

Enhance flexibility of the Green Bond Standard

The standard should better reflect issuers' needs

Introduction

Deutsches Aktieninstitut¹ appreciates the opportunity to respond to the EU Commission's consultation on the establishment of an EU Green Bond Standard. This position paper reflects the view of German non-financial companies on the issues raised.

¹ Deutsches Aktieninstitut (EU transparency register: 38064081304-25) represents the entire German economy interested in the capital markets. The about 200 members of Deutsches Aktieninstitut are listed companies, banks, stock exchanges, investors and other important market participants.

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

Question 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).

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]

Question 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).

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)

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

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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)

The EU Green Bond Standard provides comparability and transparency about the financing of green investments. It is a step into the right direction. Nevertheless, over-regulation and bureaucracy must not hinder the application of the standard by the companies.

This holds especially true for the following aspects:

The “use of proceeds approach”, where the proceeds of a Green Bond should solely finance green projects, should be extended for companies having difficulties to identify these projects separately/accurately (please see our answer to Q6).

A further obstacle is the complexity and the effort involved in reporting. We therefore propose to solely rely on the external verifier at the end of the process and to refrain from the annually allocation/impact reporting requirement (please see our answer to Q4).

In addition, the maximum look-back period should be based on the respective business model of the company (or industry). A look-back period is generally fine as long as it is reasonable, up-to-date and still delivers a positive impact. Issuers should be able to refinance eligible green Projects throughout their lifetime.

The average lifetime of e.g. an onshore wind-turbine or a solar panel is around 20-25 years. Issuers should be able to finance for 10 years with two subsequent 5 year bonds instead of a 10 year bond. The life-span has nothing to do with the underlying asset. With a Maximum look back-period refinancing is not possible. Lastly, it is of utmost importance for the success of the GBS that market participants, especially international investors and index providers, follow the eligible green project definition of the EU taxonomy approach. So far, the majority of green bond investors apply the MSCI Green Bond Index as a benchmark and a smaller part of them even reproduces it. Unfortunately, MSCI follows its own set of rules when assessing whether a bond is “green” which are not comprehensible for the market. Reliance on the GBS should increase transparency and comparability in the market and, hence, reduce this problem.

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

Question 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).

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]

f. Please specify the reasons for your answer

Reporting should be simplified in order to increase the supply of Green Bonds. We propose to rely solely on the external verifier at the end of the process and to refrain from the annually allocation/impact reporting requirement.

Companies that have not used their funds according to the standard, as monitored by the verifier, will quickly lose investor confidence and will not be able to raise new green funds again. In our view, it is an incentive for companies to comply with the standard during maturity in order to create legal certainty and be attractive for future Green Bond issuances. Therefore, annual reviews and reporting provides no value added either for investors or for the companies themselves.

In addition, for reasons of competition, verification should be provided from different institutions. Thus, the requirements for the accreditation of verifiers shall be reasonable to allow a sufficiently large market to develop

Question 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?

Select which elements you agree with.

- a. I agree with the proposed content of the Green Bond Framework. **Yes**
- b. I agree with the proposed content of the Green Bond Allocation Report. **Yes**
- c. I agree with the proposed content of the Green Bond Impact Report. **Yes**
- 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

We generally, agree but want to point out that this process will lead to a lot of effort in case of many separate projects.

Question 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
- b. No
- c. **Do not know**

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

Question 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:

In order to increase the attractiveness of Green Bonds and, hence, their supply by companies from different sectors, more flexibility is needed.

Although the definition “use of proceeds” is crucial for a green/sustainable instrument, Green bonds so far limited to project funding into sustainable investment projects (e.g. funding of an offshore wind power park). However, as many companies have difficulties in identifying such specific projects, Green bonds should in general be open for “general corporate purpose” finance at least to the share of green activities of the total business activities. This would make the instrument accessible to more companies and thus accelerate the green transformation.

The Commission should therefore introduce two types of Green Bonds: A Green Bond A with the requirement of concrete project references and a Green Bond B that can only be issued by companies proving, according to the EU- Taxonomy, green business activities. The latter could be, to a certain extent, open to "general corporate purpose" finance. In order to retain the link to the green activities and to prevent green washing, the funds raised by the Green Bond should be restricted to the financing of the green activity, e.g. measured as proportion of turnover/revenues, CAPEX or OPEX aligned with the EU Taxonomy. Reporting obligations at the end of the maturity would ensure that the do no significant harm principle and minimum safeguards were not violated.

Such a differentiated approach creates the incentive for companies to become sustainable per se and not just individual projects. It is also a market led solution, as investors can choose whether they buy a Green Bond reflecting the financing of a specific project (Type A) or a more generally applied Green Bond reflecting the share of green activities of a company (Type B).

Lastly, more flexibility is needed regarding the “use of proceeds” definition, as project cost might differ from the initial planning. Examples are the following

questions: What happens in case the portfolio of a company changes (M&A activities) and parts of the proceeds of the green bond are allocated to the M&A activities? In addition, what will happen if a bond promoted as green cannot prove enough green projects until final maturity?

Question 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.

The TEG proposals are very important as long as the Taxonomy currently does not cover all industries and by that excludes companies.

Question 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

Question 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 identify 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

4 Questions on grandfathering and new investments

Question 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

If you are in favour of changes, please explain what changes should be made

In order to lead to new green investments the "use of proceeds approach" should be extended to companies

that have difficulties in identifying green projects (please see our answer to Q6). Furthermore, the complexity and the effort involved in reporting should be reduced (please see our answer to Q4).

Question 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

Issuers and investors need legal certainty, reliable and transparent frameworks at the time of the issuance of the green bond. Adjustments to a recalibrated taxonomy during the maturity contradict these fundamental needs and hinder the development of the green bond market.

5 Question on incentives

Question 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

Question 13: In your view, how would the costs of an official standard as proposed by the TEG compare to existing market standards?

1- Substantially smaller

2 -Somehow smaller

3 - Approximately the same

4 - Somehow higher

5 - Substantially higher

Please specify the reasons for your answer to question 13

The application of certain elements of already existing market standards are usually voluntary (such as the verification procedure). The mandatory implementation e.g. of verification, as proposed in the GBS, will therefore increase costs.

So far, many issuers apply, according to the ICMA Green Bond Standard, a Second Party Opinion (SPO) on the Green Bond Framework and the external review on the reporting. They made the experience that the external review of the reporting can be very time-consuming and detailed. Therefore, it is very likely that the verification of the Green Bond Framework and the Final Allocation Report in particular will lead to significant additional costs.

Question 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)

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

Any direct intervention within the capital markets could be seen critical as it might deteriorate functioning markets and put certain financial market participants at a disadvantage, therefore no tax support, no equity support etc.

6 Other questions related to the EU GBS

Question 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**

Question 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**

Question 17: No answers to question 17

Question 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

We deem Social Bonds as an important financing instrument promoting social projects. Nevertheless, in order not to over-burden issuers with additional bureaucracy the standards for Social Bonds should correspond as close as possible with the Standards already developed for Green Bonds.

Question 19: No answers to question 19

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