DNSH- Do No Significant Harm

The European Union Taxonomy for Sustainable Activities, commonly referred to as the EU Taxonomy, is an attempt to equip financial markets with a classification system that fosters a shared understanding of sustainability. You can think of the Taxonomy as a dictionary defining which economic activities can be considered environmentally sustainable. The core question now facing companies, investors, and financial institutions is how to identify Taxonomy-aligned activities and revenue.

Why the requirement to avoid significant harm?

The six environmental objectives of the Taxonomy are (1) climate change mitigation, (2) climate change adaptation, (3) sustainable use and protection of water and marine resources, (4) transition to a circular economy, (5) pollution prevention and control, and (6) protection and restoration of biodiversity and ecosystems. Once a company has demonstrated that an eligible activity makes a substantial contribution to one of the Taxonomy's objectives, the activity is then subject to evaluation against the DNSH criteria. The DNSH criteria encompass the remaining five objectives to which the activity does not contribute. For example, if a company's activities substantially contribute to the climate change mitigation objective, it is subsequently required to consider the DNSH criteria for:

- climate change adaptation
- sustainable use and protection of water and marine resources
- transition to a circular economy
- pollution prevention and control
- protection and restoration of biodiversity and ecosystems

The primary objective of the DNSH criteria is to ensure that an activity, despite making a substantial contribution, does not have adverse effects on other environmental objectives in Europe. One example of this dynamic is found in a case where, "electricity generation using solar photovoltaic technology," which is a key technology for the EU's renewable energy transition. Solar photovoltaic (PV) technology intrinsically assists with climate change mitigation, and the criterion for substantial contribution is simply an activity that "generates electricity using solar PV technology," according to the Taxonomy **regulation**.

However, the large-scale deployment of solar PV technology carries the potential for negative impacts on other environmental objectives. First, the PV panels themselves contain chemicals and materials that currently lack sufficient end-of-life processes for recycling or disposal, which is relevant to the circular economy objective. Secondly, the land-use change associated with large-scale solar PV panel installations could impact areas with intact natural ecosystems such as woodlands, which is relevant to the objective of protecting biodiversity.

Therefore, the DNSH requirements for solar PV electricity generation link to these two other environmental objectives. Under the circular economy objective, the expectation is that the activity "assesses the availability of and, where feasible, uses equipment and components of high durability and recyclability and that are easy to dismantle and refurbish," according to the Taxonomy **regulation**. To meet the requirements under the objective for the protection and restoration of biodiversity and ecosystems, the activity must comply with a broader set of biodiversity thresholds outlined in the regulation's annex, which encompasses environmental impact assessments, mitigation and compensation measures, and the necessity to preserve biodiversity-sensitive areas.

This example shows how once a company has made a substantial contribution, it must then consider other environmental objectives. DNSH criteria do not necessarily encompass all five objectives; rather, they are

applied based on the specific circumstances of each activity. Some activities, such as battery manufacturing, may contribute to one objective but must consider the DNSH criteria of all five of the other objectives. On the other hand, some activities do not have any DNSH criteria they are required to meet. For example, creative, arts, or entertainment **activities** can substantially contribute to climate change adaptation and do not need to meet any of the remaining five DNSH criteria[1].

Taxonomy alignment is the positive assessment that an eligible activity meets the applicable Taxonomy requirements to substantially contribute to at least one of the Taxonomy's six objectives; while also doing no significant harm (DNSH) to any other objective; and meeting the minimum social safeguards (MSS). In 2022, the European Commission mandated that companies disclose their eligibility, and in 2023, companies were directed to disclose broader key performance indicators, including data on their alignment.

[1] https://www.spglobal.com/esg/insights/a-short-guide-to-the-eu-s-taxonomy-regulation#:~:text=The%20EU%20Taxonomy's%20definitions%20and,sustainable%20assets%20with%20more%20confidence.