

MVM Group EU Taxonomy Report 2021

The EU Taxonomy Regulation

By signing the Paris Agreement on climate change, the European Union (EU) has committed to the climate targets set and to more sustainable economic and social development.

Accordingly, as part of its action plan for financing sustainable growth, the European Commission decided to establish an EU classification framework for environmentally sustainable economic activities (hereinafter "EU Taxonomy"), thus Regulation (EU) 2020/852 (hereinafter "Taxonomy Regulation") entered into force on 12 July 2020.

The disclosure requirement under the Taxonomy Regulation aims to identify and classify green economic activities, primarily intended to support the financing of sustainable activities by providing the financial sector with information on the sustainability performance and commitment of companies, which lenders take into account in their decisions. In this way, companies, investors, and policy makers have a stake in channelling their investments to areas where they are most required for sustainable development and in realising their revenues through the most sustainable activities.

Environmental objectives defined by the Taxonomy Regulation and assessment of the contribution to them

The Taxonomy Regulation sets six environmental objectives. From an environmental point of view, an economic activity is considered sustainable if it contributes substantially to at least one of these objectives and does not cause significant harm to another environmental objective.

Environmental objectives defined by the Taxonomy Regulation:

1. climate change mitigation;
2. climate change adaptation;
3. the sustainable use and protection of water and marine resources;
4. the transition to a circular economy;
5. pollution prevention and control;
6. the protection and restoration of biodiversity and ecosystems.

The relevant EU Taxonomy activities and their associated criteria - technical screening criteria (TSC) for significant contribution, and other requirements for do no significant harm (DNSH) - have been defined in relation to the environmental objectives.

By the end of 2022, the essential contribution criteria for the first two objectives have been adopted and the other four objectives are being developed.

The assessment of the significant contribution to environmental objectives consists of the following parts:

1. Eligibility assessment
 - to determine whether each economic activity carried out by the undertaking and the related KPI elements can be aligned with one of the relevant activities of the EU Taxonomy.
2. Alignment assessment
 - to determine whether each of the undertaking's qualifying activities meets the Technical Screening Criteria (TSC) and Do No Significant Harm (DNSH) requirements of the relevant EU Taxonomy,
 - to demonstrate that the undertaking meets the minimum (social) safeguards (MS)¹.

The relevant activities and assessment criteria for the EU Taxonomy are defined in the Delegated Regulation (EU) 2021/2139, which will be amended from January 2023 by the Delegated Regulation (EU) 2022/1214, with several relevant activities for the MVM Group.

¹ „The minimum safeguards referred to in point (c) of Article 3 shall be procedures implemented by an undertaking that is carrying out an economic activity to ensure the alignment with the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights, including the principles and rights set out in the eight fundamental conventions identified in the Declaration of the International Labour Organisation on Fundamental Principles and Rights at Work and the International Bill of Human Rights.”

Accounting policies - Relevant disclosures

According to the Delegated Regulation (EU) 2021/2178 I. 1.2 of the Annex to the EU Taxonomy, companies are bound to present the following EU Taxonomy relevant financial indicators:

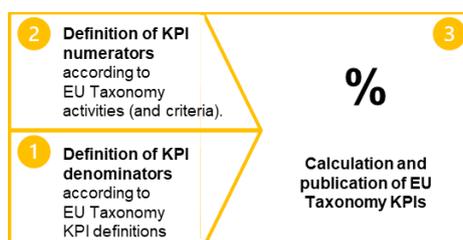
- Basis of the KPI related to turnover (Turnover KPI) according to the given international accounting standards:
 - IFRS 15 - Revenue from Contracts with Customers
 - IFRS 16 - Leases
 - Other revenue
- Basis of CAPEX KPI according to the international accounting standards provided:
 - IAS 16 - Property, Plant and Equipment
 - IAS 38 - Intangible Assets
 - IFRS 16 - Leases
 - IAS 40 - Investment Property
 - IAS 41 - Agriculture
- Basis of the KPI related to operating expenses (OPEX KPI):
 - R&D expenditure
 - Building renovation measures
 - Direct non-capitalised costs related to maintenance and repair
 - Any other direct expenditure related to the day-to-day maintenance of assets, including property, plant and equipment, by the undertaking or, in the case of outsourcing, by a third party, which is necessary to ensure the continuous and effective operation of such assets
 - Short-term leasing

Undertakings will present the percentage of their relevant financial indicators that are derived from activities contributing to sustainability under the EU Taxonomy.

General methodological approach of the MVM Group

Since the MVM Group is obliged to comply with the provisions of Act C of 2000 on Accounting (hereinafter: Accounting Act) 95/C.§, the Group is subject to the disclosure obligation in accordance with the EU Taxonomy. The corresponding EU Taxonomy KPIs have been derived from the consolidated financial indicators and therefore only include data from fully consolidated subsidiaries. Considering the Group's activities inside and outside the EU, the eligibility KPIs for the financial year 2021 have been assessed along 3 main KPIs: Turnover, CAPEX, OPEX. The fiscal year 2021 has been analysed in the light of the substantial contribution to the environmental objective of climate change mitigation. Potential duplications between KPIs and member companies have been eliminated. Items related to supporting activities have been allocated to the EU Taxonomy activity supported.

KPIs are defined as follows:



The denominator is determined on the basis of data from the consolidation system and from the subsidiaries' „separation of activities” reports and controlling statements. In all cases, the first step in defining the numerator is the identification of eligible activities in accordance with the Taxonomy Regulation, followed by the assignment of financial data corresponding to the three KPI indicators to the activities concerned.

Implementation of the MVM Group

Turnover KPI:

The consolidated figure in the denominator of the Sales KPI is the same as the Sales revenue line item in the Consolidated statement of comprehensive income. The MVM Group would lose a significant part of its turnover if intercompany sales were completely excluded, as most of the energy produced within the vertically integrated group is sold through its own trading companies. Therefore, the following specific approach has been adopted:

- In the case of energy producing companies, intercompany sales are recognised by allocating back the turnover of the trading companies on volume basis.
- For subsidiaries engaged in electricity transmission and distribution activities, system charges invoiced to the group have also been recognised through the trading companies' turnover, net of system charges for electricity consumption within the group.

CAPEX KPI:

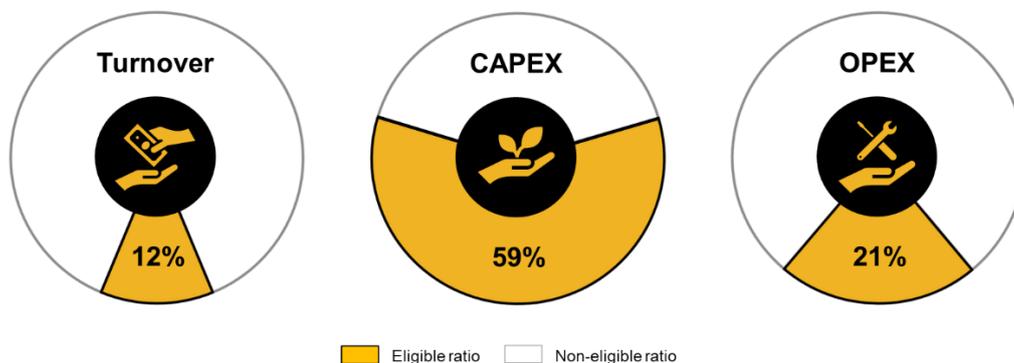
The consolidated figure in the denominator of the CAPEX KPI is equal to the sum of the "Purchase", "Additions" and "Assets acquired in business combination / assets acquired in transactions with the parent company" line items in the "Property, plant and equipment", "Investment property" and "Goodwill and other intangible assets" movement tables in the consolidated financial statement. The increase in goodwill is not included in the denominator and numerator of the CAPEX KPI under the regulation. The CO₂ allowance and acquisitions are part of the Taxonomy study under the regulations. The entire investment portfolio of the MVM Group was analysed and classified during the assessment. For gas distribution activities, the following approach has been applied:

- A significant part of the network investments to make the network suitable for hydrogen conversion and to reduce methane leakage have been identified as eligible activities.

OPEX KPI:

In several cases, the subsidiary reports provided main inputs for the assessment, as the data cannot be acquired from the consolidation system as required for the taxonomy definition. The data provided by subsidiaries are in line with the data required and reported to the Hungarian Energy and Public Utility Regulatory Authority (HEPURA). For the OPEX KPI, the denominator was built up from expenditures defined above of subsidiaries that carry out sustainable activities or hold significant assets, with the addition that costs related to service interruption recovery and network diagnostics are also considered OPEX.

MVM Group EU Taxonomy KPIs for the fiscal year 2021



Evaluation of defined KPIs

Turnover

The MVM Group's EU Taxonomy Turnover KPI for 2021 is 12.48%. In 2021, the Group realised HUF 2,851 billion EU Taxonomy assessable revenue in 2021, which equals to the given year's consolidated statement of comprehensive income Sales revenue line item. Nearly HUF 356 billion is related to climate change mitigation activities, which meet the environmental objective, considered as eligible turnover.

Turnover	HUF million
Total	2,850,817
Eligible	355,743
Non-eligible	2,495,074

The majority of the MVM Group's eligible turnover (HUF 340,112 million) was generated by transmission and distribution of electricity activities. In addition, electricity generation using solar photovoltaic technology (HUF 8,118 million) and electricity generation from hydropower (HUF 3,612 million) activities generated significant turnover.

Turnover - EU Taxonomy eligible activities		Eligible Turnover ratio
4.9.	Transmission and distribution of electricity	95.6%
4.1.	Electricity generation using solar photovoltaic technology	2.3%
4.5.	Electricity generation from hydropower	1.0%
n.a.	Other activities	1.1%

CAPEX

The MVM Group's 2021 EU Taxonomy CAPEX KPI is 59.12%. In FY2021, the Group has made an investment of nearly HUF 391 billion of EU Taxonomy assessable investment, which corresponds to the regulatory value of total group consolidated CAPEX less goodwill. Nearly HUF 232 billion was for activities meeting the environmental objective of mitigation, considered as eligible investment.

EU Taxonomy CAPEX	HUF million
Total	391,665
Eligible	231,570
Non-eligible	160,095

More than four fifths of the MVM Group's eligible investments (HUF 190,034 million) were related to the development and refurbishment of its transmission and distribution of electricity activities. In addition, investments in transmission and distribution networks for renewable and low-carbon gases (HUF 19,855 million) and electricity generation using solar photovoltaic technology (HUF 14,154 million) were significant.

CAPEX - EU Taxonomy eligible activities		Eligible CAPEX ratio
4.9.	Transmission and distribution of electricity	82.1%
4.14.	Renewable and low carbon gas transmission and distribution networks	8.6%
4.1.	Electricity generation using solar photovoltaic technology	6.1%
4.5.	Electricity generation from hydropower	2.1%
n.a.	Other activities	1.1%

OPEX

The MVM Group's EU Taxonomy 2021 eligible OPEX KPI is 21.19%. The Group had over HUF 63 billion of operating costs to be considered for EU Taxonomy in 2021. More than HUF 13 billion was spent on activities in line with the environmental objective of mitigation, considered as eligible operating costs.

EU Taxonomy OPEX	HUF million
Total	63,374
Eligible	13,426
Non-eligible	49,948

More than 90% of the MVM Group's eligible operating costs (HUF 12,296 million) were incurred in its transmission and distribution of electricity activities. In addition, the operating costs of the electricity generation using solar photovoltaic technology (HUF 634 million) and electricity generation from wind power (HUF 226 million) activities are also mentionable.

OPEX - EU Taxonomy Eligible activities		Eligible OPEX ratio
4.9.	Transmission and distribution of electricity	91.6%
4.1.	Electricity generation using solar photovoltaic technology	4.7%
4.3.	Electricity generation from wind power	1.7%
4.5.	Electricity generation from hydropower	1.1%
n.a.	Other activities	0.9%

When compiling the 2021 eligibility report, the MVM Group conducted a preliminary analysis for nuclear and natural gas-based activities and a pilot alignment assessment for electricity generation from renewable energy sources (photovoltaic and hydro) through a subsidiary.

Proposal for EU Taxonomy

During the interpretation, processing and reporting of the EU Taxonomy, several points were identified where the current regulatory environment does not clarify the exact framework. In general, the methodological processing of turnover and OPEX KPIs might not be straightforward enough, leaving room for different approaches, thus making the indicators non-comparable and difficult to evaluate.

In the case of the OPEX KPI, it is not possible to clearly separate operating and maintenance costs for many activities, neither from an accounting-controlling nor from a technical point of view. In addition, there is no clear formulation of the contribution to sustainability for several manufacturing companies engaged in support activities. A proper and precise definition of these activities (direct and indirect contribution to sustainability) would greatly contribute to a more coherent assessment.