Ref: Targeted consultation on the establishment of an EU Green Bond Standard

Link to consultation: https://ec.europa.eu/info/consultations/finance-2020-eu-green-bond-standard_en

BETTER FINANCE Response to the consultation on EU Green Bond Standards

Executive Summary

What are Green bonds?	Green bonds are fixed-income debt securities that are issued to finance environmental and climate projects.
What are EU Green Bond Standards?	The Technical Expert Group on Sustainable Finance (TEG) proposed EU green bond standards (EU GBS) that are voluntary guidelines for issuers to align market practices on the issuance and verification of green bonds in the EU. These standards are developed around the already existing practices such as Green Bonds Principles (GBP), developed by the International Capital Market Association (ICMA). EU GBS are defined on the following key elements[1]: (i) The use-of-proceeds alignment with the EU Taxonomy.[2] (ii) The content of a Green Bond Framework to be produced by the issuer.[3] (iii) The required Allocation and Impact Reporting.[4] (iv) The requirements for external verification by an approved verifier.[5]
Why do we need green bond standards?	The green bond market has been growing rapidly in the recent years. But several issues are affecting this market and eroding investor confidence in this financial instrument. Ensuring transparency on the underlying assets is fundamental for this market to reach scale and its objectives. Specific and credible guidelines on how to identify and classify green projects based on evidence is essential to prevent *greenwashing* and ensure *green bonds* are trustworthy.. [6] One of the main issues linked to green bonds is the difficulty to assess if funding is channelled to actually "green" or new environmental projects. In order to ensure money is channelled into impactful green projects, the

[1] https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/200309-sustainable-finance-teg-green-bond-standard-usability-guide_en.pdf.

[2] Ibid.

[3] Ibid.

[4] Ibid.

[5] Ibid.

[6] https://ec.europa.eu/environment/enveco/pdf/potential-green-bond.pdf.

	EU green bond standards should impede practices such as repackaging[7], loans that banks already have in their portfolio into green/social bonds.
Verification and impact reporting	The verification and the assessment of the impact of green bonds is pivotal to ensure that only projects with a significant impact on the real economy are funded by green bonds. Additional requirements regarding impact reporting should be provided.
Social Bonds	Europe held a leading position in the issuance of social bonds, with 67% of the global issuance in 2019. The main issue for institutional investors to take up more social bonds is the reduced liquidity, which makes them riskier. However, social bonds often provide better yields than traditional sovereign or corporate bonds: for instance, almost all social bonds listed on the Luxembourg Stock Exchange have positive (and quite high) yields compared to the already-usual negative rates practiced with traditional sovereign bonds.[8] Therefore, this specialised part of sustainable debt finance could be a significant factor in speeding up economic recovery and to improving the returns on bond exposures of pension products. In addition, we believe that EU Commission should not only focus on environmental standards but should develop an official **Sustainability Bond Standard** that would include environmental social **and governance** objectives.

About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the public interest non-governmental organisation advocating and defending the interests of European citizens as financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances. It is the one and only European-level organisation solely dedicated to the representation of individual investors, savers and other financial services users.

BETTER FINANCE acts as an independent financial expertise and advocacy centre to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

CONSULTATION QUESTIONS

What type of organisation are you, in relation to the green bond market?

a. Issuer

b. Investor

[7] https://www.ft.com/content/16bd9a48-0f76-11e5-b968-00144feabdc0

[8] See here the list of the 46 social bonds traded on the LSE: https://www.bourse.lu/lgx-displayed-international-bonds?bonds=social.

c. Verifier / external reviewer / 3rd party opinion provider

d. Intermediary

e. Market-infrastructure

f. NGO

g. Public Authority

h. Trade or Industry Association

i. Other (if so, please specify) [BOX]

Federation of individual, non-professional ("retail") investors and financial services users

I. QUESTIONS ON THE EU GREEN BOND STANDARD

About the TEG proposed EU GBS

The EU GBS aims to address several barriers identified in the current market. Firstly, by reducing uncertainty about what constitutes green investment by linking it to the EU taxonomy. Secondly, by standardising costly and complex verification and reporting processes, and thirdly, by establishing an official standard to which potential incentives could be linked.

The EU GBS as proposed by the TEG is intended to finance both physical and financial assets and includes the use of the latter as security (i.e. as a covered bond or asset backed securities).

The key components of such a standard – as recommended by the TEG and building on best market practices such as the Green Bond Principles and the Climate Bonds Initiative labelling scheme – should be:

(1) alignment of the use of the proceeds from the bond with the EU Taxonomy;

(2) the publication of a Green Bond Framework;

(3) mandatory reporting on the use of proceeds (allocation reports) and on environmental impact (impact report); and

(4) verification of compliance with the Green Bond Framework and the final allocation report by an external registered/authorised verifier.

Questions on the potential need for an official / formalised EU GBS

1) In your view, which of the problems mentioned below is negatively affecting the EU green bond market today? How important are they? Please select and rate the extent of the impact on a scale of 1 to 5 (1 no impact, 5 very strong impact). Multiple answers are possible.

a. Absence of economic benefits associated with the issuance of green bonds

~~[1]~~ [2] [3] [4] [5]

b. Lack of available green projects and assets

[1] [2] ~~[3]~~ [4] [5]

c. Uncertainty regarding green definitions

[1] [2] [3] [4] ~~[5]~~

d. Complexity of the external review procedure(s)

[1] [2] [3] ~~[4~~] [5]

e. Cost of the external review procedure(s)

[1] [2] ~~[3]~~ [4] [5]

f. Costly and burdensome reporting processes

[1] ~~[2]~~ [3] [4] [5]

g. Uncertainty with regards to the eligibility of certain types of assets (physical and financial) and expenditure (capital and operating expenditure)

[1] [2] [3] ~~[4]~~ [5]

h. Lack of clarity concerning the practice for the tracking of proceeds

[1] [2] [3] ~~[4~~] [5]

i. Lack of transparency and comparability in the market for green bonds

[1] [2] [3] [4] ~~[5]~~

j. Doubts about the green quality of green bonds and risk of green washing

[1] [2] [3] ~~[4]~~ [5]

k. Other (if so, please specify) [BOX]

The affluent investor base exists – as evidence put forward by BETTER FINANCE showing that individual, non-professional investors are concerned and wish to be more involved in “green” projects. As such, we believe that the reason for a low uptake in the market is the unattractiveness for issuers.

2) To what extent do you agree that an EU GBS as proposed by the TEG would address the problems and barriers mentioned above in question 1? Please indicate which specific barriers it would address on a scale of 1 to 5 (1 negative impact, 3 no impact, 5 positive impact). Multiple answers are possible.

a. Absence of economic benefits associated with the issuance of green bonds

~~[1~~] [2] [3] [4] [5]

b. Lack of available green projects and assets

[1] [2] [3] [4] ~~[5]~~

c. Uncertainty regarding green definitions

[1] [2] [3] [4] **[5]**

d. Complexity of the external review procedure(s)

[1] [2] [3] [4] ~~**[5]**~~

e. Cost of the external review procedure(s)

[1] [2] ~~**[3]**~~ [4] [5]

f. Costly and burdensome reporting processes

[1] [2] **[3]** [4] [5]

g. Uncertainty with regards to the type of assets (physical and financial) and expenditure (capital and operating expenditure)

[1] [2] [3] [4] ~~**[5]**~~

h. Lack of clarity concerning the practice for the tracking of proceeds

[1] [2] [3] [4] ~~**[5]**~~

i. Lack of transparency and comparability in the market for green bonds

[1] [2] [3] [4] ~~**[5]**~~

j. Doubts about the green quality of green bonds and risk of green washing

[1] [2] [3] [4] ~~**[5]**~~

k. Other (if so, please specify) [BOX]

Questions on the proposed content of the standard

3) To what extent do you agree with the proposed core components of the EU GBS as recommended by the TEG? Please express your views using the scale from 1-5 (1 strongly disagree, 3 neutral, 5 strongly agree). Multiple answers are possible.

a. Alignment of eligible green projects with the EU Taxonomy

[1] [2] [3] [4] ~~**[5]**~~

b. Requirement to publish a Green Bond Framework before issuance

[1] [2] [3] [4] ~~**[5]**~~

c. Requirement to publish an annual allocation report

[1] [2] [3] [4] ~~**[5]**~~

d. Requirement to publish an environmental impact report at least once before final allocation

[1] [2] [3] [4] ~~**[5]**~~

e. Requirement to have the (final) allocation report and the Green Bond framework verified

[1] [2] [3] [4] ~~[5]~~

Please specify the reasons for your answer [BOX]

These measures will have the positive impact of increasing transparency and investor confidence. However, they should guarantee that the green bonds proceeds are used to fund certain green projects with specific environmental targets. On a second stage, standards and reporting will help the market of green bonds to grow and increase liquidity for green projects. One of the main issues linked to green bonds is the difficulty to assess if funding is channelled to actually "green" or new environmental projects. In order to ensure money is channelled into impactful green projects, the EU green bond standards should impede practices such as repackaging[9], loans that banks already have in their portfolio into green/social bonds.

4) Do you agree with the proposed content of the (a) Green Bond Framework, (b) Green Bond allocation report, and (c) Green Bond impact report as recommended by the TEG? [10]Select which elements you agree with. Multiple answers are possible.

a. I agree with the proposed content of the Green Bond Framework.

b. I agree with the proposed content of the Green Bond Allocation Report.

c. I agree with the proposed content of the Green Bond Impact Report.

d. None

e. Do not know

If you disagree with the proposed content for some or all of these documents by the TEG, please specify the reasons for your answer [BOX]

We believe that green bond impact report should be improved. Criteria and metrics on the impact of the environmental projects should be disclosed regularly.

5) Do you expect that the requirement to have the Green Bond Framework and the Final Allocation report verified (instead of alternatives such as a second-party opinion) will create a disproportionate market barrier for third party opinion providers that currently assess the alignment of EU green bonds with current market standards or other evaluation criteria?

a. Yes

[9] https://www.ft.com/content/16bd9a48-0f76-11e5-b968-00144feabdc0

[10] Please note that these reporting requirements refer only to the requirements in relation to the issued green bond (it is common in the green bond market to have reporting on the bond). These reporting requirements are not related to disclosure requirements for companies or funds, which arise from the EU Taxonomy Regulation or the Sustainability –related Disclosures Regulation.

b. No

c. Do not know

If yes, please specify the reasons for your answer [BOX]

Questions on the use of proceeds and the link to the EU Taxonomy

The EU Taxonomy Regulation specifies that the Union shall apply the EU Taxonomy when setting out the requirements for the marketing of corporate bonds that are categorised as environmentally sustainable. Given that the EU Green Bonds initiative will pursue, as its core objective, the aim of delineating the boundaries of what shall constitute an 'environmentally sustainable' bond, the Taxonomy will need to be applied to determine the eligibility of the proceeds of the bond issuance. However, there may be reasons to provide a degree of flexibility with regard to its application, or its application in specific cases. Building on market practice, the proposed EU GBS by the TEG recommends a use-of proceeds approach, where 100% of the proceeds of an EU Green Bond should be aligned with the EU Taxonomy (with some limited flexibility).

The below questions aim to gather stakeholder input on the application of the taxonomy in the context of EU Green Bonds.

6) Do you agree that 100% of the use of proceeds of green bonds should be used to finance or refinance physical or financial assets or green expenditures that are green as defined by the Taxonomy?

a. Yes, with no flexibility

b. Yes, but with some flexibility (i.e. <100% alignment)

c. No

d. Do not know

Please specify the reasons for your answer. If you selected b., please indicate what thresholds you would suggest, and why. [BOX]

There should be a certain degree of flexibility for those companies that are not included in the taxonomy but that want to raise money for concrete and impactful green projects.

7) The TEG proposes that in cases where (1) the technical screening criteria have not yet been developed for a specific sector or a specific environmental objective or (2) where the developed technical screening criteria are considered not directly applicable due to the innovative nature, complexity, and/or the location of the green projects, the issuer should be allowed to rely on the fundamentals of the Taxonomy to verify the alignment of their green projects with the Taxonomy. This would mean that the verifier confirms that the green projects would nevertheless (i) substantially contribute to one of the six environmental objectives as set out in the Taxonomy Regulation, (ii) do no significant harm to any of these objectives, and (iii) meet the minimum safeguards of the Taxonomy Regulation. Do you agree with this approach?

a. Yes, both (1) and (2)

b. Yes, but only for (1)

c. Yes, but only for (2)

d. No

e. Do not know

Please specify the reasons for your answer. Do you see any other reasons to deviate from the technical screening criteria when devising the conditions that Green Bond eligible projects or assets need to meet? If so, please clearly specify the reason for your answer and, where applicable, the respective area or (taxonomy-defined) activity. [BOX]

8) As part of the alignment with the EU Taxonomy, issuers of EU Green Bonds would need to demonstrate that the investments funded by the bond meet the requirements on do-no-significant-harm (DNSH) and minimum safeguards. The TEG has provided guidance in both its Taxonomy Final Report and the EU GBS user guide on how issuers could show this alignment. Do you foresee any problems in the practical application of the DNSH and minimum safeguards for the purpose of issuing EU green bonds?

a. Yes

b. No

c. Do not know

Please specify the reasons for your answer [BOX]

Full compliance with the EU taxonomy is necessary in order to ensure that the environmental project do not significant harm to either of the 6 environmental objectives and does not breach any minimum safeguards.

9) Research and Development (R&D) plays a crucial role in the transition to a more sustainable economy, and the proposed EU GBS by the TEG explicitly includes such expenditure as eligible use of proceeds. Do you think the EU GBS should provide further guidance on these types of activities, to either solve specific issues with green R&D or further boost investment in green R&D? If so, please identity the relevant issues or incentives.

a. Yes, as there are specific issues related to R&D that should be clarified.

b. Yes, the proposed EU GBS by the TEG should be changed to boost R&D.

c. No, the proposed EU GBS by the TEG is sufficiently clear on this point.

d. Do not know

Please specify the reasons for your answer [BOX]

Questions on grandfathering and new investments

10) Should specific changes be made to the TEG's proposed standard to ensure that green bonds lead to more new green investments?

a. Yes

b. No

c. Do not know

Please specify the reasons for your answer. If you are in favour of changes, please explain what changes should be made [BOX]

The verification and the assessment of the impact of the green bonds is extremely important to push the market towards green bonds that have a significant impact on the real economy. Additional requirements regarding impact reporting should be provided.

11) The EU Taxonomy technical screening criteria will be periodically reviewed. This may cause a change in the status of issued green bonds if the projects or assets that they finance are no longer eligible under the recalibrated taxonomy. In your opinion, should an EU Green Bond maintain its status for the entire term to maturity regardless of newly adapted taxonomy criteria?

a. Yes, green at issuance should be green for the entire term to maturity of the bond.

b. No, but there should be some grandfathering.

c. No, there should be no grandfathering at all. If you no longer meet the updated criteria, the bond can no longer be considered green.

d. Do not know

Please specify the reasons for your answer [BOX]

No grandfathering allowed in order to motivate all to agree on ambitious but realistic forward-looking/ dynamic criteria to avoid having recalibrations too often and then "transitional periods" allowing for re-adjusting to the new criteria in order not to lose the GB status. Choosing option B also for strategic reasons as naturally the majority of respondents to the consultation = industry is going to "vote" for A and B (and then the EC normally is using the results from the consultations without any weighing just saying how many respondents in% were in favour of different options).

If you select b, what should the maximum amount of years for grandfathering?

a. 3 years

b. 5 years

c. 10 years

d. 20 years

e. Different approach all together, please specify reasons for your answer [BOX]

Question on incentives

12) Stakeholders have noted that the issuance process for a green bond is often more costly than for a corresponding plain vanilla bond. Which elements of issuing green bonds do you believe lead to extra costs, if any? Please use the scale from 1 (no additional costs) to 5 (very high extra cost) – multiple answers possible:

a. Verification

[1] [2] [3] [4] [5]

b. Reporting

[1] [2] [3] [4] [5]

c. More internal planning and preparation

[1] [2] [3] [4] [5]

d. Other

Please explain and specify the reasons for your answer. [BOX]

If possible, please provide the estimated percentage and monetary increase in costs from issuing using the EU GBS, or – ideally – the costs (or cost ranges) for issuing green bonds under the current market regimes and the estimated costs (or cost range) for issuing under the EU GBS. [BOX]

13)In your view, how would the costs of an official standard as proposed by the TEG compare to existing market standards? Please rate on a scale of 1 to 5 (1 substantially smaller, 3 approximately the same, 5 substantially higher).

[1] [2] [3] [4] [5]

Please specify the reasons for your answer [BOX]

14) Do you believe that specific financial or alternative incentives are necessary to support the uptake of EU green bonds (green bonds following the EU GBS), and at which level should such incentives be applied (issuer and/or investor)? Please express your view on the potential impact by using the scale from 1 (not strong at all) to 5 (extremely strong) – multiple answers possible:

a. Public guarantee schemes provided at EU level, as e.g. InvestEU

[1] [2] [3] **[4]** [5]

b. Alleviations from prudential requirements

[1] [2] [3] [4] [5]

c. Other financial incentives or alternative incentives for investors

[1] [2] [3] **[4]** [5]

d. Other Incentives or alternative incentives for issuers?

[1] [2] [3] **[4]** [5]

e. None

Please specify the reasons for your answer, in particular if you have chosen "other incentives or alternative incentives" [BOX].

Tax incentives would be applied for a transitional period to stimulate the development of the market. There are various tax incentives can be implemented in order to foster the issuance of green bonds: 1. tax-exempt bond: investors don't have to pay income tax on interests from green bonds. [11] 2. Direct subsidy bonds: it's a form of subsidy for bond issuers for their net interest payments. [12] 3. Tax credit bonds: the bond investor instead of interest payments receives tax credits. [13]

Other questions related to the EU GBS

The EU GBS as recommended by the TEG is intended to apply to any type of issuer: listed or non-listed, public or private, European or international.

15) Do you foresee any issues for public sector issuers in following the Standard as proposed by the TEG?

a. Yes

b. No

c. Do not know

Please specify the reasons for your answer. [BOX]

16) Do you consider that green bonds considerably increase the overall funding available to or improve the cost of financing for green projects or assets?

a. Yes

b. No

c. Do not know

[11] https://www.climatebonds.net/policy/policy-areas/tax-incentives
[12] https://www.climatebonds.net/policy/policy-areas/tax-incentives
[13] https://www.climatebonds.net/policy/policy-areas/tax-incentives

Please specify the reasons for your answer. If possible, please provide estimates as to additional funds raised or current preferential funding conditions. [BOX]

Green bonds are specifically used to raise financing for environmental and or climate projects.

II. QUESTIONS ON SOCIAL BONDS AND COVID-19

During the ongoing COVID-19, financial markets have so far responded with significantly increased issuance of social bonds responding to the impact of COVID19. These social bonds often follow established market-based Social Bond Principles. The Commission is seeking the input of stakeholders on the lessons learned from this new development, including whether the Commission can play an even greater supportive role in building resilience to address future potential crises.

17) To what extent do you agree with the following statements? Please use the scale from 1 (strongly disagreeing) to 5 (strongly agreeing) – multiple answers possible:

a. Social bonds are an important instrument for financial markets to achieve social objectives.

[1] [2] [3] **~~[4]~~** [5]

b. Social bonds targeting COVID19 are an important instrument for financial markets in particular to help fund public and private response to the socioeconomic impacts of the pandemic.

[1] [2] [3] **~~[4]~~** [5]

c. Social bonds targeting COVID19 are mostly a marketing tool with limited impact on funding public and private responses to the socio-economic impact of the pandemic.

[1] **~~[2]~~** [3] [4] [5]

d. Social bonds in general are mostly a marketing tool with limited impact on social objectives.

[1] **~~[2]~~** [3] [4] [5]

e. Social bonds in general require greater transparency and market integrity if the market is to grow.

[1] [2] [3] [4] **[5]**

18) The Commission is keen on supporting financial markets in meeting social investment needs. Please select one option below and explain your choice:

a. The Commission should develop separate non-binding social bond guidance, drawing on the lessons from the ongoing COVID19, to ensure adequate transparency and integrity.

b. The Commission should develop an official EU Social Bond Standard, targeting social objectives.

c. The Commission should develop an official "Sustainability Bond Standard", covering both environmental and social objectives.

d. Other Commission action is needed.

e. No Commission action is needed in terms of social bonds and COVID19.

Please specify the reasons for your answer. [BOX]

The commission should develop an official sustainability bond standard that would include environmental social **and governance** objectives.

19)In your view, to what extent would financial incentives for issuing a social bond help increase the issuance of such bonds? Please use the scale from 1 (very strong increase) to 5 (no increase at all).

[1] [2] [3] ~~**[4]**~~ [5]

Please explain what kind of financial incentives would be needed, if any. [BOX]

Based on our research, a social bond has a specific purpose to finance projects that address social issues such as employment or avoidance of unemployment, reduction of income inequality or better integration of target groups in the market and society. Among the target groups, examples include the unemployed or aging populations.[14] As such, the current socioeconomic challenges faced by most EU countries could be helped to overcome through the issuance of social bonds. Industry reports show that, although trailing behind, social bonds are gaining momentum in tandem with green bonds.[15]

So far, the main social bond issuers were public authorities and supranational authorities, with 77% of the total issuance up to mid-2019, followed by corporate (21%) and private (2%) issuers.[16] Due to the global health crisis, social bond issuance increased five-fold from €5.5 billion in April 2019 to €30.4 in April this year. Among the largest issuers of social bonds in response to the Coronavirus pandemic were the Regional Authority of Madrid (€52 mln in April),[17] the European Investment Bank (€2 bln in April and May) or the IBRD (€3 bln in April).[18]

According to the pre-cited sources, Europe held a leading position in issuance of social bonds, with 67% of the global issuance in 2019. The main issue for institutional investors to take up more social bonds is the reduced liquidity, which makes them riskier. However, social bonds often provide better yields than traditional sovereign or corporate bonds: for instance, almost

[14] International Capital Markets Association. 'Social Bond Principles: Voluntary Process Guidelines for Issuing Social Bonds' (June 2020) ICMA, available at: https://www.icmagroup.org/assets/documents/Regulatory/Green-Bonds/June-2020/Social-Bond-PrinciplesJune-2020-090620.pdf;

[15] See Nadege Tillier, Benjamin Schroeder, 'Green Bonds Fade with Social Bonds' (ING.com, 8 July 2020) available at: https://think.ing.com/articles/sustainable-finance-green-bonds-fade-social-bonds-flare/; Natalie Kenway, 'Covid-19 Fuels Social Bond Issuance: Will They Overtake Green Bonds in 2020?' (ESGclarity.com, 2 June 2020), available at: https://esgclarity.com/covid-19-fuels-social-bond-issuance-will-they-overtake-green-bonds-in-2020/.

[16] Agnes Gourc, 'Social Bonds: The Next Frontier for ESG Investors' (CIB.Bnpparibas.com, 23 July 2019) BNP Paribas, available at: https://cib.bnpparibas.com/sustain/social-bonds-the-next-frontier-for-esg-investors_a-3-3005.html.

[17] Elisabet Furio, 'MAPFRE, the Autonomous Community of Madrid and BBVA Issue Spain's First Social Bond Against the Coronavirus' (BBVA.com, 24 April 2020) available at: https://www.bbva.com/en/mapfre-the-autonomous-community-of-madrid-and-bbva-issue-spains-first-social-bond-against-the-coronavirus/

[18] BNP Paribas, 'COVID-19 Response: Led or Supported by BNP Paribas' (Cib.bnpparibas.com, 7 May 2020), available at: https://cib.bnpparibas.com/documents/covid-19-response-bonds.pdf.

all social bonds listed on the Luxembourg Stock Exchange have positive (and quite high) yields compared to the already-usual negative rates practiced with traditional sovereign bonds.[19]

Therefore, this specialised part of sustainable debt finance could be a significant factor in speeding up economic recovery and to improving the returns on bond exposures of pension products.

[19] See here the list of the 46 social bonds traded on the LSE: https://www.bourse.lu/lgx-displayed-international-bonds?bonds=social.