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The Taxonomy Regulation:
more important than just as an element of
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The Taxonomy Regulation: more important than just as an element of the Capital Markets Union¹

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Abstract

On the basis of the European Commission’s 2015 Action Plan “on Building a Capital Markets Union” (CMU), as further specified in the 2017 “Mid-Term Review of the [CMU] Action Plan”, the European Parliament and the Council adopted on 27 November 2019 Regulation (EU) 2019/2088 “on sustainability-related disclosures on the financial services sector” (SFDR) and Regulation (EU) 2019/2089 “as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks”. The third – and probably most important – part of the related ‘trilogy’, which is also based on the Commission’s 2018 “Action Plan on Financing Sustainable Growth”, is Regulation (EU) 2020/852 “on the establishment of a framework to facilitate sustainable investment” (the so-called Taxonomy Regulation, TR). The objective of this legislative act (which, *inter alia*, also introduces specific amendments to the SFDR) is to establish uniform criteria for determining whether an economic activity qualifies as environmentally sustainable for the purpose of establishing the degree to which an investment is environmentally sustainable as well. It does not itself establish a label for sustainable financial products; the details of what constitutes an environmentally sustainable activity or product is being built-up through delegated acts to be adopted by the Commission, of which the first two will apply from 31 December 2021 and the other four from 31 December 2022. The main purpose of this Chapter, which contains a thorough analysis of the entire legislative act, is threefold:

First, briefly albeit systematically present the “system of rules” relating to the “core element” of the TR, namely the criteria according to which an economic activity will be considered environmentally sustainable and the six environmental objectives (the six types of economic activities which qualify as environmentally sustainable activities for the purposes of the taxonomy).

Second, analyse the TR’s field of application, covering measures adopted by Member States and by the EU that set out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable, financial market participants that make available (environmentally sustainable) financial products (applying to credit institutions only to the extent that they provide portfolio management services) and undertakings falling under the scope of the “Non-Financial Reporting Directive”, as well as analyse the disclosure requirements for environmentally sustainable investments, as set out in the TR.

Third, conclude with some considerations on how the core element of the TR will be of primary importance even for entities which are not covered by its scope of application, namely beyond the reach of the CMU project. These considerations will be based on the observation that the taxonomy system, as developed within the TR, will be used, *inter alia*, as a benchmark in the course of new rules pertaining to the micro-prudential supervision of several categories of regulated

financial firms, including credit institutions, by virtue of other legislative acts which are sources of EU financial law.

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A. Subject matter and scope of the Regulation – environmental objectives²

1. Subject matter

1.1 Introductory remarks

(1) On 18 June 2020, the European Parliament and the Council adopted in accordance with the ordinary legislative procedure³ **Regulation (EU) 2020/852** “on the establishment of a framework to facilitate sustainable investment and amending **Regulation (EU) 2019/2088**”⁴ (the ‘Taxonomy Regulation’, **TR**). This legislative act was adopted on the basis of **Article 114 TFEU**, entered into force on **12 July 2020**,⁵ is binding in its entirety and directly applicable in all Member States⁶ and is consistent with the principles of subsidiarity and proportionality.⁷ It constitutes, along with the legislative act it amends, namely **Regulation (EU) 2019/2088** of the same institutions of 27 November 2019 “on sustainability-related disclosures in the financial services sector”,⁸ (commonly referred to as the ‘**Sustainable Finance Disclosure Regulation**’, **SFDR**) and **Regulation (EU) 2019/2089** of the same institutions of 27 November 2019 (as well) “amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks”⁹ (the ‘**Low Carbon Benchmarks Regulation**’), the ‘regulatory trilogy’ implementing the (European) Commission’s 2015 **Action Plan** “on Building a Capital Markets Union”¹⁰ (**CMU**) in relation to sustainable finance.¹¹

² The cut-off date for information included in this Chapter is **30 November 2020**.

³ **TFEU**, Article 289(1).

⁴ OJ L 198, 22.6.2020, pp. 13-43.

⁵ **TR**, Article 27(1).

⁶ *Ibid.*, last sentence.

⁷ *Ibid.*, recital (60).

⁸ OJ L 317, 9.12.2019, pp. 1-16.

⁹ OJ L 317, 9.12.2019, pp. 17-27.

¹⁰ COM/2015/468 final, available at: https://ec.europa.eu/info/publications/mid-term-review-capital-markets-union-action-plan_en.

¹¹ ‘Sustainable finance’ can be defined as the aggregate of financing and related institutional and market arrangements that contribute to the achievement of strong, sustainable, balanced and inclusive growth, through supporting directly and indirectly the framework of the Sustainable Development Goals (SDGs) (see **G20 Sustainable Finance Study Group (2018): Synthesis Report**, July, available at: http://www.g20.utoronto.ca/2018/g20_sustainable_finance_synthesis_report.pdf). It is also noted that the establishment of an internal market that works for the sustainable development of the EU, based, *inter alia*, on balanced economic growth and a high level of protection and the improvement of the quality of the environment, is laid down in **Article 3(3) TEU** (on this Article, see by means of mere indication **U. Becker (2019)**: Artikel 3 des

(2) It is noted in this respect that the **Commission Communication** of 8 June 2017 on the “Mid-Term Review of the [CMU] Action Plan”¹² set *nine priority actions* concerning *seven issue-areas*, which should constitute the basis for the foundation of the CMU by 2019.¹³ **Priority action (6)** of this Review concerned a concrete follow-up to the recommendations of the High-Level Expert Group (HLEG) on Sustainable Finance, which was set up by the Commission in December 2016 with the mandate to develop an overarching and comprehensive EU strategy on sustainable finance,¹⁴ addressing climate-related and environmental risks.¹⁵ In this respect, the

EUV, in Schwarze, J., Becker, U., Hatje, A. und J. Schoo (2019, Hrsg.): *EU-Kommentar*, 4. Auflage, Nomos Verlagsgesellschaft, Baden-Baden, pp. 53-59). Sustainability and the transition to a safe, climate-neutral, climate-resilient, more resource-efficient and circular economy are crucial to ensuring the long-term competitiveness of the EU economy (TR, recital (4)).

¹² COM(2017) 292 final, available at: https://ec.europa.eu/info/sites/info/files/communication-cmu-mid-term-review-june2017_en.pdf.

¹³ The consolidated set of measures is laid down in the Annex to the Communication. The Commission’s Q&As on this Review are available at: [http://europa.eu/rapid/press-release MEMO-17-1528_en.htm](http://europa.eu/rapid/press-release_MEMO-17-1528_en.htm). On the evolution of the CMU project, see the various contributions in **Busch, D., Avgouleas, E. and G. Ferrarini (2018, editors): *Capital Markets Union in Europe***, Oxford EU Financial Regulation Series, Oxford University Press, United Kingdom, **Lannoo, K. and A. Thomadakis (2019): *Rebranding Capital Markets Union: A market finance action plan***, CEPS-ECMI Task Force Report, Centre for European Policy Studies (available at: <https://www.ceps.eu/wp-content/uploads/2019/06/Rebranding-Capital-Markets-Union.pdf>), the Final Report of the **High-Level Forum on the Capital Markets Union** of June 2020 “A New Vision for Europe’s Capital Markets” (at: https://ec.europa.eu/info/files/200610-cmu-high-level-forum-final-report_en), and the Special Report 25/2020 of the **European Court of Auditors** of 11 November “Capital Markets Union – Slow start towards an ambitious goal” (at: <https://www.eca.europa.eu/en/Pages/DocItem.aspx?did=57011>). The most recent Action Plan on this field, amidst the current pandemic crisis, is contained in the **Commission Communication** of 24 September 2020 “A Capital Markets Union for people and businesses – new action plan” (COM(2020) 590 final, at: https://ec.europa.eu/info/publications/200924-capital-markets-union-action-plan_en).

The measures to support, *inter alia*, a green recovery, are contained in Section 1 (pp. 7-10, Actions 1-6).

¹⁴ Its Report of 31 January 2018, titled “Financing a Sustainable European Economy”, called for the creation of a technically robust classification system at EU level to establish clarity on which activities qualify as ‘green’ or ‘sustainable’ (TR, recital (5)) (available at: https://ec.europa.eu/info/sites/info/files/180131-sustainable-finance-final-report_en.pdf). On the work of the HLEG, see **Alexander, K. (2019): *Principles of Banking Regulation***, Cambridge University Press, United Kingdom, pp. 366-369.

¹⁵ On these risks, which combine two main risk drivers (i.e., physical and transition risk), see by means of indication **European Central Bank (2020): “Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure”**, 27 November, pp. 10-15 (available at:

Commission submitted proposals aimed at improving disclosure and integrating sustainability as well as environmental, social and governance (**ESG**) considerations fully in rating methodologies and supervisory processes, as well as in the investment mandates of institutional investors and asset managers. It also committed to develop an approach for taking sustainability considerations **into** account in upcoming legislative reviews of financial legislation.¹⁶

(3) The TR builds on the work of the HLEG and is also substantially based on the Report of the Technical Expert Group on Sustainable Finance (**TEG**) set up by the Commission in line with its legislative proposals of May 2018¹⁷ to assist it in developing, *inter alia*, the so called “EU taxonomy”. This is a unified EU (green) classification system to determine if an economic activity is environmentally sustainable, which was published in March 2020.¹⁸ Of particular relevance in this context is also the Commission Communication of 8 March 2018 on an “**Action Plan on Financing Sustainable Growth**”,¹⁹ Action 1 which calls for the establishment of the EU taxonomy.²⁰

<https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf>.

¹⁶ In this respect, *inter alia*, all three Regulations governing the European Supervisory Authorities (**ESAs**, namely the EBA, the ESMA and the EIOPA) were amended by virtue of **Regulation (EU) 2019/2175** of the European Parliament and of the Council of 18 December 2019 (OJ L 334, 27.12.2019, pp. 1-145), which clarifies and strengthens their existing powers, while also attributing new powers to them in targeted areas, including the taking into account of sustainable business models and the integration of environmental, social and governance (ESG) factors when acting within its scope of action and carrying out its tasks (Article 1(3)). See further **Section F below, under 2**.

¹⁷ See at: https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance_en#implementing.

¹⁸ On the TEG, see at: https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en. Its Report provides recommendations relating to the TR’s overarching design, as well as guidance on making disclosures using the taxonomy. It is supplemented by a technical annex containing technical screening criteria (TSC) for 70 climate change mitigation and 68 climate change adaptation activities, including criteria for do no significant harm to other environmental objectives, as well as a methodology section to support the recommendations on the TSC (see **Section C below**). The Report is available at: https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/200309-sustainable-finance-teg-final-report-taxonomy_en.pdf.

¹⁹ COM/2018/097 final (available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52018DC0097>).

²⁰ A main objective set out therein is the reorientation of capital flows towards sustainable investments to achieve sustainable and inclusive growth and, in that respect, the most important and urgent action envisaged is the establishment of a unified classification system for sustainable activities. Since the shift of capital flows towards more sustainable activities must be underpinned by a holistic understanding of the environmental sustainability of

1.2 The considerations set out in the Regulation on harmonisation of rules, the disclosure framework and private sector initiatives

(1) In accordance with its title, the TR establishes *“a framework to facilitate sustainable investment”*. In this respect, it is considered that a necessary condition to enable the development of future EU policies in **support of sustainable finance**, including EU-wide standards for environmentally sustainable financial products and the eventual establishment of labels that formally recognise compliance therewith (‘eco-labels’), is the establishment of a classification system for environmentally sustainable economic activities at EU level, which could also serve as the basis for other economic and regulatory measures.²¹ Hence, uniform legal requirements for determining the degree of investments’ environmental sustainability, based on uniform (as well) criteria for environmentally sustainable economic activities, are necessary as a reference to facilitate investments’ shift towards such economic activities.²²

(2) Within this conceptual framework, the TR sets out the criteria for determining whether an **economic activity** qualifies as environmentally sustainable for the purposes of establishing the degree to which an **investment** is environmentally sustainable as well.²³ The harmonisation (at EU level) of these criteria aims at both removing barriers to the functioning of the internal market with regard to raising funds for sustainability projects and preventing the future emergence of barriers to such projects. The expectation is that such a harmonisation will allow economic operators *“to find it easier to raise funding across borders for their environmentally sustainable activities, as their economic activities could be compared against uniform criteria in order to be selected as underlying assets for environmentally sustainable investments”* and, hence, facilitate cross-border sustainable investment in the EU.²⁴

(3) In accordance with **recital (10)**, *“in view of the scale of the challenge and the costs associated with inaction or delayed action, the financial system should be gradually adapted in order to support the sustainable functioning of the economy. To that end, sustainable finance needs to become mainstream and consideration needs to be given to the sustainability impact of financial products and services”*. **The channeling of private investments (capital flows) towards sustainable investments** is considered (correctly so) as a

activities and investments, the Action Plan considers that, as a first step, clear guidance on activities that qualify as contributing to environmental objectives would help inform investors about the investments funding environmentally sustainable economic activities, while further guidance on activities contributing to other sustainability objectives (e.g., social ones) might be developed at a later stage (TR, recital (6)).

²¹ See **Section F below, under (2)**.

²² TR, recital (16).

²³ *Ibid.*, Article 1(1).

²⁴ *Ibid.*, recital (12).

precondition for achieving the **Sustainable Development Goals (SDGs)**, as laid down in the 2015 United Nations (UN) global sustainable development framework (“The 2030 Agenda for Sustainable Development”²⁵), which covers sustainability’s three dimensions, namely **economic, social and environmental**. An effective way for achieving this is to make available financial products which pursue environmentally sustainable objectives.²⁶

Member States and the EU should (be required to) use a common concept of environmentally sustainable investment when introducing requirements at national and EU level regarding financial market participants or issuers for the purpose of labelling financial products or corporate bonds that are marketed as environmentally sustainable in order to promote the functioning of the internal market.²⁷ National requirements that financial market participants or issuers have to comply with in order to market financial products or corporate bonds as environmentally sustainable should build on the above-mentioned uniform criteria for environmentally sustainable economic activities to avoid market fragmentation and harm to the interests of consumers and investors as a result of diverging notions.²⁸ In that respect, the term ‘**environmentally sustainable investment**’ is defined to mean an investment in one or more economic activities that qualify as environmentally sustainable under the TR.²⁹

(4) Apart from setting out the criteria for determining whether an economic activity qualifies as environmentally sustainable for the purposes of establishing the degree to which an investment is environmentally sustainable, the TR **lays down a disclosure framework**, which supplements the disclosure requirements laid down in the SFDR.³⁰ By setting requirements for marketing financial products or corporate

²⁵ Available at: <https://sustainabledevelopment.un.org/content/documents/21252030%20Agenda%20for%20Sustainable%20Development%20web.pdf>.

²⁶ TR, recital (11), first sentence. See also Bose, S., Dong, G. and A. Simpson (2019): *The Financial Ecosystem: The Role of Finance in Achieving Sustainability*, Palgrave Studies in Impact Finance, Palgrave Macmillan, Cham – Switzerland.

²⁷ On the current situation concerning national labelling schemes in place and the need to establish uniform criteria to incentivise economic operators to access cross-border capital markets for the purposes of sustainable investment, see the considerations in recital (11), fourth to last sentences.

²⁸ *Ibid.*, recital (14), first and second sentences.

²⁹ In this respect and from a global perspective, see also the Report of 29 June 2017 by the Task Force on Climate-related Financial Disclosures (TCFD) of the Financial Stability Board (FSB), which provides recommendations for consistent, comparable, reliable, clear and efficient climate-related financial disclosures by companies (“Recommendations of the Task Force on Climate-related Financial Disclosures, available at: <https://www.fsb.org/wp-content/uploads/P290617-5.pdf>).

³⁰ TR, recital (55), first sentence (see also **Section D below, under 1 (2)**). In accordance with its Article 1, the objective of that legislative act is to lay down harmonised rules for financial

bonds as environmentally sustainable investments, including requirements set by Member States and the EU to allow **financial market participants and issuers** to use national labels, it aims at enhancing investor confidence and awareness of the environmental impact of these financial products or corporate bonds and at creating visibility. It also intends to alleviate the burden on investors' own due diligence with regard to products' environmental sustainability and address concerns of 'greenwashing', i.e., the practice of gaining an unfair competitive advantage by inaccurately marketing a financial product as environmentally friendly or "green", when in fact basic environmental standards have not been met.³¹

(5) It is finally worth noting that in the context of achieving the SDGs in the EU, the creation, *inter alia*, of a **European Fund for Strategic Investment** has been effective in contributing to the channeling of private funds towards sustainable investments alongside public spending.³² Furthermore, **recital (8)** considers that, in accordance with **Decision No 1386/2013/EU** of the European Parliament and of the Council of 20 November 2013 "on a General Union Environment Action Programme to 2020 'Living well, within the limits of our planet'",³³ private sector funding for climate-related and environmental expenditure should also be increased. This could in particular be achieved by initiating incentives and methodologies that stimulate companies to measure the environmental costs of their business and profits derived from using environmental services.

2. Scope

On the basis of the above-mentioned considerations, the system of rules laid down in the TR is anchored in the definition of six specific environmental objectives;³⁴ these constitute the benchmark on the basis of which an economic activity can (be assessed to) qualify as environmentally sustainable³⁵ and, consequently, the degree

market participants and financial advisers on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes and the provision of sustainability-related information with respect to financial products. That legislative act is analysed in **Chapter 11 (Busch, D.: Sustainability Disclosure in the financial sector)**.

³¹ *Ibid.*, recital (11), second and third sentences.

³² **Regulation (EU) 2015/1017** of the European Parliament and of the Council of 25 June 2015 "on the European Fund for Strategic Investments, the European Investment Advisory Hub and the European Investment Project Portal (...) – the European Fund for Strategic Investments" (OJ L 169, 1.7.2015, pp. 1-38) specifies a 40% climate investment target for infrastructure and innovation projects under the Fund (see recitals (2), (9) and (17)).

³³ OJ L 354, 28.12.2013, pp. 171-200.

³⁴ See just below, **under 3**.

³⁵ See **Section B below**.

to which a financial investment is environmentally sustainable is established. The field of application of this legislative act covers:³⁶

first, any legislative or other **measures** adopted by Member States or by the EU that set out requirements for **financial market participants**³⁷ or **issuers**³⁸ in respect of financial products³⁹ or corporate bonds that are **made available as environmentally sustainable**;

second, **financial market participants** that make available (environmentally sustainable) financial products; and

third, **undertakings** which are subject to the obligation to publish a non-financial statement or a consolidated non-financial statement pursuant to **Articles 19a or 29a**, respectively, of **Directive 2013/34/EU** of the European Parliament and of the Council, of 26 June 2013 “on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings (...)”⁴⁰ (**EU Non-Financial Reporting Directive**) and issue environmentally sustainable corporate bonds.

3. Environmental objectives

For the purpose of determining the environmental sustainability of a given economic activity, and on the basis of the recommendations contained in (above-mentioned) TEG’s final Report, the TR contains an **exhaustive list** of six environmental objectives. These are the following:⁴¹

³⁶ **TR**, Article 1(2), points (a)-(c), respectively and recital (14), third sentence.

³⁷ The term ‘**financial market participant**’ is defined with reference to Article 2, point (1) SFDR and includes a manufacturer of a pension product to which a Member State has decided to apply that legislative act in accordance with Article 16 thereof (*ibid.*, Article 2, point (2)).

³⁸ The term ‘**issuer**’ is defined with reference to Article 2, point (h) of the **Prospectus Regulation (Regulation (EU) 2017/1129)** of the European Parliament and of the Council of 14 June 2017, OJ L 168, 30.6.2017, pp. 12-82) (*ibid.*, Article 2, point (4)).

³⁹ The term ‘**financial product**’ is defined (*ibid.*, Article 2, point (3)) with reference to Article 2, point (12) SFDR, meaning all of the following: a portfolio which is managed in accordance with Article 2, point (6); an alternative investment fund (**AIF**); an ‘insurance-based investment product’ (**IBIP**); a pension product; a pension scheme; an undertaking for collective investment in transferable securities (**UCITS**); or a ‘pan-European Personal Pension Product’ (**PEPP**). It is noted that bank lending is not covered either by this definition or by the TR (and the SFDR) in general.

⁴⁰ OJ L 182, 29.6.2013, pp. 19-76.

⁴¹ **TR**, Article 9 and recital (23). According to recital (7) given the systemic nature of global environmental challenges, environmental sustainability should be approached on a systemic and forward-looking basis, addressing growing negative trends, such as climate change, the loss of biodiversity, the global overconsumption of resources, food scarcity, ozone depletion,

First, climate change mitigation, meaning the process of holding the increase in the global average temperature to well below 2 °C and pursuing efforts to limit it to 1,5 °C above pre-industrial levels, as laid down in the **Paris Agreement**.⁴² This environmental objective should be interpreted in accordance with relevant EU law, including **Directive 2009/31/EC** of the European Parliament and of the Council of 23 April 2009 “on the geological storage of carbon dioxide (...)”.⁴³

Second, climate change adaptation, meaning the process of adjustment to actual and expected climate change and its impacts.⁴⁴ This objective should be interpreted in accordance with relevant EU law and the **Sendai Framework for Disaster Risk Reduction 2015–2030**.⁴⁵

Third, sustainable use and protection of water and marine resources.⁴⁶

Fourth, transition to a “circular economy”; circular economy means an economic system whereby the value of products, materials and other economic resources

ocean acidification, the deterioration of the fresh water system, and land system change as well as the appearance of new threats, such as hazardous chemicals and their combined effects.

⁴² *Ibid.*, Article 2, point (5). The Paris Agreement was approved in the EU by **Council Decision (EU) 2016/1841** of 5 October 2016 “on the conclusion, on behalf of the European Union, of the Paris Agreement adopted under the UN Framework Convention on Climate Change” (OJ L 282, 19.10.2016, pp. 1-3). Article 2(1), point (c) of the Paris Agreement aims to strengthen the response to climate change by making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development, *inter alia*. In that context, on 12 December 2019, the European Council adopted conclusions on climate change, in light of which the TR represents a key step towards the objective of achieving a **climate-neutral EU** by 2050 (TR, recital (3)).

⁴³ OJ L 140, 5.6.2009, pp. 114-135; *ibid.*, recital (24), third sentence.

⁴⁴ *Ibid.*, Article 2, point (5).

⁴⁵ *Ibid.*, recital (25), second sentence. The Sendai Framework, which was adopted at the Third UN World Conference in Sendai, Japan, on 18 March 2015, is the outcome of stakeholder consultations initiated in March 2012 and inter-governmental negotiations from July 2014 until March 2015, supported by the UN Office for Disaster Risk Reduction at the request of the UN General Assembly; its text is available at: https://www.preventionweb.net/files/43291_sendaiframeworkfordrren.pdf. On this Framework, see, by means of mere indication, Aitsi-Selmi, A., Blanchard, K. and V. Murray (2016): Ensuring Science is Useful, Usable and Used in Global Disaster Risk Reduction and Sustainable Development: A View Through the Sendai Framework Lens, Palgrave Communications, Vol. 2, available at: <https://ssrn.com/abstract=2780391>.

⁴⁶ This environmental objective should be interpreted in accordance with the sectoral legislative acts laid down in **recital (26)** and the Commission Communications of 18 July 2007 on “Addressing the challenge of water scarcity and droughts in the European Union”, of 14 November 2012 on “A Blueprint to Safeguard Europe’s Water Resources” and of 11 March 2019 on “European Union Strategic Approach to Pharmaceuticals in the Environment”.

is maintained for as long as possible, enhancing their efficient use in production and consumption, thereby reducing the environmental impact of their use, minimising waste and the release of hazardous substances at all stages of their life-cycle, including through the application of the waste hierarchy.⁴⁷

Fifth, pollution prevention and control; the term ‘pollution’ has a threefold meaning:⁴⁸ (i) the direct or indirect introduction of pollutants⁴⁹ into air, water or land as a result of human activity; (ii) in the context of the marine environment, pollution as defined in Article 3, point (8) of **Directive 2008/56/EC** of the European Parliament and of the Council of 17 June 2008 “establishing a framework for community action in the field of marine environmental policy” (the **Marine Strategy Framework Directive**);⁵⁰ and (iii) in the context of the water environment, pollution as defined in Article 2, point (33) of **Directive 2000/60/EC** of the same institutions of 23 October 2000 “establishing a framework for Community action in the field of water policy”.⁵¹

Finally, protection and restoration of biodiversity and ecosystems (healthy ecosystem). In this respect: ‘biodiversity’ means the variability among living organisms arising from all sources including terrestrial, marine and other aquatic ecosystems and the ecological complexes of which they are part and includes diversity within species, between species and of ecosystems; and ‘ecosystem’ means a dynamic complex of plant, animal, and micro-organism communities and their non-living environment interacting as a functional unit.⁵²

⁴⁷ *Ibid.*, Article 2, point (9). ‘Waste hierarchy’ has the meaning laid down in Article 4 of **Directive 2008/98/EC** of the European Parliament and of the Council of 19 November 2008 “on waste and repealing certain Directives” (the **Waste Framework Directive**, OJ L 312, 22.11.2008, pp. 3-30) (*ibid.*, Article 2, point (8)). This environmental objective should be interpreted in accordance with relevant EU law in the areas of the circular economy, waste and chemicals, and with the Commission Communications of 2 December 2015 on “Closing the loop – An EU action plan for the Circular Economy” and of 16 January 2018 on “A European Strategy for Plastics in a Circular Economy” (*ibid.*, recital (27)).

⁴⁸ *Ibid.*, Article 2, point (12).

⁴⁹ ‘Pollutant’ means a substance, vibration, heat, noise, light or other contaminant present in air, water or land which may be harmful to human health or the environment, which may result in damage to material property, or which may impair or interfere with amenities and other legitimate uses of the environment (*ibid.*, Article 2, point (10)).

⁵⁰ OJ L 164, 25.6.2008, pp. 19-40.

⁵¹ OJ L 327, 22.12.2000, pp. 1-73. This environmental objective should be interpreted in accordance with the sectoral legislative acts set out in **recital (29) TR**.

⁵² *Ibid.*, Article 2, points (15) and (13), respectively. The term ‘ecosystem services’ is defined to mean the direct and indirect contributions of ecosystems to the economic, social, cultural and other benefits that people derive from those (*ibid.*, Article 2, point (14)). This environmental objective should be interpreted in accordance with the sectoral legislative acts and the Commission Communications set out in **recital (30)**.

B. Criteria for determining whether economic activities qualify as environmentally sustainable

1. General overview

(1) In accordance with **recital (34)**, for each of the above-mentioned environmental objectives, the TR should lay down uniform criteria for determining whether economic activities substantially contribute to it, including the avoidance of significant harm to it. The objective is to avoid that investments qualify as environmentally sustainable where the economic activities benefitting from those cause harm to the environment to an extent that outweighs their contribution to an environmental objective. Such criteria should take into account the life-cycle of the products and services provided by each economic activity in addition to the environmental impact of the economic activity itself, including taking into account evidence from existing life-cycle assessments, in particular by considering their production, use and end of life.

(2) In accordance with these considerations, for the purposes of establishing the degree to which an **investment** is environmentally sustainable, an **economic activity** qualifies as environmentally sustainable if four criteria are met cumulatively:⁵³

first, it substantially contributes to (at least) one or more environmental objectives in accordance with **Articles 10-16**;⁵⁴ hence, a direct link is established between the environmental objectives and the *substantial* contribution of economic activities to each of them;

second, it does not significantly harm any other environmental objective in accordance with **Article 17**;⁵⁵

third, it is carried out in compliance with the safeguards laid down in **Article 18**;⁵⁶ and

fourth, it complies with applicable technical screening criteria (TSC) set out in the Commission's delegated acts, which supplement the TR.⁵⁷

(3) These criteria must be applied by Member States and the EU in order to determine whether an economic activity qualifies as environmentally sustainable for the purposes of any measure setting out requirements for financial market

⁵³ *Ibid.*, Article 3.

⁵⁴ See just below, **under 2**.

⁵⁵ See below, **under 3**.

⁵⁶ See below, **under 4**.

⁵⁷ See **Section C** below.

participants or issuers in respect of financial products or corporate bonds made available as environmentally sustainable.⁵⁸

2. Substantial contribution to environmental objectives

2.1 Substantial contribution to climate change mitigation

2.1.1 Means for meeting this criterion

(1) An economic activity **meets this criterion** where it substantially contributes to the **stabilisation of greenhouse gas** concentrations in the atmosphere,⁵⁹ at a level which prevents dangerous anthropogenic interference with the climate system consistent with the long-term temperature goal of the Paris Agreement of limiting the global temperature increase to 1.5 degrees Celsius above pre-industrial levels. This can be **achieved** either by avoiding or reducing greenhouse gas concentrations or by enhancing greenhouse gas removals, through process or product innovations, *via* any of the following means:

first, by generating, transmitting, storing, distributing or using renewable energy (e.g., through extension of the grid) in accordance with **Directive (EU) 2018/2001** of the European Parliament and of the Council of 11 December 2018 “on the promotion of the use of energy from renewable sources”;⁶⁰

second, by improving energy efficiency,⁶¹ except for power generation activities;⁶²

third, by increasing clean or climate-neutral mobility, as well as the by use of environmentally safe carbon capture and utilisation (CCU) and carbon capture and storage (CCS) technologies, which deliver a net reduction in greenhouse gas emissions;

⁵⁸ **TR**, Article 4. This provision does not apply to certificate-based tax incentive schemes, which existed prior to the entry into force of the TR and set out requirements for financial products that aim to finance sustainable projects, without prejudice to the respective competences of the EU and the Member States with respect to tax provisions, as set out by the Treaties (*ibid.*, Article 27(3) and recital (58)).

⁵⁹ The definition of the term ‘greenhouse gas’ is made with reference to Annex I to **Regulation (EU) No 525/2013** of the European Parliament and of the Council of 21 May 2013 “on a mechanism for monitoring and reporting greenhouse gas emissions and for reporting other information at national and Union level relevant to climate change (...)” (OJ L 165, 18.6.2013, pp. 13-40) (*ibid.*, Article 2, point (7)).

⁶⁰ OJ L 328, 21.12.2018, pp. 82-209.

⁶¹ ‘Energy efficiency’ means the more efficient use of energy at all the stages of the energy chain from production to final consumption (**TR**, Article 2, point (17)). For the purposes of the TR, this term is used in a broad sense and should be construed by taking into several sectoral legislative acts of the European Parliament and of the Council as well as the implementing measures adopted by the Commission (*ibid.*, recital (33)).

⁶² On this, see **Section C** below, under 2 (2).

fourth, by switching to the use of sustainably sourced renewable materials;

fifth by strengthening land carbon sinks (e.g., through avoiding deforestation and forest degradation, restoration of forests, sustainable management and restoration of croplands, grasslands and wetlands, afforestation, and regenerative agriculture);

sixth, by establishing energy infrastructure required for enabling the decarbonisation of energy systems;

furthermore, by producing clean and efficient fuels from renewable or carbon-neutral sources; or

finally, by enabling any of the above activities in accordance with **Article 16**.⁶³

2.1.2 Enabling and transitional activities

(1) An economic activity qualifies as contributing substantially to this (or any other⁶⁴) environmental objective by *directly enabling* other activities to make a substantial contribution to one or more of those objectives as well. Such ‘**enabling activities**’ should not lead to a lock-in of assets that undermine long-term environmental goals (considering their economic lifetime) *and* should have a substantial positive environmental impact on the basis of life-cycle considerations.⁶⁵

(2) An economic activity for which there is no technologically and economically feasible low-carbon alternative is considered to qualify as contributing substantially to climate change mitigation if it supports the transition to a climate-neutral economy consistent with a pathway to limit the temperature increase to 1,5°C above pre-industrial levels (e.g., by phasing out greenhouse gas emissions, in particular emissions from solid fossil fuels) *and*, in addition, meets the following conditions: has greenhouse gas emission levels corresponding to the best performance in the sector or industry; does not hamper the development and deployment of low-carbon alternatives; and does not lead to a lock-in of carbon-intensive assets, considering their economic lifetime (‘**transitional activity**’).⁶⁶

2.2 Substantial contribution to climate change adaptation

An economic activity **meets this criterion** in two (alternative) cases: *first*, if it includes adaptation solutions, which either substantially reduce the risk of the adverse impact of the current and expected future climate on that economic activity

⁶³ TR, Article 10(1) and recital (24), first and second sentences.

⁶⁴ See below, **under 2.3-2.6**.

⁶⁵ TR, Article 16 and recital (42).

⁶⁶ For this purpose and for the establishment of TSC pursuant to **Article 19** (see **Section C** below), the Commission must assess the potential contribution and feasibility of all relevant existing technologies (*ibid.*, Article 10(2)).

or substantially reduce that adverse impact, without increasing the risk of an adverse impact on people, nature or assets. Such solutions must be assessed and ranked in order of priority using the best available climate projections and, at a minimum, prevent or reduce either the location-specific and context-specific adverse impact of climate change on the economic activity; or the potential adverse impact of climate change on the environment within which the economic activity takes place; or *second*, if it provides adaptation solutions which satisfy the conditions set out in **Article 16** and, in addition, contribute substantially to preventing or reducing the risk of the adverse impact of the current and the expected future climate on people, nature or assets, without increasing the risk of an adverse impact on them.⁶⁷

2.3 Substantial contribution to the sustainable use and protection of water and marine resources

An economic activity meets this criterion if it substantially contributes *either* to achieving the ‘good status’⁶⁸ of bodies of water (including bodies of surface water and groundwater) or to preventing the deterioration of bodies of water that already have good status, *or* to achieving the ‘good environmental status’ of marine waters⁶⁹ or to preventing the deterioration of marine waters that are already in good environmental status. This can be achieved by means of any of the following (including through enabling activities):

first, by protecting the environment from the adverse effects of urban and industrial waste-water discharges, including from contaminants of emerging concern, such as pharmaceuticals and microplastics, e.g., by ensuring the adequate collection, treatment and discharge of urban and industrial waste-waters;

second, by protecting human health from the adverse impact of any contamination of water intended for human consumption, ensuring that it is free from any micro-organisms, parasites and substances that constitute a potential

⁶⁷ *Ibid.*, Article 11(1)-(2) and recital (25), first sentence.

⁶⁸ ‘Good status’ means the following: for *surface water*, having both ‘good ecological status’, as defined in Article 2, point (22) of **Directive 2000/60/EC** and ‘good surface water chemical status’, as defined in Article 2, point (24) thereof; and for *groundwater*, having both ‘good groundwater chemical status’, as defined in Article 2, point (25) of **Directive 2000/60/EC** and ‘good quantitative status’, as defined in Article 2, point (28) thereof (*ibid.*, Article 2, point (22)). In this respect, the terms ‘surface water’ and ‘groundwater’ have the meaning as defined in Article 2, points (1) and (2), respectively of **Directive 2000/60/EC** (*ibid.*, Article 2, points (19)-(20)).

⁶⁹ ‘Good environmental status’ has the meaning as defined in Article 3, point (5) of **Directive 2008/56/EC** and ‘marine waters’ the meaning as defined in Article 3 point (1) thereof (*ibid.*, Article 2, points (21) and (18), respectively).

danger to human health as well as increasing people's access to clean drinking water;

third, by improving water management and efficiency (e.g., by protecting and enhancing the status of aquatic ecosystems), by promoting the sustainable use of water through the long-term protection of available water resources (*inter alia*, through water reuse), by ensuring the progressive reduction of pollutant emissions into surface water and groundwater, by contributing to mitigating the effects of floods and droughts, or by any other activity protecting or improving the qualitative and quantitative status of water bodies; or

fourth, by ensuring the sustainable use of marine ecosystem services or by contributing to the good environmental status of marine waters (e.g., by protecting, preserving or restoring the marine environment) and by preventing or reducing inputs in the marine environment.⁷⁰

2.4 Substantial contribution to the transition to a circular economy

An economic activity qualifies as substantially contributing to the transition to a circular economy, including waste prevention, re-use and recycling, by any of the following means (including through enabling activities):

first, it uses natural resources (such as sustainably sourced bio-based and other raw materials) in production more efficiently, including by reducing the use of primary raw materials or increasing the use of by-products and secondary raw materials or by resource and energy efficiency measures;

second, it increases the durability, reparability, upgradability, reusability and recyclability of products (including the recyclability of individual materials contained in them); the use of secondary raw materials and their quality, including by high-quality recycling of waste; the preparation for the re-use and recycling of waste; and the development of the waste management infrastructure needed for prevention, preparing for re-use and recycling, while ensuring that the recovered materials are recycled as high-quality secondary raw material input in production (avoiding thus downcycling);

third, it substantially reduces the content of hazardous substances and substitutes substances of very high concern in materials and products throughout their life-cycle, in accordance with the objectives set out in EU law, including by replacing such substances with safer alternatives and ensuring traceability;

fourth, it prolongs the use of products, including through reuse, design for longevity, repurposing, disassembly, remanufacturing, upgrades and repair, and sharing them; or

fifth, it prevents or reduces waste generation, including the generation of waste from the extraction of minerals and waste from the construction and demolition

⁷⁰ *Ibid.*, Article 12(1).

of buildings, minimises the incineration of waste and avoids the disposal of waste (including landfilling), in accordance with the principles of the waste hierarchy, or it avoids and reduces litter.⁷¹

2.5 Substantial contribution to pollution prevention and control

An economic activity meets this criterion: *first*, by preventing or (if that is not practicable) reducing pollutant emissions into air, water or land, other than greenhouse gasses, or by preventing or minimising any adverse impact on human health and the environment of the production, use or disposal of chemicals; *second*, by improving levels of air, water or soil⁷² quality in the areas where the economic activity takes place, while also minimising any adverse impact on human health and the environment or the risk thereof; *third*, by cleaning up litter and other pollution; or *finally*, through enabling activities.⁷³

2.6 Substantial contribution to the protection and restoration of biodiversity and ecosystems

An economic activity meets this criterion where it substantially contributes to protecting, conserving or restoring biodiversity or to achieving the good condition of ecosystems⁷⁴ or to protecting ecosystems already in good condition by any of the following means: *first*, by nature and biodiversity conservation (including by achieving favourable conservation status of natural and semi-natural habitats and species or preventing their deterioration where they already have favourable conservation status) and by protecting and restoring terrestrial, marine and other aquatic ecosystems in order to improve their condition and enhance their capacity to provide ecosystem services; *second*, by sustainable land use and management, including adequate protection of soil biodiversity, land degradation neutrality and the remediation of contaminated sites; *third*, by sustainable agricultural practices (including those contributing to the enhancement of biodiversity or to the halting or prevention of the degradation of soils and other ecosystems, deforestation and

⁷¹ *Ibid.*, Article 13(1) and recital (28).

⁷² ‘Soil’ means the top layer of the earth’s crust situated between the bedrock and the surface, composed of mineral particles, organic matter, water, air and living organisms (*ibid.*, Article 2, point (11)).

⁷³ *Ibid.*, Article 14(1).

⁷⁴ ‘Good condition’ means, in relation to an ecosystem, that this is in good physical, chemical and biological condition or is of a good physical, chemical and biological quality with self-reproduction or self-restoration capability, in which species composition, ecosystem structure and ecological functions are not impaired (*ibid.*, Article 2, point (16)).

habitat loss), as well as by sustainable forest management;⁷⁵ or *finally*, through enabling activities.⁷⁶

3. No significant harm to any other environmental objective

(1) An economic activity must also meet the “**do no significant harm**” principle, referred to in **Article 2, point (17) SFDR**, by virtue of which an activity substantially contributing to one of the environmental objectives must also do no significant harm to any of the other objectives. Hence, an economic activity should not qualify as environmentally sustainable if it causes more harm to the environment than the benefits it brings.

Taking thus into account the life-cycle of products and services provided by an economic activity, including evidence from existing life-cycle assessments, an economic activity is considered to significantly harm: the *first* environmental objective (climate change mitigation), where it leads to significant greenhouse gas emissions; the *second* objective (climate change adaptation), where it leads to an increased adverse impact on the current and expected future climate, on the activity itself or on people, nature or assets; the *third* objective (sustainable use and protection of water and marine resources), where it is detrimental *either* to the good status or the good ecological potential of bodies of water,⁷⁷ including surface water and groundwater, *or* to the good environmental status of marine waters; the *fourth* objective (circular economy), where: *first*, it leads to significant inefficiencies in the use of materials or in the direct or indirect use of natural resources such as non-renewable energy sources, raw materials, water and land at one or more stages of products’ life-cycle; *second*, it leads to a significant increase in waste generation, incineration or disposal, with the exception of the incineration of non-recyclable hazardous waste; or *third*, the long-term disposal of waste may cause significant and long-term harm to the environment; the *fifth* objective (pollution prevention and control), where it leads to a significant increase in the emissions of pollutants into air, water or land, as compared with the situation before the activity started; and the *sixth* objective (protection and restoration of biodiversity and ecosystems), where it is significantly detrimental to the good condition and resilience of ecosystems or detrimental to the conservation status of habitats and species, including those of EU interest.⁷⁸

(2) In the course of assessing an economic activity against the above criteria, both the environmental impact of the activity itself and the environmental impact of the

⁷⁵ The term ‘sustainable forest management’ should be construed by taking into account the factors laid down in recital (32).

⁷⁶ *Ibid.*, Article 15(1) and recital (31).

⁷⁷ The term ‘good ecological potential’ is defined with reference to Article 2, point (23) of Directive 2000/60/EC (*ibid.*, Article 2, point (23)).

⁷⁸ *Ibid.*, Article 17(1), with reference to Article 3, point (b).

products and services provided by it throughout their life-cycle must be taken into account, by considering the production, use and end of life of those products and services.⁷⁹

4. Compliance with minimum safeguards

Taking into account the joint commitment of the European Parliament, the Council and the Commission to pursuing the principles enshrined in the **European Pillar of Social Rights** in support of sustainable and inclusive growth,⁸⁰ and recognising the relevance of international minimum human and labour rights and standards, economic activities qualify as environmentally sustainable upon the condition that they are also compliant with the ‘minimum safeguards’ referred to in **Article 18 TR**.⁸¹ These are **procedures** implemented by undertakings carrying out economic activities in order to ensure consistency with the OECD “Guidelines for Multinational Enterprises” and the UN “Guiding Principles on Business and Human Rights”,⁸² including the 1988 “Declaration on Fundamental Principles and Rights at Work” of the International Labour Organisation (ILO),⁸³ the 8 fundamental conventions of the ILO 1998 (defining human and labour rights to be respected by undertakings), and the “International Bill of Human Rights”.⁸⁴ When implementing these procedures, undertakings must adhere to the “do no significant harm” principle and take into account the regulatory technical standards (RTSs) adopted pursuant to the SFDR.⁸⁵

⁷⁹ *Ibid.*, Article 17(2).

⁸⁰ See at: https://ec.europa.eu/commission/priorities/deeper-and-fairer-economic-and-monetary-union/european-pillar-social-rights/european-pillar-social-rights-20-principles_en.

⁸¹ **TR**, Article 3, point (c).

⁸² Available at: <https://www.oecd.org/corporate/mne>.

⁸³ Available at: <https://www.ilo.org/declaration/lang-en/index.htm>.

⁸⁴ **TR**, Article 18(1) and recital (35), first and second sentences. The International Bill of Human Rights was adopted and proclaimed by UN General Assembly Resolution 217 A (III) of 10 December 1948 (available at: <https://www.ohchr.org/Documents/Publications/Compilation1.1en.pdf>). Several of these international standards are enshrined in the **Charter of Fundamental Rights of the EU**. The minimum safeguards are without prejudice to the application of more stringent requirements related to environmental, health, safety and social sustainability as set out in EU law, where applicable (*ibid.*, recital (35), third and fourth sentences).

⁸⁵ *Ibid.*, Article 18(2) and recital (35), last sentence.

C. In particular: requirements for Technical Screening Criteria (TSC)

1. The considerations set out in the Regulation

(1) In order to determine whether an economic activity qualifies as sustainable, the Commission must adopt delegated acts establishing TSC pursuant to **Articles 10(3), 11(3), 12(2), 13(2), 14(2) and 15(2) TR**.⁸⁶ With regard to these criteria, the following considerations are set out in the recitals:⁸⁷

First, given the specific technical details needed to assess the environmental impact of an economic activity and the fast-changing nature of both science and technology, the TSC should be regularly adapted to reflect such changes. In addition, in order to ensure that they are up to date, based on scientific evidence and input from experts as well as relevant stakeholders, the conditions for ‘substantial contribution’ and ‘significant harm’ should be specified with more granularity for different economic activities. Accordingly, the Commission must establish granular and calibrated TCS for the different economic activities, based on technical input from the Platform on Sustainable Finance.⁸⁸

Second, given that the potential capacity to contribute to one or more environmental objectives can vary across sectors, the TSC should ensure that relevant economic activities within a specific sector can qualify as environmentally sustainable and are treated equally if they equally contribute to one or more environmental objectives. However, within each sector, they should not unfairly disadvantage certain economic activities over others if all contribute to the environmental objectives to the same extent.

Third, in order to avoid overly burdensome compliance costs on economic operators, the TSC must provide for sufficient legal clarity, be practicable and easy to apply, while, in order to avoid unnecessary administrative burden, verification of compliance therewith within reasonable cost-of-compliance boundaries should also be granted.

Furthermore, if sufficiently practicable and necessary, the TSC could require carrying out a life-cycle assessment.

Finally, in order to ensure that private investments are channeled towards economic activities that make the greatest positive impact on the environmental objectives, the Commission should prioritise the establishment of TSC for economic activities that potentially contribute most to such objectives.

(2) In establishing and updating the TSC for the environmental objective of climate change mitigation, the Commission should take into account and provide incentives for the ongoing and necessary transition towards a climate-neutral economy in accordance with **Article 10(2)**. In addition to the use of climate-neutral energy and

⁸⁶ See below, **under 2**.

⁸⁷ **TR**, recitals (38), (45) and (47)-(48).

⁸⁸ On this Platform, referred to in Article 20, see **Section E below, under 1.1**.

more investments in already low-carbon economic activities and sectors, the transition requires substantial reductions in greenhouse gas emissions in other economic activities and sectors for which there are not any technologically and economically feasible low-carbon alternatives. These transitional economic activities should qualify as contributing substantially to climate change mitigation if their greenhouse gas emissions are substantially lower than the sector or industry average, do not hamper the development and deployment of low-carbon alternatives and do not lead to a lock-in of assets incompatible with the objective of climate-neutrality, considering the economic lifetime of those assets. Furthermore, the TSC should ensure the existence of a credible path towards climate-neutrality and should be adjusted accordingly at regular intervals.⁸⁹

(3) Finally, appropriate TSC must be established for the transport sector, including for mobile assets, which should take into account that this sector, including international shipping, contributes close to 26% of total greenhouse gas emissions in the EU. As stated in the 2018 “**Action Plan on Financing Sustainable Growth**”⁹⁰ the transport sector represents about 30% of the additional annual investment needed for sustainable development in the EU, e.g., to increase electrification or to support the transition to cleaner modes of transport by promoting modal shift and better traffic management.⁹¹

2. The provisions of Article 19

(1) On the basis of the above considerations, TSC must meet the following requirements:⁹²

- (a) identify the most relevant potential contributions to the given environmental objective, while respecting the principle of technological neutrality, considering both the short- and long-term impact of a given economic activity;
- (b) specify the minimum requirements to be met in order to avoid significant harm to any of the environmental objectives, considering both the short- and long-term impact of each economic activity;
- (c) be quantitative and, to the extent possible, contain thresholds; otherwise be qualitative;
- (d) where appropriate, build upon EU labelling and certification schemes, methodologies for assessing environmental footprint, and statistical classification systems, and take into account any relevant existing EU legislation;

⁸⁹ TR, recital (41).

⁹⁰ See above in **Section A, under 1.1 (2)**.

⁹¹ TR, recital (49).

⁹² *Ibid.*, Article 19(1).

- (e) to the extent feasible, use existing sustainability indicators as proposed by the European Parliament in its Resolution of 29 May 2018 on sustainable finance and referred to in **Article 4(6) SFDR**, in order to ensure the reliability, consistency and comparability of sustainability-related disclosures in the financial services sector;
 - (f) be based on conclusive available scientific evidence and if scientific evaluation does not allow for a risk to be determined with sufficient certainty, the **precautionary principle** should apply in accordance with **Article 191 TFEU**;⁹³
 - (g) take into account the life-cycle, including evidence from existing assessments, by considering the environmental impact of both the economic activity itself and of the products and services provided by that economic activity, in particular by considering the production, use and end of life of those products and services;
 - (h) take into account the nature and scale of the economic activity, including whether it is an enabling or a transitional one as referred to in **Articles 16 and 10(2)**;⁹⁴
 - (i) take into account the potential market impact of the transition to a more sustainable economy, including the risk of certain assets becoming stranded as a result of such transition and that of creating inconsistent incentives for investing sustainably;
 - (j) cover all relevant economic activities within a specific sector and ensure that those are treated equally if they equally contribute towards the environmental objectives in order to avoid distorting competition in the market; and
 - (k) be easy to use and set in a manner facilitating the verification of their compliance.
- (2) The TSC must also: include criteria for activities related to the clean energy transition consistent with a pathway to limit the temperature increase to 1,5 °C above pre-industrial levels (in particular energy efficiency and renewable energy) to the extent that these substantially contribute to any of the environmental objectives; ensure that power generation activities using solid fossil fuels do not qualify as environmentally sustainable;⁹⁵ and include criteria for activities related to the switch to clean or climate-neutral mobility (e.g., through modal shift, efficiency

⁹³ On this requirement, see also recital (40), third and fourth sentences. On **Article 191 TFEU**, see by means of mere indication **A. Kaller (2019)**: Artikel 191 des AEUV, in Schwarze, J., Becker, U., Hatje, A. und J. Schoo (2019, Hrsg.): *EU-Kommentar*, 4. Auflage, Nomos Verlagsgesellschaft, Baden-Baden, pp. 2436-2452 (with extensive further references to primary and secondary sources).

⁹⁴ On these Articles, see **Section B above, under 2.1.2**. The TSC must clearly indicate that fact that the economic activity belongs to one of these categories.

⁹⁵ On this aspect, see also **Section B above, under 2.1.1 (1)**.

measures and alternative fuels, to the extent that these substantially contribute to any environmental objective).⁹⁶

3. Specific provisions

(1) **Articles 10-15** contain specific provisions with regard to the TSC provided therein. In particular, the Commission must adopt a delegated act in accordance with **Article 23** to supplement: *first*, **Article 10(1)-(2)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to climate change mitigation; *second*, **Article 11(1)-(2)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to climate change adaptation; *third*, **Article 12(1)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to sustainable use and protection of water and marine resources; *fourth*, **Article 13(1)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to the transition to a circular economy; *fifth*, **Article 14(1)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to pollution prevention and control; and *sixth*, **Article 15(1)** by establishing TSC for determining the conditions under which a specific economic activity qualifies as contributing substantially to the protection and restoration of biodiversity and ecosystems.⁹⁷

(2) In all cases, the delegated act must also supplement **Article 17**⁹⁸ by establishing, for each relevant environmental objective, TSC for determining whether an economic activity causes significant harm to one or more of those objectives.⁹⁹

4. Obligations imposed on the Commission

(1) When establishing and updating the TSC, the Commission should assess whether their establishment would give rise to stranded assets, result in inconsistent incentives or have any other adverse impact on financial markets.¹⁰⁰ It must also take into account:

first, **Regulations (EC) No 1221/2009** of the European Parliament and of the Council of 25 November 2009 “on the voluntary participation by organisations in a Community eco-management and audit scheme (EMAS) (...)”, and **(EC) No**

⁹⁶ **TR**, Article 19(2), (3) and (4), respectively.

⁹⁷ *Ibid.*, Articles 10(3), point (a), 11(3), point (a), 12(2), point (a), 13(2), point (a), 14(2), point (a) and 15(2), point (a).

⁹⁸ See **Section B above, under 3**.

⁹⁹ **TR**, Articles 10(3), point (b), 11(3), point (b), 12(2), point (b), 13(2), point (b), 14(2), point (b) and 15(2), point (b).

¹⁰⁰ *Ibid.*, recital (46).

66/2010 “on the EU Ecolabel”,¹⁰¹ its **Recommendation 2013/179/EU** of 9 April 2013 “on the use of common methods to measure and communicate the life-cycle environmental performance of products and organisations”¹⁰² and its **Communication** of 16 July 2018 on “Public procurement for a better environment”;¹⁰³

second, the statistical classifications in the environmental goods and services sector in order to avoid inconsistencies with existing classifications of economic activities for other purposes;¹⁰⁴ *third*, existing environmental indicators and reporting frameworks, developed (*inter alia*) by itself and the European Environment Agency, as well as existing international standards, such as those developed (*inter alia*) by the OECD; and

finally, the specificities of the infrastructure sector, as well as environmental, social and economic externalities within a cost-benefit analysis, taking into account several related sectoral **Directives** of the European Parliament and of the Council,¹⁰⁵ standards and current methodology, as well as the work of international organisations, such as the OECD; the TSC should promote appropriate governance frameworks integrating environmental, social and governance (ESG) factors as referred to in the UN-supported **Principles for Responsible Investment (PRI)**¹⁰⁶ at all stages of a project’s life-cycle.¹⁰⁷

(2) Prior to adopting the above-mentioned delegated acts, the Commission must consult the Platform on Sustainable Finance regarding the TSC. The TSC referred to in **Articles 10-15** must each be adopted in one delegated act, taking into account the

¹⁰¹ OJ L 342, 22.12.2009, pp. 1-45 and OJ L 27, 30.1.2010, pp. 1-19, respectively.

¹⁰² OJ L 124, 4.5.2013, pp. 1-210.

¹⁰³ COM (2008) 400.

¹⁰⁴ These include the classification of environmental protection activities (**CEPA**) and resource management activities (**CRema**) pursuant to **Regulation (EU) No 538/2014** of the European Parliament and of the Council of 16 April 2014 “amending Regulation (EU) No 691/2011 on European environmental economic accounts” (OJ L 158, 27.5.2014, pp. 113-124).

¹⁰⁵ **Directive 2001/42/EC** of 27 June 2001 “on the assessment of the effects of certain plans and programmes on the environment” (OJ L 197, 21.7.2001, pp. 30-37), **Directive 2011/92/EU** of 13 December 2011 “on the assessment of the effects of certain public and private projects on the environment” (OJ L 26, 28.1.2012, pp. 1-21), and **Directives 2014/23/EU, 2014/24/EU and 2014/25/EU** of 26 February 2014 “on the award of concession contracts”, “on public procurement (...)” and “on procurement by entities operating in the water, energy, transport and postal services (...)” (OJ L 94, 28.3.2014, pp. 1-64, 65-242 and 243-374, respectively).

¹⁰⁶ The PRI is a leading proponent of responsible investment, working to understand the investment implications of ESG factors and to support its international network of investor signatories in incorporating these factors into their investment and ownership decisions. It acts in the long-term interests of its signatories, as well as of the financial markets and economies in which they operate (see at: <https://www.unpri.org>).

¹⁰⁷ **TR**, recitals (43)-(44) and (46).

requirements of **Article 19**.¹⁰⁸ It must also regularly review the TSC and, where appropriate, amend the relevant delegated acts in line with scientific and technological developments.¹⁰⁹

D. Disclosure requirements for environmentally sustainable investments

1. Considerations and relationship to the SFDR

(1) In order to avoid harming investor interests and as already noted,¹¹⁰ the TR introduces specific disclosure requirements for environmentally sustainable investments. In this respect, **recital (18)** makes the following considerations:

First, fund managers and institutional investors that make available financial products should disclose how and to what extent they use the criteria for environmentally sustainable economic activities to determine the environmental sustainability of their investments.¹¹¹ The information disclosed should enable investors to understand the proportion of the investments underlying the financial product in environmentally sustainable economic activities as a percentage of all investments underlying it, thereby enabling them to understand the degree of investments' environmental sustainability.

Second, if these investments are in economic activities that contribute to environmental objectives, the information to be disclosed should specify the objective or objectives to which these investments contribute, as well as how and to what extent they fund environmentally sustainable economic activities. The information should also include details on the respective proportions of enabling and transitional activities.

Third, the information that needs to be disclosed should be specified by the Commission and should enable national competent authorities (NCAs) to easily verify compliance with that disclosure obligation and to enforce such compliance in accordance with applicable national law.

¹⁰⁸ *Ibid.*, Articles 10(4)-(5), 11(4)-(5), 12(3)-(4), 13(3)-(4), 14(3)-(4) and 15(3)-(4); on Article 19, see **above, under 1**.

¹⁰⁹ *Ibid.*, Article 19(5), first sentence. In that context, before amending or replacing a delegated act, the Commission must assess the implementation of those criteria taking into account the outcome of their application by financial market participants and their impact on capital markets, including on the channelling of investment into environmentally sustainable economic activities. To ensure that economic activities as referred to in **Article 10(2)** remain on a credible transition pathway consistent with a climate-neutral economy, the Commission must review the TSC for those activities at least every three years and, where appropriate, amend the delegated act referred to in **Article 10(3)** in line with scientific and technological developments (*ibid.*, Article 19(5), second and third sentences).

¹¹⁰ See **Section A above, under 1.2**.

¹¹¹ On this aspect, see also the analytical considerations in recital (13).

Finally, in cases where financial market participants do not take the criteria for environmentally sustainable investments into account, they should provide a statement to that end. In order to avoid the circumvention of the disclosure obligation, this should also apply where financial products are marketed as promoting environmental characteristics, including financial products that have as their objective environmental protection in a broad sense.

(2) The disclosure obligations laid down in the TR supplement the rules on sustainability-related disclosures laid down in the SFDR. In particular, in order to enhance transparency and to provide an objective point of comparison by financial market participants to end investors on the proportion of investments that fund environmentally sustainable economic activities, the TR supplements the rules on disclosures (transparency) in pre-contractual disclosures and in periodic reports laid down in the SFDR.¹¹²

(3) In exceptional cases relating to economic activities carried out by undertakings not required to disclose information under the TR and for which complete, reliable and timely information cannot be obtained, financial market participants can make complementary assessments and estimates on the basis of information obtained from other sources. In order to ensure that the disclosure to end investors is clear and not misleading, financial market participants should clearly explain the basis for their conclusions and the reasons for having to make such complementary assessments and estimates.¹¹³

2. The provisions of Articles 5-7

2.1 Disclosure of environmentally sustainable investments in pre-contractual disclosures and in periodic reports

When a financial product as referred to in **Article 9(1), (2) or (3) SFDR**¹¹⁴ invests in an economic activity that contributes to an environmental objective within the

¹¹² It is noted that the definition of ‘sustainable investment’ in the SFDR includes investments in economic activities that contribute to an environmental objective which, *inter alia*, should include those into ‘environmentally sustainable economic activities’ within the meaning of the TR. Moreover, the SFDR only considers an investment to be a sustainable investment if it does not significantly harm any environmental or social objective as set out therein (*ibid.*, recital (19)).

¹¹³ *Ibid.*, recital (21). Economic operators not covered by the TR may be encouraged to publish and disclose information on their websites on a voluntary basis on the environmentally sustainable economic activities they carry out, which will assist financial market participants to easily identify which economic operators carry out environmentally sustainable economic activities and facilitate the latter to raise funds for their environmentally sustainable activities (*ibid.*, recital (15)).

¹¹⁴ Article 9(1) SFDR refers to financial products whose objective is sustainable investment and contain an index designated as a reference benchmark; Article 9(2) refers to financial products with the same objective but no index has been designated as a reference

meaning of **Article 2, point (17)** thereof, the information to be disclosed in accordance with **Articles 6(3)** and **11(2)** thereof must include the following:

first, the information on the environmental objective(s) to which the investment underlying the financial product contributes; and

second, a description of how and to what extent the investments underlying the financial product are in economic activities qualifying as environmentally sustainable pursuant to **Article 3 TR**, which must specify the proportion of investments in environmentally sustainable economic activities selected for the financial product, including details on the proportions of enabling and transitional activities referred to in **Articles 16 and 10(2)**,¹¹⁵ respectively, as a percentage of all investments selected for that product.¹¹⁶

2.2 Disclosure of financial products that promote environmental characteristics in pre-contractual disclosures and in periodic reports

The (just) above-mentioned **Article 5 TR** is also applicable, *mutatis mutandis*, where a financial product as referred to in **Article 8(1) SFDR**¹¹⁷ promotes environmental characteristics. For “non-sustainable” products the TR also introduces in this case a requirement to include a statement confirming that the investments underlying the product do not fully take into account the EU criteria for environmentally sustainable economic activities. Hence, the information to be disclosed in accordance with **Articles 6(3)** and **11(2) SFDR** must be accompanied by the following statement: “The “do no significant harm” principle applies only to those investments underlying the financial product that take into account the EU criteria for environmentally sustainable economic activities. The investments underlying the remaining portion of this financial product do not take into account the EU criteria for environmentally sustainable economic activities”.¹¹⁸

2.3 Transparency of other financial products in pre-contractual disclosures and in periodic reports

If a financial product is not subject to any of the above-mentioned (under 2.1 and 2.2) SFDR Articles, the information to be disclosed in accordance with the provisions of sectoral legislation referred to in **Articles 6(3)** and **11(2)** thereof must be

benchmark; and Article 9(3) refers to financial products whose objective is a reduction in carbon emissions.

¹¹⁵ On these Articles, see **Section B above, under 2.1 (1), in finem, and (2)**.

¹¹⁶ **TR**, Article 5.

¹¹⁷ Article 8(1) SFDR refers to financial products which promote, *inter alia*, environmental or social characteristics, or a combination thereof, provided that the companies in which the investments are made follow good governance practices.

¹¹⁸ **TR**, Article 6.

accompanied by the following statement: “The investments underlying this financial product do not take into account the EU criteria for environmentally sustainable economic activities”.¹¹⁹

3. Competent authorities – measures and penalties

(1) The monitoring of financial market participants’ compliance with the requirements laid down in **Articles 5-7 TR** has been assigned to the NCAs referred to in **Article 14(1) SFDR**. These must have all the necessary supervisory and investigatory powers for the exercise of their functions under the TR, cooperate and provide each other, without undue delay, with such information as is relevant for the purposes of carrying out their duties.¹²⁰

(2) Furthermore, in order to enforce compliance, Member States must lay down rules on effective, proportionate and dissuasive measures and penalties applicable to infringements of **Articles 5-7 TR**.¹²¹ NCAs and the ESAs should exercise the product intervention powers laid down in three relevant Regulations of the European Parliament and of the Council¹²² also with respect to mis-selling practices or misleading disclosures of sustainability-related information, including the information required under the TR.¹²³

4. The provisions of Article 8 on non-financial reporting

(1) The TR imposes additional requirements on **undertakings**, which are covered by the field of application of the **EU Non-Financial Reporting Directive (2013/34/EU)**. In particular, any undertaking which is subject to an obligation to publish non-financial information pursuant to **Articles 19a or 29a** of that legislative act must include in its non-financial statement or consolidated non-financial statement information on how and to what extent its activities are associated with economic activities qualifying as environmentally sustainable under (the above-mentioned) **Articles 3 and 9 TR**.¹²⁴ The information to be disclosed, which is considered as useful

¹¹⁹ *Ibid.*, Article 7.

¹²⁰ *Ibid.*, Article 21 and recital (55), second sentence.

¹²¹ *Ibid.*, Article 22 and recital (55), third sentence.

¹²² Notably: **Regulation (EU) No 600/2014** of 15 May 2014 “on markets in financial instruments (...)” (OJ L 173, 12.6.2014, pp. 84-138, **MiFIR**); **Regulation (EU) No 1286/2014** of 26 November 2014 “on key information documents for packaged retail and insurance-based investment products (PRIIPs)” (OJ L 352, 9.12.2014, pp. 1-23); and **Regulation (EU) 2019/1238** of 20 June 2019 “on a pan-European Personal Pension Product (PEPP)” (OJ L 198, 25.7.2019, pp. 1-63).

¹²³ **TR**, recital (55), fourth sentence.

¹²⁴ This requirement is based on the **Commission Communication of 20 June 2019** “Guidelines on non-financial reporting: Supplement on reporting climate-related information”, which recommends that certain large companies report on certain climate-

to investors interested in companies whose products and services contribute substantially to any of the environmental objectives, contains two pillars: *first*, the proportion of turnover derived from products or services associated with economic activities that qualify as environmentally sustainable; and *second*, the proportion of capital expenditure (**CapEx**) and of operating expenditure (**OpEx**) related to assets or processes associated with environmentally sustainable economic activities.¹²⁵

(2) By **1 June 2021**, the Commission must adopt a delegated act specifying the content and presentation of the information to be disclosed in accordance with the above-mentioned, including the methodology to be used in order to comply with them, taking into account the specificities of both financial and non-financial undertakings and the TSC established.¹²⁶

E. Other provisions

1. Advisory bodies

1.1 The Platform on Sustainable Finance

1.1.1 Rationale, composition, constitution

(1) When developing the TSC, the Commission should carry out appropriate consultations in line with the Better Regulation Agenda,¹²⁷ while the process for their establishment and updating should involve relevant stakeholders and build on the advice of experts who have proven knowledge and experience in the relevant areas.¹²⁸ Based on these considerations, the Commission should set up of a multi-stakeholder “Platform on Sustainable Finance” (the **Platform**), which is, indeed, operational since **October 2020**.¹²⁹

(2) The Platform is chaired by the Commission¹³⁰ and is composed, in a balanced manner, of experts representing both the public and private sector as well as the civil society: *public-sector experts* include representatives of the European Environmental Agency, the European Supervisory Authorities (**ESAs**), the

related key performance indicators (**KPIs**) on the basis of the TR framework (*ibid.*, recital (22), first sentence).

¹²⁵ *Ibid.*, Article 8(1)-(2). If an undertaking publishes non-financial information pursuant to the above-mentioned Articles 19a or 29a in a separate report pursuant to **Articles 19a(4) or 29a(4)**, this information must be published in that separate report (*ibid.*, Article 8(3)). Smaller companies may voluntarily decide to publish such information as well (*ibid.*, recital (22), last sentence).

¹²⁶ *Ibid.*, Article 8(4).

¹²⁷ See below, **under 2**.

¹²⁸ **TR**, recital (50), first and second sentences.

¹²⁹ See at: https://ec.europa.eu/info/publications/sustainable-finance-platform_en.

¹³⁰ **TR**, Article 20(4), first sentence.

European Investment Bank (EIB) and the EU Agency for Fundamental Rights; *private sector experts* include representatives of financial and non-financial market participants and business sectors, representing relevant industries, and persons with accounting and reporting expertise; and *experts representing civil society* include experts in the field of environmental, social, labour and governance issues. Further members of the Platform are experts appointed in a *personal capacity*, with proven knowledge and experience in the areas covered by the TR, as well as of experts representing *academia*, including persons with global expertise.¹³¹

(3) The Platform is constituted in accordance with the horizontal rules on the creation and operation of Commission expert groups, including with regard to the selection process, which should aim to ensure a high level of expertise, geographical and gender balance, as well as a balanced representation of relevant know-how, taking into account the Platform's specific tasks. During the selection process, the Commission should perform an assessment in accordance with those horizontal rules to determine whether potential conflicts of interest exist and should take appropriate measures to resolve any such conflicts. In that context, the Commission may invite experts with specific expertise on an *ad hoc* basis.¹³²

The minutes of the Platform's meetings and other relevant documents must be published on the Commission's website. In order to ensure the efficient and sustainable organisation of its work and meeting practices and to enable broad participation and efficient interaction within the groups, their subgroups, the Commission and stakeholders, the Platform should consider, where appropriate, the increased use of digital, including virtual, technologies.¹³³

1.1.2 Role

(1) The main role of the Platform is to advise the Commission on the development, analysis and review of TSC, including the potential impact of such criteria on the valuation of assets that qualify as environmentally sustainable assets under existing market practices, and on the potential need to update them. Its advisory role is further extended to the following issues: where appropriate, on the possible role of sustainability accounting and reporting standards in supporting the application of the TSC; on the possible need to develop further measures to improve data availability and quality; on the usability of the TSC in future EU policy initiatives aimed at facilitating sustainable investment, taking into account the objective of avoiding undue administrative burdens; on the possible need to amend the TR; on the evaluation and development of sustainable finance policies, including with regard to policy coherence issues; on addressing other sustainability objectives, including social objectives; and on the application of **Article 18** (on the functioning

¹³¹ *Ibid.*, Article 20(1) and recital (50), fourth – seventh sentences.

¹³² *Ibid.*, Article 20(4), first and second sentences, and recital (51).

¹³³ *Ibid.*, Article 20(5) and recital (56).

of minimum safeguards¹³⁴) and the need to supplement the requirements thereof. Furthermore, the Platform must analyse the impact of the TSC in terms of potential costs and benefits of their application; assist the Commission in analysing requests from stakeholders to develop or revise TSC for a given economic activity; as well as monitor and regularly report to the Commission on trends at EU and Member State level regarding capital flows into sustainable investment.¹³⁵ It must take into account the views of a wide range of stakeholders and carry out its tasks in accordance with the transparency principle.¹³⁶

(2) In order to help the Commission in evaluating the appropriateness of complementing or updating the TSC, financial market participants are encouraged to inform it if they consider that an economic activity that does not meet the TSC, or for which such criteria have not yet been established, should qualify as environmentally sustainable.¹³⁷

1.2 Formalisation of the Member State Expert Group on Sustainable Finance

The TR provides that the (existing) “**Member State Expert Group on Sustainable Finance**” (i.e., the TEG)¹³⁸ should be vested a formal status and, *inter alia*, advise the Commission on the appropriateness of the TSC and the approach taken by the Platform regarding their development pursuant to **Article 19**. For this purpose, the Commission must keep the Member States informed through regular meetings of that Group in order to facilitate an exchange of views between them on a timely basis, in particular as regards the main output of the Platform, such as new TSC, material updates thereof or draft reports.¹³⁹

2. Exercise of the delegation

(1) In order to specify the requirements set out in the TR, and in particular to establish and update for different economic activities granular and calibrated TSC for what constitutes ‘**substantial contribution**’ and ‘**significant harm**’ to the environmental objectives, the power to adopt delegated acts (in accordance with Article 290 TFEU) in respect of the content and presentation of the information referred to in **Article 8(4)**,¹⁴⁰ as well as in respect of the TSC laid down in **Articles**

¹³⁴ See **Section B above, under 4**.

¹³⁵ **TR**, Article 20(2) and recital (52).

¹³⁶ *Ibid.*, Article 20(3).

¹³⁷ *Ibid.*, Article 20(6) and recital (50), last sentence.

¹³⁸ See above in **Section A, under 1.1 (2)**.

¹³⁹ **TR**, Article 24 and recital (53). As in the case of the Platform, the increased use of digital, including virtual, technologies should be considered, where appropriate (*ibid.*, recital (56)).

¹⁴⁰ See **Section D above, under 3 (2)**.

10(3), 11(3), 12(2), 13(2), 14(2) and 15(2)¹⁴¹ has been conferred on the Commission for an indeterminate period from **12 July 2020**. This delegation of powers may be revoked at any time by the European Parliament or by the Council, by a decision putting an end to the delegation of specified therein, taking effect on the day following its publication in the *OJ* or at a later date specified therein and not affecting the validity of any delegated acts already in force.¹⁴²

(2) The Commission must notify any delegated act adopted simultaneously to the European Parliament and to the Council; such delegated act will enter into force only if no objection has been expressed by either of these two EU institutions within a period of four months of notification of that act to them or if, before the expiry of that period, both these EU institutions have informed the Commission that they will not object. That period can be extended by two months at the initiative of the European Parliament or of the Council.¹⁴³

3. Amendments to the SFDR

(1) In order to ensure consistency between the two **fundamental EU sustainability-related** legislative acts, the TR amends the **SFDR**, inserting, *inter alia*, an obligation for the ESAs to jointly develop RTSs further specifying the details of the content and presentation of the information in relation to the “do no significant harm” principle; draft RTSs must be provided to the Commission by **30 December 2020**.¹⁴⁴ These must be consistent with the content, methodologies and presentation of the sustainability indicators in relation to adverse impacts as referred to in the SFDR; they must also be compliant with the principles enshrined in the **European Pillar of Social Rights**, the **OECD Guidelines for Multinational Enterprises**, the UN Guiding Principles on Business and Human Rights, including the ILO Declaration on Fundamental Principles and Rights at Work, the eight fundamental conventions of the ILO and the International Bill of Human Rights.¹⁴⁵

¹⁴¹ See **Section C above, under 3**.

¹⁴² **TR**, Article 23(1)-(3) and recital (54), first sentence. The Commission must gather all necessary expertise, prior to the adoption and during the development of delegated acts, including through the consultation of the experts of the Expert Group on Sustainable Finance. Before adopting a delegated act, it must act in accordance with the principles and procedures laid down in the **Interinstitutional Agreement** of 13 April 2016 “on Better Law-Making” (OJ L 123, 12.5.2016, pp. 1-14). In particular, to ensure equal participation in the preparation of delegated acts, the European Parliament and the Council should receive all documents at the same time as Member States’ experts, and their experts should systematically have access to meetings of Commission expert groups dealing with the preparation of delegated acts (*ibid.*, Article 23(4) and recital (54), second and third sentences).

¹⁴³ *Ibid.*, Article 23(5)-(6).

¹⁴⁴ *Ibid.*, **Article 25** and recital (36), first sentence.

¹⁴⁵ *Ibid.*, recital (36), second and third sentences; see also **above in Section B, under 4**.

(2) The SFDR has been further amended to mandate the ESAs to develop, through the **Joint Committee**, draft RTSs to supplement the rules on transparency of the promotion of environmental characteristics and of environmentally sustainable investments in pre-contractual disclosures and in periodic reports.¹⁴⁶

4. Review clause

(1) By **13 July 2022**, and subsequently every three years thereafter, the Commission must publish a Report on the application of the TR, evaluating the following aspects:¹⁴⁷

first, the progress in its implementation with regard to the development of TSC for environmentally sustainable economic activities;

second, the possible need to revise and complement the criteria set out in Article 3 for an economic activity to qualify as environmentally sustainable;

third, the use of the definition of environmentally sustainable investment both in EU law and at Member State level, including the provisions required for setting up verification mechanisms of compliance with the criteria set out in the TR;

fourth, the effectiveness of the application of the TSC in channeling private investments into environmentally sustainable economic activities and in particular as regards capital flows, including equity, into private enterprises and other legal entities, both through financial products covered by the TR and other financial products;

fifth, the access by financial market participants covered by the TR and by investors to reliable, timely and verifiable information and data regarding private enterprises and other legal entities, including investee companies within and outside its scope and, in both cases, as regards equity and debt capital, taking into account the associated administrative burden, as well as the procedures for the verification of the data necessary for determining the degree of alignment with the TSC and to ensure compliance with those procedures; and

finally, the application of Articles 21-22 on NCAs, measures and penalties.¹⁴⁸

(2) The Commission must also publish, by **31 December 2021**, a report describing the necessary provisions in order to meet the following goals: extend the TR's scope **beyond environmentally sustainable economic activities**; cover economic activities that do not have a significant impact on environmental sustainability and

¹⁴⁶ *Ibid.*, **Article 25** and recital (37). On the Joint Committee, see **Gortsos, Ch.V. (2020): European Central Banking Law – The Role of the European Central Bank and National Central Banks under European Law**, Palgrave Macmillan Studies in Banking and Financial Institutions, Palgrave Macmillan Springer, Cham – Switzerland, p. 127; see also at: <https://esas-joint-committee.europa.eu>.

¹⁴⁷ *Ibid.*, Article 26(1) and recital (59).

¹⁴⁸ On Articles 21-22, see **Section D above, under 3**.

significantly harm it, as well as a review of the appropriateness of specific disclosure requirements related to transitional and enabling activities; and also cover **social objectives**. Furthermore, by **13 July 2022**, it must assess the effectiveness of the **advisory procedures** for the development of the TSC established under the TR.¹⁴⁹

5. Start of application

(1) The Commission delegated acts on the first two **climate-related objectives** (i.e., climate change mitigation and adaptation) must be adopted by 31 December 2020 and will apply from 1 January 2022.¹⁵⁰ Those on the other four environmental objectives will have to be adopted by the Commission by 31 December 2021 and will apply from 1 January 2023.¹⁵¹

(2) In order to allow relevant actors to familiarise themselves with the criteria for qualification as environmentally sustainable economic activities and to prepare for their application, the **disclosure obligations** set out in the TR will apply 12 months after the establishment of the relevant TSC, depending on the environmental objective they relate to. In particular, **Articles 4-7** and **8(1)-(3)** will apply in respect of the first two **climate-related objectives** from 1 January 2022; and in respect of the other four remaining four environmental objectives from 1 January 2023.¹⁵²

F. Concluding remarks

1. A summary

(1) The Taxonomy Regulation (TR), adopted in 2019, is a key milestone in defining legally sustainable activities. It should be viewed within the context of the climate and energy targets set by the EU for 2030 in order to become climate-neutral by 2050, and constitutes, along with the Sustainable Finance Disclosure Regulation (SFDR) and the **Low Carbon Benchmarks Regulation**, the regulatory ‘trilogy’ implementing the CMU Action Plan in relation to sustainable finance. It substantially builds on the 2020 Report of the Technical Expert Group on Sustainable Finance (TEG), which developed the “EU taxonomy” classification system to determine whether an economic activity can qualify as environmentally

¹⁴⁹ TR, Article 26(2)-(3).

¹⁵⁰ *Ibid.*, Articles 10(6) and 11(6). The Draft Delegated Act on climate change mitigation and climate change adaptation were published on November 20, containing a draft Delegated Regulation, Annex I on the climate change mitigation environmental objective (233 pages) and Annex II on the climate change adaptation objective (281 pages); available at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12302-Climate-change-mitigation-and-adaptation-taxonomy#ISC_WORKFLOW.

¹⁵¹ *Ibid.*, Articles 12(5), 13(5), 14(5) and 15(5).

¹⁵² *Ibid.*, Article 27(2), first sub-paragraph and recital (57).

sustainable.¹⁵³ The system of its rules is anchored in the definition of six specific environmental objectives,¹⁵⁴ which constitute the benchmark on the basis of which an economic activity can be assessed to qualify as environmentally sustainable and, hence, the degree to which a financial investment is environmentally sustainable is established.

For this latter purpose, an economic activity qualifies as environmentally sustainable if it substantially contributes to one or more environmental objectives, does not significantly harm any other environmental objective, is carried out in compliance with specific safeguards¹⁵⁵ and complies with applicable technical screening criteria (TSC), as set out in the delegated acts to be adopted by the Commission pursuant to the TR.¹⁵⁶ When developing the TSC, the Commission is assisted by the advisory Platform on Sustainable Finance, composed of experts representing the public sector, the private sector and the civil society. It is also advised by the Expert Group on Sustainable Finance on the appropriateness of the TSC and the approach taken by the Platform regarding their development.¹⁵⁷ The delegated acts will be adopted in two stages: those on climate change mitigation and adaptation by 31 December 2020 (and will apply from 1 January 2022) and those on the other four objectives by 31 December 2021 (to apply from 1 January 2023).¹⁵⁸

(2) The TR applies to any measures adopted by Member States or by the EU setting out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable, to financial market participants that make available environmentally sustainable financial products and to undertakings which are subject to the obligation to publish a non-financial statement or a consolidated non-financial statement pursuant to the EU Non-Financial Reporting Directive and issue environmentally sustainable corporate bonds. In order to avoid harming investor interests, it introduces specific disclosure requirements for marketing financial products or corporate bonds as environmentally sustainable investments. These obligations supplement the sustainability-related disclosure rules of the SFDR in pre-contractual disclosures and in periodic reports; in this respect, firms will have to consider the impact that the new rules will have at both entity and product

¹⁵³ See **Section A, under 1.1.**

¹⁵⁴ See **Section A, under 3.**

¹⁵⁵ See **Section B, under 2-4, respectively.**

¹⁵⁶ See **Section C and Section E, under 2.**

¹⁵⁷ See **Section E, under 1**

¹⁵⁸ See **Section E, under 1 and 5 (1).**

level.¹⁵⁹ Furthermore, in order to ensure consistency between the two TR and the SFDR, the former amends the latter.¹⁶⁰

(3) It is finally noted that the TR contains a review clause, on the basis of which, by 13 July 2022, the Commission must publish a Report on its application, evaluating, *inter alia*, the progress in its implementation with regard to the development of TSC for environmentally sustainable economic activities, the potential need to revise and complement the TSC set out for an economic activity to qualify as environmentally sustainable and the effectiveness of the application of the TSC in channeling private investments into such economic activities. Furthermore, and most importantly, by 31 December 2021, the Commission must publish a Report describing the necessary provisions in order to extend the TR's scope beyond environmentally sustainable economic activities and cover both economic activities that do not have a significant impact on environmental sustainability and significantly harm it, as well as social objectives.¹⁶¹

2. The impact on credit institutions' management and supervision of ESG risks

(1) The significance of the impact of the TR is not confined to the firms which are directly covered by its scope and the disclosure requirements imposed on them. The EU taxonomy classification system, which constitutes the core of this legislative act, will be taken over in other sources of EU financial regulation, which apply to credit institutions, investment firms and investment fund managers, as well as insurance companies.¹⁶² Even though the TR in itself is a legal instrument setting out disclosure requirements only and does not **directly** apply to the lending activities of credit institutions, its impact on the latter activity is significant **indirectly** through Guides developed by the European Central Bank (ECB)¹⁶³ and to be developed by the European Banking Authority (EBA).

(2) Among other related initiatives,¹⁶⁴ on **30 October 2020**, the EBA issued a discussion paper "On management and supervision of ESG risks for credit

¹⁵⁹ See **Section D**.

¹⁶⁰ See **Section E, under 3**.

¹⁶¹ See **Section E, under 4**.

¹⁶² See by means of mere indication **Alexander, K. and P.G. Fisher (2018)**: Banking regulation and sustainability, available at <https://ssrn.com/abstract=3299351> and **Alexander, K. (2019)**, *op. cit.*, pp. 357-364.

¹⁶³ See the ECB "Guide on climate-related and environmental risks: Supervisory expectations relating to risk management and disclosure" of 27 November 2020 (referred to in **Section A above, under 1.1 (2)**).

¹⁶⁴ E.g., "EBA Action Plan on Sustainable Finance", 6 December 2019, available at: https://eba.europa.eu/sites/default/documents/files/document_library//EBA%20Action%20plan%20on%20sustainable%20finance.pdf.

institutions and investment firms (**EBA/DP/2020/03**)”.¹⁶⁵ Its purpose is to define and develop assessment criteria for ‘ESG factors’ that may impact the financial performance and solvency of credit institutions (and investment firms) through their counterparties, as well as to present the EBA’s understanding on the relevance of ‘ESG risks’ for a sound functioning of the financial sector.¹⁶⁶ On the basis of the comments to be collected from stakeholders, the EBA will adopt and submit (expectedly in June 2021) its final Report,¹⁶⁷ which will have:

first, to elaborate on the arrangements, processes, mechanisms and strategies to be implemented by credit institutions (and investment firms) to identify, assess and manage ESG risks, embedding them in their internal governance and risk management frameworks in a proportionate manner; and

second, to assess, under the provisions of the so-called “Pillar 2” of the framework governing the micro-prudential regulation and supervision of credit institutions (and investment firms), the inclusion of ESG factors and ESG risks in the review and evaluation performed by competent (supervisory) authorities (including the ECB for significant credit institutions within the Single Supervisory Mechanism (SSM)).¹⁶⁸

¹⁶⁵ Available at: <https://eba.europa.eu/financial-innovation-and-fintech/sustainable-finance/discussion-paper-management-and-supervision-esg-risks-credit-institutions-and-investment-firms-0>.

¹⁶⁶ ESG factors are defined as environmental, social or governance characteristics, that may have a positive or negative impact on the financial performance or solvency of an entity, sovereign or individual (**EBA/DP/2020/03**, para. 30). ESG risks are defined to mean the risks of any negative financial impact to an institution stemming from the current or prospective impacts of ESG factors on its counterparties and materialise themselves through their impact on prudential risk categories (*ibid.*, para. 38). These include, but are not confined to, the climate-related and environmental risks, as defined in the above-mentioned ECB 2020 Guide (*ibid.*, para. 8, point a). ESG factors, ESG risks and their transmission channels are discussed in detail in Chapter 4 (pp. 20-47), while Chapter 5 (pp. 48-77) develops on quantitative and qualitative indicators, metrics and methods to assess ESG risks. Annex 1 (pp. 141-153) contains a non-exhaustive list of ESG factors, indicators and metrics.

¹⁶⁷ The legal bases of this Report are **Article 98(8) of Directive 2013/36/EU** of the European Parliament and of the Council of 26 June 2013 “on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (...)” (**CRD IV**, OJ L 176, 27.6.2013, pp. 338-436), which was inserted by Article 1, point 29(d) of **Directive (EU) 2019/878** of the same institutions of 7 June 2019 amending the CRD IV (**CRD V**, OJ 150, 7.6.2019, pp. 253-295), and **Article 35 of Directive (EU) 2019/2034** of the same institutions of 27 November 2019 “on the prudential supervision of investment firms” (**IFD**, OJ L 314, 5.12.2019, pp. 64-114).

¹⁶⁸ **EBA/DP/2020/03**, Chapter 6 (pp. 78-117) on the management of ESG risks by credit institutions and investment firms and Chapter 7 (pp. 118-140) on ESG factors and ESG risks in supervision, respectively. Chapter 7 elaborates, in particular, on the effective way to proportionately reflect ESG risks in the supervisory review for credit institutions and makes several related policy recommendations.

The taxonomy framework, as laid down in the TR, will, *inter alia*, be used as one of the benchmarks in this respect.¹⁶⁹

(3) For the sake of completeness, it is noted that the EBA is required to take related action also with regard to the two other Pillars of the regulatory framework. In particular (and taking into account only the provisions relating to credit institutions):

first, in accordance with **Article 501c of Regulation (EU) No 575/2013** of the European Parliament and of the Council of 26 June 2013 “on prudential requirements for credit institutions and investment firms (...)”¹⁷⁰ (**CRR**), which was inserted by **Article 1 of Regulation (EU) 2019/876** of the same institutions of 7 June 2019 amending the CRR¹⁷¹ (**CRR II**), it must assess whether a dedicated prudential treatment of exposures related to assets or activities associated substantially with environmental and/or social objectives would be justified as a component of Pillar 1 capital requirements; and

second, **Article 449a CRR** provides that large credit institutions with publicly listed issuances must, under the Pillar 3 provisions, disclose information on ESG risks, including physical and transition risks; in this respect, the EBA must develop a technical standard implementing this disclosure requirement.¹⁷²

¹⁶⁹ The frequency of references to the TR in the discussion paper (15 times) is notable.

¹⁷⁰ OJ L 176, 27.6.2013, pp. 1-337.

¹⁷¹ OJ 150, 7.6.2019, pp. 1-225.

¹⁷² CRR, Article 434a.

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