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EU Taxonomy 2022

The transformation of non-financial reporting



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EU Taxonomy 2022

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Preface

Dear Readers,

Since 2017, it has been necessary for large European public interest entities with an average number of more than 500 employees over the course of a financial year to supplement their (group) management reports with a non-financial (group) statement. This statement must contain information regarding environmental, social and employee matters as well as respect for human rights and anti-corruption and anti-bribery affairs.

For these entities that are obligated to provide non-financial reporting, the European Union published an additional regulation in 2020: the EU Taxonomy (Taxonomy Regulation – Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment). For non-financial statements as well as separate non-financial reports published after 1 January 2022, entities subject to a reporting requirement must start incorporating the disclosures pursuant to Article 8 of the EU Taxonomy into their non-financial reporting.

The EU Taxonomy is the focus of this study. The Taxonomy Regulation provides the framework for the EU's new classification system regarding ecologically sustainable ("green") economic activities and the associated reporting requirement for the undertakings concerned. It calls for the reporting of "green" key figures: "green" turnover, "green" capital expenditure and "green" operating expenditure. We are currently waiting on further details to clarify and specify these three key figures.

Furthermore, legal acts supplementing the EU Taxonomy were published in the Official Journal of the EU in December 2021: Commission Delegated Regulation (EU) 2021/2178 specifying the content and presentation of information concerning environmentally sustainable economic activities, and specifying the methodology to comply with that disclosure obligation, as well as Commission Delegated Regulation (EU) 2021/2139 establishing the technical screening criteria for the first two environmental objectives of "climate change mitigation" and "climate change adaptation".

An exempting provision for the initial reporting year meant it was possible to limit disclosures to "taxonomy-eligible" activities. This means, among other ramifications, that such taxonomy-eligible activities do not necessarily have to meet the specified technical criteria for "green" turnover. Nevertheless, there was still an obligation to identify activities of relevance under the Taxonomy and to disclose them accordingly. In the second reporting year, the taxonomy-eligible activities previously disclosed are to be assessed in order to determine the degree to which they fulfil the specified criteria and in order to align such activities with the Taxonomy.

Undertakings within the scope of application of the Taxonomy Regulation must therefore immediately analyse their economic activities based on the descriptions of the delegated regulation on technical screening criteria.

If the changes planned to take place through the enactment of the Corporate Sustainability Reporting Directive (CSRD) are implemented, these key figures will be subject not only to a reporting requirement but also an auditing requirement from 2024 onwards. In addition, the European Commission envisages that they will also be subject to an electronic reporting requirement (referred to as "tagging") from the same year onwards. This will entail additional requirements that will inevitably result in immense organizational changes – especially given that the European Securities and Markets Authority (ESMA) has singled out the EU Taxonomy as one of its areas of focus for European auditing in 2022 and because it is expected that the disclosures will fall within the scope of responsibility of the German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht* – BaFin).

Last year, we surveyed undertakings in Germany, Austria, the Netherlands and Switzerland regarding non-financial reporting and published the results in the study *"EU Taxonomy – The Transformation of Non-financial Reporting"*. The focus here was on the extent to which undertakings have addressed the EU Taxonomy and how good the current data situation and processing of non-financial data is with a view to fulfilling the requirements of the EU Taxonomy. Because the undertakings subject to a reporting requirement have been obligated to incorporate disclosures regarding the EU Taxonomy into their financial reporting since 1 January 2022, our intention here is to carry out the study again. We would like to find out what has taken place at the undertakings in the meantime and how they have got to grips with the implementation of the EU Taxonomy. Therefore, we have updated and fine-tuned most of the questions from the prior year's study and supplemented them with new questions.

It is therefore only possible to compare the results from 2021 with the new answers in some cases.

Furthermore, the concept for the study has been broadened compared to the prior year. This is because the EU Taxonomy means that non-financial reporting will become increasingly important for investors and other capital providers, especially banks. Banks have a key function to perform in the implementation of the Green Deal. They must, among other tasks, specify a green asset ratio, i.e. the proportion of "green" loans and investments within their portfolios.

To do so, they require information from undertakings. For this reason, we also surveyed large European banks regarding their views on the EU Taxonomy.

This study is therefore structured as follows:

A **Undertakings and the EU Taxonomy – quantitative survey**

1. Significance of the topic of sustainability
2. Implementation of the EU Taxonomy
3. Reporting and data collection

B **Banks and the EU Taxonomy – qualitative survey**

For part A, we surveyed a total of 170 undertakings from Germany, Austria, Switzerland and the Netherlands. While Switzerland itself is not an EU member state and thus not obligatorily subject to the EU Taxonomy, Swiss companies nevertheless often orient themselves towards the reporting requirements of EU countries. Moreover, Swiss groups could be indirectly affected if individual subsidiaries are domiciled within the EU and thus fall within the scope of application of the EU Taxonomy. For part B, we were able to conduct intensive discussions with a total of nine large banks from eight European countries.

We would like to express our deep gratitude to all who participated. If you have any questions regarding the EU Taxonomy in particular or sustainability reporting in general, please feel free to contact us. We will be pleased to discuss them with you.

We hope that reading this study is both enjoyable and informative for you.



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Executive Summary

Two thirds of undertakings have no standardized process for data provision

One key finding of our survey of undertakings is that the EU Taxonomy seems to be achieving its intended effect and is motivating companies to conduct business more sustainably. However, what exactly is the current implementation status of the EU Taxonomy? What expenditure is required to overhaul processes and tools in order to ensure reliable reporting? These questions and others are addressed in the pages ahead. In addition, you will be provided with the most important insights from our intensive discussions with nine large European banks.

Significance of sustainability rising – due in part to the EU Taxonomy

Almost two thirds of the survey participants (63%) stated that sustainability is viewed as highly significant within their organization. 42% of undertakings state that the EU Taxonomy is an influencing factor that has made the topic of sustainability more important. The EU Taxonomy is therefore a driver for sustainable economic activities and thus seems to be achieving its key objectives in numerous cases.

Nevertheless, approximately three out of five undertakings stated that the EU Taxonomy is not (yet) a driver of transformation. We view this proportion as high and it is understandable in light of the current changes and influencing factors that companies are currently dealing with (such as the raw material and energy crisis or inflation). It is possible that this is the reason that less priority is being given to environmental, social and governance (ESG) matters.

We believe that changes in remuneration models could provide incentives to direct greater investment and funding towards sustainability. The remuneration of management is currently linked to non-financial indicators at just over a quarter of undertakings and has thus not changed compared to the previous year. Nevertheless, the number of undertakings that wish to strengthen this link in future has almost doubled since 2021, rising from 8% to 15%.

Around half of the undertakings have started reporting on alignment

Almost half of the undertakings (48%) have already started reporting on alignment and, given the implementation expenditure that this entails, such a proportion can be viewed positively. The majority of companies that have started to conduct such reporting have already dealt with the alignment criteria – 80%. The criteria dealt with most often by the undertakings surveyed (59%) were those relating to substantial contributions.

This is surprising when compared to the proportion of respondents dealing with the “minimum safeguards” criteria (43%) and the “do no significant harm” criteria (37%). The latter here explicitly and specifically describe economic activities and entail significant requirements relating to data collection. We therefore believe it would be rational for companies to prioritize the “do no significant harm” criteria. Furthermore, 70% stated that they had at least some questions regarding how alignment criteria should be applied. Such undertakings might require greater support in this area.

Around six out of ten respondents rely on external service providers

Under no circumstances should undertakings underestimate the expenditure relating to reporting. 13% of undertakings with experience of the Taxonomy deem such expenditure to be low while 54% deem it to be medium-sized. Approximately seven out of ten undertakings required up to six months to implement the requirements of the EU Taxonomy. 76% of undertakings with experience of the Taxonomy have thus far been able to implement the requirements with their existing resources, although 46% believe that they will require more personnel over the course of the year. We share this assessment, especially given that alignment topics will need to be dealt with from this year onwards and this will result in even greater expenditure.

Approximately six out of ten respondents were already using external assistance for their implementation efforts, a significantly higher level than had been anticipated in the prior year (49%). We view this as a further indication that undertakings had previously underestimated the expenditure relating to the implementation of the EU Taxonomy.

Only one in five undertakings has a standard process for data relating to Taxonomy eligibilit

The most surprising result of the overall survey was that two thirds of undertakings still do not have a standardized process in place for the provision of taxonomy-related data – more than in 2021 (61%). Only one in five undertakings (20%) has a standard process for taxonomy-eligible information and only 11% have a standard process for taxonomy-eligible as well as taxonomy-aligned information. A standardized process is absolutely necessary to ensure that the reported data are valid and to facilitate reliable management. Comprehensible and meaningful data are also particularly important for investors and banks.

It is clear that the requirements for non-financial, taxonomy-related information – such as product portfolios, investments, limit values and production processes – will continue to rise. This is confirmed by just under half of the undertakings that have already prepared reports on taxonomy-eligibility and alignment. Such undertakings state that the gathering of taxonomy-related data will entail considerable expenditure in the coming years. Only 13% of the respondents believe their undertaking is currently well prepared for this task. In light of the rising level of requirements, we believe it is urgently necessary to clearly define processes and responsibilities as quickly as possible.

Over 70% of undertakings currently base their reporting on Excel

Dedicated tools for sustainability reporting are crucial components for the reporting processes involved. To date, just under one third (31%) of the undertakings have implemented such a tool and only 9% have a special tool in place for Taxonomy reporting. 41% of the respondents plan to use a dedicated tool for EU Taxonomy reporting in future.

A critical view must be taken of the fact that – among other tools – 72% of undertakings use Excel, 24% use Word and 21% use email for reporting. This is because these tools do not facilitate (verifiably) secure documentation as they lack both access controls and functions for transparently tracking modifications.

Implementation expenditure many times greater for banks

Overall, the implementation of the EU Taxonomy will result in enormous expenditure for undertakings. The expenditure for banks will be many times greater because, in many cases, they must carry out classifications both at the level of the undertakings concerned and at the level of individual transactions.

Ensuring the consistency of results frequently poses a challenge. In particular, different members of staff entrusted with the assessment of obligatory taxonomy alignment from 2023 onwards could often arrive at varying results if they do not have process-oriented tools.

Taxonomy alignment expected to be a decisive factor for loan conditions in future

A further difficulty is posed by the fact that the processes at banks for issuing loans are currently oriented towards the company level rather than the level of economic activities as envisaged under the EU Taxonomy. Banks must therefore modify the associated processes and IT systems. This is resulting in significant expenditure in terms of both time and costs.

Banks are increasingly relying on data from external service providers because they have not yet been provided with some of the necessary information by undertakings. This is resulting in significant costs and is not rational from a macroeconomic standpoint because all banks require the same information. It would therefore be significantly more efficient to make such regulatory data publicly accessible via jointly organized infrastructure. This would significantly reduce both time and financial expenditure for banks and companies alike.

Because banks are a crucial transmission mechanism for the implementation of the European Green Deal, regulatory authorities will most likely call for increased equity backing for loans that are not aligned with the Taxonomy in future. This will mean that banks can be expected to differentiate between taxonomy-aligned and non-taxonomy-aligned loans in future – including when it comes to pricing.

You can find out more about these results and others in the pages ahead.

> For many companies, it is likely that the costs of implementing the EU Taxonomy will only become apparent once they deal with alignment in greater detail.



A Undertakings and the EU Taxonomy

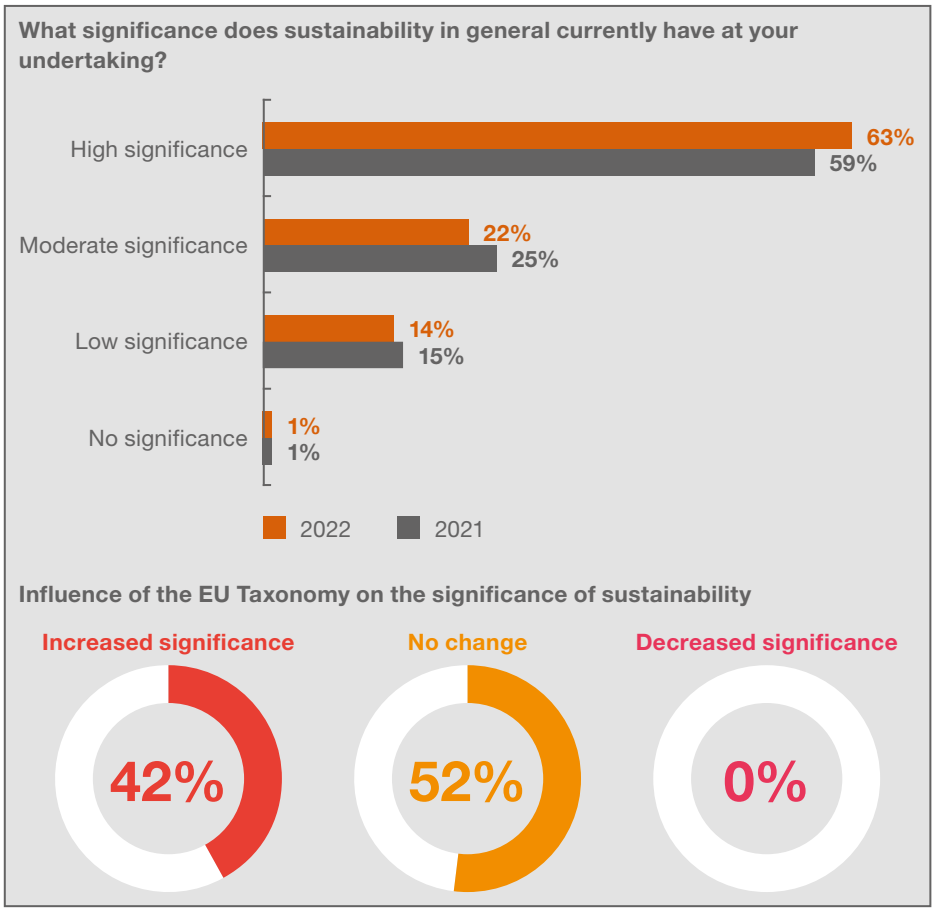
1. Significance of the topic of sustainability

This part of the study outlines, among other matters, how undertakings use non-financial data, the extent to which they link the remuneration of management to non-financial objectives and which corporate functions are primarily responsible for sustainability reporting.

Sustainability very important for six out of ten undertakings

63% of the respondents view sustainability as highly significant for their undertakings at present. This equates to an increase of four percentage points compared to our survey in 2021. It is a matter of moderate significance for 22% of respondents (2021: 19%). 14% view it as a matter of little significance and this is one percent lower than in 2021. Among the undertakings that classified sustainability as a matter of little significance, 13% acknowledge the increasing relevance of the topic. Moreover, 42% of the respondents stated sustainability has become more important for them due to the EU Taxonomy while 52% indicated no change in significance for them. None of the companies surveyed indicated that the importance of the topic had decreased.

Fig. 1 Significance of sustainability at undertakings



PwC's view on the matter

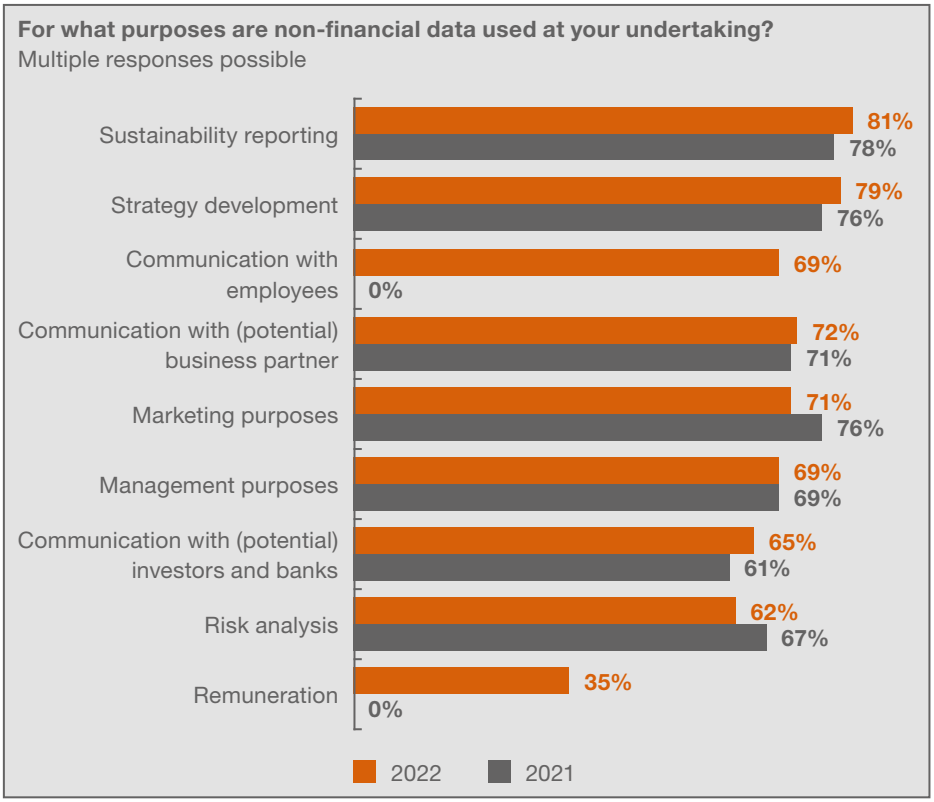
Sustainability has become more important for 42% of the undertakings surveyed as a result of the EU Taxonomy. This figure makes it clear that the regulation has already achieved one of its objectives – encouraging companies to orient themselves towards more sustainable business.

Slight increase in use of non-financial data for strategic purposes

More companies have now started using non-financial data for a wider range of purposes than in the prior year. Such data continues to be used primarily for sustainability reporting (2022: 81%; 2021: 78%).

This is followed by usage for strategy development (2022: 79%; 2021: 76%). Only 71% of undertakings are now using such data for marketing purposes (2021: 76%).

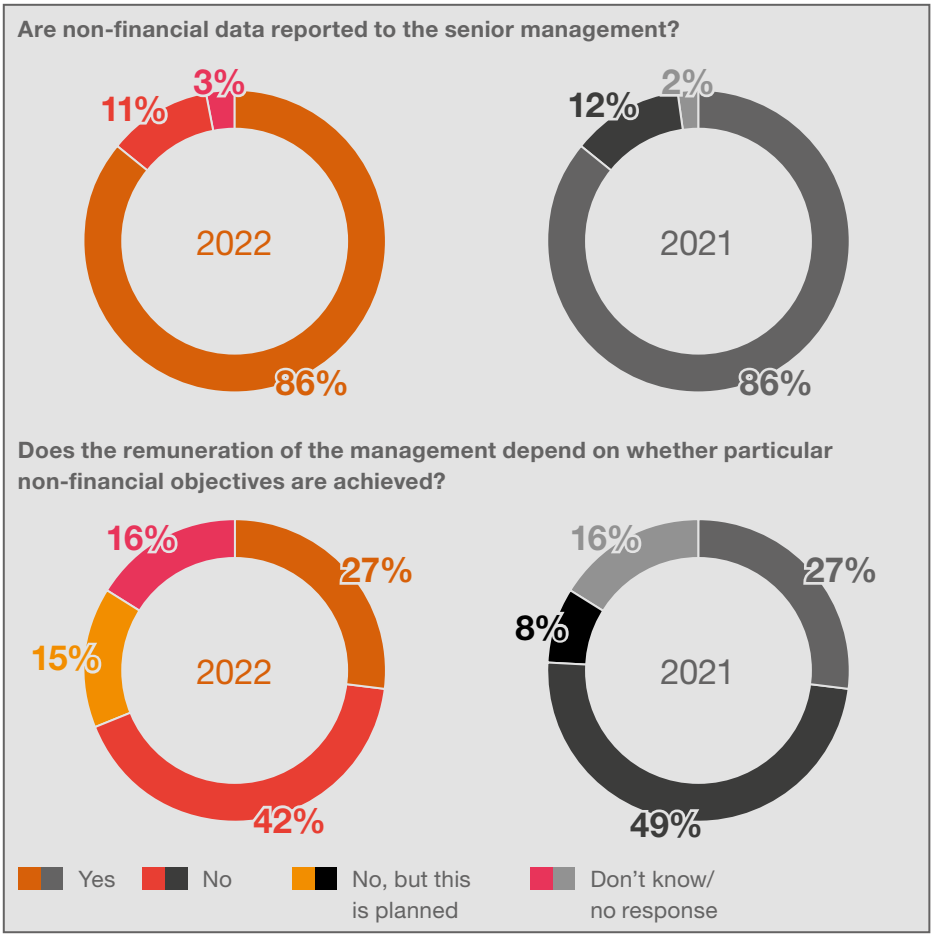
Fig. 2 Use of non-financial data



Significantly more undertakings want to link management remuneration to non-financial objectives

Reports regarding non-financial data are provided to management at most undertakings (86%). The remuneration of management is nevertheless only linked to non-financial objectives at around a quarter of undertakings. There has been little change here compared to the prior year. Nevertheless, 15% of the undertakings are currently planning to link such remuneration to non-financial objectives. This represents an increase from only 8% in 2021.

Fig. 3 Role of non-financial data for management



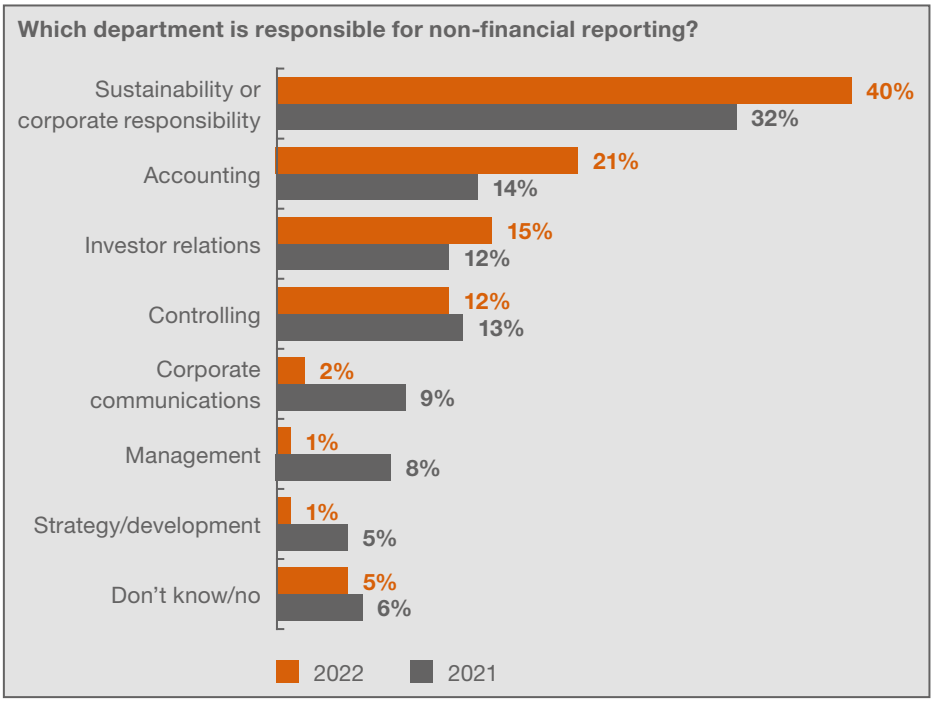
PwC's view on the matter

Managerial remuneration is roughly as dependent on non-financial objectives as it was in the prior year. Nevertheless, the number of companies planning to strengthen this link has approximately doubled. We believe that such changes in remuneration models can certainly create an incentive to direct greater investment and funding towards sustainability and thus assist in achieving the associated objectives even more quickly.

Accounting departments increasingly assuming responsibility for sustainability reporting

At four out of ten undertakings, the sustainability or corporate responsibility department is responsible for sustainability reporting (2021: 32%). In approximately one in five companies (21%) the accounting department is responsible (2021: 14%). This means that accounting departments are taking the place of investor relations departments (2022: 15%, 2021: 12%) and controlling departments (2022: 12%; 2021: 13%). In 2021, an almost equal percentage was attributed to each of these department types.

Fig. 4 Departments responsible for non-financial data



PwC's view on the matter

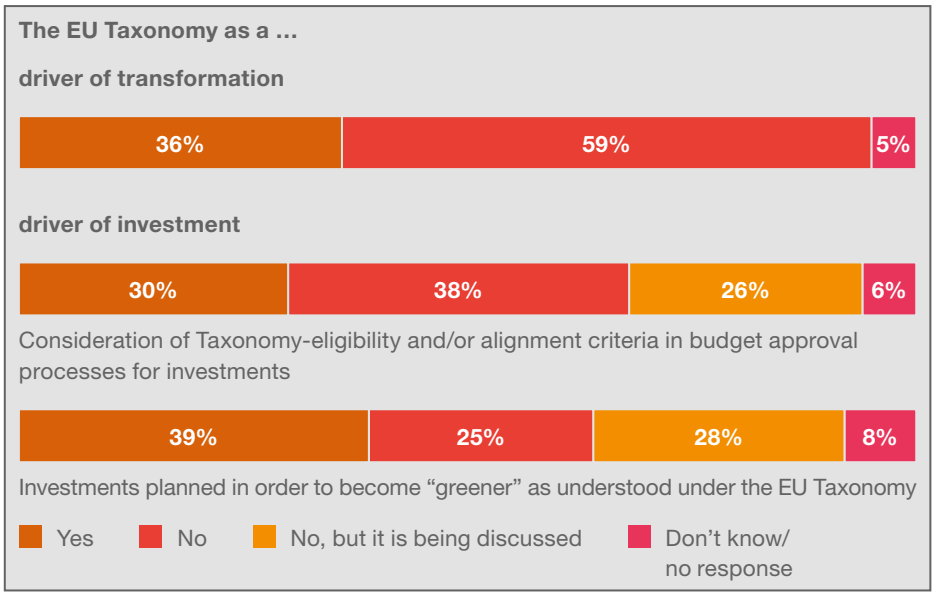
We believe that accounting departments taking on greater responsibility for sustainability is a development in the right direction. This is in part because of the rising importance of interactions between financial and non-financial performance indicators. In addition, based on our experiences with financial performance indicators, we believe that firmly embedding process security into accounting will act as an additional advantage for the management of sustainability reporting.



EU Taxonomy influencing investment strategies at three out of ten undertakings

36% of undertakings surveyed state that the EU Taxonomy is a driver for transformation in relation to sustainability. This is not the case for 59%. 39% are planning investments to become "greener" as understood under the Taxonomy. Furthermore, three in ten undertakings want to take the criteria of Taxonomy eligibility and alignment into consideration when it comes to approving investment budgets.

Fig. 5 Strategic impact of the EU Taxonomy



PwC's view on the matter

For almost six out of ten undertakings, the EU Taxonomy is not a significant driver for any substantial transformation towards sustainability – and we view this as far too many. However, companies are currently being compelled to deal with a large number of external challenges such as the raw materials crisis, the energy crisis and inflation. This means that ESG concerns could lose priority for some time. However, anyone who has not been active in this area should act as quickly as possible – at the latest once the alignment criteria of the EU Taxonomy for the four other environmental goals have been published in finalized form and provide additional clarity regarding the requirements. Four out of ten companies are already planning investments in increased sustainability and we view this as a highly positive development.

Conclusion regarding the significance of the topic of sustainability

The EU Taxonomy is clearly influencing how undertakings view sustainability as a topic as more than four in ten respondents state that the significance of this topic has increased as a result of the Taxonomy. The Regulation is thus achieving one of its key objectives: to motivate undertakings to act more sustainably.

In many cases, however, the EU Taxonomy is evidently not yet acting as a driver for sustainable transformation processes with six out of ten undertakings stating this to be the case. It is possible that focus is not yet being directed towards ESG topics because undertakings are currently being compelled to address numerous crisis situations, such as rising costs for raw materials and energy, disrupted or failing supply chains as well as inflation, to name just a few.

The remuneration of management has not yet been linked to specific sustainability goals at many undertakings either. Nevertheless, approximately twice the number of undertakings are planning to do so compared to the prior year. A further positive point to note is that 40% of respondents plan to invest in more sustainable economic activities.

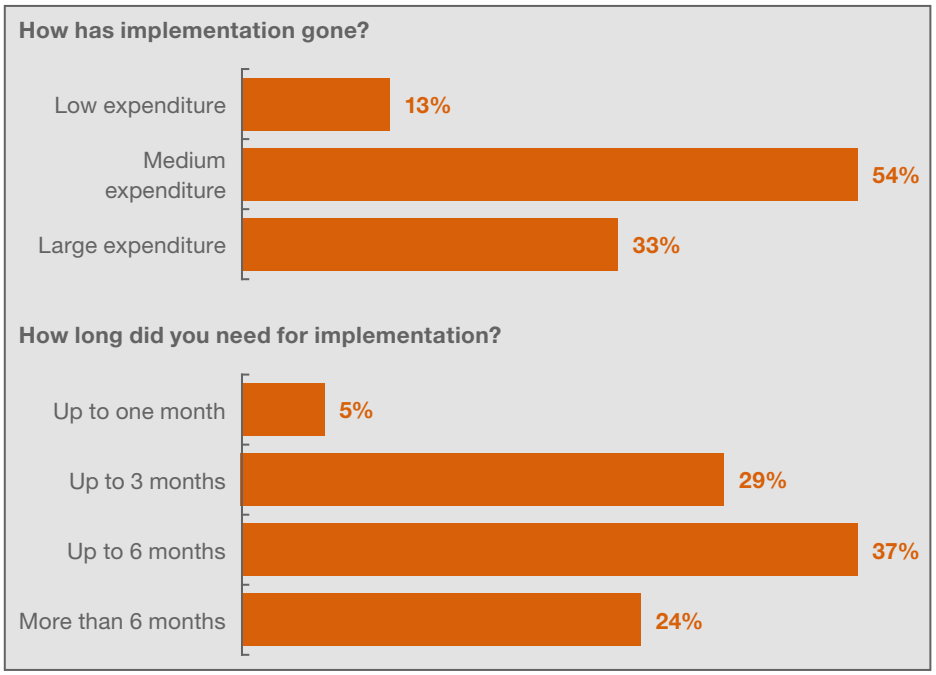
2. Implementation of the EU Taxonomy

This second part of this study describes how undertakings assess implementation expenditure and personnel requirements for the EU Taxonomy. Furthermore, it outlines how far undertakings have progressed with their alignment reporting.

Expenditure for Taxonomy implementation medium or large for most respondents

Only 13% of undertakings that have already gained some experience of implementing the Taxonomy state that the associated expenditure was low. More than half of these undertakings (54%) said that this entailed a medium level of expenditure while 33% of the respondents viewed such expenditure as large. Very few undertakings (5%) were able to implement the Taxonomy within one month. 29% needed up to three months while 37% needed up to six months. Around a quarter of the undertakings (24%) needed more than six months.

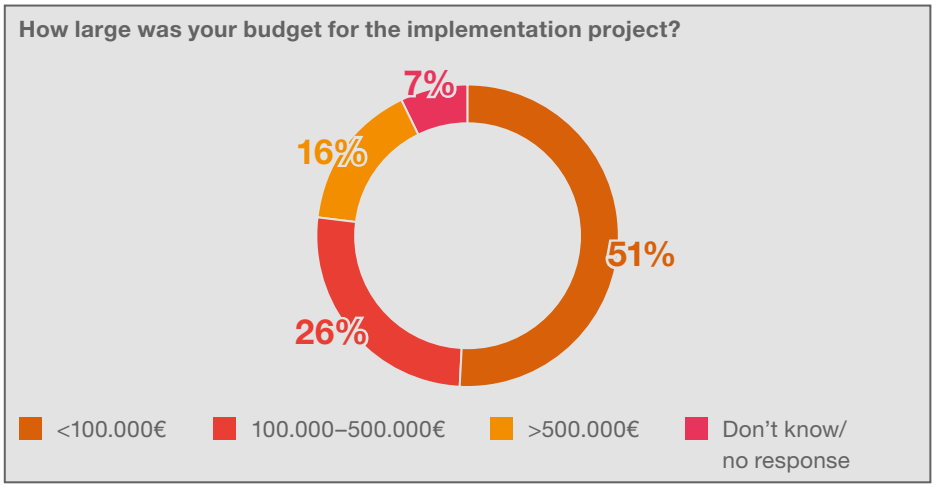
Fig. 6 Expenditure for implementing the EU Taxonomy



Implementation often costs less than €100,000

Implementation of the Taxonomy cost less than €100,000 for around half of the undertakings. The costs amounted to between €100,000 and €500,000 for around one quarter of them. EU Taxonomy implementation costs amounted to more than €500,000 for around one sixth of the undertakings.

Fig. 7 Budgets for implementation projects



PwC's view on the matter

This result corresponds to our expectations. Most undertakings with Taxonomy experience reported a medium level of expenditure for implementation and the implementation period of up to six months can also be viewed as a medium-level figure. The breakdown of costs corresponds roughly to the size of the undertakings surveyed. It should nevertheless be noted that the topic of alignment also came into play during the year under review. This will require intensive efforts on the part of companies and result in another significant increase in expenditure on implementing the EU Taxonomy within their processes, organizational structures and systems. Undertakings should start preparing now by taking the resources required by the departments primarily tasked with implementation – sustainability, IT, accounting and procurement – into consideration in their planning.

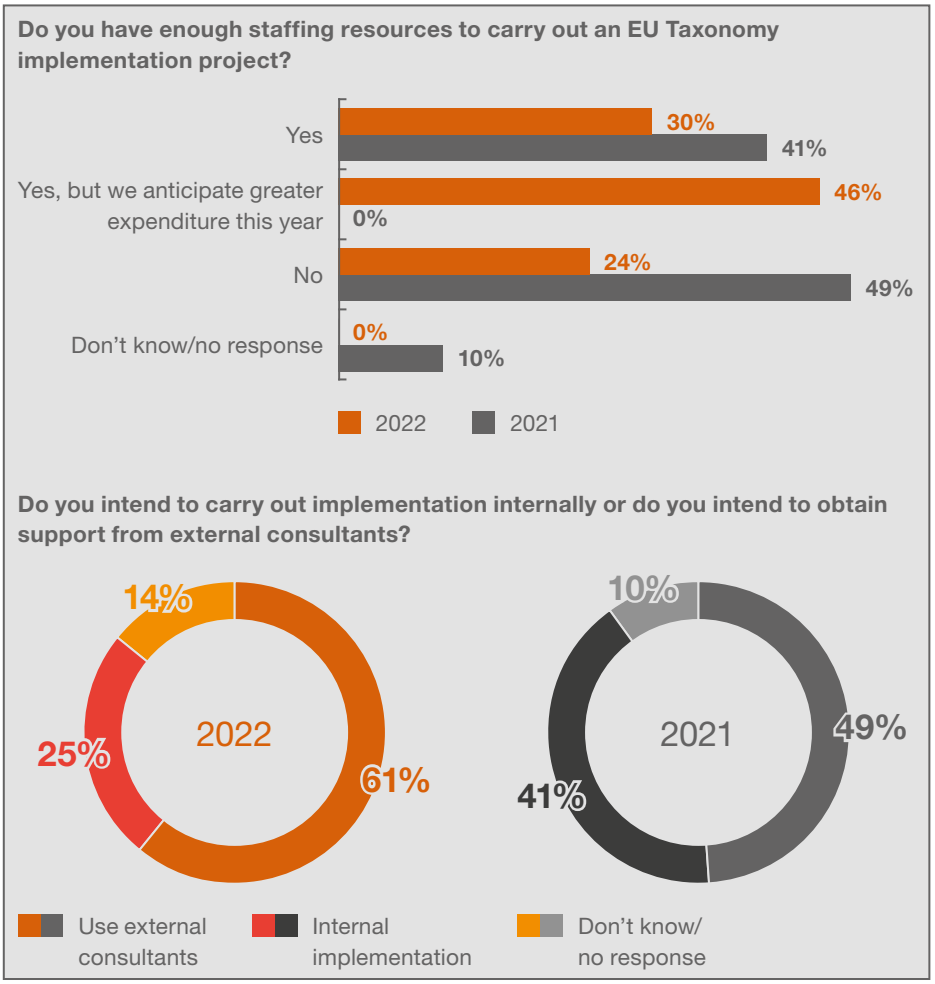
Almost half of respondents expect that implementation will require additional personnel

76% of respondents were able to implement the EU Taxonomy with their existing resources. However, almost half of them (46%) believe that additional personnel will be required over the course of the year. 24% did not have sufficient resources to implement the Taxonomy. Furthermore, around six out of ten of the undertakings that have already commenced implementation use external service providers. Of the undertakings that have not yet implemented the Taxonomy, only 25% intend to use external service providers.

PwC's view on the matter

In last year's survey, 49% of undertakings stated that they intended to use external consulting services for the implementation of the Taxonomy. We viewed this percentage as relatively low at the time. Indeed, 61% of undertakings with experience of implementation obtained external support. We believe that this highlights how some undertakings have in fact underestimated the level of expenditure. Such expenditure is due to increase again soon due to the alignment assessments for the EU Taxonomy. Those who approve or procure all necessary resources at an early stage will save time in future.

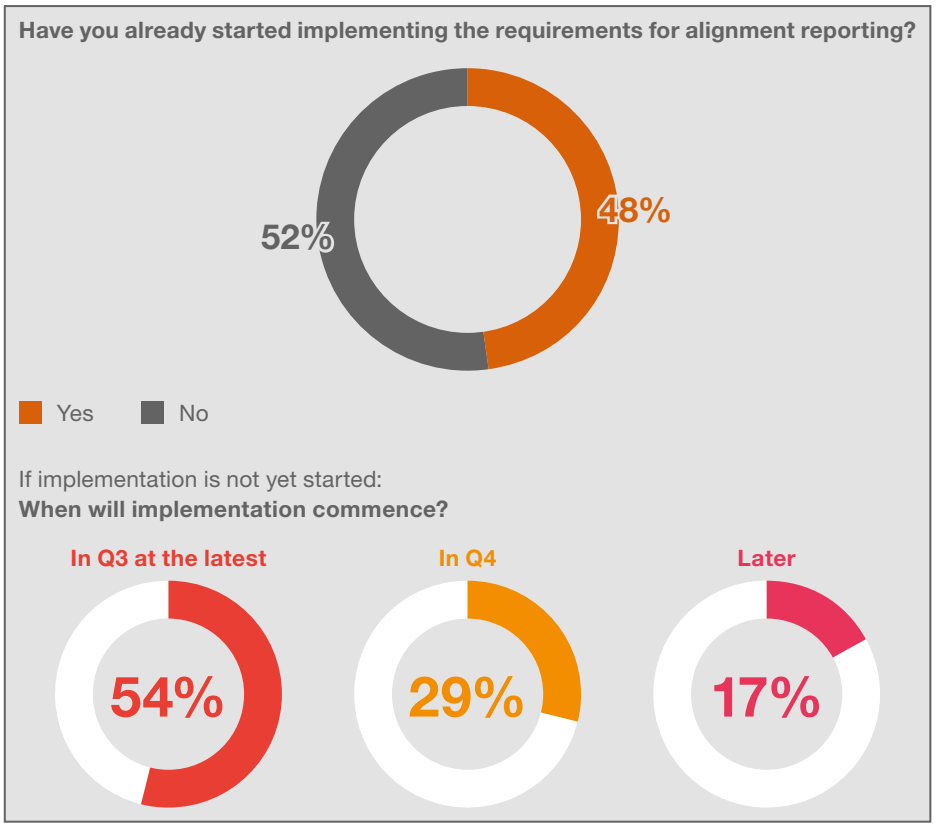
Fig. 8 Staffing resources for EU Taxonomy implementation projects



17% not yet focusing on alignment analysis

Approximately half of the undertakings have already started to implement their alignment reporting. Of the undertakings that have not yet dealt with this topic, 54% intend to start doing so in the third quarter of 2022 at the latest. 29% of respondents do not intend to start until the fourth quarter and 17% intend to do so even later.

Fig. 9 Timescale for implementation



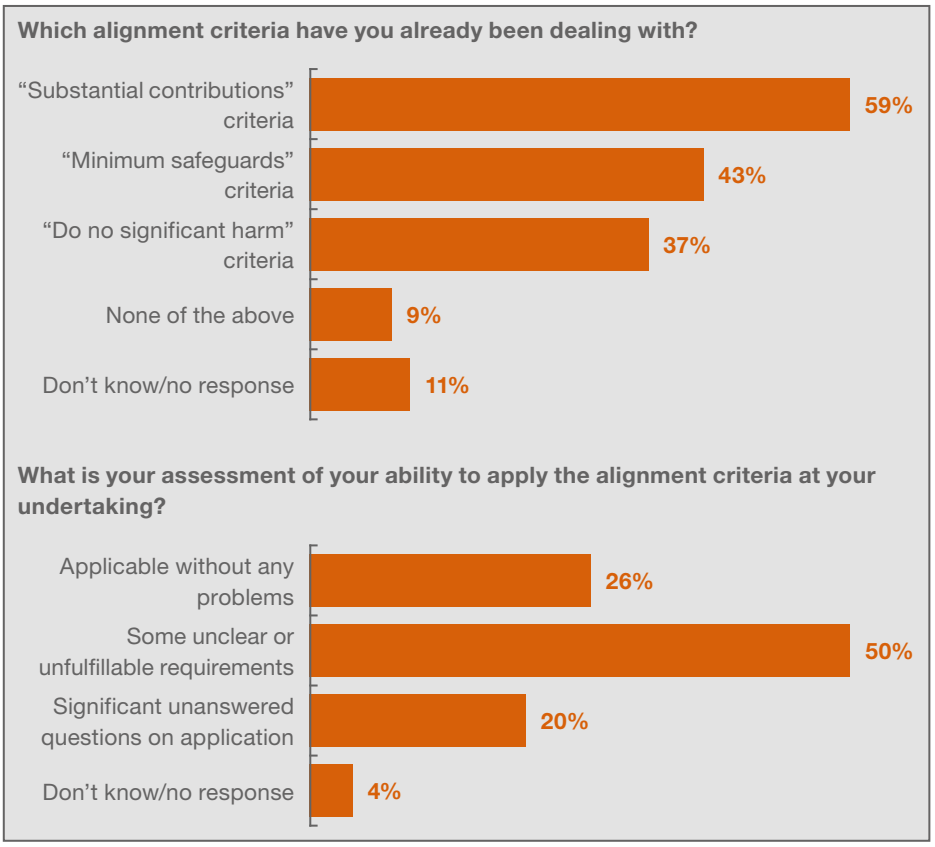
PwC's view on the matter

Approximately half of the respondents have already started their alignment analysis and this is a good figure. We would advise the remaining half not to underestimate the amount of time needed to gather the extensive information and data required in this context. Managed buildings and company cars provide two clear examples here. In the case of the latter, undertakings must state, among other details with how high the CO_2 emissions are, which pollutants result from production and whether human rights are jeopardized. It is likely that undertakings will have to request such information from their suppliers and then integrate it into their existing processes.

One in ten undertakings not addressing alignment criteria

A large majority of undertakings that have started to conduct alignment reporting are already dealing with the relevant criteria. 59% have already dealt with the "substantial contributions" criteria, 43% have dealt with the "minimum safeguards" criteria and 37% have dealt with the "do no significant harm" criteria. Contrasting this, one in ten undertakings have not yet dealt with the criteria at all.

Fig. 10 Addressing the alignment criteria of the EU Taxonomy



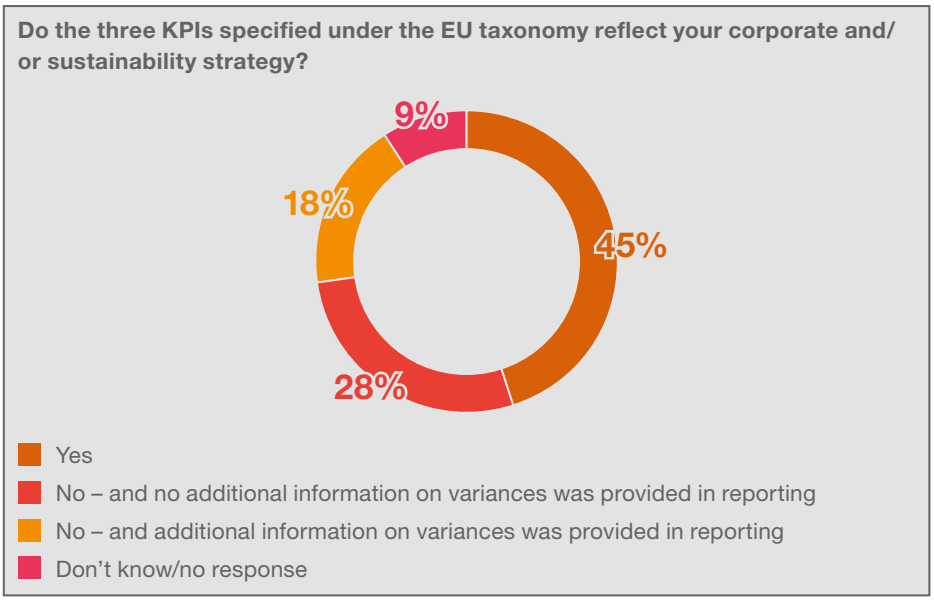
PwC's view on the matter

We view the fact that merely 9% of respondents have not yet dealt with the criteria as a positive development. Moreover, the fact that the majority of respondents have dealt with the "substantial contributions" criteria is in line with the logic of the EU Taxonomy. It was not expected that undertakings would be increasingly dealing with the "minimum safeguards" criteria over the "do no significant harm" criteria. Here, we had anticipated that the latter would be subject to greater efforts because such criteria entails particularly detailed information relating to economic activities. We believe that the "do no significant harm" criteria will involve greater expenditure. It would therefore be rational to prioritize work in this area. The fact that 70% of the respondents still have some unanswered questions regarding criteria application indicates the need for assistance here.

Taxonomy KPIs often not in line with corporate strategy

Almost half of undertakings (45%) state that the KPIs pursuant to the EU Taxonomy reflect the content of their corporate and/or sustainability strategies. This is not the case for 18% of undertakings. This is the percentage of companies note variances between their reporting on taxonomy alignment and the KPIs, while a further 28% did not provide any information regarding variances.

Fig. 11 Agreement between EU Taxonomy KPIs and corporate strategy



PwC's view on the matter

Almost half of the respondents believe that the criteria of the EU Taxonomy reflect features of their corporate strategy. The fact that 28% of the undertakings surveyed did not note any variances in their reporting is viewed by us as an indication that the criteria concerned are not yet applicable to them. Furthermore, approximately 20% of undertakings describe activities in their reporting that they view as sustainable but that are not recognized as such under the EU Taxonomy. They thus clearly express their view that the EU Taxonomy does not fully cover their own understanding of sustainable economic activities.

Conclusion regarding the implementation of the EU Taxonomy

The large majority of undertakings with Taxonomy experience believe that the implementation of the EU Taxonomy requires a medium level of expenditure and a majority also reported an implementation period of six months. When the topic of alignment comes into play in 2023, the expenditure required for reporting will increase significantly. The resource planning of undertakings should take this into account. This includes addressing the question of external consulting at an early stage.

One positive surprise for us was that around half of the respondents had already started to conduct alignment reporting. Those who have not yet done so should bear in mind that many undertakings will have to gather and compile large volumes of – at times scattered – information for this purpose. It is noteworthy that seven in ten of the respondents have some or many questions regarding the application of alignment criteria.

Furthermore, almost half of the respondents believe that the criteria of the EU Taxonomy reflect their undertakings. The reporting of more than a quarter of respondents did not provide details on variances – a clear indication that the relevant criteria of the EU Taxonomy is not yet applicable to them.

3. Reporting and data collection

The third chapter of this study describes the extent to which the surveyed undertakings have established standard processes for taxonomy-related data, how they perform quality assurance and the degree to which they are prepared for data collection.

Deep dive into ESG transformation
From strategy to reporting

There is a growing expectation among today's investors, shareholders, consumers and other stakeholders that undertakings act in a sustainable and forward-looking manner. Many employees desire the same thing from their employers, as reflected in PwC's *Hopes and Fears 2022* report. In addition, undertakings are required to fulfil an increasing number of requirements, such as those pursuant to the EU Taxonomy.

In order to do so as efficiently and effectively as possible and in order to improve their organizational management by using ESG data, most undertakings need to adjust their reporting processes. Moreover, the EU Taxonomy requires large quantities of information from a wide range of sources. How is such change brought about?

Transforming reporting – the most important steps

First of all, undertakings have to define a target operating model – and in so doing specify which functions and persons will be responsible for which ESG-related tasks. They must also establish governance structures with monitoring mechanisms that ensure that all parties involved adhere to the specified processes. Furthermore, they should define an ESG strategy that is in line with their general corporate strategy. Such a strategy should also describe their level of ambition. For example, do undertakings wish merely to fulfil the statutory requirements or do they wish to go beyond this with a voluntary ESG framework for their reporting?

This is followed by an analysis of the most important regulatory requirements. For most undertakings, this includes the CSRD, the EU Taxonomy and the German Act on Corporate Due Diligence in Supply Chains (*Lieferkettensorgfaltspflichtengesetz* – LkSG). These could potentially be supplemented with voluntary frameworks. The responsible parties can use a gap analysis to determine how well prepared the undertaking is to fulfil the requirements and which KPIs have not yet been determined. The reporting concept defines which matters the undertaking intends to report on and which data points are relevant for doing so. This then serves as the basis for designing business and reporting processes.

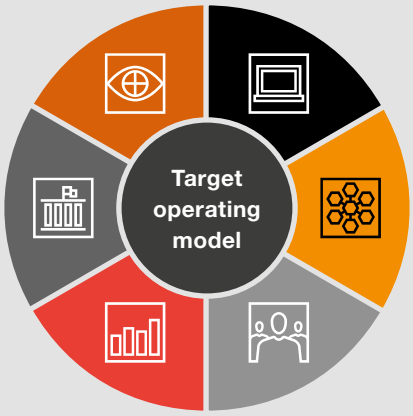
The requirements for IT system architecture can then be specified and the tools required for reporting can be selected and implemented. The responsible parties can then implement the reporting process. To this end, they gather the required data, calculate the KPIs, train employees and coordinate reporting by working closely together with their financial auditor.

Fig. 12 ESG target operating model

Strategy and vision
- Definition of a comprehensive ESG strategy that is in line with the corporate strategy
- Specifying the level of ambition based on the relevant regulatory requirements (e.g. EU Taxonomy, CSRD, LkSG) as well as voluntary frameworks
- Determining the relevant requirements for all business units

Data and technology
- Establishing clear definitions of the relevant KPIs and data structures (based on business activities)
- Definition of relevant information, data and forms of proof
- Defining the relevant system landscape for the collection of data, calculations and reporting

Organization and governance
- Specifying a clear governance system for ESG matters across all business units
- Defining and updating the relevant standards and policies concerning ESG matters
- Establishing clear roles and responsibilities within operating processes (organizational structure)



Process architecture
- End-to-end definition of processes based on information and data flows in line with the relevant business activities and across all corporate functions
- Determining a clear segregation of activities across existing corporate functions/business units
- Using automation and digitalization technologies

Performance management
- Defining clear performance indicators (strategic and process-related)
- Defining a sustainable management concept, including data analytics/predictive analytics

Employees and culture
- Upskilling all employees and managerial staff with a view to the defined responsibilities
- Establishing a new awareness in relation to ESG with the assistance of change management measures and by embedding it within the corporate culture

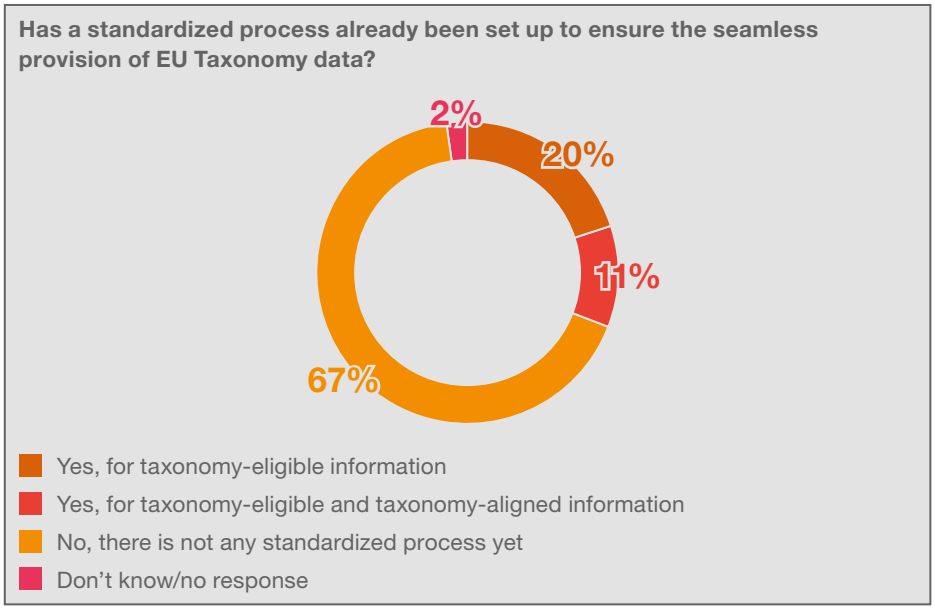
The objective is to ensure high-quality and reliable reporting.
It is important to note that there is no one single solution that will uniformly guarantee the successful transformation of reporting at every single undertaking. It is instead necessary for each company to chart its own course in accordance with its own internal culture. A particular area of variance here is the scope for enforcement relating to ESG responsibilities. At some undertakings, such responsibilities are heavily decentralized while at others they are all centralized into a single function for the entire company – or even for entire groups together with their subsidiaries. Regardless of how ESG reporting is organized, the following tasks have to be fulfilled by the responsible parties:
- specifying ESG-relevant business activities, processes data structures and standards
- monitoring adherence to internal and external compliance requirements
- safeguarding processes and data quality

The objective of any effective and efficient ESG reporting system is to ensure high-quality and reliable reporting while providing all the required information in order to:
- fulfil regulatory requirements,
- inform all relevant internal and external stakeholders and
- manage the undertaking.

Majority have no standardized processes for taxonomy-related data

Two thirds of the undertakings surveyed have not yet established any standardized processes to ensure the seamless provision of taxonomy-related data. Two out of ten respondents have a standardized process for taxonomy-eligible information and a further 11% have a standardized process for taxonomy-eligible and taxonomy-aligned information.

Fig. 13 Standardized process for data provision



PwC's view on the matter

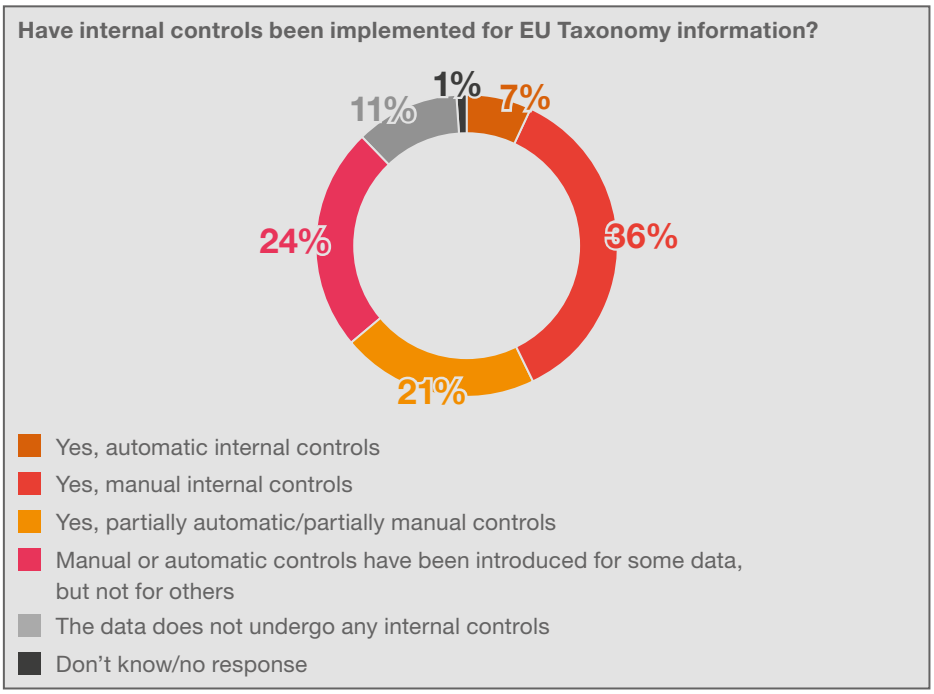
For us, the most surprising finding of the entire survey is that two thirds of respondents do not currently have a standardized process for providing taxonomy-related data. This is even more than in our previous survey last year when 61% had such a process. Having such a standardized process is absolutely necessary for ensuring the reliability of the reported data, so that such data have informational value for investors and capital providers and in order to facilitate reliable management. We once again stress that undertakings are required to gather non-financial, taxonomy-related information at least once per year from 2022 onwards and in line with the rising level of requirements. The requirements here relate to product portfolios, investments, limit values and production processes and could change at any time. Obtaining such information – potentially from numerous different subsidiaries – will multiply the amount of expenditure required. Undertakings can reduce such expenditure by establishing reliable – i.e. verifiable – processes in advance.



Quality assurance for Taxonomy data rarely automated

Of the undertakings that have already reported on their Taxonomy eligibility and alignment, 87% have implemented internal controls for the associated data. Around one third (36%) perform the internal controlling of their data manually and around one fifth (21%) have already implemented partially manual and partially automated controls. Just under a quarter of the undertakings (24%) have implemented manual or automated internal controls for some data but not for others. Only 7% have fully automated controls. Finally, data does not undergo any controls at more than one in ten undertakings (12%).

Fig. 14 Quality assurance for EU Taxonomy data



PwC's view on the matter

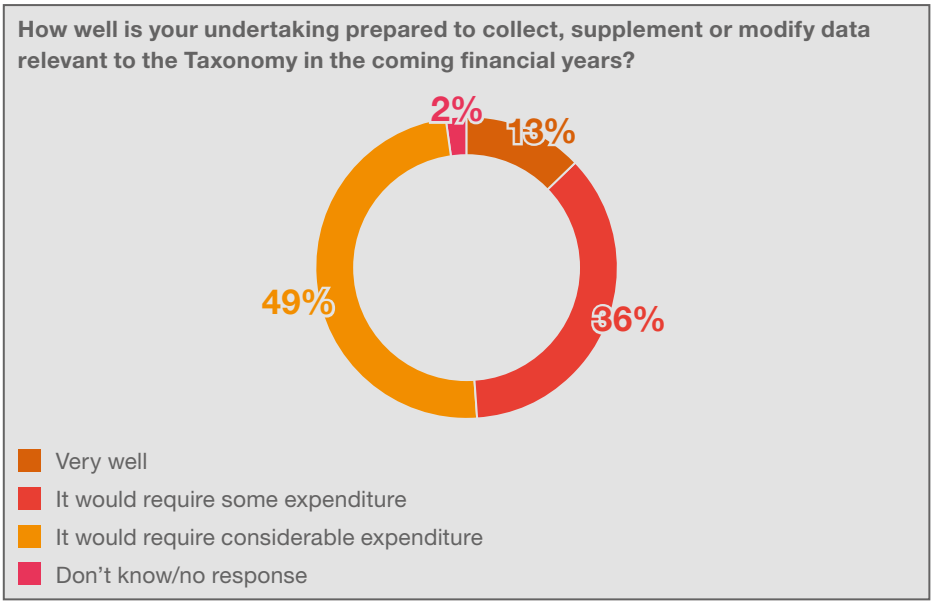
A significant majority of respondents (64%) believe that they have established effective internal controls even if the majority of them are still performed manually. We, however, view this assessment as far too optimistic. Stated plainly, this would mean that many companies apply controls to information that they do not (cannot) have because they still do not have standard processes for providing such data. We therefore again wish to state our urgent warning that undertakings should not underestimate the procedural and thus organizational workload relating to the EU Taxonomy.



Only a few undertakings are very well prepared for data collection

Almost half of the undertakings that have already reported on their Taxonomy eligibility and alignment state that "significant expenditure" will be necessary in order to collect, supplement or modify data relevant to the Taxonomy in the coming financial years. Just over a third (36%) believe such preparations require "some expenditure" and only 13% of undertakings believe they are very well prepared.

Fig. 15 Preparation for the collection of taxonomy-related data



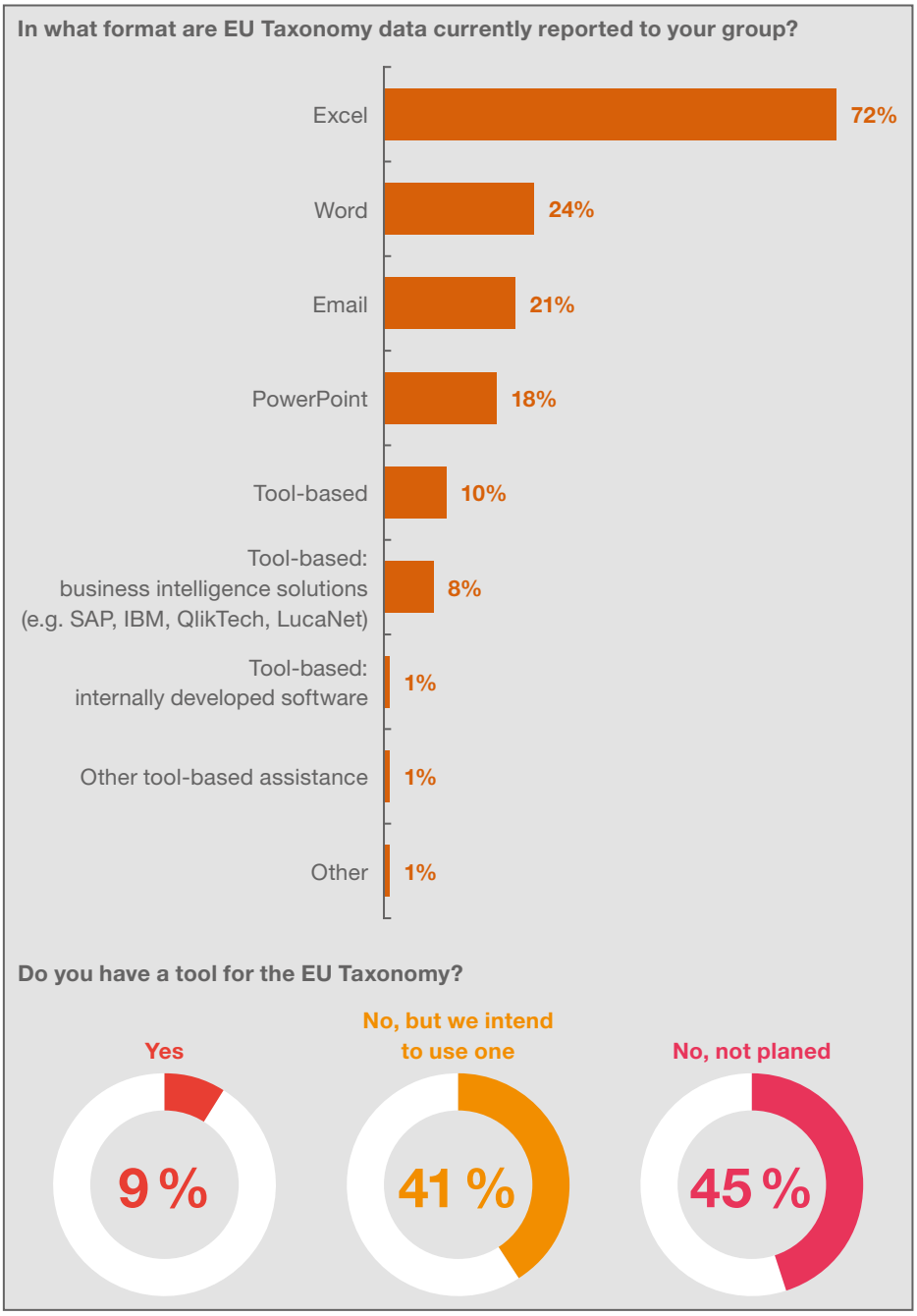
PwC's view on the matter

Around half of the undertakings with Taxonomy experience anticipate "significant expenditure" for the implementation of the Taxonomy in the coming financial years. By contrast, only one third described the expenditure for implementation to date as "large" (cf. fig. 6). The majority of undertakings with Taxonomy experience therefore expect that it will become more expensive to implement the EU Taxonomy. We can confirm this and encourage undertakings to prepare themselves in a targeted manner. To this end, they should examine the requirements from a technical standpoint and, for example, discuss the information that they will need with their suppliers. In particular, they should clearly specify the related processes and responsibilities. This is an important step for automating many of the necessary reporting processes over the medium term and thus for achieving significant advantages relating to efficiency and quality.

Fig. 16 Timescale for Taxonomy eligibility and alignment according to environmental objectives

	Publication of the non-financial report		
Environmental objectives	Financial year 2022 for reporting year 2021	Financial year 2023 for reporting year 2022	Financial year 2024 for reporting year 2023
1–2	Taxonomy eligibility	Taxonomy eligibility and alignment	Taxonomy eligibility and alignment
3–6	n/a	n/a	Taxonomy eligibility and alignment

Fig. 17 Reporting of taxonomy-related data



Excel is the most popular reporting tool

Around three in ten of the undertakings surveyed have a dedicated reporting tool for sustainability reporting while the rest possess no such tool. Most undertakings with experience of implementation use Excel for reporting EU Taxonomy data (72%). Far behind in second place comes Word (24%) followed by email (21%) and PowerPoint presentations (18%). Only 11% use tools such as business intelligence solutions or internally developed solutions. To date, 9% of undertakings with experience of implementation use a special tool for sustainability reporting. 41% of the undertakings surveyed intend to use a special tool compared to 45% who have no such plans.

PwC's view on the matter

9% of the respondents are already using a special reporting tool while 41% plan to do so – a good figure in our opinion. We hold a critical view of classifying Excel and Word files as sufficiently reliable reporting formats. These tools do not feature access controls or modification tracking functions and thus do not facilitate (verifiably) secure documentation. Appropriate processes and tools are required for implementing the EU Taxonomy, especially with regard to alignment.

Conclusion regarding reporting and data collection

Our findings are sobering. Two thirds of the respondents have not established a standardized process for the provision of taxonomy-related data. Surprisingly, this is even more than in our 2021 survey. Such a standard process is necessary to generate reliable and meaningful data for potential investors and other capital providers, for example.

In our view, there is also an excessive level of optimism in the statement that 64% of the respondents have established effective internal controls – be they manual or automatic. Without standardized processes, it is significantly more difficult to control data in a reliable manner.

In our view, the expectation that expenditure for taxonomy implementation will increase in future is correct. Undertakings must therefore examine the requirements from a technical standpoint and, for example, communicate with suppliers to clarify which information they will need and at what point in time.

Defining processes and responsibilities clearly is one of the most important tasks here – not least in order to prepare for the automation of numerous important reporting steps in future so that significant quality and efficiency improvements can be achieved. In this regard, there is a need to catch up on work among around half of the respondents. Undertakings state that they use Excel and Word files to report data. These tools, however, do not have access controls or modification tracking functions – features that are absolutely necessary for (verifiably) secure documentation.





B Banks and the EU Taxonomy

In the first part of this study, we described how the surveyed undertakings responded to our questions regarding the EU Taxonomy and summarized the findings of our survey for you. We now move on to present matters from the point of view of the banks. This is because banks require data from undertakings in order to fulfil the EU Taxonomy requirements relating to their own reporting. Moreover, they anticipate that own funds requirements will increase for loans that are not aligned with the Taxonomy in future. In order to fulfil these requirements while maintaining the same level of profitability, banks will have to apply higher interest rates than in the past in certain cases.

How do banks perceive the various facets of the EU Taxonomy? This is what we wanted to find out and what we discussed with nine large banks from eight European countries. We have qualitatively analysed their assessments. One key finding here is that while the expenditure for implementing the EU Taxonomy is immense among undertakings, it is many times greater for banks. The reasons for this and other key findings are outlined below.

Question 1:

What strategies do banks have for data collection?

Data collection still a source of problems

One key finding is that banks are still largely gathering taxonomy-related and other data manually and comparing them with external data sets that are available on the market. The quality here varies and banks therefore find themselves considering whether to use one or multiple external service providers. In cases where the respondents use an IT solution for collecting data, it rarely functions consistently well for small and large customers.

PwC's view on the matter

The application of the EU Taxonomy is posing a major challenge for undertakings. The challenge is many times greater for banks. For them, it is necessary to carry out EU Taxonomy classifications at the level of undertakings and at the level of individual transactions in a large number of cases. In particular, data collection for existing portfolios entails huge expenditure for banks and somewhat lower expenditure for the classification of new transactions.

Ensuring the consistency of results is also challenging. If the same individual transactions were assessed by different employees without the use of process-oriented tools, they could potentially arrive at different results. This issue is particularly acute in the case of the assessment of Taxonomy alignment, which is obligatory from 2023 onwards.

A further obstacle is posed by the fact that the EU Taxonomy is oriented towards economic activities rather than the level of undertakings. Contrasting this, the current processes of banks for granting loans focus specifically on undertakings themselves rather than economic activities. Banks have to readjust these processes and the associated IT systems, resulting in significant expenditure in terms of both time and costs.

Question 2:

Is reporting pursuant to the EU Taxonomy causing difficulties for banks?

The implementation of the Taxonomy is highly technically challenging for banks

The full and comprehensive implementation of reporting as specified by the EU Taxonomy is proving highly challenging for banks because, among other factors, they must adjust existing IT systems or develop new ones within a short period of time. This is because the EU Taxonomy requires banks to request a wide range of new information from customers – information that was not previously an area of focus.

PwC's view on the matter

In order to shift focus from the level of undertakings to the level of economic activities as outlined above, banks have to modify their database structures from the bottom up. To do so, many credit institutions are establishing new IT infrastructures alongside their existing core banking systems. In such cases, the new systems reconcile their information with that of the core systems. In many cases, standardized process-oriented input masks have yet to be implemented, although they are of vital importance for the implementation of legal requirements and for the consistent assessment of transactions and undertakings.

Question 3:

Who is responsible for the EU Taxonomy at banks?

Responsibility for the EU Taxonomy often has yet to be specified

There is an absence of complete clarity at the banks as to which unit or function is responsible for the EU Taxonomy. In some cases, business and/or sustainability teams are responsible while in others it is the finance function.

PwC's view on the matter

The question of responsibility for the EU Taxonomy at banks has yet to be conclusively clarified. Because the EU Taxonomy is dealt with in audit reports, we believe that the associated responsibility should be primarily borne by the financial function of banks. Sustainability departments and teams would then take responsibility for implementing regulatory requirements as well as providing the associated technical specifications and necessary data.

> Which function is responsible for Taxonomy-related data? Here there is still a lack of consensus.

Question 4:

What do banks do when the required data are not available?

If data are not available, banks use estimates

Banks do not have access to all the data that they require for their reporting. The surveyed banks generally do not obtain the data in its entirety from either the undertakings concerned or from external providers. This is particularly evident in the case of small and medium-sized enterprises that are not yet subject to any reporting obligation. If no customer data are available, the banks use estimates based on their own information and industry data. However, such estimates cannot be used for the calculation of the green asset ratio that becomes obligatory for banks from 2023 onwards.

PwC's view on the matter

Numerous undertakings contained in the loan portfolios of banks have not yet collected data for the EU Taxonomy and are therefore not capable of providing answers to enquiries from banks. So long as this is the case, it is advisable for banks conducting data collection to combine their internal data from interactions with clients with data from external service providers. We strongly advise undertakings to invest in data generation and collection. This is because sooner or later banks will almost inevitably introduce differentiated lending conditions based on such data. It would nevertheless also be advantageous for all banks and undertakings alike to pool together data collection for certain parts of the EU Taxonomy as this would reduce transaction costs for all parties involved.

Question 5:

What challenges do banks anticipate in 2023?

Banks are seeking cost-efficient solutions for data procurement

All banks have to obtain the same information from their customers in order to grant operating loans. To date, all banks have been individually gathering the same data or purchasing them expensively. This is not economically rational. Moreover, banks are often unsatisfied with both the quantity and quality of the available information. This problem will become more acute in future once more companies become subject to a reporting obligation under the EU Taxonomy and more data is therefore required.

What PwC says

We again emphasize that – where possible and rational – gathering the necessary data on a joint basis would significantly reduce expenditure in terms of time and costs for both banks and undertakings alike. Because this constitutes regulatory data, it would be advisable to make it publicly accessible via jointly organized infrastructure, e.g. from a foundation. A prerequisite here is the preparedness of the banks to cooperate on this matter. It should however also not be forgotten that past efforts to jointly gather know-your-customer (KYC) data failed or were only successful at a local level. One problem here was that KYC data constitutes customer-specific information that is in part subject to banking secrecy. In the case of EU Taxonomy data, however, a joint approach could prove successful. The EU Taxonomy data used for the granting of operating loans (e.g. primary NACE code, CapEx or OpEx) should be publicly available and all parties concerned wish to gather such data as cost-efficiently as possible.

Data procurement is by far the largest challenge!

Question 6:

How high is the response rate for the requested EU Taxonomy data and other sustainability data?

The larger the undertaking, the higher the response rate

Banks request the taxonomy-related data as well as other sustainability data from their customers. The response rate here varies and is largely dependent on the size of the respective undertaking. The larger the undertaking, the higher the response rate. This is because larger undertakings themselves often have to report such data under the EU Taxonomy and prepare other sustainability reports. At smaller undertakings, this is not usually the case. According to the banks, some smaller undertakings were not even aware of the existence of the EU Taxonomy.

PwC's view on the matter

Small and medium-sized enterprises are currently not affected by the EU Taxonomy. They are therefore not subject to any regulatory pressure to gather taxonomy-related data. Such pressure is now nonetheless being exerted by banks because they require such taxonomy-related data in order, among other purposes, to determine their green asset ratio, i.e. the proportion of "green" loans and investments in their portfolios. The banks are thus playing an important role in the implementation of the European Union's Green Deal.



Question 7:

How do banks know which undertakings are subject to a reporting requirement pursuant to the EU CSRD?

Banks often do not know which undertakings are subject to a reporting requirement

Before banks can request taxonomy-related data from undertakings, they must first determine which undertakings are even required to provide EU Taxonomy data pursuant to the European Union's Non-Financial Reporting Directive (NFRD – and from 2023 onwards CSRD). Determining this is demanding and time-consuming. This is because although some undertakings are listed by external data providers, it is not the case for many. In such cases, banks have to perform independent research into whether the undertaking is subject to a reporting requirement under the EU Taxonomy.

PwC's view on the matter

One difficulty for banks with international operations is that some EU countries have transposed the reporting obligation pursuant to the NFRD and CSRD into national law in varying manners. This complicates the task of determining which undertakings are subject to a reporting requirement under the EU Taxonomy. Even basic details such as the number of employees at a particular point in time are difficult to ascertain, especially in the case of companies not listed on any stock exchange. Should part-time or temporary employees be taken into account here, for example? Put simply, banks have varying interpretations of which undertakings in their loan portfolios are subject to a reporting obligation.

Question 8:

How do banks ensure high data quality?

Data quality often still cannot be assessed with certainty

With regard to data quality, the majority of banks surveyed reported shortcomings as they have either very limited or no systems to ensure the quality of the data provided to them. Some are working to draw up an appropriate data strategy, but most are still at the start of the process. At the same time, they emphasize how important the ability to assess data quality will be in future.

PwC's view on the matter

Due to the varying quality of the data provided to them by undertakings, banks should start off by classifying such data based on, for example, whether it consists of "estimated", "non-assessed" or "assessed" data points. The second step should be for banks to pursue the medium to long-term objective of increasing data quality to the highest standard possible. This can be done by communicating with the undertakings concerned and by using collaborative data procurement models.

Question 9:

What level of financial expenditure is reporting pursuant to the EU Taxonomy resulting in for banks?

Data procurement is costing banks (excessively) large sums of money

Procuring the data required pursuant to the EU Taxonomy is resulting in significant costs for banks – regardless of whether they use external service providers or obtain the data independently themselves. The surveyed banks desire more cost-efficient solutions that still meet the same high standards in terms of both quality and quantity.

PwC's view on the matter

This result again highlights how it is not economically rational for each bank to continue gathering the legally required data by itself. This is particularly clear in the case of operating loans for which all banks require the same data from undertakings. Once again it can be noted that jointly gathering regulatory mandated data would increase quality and quantity while also significantly reducing the costs for all parties involved.

> As a whole the banking sector is wasting large sums of money due to the EU Taxonomy because each bank procures the required data individually. A joint initiative would be both more cost-efficient and more time-efficient.

Question 10:

How do banks motivate their business partners to make data available to them?

Those who do not provide data will receive poorer conditions in future

Some of the banks surveyed stated that they were already applying a higher interest rate for undertakings that do not provide them with taxonomy-related data. Others are planning to do so in future. Beyond this, other banks believe that regulators will introduce tougher capital requirements for loans that are not aligned with the EU Taxonomy.

PwC's view on the matter

It is clear that banks will function as a crucial transmission mechanism for the implementation of the European Green Deal. It is therefore very likely that the regulatory authorities will require banks to ensure increased equity backing for loans that are not aligned with the Taxonomy in future. Banks can be expected to introduce differentiated prices for taxonomy-aligned and non-taxonomy-aligned loans in future. Put simply, this means that non-taxonomy-aligned loans will become more expensive, although it is not currently possible to predict how large the difference will be. Some of the banks we surveyed referred to a difference of 0.1 percent.

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