



## **An EU Social Taxonomy: why do we need it and how to design it?**

### *Introduction*

Public spending and investment in the EU is likely to reach unprecedented levels in the coming years, amongst all due to the *Green Deal*, the *Just Transition Mechanism* as well as the *Next Generation EU* Covid recovery package. In addition, this spending will for the first time in history be covered with joint European debt, a third of which will be issued in the form of green bonds. This is positive news in terms of sustainability of that spending, given that the EU Green Bond Standard is consistent with its framework of sustainable investments, namely the EU Taxonomy which will go live in 2022.

Private spending on sustainable initiatives is also expected to increase substantially as a result of the [rising popularity of 'purpose investing'](#) in general. Accordingly, starting from the next year, any financial product labelled as 'green' or 'sustainable', sold or distributed in the EU, will need to comply with the Taxonomy.

### *The EU Environmental Taxonomy*

The [Taxonomy \(Regulation \(EU\) 2020/852\)](#) sets out a catalogue of economic activities that contribute to climate change mitigation or adaptation, as well as those which harm the environment in any case. The Taxonomy, however, has focused predominantly on climate and environmental aspects, while any social concerns, related to the quality of jobs, healthcare or access to basic infrastructure, remain largely unaddressed. Its Article 18 only includes some minimum safeguards requiring entities carrying out 'sustainable' economic activities to comply with the [OECD Guidelines for Multinational Enterprises](#) as well as the [UN Guiding Principles on Business and Human Rights](#), including the eight fundamental International Labour Organisation's conventions.

### *Rationale for a social taxonomy*

Meanwhile, social investment is growing rapidly, in such areas as healthcare or tackling unemployment, recently due to the COVID pandemic. Only in 2020, the [issuance of social bonds globally has increased eightfold](#) compared to 2019. The European Union alone raised \$47 bn in response to the coronavirus pandemic through several record breaking social bonds.

Unfortunately, apart from setting minimum standards to avoid causing social harm while saving the environment (e.g. preventing green infrastructure investments being accompanied by child or forced labour), the existing EU Taxonomy does not provide any guidance as to what 'social' investments actually entail. This would be the rationale for introducing a social taxonomy - to define social investment.

### *The objectives*

In order to ensure that funds are allocated only to projects and activities with truly positive social impact, the EU should introduce a Social Taxonomy setting out those initiatives which contribute to the wellbeing of European citizens, workers and communities. By providing guidance as to which activities are considered to have positive social impacts, a social taxonomy would prevent funds from being misspent. For example, creating high quality jobs (with living wages, skills development programmes and avoiding zero-hours contracts) available to local communities would be considered as having social benefits, while creating employment based on precarious forms or ignoring health & safety standards would not.

Social Taxonomy would also increase public support for such initiatives as the transition towards a net-zero economy by providing minimum social safeguards for all related investments. For example, Social Taxonomy would promote investment in instruments issued by corporates ensuring workers participation (e.g. in developing transition strategies or having workers' representatives on boards) over those which do not.

Finally, developing a social taxonomy would serve as a process of building a new public consensus around what a positive social impact means for all stakeholders. At the moment, certain investment products can be labelled 'sustainable' merely on the basis that they are based on indices not including companies supporting abortion or producing weapons.

### *The design*

In order to achieve the above objectives, Social Taxonomy should be introduced in a form of an EU regulation and composed of the following pillars:

- ❖ **A catalogue of economic activities, projects and initiatives which have positive social impacts** by enhancing the well-being of citizens, workers and communities. It could build upon existing classifications such as the [\*ICMA Social Bond Principles\*](#). This would serve to provide inspiration and information about what social investments could entail as well as verification to prevent funds from being misspent. Any financial product or

initiative labelled as 'social' would be required to comply with the catalogue, notwithstanding that other instruments, not explicitly 'social' instruments could have social co-benefits (*vide* the Green+ Gilt proposal).

- ❖ **Minimum social safeguards** for all financial products and investment, either private or public, to prevent funds from being channelled towards harmful initiatives or businesses, e.g. those violating health standards or labour rights. These could build upon existing principles, such as the UN Guiding Principles on Business and Human Rights or ILO conventions, and apply regardless of whether the 'social' label is used.
- ❖ **Minimum environmental safeguards**, linking back to the EU Environmental Taxonomy, to ensure that even most socially beneficial investments do not harm the environment or defeat the transition towards net-zero. E.g. that providing a local community with better access to clean water does not contribute to a loss of biodiversity around the area.

### *The scope*

The social taxonomy should apply to both private and public institutions. This would ensure that spending and public investment by the EU and national institutions, such as central and development banks, would adhere to the highest social standards, and be channelled towards initiatives with genuinely positive social results. Most of all, a social taxonomy should underpin investments from the Just Transition Fund, the Sustainable Europe Investment Plan as well as the Next Generation EU.

In addition, the social taxonomy should apply to financial instruments manufactured, sold or distributed in the EU, as well as overseas investment of EU entities.

### *Next steps*

As the first step towards developing an EU social taxonomy, an expert group should be established to consider its contents. The group should have balanced membership to represent interests of workers, local communities, consumers, youth, ethnic and other minorities, and other vulnerable groups. The group should work closely with the financial sector experts, including private institutions (e.g. investment funds, banks) as well as public bodies (development banks, public investment funds, the EU Social and Economic Committee).

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Further reading:

Schneeweiss A. (2020). *Human Rights Are Investors' Obligations* Antje Schneeweiß *A Proposal for a Social Taxonomy for Sustainable Investment*.  
Access:

<https://www.suedwind-institut.de/files/Suedwind/Publikationen/2020/2020-14%20Human%20Rights%20Are%20Investors%20Obligations.pdf>