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From: General Secretariat of the Council
To: Delegations

Subject: Implications of the EU taxonomy for the transition to a sustainable economy

- Information from the Czech delegation, supported by the Bulgarian, Greek, Cyprus, Hungarian, Romanian and Slovak delegations

Delegations will find in the Annex an information note from the Czech delegation, supported by the Bulgarian, Greek, Cyprus, Hungarian, Romanian and Slovak delegations on the above subject, to be dealt with under ‘Any other business’ at the Council (Environment) meeting on 10 June 2021.

Implications of the EU taxonomy for the transition to a sustainable economy**- Information from the Czech delegation, supported by the Bulgarian, Greek, Cyprus, Hungarian, Romanian and Slovak delegations -**

The EU taxonomy has been developed as a catalogue of fully environmentally sustainable economic activities, providing a common language for sustainable finance policies and aiming to stimulate private finance participation in order to facilitate the transition to a sustainable and climate-neutral economy by 2050. Within the current legislative framework, the taxonomy provides a transparency tool in order to prevent greenwashing when ‘sustainable’ or ‘green’ financial products and services are established and promoted. Along with the recently proposed Corporate Sustainability Reporting Directive (revision of the Non-Financial Reporting Directive), it will also make companies’ alignment with the EU’s sustainability and climate goals more visible and transparent.

The taxonomy facilitates the identification of activities which make a substantial positive contribution to environmental objectives, while doing no significant harm in other environmental areas and fulfilling minimum social safeguards. There are several limitations to the current taxonomy framework:

- The taxonomy criteria ultimately allow only a one-size-fits-all approach which has already proved to be controversial in relation to climate change mitigation. The interpretation of the transitional activities for climate change mitigation has been too narrow, and has not allowed for any different pathways to decarbonisation.
- Even though the criteria are being developed to be science-based and technology neutral, several essential thresholds are based on indicators and metrics that do not take into account technological and economic feasibility, which still results in the exclusion of some transitional activities.

- The concept of defining only sustainable activities which actively contribute to environmental objectives is broadly misunderstood by the public, policymakers and businesses including the financial sector. Anything that is not included in the taxonomy is commonly considered to be environmentally harmful. Even though this is not the case from a legal point of view, the practical consequences for financing and insurance options may be detrimental in many areas, where an individual approach and specific assessment is needed.

We are of the opinion that these shortcomings should be fixed and that the taxonomy should be applied only as a transparency tool. However, the taxonomy is progressively becoming a new standard for EU policies, through its gradual implementation by the European Commission. We feel the need to initiate a broad discussion on its application outside of the original scope. There are certain implications which arise from the current developments:

- We fully acknowledge the need to stop financing environmentally harmful activities in line with the ‘do no harm’ principle of the European Green Deal and the ‘do no significant harm’ principle of the Taxonomy Regulation. However, a proper discussion about the limitations of using the taxonomy criteria as a reference system for public financing is essential. Public sector financing differs in many respects from private financing. The taxonomy was not developed with a view to becoming the sole standard for financing, nor the standard for legislation.
- There is an inconsistency in the way that the Commission understands and applies the ‘do no significant harm’ criteria and in some cases, the substantial contribution becomes the mandatory threshold, leaving some investments with positive environmental impacts behind.
- It is a widely acknowledged shortcoming of the taxonomy that it is not a complete tool for the transition and that it cannot serve as an indicator of the transition. The transition, from the perspective of a Member State, is a matter of complex interdependencies between the economy and public policies within a specific time and context, and with a specific path-dependency.

- Transitional investments are needed in order to fulfil the ambitious mitigation targets. Individual approaches taken by the Member States should be explained and understood, but individual approaches cannot be implemented without real technological neutrality and sovereignty over the energy mix. The transition pathways are and will be different in different Member States. We fully respect our environmental obligations, but we will not be able to meet them without both private and public transitional investments.

We call on the European Commission and the Member States:

- to discuss, at appropriate expert level as well as in political forums, the limitations of the taxonomy and its ‘do no significant harm’ criteria as a reference system for EU financing;
- to acknowledge that the transition cannot be achieved with a one-size-fits-all approach and that the taxonomy needs to be a flexible tool for all transitional pathways;
- to assess the consequences of the practical application of the taxonomy, which is already broader than originally intended;
- to ensure that the taxonomy criteria are science-based, technologically neutral, but also feasible given the state of the art in different sectors and Member States.
