

Final Report on Social Taxonomy

Highlights of the PSF proposal



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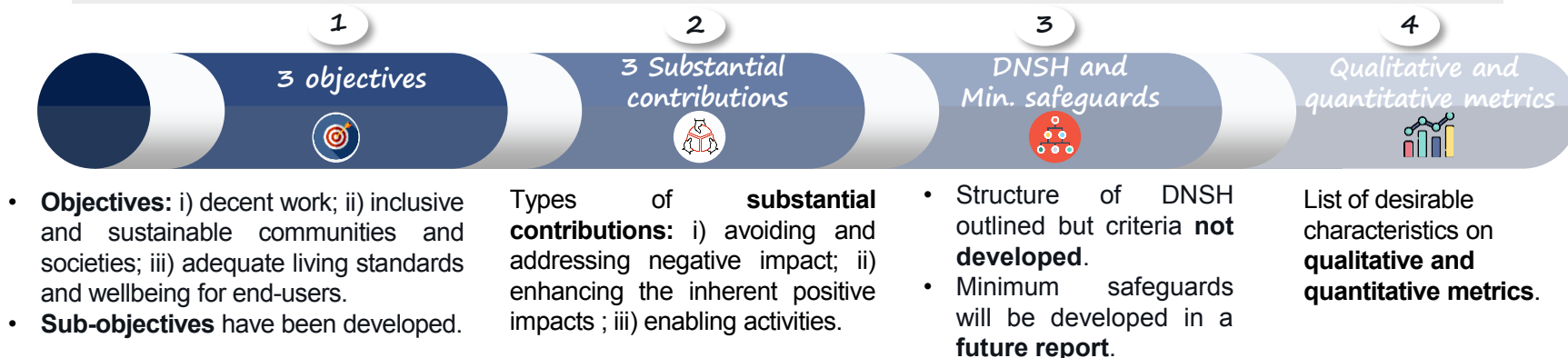


1 | Executive summary

In the Final Report of a Social Taxonomy the PSF summarises the initial observations and recommendation on the mandate given by the EC to work on extending the taxonomy to social objectives

| 1-Application | 2-Regulatory context | 3-Next steps |
|--|---|--|
| This paper constitutes an input for the definition of the final objectives by the EC and might not be the final objectives that the EC will use. | Art. 26 of the TR mandates the EC to elaborate a report to extend the initial objectives to social objectives. For this propose, the EC established the PSF (Art. 20), which shall advise the EC in the matter. | <ul style="list-style-type: none">• The PSF and the EC to deepen in some of the aspects of the study.• The EC to publish the final report of the TR. |

The PSF outlines the key elements of the social taxonomy¹ following the steps of the environmental taxonomy²:



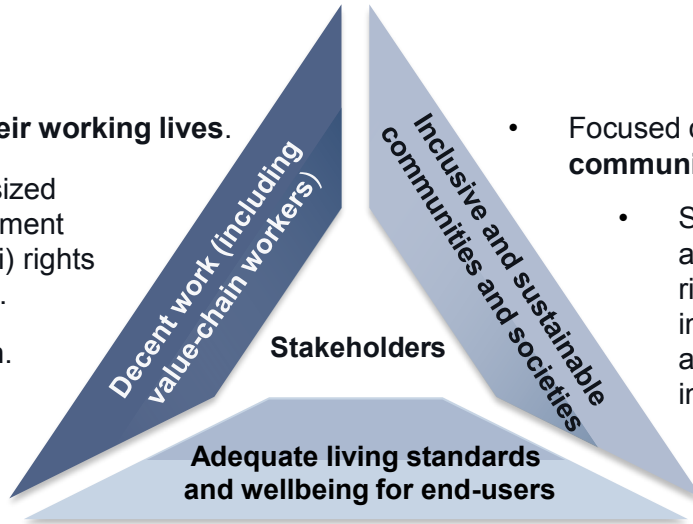
2 | Articulating and setting social objectives

Defining the objectives

Three objectives for a social taxonomy: i) decent work; ii) adequate living standards and wellbeing for end-users; and iii) inclusive and sustainable communities and societies¹



- Focused on people in **their working lives**.
- **Four pillars**, (that are emphasized with sub-objectives): i) employment creation, ii) social protection, iii) rights at work and iv) social dialogue.
- Not limited to the **European Union**.



- Focused on the impacts of **activities on communities and the wider society**.
- Sub-objectives **emphasize issues** such as: i) land rights; ii) indigenous people's rights; iii) human-rights defenders; and iv) improving/maintaining the accessibility and availability of basic economic infrastructure.



- Focused on people in their role as **end-users** of certain **products and services**.
- Sub-objectives will emphasize aspects related to **consumer protection** and the realization of economic and social rights: i) right to health; ii) food, iii) housing and iv) education.




(1) For more information on how the objectives are defined see [Annex III](#)

2 | Articulating and setting social objectives

The development of sub-objectives

Each objective includes a list of sub-objectives which emphasize the content of the objective and ensures that various aspects integral to these objectives can be addressed

The sub-objectives must cover all the **essential topics of each objective without overlapping between them.**

| Objectives | Topics | | | |
|---|--------------------------------------|--|--|--|
|  <p>1- Decent work</p> | Promoting decent work | Promoting equality and non-discrimination at work | Respect for the human rights and workers' rights | |
|  <p>2- Adequate living standards and wellbeing for end-users</p> | Healthy and safe products | Durable and repairable products | Protection of personal data and privacy | Responsible marketing practices |
|  <p>3- Inclusive and sustainable communities and societies</p> | Equality and inclusive growth | Sustainable livelihoods and land rights | Respect for the human rights of affected communities | |

Non-Exhaustive

2 | Articulating and setting social objectives

Types of substantial contribution

Three types of substantial contributions: i) avoiding and addressing negative impact; ii) enhancing the inherent positive impacts; and iii) enabling activities

Avoiding and
addressing negative
impact

Targeting:

- **High-risk sectors** with documented human-rights and labor-rights abuses of relevance to the objective.
 - Sectors that are **less likely to contribute** to the objectives of the European social pillar.
- E.g: Improving OHS*

Enhancing the inherent
positive impacts

Targeting:

- Social goods and services sectors that provide goods and services for basic human needs.
 - **Basic economic infrastructure** of direct relevance to the right to an adequate standard of living.
- E.g: Providing affordable pharmaceuticals to certain groups of people.*

Enabling activities

- Having the potential to enable **substantial risk reductions** in other sectors.
- E.g: Social auditing services which help to reduce negative impacts on value-chain workers.*

2 | Articulating and setting social objectives

DNSH criteria, selecting sectors, CapEx & OpEx

DNSH criteria ensure that when an activity makes a substantial contribution to one social objective, it does not harm the other social objectives. On the other hand, an economic activity based framework is required to underpin the social taxonomy. These activities are linked with CapEx, OpEx or turnover

DNSH

DNSH criteria which must be **developed at the level of the sub-objectives**. For example, an economic activity that makes a substantial contribution to living wages should not: i) harm equal employment opportunities for women; ii) undermine collective bargaining processes; iii) use child or forced labour in supply chains.

Selecting sectors

It is needed to justify a prioritization of the sectors for each objective and sub-objectives. A methodology has been developed based on the use of the framework of economic sectors and activities (determined by the NACE industrial classification system) and considering the selection of the relevant sectors (according to the criteria defined to determine the substantiality of the activities): i) sectors that avoid **negative impacts**; ii) that enhance **positive impacts**; iii) the sectors that **enable said positive impacts**.

KPIs

Linking **CapEx, OpEx and turnover** to social activities build on the differentiation between 'reducing negative impacts' on the one hand and 'enhancing inherent social benefits' on the other.

1. A company's investments made to address and avoid their negative impact might count as a social contribution (e.g. the expenditure for training as defined in a social taxonomy will count as socially sustainable). **The amount of this investment would then be reflected as OpEx.**
2. This might be different if a **whole bundle of social criteria is attached to an activity**, such as for a fair-trade product or a mineral sourced from a mine with an approved social certificate. In this case, it might be that the **turnover made with the sale of the product** will be counted as socially sustainable.
3. Finally, it is suggested that the company selling the product/service which **enables** other company to address and avoid negative impacts, counts the **turnover made with these products/services as 'socially sustainable'**.

2 | Articulating and setting social objectives

NACE sectors classification

The PSF has set some examples of the different sectors related to the different objectives and selected sub-objectives, which can be classified according to NACE codes¹

Objective 1: Decent work

| Sub-objective | Sectors | Related NACE | Substantial contribution criteria |
|---------------------------------------|--|----------------------------------|--|
| Occupational health and safety | e.g: 1. mining and quarrying 2. manufacturing; 3 construction; 4. agriculture, forestry and fishing; 5. transportation and storage; and 6.electricity, gas, steam and air conditioning supply | 1. B; 2. C; 3.F; 4.A; 5.H; 6.D | Addressing and avoiding negative impacts |
| Training | e.g ² : 1. manufacturing; 2. education; 3. human health and social work activities; 4. arts, entertainment and recreation; 5. other services activities | 1.C; 2.P; 3.Q; 4.R; 5.S | Addressing and avoiding negative impacts |
| Diversity and inclusion | Relevant in all sectors | - | Addressing and avoiding negative impacts |
| Living wage | All sectors (in particular sectors with many workers on lower wage); Sector exposed to international competition (e.g. 1- textiles); Sectors exposed to social dumping (e.g. 2. agriculture); Labour-intensive sectors with little added value (e.g. 3 - some construction sub-sectors). | 1. C13, G46.4. G47.5.1; 2.A; 3.F | Reducing negative impacts for workers |
| Not specified | e.g: social audits | M69.2 | Enabling activities |

Non-Exhaustive

(1) For the social taxonomy, NACE may in some areas **need to be supplemented** by additional categories, where the current level of granularity within NACE is not sufficient.

(2) Example of sectors with [skills shortages according to OECD](#)

2 | Articulating and setting social objectives

NACE sectors classification

The PSF has set some examples of the different sectors related to the different objectives and selected sub-objectives, which can be classified according to NACE codes

| Objective 2: Adequate living standards and wellbeing for end-users | | | |
|--|---|--|--|
| Sub-objective | Sectors | Related NACE | Substantial contribution criteria |
| Access to housing | e.g: building and managing apartments and houses | F.41.20 | Enhancing the positive impact inherent in an economic activity |
| Access to health | e.g: 1. water, including waste-water management; 2. food, including the food value chain; 3. housing; 4. healthcare, including care work; 5. education (including vocational training); | 1. E, C11.0.7, F42.9.1; 2. C10, C28.9.3, G46.1.7, G46.3, G47.2, I; 3. F.41.20; 4 Q; 5. P | |

Non-Exhaustive

| Objective 3: Inclusive and sustainable communities | | | |
|--|---|---|--|
| Sub-objective | Sectors | Related NACE | Substantial contribution criteria |
| Supporting sustainable livelihoods and land rights | e.g: 1. agriculture, forestry and fishing, 2. mining, 3. electricity, 4. construction, 5. transportation and storage. | 1. A; 2.B; 3.D; 4.F; 5.H | Addressing and avoiding negative impacts |
| Promoting equality and inclusive growth | e.g: 1 transport; 2. telecommunications including the internet; 3. financial services; and 4. electricity | 1.H49,H50,H51,N77.3.4, N77.3.4; 2.J61; 3. K; 4.C27.1, D | Enhancing the positive impact inherent in an economic activity |

3 | Technical Screening Criteria

Qualitative and quantitative metrics

Stakeholder-centric technical screening criteria would ultimately include qualitative and quantitative metrics and thresholds that target key business impacts on these stakeholder groups

- Some of the data needed for social criteria (for example on staff wages, health and safety) are already at the disposal of companies and official bodies. In addition, the **EFRAG taskforce** is currently working out non-financial reporting requirements on the three stakeholder groups.
- For further consideration, the Platform suggests the following criteria for indicators for a social taxonomy:



- ✓ **Relate to a norm, process or goal** in internationally **recognized standards**, such as the UN guiding principles, the SDGs, the EU Social Charter and the EU pillar of social rights.
- ✓ The indicator must be a **good proxy** for the objective it addresses.
- ✓ The indicator should be specific enough to relate it to an **economic activity**.
- ✓ The indicator must have a **clear direction**. For example, when evaluating complaint mechanisms, we should ask the following questions: Is it good if there are many complaints, as this shows that workers trust the complaint mechanism?
- ✓ The indicator should be **precise** so that there is no doubt whether an activity fulfils it or not.
- ✓ Indicators should avoid **driving perverse incentives** or unintended consequences, such as unintendedly driving divestments from SMEs.
- ✓ Data should be **available at reasonable cost**. Differences between larger and smaller companies should be considered.

4 | Reflections and Next steps

Considering all the analysis carried out, the PSF suggests what should be the next steps for the development of the Social Taxonomy by the EC

Reflections

There are still many unanswered questions as to what a social taxonomy will look like and what the relationship between a social and an environmental taxonomy will be.

Due to the impact on the market participants, the social taxonomy will have a knock-on effect on economic entities, which will strive to **be recognized as 'social' investments, provide the necessary data, intensify efforts on social economic activities, and implement the necessary processes.**

Next Steps appointed by the PSF

1. Clarify the **minimum safeguards**;
2. Conduct a **study on the impacts of a social taxonomy** considering different options for application and designs;
3. Work out a **rationale for prioritizing objectives and sub-objectives**;
4. Prioritize objectives **according to the rationale**;
5. Define **substantial-contribution and DNSH criteria** for the first objective(s) and sectors.

EFRAG mandates

Under the CSRD proposal (art 49.3), EFRAG would develop draft EU Sustainability Reporting Standards. The timeline contained in the proposal assumes the elaboration of draft sustainability reporting standards in parallel to the legislative process of the proposed CSRD. In order to respect tis timelines, EFRAG should aim to submit the first set of standards by **15 June 2022**¹.

A₁ | Summary of the methodology

These examples do not represent fully worked out criteria of a social taxonomy. Instead, they should be considered as sketches to illustrate how the suggested structure would work in practice

Objective: Decent work, sub-objective: training

| | Rationale for selecting sectors | | |
|---|--|---|---------------------------------------|
| Selection of sectors | High-impact NACE codes could be selected via: <ol style="list-style-type: none"> 1) sectors with skills shortages – according to OECD and EU data 2) sectors negatively affected by the green transition or digitalization with risks of layoffs and therefore a special need to train certain groups of employees 3) sectors with general shortages of skills. | | |
| | Reducing negative impacts for workers | | |
| Type of Substantial contribution | The entity runs extensive programs for skills and lifelong learning/upskilling/reskilling for workers in situations of vulnerability. There is a high level of worker involvement in the development of these programs (OpEx for training). | | |
| | Decent work | Adequate living standards and wellbeing for end-users | Inclusive communities & societies |
| DNSH | Workers must be paid at least the national minimum wage, where available, or according to negotiations and collective bargaining by social parties. ILO core labor standards must be met. There must be adequate OHS. | N/A | No discrimination in training offers. |



A₁ | Example of social taxonomy structure

These examples do not represent fully worked out criteria of a social taxonomy. Instead they should be considered as sketches to illustrate how the suggested structure would work in practice



Objective: Adequate living standards and wellbeing for end-users, sub-objective: access to housing

| | | | |
|--|---|---|---|
| <p>Selection of sectors</p> | <p>Rationale for selecting sectors</p> | | |
| <p>Substantial contribution</p> | <p>Enhancing positive impact inherent in economic activity (examples)</p> | | |
| <p>DNSH</p> | <p>Decent work</p> | <p>Adequate living standards and wellbeing for end-users</p> | <p>Inclusive communities & societies</p> |
| <p>ILO core labor standards must be met. There must be adequate OHS. Minimum wage must be paid to workers.</p> | <p>Guarantee quality (examples) Meeting internationally accepted standards of quality</p> | <p>Effluent must not pollute drinking water.</p> | <p>Effluent must not pollute drinking water.</p> |



A₂ Differences between environmental and social taxonomy

It is recommended that the development of a social taxonomy follow the model of the environmental taxonomy where possible. This might help with global market acceptance and understanding. However, differences between them must be taken into account

| | Economic activities | Foundations | Quantitative vs Qualitative criteria |
|--|---|--|---|
| Environmental taxonomy  | Aim at: <ul style="list-style-type: none"> • Reducing negative environmental impacts. • or reversing these impacts through carbon capture or ecosystem restoration. | <ul style="list-style-type: none"> • Criteria developed on the basis of scientifically validated research results (natural science). | <ul style="list-style-type: none"> • Scientific research makes it possible to attach highly relevant quantitative criteria to economic activities. |
| Social taxonomy  | <ul style="list-style-type: none"> • Tend to have inherent social benefits (e.g creating jobs, or contributing to taxes). • Its role is to differentiate between the inherent and additional social benefits of economic activities (e.g if a pharmaceutical company improves the accessibility and affordability of certain drugs for certain people). | <ul style="list-style-type: none"> • Internationally agreed authoritative norms and principles. | <ul style="list-style-type: none"> • Social sustainability is at the moment often described in more qualitative terms. • Nevertheless, developments are occurring in the field of quantifiable social data (e.g. EU acquis in the social fields gives clear policy and legislative indicators that measure social impact). |

A₃ | Articulating and setting social objectives

Defining the objectives

The foundations of a social taxonomy are established international norms and principles



The Universal Declaration of Human Rights

The International Covenant on Economic, Social and Cultural Rights



The International Covenant on Civil and Political Rights



The ILO Declaration on Fundamental Principles and Rights at Work

The ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy



The European Convention on Human Rights



The European Social Charter

The Charter of Fundamental Rights of the European Union



The European pillar of social rights

The SDGs

The UNGPs

The UN Global Compact

The OECD guidelines for MNEs.



These documents explicitly cover and/or reference a set of fundamental freedoms and rights that countries have agreed to uphold and enforce to ensure that people and communities live dignified lives.

A₃ | Articulating and setting social objectives

Defining the objectives

The social taxonomy differentiate three type of stakeholders: workers, end-users and communities

- The most convincing way to articulate the objectives of a social taxonomy is setting out the type of stakeholders that different economic activities can affect. Stakeholders affected by business activities include:



An entity's own workforce
(including value-chain workers)



End-users or
consumers



Affected communities
(directly or through the
value chain)

- A future social taxonomy should be focused around these **three groups of stakeholders** to whose lives and livelihoods economic activities can make a positive contribution.
- With this stakeholder-centric approach in mind, the social topics covered by the referential norms and principles can be linked to **stakeholder groups**:

| Social topics in scope of social taxonomy | Stakeholder group |
|---|--------------------------------------|
| Labor rights and working conditions | Workers |
| Social protection and inclusion | Workers, communities and societies |
| Non-discrimination | Workers, communities and societies |
| The right to health care, housing, education (including professional training) and food | End-users, communities and societies |
| Assistance in the event of unemployment, self-employment, and old age | Workers |
| Consumer protection including data protection | End-users |
| Peaceful and inclusive societies | Communities and societies |
| Fighting corruption and tax evasion | Societies |



A₅ | List of abbreviations

| Abbreviations | Meaning |
|---------------|--|
| CRSD | Climate Resilience and Sustainable Development |
| DNSH | Do no Significant Harm |
| EFRAG | European Financial Reporting Advisory Group |
| ILO | International Labor Organization |
| MNE | Multinational Enterprises |
| OECD | Organization for Economic Co-operation and Development |
| OHS | Occupational Health and Safety |
| PSF | Platform on Sustainable Finance |
| SCG | Sustainability Corporate Governance |
| SDGs | Sustainable Development Goals |
| SFDR | Sustainable Finance Disclosure Regulation |
| TEG | Technical Expert Group |
| TR | Taxonomy Regulation |
| UNs | United Nations |
| UNGP | UN Guiding Principles |



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