

FACT SHEET

Be ready for the EU Taxonomy



On 1 January 2022, the first part of the European Taxonomy Regulation came into force. This Regulation sets out the sustainable economic activities to be reported on by businesses, known as the EU Taxonomy. Investments and activities must meet certain criteria to qualify as 'green'. This will promote transparency, combat 'greenwashing' and steer capital towards sustainable investments. But what exactly is the EU Taxonomy, and what businesses are required to report on it and when?

EU Taxonomy as a universal language for sustainable activities

The EU Taxonomy has been introduced by the European Commission as a common dictionary for defining and identifying sustainable economic activities. It is a universal language for businesses, investors, financial institutions and legislators. The EU Taxonomy is meant to ensure that businesses understand and communicate how 'green' their

activities are. Green activities are classified on the basis of the existing European activity coding system, known as the NACE codes. NACE represents the (industrial) classification system of the strategic classification of economic activities in the European Union.

The EU Taxonomy has been supplemented with technical screening criteria (TSC), which describe definitions and methods for identifying sustainable activities. The EU Taxonomy identifies six environmental objectives:

- ▶ Climate change mitigation;
- ▶ Climate change adaptation;
- ▶ The sustainable use and protection of water and marine resources;
- ▶ The transition to a circular economy;
- ▶ Pollution prevention and control;
- ▶ The protection and restoration of biodiversity and ecosystems.

Formally adopted in June 2021, the EU Taxonomy sets out the TSC for the first two of the six environmental objectives, which are in force for the financial year 2021. The TSC for the other objectives will follow in 2022. In short, while not all requirements and criteria are known yet, they will eventually impact many businesses. This publication explains what businesses are (or will be) in scope of the EU Taxonomy, what obligations exist and what steps your business can take today to meet them.



When is a business required to report?

Not every business falls within the scope of the EU Taxonomy. From 1 January 2022, the EU Taxonomy is mandatory for all portfolio managers, banks, insurance companies and (non-financial) public interest entities having in excess of 500 employees (known as large PIEs).

The European Taxonomy Regulation (2020/852/EU) thus dovetails with the criteria of the Non-Financial Reporting Directive (NFRD). In the Netherlands, the NFRD (Directive 2014/95/EU) has been implemented in the Non-Financial Disclosure Decree (*Besluit bekendmaking niet-financiële informatie*), referred to in Article 2:391(5) of the Dutch Civil Code.

The introduction of the Corporate Sustainability Reporting Directive (CSRD) will expand the scope of the Taxonomy Regulation. Whereas the NFRD applies only to PIEs having in excess of 500 employees, the CSRD considerably enlarges the scope of undertakings required to disclose information on how they deal with matters of environmental pollution, corporate social responsibility, human rights and diversity. The CSRD will apply to all listed undertakings, PIEs and undertakings qualifying as large. Large undertakings are undertakings exceeding on the balance sheet date the limits of at least two of the three following criteria:

- ▶ In excess of 250 employees;
- ▶ Turnover in excess of € 40 million;
- ▶ Balance sheet total in excess of € 20 million.

The CSRD is scheduled to come into force as from the financial year 2023. It is still unclear at present whether the CSRD will indeed take effect then or whether its introduction will be postponed to 2024. Regardless of any postponement, it would be unwise to delay getting started with the CSRD. This will be explained in more detail below at 'Get started with the EU Taxonomy well in advance'.

As the CSRD also links up to the EU Taxonomy, large undertakings that are not currently required to comply with the EU Taxonomy may be so required as from 2023.

Reporting requirements for large PIEs in 2021

On 6 July 2021, the Delegated Act supplementing Article 8 of the Taxonomy Regulation (hereinafter: 'Delegated Act') was adopted by the European Commission. In concrete terms, this means that already for the 2021 financial year, large PIEs are required to comply with the EU Taxonomy as well as the requirements in the Delegated Act.

This Delegated Act specifies the content, methodology and presentation of information to be disclosed by financial and non-financial undertakings on to what extent their business, investment or lending activities are associated with environmentally sustainable economic activities, as defined in the Taxonomy Regulation. This means the following:

- ▶ Non-financial undertakings must disclose certain performance of the past financial year ('eligibility'). This refers to the proportion of their turnover, capital and operational expenditure associated with 'environmentally sustainable economic activities'. The Taxonomy Regulation and the Delegated Act define how this should be construed.
- ▶ Financial undertakings are required to disclose the proportion of environmentally sustainable economic activities in their overall financed or invested assets. This applies mainly to large banks, portfolio managers, investment firms and insurance and reinsurance companies.

For the financial year 2021, large PIEs are only required to disclose Taxonomy eligible and Taxonomy non-eligible economic activities ('eligibility'). This means that economic activities described in the Delegated Act must be disclosed, regardless of whether they meet one or all of the TSC.

From 1 January 2023 – i.e. for the 2022 financial year – they must establish whether the Taxonomy eligible activities meet the TSC in place (alignment).

This requirement follows a year later, i.e. for the 2023 financial year, for financial undertakings. We recommend not to wait too long with identifying eligible economic activities and checking to what extent these activities meet the TSC.

The Taxonomy methodology

In summary, the EU Taxonomy effectively follows a six-step process:

1. Determine whether and from when the undertaking falls within the scope of the EU Taxonomy.
2. Identify the activities conducted by the undertaking that could be aligned, using the NACE codes set out in the EU Taxonomy. If the activity is not included, it is not a green activity according to the Taxonomy and is not eligible.
3. For each identified activity, verify whether it contributes substantially to the environmental objective – in other words, whether it meets the criteria established for each environmental objective, e.g. solar panel energy generation <100 g CO₂/kWh.
4. Verify that the 'DNSH' criteria are being met; these 'Do No Significant Harm' criteria have been included to ensure that a green activity for a specific environmental objective does not significantly harm the other environmental objectives.
5. Conduct due diligence to avoid any violation of the social minimum safeguards stipulated in the EU Taxonomy.
6. Calculate alignment of green activities with the EU Taxonomy and prepare disclosures.

Executing these steps also raises some practical issues for organisations in implementing the Taxonomy, such as:

- ▶ How can alignment with existing processes and procedures within the organisation be ensured?
- ▶ What can the organisation do to adhere to the TSC yet to be issued to ensure that these new requirements will be met on time?
- ▶ How will the required data be collected (and will this require modification of the existing IT infrastructure)?
- ▶ Who within the organisation will be responsible for compliance with and further monitoring of the Taxonomy Regulation?

2022	
<p>TAXONOMY ELIGIBILITY</p> <p>Which activities can potentially contribute directly to one of the six objectives?</p>	<p>TAXONOMY ALIGNMENT</p> <p>Technical screening criteria</p> <p>Substantial contribution Which business activities contribute to one or more of the environmental objectives?</p> <p>'Do no significant harm' criteria Which business activity causes no significant harm to any of the other environmental objectives?</p>
2021	

Get started with the EU Taxonomy well in advance

The importance of starting the EU Taxonomy implementation process well in advance cannot be stressed enough.

This is why:

1. Large PIEs are required to report on the 2021 financial year based on Article 8 of the Delegated Act. Accordingly, periodic reports published after this date must contain the information required. Large PIEs should therefore already have started their reporting.
2. Large undertakings that will fall within the scope of the CSRD will also be subject to the EU Taxonomy. Reporting on 2023 (and possibly 2024) may still seem a long way off, but do not underestimate the investments in expertise and information requirements necessary to meet the requirements.

3. Banks or other financiers may request information on sustainable activities from (smaller) companies. Banks need this information to assess whether the company complies with the EU Taxonomy. This may make it easier for aligned projects to obtain financing.
4. In addition, the demand for information on banks' or financiers' sustainable activities is new to most companies; it comprises information based on complex criteria as included in the EU Taxonomy for the sustainable economic activities. Be very alert to whether this information is available and when it must be disclosed.
5. There are still other European sustainability rules that might be relevant, such as the Sustainable Finance Disclosure Regulation. Non-financial reporting will be much more comprehensive, making it important to verify what rules apply.
6. A sustainability label or classification for a company's activities has commercial advantages. An inaccurate classification, on the other hand, can lead to 'greenwashing' (a business presenting itself as being more sustainable than it really is). Timely preparation will contribute to reporting in line with the EU Taxonomy.
7. Regulators monitor compliance with new laws and regulations, such as the EU Taxonomy and the CSRD. Users of this new information will also be critical of their implementation and ask questions if a company is obscure about its sustainable activities.

Positive effects of EU Taxonomy

We would also like to highlight the following positive effects of the EU Taxonomy. The TSC improve transparency and uniformity in the area of environmentally sustainable activities. This could lower (research) costs for investors wishing to invest in activities of this kind. Improved transparency in reporting also works to the benefit of businesses trying to distinguish themselves with their sustainable activities in this area, making it easier for them to raise capital. This way, an increase in capital flows towards environmentally sustainable activities can eventually contribute to a cleaner, healthier and more climate-proof living environment.

More information

We will be happy to talk you through the implications of the EU Taxonomy for your business and the steps you can take to be ready for this sustainable activities classification system. If you have any questions about the Taxonomy Regulation or would like assistance in implementing it within your organisation, please contact:



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