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COMPARING ESG STANDARDS: A COMMON BASIS FOR THE SOCIAL SUSTAINABILITY TAXONOMY

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RESEARCH OVERVIEW

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- New EU sustainable finance framework: **new rules on environmental and social sustainability.**
- Several **references to international standards** in SFDR and Taxonomy Regulation (and implementing rules).
- International standards **embedded in the new framework.**
- Investigating the **relationship between EU framework and international standards** (alignment, contradiction, differences, similarities and overlaps).

SFDR AND INTERNATIONAL STANDARDS

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- SFDR has introduced some new interrelated concepts:

1) Principal adverse impacts (PAIs)

2) Investment decisions

3) Sustainability factors

- Objective(s): **disclosure** (entity and product level) of **negative impacts of investment decisions** on environmental, social and employee matters, human rights, anti-corruption and anti-bribery.
- **Several indicators** concerning investee companies used to assess negative impacts: some **referring to international standards**.
- Indicators used also to assess environmental and/or social characteristics (article 8 products) and sustainable investments (article 9 products).

LIGHT GREEN PRODUCTS vs DARK GREEN PRODUCTS

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Light green products (art. 8 SFDR)	Dark green products (art. 9 SFDR)
Can promote environmental or social characteristics e.g. by taking into account principal adverse impacts	Must consider adverse impact indicators as part of their disclosures of no significant harm to sustainability objectives
Can invest in different assets , including assets that do not contribute to the specific environmental or social characteristics promoted by the financial product	Can make only sustainable investments
DNSH principle relevant where they also make sustainable investments	Must comply with the DNSH principle
Must use sustainability indicators to measure attainment of environmental or social characteristics	Must use sustainability indicators to measure attainment of sustainable investment objective

ADVERSE SUSTAINABILITY INDICATORS - CLIMATE AND OTHER ENVIRONMENT-RELATED INDICATORS

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Annex I – Table 1 (ESAs JC DRAFT RTS)

1. GHG emissions
2. Carbon footprint
3. GHG intensity of investee companies
4. Exposure to companies active in the fossil fuel sector
5. Share of non-renewable energy consumption and production
6. Energy consumption intensity per high impact climate sector
7. Activities negatively affecting biodiversity-sensitive areas
8. Emissions to water
9. Hazardous waste ratio

ADVERSE SUSTAINABILITY INDICATORS – SOCIAL AND EMPLOYEE, FOR HUMAN RIGHTS, ANTI-CORRUPTION AND ANTI-BRIBERY MATTERS

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Annex I - Table 1 (ESAs JC DRAFT RTS)

10. Violations of UN Global Compact Principles & OECD Guidelines for Multinationals

11. Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact Principles & OECD Guidelines for Multinationals

12. Unadjusted gender pay gap

13. Board gender diversity

14. Exposure to controversial weapons

ADVERSE-SUSTAINABILITY INDICATOR NO. 10

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Adverse-sustainability indicator no. 10:
**Violations of UN Global Compact Principles
& OECD Guidelines for Multinationals**




Metric: share of investments in investee companies that have been involved in violations of the UNGC principles or OECD Guidelines for Multinational Enterprises

ADVERSE-SUSTAINABILITY INDICATOR NO. 11

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Adverse-sustainability indicator no. 11: Lack of processes and compliance mechanisms to monitor compliance with UN Global Compact Principles & OECD Guidelines for Multinationals

A large, light blue downward-pointing arrow connects the indicator title box to the metric box.

Metric: share of investments in investee companies without policies to monitor compliance with the UNGC principles or OECD Guidelines for Multinational Enterprises or grievance/complaints handling mechanisms to address violations of the UNGC principles or OECD Guidelines for Multinational Enterprises

SUSTAINABLE INVESTMENTS AND INTERNATIONAL STANDARDS

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Sustainable Investment Art. 2(17) SFDR

Environmentally sustainable investment (ESI)
Measured Contribution to an Environmental Objective

e.g. key resource efficiency indicators:

- use of energy
- renewable energy
- raw materials
- water and land
- production of waste
- greenhouse gas emissions
- biodiversity
- circular economy

Socially sustainable investment (SSI)
Contribution to a Social Objective

- Tackling inequality
- Fostering social cohesion
- Fostering social integration
- Fostering labour relations
- Investment in human capital
- Investment in economically or socially disadvantaged communities

DNSH referring to both environmental and social objectives: reporting on alignment with **OECD Guidelines MNEs** and **UN Guiding Principles on Business and Human Rights**, including **ILO Declaration on Fundamental Principles and Rights at Work** and **International Bill of Human Rights**

Good governance at investee company level

TAXONOMY REGULATION AND INTERNATIONAL STANDARDS

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Substantial contribution to one of the six environmental objectives –
all defined by the Taxonomy Regulation + technical screening criteria



Economics

No significant harm (DNSH) to other environmental objectives



Law

**Compliance with Minimum Legal Safeguards
(article 18 Taxonomy Regulation)**

**OECD Guidelines for
Multinational Enterprises**

**UN Guiding Principles
for Business and
Human Rights**

**ILO Declaration on
Fundamental Principles
and Rights at Work +
International Bill of
Human Rights**

MAIN REFERENCES TO INTERNATIONAL STANDARDS IN THE EU SUSTAINABLE FINANCE FRAMEWORK

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Standards recalled	ESG dimension covered	Content: disclosure and/or operations	EU provision(s) recalling international standards
1. OECD Guidelines for MNEs	E-S-G	Disclosure and operations	Recitals 35, 36, 43 and art. 18 TR; JC RTS
2. UN Guiding Principles on Business and Human Rights	S	Operations	Recitals 35, 36 and art. 18 TR; JC RTS
3. ILO Declaration on Fundamental Principles and Rights at Work	S	Operations	Recitals 35, 36 and art. 18 TR, JC RTS
4. International Bill of Human Rights	S	Operations	Recitals 35, 36 and art. 18 TR, JC RTS
5. European Pillar of Social Rights	S	Operations	Recitals 35, 36 TR
6. Charter of Fundamental Rights of the EU	E-S-G	Operations	Recitals 35, 36 TR
7. UN Principles for Responsible Investment	E-S-G	Operations	Recital 18 SFDR
8. UN Global Compact Principles	E-S-G	Disclosure and operations	JC RTS – Annex 1

THE MAIN SETS OF STANDARDS RECALLED IN THE EU FRAMEWORK: CONTENT AND FEATURES

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OECD Guidelines for MNEs	UN Guiding Principles for Business and HR	UN Global Compact Principles	UN Principles for Responsible Investment
<ul style="list-style-type: none"> - ESG matters - They target MNEs - High-level general principles and standards on operations and disclosure - On environment, they focus on establishment of internal systems to collect info and assess performance - Engagement with local communities - Impacts on environment included in decision-making 	<ul style="list-style-type: none"> - Human rights' protection in doing business - They target States and businesses - High-level principles and standards aiming at enhancing human rights' protection while performing business activities - For States, duty to create systems (prevention, control, judiciary) protecting against HR violations - For businesses, establishment of internal systems to assess and prevent risk of being involved in HR violations 	<ul style="list-style-type: none"> - ESG matters - They target businesses - High-level general principles and standards on operations - Businesses should support a precautionary approach to environmental challenges - Businesses should undertake initiatives to promote greater environmental responsibility - Businesses should encourage the development and diffusion of environmentally friendly technologies 	<ul style="list-style-type: none"> - ESG matters - They have been developed by investors and target investors - High-level general principles and standards on operations and disclosure in making investments - The underlying idea is that ESG issues can affect the performance of investment portfolios, so they should be considered in the decision-making process concerning investment choices

FINAL REMARKS

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- New EU sustainable finance framework introduced very detailed and strict **rules on environmental sustainability**; this is **not yet** the case as to **social sustainability**.
- Financial market participants manufacturing **environmentally sustainable products** will have to align to **requirements more stringent** than the ones under ESG international standards.
- **Environmental standards** will still be key as **minimum requirements** for **investments not aligned with taxonomy and not qualified as sustainable**.
- On **social sustainability**, EU provisions refer to **international standards**, which will be **key** also for **manufacturing financial products making socially sustainable investments**. This might change with the adoption of a social taxonomy and introduction of the concept of substantial contribution along with technical screening criteria.

Thank you