DISCLOSURE INSIGHT ACTION

Seeking clarity amidst fragmentation

The development of sustainable finance taxonomies and the drive towards integration in CDP's disclosure system

September 2022

Contents

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Foreword

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The last decade has seen the disclosure of Environmental, Social and Government (ESG) risk, opportunities and impacts become a business norm, rocketing up the agendas of boardrooms and policymakers.

There is general agreement from corporates, financial institutions, investors, governments and regulators that disclosure is a market necessity that can improve corporate financial performance, boost resilience and, most critically, direct capital flows towards the global policy goals set in the Paris Agreement, the 2030 Agenda on Sustainable Development and the upcoming Global Biodiversity Framework. However, the normalization of ESG disclosure has gone hand in hand with a rise in reported confusion around a growing ecosystem of related ratings, indices, and tools, as well as accusations that companies are "**greenwashing**": making false claims around their environmental performance. Combined, these phenomena are detracting from the fundamental purpose of disclosure: to allow better capital allocation.

Sustainable finance taxonomies are tools that have been developed to tackle these challenges and which have grown considerably in number over recent years. At CDP, we strongly believe taxonomies can drive capital allocation towards sustainable activities, reduce greenwashing and enable simpler comparison between investment opportunities. Our research identified at least 28 taxonomies globally, which have been adopted or are on the path to adoption. While we acknowledge one global taxonomy may not be achievable and regional conditions often require a level of regional nuance, the plethora of taxonomies under development risks defeating the core purpose of a taxonomy. Yet, we argue that a set of common criteria can, and should, be applied. This policy brief explores those criteria.

As the only global, independent, environmental disclosure mechanism, CDP plays a crucial role in accelerating the implementation and rollout of standards –including sustainable finance taxonomies. Our system mainstreams their widespread adoption in a structured, comparable format, allowing investors access to information that is consistent, comprehensive, and comparable across geographies and regulatory requirements. Sustainable finance taxonomies can be used to guide CDP's questionnaire development and thought leadership around best practice in sustainability and disclosure. Over the first few months of 2022, CDP ran an analysis of the taxonomies in development globally, in order to start designing an integration model to guide our future activities in this space. The study aimed to identify the different approaches for integrating sustainable finance taxonomies into the CDP disclosure system. Its findings are outlined in this policy brief and we look forward to continuing to drive development in this important area.

Introduction

> **As highlighted in CDP's 2025 strategy, it will be critical to focus on creating a coherent disclosure system and, on equal footing, a common language for internationally agreed taxonomies.**

Sustainable finance taxonomies (taxonomies) are one of the instruments that have been developed to support the redirection of financial flows towards environmentally (and socially) sustainable activities.

According to the Bank for International Settlements, sustainable finance taxonomies are "set[s] of criteria which can form the basis for an evaluation of whether and to what extent a financial asset can support given sustainability goals"[1]. The central goal of taxonomies is driving capital allocation towards sustainable activities, reducing greenwashing and enabling simpler comparison.

The most widely recognized public sustainable finance taxonomy at this point in time is the EU Taxonomy, however others have been developed including the Chinese NDRC Green Industry Guiding Catalogue and PBC Green Bond Endorsed Project Catalogue, and the Climate Change and Principle-Based Taxonomy developed by Bank Negara Malaysia. Moreover, as shown by the infographic below, there are currently over 28 different taxonomies in development around the world, both at the public and the private level. Most of these differ in scope, range, and focus. As highlighted in CDP's 2025 strategy[2], the risk is that this trend will lead to the development of several different taxonomies that are incompatible with each other, increasing uncertainty and undermining their core goal.

Achieving consistency between regulatory requirements is paramount. The best way to achieve this would be to have one global taxonomy. Lacking that, and in light of the clear challenges in achieving an agreement on such an instrument, it will be critical to focus on creating a coherent disclosure system and, on equal footing, a common language for internationally agreed taxonomies to ensure data access, analysis and use by the investor community. Taxonomies structure information to enable greater connectivity between disclosure producers and users, while allowing for information to be easily searched, filtered and aggregated, and integrated into end-user technologies. In order to achieve this connectivity, it is essential for the data to be structured around agreed taxonomies and available digitally.

1 BIS (2021) 'A taxonomy of sustainable finance taxonomies'. https://www.bis.org/publ/bppdf/bispap118.pdf

2 CDP (2021) 'Accelerating the rate of change – CDP Strategy 2021-2025'. https://cdn.cdp.net/cdp-production/comfy/cms/files/files/000/005/094/original/CDP_STRATEGY_2021-2025.pdf

The global sustainable finance taxonomies landscape

Taxonomies should not be limited to climate-related activities but extend to other environmental issues.

Just before COP26, CDP published the policy brief **Shaping a Sustainable Financial System**[3], which included steps that policymakers should take with regards to taxonomies:

- Policymakers must develop internationally aligned taxonomies, using a common language but allowing for regional specificities;
- The principle of Do No Harm should form the basis of any taxonomy developed;
- Taxonomies should not be limited to climate-related activities but extend to other environmental issues. Climate may be a first stepping-stone, but the goal should be to get a comprehensive regulation for a wider range of environmental issues; and
- Taxonomies should be created in digital form, allowing systems to automatically read and work with the information contained, thus simplifying classification of investments.

While these recommendations are still highly relevant, much has changed since the launch of the policy brief. The number of taxonomies in development has further increased, the International Platform on Sustainable Finance has released the EU-China Common Grounds Taxonomy[4], and discussions have grown over the inclusion of certain activities (namely nuclear and natural gas) in the EU Taxonomy.

During this time, CDP has undertaken a project, funded by the Tipping Point Fund on Impact Investing (TPF), with the goal to:

- Conduct research and analysis of existing taxonomy systems being developed by policymakers (eg EU, China) and markets (eg Climate Bonds Initiative);
- Guide a strategy for the integration of taxonomies into CDP's disclosure platform; and
- Create a summary addressing alignment and remaining gaps of taxonomies that also outlines the internal CDP process for future taxonomies and recommendations.

3 CDP, Shaping a Sustainable Financial System (2021). https://www.cdp.net/en/policy-and-public-affairs/policy-briefings/shaping-a-sustainable-financial-system

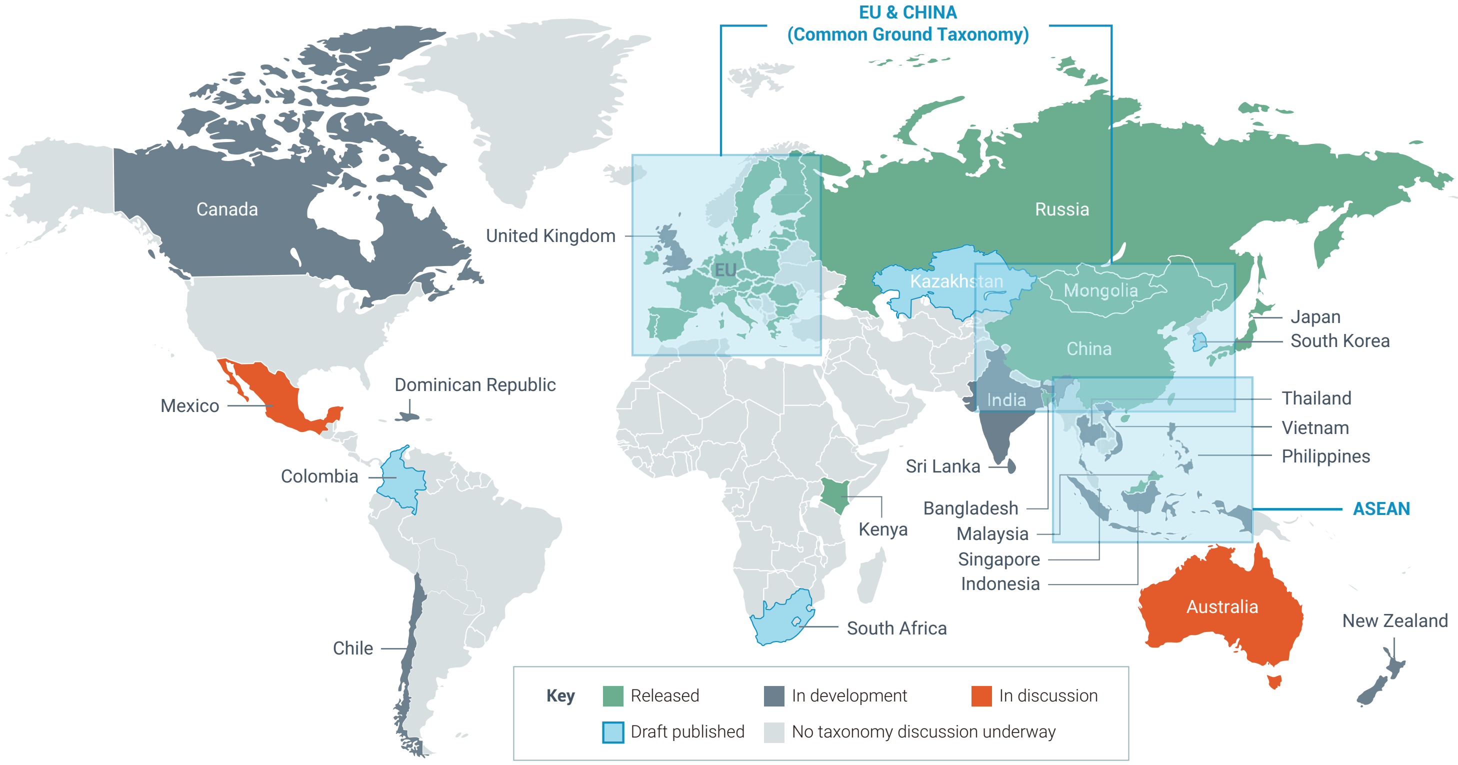
4 International Platform on Sustainable Finance on Common Ground Taxonomy (2021) 'Instruction Report'.

Taxonomy landscape

Taxonomy List*	Year of release**	
1. EU Taxonomy	2020	
2. China Green Catalogue	2015	
3. Japan	2017	
4. ASEAN	2021	
5. UK	2022	
6. India	TBD	
7. Canada	2021	
8. South Korea	2021	
9. Russia	2021	
10. Indonesia	2022	
11. Thailand	2025	
12. Philippines	TBD	
13. Singapore	TBD	
14. Malaysia	2021	
15. Bangladesh	2020	
16. South Africa	2021	
17. Colombia	2021	
18. Vietnam	2021	
19. Chile	TBD	
20. New Zealand	TBD	
21. Kazakhstan	2021	
22. Kenya	2019	
23. Sri Lanka	TBD	
24. Dominican Republic	TBD	
25. Mongolia	2019	
26. Common Ground	2021	
27. Climate Bonds Initiative	2013	Climate Bonds
28. MDBs-IDFC	2015	IDFC International Development Finance Club

* Sorted by 2020 GDP;
**year draft published, or likely to be released taken where taxonomy is yet to be finalised.

Source: Future of sustainable data alliance; Reuters; OECD Developing sustainable finance definitions and taxonomies.



Note: View reflective of Nov 2021. Mexico and Australia are in discussion about launching taxonomies;

In October 2021 the Bank for International Settlements (BIS) released a paper defining a "taxonomy of sustainable taxonomies"[5]. Key policy messages emerging from the BIS analysis are:

- Endeavor that taxonomies correspond to specific sustainability objectives;
- Encourage the development of transition taxonomies and focus alignment with the objectives of the Paris Agreement;
- Monitor and supervise the evolution of certification and verification processes; and
- Shift to mandatory impact reporting for green bonds.

5 Torsten Ehlers, Diwen (Nicole) Gao and Frank Packer (2021) 'A Taxonomy of Sustainable Finance Taxonomies'. https://www.bis.org/publ/bppdf/bispap118.pdf

CDP and FoSDA

CDP is proud to be a member of the Future of Sustainable Data Alliance (FoSDA): a global partnership of sustainability data providers aiming to identify and accelerate the reliable, actionable ESG data and related technology that is needed for improved investor decision making on the global journey to sustainable development. The FoSDA Taxonomy working group is working to create a Taxonomy repository, which will be an open-source database to capture critical features of sustainable finance taxonomies and keep track of taxonomy development worldwide. The repository will be a tool for navigating regulation and identifying similarities and differences between taxonomies.

Key elements for sustainable finance taxonomies classification

Using this and other sources, CDP, with the help of Bain Consultancy, ran an analysis of existing sustainability finance taxonomies, and identified eight elements that can help classify sustainable finance taxonomies. These elements are divided into three clusters:

Objectives:

- **Objectives beyond environment** – Taxonomies may be purely environment focused or extended to social issues;
- **"Do no harm" requirement** – Respondents may have to prove that an activity has no negative impacts on other goals; and
- **High level policy goals** – Definitions of "green" may be aligned to high-level policies (eg "net-zero" by 2050).

Scope:

- **Scope of activities** – May only cover green technologies or extend to broader activity set; in addition, the scope may expand over time;
- **Inclusion of "transition activities"** – These (eg natural gas) may be included within taxonomy, as a separate report, or not at all; and
- **Industrial classification** – May use different classification systems to define activities (eg NACE) at different levels of detail.

Detail:

- **Level of specificity** – Taxonomies can be principle-based (eg reduce emissions), activity-based (eg manufacture energy saving equipment) or project-based (a usual focus of green bonds taxonomies eg China's Green Bonds Catalogue); and
- **Binary or scale measure** – Classification as "green" may be binary (reaching a threshold) or scaled (eg traffic lights).

In addition, the analysis helped identify criteria for prioritization, all with the goal of identifying the most complete taxonomy to be first integrated into the CDP system. These criteria included **company reach** (number of companies affected by disclosure requirements) and whether **disclosure on the taxonomy is mandatory or voluntary**.

Taxonomy classification:
8 classification criteria agreed, plus 2 criteria for prioritization

PRELIMINARY

← Classification criteria – used to assess similarity to EU → **← Prioritization Criteria →**

Objective

Objective beyong environment

Taxonomies may be purely environment focused or extended to social issues.

'Do no harm' requirement

Respondents may have to prove an activity has no negative impact on other goals.

High level policy goals

Definitions of 'green' may be aligned to high level policies eg net-zero 2050.

Scope

Scope of activities

May only cover green technologies or extend to broader activity set; scope may expand over time.

Inclusion of 'transition activities'

Eg natural gas. May be included within taxonomy, as separate report, or not at all.

Industrial classification

May use different classification systems to define activities (eg NACE[1]) at different levels of detail.

Detail

Level of specificity

Taxonomies can be principles-based (eg reduce emissions), activity-based (eg manufacture energy saving equipment) or project-based (eg install boilers and smart meters).

Binary or scale measure

Classification as 'green' may be binary (reaching a threshold) or scaled (eg traffic lights).

Reach

Company reach

Taxonomies may impact a large number of companies (eg if released by large governmental organization) or a small number of companies (eg if released by small industry group).

Mandatory or voluntary

Reporting on taxonomies may be legally required, or may be done on a voluntary basis.

Note: (1) The industry standard classification system for economic activities used in the European Union.
Source: OECD library; Reuters; World Bank; ICMA; Bank for International Settlements;

As a result, an initial decision was reached to initiate an alignment process with the EU Taxonomy, as it is most complete against the criteria identified by CDP. However, the EU instrument is not free from sticking points: the inclusion of activities such as nuclear power generation and natural gas, together with questions about the lack of robustness of certain forestry criteria, have sparked discussions about the ground-breaking credentials of the EU Taxonomy[6]. This is especially true in light of the current energy crisis resulting in part from Russia's invasion of Ukraine[7].

For this reason, the suggested approach for CDP is now to focus on alignment with the best practice sustainable finance taxonomy criteria defined in the original proposal of the High-Level Expert Group on Sustainable Finance[8].

6 https://www.euractiv.com/section/energy-environment/news/ngos-walk-out-on-eu-green-finance-group-over-forestry-bioenergy-rules/
7 https://www.euractiv.com/section/energy-environment/news/lawmakers-urge-brussels-to-ditch-green-label-for-gas-in-eu-taxonomy/
8 https://ec.europa.eu/info/publications/sustainable-finance-high-level-expert-group_en

Mandatory environmental disclosure and the disclosure of taxonomy-aligned activities

As highlighted in CDP's Shaping High-Quality Mandatory Disclosure policy brief[9], mandating disclosure of environmental information from both companies and financial institutions supports several goals including de-risking investment, fighting greenwashing, and allowing countries to develop better policies that support the achievement of their Nationally Determined Contributions (NDCs).

As the global environmental disclosure system and the pioneer of environmental disclosure, CDP is a leader in this area.

A coherent disclosure system, with internationally agreed standards and taxonomies, is needed to ensure effective data access, analysis and use by the data users. While potentially challenging in terms of coordination and alignment between policies and regulations, creating a harmonized system would help support the investment decisions of capital market actors and help to prevent greenwashing[10]. An example is currently in development in the EU with the upcoming Corporate Sustainability Reporting Directive (CSRD), the Sustainable Finance Disclosures Regulation (SFDR), and the EU Taxonomy.

In the EU, the upcoming CSRD will require companies to publish a non-financial statement including information on how and to what extent the companies' activities are associated with economic activities that qualify as environmentally sustainable under the EU Taxonomy Regulation. In particular, non-financial companies must disclose the following key performance indicators (KPIs):

- the proportion of their turnover derived from products or services associated with taxonomy aligned economic activities;
- the proportion of their capital expenditure (CapEx); and
- the proportion of their operating expenditure (OpEx) related to assets or processes associated with taxonomy-aligned economic activities.

9 CDP, Shaping High-quality Mandatory Disclosure (2021) https://cdn.cdp.net/cdp-production/cms/policy_briefings/documents/000/005/863/original/TCFD_disclosure_report_2021_FINAL.pdf?1631608521.

10 According to a recent IOSCO paper, greenwashing is "the practice of misrepresenting sustainability-related practices or the sustainability-related features of investment products".

As of March 2022,

15

countries and territories have implemented or proposed to implement mandatory, Task Force on Climate-related Financial Disclosures (TCFD)-aligned climate disclosure.

4

countries have established voluntary, TCFD-aligned disclosure frameworks.

This information is intended to be used by different stakeholders, including financial market participants who are subject to the requirements of the Sustainable Finance Disclosures Regulation (SFDR). Activities aligned with the EU Taxonomy are included in the definition of **'sustainable investment'** as relating to SFDR Articles 8 and 9.

Given the strict connection just highlighted, taxonomies and mandatory disclosure of environmental activities should go hand in hand in order to provide full, comparable, and trustworthy data to capital market actors and policymakers. Where a sustainable finance taxonomy has been adopted, mandatory disclosure regimes should therefore include the disclosure of taxonomy-aligned activities.

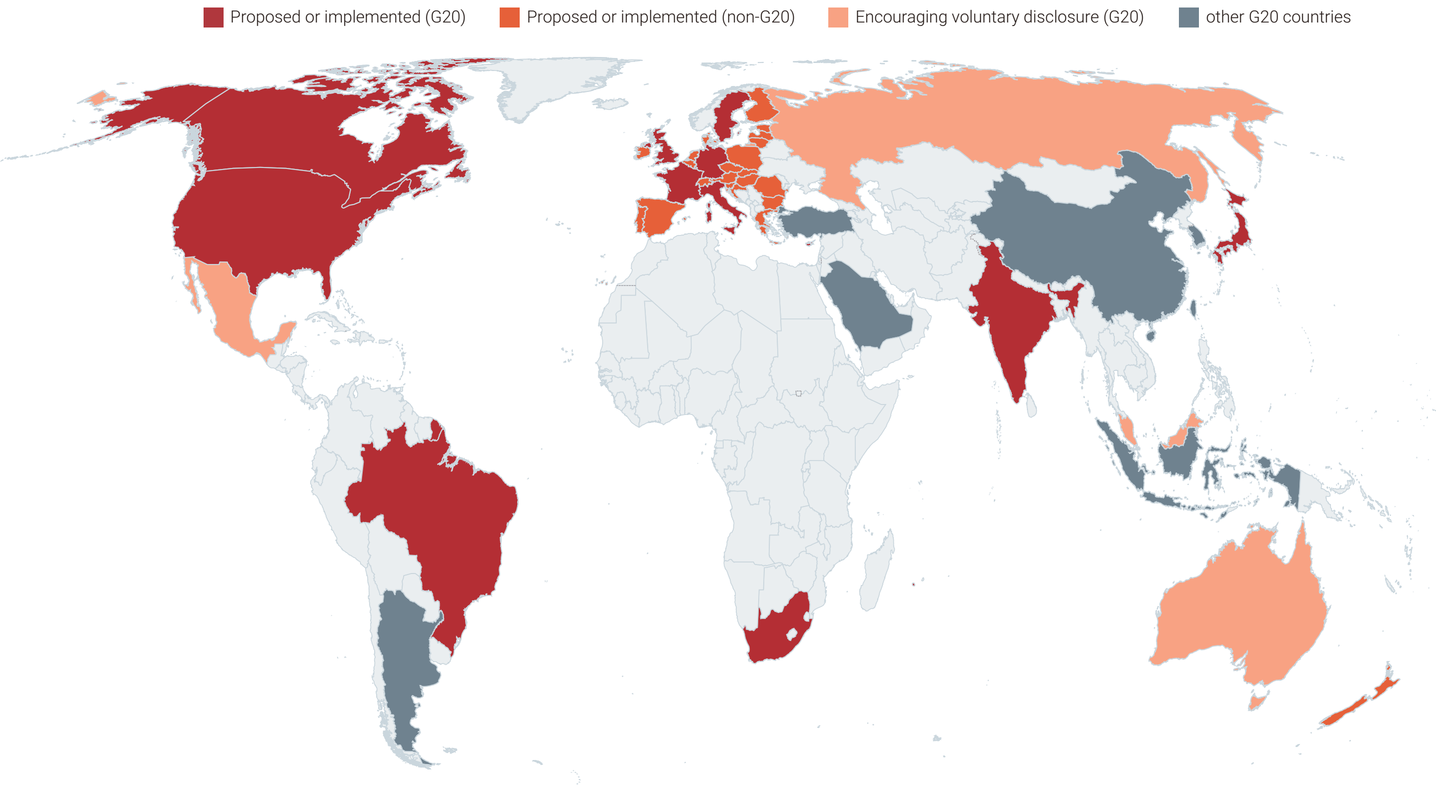
The EU is not the only place where mandatory disclosure regulation is currently being developed. As of March 2022, 15 countries and territories had implemented or proposed to implement mandatory, Task Force on Climate-related Financial Disclosures (TCFD)-aligned climate disclosure[11]. An additional four countries have established voluntary, TCFD-aligned disclosure frameworks[12]. In addition, in January 2022 China's Ministry of Ecology and Environment (MEE) issued new disclosure rules that will require domestic entities to disclose a range of environmental information on an annual basis, effective 8 February 2022[13].

11 These countries are: the UK; EU; US; New Zealand; Switzerland; Hong Kong, China; Japan; Taiwan; India; Brazil; Canada; South Africa; Norway (through NFRD); Singapore; and Malaysia.

12 Mexico; Chile; Australia; and Russia.

13 https://www.mee.gov.cn/xxgk2018/xxgk/xxgk02/202112/t20211221_964837.html

TCFD-aligned mandatory environmental disclosure around the world



Source: World Bank

Nb China is in the process of introducing a regulation on environmental disclosure. This is not currently aligned with TFCD. India accepts TCFD disclosures as compliant with its BRSR reporting requirements.

In some jurisdictions, disclosure requirements have been set for specific environmental factors. For example, CDP research found that a number of countries including Malaysia, China, and India have included mandatory disclosures related to water-related issues. This represents a particular interest for specific areas of environmental disclosure dictated by the most pressing environmental issues as perceived by policymakers. This adaptation of disclosure requirements to local characteristics is an element that has been identified (and in many cases hailed as a foundational principle) in the design of several taxonomies.

Just like specific disclosure requirements have been set by regulators around the world, the disclosure of taxonomy-aligned activities should be made mandatory. This would support meeting the goals highlighted in CDP's paper **Shaping High-Quality Mandatory Disclosure**[14], including that of ensuring compatibility of disclosure standards, and adhering to technical quality and content of the disclosure process.

14 CDP, 'Shaping High-quality Mandatory Disclosure' https://cdn.cdp.net/cdp-production/cms/policy_briefings/documents/000/005/863/original/TCFD_disclosure_report_2021_FINAL.pdf?1631608521

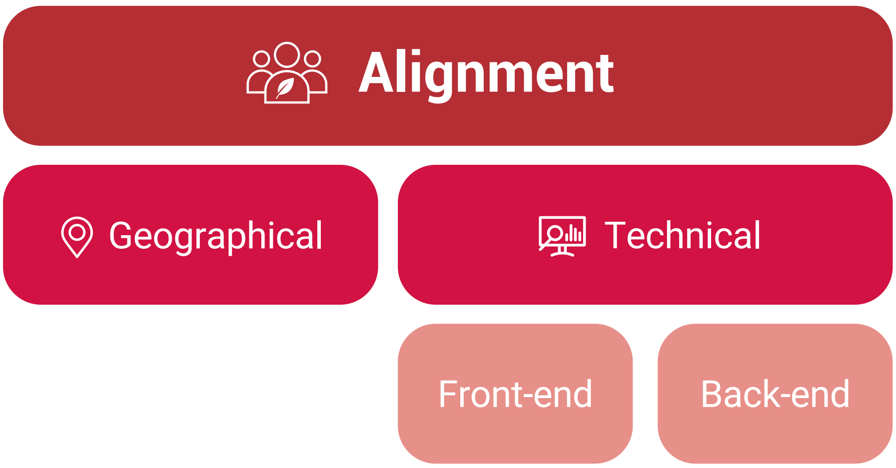
A proposed integration model of sustainable finance taxonomies into CDP's disclosure system

As previously stated, as the global environmental disclosure mechanism, CDP will accelerate the implementation and rollout of disclosure standards. As countries and regions introduce mandatory ESG disclosure requirements and taxonomies as tools to support these requirements, it is critical that they are reflected in CDP's questionnaires for CDP to continue its role in the implementation of standards at scale.

CDP's analysis of taxonomies in development, using the classification criteria highlighted above, aimed to identify the different approaches for integrating sustainable finance taxonomies into the CDP disclosure system. The EU Taxonomy was used as a case study to assess the steps and resources required through a detailed mapping process, with the following findings arising.

1 Alignment options for integration of sustainable finance taxonomies into CDP disclosure

Different types of potential alignment are relevant as CDP considers incorporating sustainable finance taxonomies into its questionnaires. These have been broken down in the following diagram, and each have implications that make different integration models more or less viable.



Geographical alignment

Geographical alignment involves declaring alignment with a particular taxonomy associated with a region or jurisdiction and implies support of it to the exclusion of others. To align in this manner, the taxonomy would need to be assessed against and conform to CDP's best practice criteria.

Geographical alignment has several implications which CDP must consider. CDP should:

- Maintain its position as a "super partes" disclosure partner for companies and regulators, and as a tool for implementing standards at scale; and
- Use its position as an implementation mechanism to influence the development of taxonomies.

CDP should not:

- Adopt others' definitions of 'green' as it is important to maintain the independence and gold standard of CDP scoring.

Technical alignment

Technical alignment involves aligning definitions and metrics with a particular taxonomy. For each taxonomy that CDP wishes to align with, a mapping exercise would need to be completed to understand how CDP's questionnaires and activity classification system relate to different parts of the taxonomy.

Technical alignment could be achieved through front-end or back-end alignment:

- *Front-end* alignment involves adjusting the CDP questionnaire content to match the taxonomy. To align to multiple taxonomies, this may require tailoring CDP questions to respondents' needs based on the taxonomies they wish to report.
- *Back-end* alignment involves translating the existing data submissions into taxonomy-aligned outputs based on respondents' needs for the taxonomy(s) they wish to report into. This would require no tailoring of CDP questions for different respondents.

CDP should clearly identify areas of a taxonomy (eg metrics, sectors etc) which are not covered, to ensure transparency for disclosing entities.

In the case of technical alignment, several implications would need to be considered. CDP should:

- Map CDP-ACS (CDP's classification system) to the activity classification system used by the taxonomy;
- Match the format of metrics (including units) to those within taxonomy wherever there is datapoint overlap;
- Clearly identify areas of a taxonomy (eg metrics, sectors etc) which are not covered, to ensure transparency for disclosing entities;
- Be additive to a company's other disclosures, eg by providing qualitative supporting evidence or enabling benchmarking; and
- Consider timings of the CDP disclosure cycle against the reporting cycle of the standards whose requirements refer to the taxonomies of interest.

CDP should not:

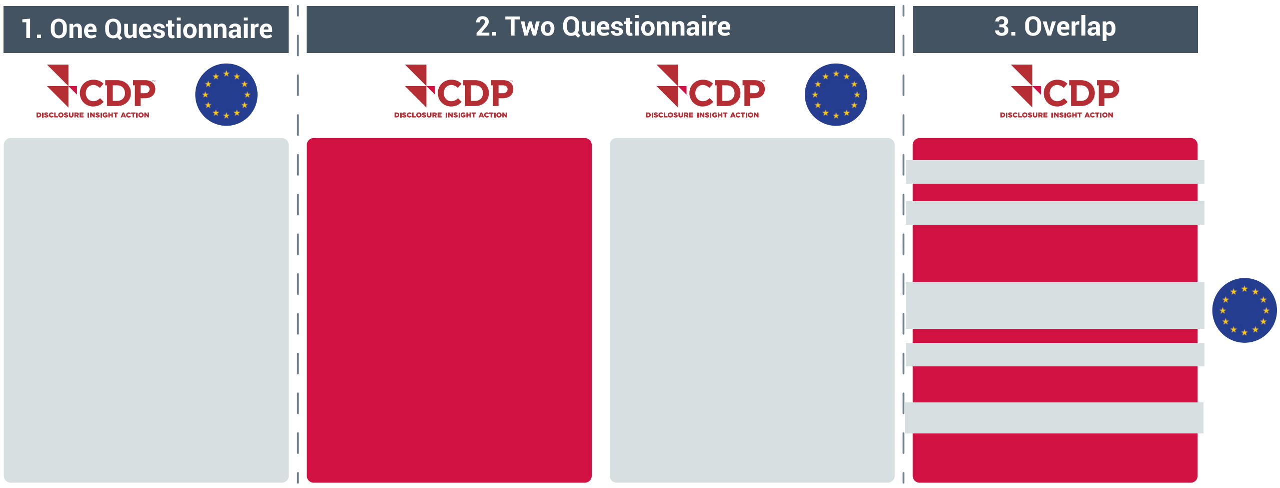
- Duplicate existing disclosure requirements – instead, CDP should leverage existing corporate disclosures and only ask for additional data when required for CDP scoring;
- Add significant additional disclosure effort since the CDP questionnaires already require a considerable amount of work to populate; and
- Increase CDP's response to score turnaround time, as this will limit the impact and relevance of CDP scores.

All these considerations led to the decision to focus on technical front-end alignment (ie adjusting the questionnaire and output to include elements of a particular taxonomy).

2 Approaches to implementation

Once confirmed that the focus would be on technical front-end alignment, the EU Taxonomy was used as a case study and three possible approaches to implementation were considered):

- **One questionnaire:** incorporation of all EU Taxonomy technical screening & Do No Significant Harm (DNSH) criteria, plus additional best practice questions extending beyond the EU Taxonomy.
- **Two questionnaires:** one questionnaire incorporating all EU Taxonomy technical screening & DNSH criteria for companies required to disclose information relating to the EU Taxonomy; one independent CDP questionnaire without EU Taxonomy criteria.
- **Overlap:** one questionnaire with some relevant, best practice EU Taxonomy technical screening & DNSH criteria, plus additional best practice questions extending beyond the EU Taxonomy.



The analysis **led to a preference for the third option – overlap**. The reasons are the following:

- The integration of relevant, best practice criteria from sustainable finance taxonomies into CDP's disclosure system is guided by CDP's mission: to focus investors, companies, cities, and governments on building a sustainable economy by measuring and acting on their environmental impact;
- Allows for additional EU Taxonomy questions and/or datapoints to 'slot in' to the existing questionnaire content, reducing questionnaire upheaval and providing a simpler and smoother user journey for disclosing companies;

- Avoids including datapoints that aren't relevant to CDP's strategic ambitions and priorities, avoiding additional disclosure effort and focusing on adding value for disclosing companies;
- Allows CDP to provide globally comparable data for EU and non-EU companies whilst maintaining relevance to both; and
- Allows CDP to go beyond the EU Taxonomy and maintain independence when defining a 'gold standard' for green activities.

Following the decision regarding the approach for technical alignment, several further activities were carried out to complete the process.

Exploring taxonomy integration using the example of the EU Taxonomy

To better understand how CDP could integrate best practice elements of the EU Taxonomy into disclosure, an initial analysis was undertaken to map CDP's activity classification system (CDP-ACS) to that proposed by the EU. Due to differences, a 'self-selection' model was proposed, where, if CDP were to decide to capture activity-level EU Taxonomy data, companies would be asked to select the EU Taxonomy Activities relevant to them in an introductory question.

At the time of writing, technical screening and Do No Significant Harm (DNSH) criteria were only available for the first two of the EU Taxonomy objectives (climate change mitigation and climate change adaptation), so the mapping exercises detailed here were focused on these objectives. As these are most relevant to the CDP climate change questionnaire for companies, this questionnaire is the focus throughout the discussion[15].

The research found that around three quarters of EU Taxonomy activities include a quantitative metric as part of the associated climate change mitigation screening criteria. Where a metric is included, the majority of these were either fully or partially aligned with the CDP questionnaire. To provide a full set of data supporting the mandatory reporting disclosures involving the EU Taxonomy, CDP would have to include all quantitative metrics found within the EU Taxonomy climate change mitigation screening criteria, along with significant additional qualitative information. The alignment between the CDP questionnaire and the high-level climate change adaptation criteria was found to be strong, but EU Taxonomy-specific guidance would need to be added to highlight relevant areas for disclosure. The principle of DNSH is not currently adequately captured within the CDP questionnaire because environmental topics are segregated into distinct questionnaires, and due to the detail relating to specific EU regulation.

15 It is worth highlighting that companies assessing their alignment with the EU Taxonomy should also undertake a qualitative assessment against minimum social safeguards. However, social aspects are currently beyond the scope of CDP's work, so they have not been included in this study.

3 The findings of the sustainable taxonomy alignment scoping project

CDP should map and analyze current and emerging priority sustainable finance taxonomies to identify key areas which build on corporate best practice and leverage those key areas by integrating them into the CDP questionnaires and scoring.

Following the analysis of the taxonomy landscape and the scoping exercise of potential taxonomy integration into the CDP questionnaire using the EU Taxonomy as an example, the conclusion was reached that it is not recommended to fully and directly integrate any specific sustainable finance taxonomy into the CDP system. Rather, CDP should map and analyze current and emerging priority sustainable finance taxonomies (ie those most similar to CDP's best practice sustainable finance taxonomy criteria) to identify key areas which build on corporate best practice and leverage those key areas by integrating them into the CDP questionnaires and scoring. This will make the most of CDP's unique position as a tool to implement standards and bring them to life in the real economy.

CDP's unique disclosure mechanism is both an acid test and source of innovation for standards and its power comes from being able to implement standards globally at scale. By its very nature, it supports standardized information generated via high-quality disclosure processes that are continually improving, and that enable the tracking of progress against targets, transition plans and performance. It is a tool for policymakers and companies to explore new areas of environmental action.

The decision not to fully and directly integrate specific sustainable finance taxonomies is justified for the following reasons:

- If fully integrating one sustainable finance taxonomy, to avoid geographical alignment with a specific region or jurisdiction CDP would need to fully integrate all future priority sustainable finance taxonomies. However, this is not future-proof due to the amount of questionnaire upheaval that would be required, potential conflicts between taxonomies, and the level of ongoing commitment necessary to monitor the taxonomies as they develop;

- There is no suitable approach which would allow CDP to be the repository of data to fully facilitate disclosure against a sustainable finance taxonomy, whilst also avoiding geographical alignment;
- It can support regulatory convergence by highlighting the most relevant activities and providing proof points on the adoption of specific elements of the different taxonomies;
- CDP should build on the areas where sustainable finance taxonomies fall short, and not adopt others' definitions of "green" because it is important to maintain both CDP's position as a trusted, independent source of data, together with its independent scoring methodology. This will ensure CDP is focused on its mission of implementing best practice within disclosing companies;
- By integrating relevant priority areas from sustainable finance taxonomies (ie as per Option 3 - Overlap of the proposed integration model), CDP can still maintain its relevancy to disclosers who have taxonomy-related mandatory disclosure requirements, without duplicating or heavily increasing their disclosure effort. To make the disclosure process easier for the respondent, CDP should clearly indicate taxonomy-related datapoints to disclosers and where elements of a taxonomy have not been integrated;
- The process of identifying areas of integration for detailed sustainable finance taxonomies via mapping exercises is time-consuming and complex – this should not be underestimated when prioritizing taxonomies to integrate to some degree into the CDP disclosure system; and
- Regardless of the integration approach, significant resources would be required once the decision to align to a taxonomy to some degree has been made, not only to adequately map the CDP disclosure system against a taxonomy and integrate the relevant priority areas, but also to continually monitor and keep up to date with future developments and modifications to the taxonomy.

CDP will continue to refine this integration model and work to identify how best to integrate sustainable finance taxonomies into its system.

Conclusion and policy recommendations

With several taxonomies under development, and while acknowledging that one global taxonomy working across different jurisdictions is unlikely in the foreseeable future, CDP **recommends policy makers to:**

- **Identify and adopt a common baseline, together with identifying linkages among taxonomies.** CDP encourages this in order to avoid policy fragmentation and encourage interoperability.
- **Ensure alignment of taxonomies to the high level policy goals,** in order to allow the capital allocation towards the policy agenda.
- **Align sustainability taxonomies against disclosure requirements.** Linkages should be made between the taxonomy criteria and economy-wide disclosure requirements. Where these requirements are put in place, they should include disclosure of taxonomy-aligned activities.
- **All ESG topics should be included.** If not, a plan should be in place to expand the scope of the taxonomy within time bound frames.
- **Ensure large scope of entities required to comply with the taxonomy** (ie issuers of green bonds, corporations, financial institutions, etc) should be as wide as possible, and a plan should be in place to extend compliance requirements to all capital markets actors.
- **Threshold and criteria should be used to assess activities.** In addition, these classifications and related tools should be science-based.
- **Transition activities and pathways should be timebound.** They should represent an improvement over the status quo. Moreover, particular attention should be given to those transition activities that require remedial efforts. CDP suggests ensuring the taxonomy does not conflate green and transition activities, and that there is a plan for transition requirements to become more stringent over time.
- **Sector coverage should extend as wide as possible.** If not all sectors, taxonomies should cover all high-emitting sectors and a plan should be put in place for the taxonomy to eventually cover all sectors.

All the criteria identified above can support the design of what this best practice should look like within sustainable finance taxonomies, which should cover a multitude of topics, interlinked by the “do no significant harm” principle and, as far as possible, be aligned to high level policy goals.

The scope of the activities involved should not only consider activities that contribute to the environmental objectives set out in the taxonomy but also ones that may play a part in the transition to a more sustainable and resilient financial system: go beyond “**green**” to identify different “s**hades of brown**".

DISCLOSURE INSIGHT ACTION

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ABOUT CDP

CDP is a global non-profit that runs the world's environmental disclosure system for companies, cities, states and regions. Founded in 2000 and working with more than 680 financial institutions with over $130 trillion in assets, CDP pioneered using capital markets and corporate procurement to motivate companies to disclose their environmental impacts, and to reduce greenhouse gas emissions, safeguard water resources and protect forests. Over 14,000 organizations around the world disclosed data through CDP in 2021, including more than 13,000 companies worth over 64% of global market capitalization, and over 1,100 cities, states and regions. Fully TCFD aligned, CDP holds the largest environmental database in the world, and CDP scores are widely used to drive investment and procurement decisions towards a zero carbon, sustainable and resilient economy. CDP is a founding member of the Science Based Targets initiative, We Mean Business Coalition, The Investor Agenda and the Net Zero Asset Managers initiative.

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