Consultation Paper

Draft advice to European Commission under Article 8 of the Taxonomy Regulation

ESMA30-379-325 | 5 November 2020

Responding to this paper

ESMA invites responses to the questions set out throughout this Consultation Paper and summarised in Annex II. Responses are most helpful if they:

- respond to the question stated and indicate the specific question to which they relate;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **4 December 2020**.

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the steps below when preparing and submitting their response:

- Insert your responses to the consultation questions in the form "Response form_Consultation Paper on TR Article 8 advice", available on ESMA's website alongside the present Consultation Paper (www.esma.europa.eu → 'Your input – Open consultations' → 'Consultation on advice under Taxonomy Regulation Article 8').
- Please do not remove tags of the type <ESMA_QUESTION_TRART8_1>. Your response to each question has to be framed by the two tags corresponding to the question.
- If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.
- When you have drafted your response, name your response form according to the following convention: ESMA_TRART8_nameofrespondent_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA_TRART8_ABCD_RESPONSEFORM.
- Upload the form containing your responses, in Word format, to ESMA's website (www.esma.europa.eu under the heading 'Your input – Open consultations' → 'Consultation on advice under Taxonomy Regulation Article 8').

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. If you do not wish for your response to be publicly disclosed, please clearly indicate this by ticking the appropriate box on the website submission page. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

Who should read this paper?

This Consultation Paper may be of particular interest to non-financial undertakings and asset managers covered by Article 8 of Regulation (EU) 2020/852 (the 'Taxonomy Regulation') as well as to investors and other users of non-financial information.

Table of contents

Acronyms and definitions

Accounting Directive	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, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC
AIF	Alternative investment fund
AIFM	Alternative investment fund manager
AIFMD	Directive 2011/61/EU on Alternative Investment Fund Managers and amending Directive 2003/41/EC and 2009/65/EC and Regulation (EC) No 1060/2009 and (EU) No 1095/2010
APM	Alternative performance measure
Asset manager	In relation to a UCITS, the UCITS management company or, in the case of a self-managed UCITS, the UCITS investment company In relation to an AIF, the AIFM or an internally-managed AIF
AuM	Assets under management
CapEx	Capital expenditure
CapEx KPI	Proportion of CapEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation
Commission	European Commission
DNSH	Do not significantly harm
EBA	European Banking Authority
EIOPA	European Insurance and Occupational Pensions Authority
EFRAG	European Financial Reporting Advisory Group
ESAs	European Supervisory Authorities (EBA, EIOPA and ESMA)
ESMA	European Securities and Markets Authority
GAAP	Generally Accepted Accounting Principles

IAS	International Accounting Standard
IAS Regulation	Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standard
IFRS Regulation	Commission Regulation (EC) No 1126/2008 of 3 November 2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council
JRC	Joint Research Centre
KPI	Key performance indicator
NACE	Nomenclature des Activités Économiques dans la Communauté Européenne
Non-Financial Reporting Directive (NFRD)	Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups
OpEx	Operating expenditure
OpEx KPI	Proportion of OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation
PFS	Primary Financial Statements
RTO	Reception and transmission of orders
SFDR	Regulation (EU) 2019/2088 of the European Parliament and of the council of 27 November 2019 on sustainability-related disclosures in the financial services sector
Short-Selling Regulation	Regulation (EU) No 236/2012 of the European Parliament and of the Council of 14 March 2012 on short selling and certain aspects of credit default swaps
Taxonomy Regulation	Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088

TEG	European Commission Technical Expert Group on Sustainable Finance
Turnover KPI	Proportion of turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation
UCITS	Undertaking for collective investment in transferable securities
UCITS Directive	Directive 2009/65/EC on the coordination laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

1 Executive summary

Reasons for publication

Regulation (EU) 2020/852 (the 'Taxonomy Regulation') was published in the Official Journal on 22 June 2020 and entered into force 20 days later.

Article 8 of the Regulation obliges undertakings covered by Directive 2014/95/EU (the 'Non-Financial Reporting Directive') to publish information on how and to what extent their activities are associated with economic activities that qualify as environmentally sustainable under the Taxonomy Regulation. For this purpose, Article 8(2) requires non-financial undertakings to use three key performance indicators ('KPIs'), namely the proportion of their turnover, their capital expenditure ('CapEx') and their operating expenditure ('OpEx') related to environmentally sustainable activities. Article 8 does not specify any KPIs to be used by financial undertakings.

Article 8(4) of the Taxonomy Regulation requires the European Commission (the 'Commission') to adopt a delegated act to supplement the above obligations by specifying the content, presentation and methodology of the information to be disclosed by both financial and non-financial undertakings subject to the Non-Financial Reporting Directive. The Commission has to adopt the delegated act by 1 June 2021.

On 15 September 2020, ESMA received a call for advice from the Commission, requesting input on the following aspects of the delegated act which the Commission shall adopt:

1) How should the three KPIs to be disclosed by non-financial undertakings be further specified?

2) What information should any asset managers subject to the Non-Financial Reporting Directive disclose on how their activities are directed at funding environmentally sustainable economic activities?

On the same date, EBA and EIOPA were also invited to provide similar advice on the delegated act to be adopted within their respective remits. ESMA, EBA and EIOPA are coordinating the three pieces of advice which will be delivered to the Commission.

The deadline for the advice is end of February 2021.

Contents

This Consultation Paper presents a draft version of ESMA's advice to the Commission.

In preparing this draft advice ESMA has conducted targeted outreach with multiple stakeholders in order to more rapidly advance in the development of the draft proposals that are included in this Consultation Paper and to ensure that its draft advice takes into account key considerations in the market.

Section 2 sets out opening considerations on the advice and provides a short introduction to the Taxonomy Regulation.

Section 3 relates to the first part of ESMA's advice concerning non-financial undertakings. Section 3.1 describes the scope of this part of the advice while Section 3.2 goes on to address the content of the three KPIs which non-financial undertakings must mandatorily disclose. Section 3.3 addresses the methodology for preparing these KPIs, and Section 3.4 sets out ESMA's considerations on the presentation of the KPIs within the non-financial statement. Sections 3.2, 3.3 and 3.4 each finish by presenting ESMA's draft advice to the Commission and by posing a number of consultation questions to stakeholders.

Section 4 of the Consultation Paper relates to the second part of ESMA's advice concerning asset managers. Section 4.1 discusses the scope of this part of the advice and Section 4.2 then goes on to provide ESMA's proposals for the content of the KPI to be provided by asset managers. This is followed by considerations on the methodology for preparing the proposed KPI in Section 4.3 and on the way this KPI should be presented in Section 4.4. Again, each of these three sections ends with the actual draft advice which ESMA proposes to submit to the Commission and accompanying consultation questions for stakeholders.

Annex I contains the Commission's call for advice to ESMA, EBA and EIOPA.

Annex II collects all the consultation questions for stakeholders which are presented throughout the Consultation Paper.

Annex III sets out ESMA's proposal for a standardised table for non-financial undertakings to use for the presentation of the three mandatory KPIs.

Annex IV sets out ESMA's proposal for a standardised table for asset managers to use for the presentation of the KPI which ESMA suggests requiring from them.

Annex V presents an analysis providing top-down estimates for the three KPIs included in the call for advice, for the EU economy as a whole and by NACE macro sector, based on a methodology developed by the European Commission's Joint Research Centre ('JRC') report on the EU Taxonomy.

Next steps

When finalising its advice to the Commission, ESMA will consider all feedback received in relation to this Consultation Paper by 4 December 2020. A Final Report containing a summary of all consultation responses and a final version of ESMA's advice is expected to be delivered to the Commission and published on ESMA's website at the end of February 2021.

2 Introduction

2.1 Overview of the Taxonomy Regulation

1. In March 2018, the European Commission (the 'Commission') issued its Action Plan on Financing Sustainable Growth,[1] a key objective of which was to reorient capital flows towards sustainable investment. In the Action Plan, the Commission called for the establishment of an EU classification system for sustainable activities, i.e. an EU Taxonomy. The Commission followed up on this call in May 2018 by publishing a legislative proposal for a regulation to establish this Taxonomy.

2. Upon publication of the Action Plan, the Commission established a Technical Expert Group ('TEG') to assist in preparing several actions under the Action Plan, including the establishment of an EU Taxonomy. The TEG delivered its final report on the Taxonomy in March 2020.[2]

3. Following negotiations between the co-legislators, Regulation (EU) 2020/852 (the 'Taxonomy Regulation') was published in the Official Journal of the European Union on 22 June 2020. The Regulation entered into force on 12 July 2020.

4. The Taxonomy Regulation creates a classification system for sustainable economic activities which is intended to serve as a common language for investors when they try to identify projects and economic activities which have a substantial positive impact on the climate and the environment. As such, the Regulation is intended as a tool to help investors as well as companies, issuers and project promoters in the transition to making the EU climate neutral by 2050.

5. The Regulation applies to financial market participants who offer financial products, financial and non-financial undertakings within the scope of Directive 2014/95/EU (the 'Non-Financial Reporting Directive') and individual Member States and the EU with regard to existing or potentially new eco-labelling or other legislative measures.

6. The Regulation establishes that economic activities shall qualify as environmentally sustainable if they:

    a. Make a substantial contribution to one or more of the following six environmental objectives:

        i. Climate change mitigation

        ii. Climate change adaptation

[1] Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions, *Action Plan: Financing Sustainable Growth*, 8 March 2018.
[2] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020.

iii. Sustainable use and protection of water and marine resources

iv. Transition to a circular economy

v. Pollution prevention and control

vi. Protection and restoration of biodiversity and ecosystems

and

b. Do no significant harm ('DNSH') to the other environmental objectives

and

c. Meet minimum safeguards (for example, UN Guiding Principles on Business and Human Rights)

and

d. Comply with technical screening criteria to be established by the Commission in delegated acts.

7. The technical screening criteria will address both how economic activities can be considered to make a substantial contribution to the environmental objectives and how to respect the DNSH criterion.

8. The TEG's report from March 2020 provided advice to the Commission on technical screening criteria for the first two environmental objectives – climate change mitigation and climate change adaptation. The Commission is required to adopt delegated acts on technical screening criteria for these two first objectives by 31 December 2020, and the delegated act shall apply from 1 January 2022.

9. The TEG's report did not cover the other four environmental objectives (as these were not within the TEG's mandate), and these will instead be covered in advice from the Commission's newly established Platform on Sustainable Finance pursuant to Article 20 of the Taxonomy Regulation. The Commission is required to adopt delegated acts on technical screening criteria for these remaining four objectives by 31 December 2021, and it shall apply from 1 January 2023.

2.2 Article 8 of the Taxonomy Regulation

10. According to Article 8(1) of the Taxonomy Regulation, undertakings required to publish non-financial information pursuant to Articles 19a and 29a of Directive 2013/34/EU (the 'Accounting Directive') have to include information on how and to what extent their activities are associated with economic activities that qualify as environmentally sustainable under the Taxonomy Regulation. For this purpose, Article 8(2) of the Taxonomy Regulation requires non-financial undertakings subject to the Non-Financial Reporting Directive to provide disclosure of three key performance indicators ('KPIs'):

turnover, capital expenditure ('CapEx') and operating expenditure ('OpEx') related to environmentally sustainable activities. The Taxonomy Regulation does not specify any KPIs for financial undertakings subject to the disclosure requirements for non-financial information in the Accounting Directive.

11. Article 8(4) of the Taxonomy Regulation requires the Commission to adopt a delegated act to supplement Article 8(1) and (2) by specifying the content and presentation of the information to be disclosed pursuant to those paragraphs, 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 technical screening criteria established pursuant to the Taxonomy Regulation. The Commission is required to adopt the delegated act by 1 June 2021.

2.3 ESMA's mandate to deliver advice

12. On 15 September 2020, the three European Supervisory Authorities ('ESAs') received a call for advice from the Commission (see Annex I). The call requested advice on KPIs and methodology on the disclosure of how and to what extent the activities of undertakings under the Non-Financial Reporting Directive qualify as environmentally sustainable under the Taxonomy Regulation.

13. The call asked each ESA to provide advice within its particular remit:

    a. EBA was asked to provide advice on KPIs for banks and investment firms;

    b. EIOPA was asked to provide advice on KPIs for (re)insurance companies; and

    c. ESMA was asked to provide advice on how to further specify the three KPIs already established for non-financial undertakings in Article 8(2) of the Taxonomy Regulation and advice on KPIs for asset management companies in the scope of the Non-Financial Reporting Directive.

14. The call also established a number of principles on which the ESAs should base their advice. As such, the ESAs are free to choose the working arrangements which they consider most efficient in developing the advice and may also choose the most efficient way of cooperating with each other, delivering three separate reports while closely coordinating their pieces of advice. The ESAs are furthermore encouraged to cooperate with other EU bodies as relevant and to engage with stakeholders in a way which ensures the absence of conflicts of interest. The advice should be based on reliable qualitative and quantitative data and choices should be justified.

2.4 Development of the draft advice

15. In developing its draft advice, in line with the invitation in the Commission's call for advice ESMA has closely coordinated with EBA and EIOPA with the purpose of ensuring that the three pieces of advice delivered by the ESAs are aligned and coherent. When

analysing the responses to this Consultation Paper and preparing its final advice, ESMA will continue this coordination with EBA and EIOPA.

16. During the preparation of its draft advice, ESMA reached out to a number of stakeholders to receive initial views on the different options which ESMA was considering for the advice. Outreach was done to stakeholders from a wide variety of categories – non-financial undertakings, asset managers, issuer associations, investor / consumer organisations, stock exchanges, data / ratings providers, members of the accounting and audit profession, standard-setters, non-governmental organisations and trade unions. Most stakeholders were identified via their membership of ESMA's Securities and Markets Stakeholder Group and Consultative Working Groups, and where certain categories were not fully covered in this way, additional stakeholders were identified and contacted. Stakeholders provided helpful feedback which was taken into account in the version of the draft advice included in this Consultation Paper.

17. As suggested in the Commission's call for advice, ESMA was furthermore in contact with the Commission's Joint Research Centre which supplied useful technical details regarding the Taxonomy Regulation. ESMA also took into account the ongoing work of the EFRAG Project Task Force which is currently conducting preparatory work for possible future non-financial reporting standards and in which ESMA is appointed in an observer capacity.

18. Due to the targeted nature of the advice requested from ESMA and the condensed timeline for delivering the advice, ESMA is conducting a shortened consultation of four weeks. This is in line with the recommendation in the Commission's call for advice which mentions that it may be necessary for the ESAs to shorten internal deadlines and procedures, such as consultations.

2.5 Horizontal considerations for the attention of the Commission

19. A number of points were brought to ESMA's attention during the development of the draft advice. ESMA does not consider these points are suitable for inclusion in its actual advice but wishes to mention them in this Consultation Paper in order to bring them to the attention of the Commission:

    a. It was suggested by a stakeholder that all Level 2 disclosure requirements on non-financial information should be set out in one legislative instrument to simplify matters for market participants. This remark was notably made in the context of the non-financial reporting standards which the co-legislators may possibly decide to put in place in the future. ESMA understands this suggestion but considers it is out of scope of the advice ESMA is covering in this Consultation Paper.

    b. A number of stakeholders highlighted the need to ensure consistency between different pieces of legislation in the sustainable finance space, especially as regards disclosure requirements on various market players. ESMA has been mindful of this point when preparing its advice, for example in considering how the KPI disclosure of non-financial undertakings could be made most useful for financial market participants who will be making use of this disclosure for their own regulatory disclosure obligations.

c. Further in connection with the large amount of legislative work going on in relation to disclosure of non-financial information, a stakeholder suggested that a review clause should be inserted in the delegated act which the Commission will adopt based on the advice from ESMA, EBA and EIOPA. Such a review clause would serve to ensure that any changes in the rapidly evolving legislative landscape could be taken into account also in relation to the KPIs under Article 8.

d. Another strong theme in both stakeholder feedback and various publications was the need to provide the market with sufficient time to implement the new disclosure requirements, a point which was assigned further importance by some stakeholders due to the COVID-19 pandemic. ESMA observes that the timing with which new legislative requirements will apply falls beyond its remit.

e. A further aspect which was drawn to ESMA's attention is the fact that even undertakings who are not required to disclose KPIs under Article 8 of the Taxonomy Regulation may receive requests from investors to provide such KPIs. ESMA considers that this point falls outside of the scope of its advice, and it will as such not be addressed further.

3 Advice relating to non-financial undertakings

3.1 Scope of this part of the advice

20. The first part of the advice which the Commission has requested from ESMA relates to non-financial undertakings subject to the requirement to disclose non-financial information under the Non-Financial Reporting Directive.

21. Article 8(1) of the Taxonomy Regulation requires undertakings which are subject to the requirement to disclose non-financial information under the Non-Financial Reporting Directive to include, either in their (consolidated) non-financial statement or in a separate report, information on how and to what extent their activities are associated with environmentally sustainable economic activities under the Taxonomy Regulation.

22. Article 8(2) of the Taxonomy Regulation adds further detail to this requirement in relation to non-financial undertakings by requiring them to use three KPIs when providing the disclosure required by Article 8(1):

a. the proportion of their turnover derived from products or services associated with environmentally sustainable economic activities under the Taxonomy Regulation;

b. the proportion of their CapEx related to assets or processes associated with environmentally sustainable economic activities under the Taxonomy Regulation; and

c. the proportion of their OpEx related to assets or processes associated with environmentally sustainable economic activities under the Taxonomy Regulation.

23. Overall, the requirement to disclose non-financial information under the Non-Financial Reporting Directive applies to the following undertakings:

   a. Large undertakings, as defined in Article 3(4)[3] of Directive 2013/34/EU (the 'Accounting Directive'),

   which are

   b. public-interest entities, as defined in Article 2(1)[4] of the Accounting Directive,

   c. exceeding on their balance sheet dates the criterion of an average number of 500 employees during the financial year.

24. Summarising these points, the Non-Financial Reporting Directive requirements to disclose non-financial information can broadly be said to cover large listed issuers, large banks and large insurance undertakings. The non-financial undertakings which are the focus of the first part of ESMA's advice correspond to the first of these three groups, i.e. large listed issuers. As such, throughout this Consultation Paper, references to 'non-financial undertakings' should be understood as generally referring to large (non-financial) listed issuers.

25. In line with the general focus of the Commission's call for advice, and the underlying focus of the delegated act which the Commission must adopt, ESMA has split its advice on KPIs for non-financial undertakings into three subtopics, namely content, methodology and presentation, as reflected in the following Sections 3.2, 3.3 and 3.4.

[3] Undertakings which on their balance sheet dates exceed at least two of the three following criteria: (a) balance sheet total: EUR 20 000 000; (b) net turnover: EUR 40 000 000; (c) average number of employees during the financial year: 250.
[4] Undertakings which are (a) governed by the law of a Member State and whose securities are admitted to trading on a regulated market; (b) credit institutions; (c) insurance undertakings or (d) designated by Member States as public-interest entities.

3.2 Content of KPIs

3.2.1 How to define the three KPIs?

3.2.1.1 Proportion of turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

26. According to Article 8(2)(a) of the Taxonomy Regulation, non-financial undertakings subject to the disclosure requirements of the Non-Financial Reporting Directive have to disclose "…the proportion of their turnover derived from products or services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9" of the Taxonomy Regulation. In other words, non-financial undertakings have to disclose a KPI corresponding to the following fraction:

$$\frac{\text{Turnover from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9}}{\text{Turnover}}$$

27. To respond to the Commission's call for advice on further specifying the content of this KPI, ESMA considers that the following questions should be addressed:

    a. Is it necessary to define 'turnover' and, if yes, how should this be done? This question is relevant for both the numerator and the denominator.

    b. Is it necessary to define 'products / services associated with economic activities which qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation' and, if yes, how should this be done? This question is relevant for the numerator and will be addressed in two parts, the first on 'products / services', the second on 'associated with economic activities which qualify as environmentally sustainable…'.

Turnover

28. Regarding the question of whether it is necessary to define turnover, ESMA is of the view that the answer is yes. As ESMA observed in its 2019 advice to the Commission on undue short-term pressure on corporations [5] and further in its response to the Commission's consultation on the review of the Non-Financial Reporting Directive,[6] the absence of detailed reporting rules under the Non-Financial Reporting Directive

[5] ESMA30-22-762 Report – *Undue short-term pressure on corporations*, 18 December 2019.
[6] ESMA32-334-245 Response to public consultation - *ESMA response to the European Commission consultation on the review of the NFRD*, 11 June 2020.

significantly impedes undertakings' ability to provide comparable disclosure. This makes it difficult for investors to use non-financial information to make investment decisions and is unhelpful for users of non-financial information in general. As evidenced in the Commission's summary of responses to the consultation on the review of the Non-Financial Reporting Directive,[7] this point is also broadly acknowledged among market participants, across both users and preparers of non-financial information.

29. ESMA is therefore of the view that an important step in making disclosure of non-financial information more useful to investors and other users is to render it more comparable.

30. When considering comparability across different companies, ESMA notes that the undertakings that are subject to the requirement to prepare a non-financial statement under the Non-Financial Reporting Directive may apply different accounting standards, i.e. some will apply IFRS while others will apply local GAAP. This situation results in partially undermining the objective of achieving full comparability of amounts – such as turnover – that are typically derived from or based on items recognised and disclosed in an undertaking's financial statements on the basis of the applicable accounting standards.

31. One way of addressing this would be to establish a separate notion of turnover and related accounting methodology only for the purpose of providing disclosures under Article 8 of the Taxonomy Regulation. However, ESMA does not believe that establishing a separate notion of turnover from the one that can be derived from the revenue figure in an undertaking's financial statements would serve the needs of users and preparers of non-financial information. Firstly, it is important to take into account that undertakings manage their activities taking into account established notions of key items, such as revenue, based on financial statements. Secondly, ESMA notes that establishing a new notion of turnover that departs from the established and applied accounting notions of revenue would add complexity and confusion for the ultimate users of the information, as well as for the preparers when trying to integrate financial and non-financial information.

32. ESMA would therefore consider it acceptable to permit undertakings reporting under different accounting standards to report turnover amounts that may be prepared on the basis of different underlying accounting principles, provided that:

    a. Such principles do not contradict the notion of turnover that is established in the Accounting Directive, as explained further below; and

    b. Transparency is provided on the accounting policy applied by the undertaking to determine the turnover amounts.

33. The question is then which definition of turnover to use as a reference point. To respond to this question, the first step is to examine whether the legislation contains any indicators

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[7] Ares(2020)3997889 *Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive*, 29 July 2020.

of how the co-legislators intended to define this term. The Taxonomy Regulation does not itself define turnover, though Recital 22 of the Regulation mentions that the purpose of using this measure – as well as CapEx and OpEx – is to provide useful information to investors who are interested in companies whose products and services contribute substantially to any one of the environmental objectives set out in the Taxonomy Regulation.

34. Recital 22 furthermore refers to the Commission's Guidelines on reporting climate-related information as the origin of the idea to use turnover. However, the Commission's Guidelines also do not define turnover or contain further indications of how it should be defined, apart from mentioning that turnover should cover the reporting year and that the KPI overall should be measured as a percentage.[8]

35. Turning then to other possible sources of a definition, the Accounting Directive – which contains the requirements relating to non-financial statements[9] – provides the following definition of net turnover in Article 2(5):

"'net turnover' means the amounts derived from the sale of products and the provision of services after deducting sales rebates and value added tax and other taxes directly linked to turnover"

36. ESMA therefore proposes that this definition should be the reference point for the way non-financial undertakings define turnover for the purpose of calculating the turnover KPI under Article 8(2) of the Taxonomy Regulation. The items in an undertaking's financial statements that are broadly consistent with this definition, most notably the revenue figure, should then be used to determine the amount of turnover to be included for the calculation of this KPI, as further explained in the following paragraphs.

37. For non-financial undertakings preparing their financial statements in accordance with the International Financial Reporting Standards ('IFRS'), it is relevant to be aware that, while IFRS as adopted in the EU do not contain a definition of turnover, they do define the related term revenue. This definition is set out in IFRS 15 *Revenue from contracts with customers* (adopted in the EU in the consolidated Regulation (EC) No 1126/2008 (the 'IFRS Regulation')):

"Income arising in the course of an entity's ordinary activities"[10]

38. ESMA notes that for some undertakings, the revenue arising in the course of ordinary business activities may be accounted for under different standards than IFRS 15 or via

[8] Communication from the Commission – Guidelines on non-financial reporting: Supplement on reporting climate-related information, OJ C 209, 20.6.2019, p. 1–30, page 18.
[9] The Non-Financial Reporting Directive provided amendments to the Accounting Directive, notably by adding Articles 19a and 29a to the Accounting Directive. The consolidated Accounting Directive as such encompasses the Non-Financial Reporting Directive. When reference is made to the Non-Financial Reporting Directive in this Consultation Paper, this is a reference to Articles 19a and 29a which present the requirements on non-financial statements.
[10] IFRS 15, Appendix A Defined terms.

a combination of different standards. For example, lessors will account for income arising from lease contracts in accordance with IFRS 16 *Leases*.

39. ESMA therefore suggests that non-financial undertakings applying IFRS should use the amounts of revenue and income that are accounted for under IFRS 15 and IFRS 16 as their turnover. The turnover should include all items of income arising from an entity's ordinary activities that constitute revenue and that is accounted for on the basis of other accounting standards than those mentioned above. The accompanying disclosures recommended by ESMA in Section 3.2.2.3 aim at enabling users of non-financial statements to understand the different sources of revenue and the related accounting bases used. By applying this approach, non-financial undertakings applying IFRS will include turnover covering all amounts derived from the sale of products and the provision of services in the course of their ordinary activities.

40. For non-financial undertakings in the scope of the Non-Financial Reporting Directive who do not apply IFRS but rather their national Generally Accepted Accounting Principles ('GAAP'),[11] ESMA proposes using the revenue figure which they account for under their national GAAP requirement.

41. To provide investors and other users of non-financial information with full transparency on the definition of turnover which a non-financial undertaking applies, ESMA suggests that some explanatory disclosures should be required. This is covered in more detail in Section 3.2.2 below.

Products / services

42. ESMA considers that the same considerations apply to whether products / services should be defined as they apply to whether turnover should be defined; in order to ensure comparability of information, it is necessary to create clarity around what each element of the KPIs means, so that non-financial undertakings can use comparable data as input for calculating the KPI.

43. However, ESMA is of the view that its advice on how to define turnover already sufficiently covers which products and services to include in the KPI and as such suggests there is no need to address this question further in its advice.

44. The only point which in ESMA's view needs to be addressed is how to avoid double counting of products / services across a non-financial undertaking's different economic activities.

45. For example, an undertaking may sell a service which is partly connected with a Taxonomy-aligned activity and partly not. For disclosure purposes, the undertaking will have to determine which part of its turnover from this service is related to the Taxonomy-

[11] Application of IFRS is only obligatory in the EU for the preparation of listed issuers' consolidated financial statements. As not all non-financial undertakings reporting under the Non-Financial Reporting Directive will belong to a group, they may not prepare consolidated financial statements and will therefore be free to prepare their financial statements in accordance with national GAAP.

aligned activity and which part of its turnover is related to the non-Taxonomy-aligned activity.

46. ESMA does not believe it is possible to establish one rule for how to do this which could apply to undertakings across all sectors and to all types of activities. Instead, ESMA suggests that non-financial undertakings must apply their best judgement of how to split turnover from this service across the two activities and avoid doing so in a way which unduly inflates the turnover related to the Taxonomy-aligned activity. To ensure transparency, the non-financial undertaking should be required to provide disclosure on how this allocation across its activities was done.

Associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

47. Similar to turnover and products / services, ESMA believes it is necessary to establish clarity around this element of the KPI to ensure comparability of the information which different non-financial undertakings will provide.

48. As already explained in Section 2.1, according to Article 3 of the Taxonomy Regulation, an economic activity qualifies as environmentally sustainable where it:

   a. Contributes substantially to one or more of the following environmental objectives set out in Article 9 in accordance with Articles 10 to 16:

      1. Climate change mitigation;
      2. Climate change adaptation;
      3. The sustainable use and protection of water and marine resources;
      4. The transition to a circular economy;
      5. Pollution prevention and control;
      6. The protection and restoration of biodiversity and ecosystems;

   b. Does not significantly harm ('DNSH') any of the abovementioned environmental objectives, in accordance with Article 17 of the Taxonomy Regulation;

   c. Is carried out in compliance with the minimum safeguards laid down in Article 18; and

   d. Complies with the technical screening criteria to be established by the Commission in delegated acts.

49. In other words, the fact that the KPIs established in Article 8(2) refer to activities which qualify as environmentally sustainable <u>under Articles 3 and 9</u> of the Taxonomy Regulation means that the activities which can be counted in this KPI do not only have

to substantially contribute to one or more of the environmental objectives (criterion a above) but have to be Taxonomy-aligned overall by respecting all four of the abovementioned criteria (a-d above). The question is then whether there is a need to further specify when these four criteria can be considered met for the purpose of ensuring a uniform calculation of the KPI *turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation* across non-financial undertakings.

50. ESMA is of the view that it is not necessary to further specify either of the four criteria in the delegated act which the Commission will adopt to address the KPIs under Article 8 of the Taxonomy Regulation. ESMA provides its detailed reasons for this view in the following paragraphs.

51. As regards criterion a (substantially contributes to one or more of the environmental objectives), Articles 10 to 15 of the Taxonomy Regulation already establish when an economic activity is considered to substantially contribute to each of the six environmental objectives, and Article 16 specifies when an economic activity is considered to substantially contribute to one or more of the six objectives by directly enabling other activities to make a substantial contribution to one or more of those objectives. Furthermore, additional detail will be added to these articles in the delegated acts which the Commission has to adopt on technical screening criteria in accordance with Articles 10 to 15. Therefore, ESMA does not consider further specification is needed of criterion a in the delegated act which the Commission will adopt to address the KPIs under Article 8 of the Taxonomy Regulation.

52. As regards criterion b (DNSH), Article 17 of the Taxonomy Regulation establishes the overall rules for when an economic activity is considered to significantly harm each of the six environmental objectives. According to Article 19(1)(b), these rules will be further detailed in the delegated acts which the Commission has to adopt on technical screening criteria in accordance with Articles 10 to 15. Again, ESMA therefore does not consider that further specification is needed of criterion b in the delegated act which the Commission will adopt to address the KPIs under Article 8 of the Taxonomy Regulation.

53. As regards criterion c (is carried out in compliance with minimum safeguards), Article 18 of the Taxonomy Regulation clarifies that these minimum safeguards consist of procedures implemented by an undertaking to ensure alignment with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights, including the principles and rights set out in the eight fundamental conventions identified in the Declaration of the International Labour Organisation on Fundamental Principles and Rights at Work and the International Bill of Human Rights. It is furthermore indicated that when implementing these procedures, undertakings should adhere to the principle of do no significant harm mentioned in Article 2(17) of Regulation (EU) 2019/2088 (the 'SFDR').

54. However, there is no requirement for the Commission to adopt delegated acts in relation to this criterion and it is therefore not expected to be covered in the technical screening criteria. As such, criterion c remains more general than criteria a and b. For this reason,

ESMA has considered whether it should further specify when this criterion can be considered met for the purpose of ensuring a uniform calculation of the KPI across non-financial undertakings. However, ESMA observes that, while the co-legislators decided to require the Commission to add detail to criteria a and b in delegated acts, no such requirement was included for criterion c. It therefore seems that a decision was made by the co-legislators that the rules for determining compliance with minimum safeguards included in Article 18 of the Taxonomy Regulation are sufficiently specific.

55. ESMA will therefore not attempt to further specify when criterion c can be considered met. Instead, ESMA is of the view that non-financial undertakings should disclose how they determined that criterion c was met to provide context to the KPI (see more detailed considerations on this in Section 3.2.2 below).

56. Finally, as regards criterion d (complies with the technical screening criteria to be established by the Commission in delegated acts), the technical screening criteria will be very specific and laid down in delegated acts in accordance with relevant articles of the Taxonomy Regulation. ESMA therefore sees no need to further elaborate on this criterion for the purpose of the turnover KPI.

57. As such, ESMA does not consider that any of the four criteria for being considered Taxonomy-aligned in Article 3 of the Taxonomy Regulation need to be further specified for the purpose of the KPI *turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation*.

58. However, ESMA considers that it is necessary to specify exactly when turnover can be counted for each of the six environmental objectives. As highlighted in the TEG's final report , *"[t]he calculation methodology for Taxonomy-aligned turnover, capex and opex, if relevant, varies depending on the financial vehicle (equity or debt) and the purpose of the investment regarding the environmental objective being pursued"*.[12]

59. The Commission acknowledges this point in its call for advice in which it explicitly invites the ESAs to "take into account that clarity is needed on how undertakings ought to determine whether their investments are associated with economic activities considered environmentally sustainable under the EU Taxonomy". The Commission observes that the issue of "what counts" is important throughout the investment chain and as such matters to the non-financial undertakings providing disclosure under Article 8 of the Taxonomy Regulation, to the financial market participants providing disclosure under Articles 5 and 7 of the Taxonomy Regulation and to investors.

60. The TEG has already proposed that inclusion of turnover should differ between the two first environmental objectives – climate change mitigation and climate change adaptation – and ESMA does not see a need to amend or add to their recommendation (set out in the two first lines of the table below). However, as the mandate of the TEG related only

[12] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 30.

to climate change mitigation and climate change adaptation, it remains to be specified how non-financial undertakings should determine whether their turnover can be counted for the four remaining environmental objectives (water and marine resources, circular economy, pollution and biodiversity and ecosystems).

61. While the TEG has not addressed these four objectives in its final report, ESMA considers that the logic proposed by the TEG in differentiating between inclusion of turnover from climate change mitigation and climate change adaptation can be expanded to cover the remaining four environmental objectives:

    a. The logic developed by the TEG is that all turnover from an economic activity related to climate change mitigation can be counted, as long as the activity meets the criteria of substantially contributing to climate change mitigation, including by meeting the technical screening criteria, and the DNSH criterion as regards the other five environmental objectives.

    b. On the other hand, not all turnover from an economic activity related to climate change adaptation can be counted. This is because the nature of this environmental objective is different – rather than covering an undertaking's impact on the climate (like climate change mitigation does), it covers the climate's impact on the undertaking. Therefore, only turnover from economic activities which enable adaptation can be counted. For example, a non-financial undertaking which provides installation of early warning systems for flood risk could count the turnover from this activity (provided that the activity respects the other Taxonomy criteria as well).[13] On the other hand, turnover from an already adapted activity cannot be counted.

62. Based on this distinction, ESMA considers that the approach for counting turnover which the TEG has proposed for climate change mitigation should apply to the remaining four environmental objectives, as they all relate to an undertaking's impact on the environment.

[13] Natixis CIB Green & Sustainable Hub, *EU Taxonomy for sustainable activities – Skydiving kit*, September 2020, page 22.

63. ESMA's suggestions for which kinds of turnover should be included in the KPI for each of the six environmental objectives are summarised in the table below. The only amendment to the wording of the TEG which ESMA proposes is the addition of a reference to minimum safeguards.

Table 1: Calculation methodology per environmental objective, turnover

	When to count turnover
Climate change mitigation	Can be counted where economic activity meets Taxonomy technical screening criteria for substantial contribution to climate change mitigation, relevant DNSH criteria and minimum safeguards.[14]
Climate change adaptation	Turnover can be recognised only for activities enabling adaptation and provided that the activity meets the other Taxonomy criteria as well. Turnover cannot be recognised for adapted activities at this stage.[15]
Water and marine resources	Can be counted where economic activity meets Taxonomy technical screening criteria for substantial contribution, relevant DNSH criteria and minimum safeguards.
Circular economy	
Pollution	
Biodiversity and ecosystems	

3.2.1.2 Proportion of CapEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

64. According to Article 8(2)(b) of the Taxonomy Regulation, non-financial undertakings subject to the disclosure requirements of the Non-Financial Reporting Directive have to disclose *"…the proportion of their capital expenditure […] related to assets or processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9"* of the Taxonomy Regulation. In other words, non-financial undertakings have to disclose a KPI corresponding to the following fraction:

$$\frac{\text{CapEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9}}{\text{CapEx}}$$

65. To provide advice on how to further specify the content of this KPI, ESMA believes the following questions should be addressed:

[14] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 30. Please not that ESMA has added the reference to minimum safeguards which is not included in the TEG report.
[15] Ibid, page 30.

a. Is it necessary to define 'CapEx' and, if yes, how should this be done? This question is relevant for both the numerator and the denominator, as CapEx is part of both.

b. Is it necessary to define 'assets / processes associated with economic activities which qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation' and, if yes, how should this be done? This question is relevant for the numerator and will be addressed in two parts, the first on 'assets / processes, the second on 'associated with economic activities which qualify as environmentally sustainable…'.

CapEx

66. Regarding whether it is necessary to define CapEx for the purpose of this KPI, ESMA considers that the same considerations apply as were set out above regarding the need to define turnover: in order to ensure that comparable disclosure is provided by undertakings reporting under the Non-Financial Reporting Directive, it is necessary to establish detailed disclosure requirements.

67. On this basis, ESMA has considered how to define CapEx for the purpose of the KPI. There are several factors to take into account for this purpose:

a. The Taxonomy Regulation does not itself set out a definition of CapEx, and neither does the Accounting Directive. There is equally no definition of CapEx in IFRS.

b. CapEx is generally referred to as expenditure for the acquisition and maintenance of fixed assets, such as property, plant and equipment. While generally CapEx is associated to tangible assets, investment in certain intangibles, such as licences or patents, may also be relevant. Article 1(4) of the Accounting Directive defines fixed assets as: "*assets which are intended for use on a continuing basis for the undertaking's activities"*.

c. One way of determining CapEx is by considering the line items in an undertaking's cash flow statement that are associated to such investments (direct method). Another alternative (indirect method) is to determine CapEx by reference to the difference in the stock of fixed assets recognised in an undertaking's statement of financial position between two reporting periods and adding the related amount of current year depreciation and amortisation charges.

d. Valuation theory also suggests that when estimating CapEx, additional factors should be taken into account that may require adjustments to figures in the financial statements. For example, when for accounting purposes certain expenses are not capitalised but directly expensed in the profit and loss statement – such as certain expenses for research and development activities – these expenses should also be considered as part of the capital purchased by the concerned undertaking. Similarly, when acquisition of fixed assets takes place by means of lease arrangements as opposed to direct purchase, then also the fixed leased assets (e.g. right-of-use assets and related depreciation in accordance with IFRS 16 *Leases*) should, in principle, be considered as part of CapEx. Lastly, capital disposals, acquisitions through business combinations, revaluations and impairments should also be taken into account as they have an impact in explaining the year-on-year variation of CapEx.

e. ESMA notes that the measurement of fixed assets with regards to the revaluations, impairments and capital disposals is largely affected by the accounting model adopted and that, considering the potential differences between IFRS and national GAAP, information regarding these items can be provided in the accompanying disclosures as further explained in paragraph 0.

f. As mentioned in the previous section in relation to turnover, considering how the accounting requirements applied by non-financial undertakings reporting under the Non-Financial Reporting Directive may provide a useful basis to determine CapEx, it is important to note that only a subset of such undertakings will apply IFRS for the preparation of financial statements, while others will apply national GAAP. This situation suggests the need to refer to a general concept of CapEx which can be applied consistently across non-financial undertakings, while still building on the applicable accounting requirements.

g. ESMA also notes that the CapEx KPI would be most useful if it were to provide a common basis for analysis by the users of non-financial statements, while taking into account the inevitable differences in the respective underlying accounting regimes (i.e. IFRS vs. local GAAP). ESMA proposes to do this by combining the disclosure of a relatively basic KPI with accompanying information relating to reconciliations explaining the drivers of change in CapEx during the reporting period and the amounts relating to right-of-use assets associated to leased fixed assets. This accompanying information would be required for the Taxonomy-aligned sustainable activities, when based on the applicable accounting standards, the undertaking is already providing this information in relation to fixed assets.

h. When considering potential sources of data from accounting regimes that are relevant to determine CapEx, International Accounting Standard ('IAS') 7 Statement of Cash Flows provides a potential starting point with the requirement to disclose cash flows from investing activities as defined by paragraph 6 of IAS 7. However, ESMA notes that a statement of cash flows will not be available for all undertakings applying national GAAP instead of IFRS. In contrast, all undertakings will be reporting information relating to fixed assets in their statement of financial position and, at least, the amount of related depreciation and amortisation charges in their profit and loss statement.

i. Therefore, ESMA proposes to determine CapEx with reference to the indirect method, thus calculating CapEx as the difference between the carrying amount of fixed assets recognised in the statement of financial position between the beginning and the end of the reporting year plus current year's related depreciation and amortisation charges.

j. For IFRS financial statements, IAS 16 Property, Plant and Equipment establishes principles for recognising property, plant and equipment as tangible assets and IAS 38 Intangible Assets addresses how to recognise and measure intangible assets and how to provide disclosure in this regard, in particular the reconciliations between amounts relating to the beginning and end of the reporting period as required by paragraphs 73(e) of IAS 16 and 118(e) of IAS 38. ESMA notes that fixed assets are also acquired for the purpose of undertaking investments, for example properties acquired to earn rentals or for capital appreciation or both, in this case IAS 40 Investment Properties provides the basis to account for such assets.

k. ESMA also highlights that some fixed assets may be acquired by means of lease arrangements and thus be accounted for under IFRS 16 Leases. ESMA notes that, in relation to leased assets, paragraph 47 of IFRS 16 requires that right-of-use assets relating to fixed assets shall be presented separately from other assets. When an entity does not provide this separate presentation, an entity shall include right-of-use assets within the same line item as that within which the corresponding underlying assets would be presented if they were owned (e.g. as property plant and equipment) and that disclosures should be provided of which line items in the statement of financial position include those right-of-use assets. Paragraph 48 of IFRS 16 further requires that right-of-use assets that meet the definition of investment property, shall be presented in the statement of financial position as investment property. In ESMA's view the accounting for leased assets may differ largely between undertakings reporting under IFRS compared to those reporting under national GAAP. Therefore, the inclusion of right-of-use assets under IFRS 16 in the CapEx KPI shall be carefully assessed. ESMA welcomes the input of stakeholders on this aspect.

68. With these above points in mind, for non-financial undertakings preparing their financial statements in accordance with IFRS, ESMA proposes that the CapEx considered for the determination of the CapEx KPI should be based on those recognised in the statement of financial position in accordance with IAS 16, IAS 40, and IAS 38 (if applicable), excluding leased assets in accordance with IFRS 16 and for which specific disclosures are recommended as further explained below. This approach would permit non-financial undertakings to apply the same accounting policy to CapEx in the financial statements and in the CapEx KPI.

69. For non-financial undertakings preparing their financial statements in accordance with national GAAP, ESMA suggests that CapEx should be defined as the change that occurred during the reporting year in the amount of fixed tangible and intangible capital,

plus any depreciation, amortisation and impairment charges for the year, as accounted for under the applicable GAAP in these undertakings' financial statements.

70. Considering the risk of divergence between non-financial undertakings reporting under IFRS and those reporting in accordance with national GAAP, ESMA suggests that the impact of amounts relating to leased fixed assets on the CapEx KPI be disclosed separately, as further explained in paragraph 0. In ESMA's view, this approach will enable users of non-financial statements to complement the disclosed quantitative KPI with quantitative information on right-of-use assets when this information is available in accordance with the applicable standards, while preserving some degree of comparability with entities reporting under national GAAP.

Assets / processes

71. As for all other elements of the KPIs, ESMA is of the view that it is important to establish a uniform understanding of assets / processes to ensure comparability of information.

72. However, ESMA considers that its considerations in the above section on how to define CapEx already sufficiently cover which assets / processes to include in the KPI. The only point which in ESMA's view needs to be addressed is how to avoid double counting of assets / processes across a non-financial undertaking's different economic activities.

73. For example, an undertaking may have a plant in which it undertakes two activities, one which is Taxonomy-aligned and one which is not. When the undertaking makes an investment in the plant (CapEx), for disclosure purposes it has to determine which part of the CapEx relates to the Taxonomy-aligned activity and which part relates to the non-Taxonomy-aligned activity.

74. ESMA does not believe it is possible to establish one rule for how to do this which could apply across all sectors and all types of activities. Instead, ESMA suggests that non-financial undertakings must apply their best judgement of how to split CapEx across the two activities and avoid doing so in a way which unduly inflates the CapEx related to the Taxonomy-aligned activity. To ensure transparency, the non-financial undertaking should be required to provide disclosure on how this allocation across its activities was done.

Associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

75. As regards the need to further specify the four criteria for being Taxonomy-aligned set out in Article 3 of the Taxonomy Regulation, ESMA makes reference to the considerations in Section 3.2.1.1 on the turnover KPI which equally apply to the CapEx KPI.

76. In addition, it is again necessary to consider exactly when CapEx can be counted for each of the six environmental objectives, as requested by the Commission in its call for advice. According to the TEG, eligible Taxonomy-aligned CapEx should not vary depending on whether the associated economic activity contributes to climate change

mitigation or climate change adaptation. This is different from the approach suggested in relation to turnover, where the TEG considers that all turnover from economic activities related to climate change *mitigation* can be counted because it is possible for an activity to reach a level of environmental performance that is aligned with net-zero emissions by 2050. On the other hand, only turnover from economic activities which enable climate change *adaptation* can be counted while turnover from already adapted activities cannot because the TEG does not at this stage consider that an activity can ever be considered fully resilient to climate change. The TEG does not consider a similar difference exists between mitigation and adaptation in relation to CapEx.

77. As such, the TEG suggests that for both environmental objectives, a non-financial undertaking should be able to count CapEx when it is part of a plan to meet the technical screening criteria for a substantial contribution to climate change mitigation / adaptation and relevant DNSH criteria. ESMA will not propose any changes to this approach.

78. Since the TEG has not proposed that the difference between climate change mitigation and adaptation should trigger a difference in when CapEx in activities associated with the objectives can be counted, ESMA has not identified any reason to propose a difference in counting with any of the four remaining environmental objectives. For the CapEx KPI, ESMA therefore proposes that the same approach to counting CapEx should apply across all six environmental objectives, as summarised in the table below. The only change which ESMA has made compared to the wording in the TEG's final report is to include a reference to minimum safeguards.

Table 2: Calculation methodology per environmental objective, CapEx

	When to count CapEx
Climate change mitigation	Can be counted where amounts incurred are part of a plan to meet Taxonomy technical screening criteria for substantial contribution, relevant DNSH criteria and minimum safeguards.[16]
Climate change adaptation	
Water and marine resources	
Circular economy	
Pollution	
Biodiversity and ecosystems	

79. With reference to the wording in the table, ESMA considers that it is necessary to specify what it means that costs incurred are *"part of a plan"* as this is a central element in deciding whether CapEx can be counted. ESMA proposes that the following requirements should apply:

[16] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 30 (applicable to climate change mitigation and climate change adaptation). Please note that ESMA has added the reference to minimum safeguards which is not included in the TEG report.

a. CapEx can be counted if the plan to which it relates aims to make the economic activity in question Taxonomy-aligned within a maximum period of five years, as recommended by the TEG;[17]

b. To ensure that the plan is a formalised and integrated part of the non-financial undertaking's strategy, the plan should have been adopted by the undertaking's administrative body and be available to the public, for example on the undertaking's website. The publication of the plan or key elements and milestones thereof is important to enable users of non-financial statements to assess progress towards taxonomy alignment;

c. For climate change adaption, the plan should furthermore directly respond to the climate risks identified in the assessment required by the adaptation principles, as recommended by the TEG.[18]

80. Notwithstanding these clarifications of what it means to be "part of a plan", it is important to be mindful that the TEG has "identified and included in the Taxonomy some exceptional cases where individual improvement measures can be considered to make a substantial contribution without needing to be part of a plan to meet the economic activity thresholds" (such as low-carbon technologies and building renovation measures).[19] The TEG highlights that these measures are included because their deployment and use is critical to reducing emissions in the EU's current building stock. The Commission should therefore take these measures into consideration when it addresses the situations in which CapEx can be counted for the purpose of the CapEx KPI.

3.2.1.3 Proportion of OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

81. According to Article 8(2)(b) of the Taxonomy Regulation, non-financial undertakings subject to the disclosure requirements of the Non-Financial Reporting Directive have to disclose *"…the proportion of […] their operating expenditure related to assets or processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9"* of the Taxonomy Regulation. This means that non-financial undertakings have to disclose a KPI corresponding to the following fraction:

[17] Ibid, page 15.
[18] Ibid, pages 15 and 40.
[19] Ibid, page 16.

OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9

OpEx

82. In order to respond to the Commission's call for advice on further specifying the content of this KPI, ESMA believes that the following questions should be addressed:

    a. Is it necessary to define 'OpEx' and, if yes, how should this be done? This question is relevant for both the numerator and the denominator.

    b. Is it necessary to define 'assets / processes associated with economic activities which qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation' and, if yes, how should this be done? This question is relevant for the numerator and will be addressed in two parts, the first on 'products / services', the second on 'associated with economic activities which qualify as environmentally sustainable…'.

OpEx

83. As for the other elements of the three KPIs, ESMA is of the view that it is important to establish a uniform understanding of OpEx to ensure that comparable disclosure is provided by undertakings reporting on the KPI proportion of OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation. ESMA presents a number of considerations in this regard in the following bullet points:

    a. As is the case for CapEx, neither the Taxonomy Regulation nor the Accounting Directive contains a definition of OpEx. The Accounting Directive does require that undertakings presenting expenses by nature within the profit and loss statement include 'other operating expenses', but this term is also not defined in the Directive.[20]

    b. Furthermore, OpEx is not defined in IFRS. It is therefore considered an APM for non-financial undertakings preparing their financial statements in accordance with IFRS.

    c. As part of its Primary Financial Statements ('PFS') project and wider work on Better Communication in Financial Reporting, the International Accounting Standards Board ('IASB') is currently considering requiring companies applying IFRS to provide three new profit subtotals in their profit and loss statement.[21] Notably, the IASB is considering to replace IAS 1 *Presentation of Financial Statements* with a new standard and in that connection to require that the new subtotal 'operating profit or loss' be mandatorily disclosed in the profit and loss statement. It is proposed that operating profit or loss should

[20] Accounting Directive, Article 13(1) and Annex V.
[21] International Accounting Standards Board, Exposure Draft ED/2019/7 *General Presentation and Disclosures*, December 2019.

exclude income / expenses classified in the other categories of the profit and loss statement, such as investing or financing, and should as such include all income / expenses from an entity's main business activities.[22]

d. While it is important at this time to be aware that a new standard may be introduced by the IASB, requiring undertakings to disclose operating profit or loss, it is not possible to know with certainty whether the proposals on which the IASB consulted will be amended in the final standard or when this final standard will become applicable. Therefore, ESMA considers that it is at this time preferable to not link its advice on OpEx too closely to the IASB's ongoing project but rather to suggest a more general definition of OpEx, whilst still, however, applying a logic consistent with the IASB's proposals and building largely on the concepts underlying such proposals.

e. ESMA notes that paragraph 6 of IAS 7 *Statement of Cash Flows,* also defines 'operating activities' in a residual manner vis-à-vis 'investing activities' and 'financing activities'. Operating activities are in fact defined as: "*the principal revenue-producing activities of the entity and other activities that are not investing or financing activities*". Investing activities are defined as "*the acquisition and disposal of long-term assets and other investments not included in cash equivalents*"*.* Financing activities are defined as: "*activities that result in changes in the size and composition of the contributed equity and borrowings of the entity*. ESMA notes that, these definitions, together with those of financing and investing activities proposed in the IASB's PFS project, may be useful to help defining a generally understood concept of operating expenses.

f. ESMA acknowledges that, at present, there is no single commonly shared definition of operating result and that the notion of OpEx could therefore be difficult to identify in a way that results in relevant and comparable information. However, ESMA considers that the above-mentioned references in IFRS and the Accounting Directive provide a useful starting point.

g. The Accounting Directive, in particular, provides some examples that are helpful in this regard. Annex V of that Directive, in fact, refers to a number of items of costs and expenses before referring to 'other operating expenses', therefore implicitly indicating that all such items are to be considered as operating expenses. For a profit and loss statement that is presented by nature of expense, these include: staff costs, raw materials and consumables, value adjustments in respect of formation expenses and of tangible and intangible fixed assets (amortisation and depreciation) and value adjustments in respect of current assets, to the extent that they exceed the amount of value adjustments which are normal in the undertaking concerned. For a profit and loss statement presented by function, the relevant items are cost of sales

[22] Ibid, page 7.

(including value adjustments), distribution costs (including value adjustments) and administrative expenses (including value adjustments). On the other hand, the expenses that are typically related to investment and financing activities should be excluded from the notion of OpEx.

84. On this basis, ESMA proposes that non-financial undertakings should include in the amount of OpEx all items of expense that:

    a. arise from the undertaking's main business activities, which are generally identified as the principal revenue-producing activities of the entity; and

    b. do not relate either to the investment or financing categories and that therefore are normally included in the amounts reported within metrics such as 'operating result'.

85. In identifying expenses relating to financing and investing activities, building on the relevant concepts in IAS 7 and in the IASB's project on PFS, ESMA suggests that non-financial undertakings take into account the following aspects:

    a. financing activities generally result in changes in the size and composition of the contributed equity and borrowings of the entity. Expenses arising from these activities typically relate to the receipt or use of a financial resource (e.g. borrowings) from a financial institution or other provider of finance with the expectation that the resource will be returned to the provider. The financing expense constitutes the compensation due to the provider of finance. Such compensation is generally dependent on both the amount of the credit and its duration.

    b. Investing activities typically relate to the acquisition, holding and disposal of financial and non-financial assets that do not relate to operating assets, such as property, plant and equipment. Expenses from such activities generally relate to assets that generate a return individually and largely independently of other resources held by the entity.

Assets / processes

86. As for the other elements of the three KPIs, ESMA considers that it is important to establish a uniform understanding of assets / processes in relation to the OpEx KPI.

87. However, ESMA considers that its above considerations on how to define OpEx sufficiently cover which assets / processes to include in the KPI. Therefore, as for the CapEx KPI, the only point which in ESMA's view needs to be addressed is how to avoid double counting of assets / processes across a non-financial undertaking's different economic activities. For this, ESMA proposes using the same approach as for the CapEx KPI, namely requiring non-financial undertakings to apply their best judgement of how to split OpEx across their activities and avoid doing so in a way which unduly inflates the OpEx related to Taxonomy-aligned activities. To ensure transparency, non-financial

undertakings should furthermore be required to provide disclosure on how this allocation across its activities was done.

Associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation

88. As regards the need to further specify the four criteria for being Taxonomy-aligned set out in Article 3 of the Taxonomy Regulation, ESMA makes reference to the considerations in Section 3.2.1.1 on the turnover KPI which equally apply to the OpEx KPI.

89. In addition, it is again necessary to consider exactly when OpEx can be counted for each of the six environmental objectives, as requested by the Commission in its call for advice. According to the TEG, eligible Taxonomy-aligned OpEx should not vary depending on whether the associated economic activity contributes to climate change mitigation or climate change adaptation. As such, the TEG suggests that for both environmental objectives, a non-financial undertaking should be able to count OpEx when it is part of a plan to meet the technical screening criteria for a substantial contribution to climate change mitigation / adaption and relevant DNSH criteria. ESMA will not propose any changes to this approach, apart from adding a reference also to minimum safeguards.

90. Furthermore, ESMA is of the view that the same considerations apply to when OpEx can be counted for the other four environmental objectives as set out in Section 3.2.1.2, and ESMA as such considers that the same approach to counting OpEx should apply across all six environmental objectives for the OpEx KPI. ESMA's suggested approach is summarised in the table below. ESMA's proposed definition of *"part of a plan"* set out in Section 3.2.1.2 on the CapEx KPI should equally apply to the OpEx KPI.

Table 3: Calculation methodology per environmental objective, OpEx

	When to count OpEx
Climate change mitigation	Can be counted where amounts incurred (if relevant) are part of a plan to meet Taxonomy technical screening criteria for substantial contribution, relevant DNSH criteria and minimum safeguards.[23]
Climate change adaptation	
Water and marine resources	
Circular economy	
Pollution	
Biodiversity and ecosystems	

91. The last element which in ESMA's view needs specification is the TEG's reference to *"if relevant"* in relation to OpEx. ESMA understands that this reference makes the situations in which OpEx can be counted narrower than the situations in which CapEx can be counted. While the TEG does not propose hard-and-fast rules in this regard, it

[23] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 30 (applicable to climate change mitigation and climate change adaptation). Please note that ESMA has added the reference to minimum safeguards which is not included in the TEG report.

recommends that OpEx should be counted when it covers, for example, maintenance costs related to green assets that either increase the lifetime or the value of the assets as well as research and development costs, whereas OpEx such as purchasing costs or leasing costs would not normally be eligible.[24]

92. ESMA suggests it would be helpful to have clearer requirements for when OpEx can be considered relevant, apart from the already applicable rule that it should be part of a plan. To allow it to develop such requirements, ESMA has included a question for stakeholders in this regard in Section 3.2.5.

3.2.2 Should non-financial undertakings make any further disclosures to accompany the three KPIs?

3.2.2.1 Are accompanying disclosures needed?

93. In its call for advice, the Commission asks ESMA to consider whether non-financial undertakings should be required to make any further disclosures to accompany the three KPIs required from them by Article 8(2) of the Taxonomy Regulation. In other words, it appears that the Commission is considering whether it should require, in its delegated act, that non-financial undertakings must disclose additional information to supplement the three KPIs.

94. ESMA considers that such supplementary information alongside the three KPIs could serve the following functions, all with the purpose of enabling users of non-financial information to better understand the KPIs:

   a. Provide information on how the KPIs were prepared (i.e. which methodology was applied in their preparation, cf. Section 3.3 below). This will enable users to make their own assessment of whether they agree with the non-financial undertaking's assessment of which of its activities can be considered Taxonomy-aligned.

   b. Describe how the KPIs should be interpreted (i.e. provide a narrative explanation of the numerical information presented by the KPI).

   c. Provide context around the KPIs (e.g. by providing comparatives for how the non-financial undertaking performed on the same KPI in previous years or information on the target the undertaking had set for itself for each KPI for the year in question).

95. With this in mind, ESMA considers that it is likely to be helpful if non-financial undertakings provide supplementary information alongside the three KPIs required by Article 8(2) of the Taxonomy Regulation. This is supported by the Commission's Guidelines on non-financial reporting which state that *"[a]ppropriate narratives explaining*

[24] Ibid, page 29.

KPIs help make the non-financial statement more understandable".[25] It was also generally supported by stakeholders during the outreach which ESMA undertook during the preparation of its draft advice.

3.2.2.2 Should the content of the accompanying information be specified in legislation?

96. The question is then whether the content of this supplementary information should be specified in legislation or should be left up to the assessment of non-financial undertakings themselves. In this regard, it is relevant to remember that Article 19a(1) / 29a(1) of the Non-Financial Reporting Directive contains a broad requirement for undertakings to disclose information *"to the extent necessary for an understanding of the [undertaking's / group's] development, performance, position and impact of its activity, relating to […] environmental […] matters […]"*.

97. The TEG observes this point as well in its final report, suggesting that this requirement "should be used to provide readers with any contextual information needed to understand a company's Taxonomy-related turnover and expenditures".[26]

98. Additionally, Article 8(1) of the Taxonomy Regulation requires undertakings to provide *"information on how and to what extent"* their activities are associated with Taxonomy-aligned activities. This is another general requirement which contributes to ensure that sufficient disclosure is provided regarding the three KPIs.

99. While non-financial undertakings can as such be expected to provide supplementary information alongside the three KPIs required by Article 8(2), it is important to note that this information is unlikely to be harmonised across different non-financial undertakings in the absence of more specific disclosure requirements.

100. As ESMA observed in its 2019 advice to the Commission on undue short-term pressure on corporations[27] and further in its response to the Commission's consultation on the review of the Non-Financial Reporting Directive,[28] the absence of detailed reporting rules under the Non-Financial Reporting Directive significantly impedes undertakings' ability to provide comparable disclosure. This makes it difficult for investors to use non-financial information to make investment decisions and is generally unhelpful for the broader group of users of non-financial information.

101. As evidenced in the Commission's summary of responses to the consultation on the review of the Non-Financial Reporting Directive,[29] this point is also broadly

[25] Communication from the Commission – Guidelines on non-financial reporting (methodology for reporting non-financial information), OJ C 215, 5.7.2017, p. 1–20, page 13.
[26] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 29.
[27] ESMA30-22-762 Report – *Undue short-term pressure on corporations*, 18 December 2019.
[28] ESMA32-334-245 Response to public consultation - *ESMA response to the European Commission consultation on the review of the NFRD*, 11 June 2020.
[29] Ares(2020)3997889 *Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive*, 29 July 2020.

acknowledged among market participants, across both users and preparers of non-financial information.

102. ESMA is therefore of the view that it is necessary to lay down some requirements for the information which non-financial undertakings should publish alongside the three KPIs. ESMA observes that it was suggested by certain stakeholders during ESMA's outreach that it is too soon to target comparability in the disclosure accompanying the KPIs. Instead, these stakeholders proposed that during the first years non-financial undertakings should be given flexibility on what to include in this disclosure and that more detailed requirements could be adopted a few years down the line.

103. However, ESMA suggests that such an approach would entail a risk to non-financial undertakings themselves, as they would be likely to adopt a certain way of preparing their accompanying disclosure. This way may be inconsistent with the detailed requirements to follow down the line, at which point the non-financial undertakings would have to change their procedures which may cause them to incur costs. On this basis, ESMA suggests it is more cost-efficient to lay down certain disclosure rules from the beginning to establish clarity. Establishing detailed requirements is also better aligned with the overall movement towards increased standardisation in the realm of non-financial disclosure. However, ESMA is mindful of the importance of avoiding undue burdens on non-financial undertakings from these disclosure rules.

3.2.2.3 Which accompanying disclosures should be required?

104. Firstly, ESMA suggests it would be helpful to make a reference to the general requirement in Article 19a(1) / 29a(1) of the Non-Financial Reporting Directive to provide information to the extent necessary for an understanding of the development, performance, position and impact of the undertaking / group.

105. With this requirement as the starting point, ESMA suggests that non-financial undertakings should be required to provide accompanying disclosure alongside the KPIs in the following categories, containing the following disclosure requirements:

   a. Methodology:

      1. Accounting policy: Explain how turnover, CapEx and OpEx were defined and the basis on which they were calculated, including a reference to the related line item in the financial statements. If the definition has changed since the previous reporting period, explain the changes and why these changes result in reliable and more relevant information in the KPI. Explain whether the KPIs disclosed in accordance with Article 8 of the Taxonomy Regulation differ from any Alternative Performance Measures (APMs) as defined in ESMA's Guidelines on APMs, which are labelled in the same way or that depict items of turnover, capital expenditures and operating expenditures.

2. Assessment of Taxonomy-alignment: Explain how turnover, CapEx and OpEx were allocated across the non-financial undertaking's different activities to avoid double counting. Explain how the undertaking performed the following assessments:

    i. Whether the substantial contribution criteria, including technical screening criteria, are met;

    ii. Whether the DNSH criteria, including technical screening criteria, are met; and

    iii. Whether minimum safeguards are met.

b. Context:

Interpretation: Explain what each of the KPIs show and why they increased or decreased in the reporting period.

For CapEx, disclosure should be provided of the drivers of the change in fixed assets during the reporting period with separate indication of the contribution of each driver to the total change, as well the portion attributable to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation. Such reconciliation shall refer to, as a minimum, the following items (where applicable): disposals and acquisitions of fixed assets, impairments, revaluations, any other valuation adjustments, depreciation and amortisation. Where a reconciliation of the change in fixed assets during the reporting period is already required by the applicable GAAP (e.g. in accordance with paragraph 73(e) of IAS 16, paragraph 118(e) of IAS 38 and paragraphs 76 and 79 of IAS 40), disclose the information requested by this reconciliation separately for assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation. In addition, disclosure should be provided of any amount of right-of-use assets recognised in relation to leased fixed assets (this requirement should only apply to undertakings who account for right-of-use assets based on the applicable accounting standards). The information on leased assets should be provided for assets / processes associated with economic activities that qualify as environmentally sustainable, accompanied by disclosure of related impact on the calculated CapEx KPI of leased assets. Both the reconciliation and the information on the leased assets can be included in the non-financial statement by means of cross-reference.

106. The accompanying information specified above constitutes a minimum requirement. In other words, non-financial undertakings should be free to provide additional disclosure

which they consider material to explain the KPIs. In particular, an undertaking may provide supplementary information with regard to its future objectives in order to explain whether it has set a future target for the size of the KPI and how it plans to achieve this target. This disclosure may be provided on a voluntary basis.

107. ESMA considers that the accompanying disclosure suggested above should be placed together with the KPIs, as this will make it most useful for investors and other users. This is consistent with the Commission's suggestion for ESMA to consider the idea of disclosure to *accompany* the KPIs, i.e. information which sits together with the KPIs.

108. However, to ensure that the KPIs and the accompanying information become an integrated and as such helpful part of the non-financial statement, ESMA suggests that it should be possible to comply with the requirement for accompanying information via reference. This would mean that if a non-financial undertaking prefers to disclose some or all of the accompanying information somewhere else in the non-financial statement, it should be allowed to do so without duplicating that information next to the KPIs. Instead, the undertaking should simply be required to insert a cross-reference – in the form of a direct hyperlink – to the relevant accompanying disclosure next to the KPIs, so that users can access the information with one click.

109. In addition to the above information, ESMA furthermore proposes that it would be relevant to require non-financial undertakings to provide comparatives for the three KPIs. This will enable investors and other users to easily understand the development of the KPIs from the previous reporting period. ESMA suggests that comparatives should be provided for one year.

110. The requirement for comparatives in ESMA's view should only start to apply in the second year of application of the requirement to disclose the KPIs, so that non-financial undertakings are not obliged to retroactively apply the requirement. Please see further considerations on this in Section 3.3.5.

111. Lastly, ESMA considers that non-financial undertakings should ensure that the accompanying information is not misleading, that it is unbiased and that they should furthermore avoid boilerplate language. ESMA expects that these requirements will be applied in a way that will not adversely affect the necessary comparability of these disclosures.

3.2.3 Relevance of KPIs for non-financial undertakings operating in a given sector

112. In its call for advice, the Commission asks ESMA to consider whether it should be specified which KPI(s) is / are relevant for non-financial undertakings in a given sector.

113. In ESMA's reading, Article 8(2) of the Taxonomy Regulation does not leave any optionality to non-financial undertakings that fall within the scope of the Non-Financial Reporting Directive regarding which KPIs they should disclose: it requires those non-financial undertakings to disclose the proportion of turnover derived from products /

services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation and the proportion of CapEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation and the proportion of OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation.

114. As such, ESMA understands that non-financial undertakings within the scope of the Non-Financial Reporting Directive will always be required to disclose all three KPIs, even if, for example, for a given non-financial undertaking one of the KPIs is 0%.

115. Nevertheless, ESMA appreciates that the CapEx KPI might for example be more relevant for sectors which are transitioning from an environmentally harmful performance to becoming Taxonomy-compliant. In the latter case, as highlighted in the TEG's final report, the CapEx KPI will give investors and other users an insight on the company's strategy and allow them to assess it.[30] However, in other cases the information provided by the three KPIs will be complementary. Furthermore, ESMA considers that the relevance of the KPIs for given sectors will likely change over time as Taxonomy-alignment is gradually attained.

116. ESMA is of the view that for the new disclosure requirements under Article 8(2) of the Taxonomy Regulation to be most useful to both users and preparers of non-financial information, they should provide a minimum set of reliable and comparable information on Taxonomy-aligned activities. To achieve this objective, ESMA considers that the applicable rules should be kept straightforward and easy to understand both by users and preparers. On this basis, ESMA is minded at this stage to adopt a cautious approach in its advice and refrain from proposing that non-financial undertakings should differentiate their disclosure of the relevant KPIs on the basis of sectoral considerations.

3.2.4 Draft advice

117. On the basis of the considerations in Section 3.2.1, 3.2.2 and 3.2.3, ESMA proposes the following draft advice in relation to the content of the three KPIs which non-financial undertakings are required to disclose in their non-financial information:

Defining the elements of the three KPIs

ESMA is of the view that it is important to establish clarity around the different elements of the three KPIs which non-financial undertakings have to disclose according to Article 8(2) of the Taxonomy Regulation. Only by having a uniform understanding of how to define each of the three KPIs and its constituent elements will non-financial

[30] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 28.

undertakings be able to provide comparable disclosure to the benefit of investors and other users of non-financial information.

As regards the KPI 'proportion of turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation', ESMA recommends that the Commission:

a. Require non-financial undertakings to use the definition of net turnover in Article 2(5) of the Accounting Directive as the reference point when calculating their turnover. More specifically,

    1. Non-financial undertakings applying IFRS should be required to count the amounts that are accounted for under IFRS 15 and IFRS 16. The turnover shall also include income accounted for under other standards when such income qualifies as arising from an entity's ordinary activities; and

    2. Non-financial undertakings applying national GAAP should be required to count the amounts that are accounted for under the corresponding provision in national GAAP.

b. Require non-financial undertakings to apply the following approach to counting turnover for the purpose of this KPI:

    1. For the environmental objectives climate change mitigation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control and protection and restoration of biodiversity and ecosystems, turnover can be counted where the economic activity meets:

        i. The criterion of making a substantial contribution to one or more of those environmental objectives, including by meeting the technical screening criteria;

        ii. The criterion of not doing significant harm to any of the other environmental objectives, including by meeting the technical screening criteria; and

        iii. The criterion of minimum safeguards.

    2. For the environmental objective climate change adaptation, turnover can be counted where the activity enables other activities to undergo climate change adaptation.

As regards the KPI 'proportion of capital expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable under

Articles 3 and 9 of the Taxonomy Regulation', ESMA recommends that the Commission:

a. Require non-financial undertakings to define CapEx in the following way:

   1. Non-financial undertakings applying IFRS should define CapEx as the change that occurred during the reporting year in the amount of fixed tangible and intangible assets, before any depreciation and amortisation charges for the year, as accounted for in accordance with IAS 16, IAS 38 and IAS 40 (if applicable); and

   2. Non-financial undertakings applying national GAAP should define CapEx as the change that occurred during the reporting year in the amount of fixed tangible and intangible capital, before any depreciation and amortisation charges for the year, as accounted for under the applicable GAAP in the financial statements of these undertakings.

b. Require non-financial undertakings to count CapEx for the purpose of this KPI where the costs incurred are part of a plan to meet:

   1. The criterion of making a substantial contribution to one or more of the environmental objectives, including by meeting the technical screening criteria;

   2. The criterion of not doing significant harm to any of the other environmental objectives, including by meeting the technical screening criteria; and

   3. The criterion of minimum safeguards.

   In this regard, 'plan' should meet the following conditions for the capital expenditure to be eligible:

   i. The plan should aim to make the economic activity in question Taxonomy-aligned within a maximum period of five years;

   ii. The plan should be approved by the non-financial undertaking's administrative body; and

   iii. The plan should be made available to the public, e.g. on the undertaking's website.

   The Commission should be mindful that the TEG has included in the Taxonomy some exceptional cases where individual improvement measures can be considered to make a substantial contribution without needing to be part of a plan.

As regards the <u>KPI 'proportion of operating expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable</u> under Articles 3 and 9 of the Taxonomy Regulation', ESMA recommends that the Commission:

a. Require non-financial undertakings to count within OpEx all items of expense that:

    1. arise from the undertaking's main business activities, which are generally identified as the principal revenue-producing activities of the entity; and

    2. relate neither to the investment nor financing categories and are therefore normally included in the amounts reported within metrics such as 'operating result'.

b. In identifying expenses relating to financing and investing activities, require non-financial undertakings take into account the following aspects:

    1. Financing activities generally result in changes in the size and composition of the contributed equity and borrowings of the entity. Expenses arising from these activities typically relate to the receipt or use of a financial resource (e.g. borrowings) from a financial institution or other provider of finance with the expectation that the resource will be returned to the provider. The financing expense constitutes the compensation due to the provider of finance. Such compensation is generally dependent on both the amount of the credit and its duration.

    2. Investing activities typically relate to the acquisition and disposal of financial and non-financial assets that do not relate to operating assets, such as property, plant and equipment. Expenses from such activities generally relate to assets that generate a return individually and largely independently of other resources held by the entity.

c. Require non-financial undertakings to count OpEx for the purpose of this KPI where the costs incurred are part of a plan to meet:

    1. The criterion of making a substantial contribution to one or more of the environmental objectives, including by meeting the technical screening criteria;

    2. The criterion of not doing significant harm to any of the other environmental objectives, including by meeting the technical screening criteria; and

    3. The criterion of minimum safeguards.

In this regard, ‘plan’ should meet the following conditions for the capital expenditure to be eligible:

i. The plan should aim to make the economic activity in question Taxonomy-aligned within a maximum period of five years;

ii. The plan should be approved by the non-financial undertaking’s administrative body; and

iii. The plan should be made available to the public, e.g. on the undertaking’s website.

The Commission should be mindful that the TEG has included in the Taxonomy some exceptional cases where individual improvement measures can be considered to make a substantial contribution without needing to be part of a plan.

For all three KPIs, to avoid double counting of turnover / CapEx / OpEx across several economic activities, ESMA advises the Commission to require non-financial undertakings to apply their best judgement of how to split turnover / CapEx / OpEx across their activities and to avoid doing so in a way which unduly inflates the turnover / CapEx / OpEx related to Taxonomy-aligned economic activities.

<u>Specifying the disclosure which should accompany the three KPIs</u>

ESMA considers that it would be helpful for investors and other users to receive accompanying information alongside the three KPIs. Such information should make it clear how the KPIs where prepared and what they cover and put them into context, so that investors and other users may more easily interpret them.

ESMA recommends that the Commission establish certain requirements on the content of this accompanying information in its delegated act to ensure comparability across the information provided by different non-financial undertakings. More specifically, ESMA advises the Commission to establish rules as specified below.

Firstly, ESMA proposes to insert a general reference in the Commission’s delegated act to the requirement in Article 19a(1) / 29a(1) of the Non-Financial Reporting Directive to provide information to the extent necessary for an understanding of the undertaking's development, performance, position and impact of its activity, relating to, inter alia, environmental matters.

Furthermore, for all three KPIs ESMA suggests that non-financial undertakings should be required to provide the following accompanying information in the following categories:

a. Methodology:

1. Accounting policy: Explain how turnover, CapEx and OpEx were defined and the basis on which they were calculated, including a reference to the related line item(s) in the financial statements. If a definition has changed since the previous reporting period, explain the changes and why these changes result in reliable and more relevant information. Explain whether the KPIs disclosed in accordance with Article 8 of the Taxonomy Regulation differ from any Alternative Performance Measures (APMs) as defined in ESMA's Guidelines on APMs, which are labelled in the same way or that depict items of turnover, capital expenditures and operating expenditures.

2. Assessment of Taxonomy-alignment: For each KPI, explain how the undertaking performed the following assessments:

    i. Whether the substantial contribution criteria, including technical screening criteria, are met;

    ii. Whether the DNSH criteria, including technical screening criteria, are met; and

    iii. Whether minimum safeguards are met;

And describe the nature of the products / services or assets / processes that are considered Taxonomy-aligned. Explain how turnover / CapEx / OpEx was allocated across economic activities to avoid double counting.

b. Context:

Interpretation: Explain what each KPI shows and why it increased or decreased in the reporting period. For CapEx, provide reconciliations explaining the drivers of change in CapEx during the reporting period for assets / processes associated with economic activities that qualify as environmentally sustainable. Such reconciliation shall refer to, as a minimum, the following items (where applicable): disposals and acquisitions of fixed assets, impairments, revaluations, any other valuation adjustments, depreciation and amortisation. For Capex, non-financial undertakings shall also disclose the amounts relating to right-of-use assets associated to leased fixed assets (the latter requirement should only apply to undertakings who account for right-of-use assets based on the applicable accounting standards), accompanied by disclosure of the impact on the calculated CapEx KPI of leased fixed assets.

In addition to the above accompanying information undertakings may provide any disclosure which they consider material to explain the KPIs. This information may include, but is not limited to, information with regard to future objectives in order to explain whether undertakings have set a future target for the size of the KPI and how they plan to achieve this target. Such disclosure may be provided on a voluntary basis.

Across all three KPIs, ESMA suggests that the accompanying information should be placed in the immediate vicinity of the KPIs, as this will make the information most helpful for investors and other users. However, to avoid undue burden on non-financial undertakings and to ensure that the KPIs and the accompanying information become an integrated part of the non-financial statement, ESMA recommends that the Commission permit compliance by reference. This would entail that where non-financial undertakings prefer to disclose some or all of the accompanying information in a different part of the non-financial statement, they should be permitted to do so on the condition that they provide a cross-reference in the form of a direct hyperlink to this other part of the non-financial statement, so that users can access the relevant information with one click.

For all three KPIs, ESMA advises the Commission to require non-financial undertakings to present one year of comparatives. This requirement should start to apply in the second year of application of the disclosure requirements.

ESMA suggests that the Commission require non-financial undertakings to ensure that the accompanying information is not misleading and that it is unbiased and that non-financial undertakings avoid boilerplate language.

3.2.5 Questions for consultation

Definitions – questions related to the KPI 'proportion of turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'

Question 1: For this KPI, do you agree with the proposed approach to <u>defining</u> turnover (bullet a in the draft advice)?

Question 2: For this KPI, do you agree with the proposed approach to when turnover <u>can be counted</u> (bullet b in the draft advice)?

Definitions – questions related to the KPI 'proportion of capital expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'

Question 3:	For this KPI, do you agree with the proposed approach to <u>defining</u> CapEx (bullet a in the draft advice)?
Question 4:	For this KPI, do you agree with the proposed approach to when CapEx <u>can be counted, including the definition of 'plan'</u> (bullet b in the draft advice)?
Definitions – questions related to the KPI 'proportion of operating expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'	
Question 5:	For this KPI, do you agree with the proposed approach to <u>defining</u> OpEx (bullet a in the draft advice)?
Question 6:	For this KPI, do you agree with the proposed approach to when OpEx <u>can be counted</u>, including the definition of 'plan' (bullet b in the draft advice)? With reference to the TEG's inclusion of the words "if relevant" in relation to OpEx, in which situations should it be possible to count OpEx as Taxonomy-aligned?
Definitions – questions related to all three KPIs	
Question 7:	Do you believe that any of the suggested approaches covered in questions 1 to 6 above will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or ongoing, and provide your best quantitative estimate of their size.
Question 8:	Do you agree that sectoral specificities should not be addressed in the advice, as proposed in Section 3.2.3?
Accompanying information – questions related to all three KPIs	
Question 9:	Do you agree with the requirements for accompanying information which ESMA has proposed for the three KPIs?
Question 10:	Do you consider that the requirement to refer to the relevant line item(s) in the financial statements for each KPI ensures sufficient integration between the KPIs and the financial statements?
Question 11:	Do you agree with ESMA's suggestion to permit compliance by reference, so that non-financial undertakings may present the accompanying information elsewhere in the non-financial statement than in the immediate vicinity of the KPIs, as long as they provide a hyperlink to the location of the accompanying information?

Question 12:	Do you consider there are additional topics that should be considered by ESMA in order to specify the content of the three KPIs? If yes, please elaborate and explain the relevance of these topics.
Question 13:	Do you believe that providing the suggested accompanying information will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

3.3 Methodology for preparing KPIs

3.3.1 Introductory considerations relating to the methodology

118. In its call for advice, the Commission asks the ESAs to determine the methodologies that undertakings should adopt when preparing their KPIs. In the specific questions addressed to ESMA, the Commission sets out certain topics which are of relevance for the determination of the methodology that non-financial undertakings should apply when complying with their disclosure requirements pursuant to Article 8(2) of the Taxonomy Regulation. ESMA is invited to consider these topics when developing the elements of its advice relating to methodology.

119. In particular, the call for advice asks that ESMA examines in its advice which KPI(s) are relevant for companies in a given sector[31] alongside the following topics:

   a. Allocating turnover, CapEx and OpEx within the undertaking or group to different economic activities;

   b. Distinguishing between activities not covered by the Taxonomy and activities covered by the Taxonomy but where the non-financial undertaking does not meet the thresholds / technical screening criteria.

120. In the call for advice, the Commission additionally raises a further point for consideration. As such, the ESAs are invited to analyse whether all existing activities should be covered retroactively or only those relevant to the time period as of when the disclosure rules start to apply. ESMA understands that this request is related to the time difference in the disclosure obligations concerning the six environmental objectives. Initially, in the course of 2022, non-financial undertakings will be required to disclose the three KPIs in relation to the environmental objectives of climate change mitigation and climate change adaptation, relating to the financial year 2021. As the technical screening criteria for the remaining four environmental objectives[32] will be adopted by 31 December 2021, non-

[31] The issue relating to the relevance of KPIs in a specific sector is discussed in Section 3.2.3 of this Consultation Paper.
[32] The four environmental objectives are sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control and protection and restoration of biodiversity and ecosystems.

financial undertakings will be required to disclose the three KPIs in relation to the other four environmental objectives, relating to the financial year 2022.

121. To examine the methodological considerations that are relevant for the disclosure of the three KPIs, ESMA undertook a preliminary identification of certain questions that appear to be of relevance. These questions relate to the analytical steps that a non-financial undertaking would take in order to prepare the required KPIs and include the topics mentioned in the Commission's call for advice as well as a few additional points which ESMA considered would be worth investigating:

    a. Should non-financial undertakings disclose the three KPIs per economic activity or as a total across all activities?

    b. Should non-financial undertakings disclose the three KPIs per environmental objective or as a total across all environmental objectives?

    c. Should non-financial undertakings disclose the three KPIs for activities which are not covered by the Taxonomy as well as for activities which are covered by the Taxonomy but for which the technical screening criteria are not met?

    d. Should non-financial undertakings disclose the three KPIs retroactively in the case of the four environmental objectives for which the delegated acts will be adopted only by 31 December 2021?

122. The sections below set out ESMA's thinking in relation to these questions and as such explain the logic behind its draft advice to the Commission concerning the methodology for the disclosure of the three KPIs by non-financial undertakings. ESMA notes that the issue of allocating turnover, CapEx and OpEx to different economic activities as well as the issue of the relevance of certain KPIs in certain sectors have been addressed in Section 3.2 of this Consultation Paper as in ESMA's view these points are closely related to the content of the KPIs.

3.3.2 Disclosure of KPIs per economic activity

3.3.2.1 Which level of granularity to require

123. Non-financial undertakings are obliged to disclose the information set out in Article 8(2) of the Taxonomy Regulation for economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Regulation. As part of its analysis for its draft advice, ESMA considered two approaches that non-financial undertakings could follow in order to calculate and disclose the three KPIs in relation to the economic activities in which it engages:

- Approach 1: Calculate and disclose the KPIs as a total across all the undertaking's economic activities.

- Approach 2: Calculate and disclose the KPIs individually for each of the undertaking's economic activities.

124. ESMA analysed the two approaches and considers that they would each provide certain advantages.

125. As regards Approach 1, ESMA appreciates that aggregate disclosure for each KPI has the advantage of simplicity for users of non-financial information which will only need to seek a single figure for each KPI to assess a company's environmental strategy and sustainability performance. Information overload is being avoided in this case, as this single figure would give users of this information a first glimpse, albeit preliminary, of an undertaking's Taxonomy-alignment. Furthermore, Approach 1 can be relatively easily implemented by companies and will likely involve less preparation effort from their side. This approach, however, does not provide transparency on the issue of double counting where an economic activity substantially contributes to one or more environmental objectives and as such, it may obscure elements which are relevant for users. This issue is relevant considering that the NFRD does not require auditing of the non-financial statement which could address this matter. For that reason, ESMA does not consider that requiring the disclosure of a single figure for each of the three KPIs would provide users with sufficient information to assess where an undertaking is in terms of the Taxonomy-alignment of its activities.

126. As regards Approach 2, ESMA observes that the starting point for non-financial undertakings to calculate the three KPIs would be the identification of their economic activities. As a next step, undertakings would need to examine these economic activities to determine to which environmental objective(s) they make a substantial contribution and check their compliance with the other three criteria set out in Article 3 of the Taxonomy Regulation, including the technical screening criteria. Based on this analysis, undertakings would possess the necessary information to decide which economic activities qualify as environmentally sustainable pursuant to Article 8 of the Taxonomy Regulation and as such be able to provide the level of granularity foreseen Approach 2.

127. ESMA therefore considers that the level of detail in Approach 2 is preferable, as it both provides users with more detailed information and as it should not place undue burden on non-financial undertakings. ESMA also notes that disclosure per economic activity is in line with the TEG's thinking. In its final report, the TEG states that *"…assessing alignment with the Taxonomy should be performed by economic activity rather than by sector or industry"*.[33] In addition, ESMA considers that non-financial undertakings should also provide totals in accordance with Approach 1. This means that non-financial undertakings should disclose the information required under Article 8 of the Taxonomy Regulation per economic activity. To complement this disclosure, ESMA will propose in its advice that undertakings also disclose a total of the three KPIs across all economic activities at the level of the company or the group.

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[33] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 35.

3.3.2.2 Economic activities contributing to more than one environmental objective

128. In applying Approach 2, it is still relevant to address the matter of double counting of turnover / CapEx / OpEx as regards activities that contribute to one or more environmental objectives. The TEG also draws attention to this issue in its final report.[34]

129. To address the issue of double counting, when a non-financial undertaking has an activity that contributes to more than one environmental objective ESMA understands that the undertaking would normally select one objective to which, in its best judgement, the activity most strongly contributes. The turnover / CapEx / OpEx related to that activity would then be assigned to that objective. This approach is in line with the TEG's assessment in its final report.[35]

130. In ESMA's view, non-financial undertakings should be required to disclose and explain how they allocated their turnover / CapEx / OpEx to prevent double counting. This disclosure should be included in the accompanying information alongside the KPIs, as addressed in Section 3.2.2 of this Consultation Paper. Given that investors and other users of non-financial information are provided with more granular information under Approach 2 than they would be given under Approach 1, it will be easier for them to understand the explanations on how double counting was avoided.

3.3.2.3 Company size

131. ESMA also considered whether it would be helpful to propose that the disclosure around the three KPIs be differentiated for proportionality considerations. However, ESMA notes that undertakings that fall within scope of the Non-Financial Reporting Directive are already fairly large as they must have at least 500 employees. Therefore, ESMA does not consider that it is necessary to adapt the methodology for preparing the three KPIs to the size of the non-financial undertaking. ESMA also points out that such an additional distinction would add complexity to the new disclosure regime and would not facilitate the application of the new disclosure rules.

3.3.2.4 Enabling and transitional activities

132. Lastly in relation to disclosure of the three KPIs per economic activity, ESMA considered whether non-financial undertakings should be required to provide additional information in relation to whether each economic activity for which the three KPIs are disclosed are enabling or transitional.

133. The Taxonomy Regulation requires disclosure in relation to enabling and transitional activities. In particular, Article 5 [36] establishes requirements for financial products investing in an economic activity that contributes to an environmental objective within the

[34] Ibid, page 37.
[35] Ibid, page 37.
[36] Transparency of environmentally sustainable investments in pre-contractual disclosures and in periodic reports.

meaning of Article 2(17) of the SFDR.[37] Under the second paragraph of Article 5, an obligation is imposed in relation to financial products to provide details on the proportions of enabling and transitional activities referred to in Article 16 and Article 10(2), respectively, as a percentage of all investments selected for the financial product. The obligations pursuant to this article will apply to undertakings that may not necessarily fall within scope of the Non-Financial Reporting Directive.

134. ESMA takes note of this provision which signals a need for reliable and public information on economic activities that would meet the criteria of enabling and transitional activities set out in the Taxonomy Regulation. This is also in line with the TEG's final report which recommends that company disclosure obligations under the Non-Financial Reporting Directive be clarified to include disclosure on the basis of enabling and transition activities.[38]

135. To ensure that helpful information is provided to financial market participants, ESMA believes that the categorisation of activities across enabling and transitional should be provided by non-financial undertakings. In this regard, financial market participants would have certainty about transitional and enabling activities and make use of this information for their own disclosure obligations.

136. ESMA observes that it would expect non-financial undertakings to have already carried out an assessment of the categorisation of their economic activities when identifying them for the purpose of calculating the KPIs. In other words, ESMA understands that non-financial undertakings will usually be in possession of the relevant information for this disclosure. ESMA notes that the table in Section 5 of the TEG's final report could be a helpful aide to non-financial undertakings in this regard as it includes an indication of whether the technical screening criteria relate to the performance of the economic activity itself or whether the activity is an enabling activity for the activities covered in its final report.[39]

3.3.3 Disclosure of KPIs per environmental objective

137. ESMA takes note that the TEG in its final report recommends that undertakings complete the calculation of its KPIs separately for each of the six environmental objectives to provide transparency around which objectives are being pursued.[40] This calculation can be provided in 2022 for the first two environmental objectives for which technical

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[37] Under Article 2(17) of the SFDR, 'sustainable investment' means an investment in an economic activity that contributes to an environmental objective, as measured, for example, by key resource efficiency indicators on the use of energy, renewable energy, raw materials, water and land, on the production of waste, and greenhouse gas emissions, or on its impact on biodiversity and the circular economy, or an investment in an economic activity that contributes to a social objective, in particular an investment that contributes to tackling inequality or that fosters social cohesion, social integration and labour relations, or an investment in human capital or economically or socially disadvantaged communities, provided that such investments do not significantly harm any of those objectives and that the investee companies follow good governance practices, in particular with respect to sound management structures, employee relations, remuneration of staff and tax compliance.
[38] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 29.
[39] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 56.
[40] Ibid, page 28.

screening criteria will have been adopted and in 2023 also for the remaining four environmental objectives. Keeping in mind the TEG's recommendations, ESMA examined the potential merits of two alternative approaches:

- Approach 1: Calculate and disclose the KPIs as a total across the six environmental objectives.

- Approach 2: Calculate and disclose the KPIs individually for each of the six environmental objectives.

138. In comparing the two approaches, ESMA notes that Approach 1 would result in the publication of a unique figure per KPI for each economic activity based on ESMA's proposal in Section 3.3.2 for disclosure of the KPIs per activity. This would serve as a single reference point of each activity's Taxonomy-alignment, which, if further aggregated at company or group level, could make it easy for users of non-financial information to compare across undertakings and across sectors.

139. Nevertheless, when adding up the KPIs across all environmental objectives undertakings will have to consider how best to aggregate this information. Even though there are merits in disclosing aggregated information, ESMA highlights that condensing diverse information into a single figure is likely to be based on assumptions and could obscure certain information that is important for investors and other users of non-financial information. As already discussed in Section 3.3.2 one such question that would need to be considered relates to the treatment of activities that contribute to more than one environmental objective and how to avoid possible double counting. The type of aggregated disclosure connected with Approach 1 is likely to leave out aspects that are relevant for users of non-financial information.

140. ESMA notes that financial market participants who are obliged to disclose how their investments are aligned with the Taxonomy would need from investee companies information with a sufficient level of granularity to allow them to assess their Taxonomy-alignment. ESMA furthermore observes that under Article 5 of the Taxonomy Regulation, issuers of financial products are required to disclose information in accordance with Articles 6(3) and 11(2) of the SFDR which should include:

    a. the information on the environmental objective or environmental objectives set out in Article 9 of the Taxonomy Regulation to which the investment underlying the financial product contributes; and

    b. a description of how and to what extent the investments underlying the financial product are in economic activities that qualify as environmentally sustainable under Article 3 of the Taxonomy Regulation.

141. It seems, therefore, that Article 5 of the Taxonomy Regulation establishes a link between the disclosure required across the investment chain and the granularity of such disclosure. From a practical point of view, therefore, the level of granularity provided by investee companies (i.e. non-financial undertakings) under Article 8 of the Taxonomy

Regulation will have a direct impact on the information that will be available to financial market participants which will need to reuse this information to fulfil their own reporting obligations.

142. Based on the above considerations, ESMA is of the view that providing aggregate disclosure across all objectives complemented with a detailed set of disclosures per objective is in line with one of the objectives of the Commission's Action Plan to reorient capital flows towards more sustainable investments. As such, ESMA is minded to recommend a combination of Approaches 1 and 2, i.e. that non-financial undertakings be required to disclose the three KPIs per environmental objective along with a total per KPI across all environmental objectives.

143. This is further supported by Recital 6 of the Taxonomy Regulation which highlights the importance of providing clear guidance on activities that qualify as contributing to environmental objectives to help inform investors about the investments that fund environmentally sustainable economic activities thereby allowing the channelling of capital into sustainable investments. Furthermore, as explained in Recital 18 of the Taxonomy Regulation this level of granular disclosure would also serve the purpose of enabling national competent authorities to more easily verify compliance of undertakings with their disclosure obligations and enforce such compliance.

3.3.4 Activities that are not Taxonomy-aligned or not covered by the Taxonomy

144. As explained in the TEG's final report,[41] the Taxonomy proposed by the TEG covers economic sectors and economic activities which have the potential to make a substantial contribution to climate change mitigation and climate change adaptation. Furthermore, there are activities which are not yet covered by the Taxonomy as well as economic activities for which there is no NACE code.

145. The Commission's Platform on Sustainable Finance has been tasked with developing a fully-fledged Taxonomy. Acknowledging, however, that currently there are activities which are not yet covered by the Taxonomy, the TEG suggests that the Platform on Sustainable Finance should consider how to enable undertakings who undertake activities which are not yet covered by the Taxonomy to explain their performance.42 In the meantime, the TEG considers that undertakings may wish to provide information on these economic activities in their disclosures on a voluntary basis.

146. As part of its analysis for its draft advice, ESMA considered two approaches to distinguishing between activities which are not covered by the Taxonomy and activities which are not Taxonomy-aligned:

[41] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 13.
[42] Ibid, page 36.

- Approach 1: Distinguish between economic activities that are a) covered by the Taxonomy and b) not covered by the Taxonomy.

- Approach 2: Distinguish between economic activities that are a) covered by the Taxonomy and Taxonomy-aligned in accordance with Article 3 of the Taxonomy Regulation, b) covered by the Taxonomy but not Taxonomy-aligned in accordance with Article 3 of the Taxonomy Regulation and c) not covered by the Taxonomy.

147. Approach 1 would entail providing disclosure in relation to economic activities that are covered by the Taxonomy, i.e. for which technical screening criteria have been developed, and for activities that are not covered by the Taxonomy. Approach 2 would entail a further breakdown of the activities which in Approach 1 are covered by a), as it would require distinguishing between activities which are covered by the Taxonomy and Taxonomy-aligned and activities which are covered by the Taxonomy but not Taxonomy-aligned.

148. ESMA appreciates that Approach 1 is relatively easy to apply. A non-financial undertaking would only need to consider whether economic activities meet one basic condition, i.e. covered or not covered by the Taxonomy in order to comply with the disclosure required under this approach. Furthermore, such disclosure would give stakeholders the minimum information they need to identify which economic activities are Taxonomy-aligned.

149. On the other hand, the additional breakdown foreseen in Approach 2 would provide users of non-financial information with a more complete picture as it includes elements that would be helpful to get a more thorough insight on an undertaking's path towards Taxonomy-alignment. As put forward by some stakeholders who provided input to ESMA during the preparation of ESMA's draft advice, the information on the economic activities which are covered in the Taxonomy, but which are not yet Taxonomy-aligned, could be used by investors for engagement purposes in order to initiate a dialogue with a non-financial undertaking's management to discuss the undertaking's environmental objectives.

150. ESMA is cognisant that the disclosure required under Approach 2 would involve a more detailed description of a non-financial undertaking's economic activities and potentially more effort to prepare. However, in general, investors and other users of non-financial information are interested in gaining a better understanding of where undertakings stand in terms of their commitment to environmental objectives and the environmental footprint of their economic activities. Furthermore, ESMA notes that in the course of preparing for their compliance with the disclosure required under Article 8(2) of the Taxonomy Regulation, undertakings will have already identified those economic activities which are covered by the Taxonomy but do not meet the relevant criteria to be Taxonomy-aligned as well as the economic activities which are not covered by the Taxonomy.

151. ESMA has taken note of the TEG's recommendations which ask for narrative disclosure for activities for which technical screening criteria have not been developed or which are not addressed by the Taxonomy, as illustrated in the below table:

Table 4: Disclosure approaches for companies with and without Taxonomy coverage[43]

Case	TEG recommendation
The economic activity is covered by existing technical screening criteria.	Disclose turnover, capex and, if relevant, opex in line with the methodology (above).
The economic activity may be able to make a substantial contribution to climate change mitigation or adaptation, but technical screening criteria have not been developed yet.	Disclose that the economic activity does not yet have technical screening criteria. Inform the Platform on Sustainable Finance.
The economic activity may be able to make a substantial contribution to the other environmental objectives, but technical screening criteria have not been developed yet. All disclosure of this kind is voluntary until the delegated acts enter into application.	Disclose that the economic activity does not yet have technical screening criteria because the Taxonomy does not yet cover the environmental objective to which it contributes (3–6). Narrative disclosure about environmental performance is still possible using NFRD guidelines. Inform the Platform on Sustainable Finance.
The economic activity does not, in the opinion of the issuer or operator, have a significant impact on the Taxonomy's environmental objective(s), and improved performance in its own operations is unlikely to make a substantial contribution to an environmental objective. Note that this situation will not apply to climate change adaptation.	Disclose that the economic activity is not addressed by the Taxonomy. Companies can (and should) disclose how they manage their environmental impacts. The fact that their activities do not make a substantial contribution to an environmental objective does not mean that the companies do not contribute positively to the environment by responsibly managing their environmental impacts, no matter how limited these are.

152. Nevertheless, ESMA observes that it is worth considering whether such disclosure should be only narrative or should be extended to include the three KPIs foreseen in Article 8 of the Taxonomy Regulation.

153. ESMA notes that a set of information that is comparable to the one provided on economic activities that are Taxonomy-aligned would enhance users' understanding of the information on activities which are not Taxonomy-aligned / not covered by the Taxonomy. This type of granular information would provide a concrete basis for the dialogue between stakeholders and the management of non-financial undertakings by establishing a high level of transparency on the commitment of non-financial undertakings to long-term environmental goals.

[43] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, page 36.

154. With this in mind, ESMA considers that it would have a positive impact on the achievement of the undertaking's environmental objectives to provide information on the three KPIs and narrative information in relation to economic activities which are not Taxonomy-aligned and economic activities which are not covered by the Taxonomy. ESMA considers that users of non-financial information would appreciate disclosure on the three metrics set out in Article 8(2) for activities covered by the Taxonomy but for which the relevant criteria are not met as well as activities not covered by the Taxonomy. In this regard, while recognising that this proposal goes further than the TEG's recommendations ESMA would like to seek the views of stakeholders about this approach.

155. ESMA, therefore, is minded to propose that undertakings should provide a breakdown of their economic activities as indicated in approach 2, namely provide the disclosure required under TR Article 8(2) on:

   a. economic activities which are covered by the Taxonomy, including in relation to economic activities which are covered by the Taxonomy but for which the relevant criteria are not met and therefore are not Taxonomy-aligned; and

   b. economic activities which are not covered by the Taxonomy.

3.3.5 Retroactive disclosure of KPIs

156. In its call for advice, the Commission invites the ESAs to analyse whether all existing activities should be covered retroactively or only those relevant to the time period as of when the disclosure rules start to apply. As mentioned previously in the Consultation Paper, the disclosure requirements set out in Article 8(2) of the Taxonomy Regulation apply with the following timing:

   a. Non-financial undertakings are required to disclose the three KPIs in relation to the environmental objectives of climate change mitigation and climate change adaptation in non-financial information published in 2022, relating to the financial year 2021.

   b. Non-financial undertakings are furthermore required to disclose the three KPIs in relation to the other four environmental objectives in non-financial information published in 2023, relating to the financial year 2022.

157. ESMA, therefore, considers that it would be possible to follow either of the two approaches mentioned below:

- Approach 1: Non-financial undertakings should cover all existing activities retroactively when providing their disclosures under Article 8(2) of the Taxonomy Regulation.

- Approach 2: Non-financial undertakings should cover only activities relevant to the time period as of the moment when the disclosure rules start to apply when providing their disclosures under Article 8(2) of the Taxonomy Regulation.

158. In practical terms, Approach 1 would require non-financial undertakings to provide comparative information in the first year of application of the disclosure rules in relation to the four environmental objectives. In other words, they would need to provide the three KPIs not only relating to the financial year 2022 but also relating to the financial year 2021 as a comparative year.

159. Given the time lag between the disclosure obligations relating to the objectives of climate change mitigation and climate change adaptation compared to the four other environmental objectives, ESMA considers that a retroactive application of all disclosures required under Article 8 would provide investors with helpful information. Such an approach would allow for an assessment of the six environmental objectives in the same period and enable a more thorough evaluation of a non-financial undertaking's sustainability strategy over time.

160. On the other hand, ESMA is mindful that the delegated acts for the establishment of the technical screening criteria in relation to the four other environmental objectives will be adopted by 31 December 2021 in order to ensure its application from 1 January 2022. Based on this timing, non-financial undertakings are not likely to have specific information on the technical screening criteria that will apply to these objectives in the course of 2021.

161. Given the absence of specific information on the applicable rules, ESMA considers it will be challenging for non-financial undertakings to set up their information systems for the collection of the information that will be needed to comply with a retroactive disclosure of information relating to the four objectives. Considering the long-term time frame of the obligations set out in the Taxonomy Regulation and taking into account the fact that for the first year of application the whole framework set out in the Taxonomy Regulation will not yet be in place, ESMA is of the view that requiring retroactive disclosure in this case would be unduly burdensome for non-financial undertakings. This undue burden in ESMA's view outweighs the potential benefit to investors and other users. ESMA will therefore not recommend retroactive disclosure in its advice and considers that Approach 2 should be followed. If non-financial undertakings wish to apply Approach 1 on a voluntary basis, ESMA considers they should be permitted to do so.

3.3.6 Draft advice

162. On the basis of the considerations in Sections 3.3.1 to 3.3.5, ESMA proposes the following draft advice in relation to the methodology for preparing the three KPIs which non-financial undertakings are required to disclose in their non-financial information:

ESMA recommends that the Commission establish a number of requirements as regards the methodology which non-financial undertakings should apply when preparing their KPIs under Article 8(2) of the Taxonomy Regulation, as follows:

a. Non-financial undertakings should provide disclosure on the three KPIs per economic activity along with a total per KPI across economic activities at the level of the undertaking or group.

b. Non-financial undertakings should identify economic activities that are enabling as well as economic activities that are transitional and provide the three KPIs.

c. Non-financial undertakings should provide disclosure on the three KPIs per environmental objective along with a total per KPI at the level of the undertaking or group across all environmental objectives.

d. Non-financial undertakings should provide the three KPIs in relation to economic activities which are covered by the Taxonomy, including on economic activities which are covered by the Taxonomy but for which the relevant criteria are not met and therefore are not Taxonomy-aligned, and economic activities which are not covered by the Taxonomy.

To provide investors and other users with transparency on the above methodological points, ESMA recommends that the Commission require non-financial undertakings to disclose the following accompanying information, in the following categories which are set out in section 3.2.4:

a. Methodology:

   2. Assessment of Taxonomy-alignment: Where an economic activity contributes to more than one objective, explain how the issue of double counting was addressed and the reasons for choosing to attribute the relevant turnover / CapEx / OpEx to the specific economic activity.

3.3.7 Questions for consultation

Questions relating to the methodology of preparing KPIs

Question 14: Do you agree that non-financial undertakings should provide the three KPIs per economic activity and also provide a total of the three KPIs at the level of the undertaking / group? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.

Question 15: Do you agree that where an economic activity contributes to more than one environmental objective, non-financial undertakings should explain how they allocated the turnover / CapEx / OpEx of that activity across

	environmental objectives and where relevant the reasons for choosing one objective over another?
Question 16:	Do you agree that non-financial undertakings should provide information on enabling and transitional activities?
Question 17:	Do you agree that the three KPIs should be provided per environmental objective as well as a total at undertaking or group level across all objectives? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.
Question 18:	Do you agree that non-financial undertakings should be required to provide the three KPIs for economic activities which are covered by the Taxonomy, economic activities which are covered by the Taxonomy but for which the relevant criteria are not met and therefore are not Taxonomy-aligned as well as for economic activities which are not covered by the Taxonomy?
Question 19:	Do you agree with the proposal not to require retroactive disclosure concerning the four environmental objectives relating to the financial year 2021?
Question 20:	Do you consider that there are specific elements in ESMA's draft advice which are not in line with the information needed by financial market participants in order to comply with their own obligations under the Taxonomy Regulation and the SFDR? If yes, please specify in your answer.
Question 21:	Are there points that should be addressed in ESMA's advice in order to facilitate compliance of financial market participants across the investment chain? If yes, please specify.
Question 22:	Do you believe that ESMA's detailed proposals under Section 3.3 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.
Question 23:	Do you consider there are additional topics that should be considered by ESMA in order to specify the methodology that non-financial undertakings should follow? If yes, please elaborate and explain the relevance of these topics.

3.4 Presentation of KPIs

3.4.1 Standardised template in the form of a table

163. In its call for advice, the Commission invites ESMA to provide advice on the presentation of the three KPIs which non-financial undertakings are required to disclose pursuant to Article 8(2) of the Taxonomy Regulation. To develop its advice on this matter, ESMA took into account the following considerations.

164. Firstly, ESMA notes that the KPIs disclosed by non-financial undertakings under Article 8(2) will eventually be used by investors and other financial market participants in their assessment of the sustainability strategy of these undertakings, i.e. their investee companies. These KPIs will also provide the data that will allow financial market participants to comply with their own disclosure requirements in relation to the Taxonomy-alignment of their investments and products. ESMA considers that non-financial undertakings should therefore present the KPIs in a way that allows efficient further disclosure and general use of the KPIs by all concerned parties.

165. The KPIs will furthermore be important to other users of non-financial information, highlighting further the importance of presenting them in an easily accessible and comparable manner.

166. With these points in mind, ESMA sees merit in presenting the three KPIs in a standardised way. ESMA furthermore considers that the most suitable way of standardising the presentation of the KPIs would be to use a tabular format. Presentation in a tabular format according to a standardised template will provide certainty to non-financial undertakings about their information obligations and serve as a useful aide during the process of preparing the relevant KPIs and accompanying information. The use of such a uniform template will also contribute to the consistency and comparability of the disclosures published under Article 8.

167. ESMA suggests that the standard table should contain the three KPIs with the level of granularity described in Section 3.3, complemented by accompanying information as addressed in Section 3.2.2.

168. ESMA has developed such a standard table which is included in Annex III. While the table in Annex III refers to the turnover KPI for illustrative purposes, ESMA underlines that a separate table should be prepared for each of the three KPIs. ESMA notes that undertakings should ensure coherence and consistency between the content of the three tables (for example, by ensuring that the same economic activity is listed as contributing to the same environmental objective across the tables).

169. Based on the considerations in Section 3.3, ESMA suggests that for each of the three KPIs, the standard table should include the following rows and columns:

a. Economic activities (row): Presentation of those of the non-financial undertaking's economic activities which contributed to turnover / CapEx / OpEx during the reporting year.

b. NACE code (column): For the economic activities which are covered in the Taxonomy, the NACE[44] codes should be provided.

c. Absolute turnover / CapEx / OpEx (column): The turnover / CapEx / OpEx related to each economic activity expressed in the currency of the non-financial undertaking's choice.

d. Proportion of turnover / CapEx / OpEx (column): The turnover / CapEx / OpEx related to each economic activity expressed as a percentage of the overall turnover / CapEx / OpEx of the non-financial undertaking or group.

e. Covered by Taxonomy (column): Indication of whether the economic activity is covered by the Taxonomy.

f. Environmental objectives (six columns corresponding to the six environmental objectives): These columns should be filled in only for activities which are covered by the Taxonomy.

They should be used to indicate whether an economic activity substantially contributes to each of the environmental objectives. When one column indicates that the economic activity substantially contributes to the corresponding environmental objective, the other five columns should indicate whether the activity meets the DNSH and minimum safeguard criteria.

In some cases, only part of the turnover / CapEx / OpEx related to an economic activity will substantially contribute to one of the environmental objectives. This should be indicated in the relevant column by including the proportion of the activity's turnover / CapEx / OpEx that substantially contributes to an objective and the proportion that does not.

In case an economic activity substantially contributes to multiple objectives, the non-financial undertaking should select under which of the environmental objectives the activity should be reported as substantially contributing, as suggested in the TEG report and as further discussed in Section 3.3.2. The undertaking should then provide appropriate disclosure in the accompanying information to clarify to users that the activity also substantially contributed to another objective (or objectives) but that it was disclosed under one environmental objective in the table to avoid double counting.

[44] During the stakeholder outreach which ESMA undertook to prepare its draft advice, some stakeholders suggested that non-financial undertakings do not normally collect data based on the NACE codes.

g. Minimum safeguards (column): Indication of whether an economic activity meets the minimum safeguards.

h. Taxonomy-aligned proportion of turnover / CapEx / OpEx, year N (column): The proportion of an economic activity's turnover / CapEx / OpEx which is Taxonomy-aligned for the reporting year.

In cases where only part of the turnover / CapEx / OpEx related to an economic activity substantially contributes to one of the environmental objectives, this column should include only the proportion of that activity's turnover / CapEx / OpEx that substantially contributes to a specific objective. To identify this figure, the proportion of the turnover / CapEx / OpEx that substantially contributes to an objective should be multiplied with the proportion of the non-financial undertaking's overall turnover / CapEx / OpEx constituted by that economic activity.

i. Taxonomy-aligned proportion of turnover / CapEx / OpEx, year N-1 (column): The proportion of an economic activity's turnover / CapEx / OpEx which is Taxonomy-aligned for the year prior to the reporting year (comparative).

j. Category (column): This column should indicate whether an activity is enabling or transitional, however, based on the comply-or-explain mechanism as explained further in Section 3.3.2.4.

3.4.2 Formatting rules to be applied in the standard table

170. ESMA also explored the idea that the information included in the standard table follows a specific set of rules relating to format (punctuation, number of decimals etc.). This suggestion is complementary to ESMA's draft advice for a standardised template. The objective behind this thought is to further enhance the usefulness and comparability of the information in the table. To this end, ESMA has considered a number of formatting rules, as summarised in the table below, and would like to seek the views of market participants in this regard. Given that the disclosures under Article 8 would be part of the non-financial statement ESMA would also be interested in exploring possible implications of the formatting rules in relation to this document. The feedback provided will assist ESMA in formulating its advice to the Commission.

Table 5: Formatting rules for consideration in ESMA's advice to the Commission

Standardised numerical arrangement
Adhere to a standardised numerical arrangement, such as ISO 20022 (without limits on the maximum). This would include: a. Harmonised decimal points and thousand identifiers (e.g. using "." instead of "," for decimal points, and using "," instead of "." for thousand identifiers) b. Denoting costs/expenditures as positive numbers, not negative numbers, and having no additional notation (e.g. do not use parentheses to denote costs/expenditures) c. Expressing all absolute numbers without any rounding, and up to two digits after the decimal point d. Expressing all absolute numbers as they are, i.e. without any conversion (no 'millions') e. Expressing all absolute numbers with an associated currency to be disclosed next to each number (using ISO 20022 format for currencies) f. Expressing percentages with two digits after the decimal point and in the following format: e.g. 54.21% expressed as 54.21 (not 0.5421)
Standardised way of expressing not available information
Expressing not available information (if this is allowed under the policy guidance) using a standardised code, such as 'N/A' or 'Not available at this time' - If this information is not available now, but it is known when it will become available in the future, use of a standardised code + date (in YYYYMMDD format), such as 'N/A20210131')

3.4.3 Other considerations on presentation of KPIs

171. In its response to the Commission's consultation on a revision of the Non-Financial Reporting Directive, ESMA noted that it would be very beneficial for non-financial information to be made available through a single access point. ESMA also argued that it would be useful to tag non-financial information and render it in a machine-readable format, provided that non-financial information is harmonised and standardised.[45] ESMA believes these recommendations equally apply to the KPIs to be included in the non-financial statement under Article 8(2) of the Taxonomy Regulation. In particular, since these KPIS by their very nature are expected to be harmonised and standardised, ESMA suggests they should be rendered in a machine-readable format.

[45] ESMA32-334-245 Response to public consultation - *ESMA response to the European Commission consultation on the review of the NFRD*, 11 June 2020, in particular responses to Questions 33 and 35.

3.4.4 Draft advice

172. On the basis of the considerations in Sections 3.4.1 to 3.4.3, ESMA proposes the following draft advice in relation to the presentation of the three KPIs which non-financial undertakings are required to disclose under Article 8(2) of the Taxonomy Regulation:

> ESMA recommends that the Commission establish the following requirements as regards the presentational aspects of the disclosure that will be published pursuant to Article 8(2) of the Taxonomy Regulation:
>
> a. This disclosure should be provided in a standardised table, as set out in Annex III.
>
> b. The disclosure in the standardised table should comply with specific rules relating to its format to be finalised by ESMA based on feedback to this Consultation Paper.
>
> c. Non-financial undertakings should ensure coherence and consistency between the content of the tables relating to the three KPIs, for example, by ensuring that the same economic activity is listed as contributing to the same environmental objective across the tables.

3.4.5 Questions for consultation

Questions relating to the presentation of KPIs

Question 24: Do you agree that in order to ensure the comparability of the information disclosed under Article 8(2) of the Taxonomy Regulation and as such facilitate its usage, ESMA should propose the use of a standardised table?

Question 25: Do you consider that the standard table provided in Annex III of this Consultation Paper is fit for purpose? Do you think the standard table provides the right information, taking into account the burden on non-financial undertakings of compiling the data versus the benefit to users of receiving the data? If not, please explain and provide alternative suggestions to promote the standardisation of the disclosure obligations pursuant to Article 8 of the Taxonomy Regulation.

Question 26: Do you agree that the disclosure in the three standard tables should comply with the formatting rules mentioned in Table 5?

Question 27: Do you believe that ESMA's detailed proposals under Section 3.4 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

4 Advice relating to asset managers

4.1 Scope of this part of the advice

173. The second part of ESMA's advice relates to the second question posed to ESMA on how asset managers that report under the Non-Financial Reporting Directive should disclose how their activities are directed at funding environmentally sustainable economic activities.

174. ESMA intends to interpret the asset managers' activities for the purpose of the question to be the investments of the investment funds that they manage, as these are used to fund underlying economic activities of investee companies.

175. ESMA understands that based on the current thresholds for reporting under Article 19a and 29a of the Non-Financial Reporting Directive, which consist of entities that are public interest entities (i.e. listed companies) with an average of 500 employees or more during the financial year, very few asset managers will fall into scope outright. Some asset managers are indirectly captured as part of a subsidiary of a public interest entity, usually a bank or an insurance company, but are not included in the scope of the Non-Financial Reporting Directive as such.

176. However, in the context of the broader Non-Financial Reporting Directive review, it is possible that the thresholds for non-financial will change in the future. ESMA notes that the recent summary statement the Commission published on its public consultation on the review of the Non-Financial Reporting Directive saw significant support for expanding the scope of the Non-Financial Reporting Directive.[46] Notably, extension to large non-listed companies, or all listed companies regardless of size, could bring more asset managers into scope.

177. Therefore, in the context of the Article 8 obligation in the Taxonomy Regulation, asset managers merit a framework for reporting how and to what extent their activities are associated with economic activities that qualify as environmentally sustainable.

178. Due to the fact that few asset managers may currently report under the Non-Financial Reporting Directive and because this is a new reporting requirement, it is ESMA's understanding that reporting quantitative information is not straightforward.

[46] Ares(2020)3997889 *Summary Report of the Public Consultation on the Review of the Non-Financial Reporting Directive*, 29 July 2020.

4.2 Content of KPI

4.2.1 KPI based on investments

179. In terms of the Article 8 reporting obligation, asset managers have a relatively simple operating model of investing in assets that deliver returns for shareholders in funds. Therefore, ESMAs' starting point for the KPI is the investment process itself and the assets held in the funds of the asset manager. Share of investment in Taxonomy-aligned activities is therefore the analytical departure point for ESMA in developing a KPI for this consultation.

180. There are also alternative possibilities, for example KPIs based on revenue, or return on investment. Such a KPI could be a ratio of fees from Taxonomy-aligned investments over the total fees accrued by the asset managers. However, ESMA believes that a share of investment or assets under management ('AuM') based approach is preferable in terms of providing investors meaningful information.

181. In taking this approach ESMA also considered how it could impact the comparability across different companies, including non-financial undertakings and financial institutions. ESMA notes that, while in principle the availability of a revenue or fee income-based KPI for asset managers would seem conducive to comparability with other type of entities, in practice this may result in misleading information given that the asset management fees earned by asset managers may relate to funds which combine investments in Taxonomy-aligned assets as well as in other assets. Nevertheless, ESMA welcomes feedback on alternative models and the potential advantages or disadvantages such models may have.

182. Therefore, a simple model, would consist of requiring the disclosure in terms of a share of investments, with all Taxonomy-aligned investments in the numerator and a representation of the value of assets in the denominator. However, ESMA recognises that there are other ways to design the calculation, but believes this model would strike the right balance between meaningful comparability and the full "extent" of the asset manager's activities required to be disclosed under Article 8 of the Taxonomy Regulation.

4.2.2 Eligible investments for investment based KPI

183. Regarding the scope of the reporting for an asset manager, ESMA considers that the reporting should cover all funds managed by the asset manager, and not only those funds that have some kind of sustainability criteria. However, it is not clear how such a limitation would be possible under Article 8(1) of the Taxonomy Regulation which requires *"information on how and to what extent the undertaking's activities are associated with economic activities that qualify as environmentally sustainable…"*.

184. Turning to the "Taxonomy-aligned investments" in the numerator, ESMA would like feedback from stakeholders to refine this concept. For equity and corporate bond investments one simple option would be to consider that any investments in investee

companies reporting any Taxonomy-aligned activities should qualify as Taxonomy-aligned for the purposes of the asset management KPI, regardless of the actual extent of Taxonomy-aligned activities that such funding goes to. This could arguably be very misleading as potentially very insignificant levels of Taxonomy-aligned activities would be disclosed as high shares of investment.

185. Alternatively, there could be considerable merit in considering a "weighted average" approach to working out the weighting of the Taxonomy-aligned investments based on the description of the underlying investee companies' activities' Taxonomy-alignment, as proposed by the TEG in its final report.[47] As a brief summary, the TEG report proposes that the extent of Taxonomy-aligned investments is calculated separately for each of the environmental objectives. Furthermore, the TEG proposes different metrics to be used by investee companies' contribution depending on the environmental objective, specifically for climate change mitigation[48] and climate change adaptation[49]. However, for the purposes of deriving a proxy for equity and corporate bond exposure to Taxonomy-aligned activities, TEG proposes to use turnover only. ESMA considers this an appropriate approach but also considers that CapEx and OpEx derived disclosures could be interesting additional disclosures for asset managers.

186. In cases of specialised Taxonomy-funding tools that funds managed by asset managers invest in, namely green bonds complying with the soon to be issued EU Green Bond Standard, 100% Taxonomy-aligned activities can be financed directly and can therefore be counted fully in the numerator.

187. Turning to the denominator, a calculation based on all assets in the funds would be comprehensive and show the ratio of Taxonomy-aligned investments compared to the total investments by the asset manager. Such an approach would be the closest representation of "the extent" to which an asset manager finances Taxonomy-aligned activities. However, such a figure would include investments in asset classes such as government bonds where the contribution to activities are more difficult to estimate for Taxonomy purposes.

188. Therefore, a potential solution could be to design a set of "eligible investments" instead of taking all assets held by the funds of the asset manager as the denominator. Such "eligible investments" could consist of green bonds complying with the EU Green Bond Standard, public and private equity, real estate and corporate bond investments in investee companies. "Eligible investments" could also be limited by type of fund instead, so for example limited to products that are Article 8 or Article 9 SFDR funds that promote environmental characteristics or have an environmental objective (themselves subject to separate disclosure requirements under Articles 5 and 6 of the Taxonomy Regulation). However, limiting the denominator to only investments made by such funds would

[47] EU Technical Expert Group on Sustainable Finance, *Taxonomy: Final report of the Technical Expert Group on Sustainable Finance*, March 2020, pages 40-41.
[48] Turnover associated with Taxonomy-aligned activities and costs incurred (CapEx and if relevant OpEx) as part of a plan to achieve the climate thresholds for the economic activity
[49] For adapted activities, only costs incurred (CapEx and, if relevant, OpEx, but not turnover) when part of a plan to respond to a climate risk assessment, and for enabling activities turnover, CapEx and, if relevant OpEx can apply.

arguably reduce the denominator and could be misleading about the extent of the asset managers' Taxonomy-aligned investments.

Simplified example to illustrate eligible-AuM based KPI

An asset manager's funds hold EUR 100 million of shares and corporate bonds issued by corporate issuers and green bonds complying with the EU Green Bond Standard. This is the denominator.

Of that EUR 100 million, EUR 80 million are shares and corporate bonds from investee companies reporting under the Non-Financial Reporting Directive their Taxonomy-aligned economic activities. On a weighted average basis, those companies report 10% of their turnover contributing to Taxonomy-aligned activities. Therefore, a proxy figure for the Taxonomy-alignment of the asset managers' investments measured by turnover is EUR 8 million. Furthermore, the asset manager holds EUR 2 million of green bonds complying with the EU Green Bond Standard, which are added to the numerator, giving a total numerator of EUR 10 million.

That gives an estimate of 10% for the Taxonomy-alignment of the asset managers' investments under this proposed KPI (EUR 10 million over EUR 100 million). Subsequent disclosure fields in the proposed template in Annex IV would then report the environmental objectives and the breakdown of Taxonomy-aligned economic activities of the investee companies that the investments contribute to .

A similar calculation could be made for the CapEx and Opex disclosures. For example, if the share of CapEx contributing to Taxonomy-aligned activities was 15% and the share of OpEx was 20%, the disclosures would be 14% for CapEx (12+2 over 100) and 18% for OpEx (16+2 over 100).

4.2.3 Draft advice

189. On the basis of the considerations in Section 4.2.1, ESMA proposes the following draft advice in relation to the content of the KPIs which asset managers subject to the obligation to disclose non-financial information under the Non-Financial Reporting Directive should be required to disclose:

The KPI for asset managers should consist of a ratio of eligible investments that are Taxonomy-aligned.

The numerator should consist of the value of green bonds complying with the EU Green Bond Standard and a weighted average of the value of the investments invested in Taxonomy-aligned activities of investee companies. The weighted average should be based on the share of Taxonomy-aligned activities of the investee companies measured by turnover. Additional calculations for CapEx and OpEx may also be provided.

The denominator should consist of the value of the total eligible set of investments in investee companies held by the asset manager's funds, where eligible investments are equity and fixed income assets of eligible investee entities.

4.2.4 Questions for consultation

Asset managers - Questions relating to the content of the KPI

Question 28: Do you agree that a share of investments is an appropriate KPI for asset managers? If you do not, what other KPI could be appropriate, please justify.

Question 29: This advice focuses on the collective portfolio management activities of asset managers. Should this advice also cover potentially any other activities that asset managers may have a license for, such as individual portfolio management, investment advice, safekeeping and administration or reception and transmission of orders ('RTO')?

Question 30: Do you agree that for the numerator of the KPI the asset manager should consider a weighted average of the investments exposed to investee companies based on the share of turnover derived from Taxonomy-aligned activities of the investee companies? If not please propose and justify an alternative.

Question 31: Do you agree that in addition to a main turnover-derived Taxonomy-alignment KPI, there is merit in requiring the disclosure of CapEx and OpEx-derived figures for Taxonomy-alignment of an asset managers' investments?

Question 32: Do you think sovereign exposures, such as sovereign bonds (but excluding green bonds complying with the EU Green Bond Standard) should be considered eligible investments and if so under what methodology?

Question 33: Should the denominator consist of the value of all assets in the funds managed by the asset manager or is it better to limit the denominator to a

	set of eligible assets based on the possibility to establish their contribution to Taxonomy-aligned activities?
Question: 34:	Do you support restricting the denominator to funds managed by the asset manager with sustainability characteristics or objectives (i.e. governed by Article 8 or 9 of Regulation (EU) 2019/2088)? What are the benefits and drawbacks of such an approach?
Question 35:	Is it appropriate to combine equity and fixed income investments in the KPI, bearing in mind that these funding tools are used for different purposes by investee companies? If not, what alternative would you propose?
Question 36:	Do you believe the proposed advice will impose additional costs on asset managers? Please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

4.3 Methodology for preparing KPI

4.3.1 Considerations relating to the methodology

190. In order to work out how to calculate the proposed KPI of the share of investments that are in Taxonomy-aligned activities, several important considerations need to be explored.

191. Dealing with limited data: ESMA considers that the absence of reported data is a significant issue that needs to be addressed by the delegated act. The methodological basis of the KPI proposed by this Consultation Paper requires accurate reporting by investee companies of their Taxonomy-aligned activities. However, the EU Taxonomy has so far only been completed for two of the six environmental objectives in the Taxonomy Regulation. This means that the extent of reportable Taxonomy-aligned activities will not immediately be very extensive.

192. ESMA would like feedback about how to treat investments falling outside the scope of the Non-Financial Reporting Directive, where it is not possible to treat them as Taxonomy-aligned, for instance because they are issued by entities not reporting under the Non-Financial Reporting Directive, the extent of their activities' association with Taxonomy activities may not be known.

193. ESMA believes that the Commission could consider using a methodology allowing investments in non-reporting companies to be included in the numerator by assigning coefficients for different industries extrapolating their Taxonomy-aligned activities from a central methodology based on estimates. For example, a non-reporting issuer could be part of a sector with a "3% Taxonomy-aligned sector" according to the methodology, in

which case the asset manager would assign investments in that issuer a 3% Taxonomy-aligned activity weighting. ESMA recommends that such a methodology for climate change mitigation developed by the Commission's Joint Research Centre[50] could be used and further adapted based on the forthcoming Delegated Acts on climate change mitigation and adaptation.

194. However, there could also be merit in only considering investments in the numerator in investee companies making relevant disclosures. If investee companies do not disclose, their issuance would be considered not aligned. Although disclosures outside the NFRD are not mandatory, non-eligibility could incentivise voluntary disclosures of Taxonomy-alignment.

195. For transparency purposes, asset managers should disclose in accompanying information what share of the calculation is based on directly reported data from investee companies and what share is based on coefficient estimates.

196. Activities contributing to multiple environmental objectives: The calculation of Taxonomy-aligned investments by asset managers requires assigning investments according to environmental objectives. However, where investee companies carry out activities contributing to more than one environmental objective, the organisation of investments by environmental objective becomes a challenge. ESMA believes that as normally investee companies would assign activities to one environmental objective, as outlined above in Section 3.3.2.2. This would then address this issue, as such choices would avoid double counting and other challenges.

197. Netting: ESMA considers that the reporting should take place after netting potential hedges and offsets, regardless of the instrument used (derivatives, repurchases, short positions…), as this would mirror the commitment approach typically used to calculate net leverage for funds. A very simplified example would be a fund portfolio in a ratio of 60 Taxonomy-aligned investments and 40 non-aligned investments, so without hedging the simple KPI would be 60/100=60%. But assuming that hedges on the Taxonomy-aligned side would cover 40, this would leave a net green exposure of 20, then the KPI should be 20/(20+40)=33%.

198. In this context, the methodology for calculating net short positions in Article 3(4)-(5) of Regulation (EU) 236/2012 (the 'Short-Selling Regulation') could be useful as a reference for the netting methodology.

199. Derivatives: Aside from margins (for example arising from futures positions), derivatives do not give rise to on-balance sheet exposures. ESMA would like feedback from stakeholders regarding how to treat such off-balance sheet items that may give rise to future exposures, which some AIFs and UCITS with sophisticated strategies heavily rely on.

[50] Alessi et al., 2020

4.3.2 Draft advice

200. On the basis of the considerations in Section 4.3.1, ESMA proposes the following draft advice in relation to the methodology which asset managers subject to the requirement to disclose non-financial information under the Non-Financial Reporting Directive should use when preparing their KPIs:

> The Commission should consider the feasibility of developing a methodology to allow KPI calculation to cover also investments in companies not reporting under the Non-Financial Reporting Directive the extent of their Taxonomy-aligned activities by assigning them a coefficient derived on a sector-basis under a common methodology.
>
> The calculation should allow netting for the purposes of reporting the share of investments that are Taxonomy-aligned derived from the methodology used to calculate net short positions in the Short-Selling Regulation.
>
> The calculation should not cover derivatives.

4.3.3 Questions for consultation

Asset managers - Questions relating to the methodology for preparing the KPI

Question 37:	What are the benefits and drawbacks of limiting Taxonomy-aligned activities to those reported by Non-Financial Reporting Directive companies?
Question 38:	Do you agree with ESMA's recommendation that the Commission develop a methodology to allow a sector-coefficient to be assigned for non-reporting investee companies?
Question 39:	Should netting be allowed, on the lines of Article 3 of the Short-Selling Regulation?
Question 40:	How should derivatives be treated for the calculation purposes? Should futures be considered as potential Taxonomy-aligned investments?
Question 41:	What are the costs and benefits associated with the different options for non-reported activity coverage, netting and derivatives treatment presented above? Please provide a quantitative estimate for each option, distinguishing between one-off and on-going costs.

4.4 Presentation of KPI

4.4.1 Standard table and accompanying information

201. ESMA believes that comparability of the disclosures is important in order to achieve meaningful disclosures under Article 8. For this reason, asset managers should include in the presentation of their disclosures the environmental objectives to which the investments contribute. In order to aid comparability and to increase transparency, ESMA believes it would also be helpful to identify the economic activities invested in contributing to the environmental objectives. The economic activities should be further divided into ‘transitional’ and ‘enabling’ activities.

202. ESMA proposes in line with the advice on non-financial undertakings to prepare a standard table presentation format to display the Taxonomy-alignment of the investments, the environmental objectives they contribute to broken down by economic activities. This table is presented for consultation in Annex IV below.

203. Accompanying information should explain any assumptions in the calculations and if relevant any additional breakdowns of investments.

204. In line with the advice on non-financial undertakings, ESMA suggests that accompanying information should be placed in the immediate vicinity of the KPI presentation, as this will make the information most helpful for investors and other users. However, to avoid undue burden on non-financial undertakings and to ensure that the KPIs and the accompanying information become an integrated part of the non-financial statement, ESMA recommends that the Commission permit compliance by reference. This would entail that where non-financial undertakings prefer to disclose some or all of the accompanying information in a different part of the non-financial statement, they should be permitted to do so on the condition that they provide a cross-reference in the form of a direct hyperlink to this other part of the non-financial statement, so that users can access the relevant information with one click

205. Furthermore, due to the similar nature of the reporting on principal adverse impacts of investment decisions on sustainability factors under Article 4 of the SFDR, where an asset manager makes such disclosures, there may be merit in including a reference to those disclosures in the accompanying information, so that it is easy to locate such disclosures.

206. In terms of formatting, ESMA believes that there is merit in adopting the same standardised formatting rules as presented in the advice for non-financial undertakings in Section 3.4.2 above.

4.4.2 Draft advice

207. On the basis of the considerations in Section 4.4.1, ESMA proposes the following draft advice in relation to the presentation of KPIs by asset managers subject to the

requirement to disclose non-financial information under the Non-Financial Reporting Directive:

The presentation of the KPI should follow a template style set out in Annex IV The presentation of the disclosure should identify which environmental objectives the investments contribute to and where possible the activities invested in should be identified for each environmental objective. The presentation of a standard table should also have appropriate accompanying information presented in the vicinity of the standard table, including a link, if relevant, to disclosures on the principal adverse impacts of investment decisions on sustainability factors under Article 4 of the SFDR.

4.4.3 Questions for consultation

Asset managers - Questions relating to the presentation of the KPI

Question 42: Do you have any views on the proposed advice recommending a standardised table for presentation of the KPI for asset managers in Annex IV?

Question 43: Do you agree with presenting accompanying information in the vicinity of the standard table?

Question 44: Do you agree that there would be merit in including in the accompanying information a link, if relevant, to an asset managers' entity-level disclosures on principal adverse impacts of investment decisions on sustainability factors?

Question 45: Do you agree with adopting the same formatting criteria as presented in Section 3.4.2 for the asset manager KPI disclosure?

Question 46: What are the one-off and on-going costs of setting up the reporting and disclosure under this obligation? Please clarify the type of costs incurred and provide a quantitative estimation where possible.

Annex I: Call for advice from the European Commission

CALL FOR ADVICE TO THE EUROPEAN SUPERVISORY AUTHORITIES ON KEY PERFORMANCE INDICATORS AND METHODOLOGY ON THE DISCLOSURE OF HOW AND TO WHAT EXTENT THE ACTIVITIES OF UNDERTAKINGS UNDER THE NFRD QUALIFY AS ENVIRONMENTALLY SUSTAINABLE AS PER THE EU TAXONOMY

With this Call for Advice, the European Commission invites the European Supervisory Authorities (ESAs) to develop advice determining key performance indicators (KPIs) and associated methodology that undertakings subject to the Non-Financial Reporting Directive (NFRD)[1] should use to disclose information on how and to what extent their activities are aligned with those that qualify as environmentally sustainable under the EU taxonomy, in line with Article 8 of the Taxonomy Regulation[2]. In order to achieve this, the ESAs should investigate with the relevant stakeholders appropriate metrics and data analysing the impacts these might have on undertakings, including in terms of costs. The content of the advice should be adequate to form the basis for an impact assessment for a delegated act based on the Taxonomy Regulation that the Commission will adopt by June 2021.

The request is made in accordance with the founding Regulations establishing the ESAs[3], which establish the obligation to protect the public interest by contributing to the short, medium and long-term stability and effectiveness of the financial system, including through ensuring the integrity, transparency, efficiency and orderly functioning of financial markets.

The advice should be based on qualitative and, when feasible, quantitative sources. The evidence discussed in the advice should be based on data samples from public and commercial databases, data submitted to the ESAs by the supervised entities and qualitative sources of information, which might include a review of the most relevant literature, where available. It may also include, but should not be limited to, concrete examples or case studies, based on the experience of the ESAs in their supervisory capacity.

The need for this request and the scope of the work have been agreed between Commission staff and the ESAs. Commission staff kindly request the delivery of the final advice by February 2021. The Commission, in close cooperation with the ESAs, may revise and/or supplement this request and revise the timetable accordingly.

The European Parliament and the Council will be informed about this request, which will be available on the website of the Directorate-General for Financial Stability, Financial Services and Capital Markets Union once it has been transmitted to the European Supervisory Authorities.

[1] 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, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC, OJ L 182, 29.06.2013, page 19, as subsequently amended.

[2] Regulation (EU) 2020/852 of the European Parliament and of the Council of 18 June 2020 on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088, OJ L 198, 22.06.2020, page 13.

[3] Regulations (EU) No 1093/2010, 1094/2010, 1095/2010 and 2019/2175 of the European Parliament and of the Council.

1. CONTEXT

By June 2021, the Commission will complement the recently adopted Taxonomy Regulation with a delegated act setting forth requirements for undertakings subject to the NFRD (i.e., large listed undertakings, large banks and large insurance undertakings with more than 500 employees). Such requirements will specify the content and presentation of information on how and to what extent their activities are associated with the EU taxonomy, including the methodology to be used. The delegated act should take into account the specificities of both financial and non-financial undertakings subject to the NFRD.

Article 8 of the Taxonomy Regulation states that non-financial undertakings under the NFRD shall disclose the proportion of their turnover, capital expenditures (CapEx) and operating expenditure (OpEx) associated with environmentally sustainable economic activities, as per the EU taxonomy. Article 8 does not specify equivalent indicators on taxonomy-alignment for financial undertakings under the NFRD (i.e., mainly large banks and large insurance undertakings), leaving this task to the delegated act.

The Commission's guidelines on reporting climate-related information[4] provide a useful starting point, since in their annexes they identify KPIs that both banks and insurance companies could use to report sustainability-related data. However, the scope of KPIs to be developed under Article 8 has to be narrower, since it needs to focus solely on taxonomy-alignment. For example, the following KPIs based on the guidelines have been modified to refer to the EU taxonomy, and could be considered by the ESAs as a starting point for their analysis.

For banks:

- Proportion of total assets invested in taxonomy-compliant economic activities.

For insurance and reinsurance undertakings:

- Proportion of total assets invested in taxonomy-compliant economic activities.
- Proportion of total non-life insurance underwriting exposure associated with taxonomy activities.
- Proportion of total reinsurance underwriting exposure associated with taxonomy activities.

The Commission invites the ESAs to consider whether to further refine these indicators for financial undertakings, for example to exclude certain assets from the calculations (e.g., derivatives, trading book exposures, central bank reserves, for banks) and to assess the need of having different indicators for taxonomy-compliant financial services (e.g. climate risk insurance as a proportion of total insurance underwriting activities/gross written premiums) and for investments into taxonomy-compliant economic activities. The ESAs should also analyse whether all existing activities should be covered retroactively or only those relevant to the time period as of the when the disclosure rules start to apply[5]. Some activity-level

[4] Communication from the Commission — Guidelines on non-financial reporting: Supplement on reporting climate-related information OJ C 209, 20.6.2019

[5] The disclosures under Article 8 apply as of 1 January 2022 for the environmental objectives of climate change mitigation and adaptation, and as of 1 January 2023 for the other four. The obligations relate to the previous financial year respectively (the disclosure obligation for 1 January 2022 covers the financial year 2021, the disclosure obligation for 1 January 2023 covers the financial year 2022).

information on taxonomy-alignment may also be hard to come by, suggesting the need to think of possible proxy-indicators.

2. SCOPE OF THE EXERCISE

The Commission invites ESMA, EBA and EIOPA to investigate and determine the content and presentation of relevant KPIs and associated methodology that should be used by different financial undertakings under their remit, in order for such undertakings to disclose their degree of taxonomy-compliance under Article 8 of the Taxonomy Regulation. Further, the ESAs are asked to consider how the three indicators for non-financial undertakings in Article 8(2) of the Taxonomy Regulation could be further specified and to determine appropriate methodologies.

In developing their advice, the ESAs are also invited to take into account that clarity is needed on how undertakings ought to determine whether their investments are associated with economic activities considered environmentally sustainable under the EU taxonomy. Namely, as set out in Article 8 and as proposed by the Technical Expert Group (TEG), whose recommendations constitute the basis for the Commission's draft delegated act on technical screening criteria for selecting economic activities to qualify as environmentally sustainable, both turnover resulting from an undertaking's investment and capital/operational expenditure constituting the investment itself should count[6]. However, the conditions can vary for different types of investments and environmentally sustainable activities. In this respect, the TEG proposed that eligible taxonomy-aligned turnover should vary depending on the environmental objective that the economic activity from which the turnover is derived contributes to, as set out in the table below, whereas for capital expenditures and operational expenditures it should not.

Financial metric	Climate change mitigation	Climate change adaptation
Turnover	Can be counted where economic activity meets Taxonomy technical screening criteria for substantial contribution to climate change mitigation and relevant DNSH criteria.	Turnover can be recognised only for activities enabling adaptation. Turnover cannot be recognised for adapted activities at this stage[7].
CapEx/OpEx	Can be counted where costs incurred (capex and, if relevant, opex) are part of a plan to meet Taxonomy technical screening criteria for substantial contribution to climate change mitigation and relevant DNSH criteria.	Can be counted where costs incurred (capex and, if relevant, opex) are part of a plan to meet Taxonomy technical screening criteria for substantial contribution to climate change adaptation and relevant DNSH criteria.

[6] Turnover reflects where a company currently is relative to the taxonomy and can be used by investors as a proxy for assessing how green a company is for equity exposures. Expenditures, in contrast, give investors a good sense of a company's direction of travel and is a key variable for investors assessing the credibility of a company's strategy in terms of improving its environmental performance.

[7] Allowing for turnover from adapted activities to count could be misleading: once the "substantial contribution" to adaptation of an activity is made (i.e. it is made resilient to climate change), it is questionable if the turnover associated with that activity (which may or may not have environmental benefits) should count as sustainable.

The issue of "what counts" matters for accurate disclosures of taxonomy-alignment throughout the investment chain: for undertakings carrying out sustainable economic activities under their disclosure obligation under Article 8, for financial market participants offering their services in relation to financial products under their disclosure obligations under Articles 5-7 of the Taxonomy Regulation[8] and for end-investors themselves. Consistency and clarity will help prevent different interpretations of what can count as 'taxonomy-aligned', minimise the risk of greenwashing, and consolidate the overall usability and appeal of the EU taxonomy. In this respect, the ESAs are invited to ensure consistency in the advice requested here and in the draft technical standards under Articles 8(4), 9(6) and 11(5) of Regulation (EU) 2019/2088.

In gathering evidence, qualitative sources and relevant literature should be complemented, where feasible, by quantitative evidence, such as data from public and commercial databases. We also expect the ESAs to engage with the most relevant stakeholders by means of an already planned or *ad hoc* stakeholder interaction or consultation, in order to develop the requested advice.

The three ESAs are asked to consider the following questions. In developing their advice, all ESAs are invited to provide data or estimates on the expected impacts, including costs, of the proposed disclosures and methodologies for relevant stakeholders.

EBA:

1. What information should banks and investment firms subject to the NFRD disclose (e.g. as part of their prudential and broader ESG disclosures) on how their financial or broader commercial activities align with economic activities identified as environmentally sustainable in the EU taxonomy, whether carried out in-house or performed by third parties? Which financial or commercial activities should be included/excluded?

2. If turnover, OpEx and CapEx were not considered appropriate, what alternative indicators would achieve the same purpose? What KPIs are best suited to disclose information identified in (1) above? What should constitute the numerator and the denominator for a specific KPI for banks and investment firms?

3. Could the green asset ratio be adapted to include taxonomy-related disclosures?

EIOPA:

1. What information should (re)insurance companies subject to the NFRD disclose (e.g. as part of their prudential and broader ESG disclosures) on how their insurance activities correspond to those identified as environmentally sustainable in the EU taxonomy? Should there be a difference between insurers and reinsurers, and between insurance and reinsurance activities?

2. Should they disclose how financial or commercial activities beyond insurance underwriting are directed at funding economic activities identified as environmentally sustainable in the EU taxonomy? If yes, what information should they disclose? Are turnover, CapEx and OpEx appropriate?

3. What should be included in (2)? Could something be excluded and if yes, what types of activities? What should constitute the numerator and the denominator of a possible specific KPI for (re)insurers?

[8] For which ESAs are preparing draft technical standards.

ESMA:

1. What information should any asset management companies subject to the NFRD, notably alternative investment fund managers or UCITS management companies, disclose on how their activities are directed at funding economic activities identified as environmentally sustainable in the EU taxonomy?

2. How should the three KPIs that non-financial undertakings are required to disclose under Article 8(2) of the Taxonomy Regulation be further specified? More specifically:

- Should non-financial undertakings make any further disclosures to accompany the KPIs?
- Should it be specified which KPI/(s) is/are relevant for companies in a given sector?
- What methodology should non-financial undertakings use to report against the identified indicators (allocating turnover/expenditures within the undertaking or group to different economic activities; distinguishing between activities not covered by the taxonomy and activities covered by the taxonomy, but where the undertaking doesn't meet the thresholds/technical screening criteria)?

3. PRINCIPLES

The subject matter of this call for advice is highly focused. It is circumscribed by the requirement of Article 8 to further specify details of the information to be disclosed, and accompanying methodology, for undertakings in relation to the taxonomy. The legal requirement to adopt the delegated act is June 2021. Consequently, the ESAs are invited to consider the task as a targeted one. This may involve shortening some internal deadlines and procedures, e.g. on consultations.

The development of the advice should be based on the following principles:

- **Autonomy:** The ESAs are free to choose working arrangements which they consider most efficient to reach the objectives described in this request, in line with better regulation principles. In particular, the ESAs are invited to utilise existing consultation channels and working formations e.g. on prudential disclosures, to derive the input.
- **Reliable qualitative and quantitative data** should be considered to assess the merits of all recommendations. The advice should aim to build on diverse, but unbiased sources.
- **Justified solution:** the KPIs the ESAs will include in the advice will need to be assessed in terms of their possible impacts while possible trade-offs with other EU objectives should also be considered. As appropriate, the ESAs should consider and justify choices e.g. regarding the need for information which is disclosed to be accurate, useful, usable, and cost-efficient.
- **Cooperation between the ESAs:** The ESAs are free to choose an arrangement for their cooperation, which they consider most efficient to reach the objectives described in this request. While work on questions specific to undertakings in their remit can proceed independently, ESMA, EBA and EIOPA are invited to closely coordinate their work on the advice to ensure consistent and coherent recommendations. The advice can be delivered in the shape of three separate reports by each ESA.
- **Cooperation with other EU bodies:** The ESAs are invited to cooperate with other EU bodies as relevant. Notably, ESAs are encouraged to liaise with the European Financial Reporting Advisory Group (EFRAG), which has been mandated to carry out preparatory

work for possible EU non-financial reporting standards, as well as the Commission's Joint Research Centre.

- **Absence of conflict of interest:** The ESAs shall ensure a transparent and balanced engagement with stakeholders and require, as appropriate, disclosure of sources and avoidance of conflict of interest in the conduct of the discussions and in the development of their advice. Cases involving potential conflict of interest will be duly noted.

4. STEPS AND TENTATIVE TIMETABLE

The advice is expected by February 2021.

The ESAs can choose the best way to approach the exercise in line with the scope and principles defined above. Below a suggested tentative timeline.

Step 1	Formal request sent	September 2020
Step 2	Collecting evidence and stakeholders views and drafting the advice	September 2020 – February 2021
Step 3	Interim drafts and preliminary findings, including KPIs and associated methodology, discussed with the Commission	Continuous
Step 4	Advice finalised	February 2021

Annex II: List of questions for consultation

Advice relating to non-financial undertakings

Definitions – questions related to the KPI 'proportion of turnover derived from products / services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'

Question 1: For this KPI, do you agree with the proposed approach to <u>defining</u> turnover (bullet a in the draft advice)?

Question 2: For this KPI, do you agree with the proposed approach to when turnover <u>can be counted</u> (bullet b in the draft advice)?

Definitions – questions related to the KPI 'proportion of capital expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'

Question 3: For this KPI, do you agree with the proposed approach to <u>defining</u> CapEx (bullet a in the draft advice)?

Question 4: For this KPI, do you agree with the proposed approach to when CapEx <u>can be counted, including the definition of 'plan'</u> (bullet b in the draft advice)?

Definitions – questions related to the KPI 'proportion of operating expenditure related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation'

Question 5: For this KPI, do you agree with the proposed approach to <u>defining</u> OpEx (bullet a in the draft advice)?

Question 6: For this KPI, do you agree with the proposed approach to when OpEx <u>can be counted</u>, including the definition of 'plan' (bullet b in the draft advice)? With reference to the TEG's inclusion of the words "if relevant" in relation to OpEx, in which situations should it be possible to count OpEx as Taxonomy-aligned?

Definitions – questions related to all three KPIs

Question 7: Do you believe that any of the suggested approaches covered in questions 1 to 6 above will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or ongoing, and provide your best quantitative estimate of their size.

Question 8:	Do you agree that sectoral specificities should not be addressed in the advice, as proposed in Section 3.2.3?
Accompanying information – questions related to all three KPIs	
Question 9:	Do you agree with the requirements for accompanying information which ESMA has proposed for the three KPIs?
Question 10:	Do you consider that the requirement to refer to the relevant line item(s) in the financial statements for each KPI ensures sufficient integration between the KPIs and the financial statements?
Question 11:	Do you agree with ESMA's suggestion to permit compliance by reference, so that non-financial undertakings may present the accompanying information elsewhere in the non-financial statement than in the immediate vicinity of the KPIs, as long as they provide a hyperlink to the location of the accompanying information?
Question 12:	Do you consider there are additional topics that should be considered by ESMA in order to specify the content of the three KPIs? If yes, please elaborate and explain the relevance of these topics.
Question 13:	Do you believe that providing the suggested accompanying information will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, including whether they are one-off or on-going, and provide your best quantitative estimate of their size.
Questions relating to the methodology of preparing KPIs	
Question 14:	Do you agree that non-financial undertakings should provide the three KPIs <u>per economic activity</u> and also provide a total of the three KPIs at the level of the undertaking / group? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.
Question 15:	Do you agree that where an economic activity contributes to more than one environmental objective, non-financial undertakings should explain how they allocated the turnover / CapEx / OpEx of that activity <u>across environmental objectives</u> and where relevant the reasons for choosing one objective over another?
Question 16:	Do you agree that non-financial undertakings should provide information on enabling and transitional activities?
Question 17:	Do you agree that the three KPIs should be provided <u>per environmental objective</u> as well as <u>a total at undertaking or group level across all</u>

objectives? If not, please provide your reasons and address the impact of your proposal to financial market participants along the investment chain.

Question 18: Do you agree that non-financial undertakings should be required to provide the three KPIs for economic activities which are covered by the Taxonomy, economic activities which are covered by the Taxonomy but for which the relevant criteria are not met and therefore are not Taxonomy-aligned as well as for economic activities which are not covered by the Taxonomy?

Question 19: Do you agree with the proposal not to require retroactive disclosure concerning the four environmental objectives relating to the financial year 2021?

Question 20: Do you consider that there are specific elements in ESMA's draft advice which are not in line with the information needed by financial market participants in order to comply with their own obligations under the Taxonomy Regulation and the SFDR? If yes, please specify in your answer.

Question 21: Are there points that should be addressed in ESMA's advice in order to facilitate compliance of financial market participants across the investment chain? If yes, please specify.

Question 22 Do you believe that ESMA's detailed proposals under Section 3.3 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

Question 23: Do you consider there are additional topics that should be considered by ESMA in order to specify the methodology that non-financial undertakings should follow? If yes, please elaborate and explain the relevance of these topics.

Questions relating to the presentation of KPIs

Question 24: Do you agree that in order to ensure the comparability of the information disclosed under Article 8(2) of the Taxonomy Regulation and as such facilitate its usage, ESMA should propose the use of a standardised table?

Question 25: Do you consider that the standard table provided in Annex III of this Consultation Paper is fit for purpose? Do you think the standard table provides the right information, taking into account the burden on non-financial undertakings of compiling the data versus the benefit to users of receiving the data? If not, please explain and provide alternative suggestions to promote the standardisation of the disclosure obligations pursuant to Article 8 of the Taxonomy Regulation.

Question 26: Do you agree that the disclosure in the three standard tables should comply with the formatting rules mentioned in Table 5?

Question 27: Do you believe that ESMA's detailed proposals under Section 3.4 will impose additional costs on non-financial undertakings? If yes, please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.

Advice relating to asset managers

Asset managers - Questions relating to the content of the KPI

Question 28: Do you agree that a share of investments is an appropriate KPI for asset managers? If you do not, what other KPI could be appropriate, please justify.

Question 29: This advice focuses on the collective portfolio management activities of asset managers. Should this advice also cover potentially any other activities that asset managers may have a license for, such as individual portfolio management, investment advice, safekeeping and administration or reception and transmission of orders ('RTO')?

Question 30: Do you agree that for the numerator of the KPI the asset manager should consider a weighted average of the investments exposed to investee companies based on the share of turnover derived from Taxonomy-aligned activities of the investee companies? If not please propose and justify an alternative.

Question 31: Do you agree that in addition to a main turnover-derived Taxonomy-alignment KPI, there is merit in requiring the disclosure of CapEx and OpEx-derived figures for Taxonomy-alignment of an asset managers' investments?

Question 32: Do you think sovereign exposures, such as sovereign bonds (but excluding green bonds complying with the EU Green Bond Standard) should be considered eligible investments and if so under what methodology?

Question 33: Do you agree that the denominator should consist of the value of eligible investments in the funds managed by the asset manager or should it be simply the value of all assets in the funds managed by the asset manager?

Question: 34: Do you support restricting the denominator to funds managed by the asset manager with sustainability characteristics or objectives (i.e. governed by Article 8 or 9 of Regulation (EU) 2019/2088)? What are the benefits and drawbacks of such an approach?

Question 35:	Is it appropriate to combine equity and fixed income investments in the KPI, bearing in mind that these funding tools are used for different purposes by investee companies? If not, what alternative would you propose?
Question 36:	Do you believe the proposed advice will impose additional costs on asset managers? Please specify the type of those costs, to which specific proposal they relate including whether they are one-off or on-going, and provide your best quantitative estimate of their size.
Asset managers - Questions relating to the methodology for preparing the KPI	
Question 37:	What are the benefits and drawbacks of limiting Taxonomy-aligned activities to those reported by Non-Financial Reporting Directive companies?
Question 38:	Do you agree with ESMA's recommendation that the Commission develop a methodology to allow a sector-coefficient to be assigned for non-reporting investee companies?
Question 39:	Should netting be allowed, on the lines of Article 3 of the Short-Selling Regulation?
Question 40:	How should derivatives be treated for the calculation purposes? Should futures be considered as potential Taxonomy-aligned investments?
Question 41:	What are the costs and benefits associated with the different options for non-reported activity coverage, netting and derivatives treatment presented above? Please provide a quantitative estimate for each option, distinguishing between one-off and on-going costs.
Asset managers - Questions relating to the presentation of the KPI	
Question 42:	Do you have any views on the proposed advice recommending a standardised table for presentation of the KPI for asset managers in Annex IV?
Question 43:	Do you agree with presenting accompanying information in the vicinity of the standard table?
Question 44:	Do you agree that there would be merit in including in the accompanying information a link, if relevant, to an asset managers' entity-level disclosures on principal adverse impacts of investment decisions on sustainability factors?
Question 45:	Do you agree with adopting the same formatting criteria as presented in Section 3.4.2 for the asset manager KPI disclosure?

Question 46:	What are the one-off and on-going costs of setting up the reporting and disclosure under this obligation? Please clarify the type of costs incurred and provide a quantitative estimation where possible.

Annex III: Standard table for the disclosure required under Article 8 of the Taxonomy Regulation (non-financial undertakings)

Proportion of turnover from products or services associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation^ - disclosure covering year N

Economic activities	**Absolute turnover** Currency	**Proportion of turnover** Percent	**Covered by Taxonomy?** Yes / No	**Covered by Taxonomy but do not meet TSC** Yes / No	**NACE code**	**Climate change mitigation** SC √ / X DNSH √ / X	**Climate change adaptation** SC √ / X DNSH √ / X	**Water and marine resources** SC √ / X DNSH √ / X	**Circular economy** SC √ / X DNSH √ / X	**Pollution** SC √ / X DNSH √ / X	**Biodiversity and ecosystems** SC √ / X DNSH √ / X	**Minimum safeguards** √ / X	**Taxonomy-aligned proportion of turnover, year N** Percent	**Taxonomy-aligned proportion of turnover, year N-1** Percent	**Category (enabling activity / transitional activity)**
Activity A		20%	Yes	No		SC √ 50% SC X 50% ^^	DNSH √	DNSH √	DNSH √	DNSH √	DNSH √	√	10%		
Activity B		11%	Yes	No		DNSH √	DNSH √	100% √	DNSH √	DNSH √	DNSH √	√	11%		
Activity C		20%	No	N/A		-	-	-	-	-	-	-	-		-
Activity D		18%	Yes	Yes		DNSH √	DNSH √	SC X	DNSH √	DNSH √	DNSH √	√	0%		

Activity E		30%	Yes	Yes		DNSH √	DNSH √	DNSH √	SC √	DNSH X	DNSH √	√	0%		
Miscellaneous^^^		1%	Yes	Yes		SC X	DNSH √	DNSH X	DNSH X	DNSH √	DNSH √	X	0%		
Total		**100%**											**21%**		
% of revenue from all economic activities per environmental objective						10%		11%							

^ ESMA notes that the above template is an example which should be adapted for the presentation of information related to the other two KPIs required under Article 8(2) of the Taxonomy Regulation, namely ‘proportion of CapEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation’ and ‘proportion of OpEx related to assets / processes associated with economic activities that qualify as environmentally sustainable under Articles 3 and 9 of the Taxonomy Regulation’.

^^ The information in this cell denotes that only 50% of activity A qualifies as environmentally sustainable and therefore only 50% of the turnover related with activity A is Taxonomy-aligned.

^^^ In this row, the undertaking may group activities which taken together constitute a small proportion of the undertaking’s turnover. The narrative disclosure accompanying this table should provide additional explanations on these activities in line with the requirements set out in Section 3.2.2.

<u>Explanation of acronyms and symbols used in standard table</u>:

TSC: Technical screening criteria, SC: Substantially contributes, DNSH: Does not significantly harm, MSF: Minimum safeguards.

√: The activity meets the criteria / X: the activity does not meet the criteria.

Annex IV: Standard table for the disclosure required under Article 8 of the Taxonomy Regulation (asset managers)

Overall Taxonomy-alignment of investments: X%		**Value breakdown**: disclose figures for numerator (net value of Taxonomy-aligned investments) and denominator (net value of eligible investments)
Taxonomy-alignment of investments measured by CapEx contribution to Taxonomy-aligned activities of investee companies: Y%		Taxonomy-alignment of investments measured by OpEx contribution to Taxonomy-aligned activities of investee companies: Z%
Breakdown of X by environmental objective and by economic activity invested in		
(1) Climate change mitigation	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D %, etc.
(2) Climate change adaptation	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D %, etc.
(3) The sustainable use and protection of water and marine resources	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D %, etc.
(4) The transition to a circular economy	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D %, etc.

(5) Pollution prevention and control	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D %, etc.
(6) The protection and restoration of biodiversity and ecosystems	%	Transitional activities: Activity A: %, Activity B %, etc. Enabling activities: Activity C: %, Activity D: %, etc.

Annex V: Estimates for the three KPIs for the EU economy as a whole and by NACE macro sector

Non-financial undertakings

1. Introduction

The TEG report (2020) identifies Taxonomy-covered sectors and their associated NACE codes[51]. However, this information is not granular enough to measure environmentally sustainable activities as within most sectors, only a few selected activities are Taxonomy-eligible. For example, activities within 'Production of electricity' (NACE D.35.1.1) that are Taxonomy-eligible concern mainly the production of electricity from renewable energies (e.g. solar power or wind power) while any production of electricity from other sources is excluded.[52]

Moreover, companies (especially large ones) tend to engage in more than one economic activity, making any company-wide sectorial classification imperfect for the purpose of measuring economic alignment with the Taxonomy.

Nonetheless, top-down market estimates can be useful for the purpose of measuring the alignment of an investment portfolio with the Taxonomy, or to monitor the share of environmentally sustainable activities in the EU.

The analysis below provides such top-down estimates for the three KPIs discussed in the draft advice for the EU economy as a whole and by NACE macro sector, based on a methodology developed by the EC Joint Research Centre (JRC) report on the EU Taxonomy.[53]

All calculations and figures in the analysis rely on assumptions and are therefore for illustration purposes only. These do not consider minimum social safeguards and therefore represent a potential upper-bound in terms of Taxonomy-aligned KPIs. As data coverage and quality improve, they are subject to future revisions.

2. Methodology

The methodology relies on three main steps:

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[51] NACE is the statistical classification of economic activities in the European Community. For more details see: https://ec.europa.eu/eurostat/documents/3859598/5902521/KS-RA-07-015-EN.PDF

[52] For a full list of Taxonomy-eligible activities by NACE sector, see TEG (2020), *Taxonomy: Final report,* Section 5.1.

[53] Alessi, L., Battiston, S., Melo, A. S. and Roncoroni, A., *The EU Sustainability Taxonomy: a Financial Impact Assessment*, EUR 29970 EN, Publications Office of the European Union, Luxembourg, 2019, ISBN 978-92-76-12991-2, doi:10.2760/347810, JRC118663.

a. **Identification of Taxonomy-covered sectors**: based on the TEG report (2020) using 4-digit NACE codes (also available in Excel format on the European Commission website).

b. **Grouping of Taxonomy-covered sectors into Climate-Policy Relevant Sectors (CPRS)**, following the methodology developed by Battiston et al. (2017)[54]; see Table 2 in Annex.

c. **Application of JRC-estimated coefficients by CPRS**, available in the JRC report (p.32-33), which aim to estimate the share of Taxonomy-eligible activities by sector; see Tables 3 and 4 in Annex[55].

The use of coefficients arises from the insufficient granularity of the data available. These coefficients set a useful bar that can be used to estimate the extent to which a given sector or industry contributes to the transition to a low-carbon economy. To compute these coefficients, the JRC relies on the EU Emissions Trading System benchmarks, based on CO2 emissions (following the TEG approach), or on the criteria set out in the 2019 TEG report.

Following this procedure, we estimate the share of Taxonomy-eligible Turnover, CapEx and OpEx in the EU non-financial sector.

3. Data

The ISINs of all companies listed in the EEA are obtained from ESMA's MiFID II Financial Instruments Reference Data System (FIRDS).[56] Company data on turnover (i.e. revenue), operational expenditure, capital expenditure, number of employees, balance sheet (i.e. total liabilities), 4-digit NACE codes and exchanges rates are from Refinitiv Eikon and Datastream.

Using NACE codes and issuer country of incorporation, the sample is restricted to EU-27 non-financial undertakings. In line with NFRD scope, the sample further excludes companies with fewer than 500 employees, annual turnover below €40 million, or balance sheet under €20 million. Finally, the following data-treatment steps are applied:

– Exclusion of invalid or null entries
– Removal of duplicate entries (i.e. multiple ISINs per issuer)
– Exclusion of companies with reporting older than 2017[57]
– Conversion of Turnover, OpEx and CapEx data to euros.[58]

[54] Battiston, S., Mandel, A., Monasterolo, I., Schütze, F., & Visentin, G. (2017), *A climate stress-test of the financial system*. Nature Climate Change, 7(4), 283.
[55] The CPRS classification preceded the TEG report, therefore not all Taxonomy-covered sectors are included in the CPRS.
[56] FIRDS covers all issuers with financial instruments available for trading in the EEA. See https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_firds
[57] For the vast majority of companies within the sample, the fiscal year of reference is 2019. Companies with no data reported since 2017 were either assumed to have been delisted or to have gone bankrupt.
[58] Since Turnover, OpEx and CapEx are reported on an annual basis, annual average exchange rates were used.

The final sample of EU-27 non-financial undertakings within NFRD scope includes 1,441 companies.[59] The EU-wide aggregate Turnover, OpEx and CapEx for the sample is as follows:

Table 1: Total Turnover, OpEx and CapEx of EU-27 non-financial undertakings in NFRD scope (million euro)

Turnover	OpEx	CapEx
6,744,988	6,188,592	453,938

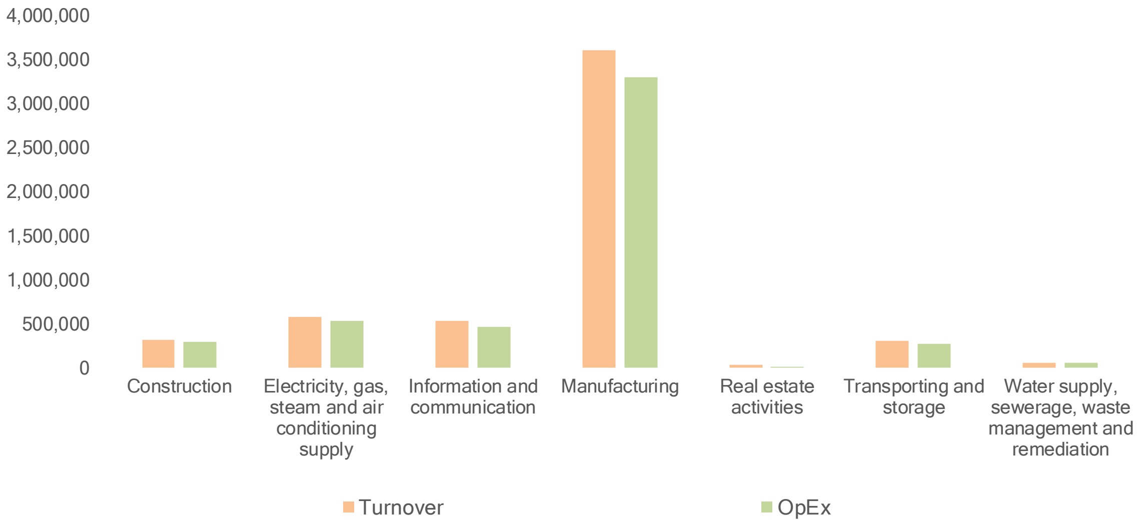
Source: FIRDS, Refinitiv Eikon, ESMA.

Turnover and OpEx data display a very high degree of correlation (99.8%) so the corresponding KPIs can generally be expected to be similar.

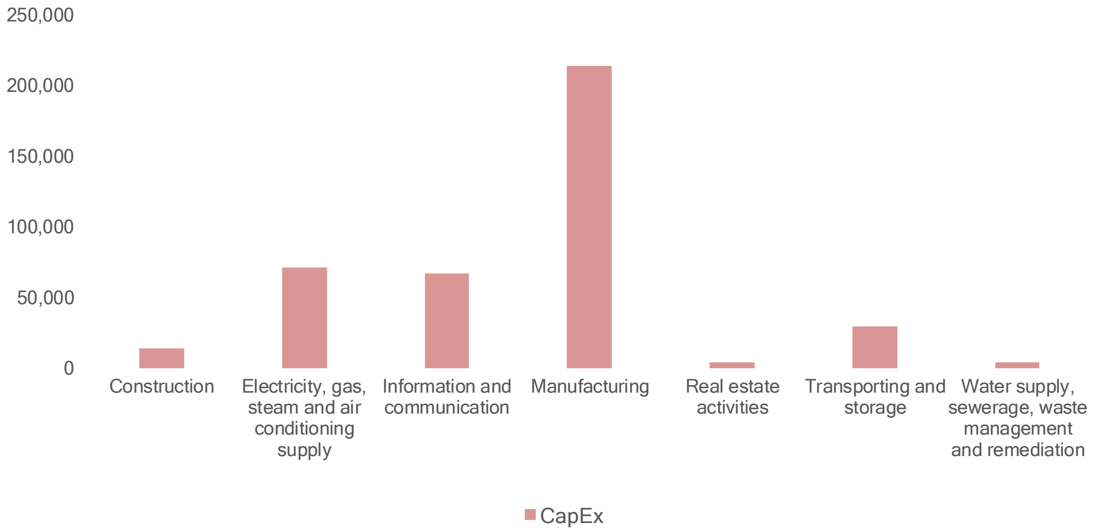
There are 21 NACE Macro-sectors in total but only seven of these include sectors that are covered in the EU Taxonomy. The share of Turnover, OpEx and CapEx of Taxonomy-relevant NACE Macro-sectors correspond respectively to 81% (Turnover), 80% (OpEx) and 89% (CapEx) of the total NFRD sample. A breakdown by relevant NACE Macro-sector is displayed below in Charts 1 and 2.

[59] The sample includes equity issuers only and excludes EU-27 companies not listed.

Charts 1 and 2: Total Turnover, OpEx and CapEx of EU-27 non-financial undertakings in NFRD scope by Taxonomy-relevant NACE-macro sector (million euro)



Note:Turnover and OpEx of EU-non financial undertakings in NFRD scope, in million euro, by NACE Macro-sector (relevant sectors only).
Sources: FIRDS, Refintiiv Eikon, ESMA



Note:CapEx of EU-non financial undertakings in NFRD scope, in million euro. by selected NACE Macro-sector (relevant sectors only).
Sources: FIRDS, Refintiiv Eikon, ESMA

4. Main findings

After applying the procedure described above, estimates of Taxonomy-aligned KPIs are obtained by sector, and subsequently grouped into NACE Macro-sectors (Table 2).

An estimated €167 billion in turnover from EU-27 non-financial undertakings is aligned with the Taxonomy, i.e. around 2.5% of the total turnover of companies reporting under NFRD. The corresponding figures for OpEx and CapEx are €151 billion (2.4%) and €14 billion (3.1%).

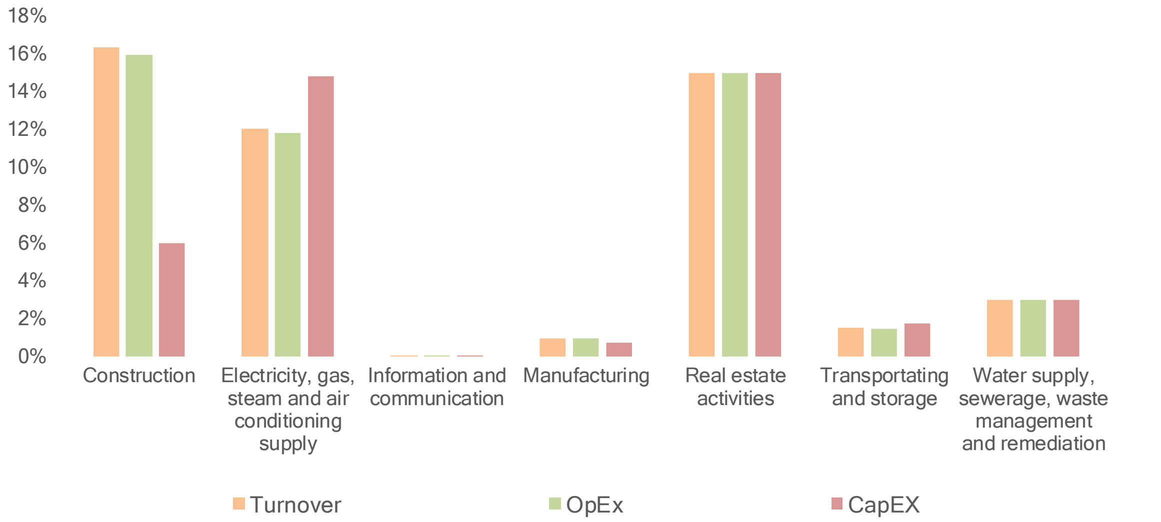
Table 2: Estimated Taxonomy-aligned Turnover, OpEx and CapEx of EU-27 non-financial undertakings in NFRD scope, by NACE Macro-sector (million euro)

NACE Macro-sector	Turnover	OpEx	CapEx
C - Manufacturing	33,181	30,957	1,546
D - Electricity, gas, steam and air conditioning supply	70,273	63,802	10,583
E - Water supply, sewerage, waste management	1,725	1,626	114
F - Construction	51,717	47,499	831
H – Transporting and storage	4,631	4,044	516
I - Information and communication	88	75	5
L - Real estate activities	5,157	2,500	654
Estimated Taxonomy-eligible total	**166,772**	**150,504**	**14,248**
Share of total NFRD sample (%)	***2.47%***	***2.43%***	***3.14%***

Sources: FIRDS, Refinitiv Eikon, Alessi et al. (2019), TEG report, ESMA.

The estimated share of Taxonomy-aligned activities can be further broken down by NACE Macro-sector (Chart 3). The Macro-sectors with the highest shares are: Construction (F); Electricity, gas, steam and air conditioning supply (D); and Real estate activities (L).

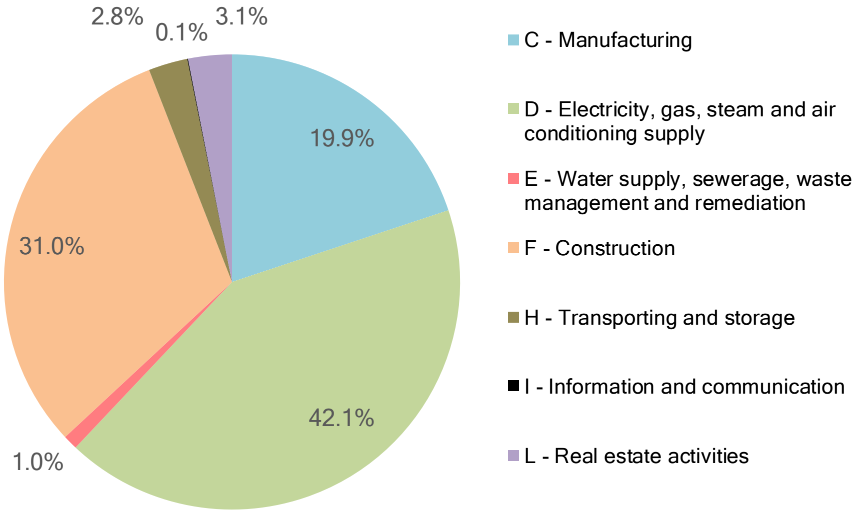
Chart 3: Estimated share of Taxonomy-aligned Turnover, OpEx and CapEx of EU-27 non-financial undertakings in NFRD scope, by Taxonomy-relevant NACE Macro-sectors



Note: Estimated share of Taxonomy-aligned Turnover, OpEx and CapEx of EU non-financial undertakings in NFRD scope.
Sources:FIRDS, Refinitiv Eikon, Alessi et al. (2019), TEG report, ESMA

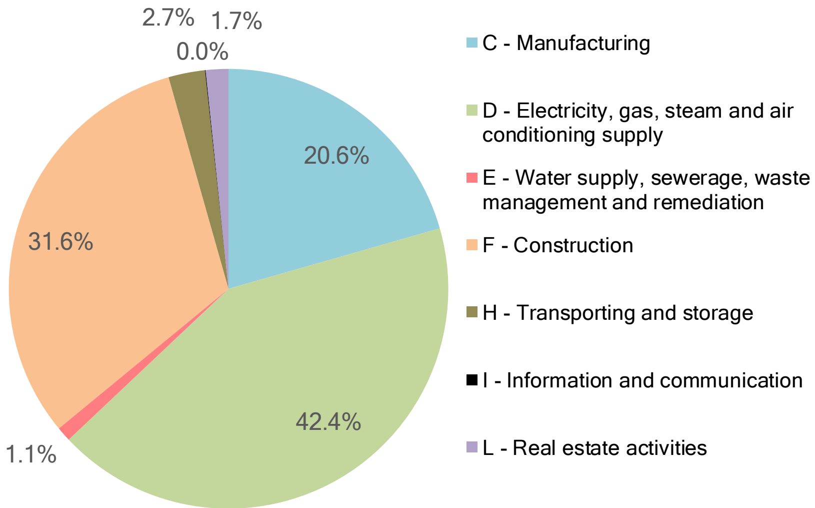
The relative share of each NACE Macro-sector in the estimated Taxonomy-aligned KPIs is displayed in Charts 4, 5 and 6. Based on Turnover and OpEx, Construction (F) and Electricity, gas, steam and air conditioning supply (D) dominate current estimates of Taxonomy-aligned economic activity.

Chart 4: Relative shares of NACE Macro-sectors in estimated Taxonomy-aligned Turnover of EU-27 non-financial undertakings in NFRD scope



Note: Share of relevant NACE Macro-sectors in estimated Taxonomy-aligned turnover of EU-27 non-financial undertakings in NFRD scope.
Sources: FIRDS, Refinitiv Eikon, Alessi et al. (2019), TEG report, ESMA

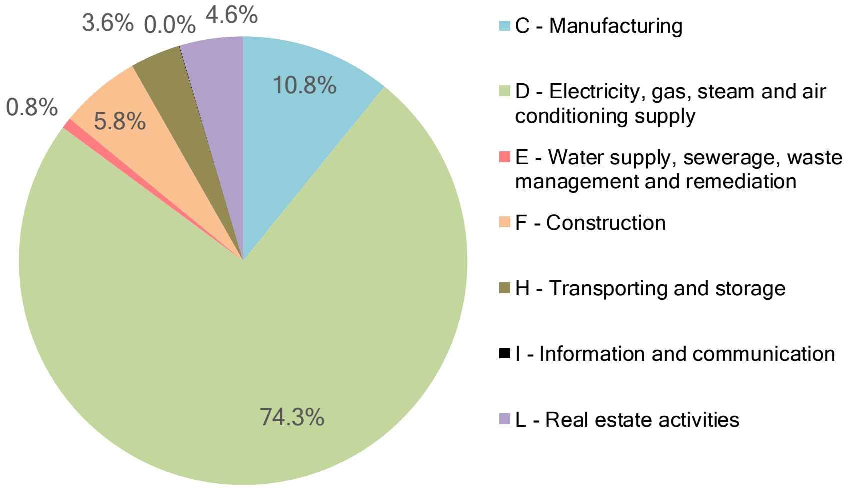
Chart 5: Relative shares of NACE Macro-sectors in estimated Taxonomy-aligned OpEX of EU-27 non-financial undertakings in NFRD scope



Note: Share of relevant NACE Macro-sectors in estimated Taxonomy-aligned OpEx of EU-27 non-financial undertakings in NFRD scope.
Sources: FIRDS, Refinitiv Eikon, Alessi et al. (2019), TEG report, ESMA

Based on CapEx, Electricity, gas, steam and air conditioning supply (D) account for 75% of the estimated Taxonomy-aligned capital expenditure. This reflects the relatively high CapEx-to-Turnover ratio of the sector, combined with a coefficient of 20,87% for the sector based on the current share of electricity production from renewable sources in Europe.

Chart 6: Relative shares of NACE Macro-sectors in estimated Taxonomy-aligned CapEx of EU-27 non-financial undertakings in NFRD scope



Note: Share of relevant NACE Macro-sectors in estimated Taxonomy-aligned CapEx of EU-27 non-financial undertakings in NFRD scope.
Sources: FIRDS, Refinitiv Eikon, Alessi et al. (2019), TEG report, ESMA

Annex

Table 3: NACE codes by Climate Policy Relevant Sector (CPRS)

NACE Rev. 2 core codes	Sectors
B5.1-B6.2, B8.9.2, B9.1, C19.1-C19.2, C20.1.1, C28.9.2, D35.2, F43.1.2, F43.1.3, H49.5	Fossil-fuel
B7.1, B7.2.9, B8.9.1, B8.9.3, B8.9.9, C10.2, C10.6.2, C10.8.1, C19.8.6, C11.0.1, C11.0.2, C11.0.4, C11.0.6, C13.1-C15.2, C16.2.9-C17.1.2, C17.2.4, C20.1.2-C20.2, C20.4.2, C20.5.3-C22.1.9, C23.1.1, C23.1.3-C23.5, C23.7, C23.9.1, C24.1-C24.2, C24.4-C24.4.6, C24.5.1, C24.5.3., C25.4, C25.7, C25.9.4-C28.9.1, C28.9.3-C29.1, C29.3.1, C30.3, C30.9, C31.0.9-C32.9,	Energy-intensive
C23.6.1, C23.6.2, C31.0.1-C31.0.3, F41.1, F41.2, F43.1-F43.9, I55.1, L68	Housing
D35.1, F42.2.2	Utilities
H49.1-H49.4, H50-H51.2.1, H52.5-H53.2.0	Transport
K	Finance
All remaining ones	Other

Note: The NACE Macro-sector B – Mining and quarrying has been excluded from the estimates of Turnover, OpEx and Capex as it is not included in the final TEG report.
Source: Battiston et al. (2017) *"A climate stress-test of the financial system"*.

Table 4: Estimated Taxonomy-aligned coefficients by CPRS

CPRS denomination	Coefficient applied
Energy-intensive	3%
Production of electricity	20,87%
Water management	3%
New buildings	100%
Building renovation	5%
Real-estate activities	15%
Manufacture of trains and bicycles	100%
Urban and suburban passenger land transport	50%

Automotive sector	0,59%

Source: Alessi et al. (2019) *"The EU Sustainability Taxonomy: a Financial Impact Assessment"*.