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Towards sustainable investments in the ecological transition: the green taxonomy of the European Union

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The adoption in December 2019 of the regulation on the taxonomy of green activities^{[1](#)} opens an ambitious project to achieve a European benchmark for sustainable finance. As technical discussions begin to determine the technical thresholds and criteria that will make it possible to define "sustainable", "transitioning" and "enabling" activities, it will be necessary to ensure, on the one hand, that these criteria are based on long-term decarbonisation pathways that are systemic, robust, transparent and shared by all stakeholders and, on the other hand, that they are well aligned with the objective of climate neutrality by 2050, which the EU is preparing to enshrine in its first climate law.

A common benchmark for sustainability

The establishment of a framework to foster sustainable investments, or "green taxonomy", is an innovative initiative that illustrates the pioneering role of the European Union on sustainable finance. It aims to provide a common definition of sustainable economic activities in order to increase transparency on financial markets and thus combat greenwashing. Once the technical criteria for classifying activities have been established, it will serve as a basis for assessing the degree of sustainability of a financial asset or an investment portfolio. In the context of the Green Deal, this initiative could also be used to guide the use of European and public budgets in their investment policies. This common benchmark is a true cornerstone of the EU sustainable finance action plan, and will have a wide scope of application; its transformational impact is currently difficult to anticipate, but potentially high if the sustainability of investments becomes a central decision-making criterion for investors.

The thorny issue of criteria definition

Initially, the creation of this taxonomy was aimed primarily at identifying sustainable economic activities taking into account six criteria: climate change mitigation; climate change adaptation; sustainable use and protection of hydrological and marine resources; transition to a circular economy and waste prevention and recycling; pollution prevention and control; and protection of healthy ecosystems. To be considered sustainable, an activity had to both contribute significantly to at least one of these objectives and not cause significant harm to other environmental objectives. Over the course of the European legislative process, other categories of activities considered unsustainable have been added: ² "enabling" activities, such as steel production for wind turbines; and "transitioning" activities, for which there is no economically viable low-carbon solution today. The definition of quantified criteria and thresholds for these types of activities must be achieved before the end of 2020 for the climate change mitigation and adaptation criteria and in 2021 for the other sustainability criteria.

The challenge now is how to define criteria that are robust enough to be in line with long-term environmental objectives. There is of course a risk that criteria that are too loose, particularly for transitioning or enabling activities, will lead to investors being directed towards activities that are not compatible with the objective of carbon neutrality. This is why a few principles have been defined: unsustainable activities must not allow for a lock-in effect (path dependency on technological pathways); enabling activities must have a positive carbon balance over the entire life cycle of the activity; and transitioning activities must not prevent the development of low-carbon solutions and must have emission rates in line with the industry's lowest emitting technology. Nevertheless, a question remains: how to ensure that these definitions are consistent with long-term environmental objectives?

Methodology and governance: the keys to success

The trade-offs on both quantitative and qualitative criteria, far from being trivial, will certainly see sharply contrasting points of view. The methodology and governance associated with the definition of these criteria will therefore be key to achieving sufficiently ambitious results. From a methodological point of view, the definition of sustainable assets will have to be anchored in long-term pathways that are systemic (all sectors) and robust, and compatible with the objective of climate neutrality, thus making it possible to define exit horizons for transitioning activities and to provide long-term perspectives that are transparent and shared by all stakeholders. As for the governance organised around the European Commission, the Sustainable Finance Experts Platform and the Member States' Expert Group, it will have to be sufficiently agile to integrate the progress of the ecological transition, the evolution of regularly updated national energy-climate plans and, more generally, the energy-climate governance process in Europe.

¹ Adoption after agreement was found between the European Parliament and the European Council: <https://www.europarl.europa.eu/news/fr/press-room/20191217IPR69202/de-nouvelles-regles-pour-determiner-quels-investissements-sont-ecologiques>

² <https://eur-lex.europa.eu/legal-content/FR/TXT/?uri=CELEX%3A52018PC0353>

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