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Unlocking the European taxonomy potential

The European taxonomy is a granular set of criteria that needs to be met in order to qualify an economic activity as sustainable. It is essentially a tool that will have multiple usages. The most important one will certainly be the requirement for non-financial companies, under the scope of the NFRD, to disclose their share of revenue, capex and opex that is aligned with the taxonomy, starting from January 2022 and based on 2021 information for the two climate related objectives. Financial companies will have similar requirements.

The taxonomy can play a pivotal role in the European environmental transition provided it is properly and swiftly implemented. It can indeed fill two important gaps that are currently preventing a quicker transition of the European economy towards a sustainable economy.

First the extent and the timeline of the industrial transformation that is required at an individual company level is usually still unknown. While the taxonomy does not directly address this issue, which is a matter of regulation of the real economy, it does address it indirectly by requiring to disclose the alignment with a granular sustainable target, creating the market incentive to converge to this target.

Second, the absence of ESG standardized, reliable and comparable data that can be shared with all users, hinders the ability to measure performance, analyze risk in a consistent way and take informed decisions on the direction of travel. The Non-Financial Reporting Standard will address this; however, the taxonomy disclosure requirements can be considered, de facto, as a first building block of an ESG reporting standard. It will be mandatory, granular, directly linked to underlying industrial activities and its implementation will require significant investments that need to be leveraged.

There are however three important issues to be addressed in order to achieve a proper implementation of the taxonomy. First, public authorities should plan a progressive implementation, the disclosure of a single alignment number can create an illusion of certainty, while most companies will only be able to produce estimates in 2022. Supervisory bodies and companies need to recognize the underlying uncertainty and be transparent about it, to avoid expectation gaps and what could become a taxonomy washing. Second the taxonomy is currently one sided, it shows what is sustainable today but

doesn't say much about the remaining dimensions of the transition: the targets, when these targets will be reached and the other dimensions of sustainability such as the social impact. It must be put in context. The completion of the taxonomy on the remaining dimensions would also help in building a meaningful picture. Lastly, the SME shouldn't not be excluded, they are part of the journey and should be supported on embarking on this journey.

The taxonomy is not a perfect tool, but it is a tool that we can build on. Both public and private sectors should create the conditions of a swift, controlled and large adoption of the taxonomy. It can be the catalyst of the necessary and urgent transformation of our economies and its operational implementation will also secure the consistency between ESG European policy choices and the reporting standards that will prevail.