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THE EUROPEAN BANKING FEDERATION ON THE LATEST DEVELOPMENTS CONCERNING THE COMMISSION PROPOSAL FOR A EUROPEAN GREEN BOND STANDARD

The European Banking Federation (EBF) welcomes the proposal for a voluntary EU Green Bond Standard (EU GBS). The development of a coherent and uniform framework for European green bonds will facilitate investors' ability to identify green bonds aligned with the EU Taxonomy while allowing best-in-class issuers to provide evidence of the green nature of their bonds.

While we support the common efforts to define a clear and reliable framework, we would like to address the following:

1. On the nature of the standard

The EBF strongly supports the voluntary nature of the standard as it will ensure that stakeholders are provided the opportunity to choose between existing standards available in the market and that the European market continues leading in terms of volume of green bond issuance.

A voluntary standard, as initially proposed by the European Commission, will better serve the growth of the green bond market and the EU GBS will likely find wide acceptance without being established as a mandatory standard. Current trends already show that the market and issuers are increasingly focusing on renewing their green bond frameworks in order to align their projects and processes with the EU Taxonomy. This also reflects the gradual increase in the proportion of Taxonomy-aligned economic activities, which currently represents a small proportion of the economy and is only expected to increase over the next years. Indeed, estimates put the volume of finance that would currently meet Taxonomy-alignment green criteria at merely 1– 5% of all financial assets[1].

We strongly believe that the standard will be widely accepted in the long run, despite its strict conditions, and that investors will appreciate the certainty provided by the EU GBS designation. A voluntary standard would, moreover, naturally attract the attention of ambitious issuers that wish to provide evidence of the green nature of their bonds to investors.

On the other hand, a mandatory standard risks limiting market developments and creating an unlevelled playing field, leaving European issuers constrained in a format which will only evolve at the pace the Technical Screening Criteria (TSC) develop, unlike extra-EU issuers that would have the possibility to choose amongst other existing standards.

[1] Platform on Sustainable Finance, "The Extended Environmental Taxonomy", p. 17, March 2022. https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/220329-sustainable-finance-platform-finance-report-environmental-transition-taxonomy_en.pdf

European Banking Federation aisbl

Brussels / Avenue des Arts 56, 1000 Brussels, Belgium / +32 2 508 3711 / info@ebf.eu
Frankfurt / Weißfrauenstraße 12-16, 60311 Frankfurt, Germany
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Furthermore, envisioning the shift to mandatory standard would limit the issuance of future green bonds only to those financing Taxonomy-aligned activities or activities which could fully align with the Taxonomy within a pre-determined timeframe. Considering the current difficulties being encountered with regards to the application of the taxonomy, a consequence could be the shrinking of the green bond market, and direct green bond funding into different currencies and markets without any foreseeable benefits for the uptake of the EU GBS.

In response to a European mandatory standard, another unintended consequence could be that other jurisdictions may also, in turn, develop mandatory standards potentially catalysing markets outside the EU. As a result, such development risks weakening the European economy in its ability to finance the green transition.

Finally, although a voluntary standard would be the preferred option, the shift to a mandatory EU GBS should only follow an in-depth assessment of the future Regulation's impact on the market and the state of development of the EU green bonds market. Such an assessment should not occur earlier than five years after the Regulation's entry into force. Any prior assessment would be premature. In the event of the shift to a mandatory standard and in order to address the significant difficulties related to demonstrating Taxonomy-alignment, there would be benefit in allowing additional flexibility concerning the requirement that proceeds be fully aligned with the Taxonomy, with this flexibility applying to both corporate and sovereign issuers equally.

2. On the extension of disclosure requirements to bonds marketed as environmentally sustainable and sustainability-linked bonds

While we strongly believe there is merit in envisioning a green bond standard which is linked to the science-based Taxonomy, we also see value in allowing European issuance under standards other than the EU GB, which rely on different disclosure requirements. Financial and non-financial companies are gradually adjusting to the operational requirements for full Taxonomy-alignment and are facing significant challenges with regards to meeting the TSC and 'do no significant harm' (DNSH) criteria. While extending the obligation to disclose Taxonomy-alignment would increase transparency and comparability across standards, it could potentially decrease the attractiveness of issuances under alternative standards (other than the EU GBS) due to the aforementioned challenges related to demonstrating Taxonomy-alignment, hence damaging market growth. It would consequently, moreover, result in an unlevelled playing field with respect to non-EU issuers, which would not be subject to Taxonomy-alignment disclosure requirements when issuing under alternative standards. We do not believe it is the intention to cause a competitive disadvantage for the EU, which is currently leading globally in terms of green bond issuance[2]. In this respect, if the obligation were to be extended to all bonds marketed as environmentally sustainable, to ensure a level playing field, the obligation should apply to all issuers (extra-EU included) offering their financial products in the EU.

[2] The EU is a global leader in green bonds, with 48 % of global issuances in 2020 being denominated in euros (source: Climate Bonds Initiative)

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The extension of disclosure requirements would mean that issuers of all green and sustainability-linked bonds would then have to provide website, pre-contractual, and periodic disclosures on the investments' principal adverse impact as already envisaged by the Sustainable Finance Disclosures Regulation (SFDR). Apart from creating unnecessary duplication of disclosure requirements, this provision could become particularly burdensome for those issuers of green bonds who are not financial market participants (i.e., corporates), and thus not in scope of the SFDR.

Therefore, this would be a great disincentive for corporates that wish to issue on the European green bond market, and thus contrary to the spirit of the Commission's proposal.

With reference to sustainability-linked bonds, imposing disclosure obligations via the EU GB framework would not be feasible as green bonds differ substantially from sustainability-linked bonds both in terms of structure and characteristics. The current framework was envisioned specifically for EU green bonds (i.e., use-of-proceeds bonds) and widening the scope to sustainability-linked bonds (for which proceeds are used for general purposes) without appropriately re-assessing the structure of the framework could result in significant risks. As we recognise that the process for finalising a framework for the EU GBS is needed and should be timely, we suggest to initially propose a framework solely intended for the EU GBS and separately develop an adequate framework tailored to the specificities of SLBs or alternatively contemplate the extension of the EU GBS framework following an attentive assessment and once transition plans have been defined at EU level.

3. <u>On full grandfathering in the event of evolving TSC</u>

The EU GB Regulation should provide legal certainty that issued EUGBs will not lose their status at any point until maturity, including when proceeds are allocated to financial assets following a portfolio approach.

Full grandfathering for both allocated and non-allocated bond proceeds is crucial in encouraging long-term investments by providing certainty to both issuers and investors. Without full-grandfathering, issuers may be forced to revoke their bond from the market, while investors may be forced to exit the investment when it ceases to be classified as green due to revision of the Taxonomy criteria.

Furthermore, as highlighted by the ECB in its Opinion[3], the investors may be incentivized to sell green bonds in anticipation of a potential loss of the EU GBS designation, which in turn could lead to a disruption of the prices of the affected bonds. The provision might also have unintended consequences on the duration of EU GBs, by potentially creating a preference for EU GBs with shorter maturities in order to avoid the negative consequences of an expected change of the Technical Screening Criteria.

In addition, full grandfathering applied to the allocation of proceeds following the "portfolio approach" is particularly relevant for the banking sector as a great number of financial institutions issue green bonds to refinance portfolios of loans (in particular related to long-term projects such as real estate loans). Regularly reassessing the individual loans

[3] European Central Bank, Opinion on a proposal for a regulation on European green bonds, 5 November 2021.
https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv%3AOJ.C_.2022.027.01.0004.01.ENG&toc=OJ%3AC%3A2022%3A027%3ATOC

included in the portfolio would become operationally over-complex and would risk rendering the EU GBS a less attractive alternative[4].

Full grandfathering would allow for such type of investments to remain relevant under the existing green bond framework and encourage the development of projects aligned with the taxonomy.

4. On the mandatory disclosure of transition plans

EBF Members strongly support the concept of transition plans and deem crucial that they be clearly defined at EU level. Clarity is needed on how such plans should be defined in a way that provides proof of consistency with EU climate law 2030/2050 objectives and that avoids any potential greenwashing.

While we support the requirement to disclose transition plans, the criteria according to which such plans should be developed is still to be determined. The development and definition of the criteria specifying minimum requirements for transition plans will depend on the developments of the Corporate Sustainability Reporting Directive (CSRD) proposal and the work of EFRAG on entity-level disclosures. To avoid a sequencing issue, as the EU GB framework will likely enter into force prior to the CSRD, it is important to clarify within the EU GB Regulation, that the mandatory disclosure of transition plans for issuers of EU GBs will only apply after transition plans have been clearly defined at EU level under the CSRD.

5. On the inclusion of the EU GB factsheet in the prospectus

While the information included in a Green Bond Factsheet should be deemed relevant for issuers, the full integration of such information in the prospectus would unduly increase the length and complexity of the latter. Incorporation of the factsheet by reference would provide sufficient transparency for investors without unduly lengthening the document.

6. On civil liability

We agree that ensuring that adequate measures be in place to certify the accuracy and accountability of the information disclosed in relation to bonds issued under the EU GBS designation is important. We believe that in this respect, the prospectus liability regime provides sufficient safeguards for investors.

[4] Some instances where long-term projects could encounter relevant issues in the instance of the 5-year grandfathering clause:

- An issuer may fund electricity generation using solar photovoltaic technology (page. 91 of the TSC here), but the project upon completion may no longer meet the future Biodiversity criteria. The solar PVs could in a few years be deemed "near" a biodiversity-sensitive area if a newly added site on the UNESCO World Heritage list is near the project (34 sites were added to the list since 2020). To meet the investor's time horizon and due to potential costs, the issuer may abandon alignment with the EUGBS but can still retain alignment with GBP (which investors are more familiar with), thereby limiting EUGB uptake.
- It is common in green covered bonds that the pool of assets varies after the release of the covered bond. The average length of a covered bond (which are mostly backed by mortgages) is 10 years. With the risk that the green bond could lose its label before then, the EU GBS would not be an attractive tool to raise capital, and regular bonds would for instance be preferred. This would reduce the incentive to promote green mortgages.

About EBF

The European Banking Federation is the voice of the European banking sector, bringing together national banking associations from across Europe. The federation is committed to a thriving European economy that is underpinned by a stable, secure, and inclusive financial ecosystem, and to a flourishing society where financing is available to fund the dreams of citizens, businesses and innovators everywhere.

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For more information contact:

Alexia Femia
Sustainable Finance Policy Adviser

a.femia@ebf.eu

+32 473 13 1569