Sustainable finance: EU reaches political agreement on a unified EU classification system

The EU will soon have in place a common classification system to encourage private investment in sustainable growth and contribute to a climate neutral economy.

EU ambassadors today endorsed a political agreement reached between Finland’s presidency of the Council and the European Parliament on a EU-wide classification system, or “taxonomy”, which will provide businesses and investors with a common language to identify what economic activities can be considered environmentally sustainable.

The taxonomy will enable investors to re-orient their investments towards more sustainable technologies and businesses. It will be instrumental for the EU to become climate neutral by 2050 and achieve the Paris agreement's 2030 targets. These include a 40% cut in greenhouse gas emissions for which the Commission estimates that the EU has to fill an investment gap of about 180 billion EUR per year.

The goals of the Paris Climate Agreement will not be achieved by using public funds alone. We need the leverage from the whole economy, including financial and capital markets, to support the transition. Today's agreement will be key in helping redirect money to investments in sustainable sectors.

Katri Kulmuni, Finland's minister of finance

At present, there is no common classification system at EU or global level which defines what is an environmentally sustainable economic activity. The proposed regulation is meant to address two challenges:

- reduce fragmentation resulting from market-based initiatives and national practices;
- reduce “greenwashing”, i.e. the practice of marketing financial products as “green” or “sustainable”, when in fact they do not meet basic environmental standards.

The future framework will based on six EU environmental objectives:

1. climate change mitigation;
2. climate change adaptation;
3. sustainable use and protection of water and marine resources;
4. transition to a circular economy;
5. pollution prevention and control; and
6. protection and restauration of biodiversity and ecosystems.

In order to qualify as environmentally sustainable, economic activities will have to fulfil the following requirements:

- contribute substantively to at least one of the six environmental objectives listed above;
- not significantly harm any of the environmental objectives;
- be carried out in compliance with minimum social safeguards;
- comply with specific 'technical screening criteria'.

Investment in coal will not be considered environmentally sustainable. The agreement retains the concept of maintaining a neutral stance in relation to different energy forms, provided that they are low in greenhouse gas emissions. The taxonomy will also include two sub-categories of "enabling" and "transitional" activities. There will be an obligation to disclose for each financial product the proportion invested in those enabling and transitional activities.

On this basis, the Commission will be tasked to establish the actual classification by defining 'technical screening criteria, in the form of delegated acts, for each relevant environmental objective and sector respectively.

The Commission will be assisted by a technical expert group, the "platform on sustainable finance", which will be mandated to provide advice for developing and revising the technical screening criteria as well as reviewing their usability. The platform will also
advise the Commission on the need to address other objectives, and analyse their impact in terms of potential costs and benefits of their application. In addition, the Commission will be advised by an expert group consisting of member states' experts on the appropriateness of the technical screening criteria and the approach the Commission takes regarding these criteria.

The taxonomy for climate change mitigation and climate change adaptation should be established by the end of 2020, in order to ensure its full application by end of 2021. For the four other objectives, the taxonomy should be established by the end of 2021 for an application by the end of 2022.

**Next steps:**

The new rules will be formally adopted by the Council and the Parliament following the legal and linguistic revision of the text, pursuant to the "early second reading agreement" procedure.

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