Reporting Taxonomy Alignment Under CSRD for Asset Managers

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In 2024, large listed EU companies came into scope of the EU's Corporate Sustainability Reporting Directive ("CSRD"). These companies will report in 2025 information on sustainability-related impacts, risks and opportunities arising from their business operations and value chains in their annual financial reports for 2024, in line with the European Sustainability Reporting Standards ("ESRS"). Large private EU companies come into scope in 2025 and will have to report in their financial reports for 2025 in 2026.

CSRD also requires a company to report on the extent that its activities are environmentally sustainable economic activities under the EU Taxonomy Regulation and its Commission Delegated Regulations (together, the "Taxonomy"), and to obtain a limited assurance opinion from a third-party assurance provider to verify this information. The Taxonomy contains the technical criteria for activities, such as renewable energy generation and low energy manufacturing and infrastructure, to be classified as environmentally sustainable economic activities. The European Securities and Markets Authority announced in October 2024 that reporting on Taxonomy alignment is one of its key enforcement priorities for 2024 annual reports.

This note outlines the requirement for asset managers, which are in scope of CSRD as large listed or private companies, to report Taxonomy alignment under CSRD.

Framework

Reporting on Taxonomy alignment is governed by a Delegated Regulation to the Taxonomy (the "Delegated Regulation"), together with draft Guidance and FAQs published by the European Commission in December 2023 and December 2021 respectively (collectively, the "Guidance"). The Delegated Regulation governs reporting on Taxonomy alignment by "financial undertakings" (which are asset managers, investment firms, insurers and credit institutions in scope of CSRD) and "non-financial undertakings" (which are all other types of companies). The Delegated Regulation includes templates for how financial and non-financial undertakings report on Taxonomy alignment.

Asset managers report on Taxonomy alignment under CSRD only by reference to the Taxonomy alignment of investee companies in their portfolios, resulting in this calculation:

$$\frac{\text{Weighted average value of all investments that are directed at funding, or are associated with Taxonomy-aligned economic activities } \textbf{[numerator]}}{\text{Value of all Assets under Management } \textbf{[denominator]}}$$

An asset manager will report Taxonomy alignment of its portfolio by reference to two broad types of exposure to underlying investments.

Exposures to investee companies reporting under CSRD

An asset manager will report the aggregate value of its equity and debt exposures to EU investee companies, based on those investee companies' separate reporting on Taxonomy alignment under CSRD, which will be subject to external assurance and available publicly. It is important to note on this obligation that:

- Asset managers are not required to include in their report on Taxonomy alignment under CSRD any data on Taxonomy alignment that they may collect from companies that are not in scope of CSRD (subject to the below exception, for loans or bonds with use of proceeds aligned with the Taxonomy);
- Where an investment is held through a special purpose vehicle ("SPV"), the asset manager will generally look through the SPV to the underlying investee company for the purpose of Taxonomy reporting;
- When an asset manager is in scope of the world-wide group reporting obligation (from 2028), that obligation does not include Taxonomy reporting.

Loans or bonds where the use of proceeds is aligned with the Taxonomy

If an asset manager invests in a company which issues bonds or debt securities for the purpose of financing environmentally sustainable economic activities (in line with the EU's green bond standard, applying in December 2024, or under a similar private framework), then it will include the value of these bonds or debt securities in the aggregate value of its equity and debt exposures to EU investee companies, based on the issuer's reported Taxonomy alignment. This is regardless of whether or not the underlying company which issued the debt or bonds is itself in scope of CSRD.

Reporting Taxonomy alignment

For both types of exposure, an asset manager will report the information in the form of the template in the Delegated Regulation. The template includes the result of the calculation above, with the numerator reported as a percentage of all assets under management, as well as an absolute monetary value. The asset manager will disclose the Taxonomy alignment reported by its investee companies, by reference to their turnover and capital expenditure. The Delegated Regulation also requires an asset manager to make additional ‘complementary’ disclosures, which include a break-down of the numerator of the key performance indicator (“KPI”) amongst the six environmental objectives listed in the Taxonomy, as well as information on Taxonomy eligibility and alignment. As provided in a separate template in the Delegated Regulation, an asset manager should also publish additional qualitative information (including relevant contextual information), to help readers understand its KPI data.

As mentioned above, the numerator will not include the value of investments in companies which are themselves not subject to CSRD, except where those investments are in environmentally sustainable bonds and debt securities.

Requirements for specific asset classes

The Guidance includes statements on reporting Taxonomy alignment for specific asset classes. For instance, where an asset manager acquires a stake in another fund such as an AIF or UCITS (for example, as part of a secondaries strategy), it should use the turnover and capital expenditure-based KPIs of the asset manager which manages that AIF or UCITS. Asset managers should not use, for this purpose, the Taxonomy KPIs that an underlying asset manager of the AIF or UCITS may report for a particular fund under the Sustainable Finance Disclosure Regulation (“SFDR”) — although an asset manager may report that information on a voluntary basis, presented separately. The Guidance is based on the principle that, whilst large asset managers are in scope of CSRD, individual AIFs or UCITS are exempt. However, this outcome is controversial, as an asset manager reporting under CSRD will rely on the general information published by the underlying asset manager in respect of all of its funds under management, rather than the specific AIF or UCITS in which the asset manager has acquired an interest.

Exposures to securitisations are dealt with in the Guidance in a similar manner to exposure to SPVs, requiring asset managers to look through the securitisation SPV to any companies to which the securitisation is exposed, and obtain Taxonomy alignment data from those companies, to the extent the companies are in scope of CSRD. How this will work in practice will depend on the assets on which the securitisation is based. For example, if the securitisation vehicle invests in corporate debt, this implies that an asset manager is required to assess Taxonomy alignment at the level of those underlying corporate borrowers, which may be challenging to do in practice, given the absence of data and the degree of separation between the asset manager and these underlying borrowers.

Investments in sovereign bonds and bonds issued by other supranational issuers are excluded from the calculation altogether. The value of derivatives is excluded from the numerator.

Practical implications

Given that few companies are in scope of CSRD yet, an asset manager in scope of CSRD may find that it cannot practically report on its Taxonomy alignment, as none of its investee companies have published their own sustainability reports. As large EU private companies come into scope of CSRD for financial years starting on or after 1 January 2025, their reports will not be available until mid-2026 at the earliest.

The Guidance states that an asset manager can consider an investee company which has not yet reported under CSRD as not Taxonomy-aligned for the purpose of its reporting, and explain this is the case in the sustainability report.

The Guidance invites (but does not require) asset managers to consider reporting Taxonomy alignment data from other sources on a voluntary basis. This includes information from investee companies which are reporting Taxonomy alignment data, but are not required to do so under CSRD, or information that the asset manager has sourced from an investee company which has not been subject to the assurance process under CSRD. An asset manager may disclose this information in its own report, in a separate section, making clear the sources of this data. Asset managers will need to consider whether any information reported on a voluntary basis is subject to assurance, and the additional work-load that will create.

Next Steps

Asset managers will need to apply the Taxonomy reporting requirement to each of their asset classes, with a process to determine whether each underlying investee company is in scope of CSRD, and determine when that investee company's report is available. Although many asset managers will have limited Taxonomy-aligned data to report for their first year of reporting, they will still need to include in the template report data on, for instance, whether investee companies are EU and non-EU financial and non-financial undertakings, and whether investee companies are in scope of CSRD.

We are available to discuss these requirements in more detail, and to assist in developing a Taxonomy alignment reporting strategy on a case-by-case basis, tailored to the business models and strategies of particular asset managers.

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Please do not hesitate to contact us with any questions.

Patricia Volhard
Partner, Paris, Frankfurt, London
Tel: +33 1 40 73 12 12
Tel: +49 69 2097 5150
pvolhard@debevoise.com

Jin-Hyuk Jang
Counsel of Debevoise & Plimpton LLP/ Partner of Debevoise & Plimpton Europe S.à r.l., Frankfurt
Tel: +49 69 2097 5115
jhjang@debevoise.com

John Young
Counsel, London
Tel: +44 20 7786 5459
jyoung@debevoise.com

Alfie Scott
Associate, London
Tel: +44 20 7786 5478
awscott@debevoise.com

Eike Björn Weidner
Associate, Frankfurt
Tel: +49 69 2097 5220
ebweidner@debevoise.com