

ESMA FINAL REPORT ON ARTICLE 8 OF THE EU TAXONOMY REGULATION

04 March 2021 | UK, Europe
Legal Briefings

On 1 March 2021 the European Securities and Markets Authority (**ESMA**) published its [Final Report](#) on advice under Article 8 of the Taxonomy Regulation. The Final Report outlines the information that non-financial undertakings and asset managers need to provide to comply with their disclosure obligations under the [Non-Financial Reporting Directive](#) (**NFRD**).

The [Taxonomy Regulation](#) came into force on 12 July 2020, and establishes the framework for the EU taxonomy by setting out conditions that economic activities must meet in order to qualify as environmentally sustainable. In so doing, the draft regulation seeks to fulfil its environmental objectives of:

- Climate change mitigation
- Climate change adaptation
- Sustainable use and protection of water and marine resources
- Transition to a circular economy
- Pollution prevention and control
- Protection and restoration of biodiversity and ecosystems

ARTICLE 8 OF THE TAXONOMY REGULATION

Article 8(1) of the Taxonomy Regulation requires organisations covered by the NFRD to include information in their non-financial statements as to how, and the extent to which, their activities are “associated with” environmentally sustainable activities. Under Article 8(2), non-financial undertakings are also required to provide disclosure of three key performance indicators (**KPIs**): turnover, capital expenditure (**CapEx**) and operating expenditure (**OpEx**) related to environmentally sustainable activities.

At present, the NFRD applies to large listed companies, banks and insurance companies with more than 500 employees. However, the European Commission is currently [reviewing the application of the NFRD](#) and considering if the scope should be widened to apply to more companies; all of which will need to conform with Article 8 of the Taxonomy Regulation when it comes into force.

The European Commission is required to adopt, by 1 June 2021, a delegated act specifying the content and presentation of the information to be disclosed under Article 8, including the methodology to be used. Article 27 of the Taxonomy Regulation states that the reporting requirements contained within Article 8 should apply:

- from 1 January 2022, as to climate change mitigation and climate change adaptation; and
- from 1 January 2023, as to the sustainable use and protection of water and marine resources, the transition to a circular economy, pollution prevention and control and the protection and restoration of biodiversity and ecosystems.

ESMA'S FINAL REPORT

The recommendations within the Final Report specify how non-financial undertakings should disclose against the three KPIs set out in Article 8(2) of the Taxonomy Regulation, outlining how each KPI should be calculated.

- The Turnover KPI should be calculated by using the definition of “net turnover” from Article 2(5) of the Accounting Directive as the denominator. The numerator should be calculated by including any turnover which arises from activities which make a substantial contribution to one of more of the environmental objectives contained within the Taxonomy Regulation, and those which do no significant harm to any of the other environmental objectives. For the environmental objective of climate change adaptation, any turnover from an activity which enables other activities to undergo climate change adaptation can be included.

- The CapEx KPI should be calculated by using the additions to tangible and intangible assets during the financial year, including those as a result of acquisitions, as the denominator. The numerator should be calculated by counting costs incurred which relate to assets or processes which meet, or are part of a plan to meet, the criterion of making a substantial contribution to one or more of the environmental objectives, including by meeting the technical screening criteria, the criterion of not doing significant harm to any of the other environmental objectives, including by meeting the technical screening criteria, and the criterion of minimum safeguards.
- The OpEx KPI should be calculated by using the following direct costs as the denominator: research and development, building renovation measures, short-term leases, maintenance and repair, and any other direct expenditures relating to the day-to-day servicing of items of property plant and equipment that are necessary to ensure the continued and effective functioning of such assets. The numerator should be calculated by counting costs incurred which relate to assets or processes which meet, or are part of a plan to meet, the criterion of making a substantial contribution to one or more of the environmental objectives, including by meeting the technical screening criteria, the criterion of not doing significant harm to any of the other environmental objectives, including by meeting the technical screening criteria, and the criterion of minimum safeguards.

In addition to the above KPIs, ESMA recommends that additional disclosures should accompany the KPIs, including but not limited to the accounting policy used, an assessment of Taxonomy-alignment and the KPIs outlined in context to previous years. ESMA has also recommended that a standardised template be used for reporting under Article 8 to increase transparency during these disclosures.

ESMA has also proposed how asset managers should disclose against the KPIs including the methodology to be applied, as well as recommending the development of a coefficient methodology to assess Taxonomy-alignment of investments in investee companies that do not report under the NFRD.

Along with ESMA, the [European Banking Authority](#) and [European Insurance and Occupational Pensions Association](#) have also published proposals as requested by the European Commission.

UK AND BREXIT

As the Brexit transition period ended on 31 December 2020, the UK is not obligated to implement the eventual delegated regulation in relation to Article 8 when it comes into force at the end of the legislative procedure. The UK has however indicated that it may decide to align itself with the EU with regard to the Taxonomy Regulation, but such a decision would only be taken once the relevant delegated regulations are finalised.

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



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