Energy Performance of Buildings Directive

April 2023

Background

- We recognise the emphasis placed in the Directive on finance to stimulate the Renovation Wave. Indeed, we have long recognised the transformative role of the banking industry in financing the improvement of the EU's building stock as evidenced by industry efforts through the Energy Efficient Mortgages Initiative (EEMI), EEM Label, as well as individual bank efforts. We also recognise the strategic importance of the Energy Performance of Buildings Directive (EPBD) and support the overall ambition of reducing energy poverty, decreasing the EU's dependence on fossil fuels, and helping meet the EU's climate targets and zero-emission building stock by 2050.

- The EU's banking industry is fully committed to channeling private finance to support the Renovation Wave, NextGenerationEU and RePowerEU and will continue to play an instrumental role in helping the EU meet its ambitious renovation targets. Due to their proximity to customers, banks are part of the solution to tailor new financing products to the specific needs of their borrowers, in line with the EU objectives, subject to these households having the ability to repay a loan.

- Ahead of the forthcoming trilogue negotiations between Member States and the European Parliament, we would like to highlight the following points which we believe are critical in securing the capacity of the banking industry in supporting the financing of the improvement of the EU's building stock in support of the climate transition.

Key Points

Article 2 (36) - Mortgage Portfolio Standards – requirement for mortgage providers

- While we recognise the intention behind the introduction of Mortgage Portfolio Standards (MPSs), we believe that the emphasis should be placed on 'incentivising' rather than requiring portfolio targets which mortgage lenders cannot achieve alone. The decision to improve the energy efficiency of properties is the choice and responsibility of borrowers, as owners. Such renovations can be supported by financing from the banking industry, which the industry is more than ready to provide, but cannot be forced. It is also important to bear in mind that banks' readiness to provide the necessary finance is subject to specific prudential requirements and the EBA Guidelines on Loan Origination and Monitoring. Any loan advanced by a bank is made pursuant to a creditworthiness assessment, based on the borrower's ability to repay.

- The European Parliament recognised the potential for mandatory MPSs to also have the unintended consequence of pushing banks towards the financing of the best-performing buildings in order to meet the requirements. However, we regret that the European Parliament did not revert to a voluntary approach to the

Standards addressing this concern at source but rather proposes the introduction of a Delegated Act requiring the European Commission to *"prescribe (…) necessary safeguards against potential counterproductive lending* *behaviours”.* It is not clear what form these safeguards would take.

- Concerning the proposal of the Parliament in Article 2(36), it is also not clear what is meant by *“reliable, evidence-based and affordable solutions”* for the clients and how banks are supposed to ensure this.

- **In a context where there is alignment of the co-legislators on the introduction of MPSs, we believe that the more appropriate and proportionate approach to the issue is the initial proposal by the European Commission also supported by the Council, namely the introduction of MPSs as mechanisms incentivising portfolio targets.**

Art 9 - Minimum Energy Performance Standards – requirements for Member States

- We recognise the need to put in place ambitious measures to achieve climate neutrality in buildings and support an approach with an initial focus on the worst performing buildings. However, we have long been concerned about the potential immediate impact of such standards on collateral values and the risk of devaluations in the event that a building does not fulfil the defined standards, most likely impacting Europe’s most vulnerable households, with related social and financial stability implications. Indeed, not all homeowners are in a financial position to take on or be granted (more) debt to finance energy renovation, in a context where the decision to grant a mortgage or a consumer credit is based on a robust creditworthiness assessment. Reductions in the values of collateral would not only impact homeowners, but potentially also financial institutions through higher capital requirements (unless new collateral is deployed by the client), potentially limiting the availability of credit. This aspect is of particular relevance taking into account the current context of rising interest rates and the very limited timeframe prescribed in the Directive to finance the renovation of a huge stock of RE properties at EU level.

- We understand public grants and subsidies to support the most vulnerable may be put in place and, in this regard, welcome the wording of Recital 46 as proposed by the European Parliament to support the most “vulnerable households, as well as owners in worst performing multi-dwelling buildings and buildings in rural areas, and other groups having difficulty to access finances or get traditional mortgages”, as well as to provide “guarantees to financial institutions in order to promote targeted financial products. However, these mechanisms are currently not readily available and will have to be put in place first. National authorities will also be required to renovate their own building stocks to cope with the provisions of the Directive. Therefore, public finance issues must be addressed with urgency, also foreseeing the use of EU Funds, in order to mitigate further fragmentation among EU regions.

- A further consideration relates to the importance of renovations only being conducted where they are technically and functionally feasible and economically viable for the building owner and society and where they lead to an actual decrease in the overall emission of GHG from a lifecycle perspective, also considering the exposure of the buildings to physical risks. We also have concerns about how achievable the targets are within the very short proposed timeframes against a current background of rising construction material prices and a shortage of materials and labour.

- With these considerations in mind, we have long advocated for a careful balance between measures needed to achieve the climate goals (climate mitigation), physical risks (climate adaptation) and measures that are technically practicable and socially and economically viable. Whilst the concerns highlighted above remain valid to a large extent, for existing residential buildings we see merits in the Council proposal to set minimum energy performance standards based on a national trajectory corresponding to the decrease of the average primary energy use in the whole residential building stock over the period from 2025 to 2050 with two control points, starting with EPC D by 2033**.**

- **Despite ongoing concerns about the feasibility of achieving this target particularly by the proposed deadline, we believe that, of the proposals under scrutiny, the Council proposal offers more appropriate and necessary flexibility in the management of building portfolios and would urge that this proposal be retained in the final agreement. It is of utmost importance that policy makers avoid defining hard EPC thresholds that may lead to unintended social consequences by excluding certain homeowners from the mortgage market. The Council proposal should also be complemented by concrete proposal for Union grants and subsidies to vulnerable**

households, guarantees to financial institutions and a framework to ensure a sufficient and qualified workforce, to avoid fragmentation amongst Member States.

Article 15 (4) (7) and article 2 (36a) – Pay as you save scheme- requirements for lenders

- We are concerned about the potential introduction of this specific loan intended exclusively to finance the improvement of the energy performance of housing and based on annualised repayments not exceeding the monetary equivalent of the yearly saving. The amount of financial savings depends on the price of energy throughout the term of the loan so it is difficult to estimate this amount and to calibrate the monthly repayment on it. Mandatory variable payments based on the variable amount of financial savings seem not as appropriate as fixed installment based on the borrower's ability of repayment. Moreover, according to CCD and MCD, the consumer credit or mortgage lender must assess the borrower's ability to repay the loan on his/her income. So, from our point of view, the monthly repayment of loans to individuals should be based first and foremost on the ability to repay.

- **With these considerations in mind and if the proposal is retained in the final agreement, we would recommend at the very least that the introduction of such schemes be left to the discretion of Member States, which in such case may make public funding available.**

Article 19 – Databases for Energy Performance of Buildings – requirements for Member States

- We welcome the alignment between the co-legislators on the requirement for Member States to establish databases for building energy performance and strongly support the proposal of the European Parliament to ensure easy and free-of-charge access to the full energy performance certificate for, among others, financial institutions.

- Indeed, in order for banks to support the financing of the climate transition, it is imperative that they are granted access to the energy performance data of buildings. **We would therefore urge that the European Parliament's proposed amendments to Article 19, which will be absolutely critical in enabling banks to meet all other requirements in this and other pieces of legislation focused on meeting the EU's climate objectives, be retained in the final agreement.** We would however like to take this opportunity to note that, while we welcome the prospect of access to the full EPC, the EPC is not actually sufficient to determine and evidence compliance with the building related elements of EU Taxonomy alignment.

Article 16(3) Annex V – Template for Energy Performance Certificates

- We welcome the co-legislators' proposals in Article 16(3) that Member States shall ensure the quality, reliability and affordability of energy performance certificates and their gradual harmonisation across EU countries, taking into account, however, the differences in primary energy demand in different European regions.

- We welcome the efforts of the European Parliament in Annex V point 2a to secure the inclusion in the EPC of relevant indicators for institutions providing finance. **This is another strong signal that the European Parliament acknowledges the importance of building energy performance data for banks in supporting the climate transition and we believe there is value in integrating this proposal into the final agreement.**

- However, we are concerned about the additional requirement in Annex V point 2a that the EPC should include a dedicated section on financing, listing financing options. **We do not believe that the EPC is the appropriate vessel for such information and question who would deliver and be responsible for this information. In addition, it may give rise to conflict-of-interest issues. We do not believe this is a responsibility that building experts would or should assume and consider that there are other mechanisms which can be put at households' disposal to deliver this type of information, for example the industry-led Energy Efficient Mortgage Label mentioned above. For these reasons, we firmly believe that such information should not be included in Annex V**. Instead, disclosing the economic cost of the recommended improvement of the energy performance and the energy performance class that would be achieved with such improvement could both help in assessing the viability of the renovation and also help banks in assessing the transition risk of the property

(ECB Expectations #8.3: "Institutions are expected to consider climate-related and environmental risks in their collateral valuations").

Wim Mijs

Chief Executive
EBF

Luca Bertalot

Secretary General
EMF-ECBC
EEMI Coordinator

Adam Farkas

Chief Executive Officer
AFME

About us

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.

Established in 1967, the European Mortgage Federation (EMF) is the voice of the European mortgage industry, representing the interests of mortgage lenders and covered bond issuers at European level. The EMF provides data and information on European mortgage markets, which were worth around 8.3 trillion EUR at the end of 2021 (EU27 + UK). As of March 2023, the EMF has 14 Full Members across 12 EU Member States and 13 Observer Members from 9 countries around the world.

In 2004 the EMF founded the European Covered Bond Council (ECBC), a platform bringing together covered bond issuers, analysts, investment bankers, rating agencies and a wide range of interested stakeholders. As of March 2023, the ECBC has 119 members across more than 30 active covered bond jurisdictions and many different market segments. ECBC members represent over 95% of covered bonds outstanding, which were worth over EUR 2.9 trillion at the end of 2021.

The Covered Bond Label Foundation (CBLF) was established in 2012 by the European Mortgage Federation - European Covered Bond Council (EMF-ECBC). The Covered Bond Label website became fully operational on the 1st of January 2013, with the first Labels being effective since then. The website features the Harmonised Transparency Template (HTT), published by 126 issuers disclosing information on 166 labelled cover pools across 24 jurisdictions. The Covered Bond Label website currently provides issuance data on over 5,300 covered bonds, amounting to a total face value of around 2.1 trillion EUR.

The Energy Efficient Mortgage (EEM) Label was established in 2020 by the European Mortgage Federation – European Covered Bond Council (EMF-ECBC) as a clear and transparent quality label for consumers, lenders and investors, aimed at identifying energy efficient mortgages (EEM) in lending institutions' portfolios, which are intended to finance the purchase/construction and/or renovation of both residential (single family & multi-family) and commercial buildings, with a focus on building energy performance. The first labels were issued in 2021 and as of March 2023, 34 lending institutions from 12 countries hold the Label covering 36 financial products. The development of the EEM Label was triggered by the EMF-ECBC's work, in its role as Coordinator, on the Energy Efficient Mortgages Initiative (EEMI).

The Association for Financial Markets in Europe (AFME) represents a broad array of European and global participants in the wholesale financial markets. Its members comprise pan EU and global banks as well as key regional banks, brokers, law firms, investors and other financial market participants. We advocate stable, competitive, sustainable European financial markets that support economic growth and benefit society.