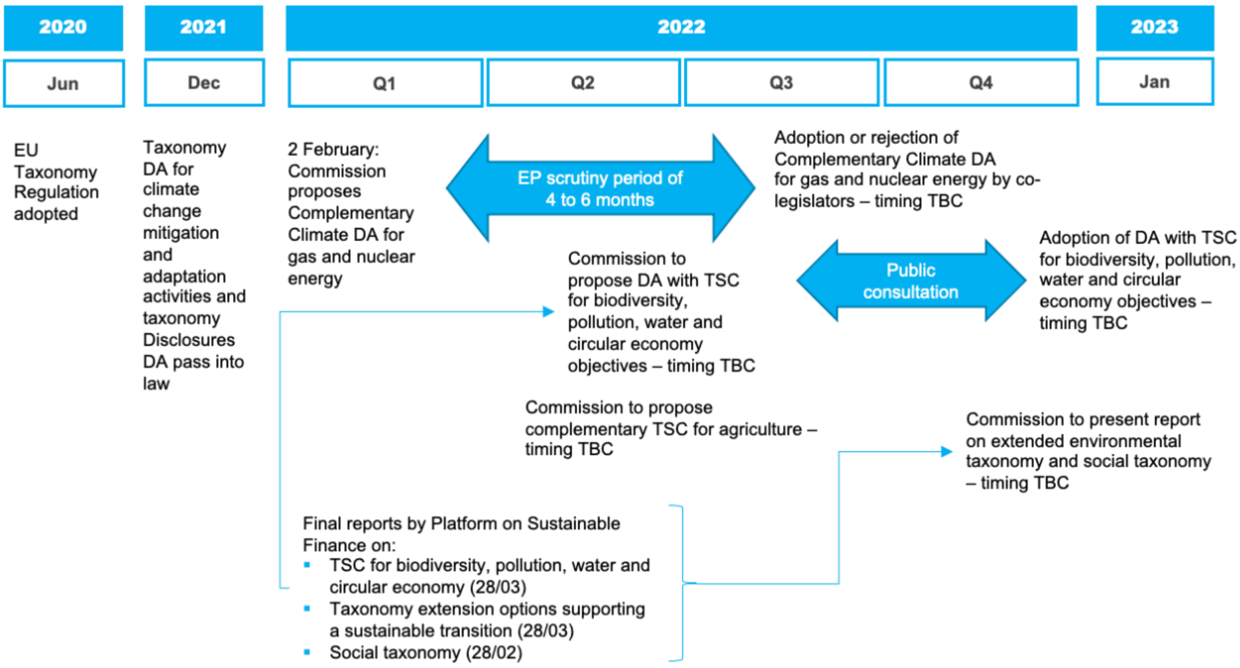
IMPLEMENTATION

This section covers the development of the technical screening criteria and reporting requirements for investors and companies. It also looks at the next steps in the development of the EU taxonomy.

TECHNICAL SCREENING CRITERIA

TIMELINE

The timeline below provides an overview of **key developments since the adoption of the EU Taxonomy Regulation, as well as the main next steps**. Further information on all the points can be found in the sections below.



Legend: DA = delegated act; EP = European Parliament; TSC = technical screening criteria

CLIMATE DELEGATED ACT

The Climate Delegated Act has applied since January 2022.

- The Climate Delegated Act contains technical screening criteria for almost 80 climate change mitigation activities and nearly 100 climate change adaptation activities, as well as criteria for determining whether that economic activity causes no significant harm to any of the other environmental objectives. This is a significant achievement for the Commission and the technical experts from the public, private and civil society sectors who have contributed to the criteria's development – most notably through the Technical expert group on sustainable finance and the Platform on Sustainable Finance. The technical screening criteria cover the economic activities of roughly 40% of EU-domiciled listed companies, in sectors that are responsible for almost 80% of direct greenhouse gas emissions in Europe[7].

- Agriculture, certain energy sectors – such as natural gas and nuclear energy – and certain manufacturing activities have not yet been included in the Climate Delegated Act. The European Commission has put forward a proposal for a Complementary Climate Delegated Act setting out technical screening criteria for gas and nuclear energy (see the next section for more information). The delegated act has to be approved by the European Council and European Parliament before it can enter into force.

The PRI has welcomed the adoption of the Climate Delegated Act as a significant achievement for the following reasons:

- As of 1 January 2022, investors and companies must report against the EU taxonomy to meet disclosure requirements under the Taxonomy Regulation as it interacts with the Sustainable Finance Disclosure Regulation and the Non-Financial Reporting Directive.
- The delegated act gives the market a clear environmental performance benchmark, setting a common language for investors, companies and other stakeholders.
- It provides the basis for other important legislative initiatives in the EU's sustainable finance strategy published in July 2021, which are linked to sustainability reporting, financial advice based on sustainability preferences, and labelling and standards for sustainability-themed financial products.

COMPLEMENTARY CLIMATE DELEGATED ACT (GAS/NUCLEAR ENERGY)

On 2 February 2022, the European Commission proposed the Complementary Climate Delegated Act. The delegated act includes technical screening criteria covering gas-fired power/cogeneration/district heating and cooling (henceforth "gas") and the construction/operation/life extension of nuclear power plants (henceforth "nuclear energy"). Gas and nuclear energy are included as "transitional activities" (see page 8 for the definition)[8].

The PRI has issued a statement on the proposed Complementary Climate Delegated Act. Key points raised are:

- If the delegated act is adopted by Parliament and Council, the EU taxonomy can no longer be considered the gold standard for a sustainability performance benchmark.
- The disclosure requirements proposed in the Complementary Climate Delegated Act would create additional implementation challenges for investors, potentially rendering the disclosures ineffective and leading to (unintended) greenwashing. The proposed rules would allow investors to distinguish their exposures to gas and nuclear energy from their other exposures to some extent. However, the Platform on Sustainable Finance has objected to the way that required performance indicators for investees are to be applied to derive investors' gas and nuclear exposures – the PRI supports the criticism. Moreover, there are questions over the application of the product-level reporting requirements outlined in Articles 5 and 6 of the

[7] See the fifth paragraph in a statement by the European Commission Communication: EU Taxonomy, Corporate Sustainability Reporting, Sustainability Preferences and Fiduciary Duties: Directing finance towards the European Green Deal.

[8] The inclusion of gas as a "transitional" activity means that the "significant contribution" technical screening criterion for the power sector of up to 100g CO2e/kWh was loosened for gas. That is, it would be permissible to emit more than that and still qualify as a sustainable economic activity under the EU taxonomy – specifically, gas activities would be allowed to produce up to 270g CO2e/kWh in direct greenhouse gas emissions. Whether or not the Complementary Climate Delegated Act is adopted, gas-fired power/cogeneration/district heating and cooling that emit less than 100g CO2e/kWh will be accepted as activities that significantly contribute to climate change mitigation, as per the adopted Climate Delegated Act. However, that level of emissions is uneconomical under present market conditions, due to the cost and technical feasibility of the options available.

Taxonomy Regulation to gas and nuclear investments, and uncertainty over their interaction with the entity-level requirements proposed in the Complementary Climate Delegated Act (which flesh out Article 8 of the Taxonomy Regulation).

- European institutions still have the opportunity to develop, outside of the EU taxonomy, a framework that recognises gas and nuclear energy as activities that can help reach net-zero emissions by 2050. For further information, please see the section on taxonomy extension on pages 15-16, as well as the PRI's position paper on the subject.

The Complementary Climate Delegated Act is now subject to a four-to-six-month scrutiny period by the European Council and European Parliament. If adopted, it will amend the Climate Delegated Act (see pages 11-12 for more information on the delegated act), and reporting will be due by 1 January 2023.

DELEGATED ACT ON BIODIVERSITY, POLLUTION, WATER AND CIRCULAR ECONOMY

The European Commission is still due to propose a delegated act for the four remaining environmental objectives (sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems).

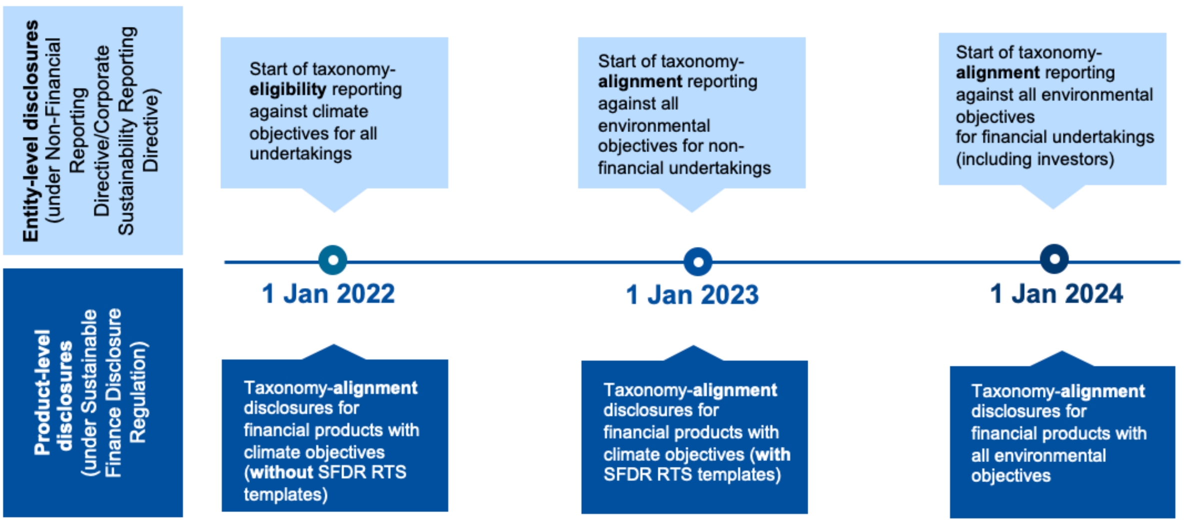
In March 2022, the European Platform on Sustainable Finance published its proposal for technical screening criteria – it will inform the European Commission's delegated act.

Reporting by investors against all technical screening criteria for the six environmental objectives of the EU taxonomy will become mandatory on 1 January 2023.

DISCLOSURE REQUIREMENTS

TIMELINE

The timeline below provides an overview of **current and future reporting requirements at entity and product levels under the EU taxonomy**, which amends disclosure obligations for investors (under the Sustainable Finance Disclosure Regulation) and non-financial corporations (under the future Corporate Sustainability Reporting Directive). Further information on all the points can be found in the sections below.



Legend: SFDR = Sustainable Finance Disclosure Regulation; RTS = Regulatory Technical Standards

ENTITY LEVEL: DISCLOSURES DELEGATED ACT

The Disclosures Delegated Act details entity-level reporting requirements for undertakings covered by Article 8 of the EU Taxonomy Regulation – namely, undertakings that fall into the scope of the Non-Financial Reporting Directive, set to be revised by the Corporate Sustainable Reporting Directive.

The Disclosures Delegated Act distinguishes between "taxonomy-eligible" and "taxonomy-aligned" economic activities:

- A taxonomy-eligible activity is defined in the act as "an economic activity that is described in the delegated acts [detailing the Taxonomy Regulation] … irrespective of whether that economic activity meets any or all of the technical screening criteria laid down in those delegated acts".
- In contrast, taxonomy-aligned economic activities do meet said technical screening criteria. Hence, they represent a much smaller share of an entity's total economic activities than taxonomy-eligible activities.

The Disclosures Delegated Act has introduced phased reporting requirements:

- As of 1 January 2022, all undertakings must disclose what share of their total activities is taxonomy-eligible. Reporting is restricted to the EU taxonomy's climate objectives (as the other four environmental objectives have not yet been covered in a delegated act).
- From 1 January 2023, non-financial undertakings will have to disclose what share of their total activities is taxonomy-aligned. Reporting will cover all six environmental objectives (as a delegated act for the four outstanding objectives will be proposed and, presumably, adopted by then).
- From 1 January 2024, financial undertakings will have to do the same.

Article 8 of the EU Taxonomy Regulation specifies the key performance indicators (KPIs) related to turnover, capital expenditure and operating expenditure that *non-financial* undertakings must disclose.

However, these indicators are not appropriate for demonstrating to what extent the economic activities of *financial* undertakings that fall under the scope of Article 8 are taxonomy-aligned. The Disclosures Delegated Act therefore clarifies that financial institutions must disclose KPIs that relate to the proportion of taxonomy-aligned economic activities in their financial activities and provides detailed requirements for different types of investors:

- **Investment firms** are required to disclose a KPI for their core investment dealing-on-own-account activities and a KPI for services and activities other than dealing on own account.
- **Asset managers** must report the proportion of taxonomy-aligned investments out of all covered assets that they manage in both collective and individual portfolios, in value terms.
- The KPI for **insurers and reinsurers** is the weighted average of investments directed at funding, or associated with, taxonomy-aligned activities. It should be shown both as a percentage of total investments and in absolute monetary units.

The European Commission has published an FAQ on the Disclosures Delegated Act. The Platform on Sustainable Finance has also published guidance on voluntary entity-level disclosures in line with the EU taxonomy.

FINANCIAL PRODUCTS: DISCLOSURE METHODOLOGY

In October 2021, the European Supervisory Authorities published draft Regulatory Technical Standards for EU taxonomy-related disclosures for financial products. These Regulatory Technical Standards are directly linked to the requirements set out in the Sustainable Finance Disclosure Regulation.

The Sustainable Finance Disclosure Regulation distinguishes between financial products that promote environmental and/or social characteristics (Article 8), those that have sustainable investment as their objective (Article 9) and all other products (loosely known as Article 6 products after the article that, in fact, applies to all financial products).

The EU taxonomy is the central tool for assessing the sustainability claims made under the Sustainable Finance Disclosure Regulation:

- Taxonomy disclosures will apply to a subset of Article 8 and 9 products.
  - For investments that are part of Article 8 products, only those that are "sustainable investments" (as defined in the Sustainable Finance Disclosure Regulation) with environmental objectives are in scope.
  - With regard to Article 9 products, only those that invest in economic activities that contribute to environmental objectives are in scope.
  - For all those investments, financial market participants must disclose how and to what extent the taxonomy has been used to determine the sustainability of the underlying investments, the environmental objective(s) to which the fund contributes and the percentage of the underlying fund that is taxonomy-aligned.
- Products to which taxonomy disclosures do not apply must be accompanied by the following statement: "The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities."
- Out-of-scope funds can elect to disclose against the EU taxonomy.

The draft Regulatory Technical Standards published by the European Supervisory Authorities detail what these taxonomy disclosures should cover and how they should be presented in pre-contractual and periodic documents. However, they have not yet been adopted:

- The formal adoption of the Regulatory Technical Standards by the European Commission is expected later this year, and their application has been deferred to 1 January 2023.
- This raises questions over the application of specific EU taxonomy-related product disclosures (under Articles 5 and 6 of the Taxonomy Regulation), which have applied since 1 January 2022
- The European Supervisory Authorities have issued a supervisory statement on the application of the Sustainable Finance Disclosure Regulation, providing further guidance on the disclosure requirements related to the EU taxonomy.

Please see our investor briefing on the Sustainable Finance Disclosure Regulation for more information about the disclosure requirements it introduces and the EU taxonomy disclosures relating to it.

EXTENDED ENVIRONMENTAL TAXONOMY AND SOCIAL TAXONOMY

Article 26(2) of the EU Taxonomy Regulation tasks the Commission with publishing a report on the provisions necessary to extend the scope of the regulation to:

- economic activities that have no significant impact on environmental sustainability, and economic activities that significantly harm environmental sustainability – this is more commonly known as "the extended environmental taxonomy";
- economic activities that cover other sustainability objectives, such as social objectives – this is more commonly known as "the social taxonomy".

The European Commission will use the work by the Platform on Sustainable Finance as an input into its report. The PSF released its final report on the creation of a social taxonomy on 28 February and its final report on the extended environmental taxonomy on 29 March.

- A social taxonomy would enable investors to identify companies that make a substantial contribution to one of three social objectives: decent work (including for value-chain workers); adequate living standards and well-being for end-users; and/or inclusive and sustainable communities and societies.
- An extended environmental taxonomy would cover four other types of economic activities classified as follows: unsustainable performance requiring an urgent transition to avoid significant harm; intermediate (or “amber”) performance; unsustainable, significantly harmful performance where urgent, managed exit/decommissioning is required; and low environmental impact (“LEnvI”) activities.

There is currently no clear timeline for the publication of the report by the European Commission.

THE PRI AND THE EU TAXONOMY

This section covers the links between the EU taxonomy and the PRI's six Principles, the role the PRI has played in the development of the taxonomy framework and how the PRI has engaged with its signatories.

As the world's leading proponent of responsible investment, the PRI works towards creating a sustainable global financial system. Sustainable taxonomies directly link to the Principles the PRI promotes. Specifically:

Principle 1: We will incorporate ESG issues into investment analysis and decision-making processes	Sustainable taxonomies will help investors develop financial products that contribute to the transition to a sustainable economy and will enable them to report on the environmental or social performance of these products in a transparent and comparable way. This will, among other things, encourage investment that is aligned with the Paris Agreement.
Principle 2: We will be active owners and incorporate ESG issues into our ownership policies and practices.	Sustainable taxonomies set clear performance criteria for investee companies, allowing investors to plan their own contributions to a sustainable economy. To execute these plans and shift corporate business models, investors will have to engage with their investees, supported by the information non-financial corporations will also have to disclose.
Principle 3: We will seek appropriate disclosure on ESG issues by the entities in which we invest.	The EU taxonomy is an example of a framework that requires corporate as well as investor disclosures. It will also lead investors to engage further with investees to obtain the ESG data they need for their own disclosures.
Principle 6: We will each report on our activities and progress towards implementing the Principles.	Disclosure frameworks, such as that set out in the EU Taxonomy Regulation, will allow retail investors and other stakeholders to assess the alignment of financial products with sustainability standards and high-level policy commitments such as the Paris Agreement.

The PRI plays an important role in the development of the EU taxonomy. As a contributor to the High-level expert group on sustainable finance and a member of the Technical expert group on sustainable finance, the PRI helped shape the EU Taxonomy Regulation and the technical screening criteria. With the PRI's Chief Responsible Investment Officer, Nathan Fabian, chairing the Platform on Sustainable Finance, the PRI can continue to provide expert advice on behalf of our signatories and in support of scientific expertise.

The PRI works closely with its signatories on the EU taxonomy:

- In late 2019, the PRI organised a Taxonomy Practitioners Group in which investors, based both in and outside the EU, talked about their tools and experiences to highlight, and help overcome, barriers to compliance with the requirements of the EU taxonomy. The PRI published a report summarising the findings of 35 case studies in September 2020, including recommendations from the practitioners group to policy makers and supervisors who would oversee the implementation and further development of the taxonomy.
- In 2021, the PRI undertook further interviews with 11 members of the Taxonomy Practitioners Group, leading to a follow-up publication in April 2022. The report aims to promote knowledge-

sharing in the responsible investment industry by highlighting examples of advanced practice; support collective problem-solving by outlining common implementation challenges and possible solutions; and encourage policy makers and supervisors to provide additional guidance to financial market participants by putting a spotlight on the main implementation challenges currently faced by investors.

FURTHER RESOURCES

OFFICIAL EU RESOURCES

- EU Taxonomy Regulation
- Climate Delegated Act
- Complementary Climate Delegated Act
- Disclosures Delegated Act
- Draft Regulatory Technical Standards regarding EU taxonomy-related disclosures for financial products
- European Commission FAQ: What is the EU Taxonomy and how will it work in practice?
- European Commission FAQ: What is the EU Taxonomy Article 8 delegated act and how will it work in practice?
- Platform on Sustainable Finance: Platform considerations on voluntary information as part of Taxonomy eligibility reporting

PRI RESOURCES

- PRI statement on Climate Delegated Act
- PRI statement on Complementary Climate Delegated Act
- PRI 2020 Taxonomy Practitioners Group report and case studies
- PRI Taxonomy Practitioners Group 2022 report

ADDITIONAL RESOURCES

- Series of webinars on the EU Taxonomy by Platform on Sustainable Finance

GLOSSARY

- **Corporate Sustainability Reporting Directive:** The Corporate Sustainability Reporting Directive, as the revised Non-Financial Reporting Directive is called, was proposed on 21 April 2021 as an amendment to the existing corporate reporting requirements under the Non-Financial Reporting Directive. The types of corporates that must make disclosures under the EU taxonomy are determined by the Non-Financial Reporting Directive but will change if the Corporate Sustainability Reporting Directive is approved.
- **Delegated act:** The EU Taxonomy Regulation tasks the European Commission with developing delegated acts for the six environmental objectives covered by the regulation. The delegated acts detail the "technical screening criteria" that determine which economic activities "significantly contribute" to one environmental objective while not doing "significant harm" to any of the other five environmental objectives. So far, one delegated act – for climate mitigation and climate adaptation – has been adopted. Technical screening criteria for the remaining four environmental objectives are currently under development. In addition, the EU has adopted the Disclosures Delegated Act, which details entity-level reporting requirements for entities covered by Article 8 of the Taxonomy Regulation.
- **"Do no significant harm":** This is the founding principle of the European Green Deal and is central to the EU Taxonomy Regulation. To be aligned with the EU taxonomy, an economic activity must not do significant harm to any of the six environmental objectives.
- **European Supervisory Authorities:** These are the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA). The European Supervisory Authorities were established in 2010 to advise the Commission on the adoption of so-called level 1 and 2 regulatory measures, and to issue guidelines on the implementation of the rules. They are also responsible for preparing "technical standards" – a particular category of level 2 measures submitted to the Commission, e.g., the Regulatory Technical Standards for the Sustainable Finance Disclosure Regulation and for the EU taxonomy disclosures at product level.
- **NACE:** Nomenclature statistique des activités économiques dans la Communauté européenne, or NACE, is a classification of economic activities in the EU.
- **Platform on Sustainable Finance:** The Platform on Sustainable Finance is a permanent expert group of the European Commission that has been established under Article 20 of the Taxonomy Regulation. The Platform assists the Commission with developing its sustainable finance policies, notably the further development of the EU taxonomy. It comprises appointed members from a wide range of sectors, including industry, academia and civil society. Nathan Fabian, Chief Responsible Investment Officer at the PRI, chairs the Platform on Sustainable Finance.
- **Regulatory Technical Standards:** These are technical standards prepared by a European Supervisory Authority. Their purpose is to further develop and specify the rules in the basic legislative act. Regulatory Technical Standards are usually then adopted by the European Commission as a delegated act or regulation.
- **Sustainable Finance Disclosure Regulation (SFDR):** The EU taxonomy complements the SFDR. For more information see our investor briefing.
- **Technical expert group on sustainable finance:** This group was set up by the European Commission in July 2018 to aid the development of, among other things, the technical screening criteria for the EU taxonomy, as well as the EU Green Bond Standard. The group consisted of 35

members from civil society, academia, corporates and the financial sector, as well as additional members and observers from EU and international public bodies. The group finished its work in September 2020.

- **Technical screening criteria:** These set thresholds that an economic activity must reach to qualify as substantially contributing to a certain environmental objective and doing no significant harm to any of the other five environmental objectives. The first set of technical screening criteria was published in the Climate Delegated Act. Draft technical screening criteria for the remaining four environmental objectives were submitted to the Commission by the Platform on Sustainable Finance in March.

The Principles for Responsible Investment (PRI)

The PRI works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a menu of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

More information: www.unpri.org

PRI Principles for Responsible Investment

The PRI is an investor initiative in partnership with UNEP Finance Initiative and the UN Global Compact.

United Nations Environment Programme Finance Initiative (UNEP FI)

UNEP FI is a unique partnership between the United Nations Environment Programme (UNEP) and the global financial sector. UNEP FI works closely with over 200 financial institutions that are signatories to the UNEP FI Statement on Sustainable Development, and a range of partner organisations, to develop and promote linkages between sustainability and financial performance. Through peer-to-peer networks, research and training, UNEP FI carries out its mission to identify, promote, and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.

More information: www.unepfi.org

FINANCE UNEP INITIATIVE

United Nations Global Compact

The United Nations Global Compact is a call to companies everywhere to align their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption, and to take action in support of UN goals and issues embodied in the Sustainable Development Goals. The UN Global Compact is a leadership platform for the development, implementation and disclosure of responsible corporate practices. Launched in 2000, it is the largest corporate sustainability initiative in the world, with more than 8,800 companies and 4,000 non-business signatories based in over 160 countries, and more than 80 Local Networks.

More information: www.unglobalcompact.org

United Nations Global Compact