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POSITION PAPER

KEY PRINCIPLES FOR AN EFFECTIVE AND INTERNATIONALLY COMPATIBLE TAXONOMY AND A FAIR TRANSITION

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## **1. Introduction**

The EU-Asia Financial Services Roundtable (EUASFRT) welcomes the European Union’s objectives to develop an EU-wide classification system for sustainable activities, which can be used internationally. One of the main challenges of making this taxonomy work globally is determining which activities are and are not sustainable, and whether a standardised approach in determining sustainability will be conducive to channelling capital flows to sustainable activities. In addition to defining sustainable activities, another challenge in developing the taxonomy is to ensure that it will not lead to unintended consequences.

The EUAFSRT supports the largest global alignment as possible on a Taxonomy to level the playing field and create comparable frameworks, which will facilitate global capital flows towards sustainable activities. This is particularly welcomed in emerging economies, where efforts to mitigate climate-change related risks must be maximised.

## **2. Key Principles for an effective taxonomy EU taxonomy**

Against this backdrop, the EUASFRT proposes the following high-level principles for an effective taxonomy:

1. The right available data is necessary for investors to determine which activities their investment is funding or the proportion of revenue of the company, which is derived from sustainable activities. This pre-condition will allow the taxonomy to recognise the reality of investment in public equity.
2. As a pre-requisite for the success of the EU’s taxonomy, the Commission should review rapidly the Non-Financial Reporting Directive and align it as much as possible with the recommendations of the Taskforce on Climate-related Financial Disclosure. Disclosure by corporate entities will allow access to the underlying data needed to use the taxonomy successfully.
3. The EU’s taxonomy should rely on existing frameworks, such as the ICMA’s Green Bonds Principles, which facilitate investors and issuers alike in electing activities classified as green. This will foster international comparability and level the playing field. The EUAFSRT believes that any new initiatives regarding the Taxonomy should first and foremost help harmonize the existing taxonomies and definitions in the market.

4. The EU's taxonomy should cater for both investments in the sustainability of the underlying asset or by the process of investing, either through ESG integration or exclusion of certain activities.
5. The EU taxonomy framework should be sufficiently flexible to evolving market environments. Because of technological and regulatory evolutions, some activities can shift from taxonomy-compliant to non-compliant (or vice-versa). Clear ex-ante mechanisms which give assurance to stakeholders on how the changes will affect them are necessary.

The EU taxonomy needs to be accompanied by a wider political movement, which will set the right conditions for the pace and take-up of the new framework. In this regard, the European Green Deal puts emphasis on the adoption of the EU taxonomy. Moreover, the work on the taxonomy should be carefully coordinated with the revision of the Non-Financial Reporting Directive and the introduction of EU Carbon Tax, which will collectively affect carbon emissions in the EU.

The ease-of-use of the taxonomy will be one of the guaranteed factors of its success. The information of an investment's sustainability must be easy to find, and disclose clearly what the implications will be should investors not be able to acquire the information.

The EUAFSRT suggests the introduction of a standard template for information disclosure by project proponents, assessing alignment with the taxonomy easier. For a limited, introductory period, qualitative data and estimates could be submitted jointly, to encourage the take-up whilst reducing the risk of green washing.

### **3. The international dimension of the taxonomy**

The EUAFSRT strongly encourages the EU taxonomy to be internationally driven and developed along the lines of the initiatives taken by the FSB and G20, to ensure that it is internationally compatible at the greatest extent. Domestic divergences in national taxonomies may prevent comparability and lead to fragmentation. An internationally consistent taxonomy that is harmonized to the fullest extent possible is therefore imperative.

Whilst recognising that the EU plays a central role in the development of a Taxonomy, the EUAFSRT recalls that the FSB and the G20 both play an important role in fostering international cooperation and exchanges of best practices in the development of an international taxonomy. Furthermore, the EUAFSRT encourages initiatives taken by the Network for Greening the Financial System (NGFS), as well the work the European Investment Bank (EIB) is pursuing in partnership with China's Green Finance Committee.

The EUAFSRT welcomes and supports the efforts undertaken by the European Commission to create and develop the International Platform on Sustainable Finance. This Platform is to be seen as an enabling tool to exchange and disseminate information to promote best practices in environmentally sustainable finance, compare the different initiatives and identify barriers and opportunities to help scale up environmentally sustainable finance internationally and enhance international coordination where appropriate on environmentally sustainable finance issues.

International cooperation on a taxonomy needs to take into account the diversity of different local markets and their stage of economic development. This may represent a challenge in global applicability of the taxonomy.

Both the taxonomy and global cooperation should take into account the UN's Sustainable Development Goals (SDGs). If seeking to align the taxonomy with the SDGs, the focus could be on specific targets against which each SDG goal could be measured.

#### **4. A Taxonomy for a fair transition**

Achieving a socially and economically fair transition is a major challenge but also the key for the sustainability transition to work for all. The EUASFRT recognises that, currently, further work is necessary to tackle the challenge of transition. Countries who produce coal and are still largely depend on it in their energy mix will need tailored measures to accompany the phasing-out, with the necessary investments in skill-sets directed towards affected populations to demonstrate that the transition towards a sustainable economy is both right environmentally and fair socially.

Looking at infrastructure investments, the EU's taxonomy must look at accompanying investments to finance improvements to existing infrastructure, even if it does not necessarily meet, post-improvement, "new-build" standards.

Moreover, the EUAFSRT is in favour of developing a stewardship model, which supports the transition. A taxonomy framework which includes stewardship and a variety of existing ESG strategies and practices (exclusionary screening, sustainability-themed investing, integration of ESG factors etc.) would further encourage the financial sector to streamline and standardise sustainable finance and impact investing, which lead to the Paris Agreement goals.

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*The EU-Asia Financial Services Roundtable promotes a shared understanding of the regulatory issues faced by financial markets participants in Europe and Asia, while also shaping the EU-Asian regulatory and policy discussions. Its members are Afore Consulting, AIG, CME Group, DTCC, HSBC, IHS Markit, London Stock Exchange, Moody's, Refinitiv, and Standard Chartered.*

*It supports regulators in developing an appropriate and balanced regulatory framework that enables long-term growth in both Europe and Asia, whilst identifying areas where regulation impedes the international flow of capital or creates unnecessary barriers to doing business. It supports the development of regulatory best practice, and a level playing field in financial services regulation in Europe and Asia, whilst promoting open and stable financial markets.*