EU Taxonomy Reporting 2024

Analysis of the financial and non-financial sector

EU Taxonomy Reporting 2024

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Preface

In recent years, the European Commission has implemented various regulations aimed at channelling financial resources towards sustainable economic activities, thereby fostering the sustainable transition of the economy. The Taxonomy Regulation, which serves as a framework for classifying sustainable economic activities, has been one of the first regulations in this regard and is being gradually implemented. Effective since FY 2021, this regulation applies to entities falling under the purview of the Non-Financial Reporting Directive (NFRD), which encompasses large public-interest entities such as listed companies, banks, and insurers, employing more than 500 individuals. Furthermore, starting in 2025, the scope of application will expand to cover all entities subject to the Corporate Sustainability Reporting Directive (CSRD).

Since 2022, the first year of application, PwC has been analysing the taxonomy reports by the non-financial sector, in 2023 the financial sector was included for the first time. This year, there have been several innovations in the reporting requirements, in particular for financial undertakings with the introduction of taxonomy alignment reporting for the first two environmental objectives. The implementation of the regulation still poses challenges for market participants. The comprehensive reporting requirements imply the adaptation of internal ESG data collection and governance processes. Furthermore, there are persisting data availability and quality issues and continuous regulatory interpretation questions which lead to diverse methodologies being applied making comparisons between the reported data difficult. However, following the current transition phase, sustainability reporting will be on par with financial reporting. If the Taxonomy data is used for steering purposes by financial and non-financial companies, it will support the transition to a more sustainable economy.

Many thanks to all who contributed their expertise to the study from PwC Germany and 11 other European PwC entities. We hope that reading this study is both interesting and informative for you!

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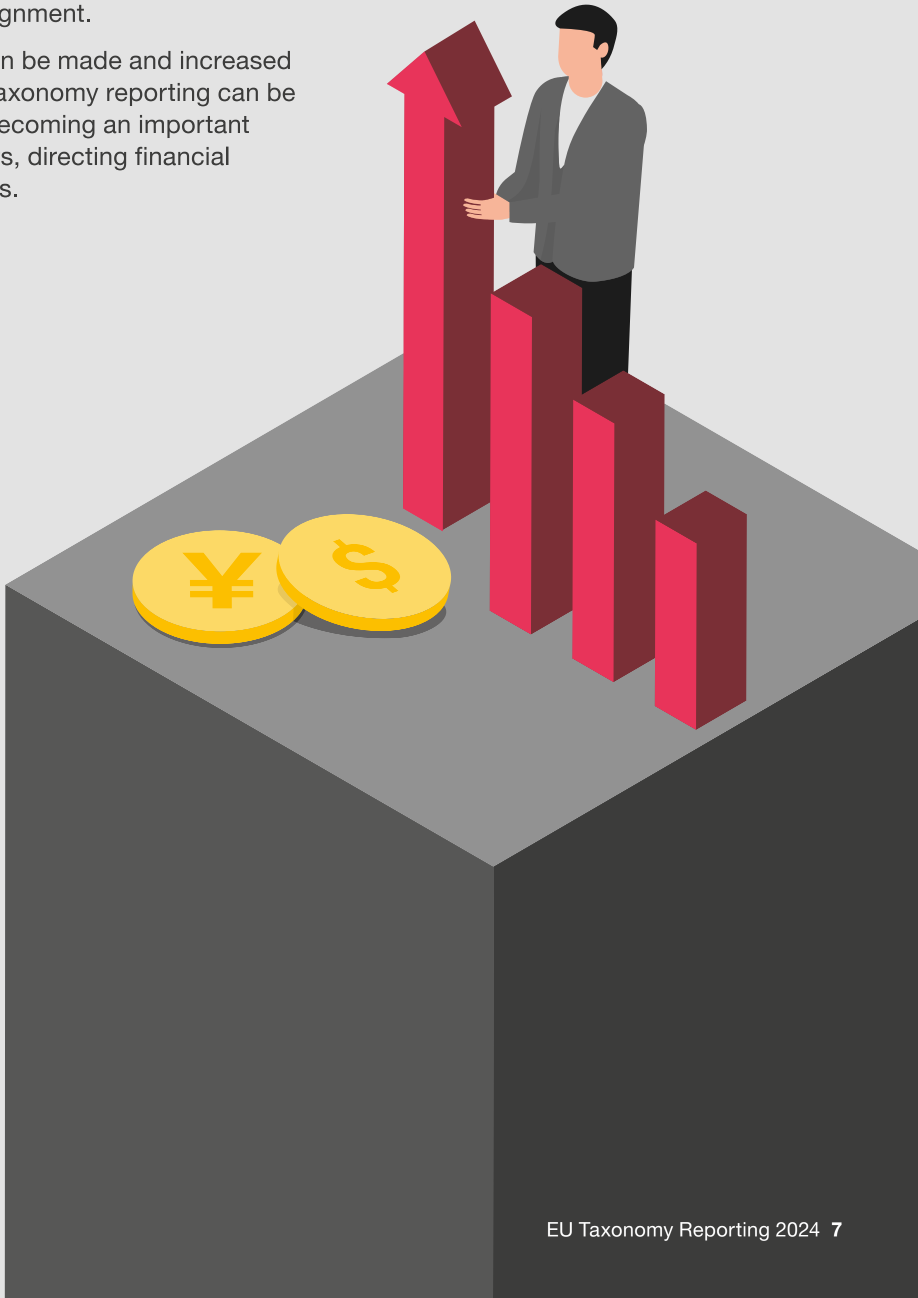
Key findings

Financial Sector

- Taxonomy eligibility reporting is now more homogenous than it was last year.[1]
  - In the banking sector, average national Taxonomy eligibility varies between 20% and 44% based on turnover and between 21% and 45% based on CapEx.
  - In the insurance sector, average national ranges of Taxonomy eligibility are still very broad in the underwriting business, with a minimum of 1% and a maximum of 47%; this variation is largely due to differing methodologies.
  - For the investment business in the insurance sector, average national Taxonomy eligibility varies between 4% and 28% based on turnover and between 4% and 32% based on CapEx.
- Taxonomy alignment is still fairly low in the financial sector.[2]
  - For banking, the average turnover-based alignment Green Asset Ratio (GAR) (stock) is 2%, with national averages ranging from 0% to 13%; the average CapEx-based alignment KPI is also 2%, with national averages again ranging from 0% to 13%.
  - For the underwriting business of insurance, average Taxonomy alignment is yet again 2%.
  - For the investment business in the insurance sector, average Taxonomy aligned exposures to financial undertakings are close to zero. The average Taxonomy aligned exposures to non-financial undertakings are 4% for the turnover-based KPI and 5% for the CapEx-based KPI.
  - The low alignment ratios are attributable to several factors: there are persisting data availability and quality issues; there are still uncertainties with regard to the interpretation of regulatory provisions, and therefore different methodologies; and there is a need for increased efforts by companies to obtain the relevant data by improving their internal processes. Finally, the low level of Taxonomy alignment also indicates that there is still a long way to go when it comes to directing financial flows towards the sustainable transition of the economy.

[1] The ranges of the Taxonomy eligibility and alignment levels given in this study are based on the average national Taxonomy eligibility and alignment levels.
[2] ibid.

- In the insurance sector, the majority of insurers used a partial premium approach based on the Commission Notice. Since the climate-related share is the main determinant for this figure, there is a need to harmonise the methods for calculating this share; these should be based on pricing data derived from risk modelling.
- Levels of Taxonomy alignment are dependent on the business model of the financial institution in question. In the insurance sector, this is due to the calculation methods used for various lines of business. In the banking sector, it is due to the limited share of Taxonomy-eligible activities in a typical bank's portfolio.
- Financial institutions do not use Taxonomy data for strategic purposes or to guide investment decision-making – in part because of the low Taxonomy alignment numbers. This is demonstrated by the fact that financial institutions make hardly any references to plans to increase Taxonomy alignment.
- If further improvements in data availability can be made and increased convergence of methods can be achieved, Taxonomy reporting can be further improved to achieve its objective of becoming an important reference point for investors and stakeholders, directing financial flows towards sustainable economic activities.



Key findings

Non-financial sector

- In the annual reports of the 530 companies analysed this year, EU Taxonomy disclosures nearly doubled, from just 38% in the FY 2022 reports to 76% in FY 2023. Non-disclosure went down by half, from 14% in 2022 to only 7% in 2023.
- Although about 67% of companies presented eligible and aligned turnover, CapEx and OpEx using the mandatory KPI templates, less than half used the additional KPI template to report on the presence or absence of gas and nuclear activities. One fifth of the companies made minor amendments to their disclosed KPI templates.
- Like last year, there is still a large gap between Taxonomy-eligible and Taxonomy-aligned economic activities.
- In general, Taxonomy eligibility and alignment increased slightly for all three KPIs compared to the previous year. Only the average Taxonomy-eligible proportion of CapEx remained unchanged. Additional economic activities, improved understanding of technical screening criteria, minimum safeguard requirements and increased data availability and quality are possible reasons for this growth.
- For turnover, average reported Taxonomy eligibility amounted to 30%; Taxonomy alignment was 9%.
- For CapEx, average Taxonomy eligibility amounted to 37%; Taxonomy alignment totalled 12%.
- For OpEx average Taxonomy eligibility was 30%; Taxonomy alignment came to 9%.

- The Real Estate industry reported the highest Taxonomy eligibility percentage for economic activities for all three KPIs.
- The Energy, Utilities and Resources industry reported the highest Taxonomy alignment percentage for economic activities for all three KPIs.
- 17% of the companies made an explicit reference to the FAQs from December 2023[3].
- Almost three quarters of the companies disclosed comparative figures from the previous year. This was an increase of 64 percentage points compared to FY 2022, when only 10% of companies had disclosed comparative figures.
- Reporting of KPIs from non-financial companies is stabilising across industries, which will allow for better comparability over time. However, non-financial companies continue to face data challenges due to the EU adding new environmental objectives and economic activities.
- From FY 2025, the number of companies that fall within the scope of the CSRD and the EU Taxonomy will increase. While the last three years' worth of reports from previously reporting entities will provide newly impacted companies with a good starting point and good guidance, they will not benefit from a transitional phase and will need to report on all requirements without any exemptions – including being subject to mandatory audits.
- The intention behind the CSRD and the EU Taxonomy is to provide a comprehensive framework that actively guides companies towards greater sustainability. We would expect to see this reflected in increasing alignment KPIs across both the financial and the non-financial sectors. However, the current level of overall alignment remains very low and has not increased significantly over the last two reporting years.

[3] European Commission (December 2023), Draft Commission notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act under Article 8 of the EU taxonomy Regulation on the reporting of taxonomy-eligible and Taxonomy-aligned economic activities and assets (approved in principle), https://ec.europa.eu/finance/docs/law/231221-draft-commission-notice-eu-taxonomy-reporting-financials_en.pdf

A The EU Taxonomy Regulation

In recent years, the EU has introduced a series of measures aimed at channelling investment into sustainable economic activities, with the overarching goal of facilitating the transition to a more sustainable economy. The involvement of the private sector is crucial for realising objectives such as the Paris Climate Goals and the UN Sustainable Development Goals, and for advancing the European Green Deal, which pledges to make Europe the world's first climate-neutral continent by 2050.

One significant development in this regard came in 2020 with the publication of the EU Taxonomy Regulation by the European Commission. This regulation established a classification framework for identifying sustainable economic activities and making the respective disclosures, thereby enhancing transparency for investors. The Taxonomy is expected to play a pivotal role in steering investment towards sustainability, and in fostering clarity and comparability across various sectors, both financial and non-financial.

The disclosure requirements of Article 8 of the Taxonomy Regulation are being phased in over a number of years. For the financial year 2021 reporting period, simplified Taxonomy reporting became mandatory for large public-interest entities with more than 500 employees. This included companies listed on EU-regulated markets, along with banks and insurance companies. In the first reporting year, companies that fell under the regulation were only required to report on Taxonomy eligibility for the first two environmental objectives: climate change mitigation (objective 1) and climate change adaptation (objective 2). The regulation required non-financial undertakings to introduce full reporting on both Taxonomy eligibility and alignment for the first two environmental objectives (including gas and nuclear activities) in FY 2022, while the financial sector had one more year of reporting Taxonomy eligibility only. Our studies in previous years have explored the outcomes of these initial reporting periods.

In 2024 (reporting on FY 2023), financial companies have had to disclose Taxonomy alignment KPIs for environmental objectives 1 and 2 for the first time. In addition, both financial and non-financial companies have had to disclose Taxonomy eligibility KPIs for the newly added activities under environmental objectives 1 and 2, and for the other four EU environmental objectives: sustainable use and protection of water and marine resources (objective 3), transition to a circular economy (objective 4), pollution prevention and control (objective 5), and protection and restoration of biodiversity and ecosystems (objective 6). Reporting Taxonomy alignment on objectives 3 to 6 will become mandatory from 2025 (for FY 2024) for non-financial undertakings and from 2026 (for FY 2025) for financial companies.

After reports of challenges regarding differing interpretations of the regulation, the European Commission has sought to create additional clarity by publishing a number of Commission Notices, including FAQs[4]. In 2023, one Commission Notice dealt with interpretation questions concerning the minimum safeguards and links to the Sustainable Finance Disclosure Regulation[5]. Another draft Commission Notice addresses the Disclosures Delegated Act (the third Commission Notice on the disclosure requirements under Article 8 of the Taxonomy Regulation), currently with a focus on financial undertakings[6].

[4] European Commission (n.d.), EU Taxonomy for sustainable activities, https://finance.ec.europa.eu/sustainable-finance/tools-and-standards/eu-taxonomy-sustainable-activities_en#faqs.

[5] European Commission (June 2023), Commission notice on the interpretation and implementation of certain legal provisions of the EU Taxonomy Regulation and links to the Sustainable Finance Disclosure Regulation, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52023XC0616(01)

[6] European Commission (December 2023), Draft Commission notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act under Article 8 of the EU taxonomy Regulation on the reporting of taxonomy-eligible and Taxonomy-aligned economic activities and assets (approved in principle), https://ec.europa.eu/finance/docs/law/231221-draft-commission-notice-eu-taxonomy-reporting-financials_en.pdf

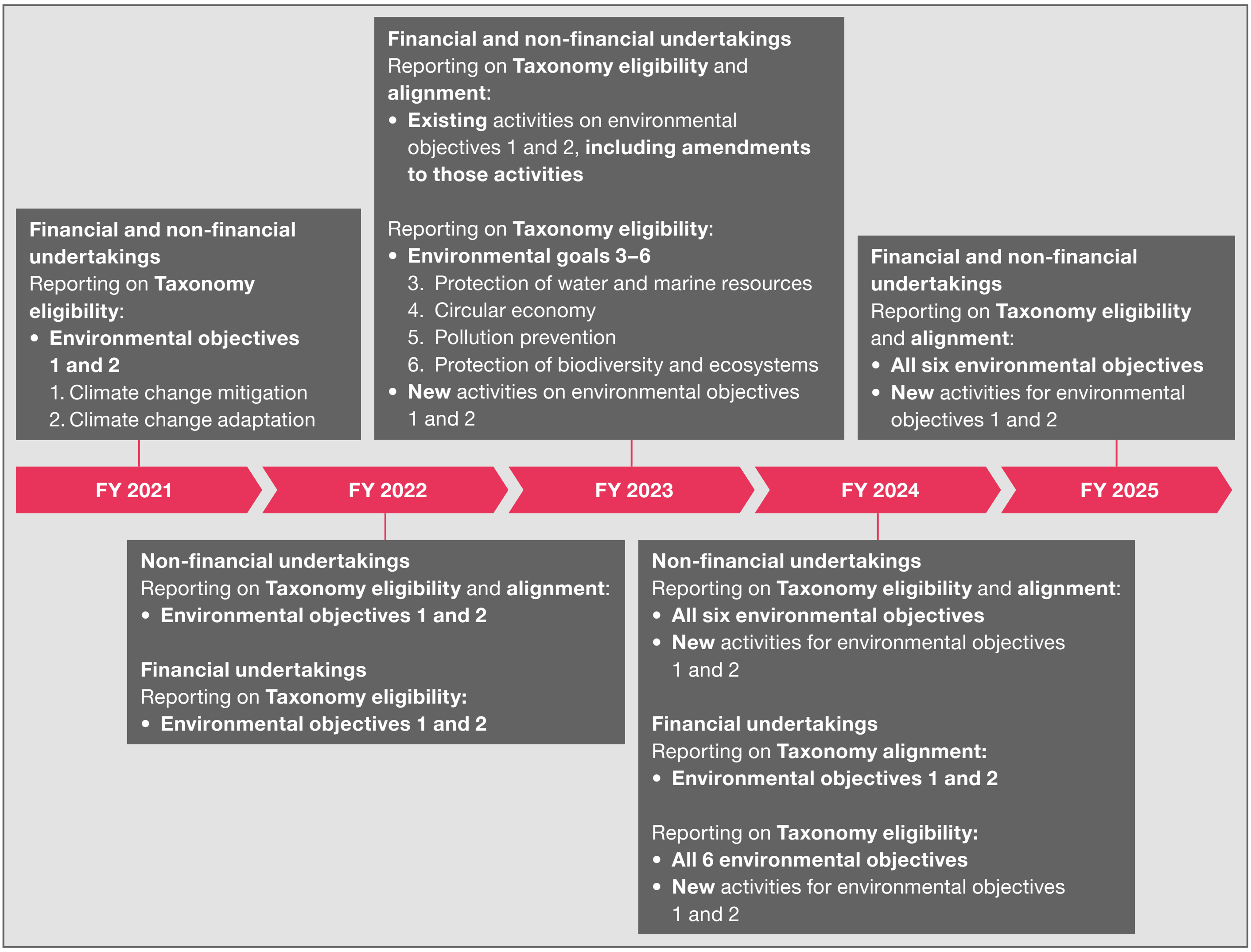
Interaction with CSRD reporting

Another important issue relating to the EU Taxonomy results from its interaction with the CSRD, which will take effect from 2025 onwards (for FY 2024) for the first wave of companies that are subject to the NFRD. In the second wave (FY 2025), all companies classified as large (exceeding at least two of the three criteria: €50 million revenue, €25 million balance sheet total or 250 employees) will fall within the scope of the CSRD. In the third wave (FY 2026), listed small and medium-sized companies will also be subject to the CSRD.

In general, the aforementioned undertakings that fall within the scope of the CSRD are also subject to the EU Taxonomy reporting requirements. The CSRD requires that Taxonomy disclosures be presented in a clearly identifiable part of the environmental section of the sustainability statement, which is a dedicated section of the company's management report. EU Taxonomy disclosures will also be subject to mandatory audits, initially providing limited assurance and later being extended to reasonable assurance.

Some European Sustainability Reporting Standards (ESRS) occasionally refer to Taxonomy disclosures (e.g. the disclosure requirements in ESRS E1), and the environmental objectives of the Taxonomy are largely in line with the thematic standards of the CSRD.

Fig. 1 Timeline for Taxonomy reporting obligations



Assessing Taxonomy eligibility and alignment

Assessing Taxonomy eligibility and alignment typically involves a five-step process applicable to both financial and non-financial undertakings. Financial institutions have to collect the relevant ESG data from their counterparties for their own Taxonomy reporting.

After identifying Taxonomy-eligible activities (using familiar procedures from previous reporting periods), undertakings must assess whether each of these economic activities substantially contributes to at least one of the six environmental objectives, does no significant harm (DNSH) to any of the other objectives, and complies with certain minimum safeguards found in Article 3 of the Taxonomy Regulation. Substantial contributions and DNSH are assessed based on TSC at economic activity level, whereas compliance with minimum safeguards requires adherence to principles – such as the OECD Guidelines for Multinational Enterprises or the UN Guiding Principles on Business and Human Rights – at entity level (Taxonomy Regulation, Article 18).

Fig. 2 Steps for assessing whether economic activities are Taxonomy aligned and for determining revenue, CapEx and OpEx KPIs

1 Is the activity Taxonomy eligible?

Screen for Taxonomy eligible activities.

2 Does it have a substantial contribution?

- Economic activities that have a substantial contribution to one of the six environmental objectives based on the TSC.
- Economic activities may provide a substantial contribution directly or indirectly by enabling other activities to make a substantial contribution to one of the six environmental objectives ("enabling activities")

3 Does it do no significant harm?

Activities that impose no significant harm to the other five environmental objectives based on the TSC.

4 Minimum safeguards

Compliance with minimum safeguards
Including, for example:
- OECD Guidelines for Multinational Enterprises
- UN Guiding Principles for Economy and
- Human Rights

5 Key performance indicator

Calculate the proportion of activities which are Taxonomy-aligned and Taxonomy-eligible.

Reporting obligations for financial companies

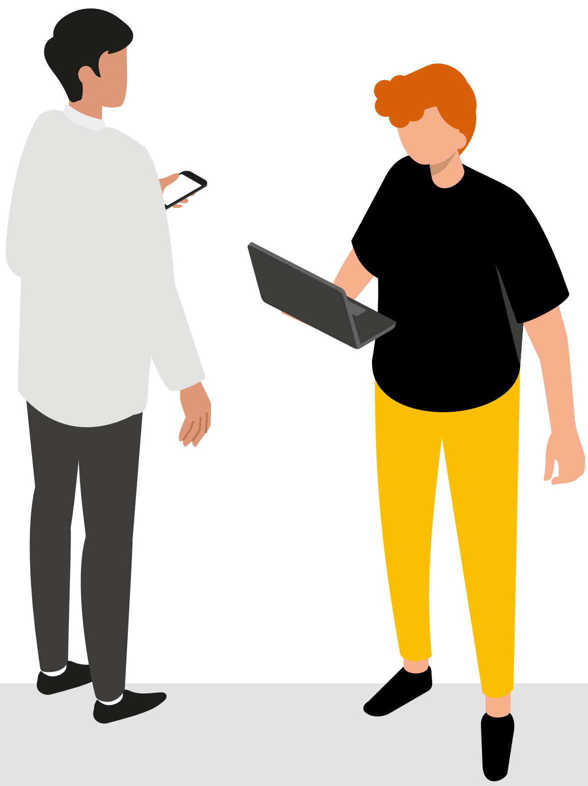
Under the Taxonomy Regulation, financial companies are subject to different reporting criteria from non-financial companies. All financial institutions that fall within the scope of the NFRD (and, after its entry into force, the CSRD) must disclose how and to what extent they fund or invest in sustainable economic activities, based on the EU Taxonomy criteria. The quality of the data reported by financial institutions largely depends on the quality of the data reported by the financial and non-financial companies they lend to or invest in, as the Taxonomy does not permit the use of estimates.

In 2024, financial companies are required to report on Taxonomy alignment for environmental objectives 1 and 2 for the first time, covering FY 2023. This implies that the usage of the reporting templates published by the European Commission is now mandatory, which will lead to greater standardisation of reporting. Furthermore, financial companies can now make use of Taxonomy alignment data for FY 2022 from non-financial companies in their portfolios for the first time. There are therefore some improvements compared to 2023 with regard to issues surrounding data availability and quality, and inconsistencies in the methodologies used.

The reporting templates for the quantitative KPIs for financial companies differ depending on the type of financial institution in question. While the green asset ratio (GAR) provides an indication of the proportion of sustainable business for banks, there are different KPIs for the sustainable share of business for capital markets, investment firms and (re)insurance undertakings.

In addition to the quantitative KPIs, financial undertakings are also required to disclose certain qualitative information[7]:

- Background information on the quantitative indicators
- Nature, objectives and development of Taxonomy-aligned economic activities
- Compliance with EU Taxonomy in business strategy, the product design process, and engagement with clients and counterparties
- Alignment of trading portfolios with the EU Taxonomy, and trading portfolio composition, trends, targets and guidelines (only applicable to credit institutions)
- Information on the strategy and importance of financing Taxonomy-aligned economic activities



[7] Article 10(3)(d) of Commission Delegated Regulation (EU) 2021/2178.

Regulatory obligations for non-financial companies

The 2024 reporting year, covering FY 2023, brought changes to the reporting obligations for non-financial companies. Two delegated acts complemented the Taxonomy Regulation – the Environmental Delegated Act[8] and the Delegated Act amending the Climate Delegated Act[9] – were officially published in the Official Journal of the European Union on 21 November 2023. The Environmental Delegated Act not only outlines specific economic activities and relevant technical screening criteria for environmental objectives 3 to 6, but also introduces amendments to the Disclosures Delegated Act.

Notably, three new reporting templates were introduced for non-financial companies' KPIs (turnover, CapEx, OpEx). Meanwhile, the Delegated Act amending the Climate Delegated Act requires that existing activities be modified in line with climate objectives and new activities added, along with their respective criteria.

In the Taxonomy, data regarding gas and nuclear activities must now be disclosed using separate templates. The draft FAQs published in December 2023 clarify that template 1 should generally be used for gas and nuclear activities (see FAQ no. 28[10]). The FAQ also states that templates 2 to 5 are not mandatory for gas and nuclear activities if the answer to all six questions on template 1 is "no".

Furthermore, some Technical Screening Criteria, such as Annex C (Substances of concern) have been amended (amendment to letter (f), and a paragraph added in place of the former letter (g)), establishing additional analysis requirements for companies.

With regard to the minimum safeguards, some clarifications have been provided by the European Commission in the form of a Commission Notice[11]. Due diligence procedures are required, including the implementation of adequate processes to identify, mitigate and decrease actual and potential negative impacts connected with a company's own operations, value chain and business relationships. Non-financial companies are required to disclose any remaining risks concerning negative impacts that cannot be avoided. In addition, the principal adverse impacts (PAIs) presented in Table 1 of Annex I to the Delegated Act supplementing the Sustainable Finance Disclosure Regulation (SFDR) must be taken into account.

Non-financial undertakings are required to take steps including the following:

- Identify each economic activity, including a subset of enabling and transitional economic activities for all environmental objectives – this also applies to new economic activities.
- Disclose the Taxonomy eligibility of all KPIs for each environmental objective and the overall KPIs at the company or group level across all environmental objectives, avoiding double counting.
- Identify and disclose the proportions of Taxonomy-aligned and Taxonomy-eligible economic activities that do not meet the TSC and/or minimum safeguards for turnover, CapEx and OpEx. This does not include new economic activities. Disclosure of the Taxonomy alignment of new economic activities and of environmental objectives 3 to 6 will be required from FY 2024.
- Provide the KPIs at the individual company level if the company prepares only individual non-financial statements, or at group level if the company prepares consolidated non-financial statements.[12]

With the economic activities added to the Climate Delegated Act and the new economic activities included in the Environmental Delegated Act, companies must now amend their processes and add additional assessment routines to cover all the environmental objectives. Regularly published guidance in the form of Commission Notices may also alter the nature of reporting, meaning companies may require additional resources and capabilities for data collection, analysis and reporting.

Aside from these technical amendments, the European Commission has published the EU Taxonomy Navigator and a Taxonomy Handbook to support undertakings in the preparation of their reports.

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8 Delegated Regulation (EU) 2023/2486 of June 27 2023 (Environmental Delegated Act), https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32023R2486

9 Delegated Regulation (EU) 2023/2485 of 27 June 2023 amending the Climate Delegated Act, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32023R2485

10 European Commission (December 2023), Draft Commission notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act under Article 8 of the EU taxonomy Regulation on the reporting of taxonomy-eligible and Taxonomy-aligned economic activities and assets (approved in principle), https://ec.europa.eu/finance/docs/law/231221-draft-commission-notice-eu-taxonomy-reporting-financials_en.pdf

11 European Commission (June 2023), Commission notice on the interpretation and implementation of certain legal provisions of the EU Taxonomy Regulation and links to the Sustainable Finance Disclosure Regulation, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52023XC0616(01)

12 Disclosures Delegated Act (2021/2178), Annex I

B Analysis of reported Taxonomy data for FY 2023

1. General observations

The EU Taxonomy was introduced to provide a uniform framework for classifying economic activities in terms of their sustainability, ensuring that investments in sustainable projects are promoted, and improving transparency regarding sustainability. Applying the EU Taxonomy allows financial undertakings to evaluate their investments and lending against a consistent and standardised framework. The Taxonomy also aims to provide clarity and comparability between companies, as well as between the financial and non-financial sectors.

Financial undertakings are dependent on the relevant ESG data from their counterparties for their Taxonomy reporting. These counterparties are predominantly non-financial companies which the undertakings are financing or in which they have invested. The quality of financial undertakings' Taxonomy reporting therefore largely depends on the quality of the Taxonomy disclosures made by their counterparties. Lack of data, poor-quality data and lack of standardisation in counterparties' Taxonomy reports were last year's reasons that hindered adequate and effective disclosures. Many of these factors can be overcome, once market practice has improved with regard to methodologies applied and data availability and quality has increased with the gradual implementation of the CSRD.

However, reporting on FY 2023 already saw an improvement in data availability: for the first time, financial undertakings were able to make use of Taxonomy alignment reports issued by their portfolio companies in a previous year (FY 2022). Non-financial companies have been required to report on Taxonomy alignment since 2023 (for FY 2022), and they did meet the applicable regulatory requirements. Previous challenges regarding non-financial undertakings' Taxonomy alignment criteria, such as data collection on the TSC, were minimised thanks to a generally improved understanding of the TSC and minimum safeguard requirements. However, some data challenges remain for non-financial undertakings as a result of the newly introduced requirement to report on Taxonomy eligibility for environmental objectives 3 to 6, and the added economic activities. Both financial and non-financial companies will generally be able to refer to these Taxonomy alignment reports in the future.

This year (FY 2023), financial undertakings have been required to use the mandatory reporting templates for the first time. As a result, standardisation of methods increased and allowed better comparability of results than was the case last year. Since non-financial companies were required to apply the mandatory templates from their FY 2022 reports onwards, this year's study has already revealed more standardised reporting and has facilitated the comparison of KPIs across industries, countries and companies.

For financial undertakings, it is evident that the range of Taxonomy eligibility has decreased compared to last year; in other words, the reported data is more homogenous. This is largely due to increased data availability, additional regulatory guidance and better practice in the market. The fact that use of the templates is now mandatory also played a role. Taxonomy alignment KPIs in the financial sector are still quite low in this first reporting year, which can be attributed to data quality and availability issues, methodological uncertainties and to a certain extent to not yet perfect internal data collection processes. It also indicates that the green part of the economy is still small, and that there is still a long way to go in the green and sustainable economic transition.

For the non-financial sector, it is noticeable that the three Taxonomy KPIs – turnover, CapEx and OpEx – for eligibility and alignment generally increased slightly in FY 2023 compared to FY 2022; only the average eligible CapEx remained unchanged. These increases may be due to more and more companies utilising systems and tools to track data and KPIs to enable higher quality and availability of data and reduce the use of estimates. Overall, the disclosure of Taxonomy KPIs has slowly begun to normalise over time. This is fundamental for auditing and assurance services, since auditing of CSRD and EU Taxonomy information is required for FY 2024 financial year.

As the incrementally increasing CSRD obligations for companies are set to reach certain threshold criteria (net turnover, assets, employees) over the next few years, it is highly probable that the availability and quality of data will significantly increase. Nevertheless, it is important that both financial and non-financial companies continue to improve their data collection and reporting processes and that market standards on still open regulatory interpretation questions emerge. It is also beneficial for both sides to gain insights on their relevant – potentially common - challenges and solutions as well as the information needs of investors to make appropriate decisions on capital allocation and risk management for the Taxonomy to fully achieve its purpose.

2. Taxonomy reporting in the financial sector

Taxonomy reporting on FY 2023 introduced reporting on Taxonomy alignment in financial undertakings for the first time, which has led to many changes. Most importantly, use of the reporting templates issued by the European Commission has now become mandatory – a significant change from our 2023 study, which concluded that many financial undertakings were not yet using the templates.

The ranges between the reported Taxonomy eligibility levels are much smaller this year than they were last year. For FY 2022, Taxonomy eligibility across all analysed financial companies was very heterogeneous, ranging between 0% and 76%. In FY 2023, the average of the turnover-based KPI for Taxonomy eligibility in banking varied between 20% and 44%, and the average of the CapEx-based KPI ranged between 21% and 45%. While the mandatory use of the templates will have played a role in standardising reporting, the increased homogeneity is attributable to many factors that have influenced Taxonomy reporting. These include some clarifications from the regulator in the form of additional guidance on interpretation, better practice in the market, and improved data availability as a result of mandatory Taxonomy compliance reporting by non-financial counterparties for FY 2022.

Fig. 3 **Taxonomy eligibility in the banking sector**

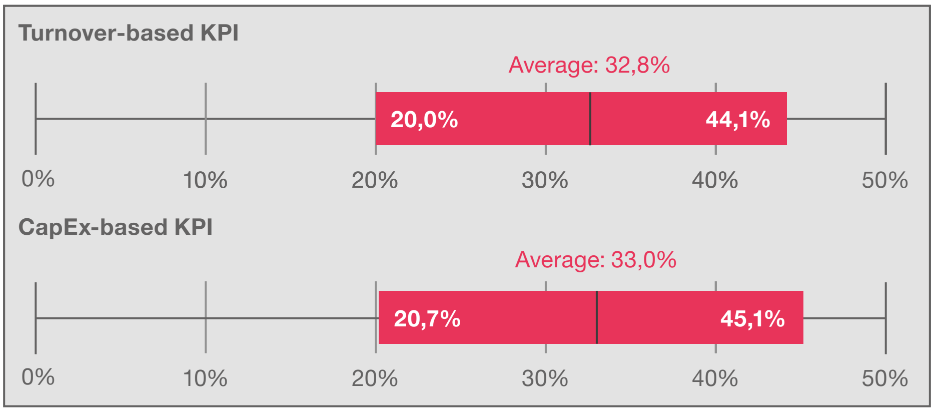
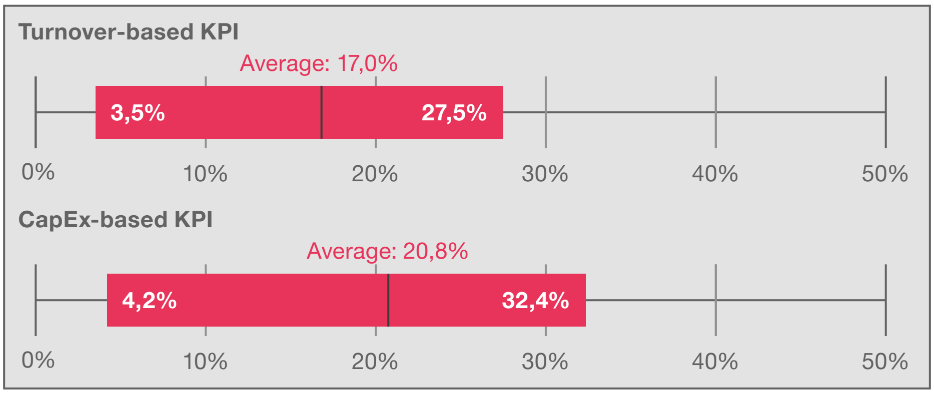


Fig. 4 **Taxonomy eligibility for the investment business in the insurance sector**



In the insurance sector, the range of average national Taxonomy eligibility in the underwriting business is still rather broad (minimum 1%, maximum 47%), which is largely due to differing methodologies which will be analysed in the insurance-specific section below. For the investment business in the insurance sector, national averages range from 4% to 28% for the turnover-based KPI for Taxonomy eligibility and from 4% to 32% for the CapEx-based KPI.

Fig. 5 Taxonomy alignment and eligibility quota for the underwriting business in the insurance sector

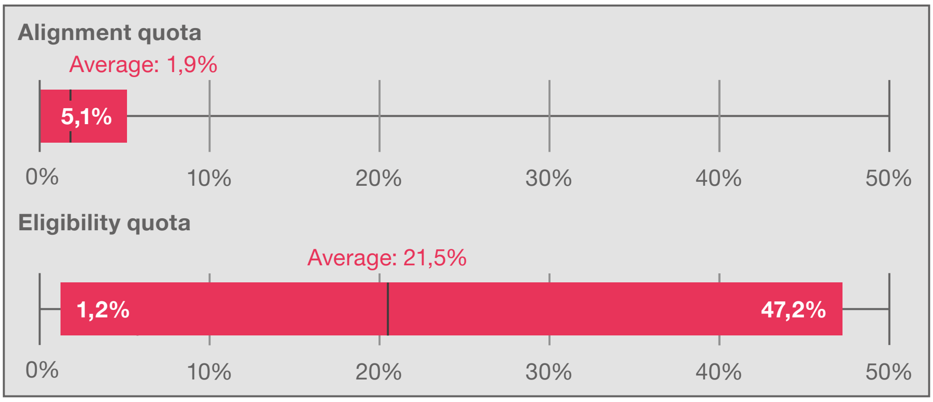
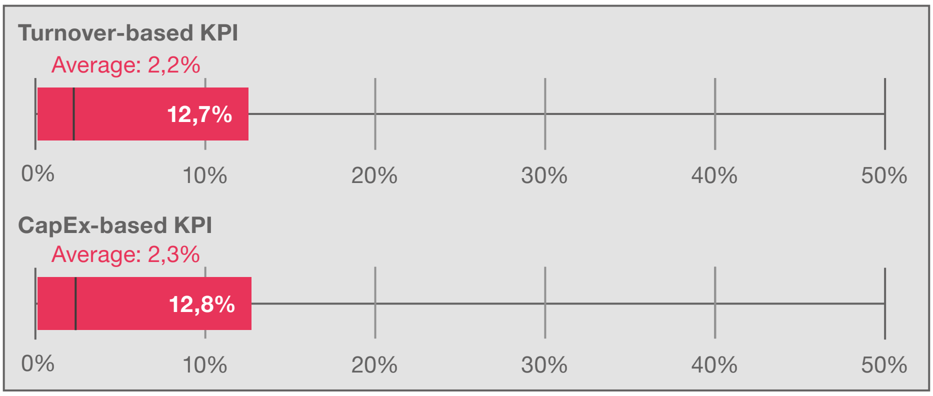


Fig. 6 Taxonomy alignment in the banking sector



By contrast, the difference between the reported levels of Taxonomy alignment is generally well below ten percentage points. For the underwriting business of insurance, the average national level of Taxonomy alignment is 2% – with the highest levels in Poland and Germany, both at 5%. The higher levels of Taxonomy alignment in these countries may be caused by factors such as varying methodologies, a generally greater effort being made to obtain relevant data, or some companies starting the implementation process earlier.

For banks, the average national turnover-based Green Asset Ratio (GAR) (stock) is 2%, with a range from 0% to 13%. The average national CapEx-based alignment KPI is also 2%, and similarly has a range from 0% to 13%. The Netherlands achieved exceptionally high average alignment – 13% for both turnover and CapEx. These high levels may be the result of greater data availability for real estate financing in the Netherlands, due to energy performance certificate (EPC) ratings being relatively easily accessible.

Taxonomy alignment is still generally low in the banking sector. This is the result of many factors which will be further explored in the banking-specific sections below. There are still various different methods being used to calculate Taxonomy eligibility and alignment in the insurance and banking sectors. This diversity of methods is a result of a lack of clarity in the regulatory instructions, which leave room for interpretation. There are also ongoing data availability and quality issues and, among other factors, a need for companies to increase their efforts in obtaining the relevant data and improving their related processes.

To provide further clarity to companies and improve the quality of Taxonomy reports, the European Commission published another set of FAQs in December 2023, shortly before companies started preparing their Taxonomy reports for 2024. There is limited transparency on the part of the financial companies analysed in this study regarding the implementation of these FAQs, but our results show that they have not yet been fully implemented, presumably due to the limited time frame and persistent lack of clarity around the interpretation of some questions. For example, Annex II of the draft Commission Notice, “Examples of computation of weighted average of KPIs on Taxonomy-aligned activities of groups”, was not completed by the companies analysed in this study. Its effects will therefore not become fully visible until next year’s reporting cycle.

Three quarters of the analysed financial companies have investments in gas and nuclear activities, which are Taxonomy eligible as transition activities.

Fig. 7 Investments in nuclear and gas activities

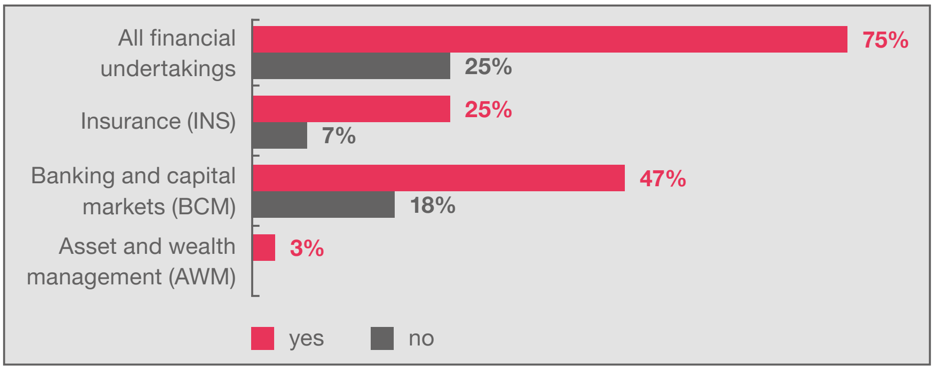
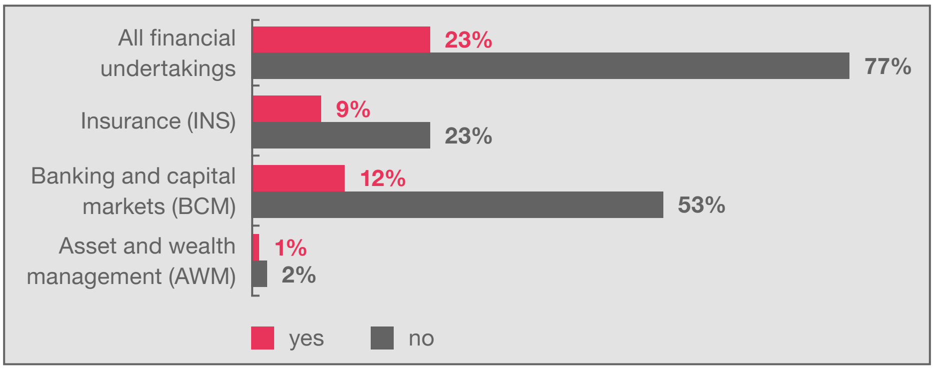


Fig. 8 Voluntary disclosures and/or use of estimates



Only about 23% of the financial institutions analysed made voluntary disclosures and/or used estimates. Given that this was the first year of Taxonomy alignment reporting for the financial sector, the previous year’s figures were not reported in most cases. However, seven companies (7%) did make a voluntary effort to report last year’s Taxonomy compliance figures.

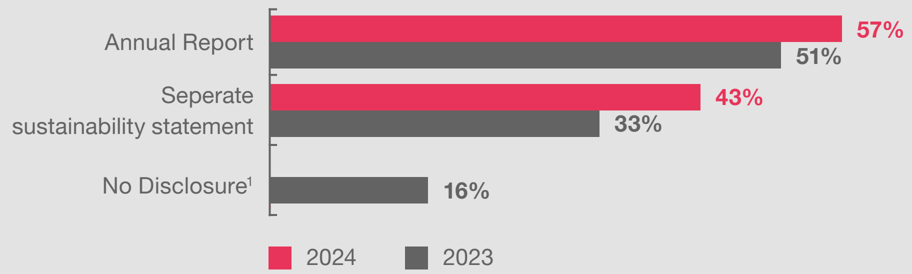
With regard to data sources, 32% of the financial institutions indicated that they used one external data provider, while 23% indicated that they used multiple data sources. However, the majority (45%) did not specify which data sources they had used.

Data availability issues are demonstrated by the fact that the numbers given for environmental objectives 1 (climate change mitigation) and 2 (climate change adaptation) did not match the reported total for Taxonomy-aligned activities in nearly a third (32%) of the analysed company reports. This could be due to data quality issues encountered by the financial institutions' counterparties or overlaps between the two climate objectives. The numbers added up in the remaining reports; however, only one objective was applicable in most of those cases.

The CSRD will gradually enter into force from 2025 for the first group of companies. It will mandate the publication of a sustainability statement, including Taxonomy disclosures in annual reports. In FY 2023, 57% of financial companies reported their EU Taxonomy data in their annual reports, while 43% did so in a separate sustainability statement.

As the Taxonomy currently covers only a limited number of economic sectors and financing activities, the level of Taxonomy alignment is highly dependent on the business model of the financial institution in question. For example, a bank that has a large financing portfolio of SMEs will be less Taxonomy aligned than a bank with a non-SME portfolio, as SME financing is not yet covered by the KPIs. Likewise, the result for an underwriter's KPIs is dependent on the proportion of the underwriter's business in Taxonomy-eligible lines of business.

Fig. 9 Location of EU Taxonomy disclosure



[1] This refers to 23 companies that had not yet published any Taxonomy data at the time of data validation.

Taxonomy data is not yet used by financial institutions for guiding management – this is presumably at least in part due to the low Taxonomy alignment numbers. This is evidenced by the fact that there are very few references to plans to increase Taxonomy alignment in the long term, and that no targets for Taxonomy alignment have been set in the reports. The large discrepancy between levels of Taxonomy eligibility and Taxonomy alignment shows that there is still a long way to go when it comes to the sustainable transition of the economy.

Insurance-specific results

The draft European Commission Notice on implementing the Delegated Disclosure Act – regarding Article 8 of the Taxonomy Regulation – clarified that insurance companies should use the partial premium approach to calculate Taxonomy alignment levels in underwriting. With this approach, only the portion of product premiums covering climate-related risks is considered aligned. This contrasts with the full premium approach, in which the full premiums of products that meet all Taxonomy alignment criteria are considered aligned.

However, the Notice did not answer the question of how to go about calculating levels of Taxonomy eligibility in underwriting, which meant that various different methodologies continued to be used and led to the broad ranges of reported eligibility levels, as set out above. When calculating Taxonomy eligibility, three quarters of the insurance companies analysed used the partial premium approach. Five out of the 31 companies used the full premium approach; the remaining companies did not specify which approach they used. If a market standard evolves in this regard, the reported data will become more comparable and there will be smaller differences in the reported levels of eligibility.

Average aligned: underwriting **2%**

Average eligible: underwriting **22%**

When calculating Taxonomy alignment in underwriting, the majority of insurance companies (84%) followed the Commission Notice and applied the partial premium approach. 10% chose the full premium approach, despite the Commission Notice, and 6% did not state their approach. Three of the insurance companies that chose the partial premium approach used historical damages claim data to calculate the proportion of their premiums that was climate related, while five used historical damage claims data together with pricing data from risk modelling. Two thirds of the insurance companies examined did not specify how they undertook this calculation. The minimum regulatory requirements call for calculations to use estimated data for expected losses, based on historical damages claims and pricing data from risk modelling. It will be important to harmonise the methods used to calculate the proportions of premiums that are climate related, as this is the main determinant for the partial premium approach. The most reliable option for a standardised approach would be to use pricing data (e.g. expected catastrophic loss) to calculate the share.

Question 70 in the Commission Notice, "How should the DNSH and minimum safeguards columns in Annex X be filled?", was another important point and was mostly taken into account by the insurance companies.

For underwriting, overall average Taxonomy alignment is 2%, whereas average eligibility is 22%. The business model of an insurance company has a strong influence on its level of Taxonomy alignment in underwriting. Insurance companies that specialise in legal or liability insurance will have significantly lower Taxonomy alignment due to the mandatory calculation methodology[13]. Meanwhile, companies with a lot of business in "fire and other damage to property insurance" will have comparatively high Taxonomy alignment.

Insurance companies must also report the relevant Taxonomy KPIs for their investment business, in addition to underwriting. In investment, the overall average level of eligibility based on turnover is 17%, whereas the average based on CapEx is 21%. Like in the underwriting business, there are various different approaches and interpretations when calculating investment KPIs. There is no standardised approach to valuation: some companies use book values to ensure alignment with accounting and valuation, while others use the current market value.

Taxonomy-aligned KPIs for insurance companies' investment business comprise the proportion of Taxonomy-aligned exposures to financial and non-financial undertakings, over the total assets covered by the KPI. The KPIs for financial undertakings are close to zero in most cases, which may be due to the fact that Taxonomy alignment reporting was not yet required for financial undertakings last year. For non-financial undertakings, the average turnover-based KPI is 4% and the average CapEx-based KPI is 5%. Taxonomy alignment and Taxonomy eligibility for investment has been calculated based largely on mortgages, although some insurance companies made the effort to obtain relevant data for property and special-purpose vehicle (SPV) financing and implemented appropriate controls.

Average eligible turnover: investment **17%**

Average eligible CapEx: investment **21%**

[13] While all non-life Lines of Business of an insurer can be included in the nominator, only the taxonomy aligned climate shares can be included in the denominator. Therefore all insurance companies with a large share of e.g. legal or liability insurance, which has no climate share and is therefore not Taxonomy eligible will have lower Taxonomy alignment.

Banking-specific results

Average Taxonomy alignment (2% for both turnover and CapEx) is still relatively low across the EU in the first Taxonomy alignment reporting year. The largest contribution to banks' GAR (stock) is the retail business – i.e. mortgages. There are several factors influencing these low levels of Taxonomy alignment. For one, data availability issues limit the extent to which Taxonomy-eligible loans and investments can be assessed as Taxonomy aligned.

In addition, a large part of a credit institution's balance sheet cannot be classified as Taxonomy eligible and is therefore not included in the numerator. For example, a bank that has a large financing portfolio of SMEs will have lower Taxonomy alignment than a bank with a large corporate portfolio, as SME financing is currently not Taxonomy eligible. Furthermore, sovereign exposures are also not Taxonomy eligible, and data availability is very limited for counterparties from local and regional governments. Both of the eligibility KPIs (turnover and CapEx) for credit institutions average 33%.

Average aligned turnover **2%**

Average aligned CapEx **2%**

As is the case with insurance companies, there are varying interpretations of the regulatory requirements, and thus differing methodologies for calculating the banking-specific KPIs. Although the GAR is calculated using a standardised approach, the other proportions required in Template 3 are calculated differently, distorting the relationship between the individual proportions. For example, different banks used different denominators in their calculations, either the total GAR assets throughout or the respective gross carrying amount of each template line item. Divergent approaches can also be found in the inclusion of SPVs in Taxonomy reporting. Including SPVs generally leads to a higher GAR; many of the banks that did not include SPVs stated that this led to their low level of Taxonomy alignment.

In general, it must be considered that the KPIs only provide a limited view of the degree of sustainability of a bank's portfolio. This is because only a limited amount of financing activities can be classified as Taxonomy eligible and there are some inconsistencies in the design of the Taxonomy with regard to sustainability ambitions – e.g. the classification of some nuclear and gas activities as transition activities, or the non-eligibility of SME financing. In the medium term, it can be expected that an increase in data availability through CSRD reporting will lead to increased GARs for banks.

Average eligible turnover **33%**

Average eligible CapEx **33%**

3. Taxonomy reporting in the non-financial sector

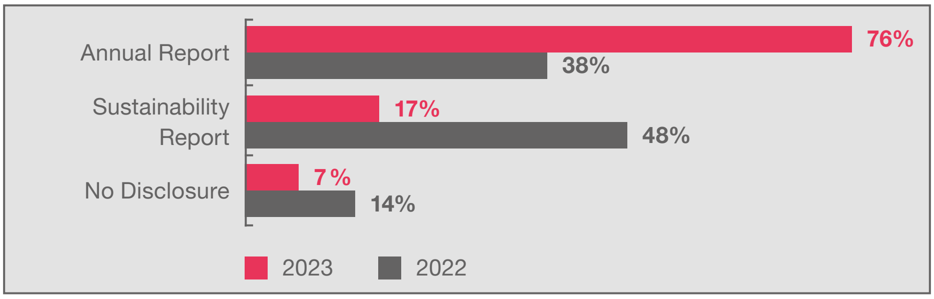
Location of Taxonomy disclosure

In 2023, more than three quarter of non-financial companies made their Taxonomy disclosures directly in their annual reports; 17% did so in a separate sustainability report. In 2022, this situation was reversed, with only approximately half of the companies disclosing Taxonomy information in a separate sustainability report and 38% doing so in their annual report. From 2022 to 2023, the number of companies not disclosing EU Taxonomy data decreased by 50%[14].

Use of the mandatory KPI template remains the same as in the previous year

It was found that the percentage of non-financial companies using the mandatory KPI template in Annex II of Delegated Regulation 2021/2178 to report their Taxonomy-eligible and Taxonomy-aligned turnover, CapEx and OpEx has remained almost unchanged since last year. Of the 530 companies analysed this year, 67% (66% last year) used the mandatory KPI templates. An additional 20% (the same as last year) disclosed the KPIs using a template that had minor changes to the prescribed format, including differing column names or with some of the columns omitted. The remainder of the companies did not report their KPIs in the templates published by the European Commission, even though doing so is mandatory.

Fig. 10 Location of EU Taxonomy disclosure of non-financial companies



The revised Delegated Regulation 2021/2178 provided an additional KPI template, in Annex XII, for disclosure of gas and nuclear activities[15]. Only 36% of non-financial companies made use of this additional table to report on the presence or absence of these economic activities.

However, economic activities for objective 1 (climate change mitigation) and objective 2 (climate change adaptation) were also published, along with corresponding TSC and details on minimum safeguards. New uncertainties thus arose from these new disclosure obligations.

Additional support and new uncertainties surrounding interpretation

In past years, there were many uncertainties surrounding the interpretation of the TSC across all industries. The European Commission therefore published additional FAQs at the end of 2023 to help companies interpret and analyse their data[16]. Comparative data and approaches across industries from the FY 2022 Taxonomy reports also assisted companies in preparing their FY 2023 reports.

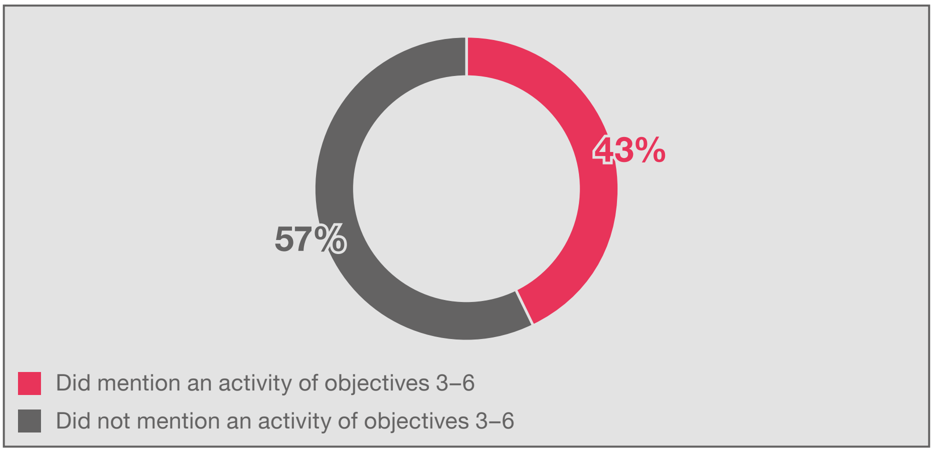
[14] Non-disclosures were not investigated further, but non-availability of information may be due to differing financial years and hence, no availability of disclosures.

[15] Commission Delegated Regulation (EU) 2022/1214 of 9 March 2022, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32022R1214

[16] European Commission (December 2023), Draft Commission notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act under Article 8 of the EU taxonomy Regulation on the reporting of taxonomy-eligible and Taxonomy-aligned economic activities and assets (approved in principle), https://ec.europa.eu/finance/docs/law/231221-draft-commission-notice-eu-taxonomy-reporting-financials_en.pdf

Reporting on environmental objectives 3 to 6

Fig. 11 Reporting on objectives 3 to 6



The new Delegated Act on environmental objectives 3 to 6 was published on 13 June 2023[17], expanding the reporting requirements for the EU Taxonomy. It poses a challenge for companies, as they already faced difficulties reporting on the first two climate objectives, namely climate change mitigation and climate change adaptation. The analysis required, and the effort that may be necessary for implementation, will further increase with the new environmental objectives. Like objectives 1 and 2, the Delegated Act on objectives 3 to 6 includes separate annexes for each objective, defining the economic activities and technical screening criteria.

The four new objectives are sustainable use of water and marine resources, the transition to a circular economy, pollution prevention and control, and protection and restoration of biodiversity and ecosystems. The new delegated acts came into effect on 1 January 2024. Reporting entities are required to report on all six environmental objectives for the 2023 financial year. However, simplifications have been provided for the first reporting period, with full Taxonomy disclosure not required until the 2024 financial year. For the 2023 financial year, companies are required to disclose only the eligible proportion of their turnover, CapEx, and OpEx under environmental objectives 3 to 6 and the newly added economic activities in the Climate Delegated Act.

For the FY 2023, less than half of companies reported any activities from objectives 3 to 6 in their EU Taxonomy disclosures; the majority mentioned none. More companies are expected to report on objectives 3 to 6 once this becomes mandatory for the 2024 financial year.

From objectives 3 to 6, objective 4 (transition to a circular economy) was reported the most across all countries and industries. Activities CE 3.1 (construction of new buildings) and CE 3.2 (renovation of existing buildings) were particularly well represented. Objective 3 (sustainable use and protection of water and marine resources) and objective 5 (pollution prevention and control) were reported less frequently, while disclosures on objective 6 (protection and restoration of biodiversity and ecosystems) were almost non-existent.

Turnover, CapEx and OpEx

The companies examined for this study represent industries that are greatly affected by the Taxonomy in relation to the turnover KPI (e.g. Real Estate), but also industries that are less affected by environmental objectives 1 and 2 (e.g. Retail & Consumer). Across all industries, the average reported Taxonomy-eligible proportion of turnover was 30%, while average Taxonomy-aligned turnover was only 9%. Nonetheless, both of these figures have increased compared to the FY 2022 averages (Eligibility: 26%; alignment: 7%).

The wide variation in reported eligibility between industries is related to the limited scope of economic activities reflected. The Taxonomy still does not cover all business sectors to the same extent, so a company's level of eligibility in the turnover KPI varies depending on its core business activities (i.e. where it generates its turnover).

[17] European Commission (June 2023), Commission notice on the interpretation and implementation of certain legal provisions of the EU Taxonomy Regulation and links to the Sustainable Finance Disclosure Regulation, https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52023XC0616(01)

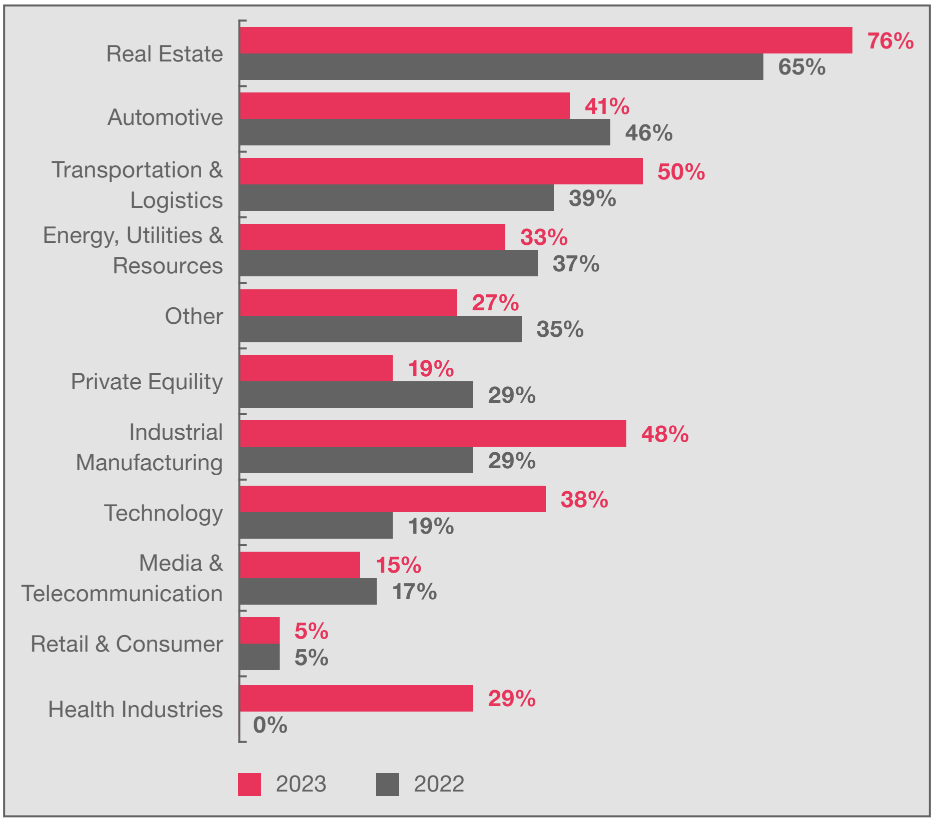
Development and sale of buildings and ownership of buildings (including building rental) are the main turnover-generating activities of the Real Estate industry. These activities are both included in the Taxonomy under environmental objectives 1 and 2, as well as in the new objective 4 (transition to a circular economy), and are thus eligible. Consequently, companies active in this area can achieve high percentages of Taxonomy-eligible turnover. The same applies to the Automotive industry: the manufacture and sale of vehicles is generally Taxonomy eligible, regardless of the powertrain technology used (e.g. internal combustion engines, electric or hybrid) or the associated emissions. Additionally, the new activity 5.4 (sale of spare parts) under objective 4 (transition to a circular economy) is highly relevant for the Automotive industry, and so a high percentage of Taxonomy-eligible turnover can generally be expected. In contrast, the core business of industries such as Retail is still largely not reflected in the Taxonomy low percentages of Taxonomy-eligible turnover.

Turnover

For turnover, average Taxonomy eligibility across all industries was 30%. The first two environmental objectives focus on the climate. Climate change mitigation affects sectors that, according to the European Commission, are responsible for the majority of greenhouse gas emissions. It is important to note that the overall percentages also include activities under objectives 3 to 6 now that additional eligibility reporting has been introduced. Industries that have not identified Taxonomy-eligible turnover, and therefore have no Taxonomy-aligned turnover because they are not yet covered by the Taxonomy, may still be able to report eligible and aligned CapEx and/or OpEx.

The highest average eligible proportions of turnover were reported by the Real Estate[18], Transportation and Logistics, Industrial Manufacturing, and Automotive[19] industries. The lowest average eligible proportion of turnover was reported by the Retail & Consumer and the Media & Telecommunication industries. The core business of the Retail & Consumer industry is rarely covered by new environmental objectives, so its low level of Taxonomy-eligible turnover was not surprising. However, with the addition of objectives 3 to 6, as well as the new activities for objectives 1 and 2, some industries were able to achieve significant increases in eligibility. The Health Industries were able to increase their eligible proportion of turnover from less than on average 1% in FY 2022[20] to 29% in FY 2023. This specific increase is most likely due to the new objective 5 (pollution prevention and control), which largely affected pharmaceutical companies in the Health sector.

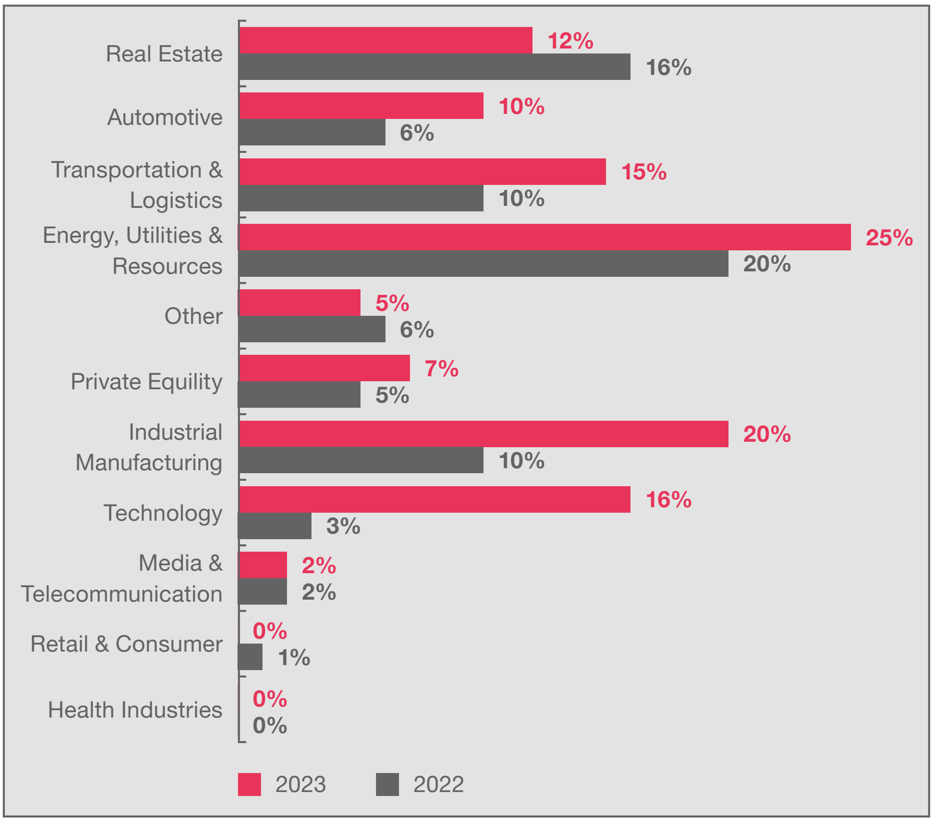
Fig. 12 Average Taxonomy eligible turnover



[18] Also includes construction services. Average eligible turnover increases if construction services are excluded.
[19] Also includes suppliers. Average eligible turnover increases significantly if suppliers are excluded.
[20] The statistic for Health Industries is given as 0% due to rounding.

Reported Taxonomy alignment on turnover was significantly lower, averaging 9% across all industries. Nonetheless, this is a slight increase from FY 2022 (average 7%). Not all the industries with the highest average eligible turnover had the highest average alignment. The highest turnover alignment was in the Energy, Utilities & Resources, the Industrial Manufacturing, and the Technology industries. In comparison to FY 2022, almost all industries reported an increase in Taxonomy alignment. Overall, Real Estate and Industrial Manufacturing are still the top industries in terms of both Taxonomy-eligible and Taxonomy-aligned turnover. The lowest average Taxonomy alignment was in the Health Industries and the Retail & Consumer industry, both of which reported alignment of less than 1%.

Fig. 13 Average Taxonomy aligned turnover



Some industries have a very large gap between eligible and aligned turnover. The results for Real Estate were particularly striking: the gap between eligible and aligned turnover was 64 percentage points[21]. The Automotive industry had a gap of 31 percentage points[22]. Even though the Health Industries reported an increase in Taxonomy eligibility to 29%, Taxonomy alignment was still below 1%.

The most widely reported activities for eligible and aligned turnover across all countries were Manufacturing, Transport, Construction and Real Estate activities. Widespread economic activities included activities 3.1 (manufacture of renewable energy technologies), 3.5 (manufacture of energy efficiency equipment for buildings) and 3.6 (manufacture of low carbon technologies) in Manufacturing, activity 6.5 (transport by motorbikes, passenger cars and light commercial vehicles) in Transport, and activity 7.1 (construction of new buildings) in Real Estate.

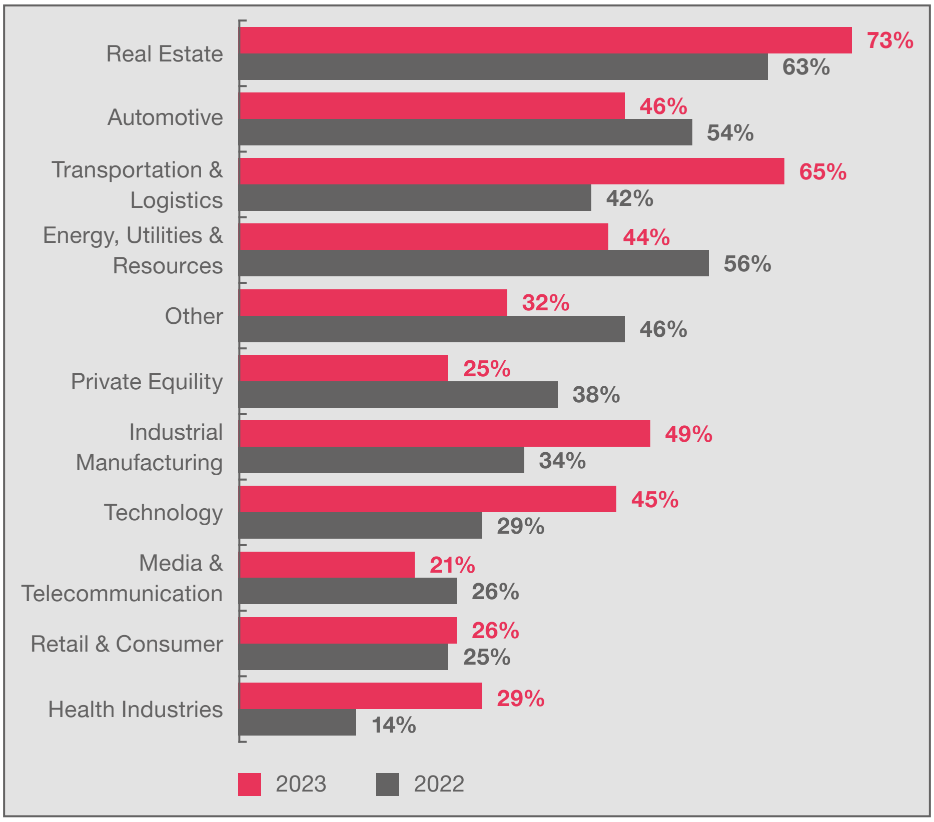
Average eligible turnover **30%** | Average aligned turnover **9%**

[21] The gap is even larger when construction services are excluded.
[22] The gap is even larger when suppliers are excluded.

CapEx

Total average CapEx eligibility was 37% across all industries. All 11 industries reported at least 21% average eligible CapEx. Total average eligible CapEx stayed the same between FY 2022 and FY 2023, while total average aligned CapEx increased slightly, from 10% to 12%. The highest average eligible proportions of CapEx were once again reported by the Real Estate, the Transportation & Logistics, Industrial Manufacturing, and the Automotive industries. The lowest average eligible proportions of CapEx were reported by the Media & Telecommunication industry, Private Equity, and the Retail & Consumer industry.

Fig. 14 Average Taxonomy eligible CapEx

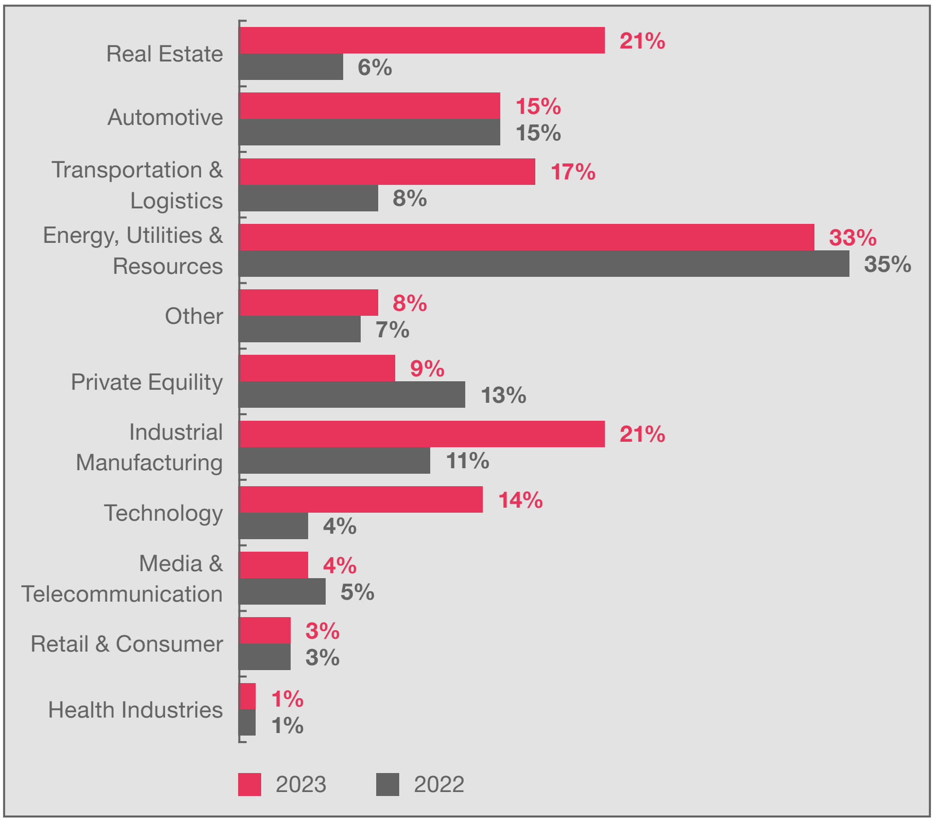


Percentages were lower when it came to Taxonomy alignment. The average aligned proportion of CapEx across all industries was 12%. Broken down by industry, the highest average level of CapEx alignment was in the Energy, Utilities & Resources industry, followed by Real Estate and Industrial Manufacturing. The lowest average proportions were reported by the Health Industries, Retail & Consumer, and Media & Telecommunication industry, all of which were below 5%. The percentages for the Retail & Consumer industry and Health Industries have not changed from FY 2022, but the for the Media & Telecommunications industry alignment decreased by 1 percentage point. Noticeable is that the Technology industry – which had one of the lowest levels of alignment in FY 2022, at just 4% – was able to increase their alignment by 10 percentage points in FY 2023.

Some industries had particularly large gaps between eligible and aligned CapEx. As with turnover, the Real Estate and Automotive industries were particularly striking in this regard: the gap was 52 percentage points in the Real Estate industry and 31 percentage points in the Automotive industry, while the Transportation & Logistics industry also had a large gap, of 48 percentage points.

The most widely reported economic activities across all countries were from the Transport, Energy, and Construction and Real Estate industries. Among them were activities 4.1 (electricity generation using solar photovoltaic technology), 6.5 (transport by motorbikes, passenger cars and light commercial vehicles), 7.3 (installation, maintenance and repair of instruments and devices for measuring, regulation and controlling energy performance of buildings) and 7.7 (acquisition and ownership of buildings).

Fig. 15 Average Taxonomy aligned CapEx



Average eligible CapEx **37%**

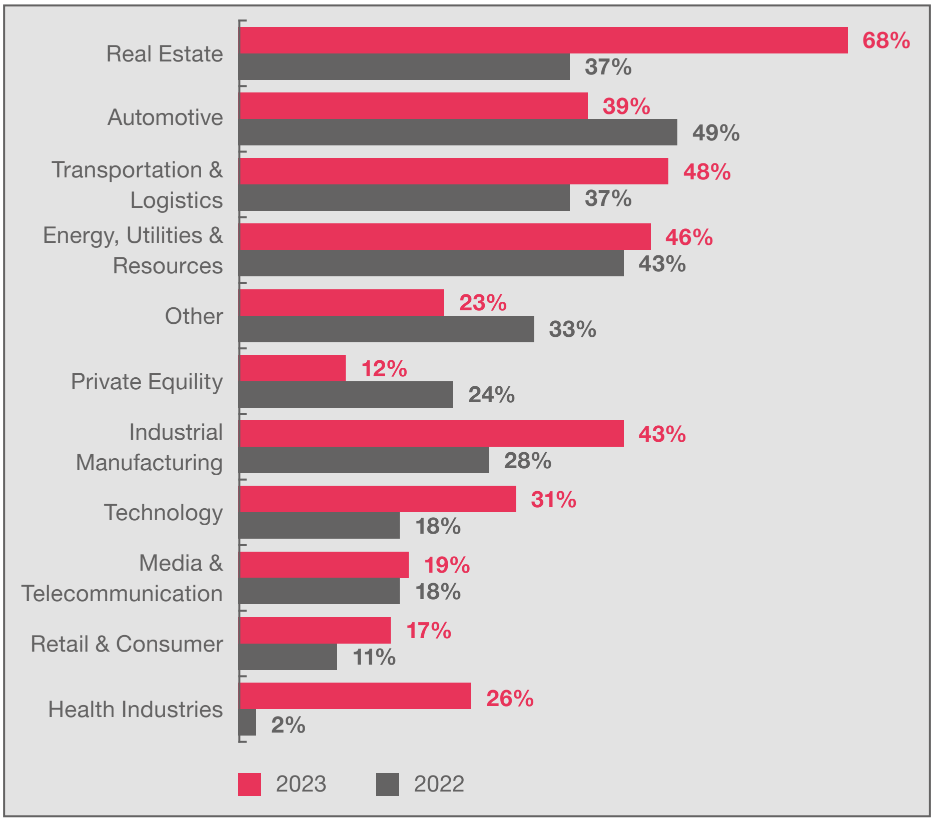
Average aligned CapEx **12%**

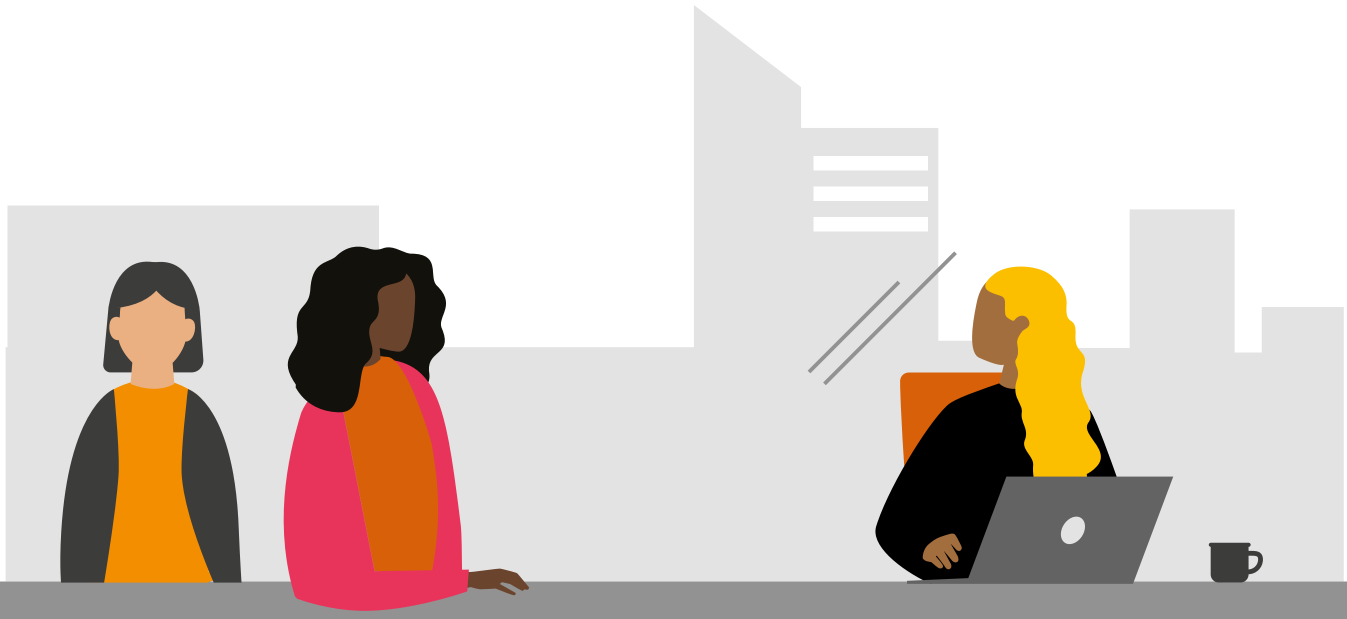
OpEx

Total average OpEx eligibility across all industries increased from 27% (FY 2022) to 30% (FY 2023), while the percentages for individual industries ranged from 12% to 68%. The field was dominated by the Real Estate industry and the Transportation & Logistics industry, which have overtaken the Automotive industry and the Energy, Utilities & Resources industry since the last reporting year. However, the Energy, Utilities & Resources industry remains in the top 3, closely followed by the Industrial Manufacturing industry.

The lowest average levels of eligible OpEx were reported by the Private Equity and Retail & Consumer industries. Here it is notable that although OpEx eligibility in the Private Equity industry has halved compared to last year, the Health Industries made a significant increase of 24 percentage points, thus moving from the lowest average eligible OpEx in FY 2022 to a midfield position among the industries.

Fig. 16 Average Taxonomy eligible OpEx



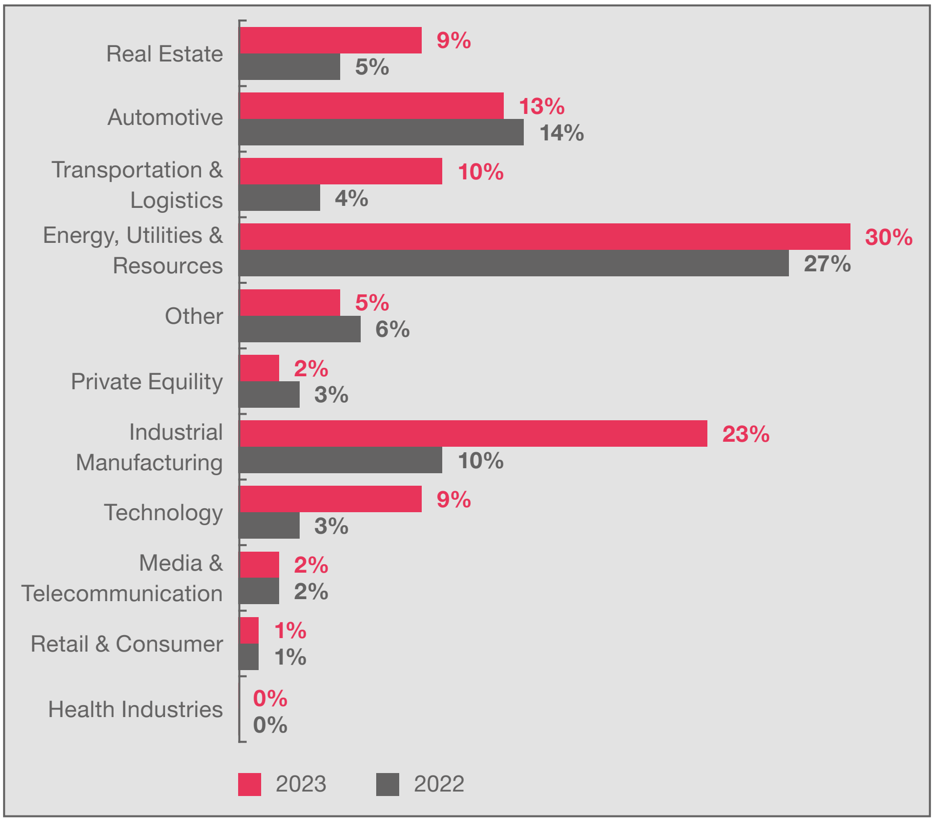


Total average OpEx alignment across all industries increased slightly from 8% (FY 2022) to 9% (FY2023). The top three industries were the same as last year, namely the Energy, Utilities & Resources, Industrial Manufacturing, and Automotive industries. Similarly, the lowest average aligned proportions of OpEx were reported by the same industries as last year: the Health Industries and the Retail & Consumer industry, both under 2%.

Looking at average aligned OpEx, there have been significant changes in some industries between FY 2022 and FY 2023. Alignment in Industrial Manufacturing, Transportation & Logistics, and Technology has more than doubled, and has almost doubled in Real Estate. These spikes may be the result of increased usage of systems and tools to support data aggregation, quality and availability, or due to companies no longer relying on estimates.

Clear differences can be observed when Taxonomy alignment is compared to eligibility, with gaps ranging from 10 to 59 percentage points. The Real Estate and Transportation & Logistics industries in particular reported significant differences of 59 and 38 percentage points, respectively. Possible explanations include a generally better understanding of TSC and minimum safeguard requirements thanks to the FAQs, knowledge sharing within industries and across companies, and better data availability.

Fig. 17 Average Taxonomy aligned OpEx



As with turnover and CapEx, the most widely reported economic activities across all countries were from the Transport and Construction and Real Estate industries. The activities reported the most were 6.5 (transport by motorbikes, passenger cars and light commercial vehicles), 7.2 (renovation of existing buildings) and 7.7 (acquisition and ownership of buildings). Disclosures on activities 8.1 (data processing, hosting and related activities) and 3.3 (manufacture of low-carbon technologies for transport) were widespread. Finally, activity 3.6 (manufacture of other low-carbon technologies) was also widely reported, primarily by the Industrial Manufacturing industry.

Average eligible OpEx **30%**

Average aligned OpEx **9%**

C Conclusions and outlook

As the findings of this study demonstrate, advances are being made in the implementation of the EU Taxonomy Regulation, though the nature and quality of reporting still varies widely. In FY 2023, the homogeneity of reported data has increased in both the financial and the non-financial sectors compared to last year. While there are persistent data quality and availability issues in the financial sector, the quality of the data reported by non-financial companies seems to be increased. Nevertheless, there are differing interpretations of the TSC, sometimes even within a single industry, leading to outliers in the reported Taxonomy alignment KPIs.

Furthermore, in both the financial and the non-financial sectors, better practice in the market is driving standardisation of reporting and the improvement of internal processes. However, there is still a long way to go, as diverse methodologies remain in use. The Commission Notice of December 2023 has sought to bring clarity to some questions around interpretation; at the same time, it has left others open. This Notice also came late in the game and, based on our data, has not yet been fully implemented by most companies. Its effects will therefore mostly not be seen until the next reporting cycle.

Non-financial companies across all industries have resorted to approximation in the reporting of KPIs, especially in comparison to FY 2022. This trend allows better comparability of performance over time. However, despite this progress, non-financial companies continue to face data challenges, particularly due to the inclusion of the newly added environmental objectives 3 to 6 and the additional economic activities for objectives 1 and 2. While the current trend has stabilised, it is important to note that the current level of Taxonomy alignment in non-financial companies remains very low and has not significantly improved. Overall, uncertainties around interpretation and disclosure processes have been reduced. However, companies are still working on redefining internal processes and reallocating resources for Taxonomy reporting purposes. The vast majority of non-financial companies analysed in this study have so far met their obligations relating to quantitative Taxonomy disclosures. Nonetheless, there are still a few companies that are not adhering to the requirements, such as using the mandatory templates or providing comparative figures. Another major reason for the low levels of alignment is that data may be available but the criteria were simply not met, which shows how far we still have to go in our transition to a sustainable economy.

In the financial sector, the homogeneity of Taxonomy eligibility reporting has increased. Taxonomy alignment is still very low, which is attributable to several factors. On the one hand, there are persistent data quality and availability issues. Increased efforts by companies to obtain the relevant data are needed, and a wide variety of methodologies remain in use owing to a lack of regulatory clarity. On the other hand, the low levels of alignment also demonstrate that there is still a long way to go before the ambitious criteria set by the EU Taxonomy are met and the green transition of the economy can be accelerated.

Taxonomy alignment in financial undertakings is still too low to be used for guiding management. One aspect to consider is that the reported level of alignment is highly dependent on the company's business model, given the limited scope of application of the Taxonomy eligibility criteria for financial undertakings and the calculation methodologies. Financial companies have therefore not yet set explicit goals for increasing their Taxonomy alignment in the future. However, doing so is indispensable if the Taxonomy is to fulfil its purpose of redirecting financial flows to sustainable economic activities.

The Taxonomy Regulation has the potential to provide relevant metrics for net-zero transition plans in both financial and non-financial companies; however, it is essential that the applied methodologies converge, and that data availability and quality significantly improve so that today's low alignment can rise to levels of relevance for decision-making. It is likely that industry associations will produce standards for Taxonomy reporting in the near future. Such guidelines will help minimise differences in interpretation, or even eliminate them altogether. It is also expected that interpretations will harmonise over time, as they did following the introduction of IFRS 15 and 16.

The introduction of mandatory audits in FY 2024 is expected to have a substantial impact on both financial and non-financial companies, and on the overall quality of disclosures. Additionally, the scope of the CSRD and the EU Taxonomy will expand, impacting a greater number of companies. While these newly affected companies will benefit from the guidance provided by the last three years' worth of reports, they will face the challenge of having no transition phase. As a result, they will be required to report on all requirements without any exemptions – including being subject to mandatory audits. The extended ESG database provided by the CSRD will help financial and non-financial companies to understand the sustainability activities of their counterparties better and thus improve their own Taxonomy reporting. This is also very likely to lead to increases in Taxonomy alignment overall.

Although Taxonomy ratios currently only serve as a value for transparency, they could potentially be used to set more specific incentives in the future. For example, companies might be required to meet certain minimum Taxonomy ratios in order to qualify as bidders in public procurement projects or a green supporting factor in lending may be introduced.

Based on our findings, we believe that there are three main considerations related to the EU Taxonomy going forward:

1. Strategic need to change business practices: companies may need to modify their business practices to align with the Taxonomy's criteria. This could involve investment in more environmentally friendly technologies and processes, or changes in supply chains and product offerings to increase alignment.

2. Significance for investors and financial markets: investors and financial markets are increasingly paying attention to companies' environmental sustainability, as it could have a growing impact on financial performance and long-term success. Companies able to enhance their environmental sustainability may be better able to attract capital and generate long-term value.

3. Opportunities for innovation and competitiveness: the requirements of the Taxonomy may motivate companies to develop innovative solutions to increase their environmental sustainability. Companies that invest in sustainable technologies and practices at an early stage are well placed to gain a competitive advantage and unlock new market opportunities.

In summary, the development of the EU Taxonomy for businesses means a heightened focus on environmental sustainability and increased reporting obligations, but also opportunities for innovation and competitiveness. It is important for companies to monitor these developments closely and modify their business practices accordingly to ensure long-term success.

Appendix

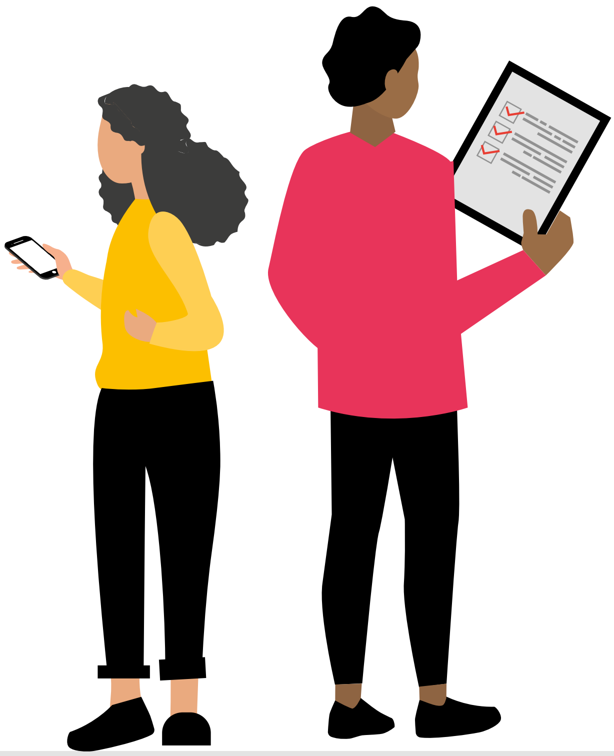
1. Methodology

This study aims to provide insights into the current state of implementation of the EU Taxonomy Regulation by analysing the disclosed Taxonomy KPIs (i.e. the proportions of relevant activities which are Taxonomy eligible/Taxonomy aligned) of listed financial undertakings and non-financial companies that fall within the scope of the regulation. The analysis is based on annual and sustainability reports for FY 2023 published by European financial undertakings and non-financial companies up to the end of April 2024. Companies that were analysed were based in Belgium, Finland, France, Germany, Ireland (non-financial sector only), Italy, Luxembourg (non-financial sector only), Malta, the Netherlands, Poland, Spain (financial sector only) and Sweden.[23] Selected indices were examined for each country.

Analysis for the non-financial sector was divided into the following industries: Automotive; Energy, Utilities & Resources; Health Industries; Industrial Manufacturing; Private Equity; Retail & Consumer; Technology; Media & Telecommunication; Transportation & Logistics; Real Estate; and Other.

The data in the study is based on publicly available information from the companies' own reports. Analysis was performed on reports from 530 non-financial companies in 12 countries. The dominant countries for non-financial undertakings were Germany (152 reports), France (90 reports) and Poland (84 reports). It should be noted that in our analysis of average Taxonomy eligibility and alignment for the three KPIs, non-disclosures by non-financial undertakings were given a value of 0%. It should also be remembered that companies can be listed on stock exchanges in multiple countries.

For the financial sector, 97 reports were examined. The largest samples were from Germany (21 reports), Italy (17 reports) and Poland (13 reports). Financial sector reports came from a variety of industries. Banking and Capital Markets made up the largest proportion (65%), while around a third (32%) of the companies analysed are in the insurance sector. The number of Asset and Wealth Management companies was the lowest, making up 3% of the total. The ranges of the Taxonomy eligibility and alignment levels given in this study are based on the average national Taxonomy eligibility and alignment levels.

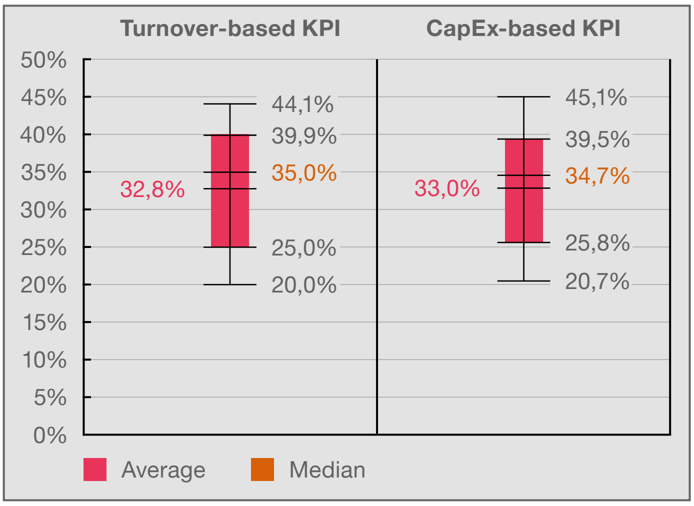


[23] DAX, MDAX, SDAX, IBEX35, GPW, AEX, LUX based, FTSE MIB, Euronext Dublin, CAC40, SBF120, ATX, C25, BEL20, OMXS30, OMX Large Cap and Prime Standard for financial institutions.

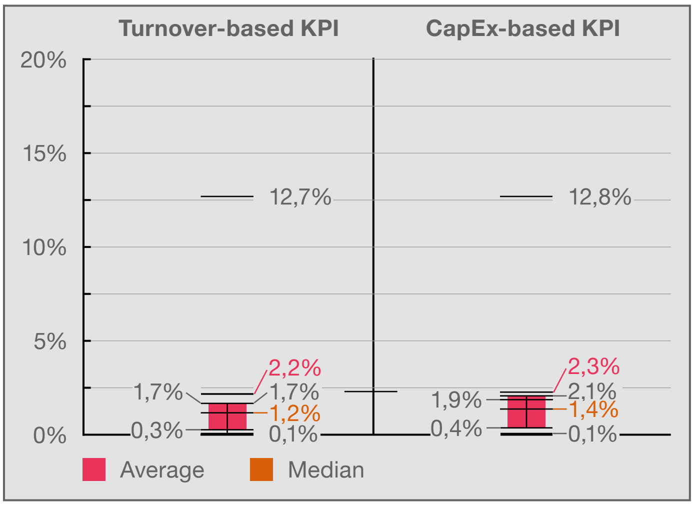
2. Taxonomy reporting in the financial sector – in detail

The boxplot illustrates the researched quota distribution with several key elements. The minimum observed value is represented by the lower end of the whisker, and the maximum observed value is shown by the upper end of the whisker. The box shows the majority of the observed values by country. These elements together demonstrate the central tendency and spread of the data.

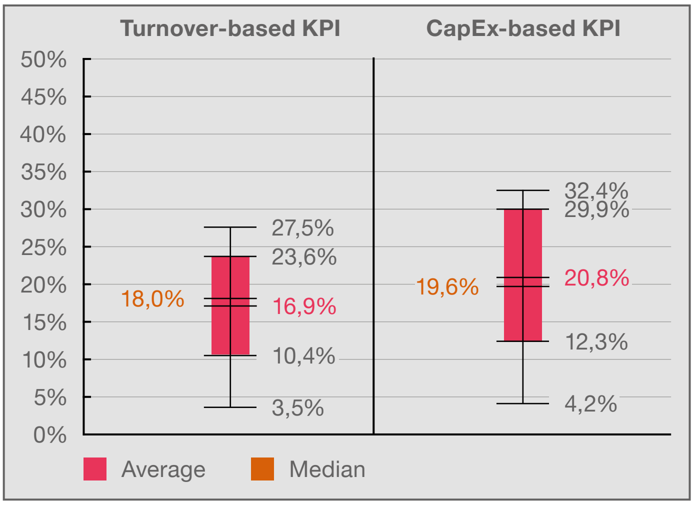
Taxonomy eligibility in the banking sector



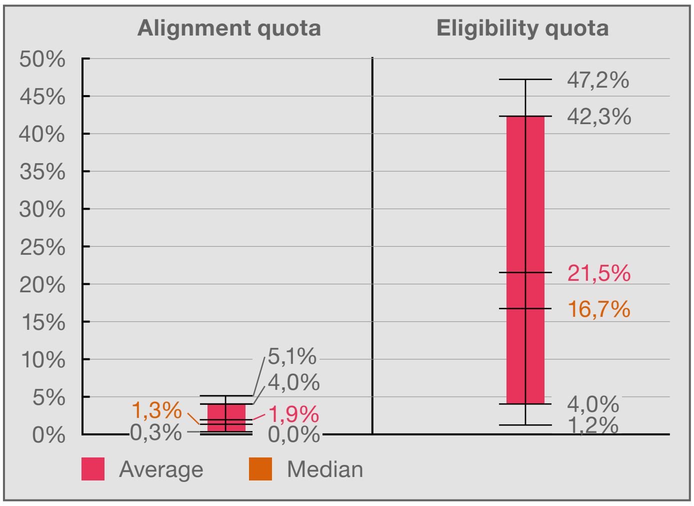
Taxonomy alignment in the banking sector



Taxonomy eligibility in the investment business of the insurance sector



Taxonomy alignment and eligibility quota in the underwriting business of the insurance sector



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