

## Final European Mortgage Federation-European Covered Bond Council (EMF-ECBC) Comments on Draft ECON & ENVI Reports & Amendments to European Commission Proposal for a Regulation on a European Green Bond Standard

17 January 2022

The European Mortgage Federation-European Covered Bond Council (EMF-ECBC) is pleased to comment on the European Commission's Proposal for a Regulation on European Green Bonds in the context of the legislative discussions on this file in the European Parliament's ECON Committee. We believe that the European Green Bond Standard (EuGBS) has the potential to boost green bond markets but would like to highlight the following considerations and propose the following amendments to the European Commission's Proposal in order to ensure the integrity of the green covered bond market in particular.

For information, covered bonds are mostly backed by mortgages on real estate and are essential to put the EU's building stock on a net-zero emissions pathway.

### *Comment on Draft ECON Report:*

In Amendment 8 (Recital 7a (new)), the draft Report proposes the following: *"To facilitate comparison between different sustainable bond issuances and encourage standardisation of data collection in respect of green bonds, transparency requirements should apply to all bonds that are marketed in the Union as sustainable. To foster investor protection and avoid greenwashing of bonds marketed as sustainable, the information disclosed in respect of such bonds should be subject to the same standard of external verification as that applying to European green bonds"*

We strongly believe that the EU should not seek to expand the Regulation to other existing market standards which have paved the way for green bonds in the past. Existing market standards will also change in the course of time and certainly move towards the "Gold Standard" gradually.

### *Comment on Draft ENVI Report:*

In his draft report for ENVI, MEP Eickhout proposes to make the EuGBs mandatory. This would have the *de facto* consequence of negating all other green bond standards. It should not be forgotten that ICMA and the Climate Bonds Initiative paved the way for the green market to develop and a mandatory and exclusive use of EU Green Bonds would very probably lead to issuers stepping back from issuing 'green'. Next to the "Gold Standard" which is respecting the Taxonomy in full, other, market-driven standards that also become more stringent over time should continue to be available for issuers. Indeed, well respected and widely accepted market initiatives should not be suppressed without necessity.

### *Proposed Amendments to European Commission's Proposal for a Regulation:*

| Text proposed by the European Commission | Amendment         |
|------------------------------------------|-------------------|
| <b>Recital 11</b>                        | <b>Recital 11</b> |

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| <p>(11) Article 4 of Regulation (EU) 2020/852 requires Member States and the Union to apply the criteria set out in Article 3 of that Regulation to determine whether an economic activity qualifies as environmentally sustainable for the purposes of any measure setting out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable. It is therefore logical that the technical screening criteria referred to in Article 3, point (d), of Regulation (EU) 2020/852 should determine which fixed assets, expenditures and financial assets can be financed by the proceeds of European green bonds. In view of the expected technological progress in the field of environmental sustainability, the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 are likely to be reviewed and amended over time. Regardless of such changes, in order to provide legal certainty to issuers and investors and prevent amendments to the technical screening criteria from having a negative impact on the price of European green bonds that have already been issued, issuers should be able to apply the technical screening criteria applicable at the moment the European green bond was issued when allocating the proceeds of such bonds to eligible fixed assets or expenditures, until maturity of the bond. To ensure legal certainty for European green bonds whose proceeds are allocated to financial assets, it is necessary to clarify that the underlying economic activities funded by those financial assets should comply with the technical screening criteria applicable at the moment the financial assets were created. Where the relevant delegated acts are amended, the issuer should allocate proceeds by applying the amended delegated acts within five years.</p> | <p>(11) Article 4 of Regulation (EU) 2020/852 requires Member States and the Union to apply the criteria set out in Article 3 of that Regulation to determine whether an economic activity qualifies as environmentally sustainable for the purposes of any measure setting out requirements for financial market participants or issuers in respect of financial products or corporate bonds that are made available as environmentally sustainable. It is therefore logical that the technical screening criteria referred to in Article 3, point (d), of Regulation (EU) 2020/852 should determine which fixed assets, expenditures and financial assets can be financed by the proceeds of European green bonds. In view of the expected technological progress in the field of environmental sustainability, the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 are likely to be reviewed and amended over time. Regardless of such changes, in order to provide legal certainty to issuers and investors and prevent amendments to the technical screening criteria from having a negative impact on the price of European green bonds that have already been issued, issuers should be able to apply the technical screening criteria applicable at the moment the European green bond was issued when allocating the proceeds of such bonds to eligible fixed assets or expenditures, until maturity of the bond. To ensure legal certainty for European green bonds whose proceeds are allocated to financial assets, it is necessary to clarify that the underlying economic activities funded by those financial assets should comply with the technical screening criteria applicable at the moment the financial assets were created. <del>Where the relevant delegated acts are amended, the issuer should allocate proceeds by applying the amended delegated acts within five years.</del></p> |
| <p align="center"><b>Article 7</b><br/><b>Application of the Taxonomy Requirements</b></p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | <p align="center"><b>Article 7</b><br/><b>Application of the Taxonomy Requirements</b></p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| <p>1. Issuers shall allocate bond proceeds to the uses set out in Article 4(1) points (a), (b) and (c), Article 4(2), or the equity referred to in Article 5(1), point (b) by applying the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU)</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                | <p>1. Issuers shall allocate bond proceeds to the uses set out in Article 4(1) points (a), (b) and (c), Article 4(2), or the equity referred to in Article 5(1), point (b) by applying the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU)</p>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |

2020/852 applicable at the point in time when the bond was issued.

Where the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 are amended following the issuance of the bond, the issuer shall allocate bond proceeds to the uses referred to in the first subparagraph by applying the amended delegated acts within five years after their entry into application.

2. When allocating bond proceeds to the debt referred to in Article 5(1), point (a), issuers shall apply the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 applicable at the point in time when the debt was created.

Where, at the time of the creation of the debt referred to in the first subparagraph, no delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 were in force, issuers shall apply the first delegated acts that were adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852.

Where the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 are amended following the creation of the debt referred to in the first subparagraph, the issuer shall allocate bond proceeds to the debt referred to in the first subparagraph by applying the amended delegated acts within five years after their entry into application.

2020/852 applicable at the point in time when the bond was issued.

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Where the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 are amended following the creation of the debt referred to in the first subparagraph, the issuer shall ~~allocate bond proceeds to the debt referred to in the first subparagraph by applying the amended delegated acts within five years after their entry into application.~~ **apply the delegated acts adopted pursuant to Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU) 2020/852 applicable at the point in time when the debt was created.**

3. **Where a European green bond refinances a previously issued European green bond as referred to in Article 4(3), the delegated acts referred to in paragraph 2 shall be those applicable at the point in time when the debt was created.**

### ***Justification***

In order to provide certainty and predictability to borrowers, lenders and investors, also in the case of financial assets refinanced through green bonds, which is crucial for the transition towards more sustainable finance, grandfathering of financial assets should not be limited to five years. There should be full grandfathering to ensure that a bond retains its EU Green Bond status until maturity. Financial assets are directly linked to economic activities, such as real estate activities. The risk of losing Taxonomy eligibility creates possible barriers to long-term investments. This proposal is fully aligned with the Technical Expert Group (TEG) recommendation on p.29 of its EuGBs Report and p.32 of the accompanying Usability Guide.

Taking into account the TEG's recommendation, the grandfathering of EU Green Bonds for their entire tenor should be considered as equivalent to considering both the covered bonds and their underlying fixed and financial assets, according to Arts. 4 and 5, as taxonomy eligible throughout their lifetime. Therefore, grandfathering should apply not only to the covered bonds but also to the underlying assets e.g. mortgage loans, given the structural link between the asset and the liability side.

| Text proposed by the European Commission                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           | Amendment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
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| <p style="text-align: center;"><b>Article 6</b><br/><b>Taxonomy-alignment of use of proceeds</b></p> <p>1. The use of proceeds referred to in Article 4 shall relate to economic activities that meet the taxonomy requirements, or that will meet the taxonomy requirements within a defined period of time as set out in a taxonomy-alignment plan.</p> <p>The taxonomy-alignment plan referred to in the first subparagraph shall describe the actions and expenditures that are necessary for an economic activity to meet the taxonomy requirements within the specified period of time.</p> <p>The period referred to in the first and second subparagraph shall not exceed five years from bond issuance, unless a longer period of up to ten years is justified by the specific features of the economic activities concerned as documented in a taxonomy alignment plan.</p> <p>2. Where proceeds from a European green bond are allocated by means of financial assets either to capital expenditures as referred to in Article 4(1), point (b), or to operating expenditures as referred to in Article 4(1), point (c), the defined</p> | <p style="text-align: center;"><b>Article 6</b><br/><b>Taxonomy-alignment of use of proceeds</b></p> <p>1. The use of proceeds referred to in Article 4 shall relate to economic activities that meet the taxonomy requirements, or that will meet the taxonomy requirements within a defined period of time as set out in a taxonomy-alignment plan.</p> <p>The taxonomy-alignment plan referred to in the first subparagraph shall describe the actions and expenditures that are necessary for an economic activity to the taxonomy requirements within the specified period of time.</p> <p>The period referred to in the first and second subparagraph shall not exceed five years from bond issuance, unless a longer period of up to ten years is justified by the specific features of the economic activities concerned as documented in a taxonomy alignment plan.</p> <p>2. <b><i>By way of derogation from Article 6(1) and for a period which will not exceed five years from bond issuance, unless a longer period of up to ten years is justified by the specific features of the economic activities concerned as documented in a taxonomy alignment plan, up</i></b></p> |

period of time referred to in paragraph 1, first subparagraph, shall start from the moment of the creation of the financial asset.

***to 20 % of the proceeds of European green bonds may be allocated to economic activities that are not aligned with the taxonomy requirements***

***This derogation may be extended to other activities which are currently not covered under Articles 10(3), 11(3), 12(2), 13(2), 14(2) or 15(2) of Regulation (EU).***

3. Where proceeds from a European green bond are allocated by means of financial assets either to capital expenditures as referred to in Article 4(1), point (b), or to operating expenditures as referred to in Article 4(1), point (c), the defined period of time referred to in paragraph 1, first subparagraph, shall start from the moment of the creation of the financial asset.

### ***Justification***

It is important that there is appropriate flexibility in relation to the requirement that 100% of the proceeds of green bonds issuances be used to finance or refinance Taxonomy-aligned assets. Indeed, the EU Taxonomy introduces a new and significant risk for financial institutions in terms of validating compliance by customers – in terms of minimum safeguards, DNSH-criteria and also the technical criteria.

In order to achieve the climate goals in the real estate sector, banks should be able to refinance Taxonomy compliant mortgage loans through EuGBs aligned covered bonds. However, this will require large volumes of such mortgage loans which would take years to accumulate to meet minimum issue size. Without appropriate flexibility, it would take years before banks – and especially small banks - could issue an EU Green Bond, with knock-on effects for financing to borrowers and for the climate goals. A threshold of 80% for a transition period of at least 5 years should be introduced, as well as the possibility to extend to categories of assets which are not included in the current Taxonomy, considering that the latter must be updated in a timely manner.