EUROPEAN COVERED BOND COUNCIL

The EBA report on a green securitization framework at a glance

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EBA Report on a glance

The amendments introduced by the EU Capital Market Recovery Package have provided the EBA with a mandate to deliver a report aimed at developing a specific EU framework for sustainable securitizations with special focus on the integration of the sustainability-related transparency requirements into the SECR

The EBA analysis has been (significantly) affected by the

- not inclusion of the notes originated via ABSs in the "financial products" as defined in the SFDR
- non-dual recourse asset backed nature of the ABS instruments → the EU Taxonomy cannot be applied to the SPPE
- heterogenous range of mobilizable assets under the ABS
- current lack of available sustainable assets

→ All these factors have been examined to ensure clarity in the application of the EU GBS to ABSs and to ensure a level playing field across all type of green bond instruments.

The EBA report recommendations advocate the

- shift of the use of proceeds from the issuer/SPPE to the originator level (not currently foreseen in the EU GBS), as an intermediate step during the transition phase, allowing the sustainable securitization market to develop
- needs for some fine-tuning on environmental performance disclosure in respect of the EU GBS framework

→ On true-sale securitisations: a dedicated framework looks desirable at a latter stage, when the EU economy has further transitioned.

EBA Report – separate disclosures for securitised exposures

Use of proceeds as well as the disclosures and sanctions should apply at the originator level and not to the issuer/SPPE. This should be **of relevance to all types of bonds issued through an SPV**, including **covered bonds**.

However, if the use of proceeds is shifted to the originator, **additional EU GBS disclosure requirements** would be necessary to offer investors transparency on the green characteristics of the underlying portfolio transferred to the SPPE

- irrespective of a green use of proceeds, assets that are significantly harmful could be part of the assets in the SPPE
- issuers should be disincentivised to originate (new) brown assets, securitise them through an EU GBS to benefit from the price advantages, while keeping their green assets on balance sheet

→ Green Asset Ratio (GAR) and Banking Book Taxonomy Alignment Ratio (BTAR) of both the originator and the securitised exposures should be disclosed in the EuGB factsheet for all EuGB asset-backed securities.

Securitisations are no "financial product" under the SFDR. With the adoption of the Capital Markets Recovery Package (CMRP) it was decided that originators of simple, transparent and standardised (STS) securitisations should have the option to voluntarily disclose information on the consideration of adverse impacts on sustainability factors. In May 2022 the ESAs proposed **two mandatory indicators** and **five additional environmental indicators** related to residential and commercial real estate assets.

According to EBA, the voluntary **Principal Adverse Impact (PAI) disclosures** should apply to all securitisations, not only to simple, transparent and standardised (STS) securitisations, and should become mandatory over the medium term.

Mandatory indictors		**Residential**	**Commercial**
Energy efficiency	Exposure to fossil fuels through real estate assets		√
	Exposure to energy-inefficient real estate assets	√	
Non-green exposures 100%-GAR	Proportion of loans to households secured by residential immovable property that is not contributing to the climate change mitigation objective as per 7.2-7.7 Appendix 1 CDA	√	√

EBA Report – focus on the use of proceeds 1/2

Even if the EBA report points out the no-necessary need to set-up a dedicated framework for green securitisations (and other social/sustainability linked bonds) at this stage, the EBA report

- designs considerations for a green securitisation framework
- grounds on the principle of shifting the «use of proceeds» from the issuer to the originator
- reckons the current lack of available sustainable assets

→ **The report contains three alternative approaches may be followed to establish a dedicated green framework**

The alternative suggested approaches propose different solutions by mixing the use of collateral/use of proceeds

Light Green
the assets underlying the ABS are green for at least a certain % of the pool (a minimum level of underlying assets have to be taxonomy-compliant)
Green collateral approach

Medium Green
a minimum threshold on the green assets underkling the ABS
and
on the green use of proceeds are required
Parallel approach

Dark Green
A minimum threshold on the green assets underkling the ABS
and
on the 100% green use of proceeds (taxonomy aligned) are required
Integrated framework

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Alternatively, the ABS could result eligible for EU GBS in the case of 100% green use of proceeds by the originator ("adjusted EU GBS framework")

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EBA Report – focus on the use of proceeds 2/2

Light Green | **Medium Green** | **Dark Green**

EU Economy Transitioning level

Low Pace | *Steady Pace* | *End of phase-in*

Eligibility criteria in the pool of green assets and green use of proceeds

- pursuant articles 1,(2)(b) and 2(3) of the EU Taxonomy Regulation, securitisation products are not considered financial products → on the other hand, the EU Taxonomy constitutes a key benchmark for EU GBS which requires that the issuance proceeds are fully allocated towards EU taxonomy-aligned activities
- the taxonomy is restrictive on the definition of the assets that could be considered green (this element could affect not only the use of proceeds but the securitisable assets as well)
- at least during the early stage (current) transitional phase
  a) a simplified 'green framework/label' could be desirable
  b) the calibration of the threshold embedded in the 'light' and 'medium' green approach could result complex
- the use of 'transitional' assets should be permitted in both the use of collateral and use of proceeds

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Covered Bond: take-aways from the EBA report

Mapping the analysis implemented by EBA on securitisations and applying it to Covered Bonds…

Key elements analysed by EBA	*To be discussed/analysed*
Compliance to SFDR	*Given the double-recourse nature of the instrument, Covered Bonds are expected to be compliant to the definition of 'financial products' of the SFDR*
EU Taxonomy Applicability	• *Use of proceeds: the EU Taxonomy Applicability could not be differentiated from the one already in place for other EU GBS* • *Use of collateral: the factors identified and highlighted by EBA for securitisations could affect the cover pools* → *Could/should temporary regimes like 'light' or 'medium' green ones be transferred/replicated to the «Green Covered Bond»?*
EU GBS principles (disclosure requirements, external review)	• *Use of proceeds: no particular elements to be addressed [tbc/tbd]* • *Use of collateral: in this case, a dedicated framework could be desirable [some synergie with the securitisation framework to ensure a level play field between single/double recourse instruments?]*