

5 April 2023

Update on the recent provisional agreement on the EU GBS

On 28 February 2023, the EU co-legislators reached a [provisional agreement](#) on the Regulation for European green bonds (EU GBS or EuGB) – a milestone development for the EU’s long-awaited official standard. We [welcome and reiterate](#) our support for the voluntary nature of the EU GBS and of the agreed disclosures for the wider market.

ICMA has actively engaged with the European Commission, the European Parliament (EP), and the Council and Member States throughout the process to promote the consistency and complementarity of the EU GBS. We also published several position papers¹ since the original proposal of July 2021. ICMA was previously represented in all of the Commission’s sustainable finance expert groups since 2017, namely the High-Level Expert Group (HLEG), Technical Expert Group (TEG) and Platform on Sustainable Finance (PSF).

Looking ahead, we believe the future uptake of the EU GBS will be closely correlated with the resolution of the considerable usability challenges of the EU Taxonomy. ICMA will also continue to make recommendations to ensure, among other things, that the proposed voluntary disclosure templates minimise duplication or inconsistencies across other EU sustainable finance legislation.

This note looks at the key elements of the provisional agreement, anticipates what the broader market disclosures could look like, and highlights the potential obstacles to the broad use of the EU GBS and wider challenge of aligning with the Taxonomy. We also report on the potential timeline for the EU GBS.

Key elements of the provisional agreement

The detailed text of the provisional agreement is not yet available. We understand nonetheless that the key elements of the agreement are:

- The **voluntary nature of the EU GBS**; there is also no indication of a review clause for making it mandatory in the future.
- The **wider scope of the regulation**, which will include: (i) rules on the EuGB label itself; (ii) rules for external reviewers of EuGBs; and (iii) [voluntary disclosures for the broader market](#) for all green use of proceeds (UoPs) bonds and environmental SLBs in the EU.
- A **flexibility pocket of up to 15% on Technical Screening Criteria (TSC) alignment**, which will potentially be limited to (i) green activities for which there are no TSC and (ii) official international green finance support (e.g., climate finance reported to the UNFCCC and official development assistance reported to the OECD DAC). The use of the flexibility pocket could also be subject to additional safeguards such as higher-level alignment with the Taxonomy’s substantial contribution and DNSH conditions.

¹ These are: (i) a [statement](#) of support for the voluntary nature of the EU GBS and broader market disclosures in March 2023; (ii) a [statement](#) with the Executive Committee of the Principles in December 2022; (iii) a [paper](#) providing an updated analysis on the trialogue negotiating positions of the [EP](#) and the [Council](#) in June 2022; (iv) a [commentary](#) on the EP Rapporteur’s proposed amendments in January 2022; and (v) a [paper](#) providing an analysis on the European Commission’s original proposal in July 2021.

- **Grandfathering of TSC alignment** for 7 years with no other detail on the application modalities.
- **Registration and supervision of External Reviewers of EuGBs** by ESMA including rules on the management of conflict of interest and disclosures. The EU GBS requires both pre- and post-issuance external reviews.

Summary of the key positions of EU legislators and the provisional agreement

Key issues	EC	Council	EP	Provisional Agreement
Nature of the EU GBS	Voluntary	Voluntary	Voluntary (with a review clause)	Voluntary
Scope of the EuGB Reg.	EU GBS + External Reviewers (ERs) of EuGBs	EU GBS + ERs of EuGBs	EU GBS + all ERs (practically) + Mandatory disclosures for all green UoPs bonds and environmental SLBs	EU GBS + ERs of EuGBs + Voluntary disclosures for all green UoPs bonds and environmental SLBs
TSC flexibility	No	Up to 20%: for (i) activities with no TSC and (ii) internationally reported green finance support	No, but a “Taxonomy equivalency” mechanism has been proposed	Up to 15%: for (i) activities with no TSC and (ii) (potentially) internationally reported green finance support
Grandfathering	Partial 5-years (with EC stating that it concerns un-allocated proceeds)	Full	Partial 5 years for UoPs other than debt (with no forced re-allocation of already allocated proceeds) and 10-years (under portfolio-based approach)	Some reports referring to an agreement on 7 years grandfathering, but no clarity yet on the treatment of already allocated/committed proceeds

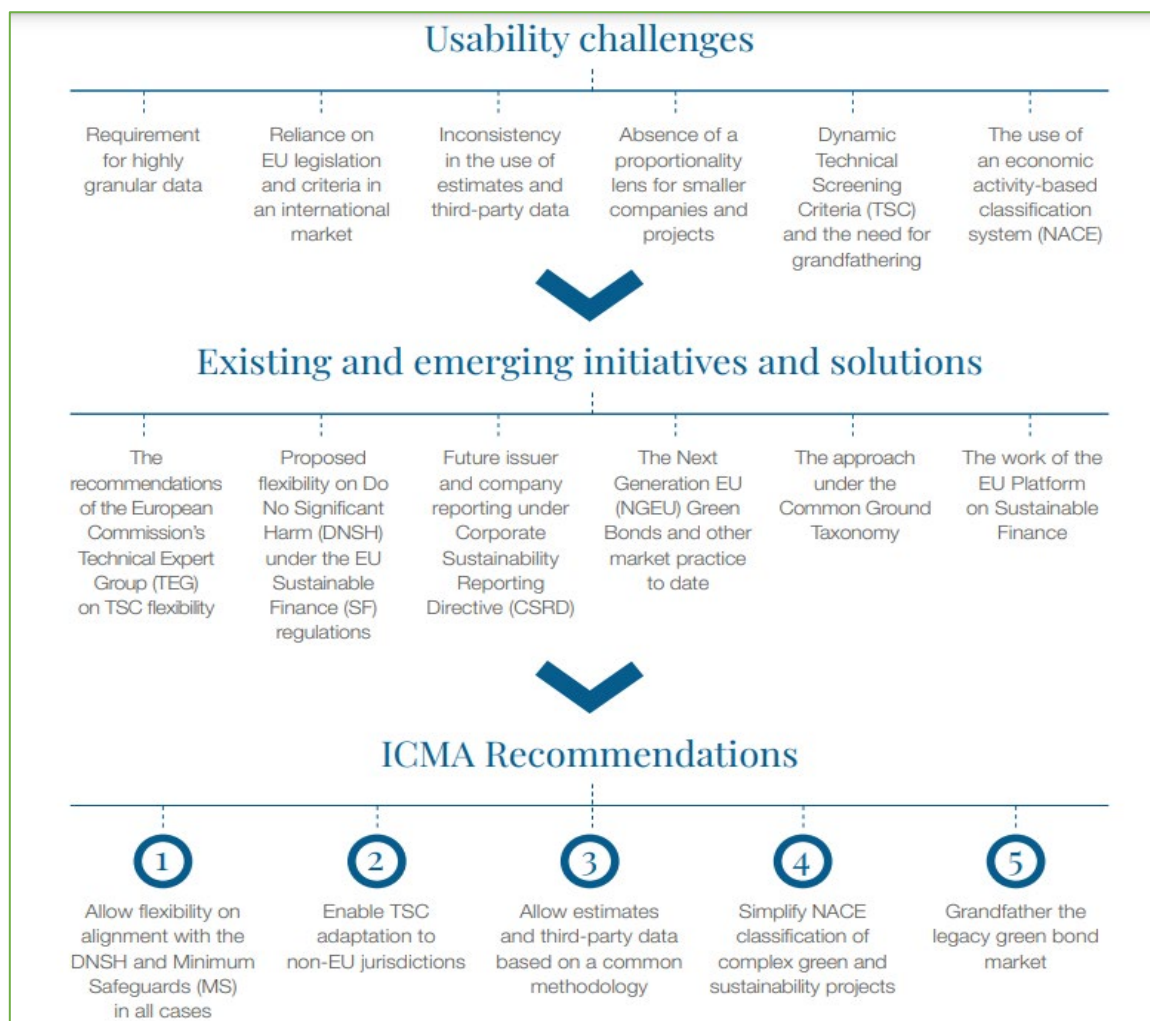
Voluntary disclosures for the broader market

The EU co-legislators decided to provide voluntary disclosure templates that will likely be recommended for green UoPs bonds and environmental-themed SLBs in the EU. While details of these templates are yet to emerge, they may potentially focus on, among other things, the Taxonomy alignment of green proceeds, how green proceeds and SLBs contribute to or are linked with issuers’ entity-level Taxonomy-alignment and transition plans, where these are published.

Future uptake of the EU GBS as a voluntary label

As mentioned, future uptake of the EU GBS as a voluntary label will be closely linked to the resolution of the Taxonomy’s usability issues. These have been identified in the [extensive report](#) of the Commission’s Platform on Sustainable Finance as well as ICMA’s [earlier report](#) (see infographic below). Most topically, they relate to the assessment of the Do No Significant Harm (DNSH) and Minimum Safeguards (MS) requirements including widespread data unavailability, heavy reliance on EU legislation and criteria (hindering the assessment of non-EU projects), and lack of assessment proportionality for smaller projects and SMEs.

Our expectation is that the EU GBS will be initially tested by EU SSAs, due mainly to their policy support and involvement with the label. Renewable energy projects in the EU, such as solar and wind power, by European power and energy companies and utilities will also very likely be financed with EuGBs.



Source: [Ensuring the usability of the EU Taxonomy](#) (February 2022)

The usability of the EU Taxonomy and the wider sustainable finance framework will be the major focus of the Commission and the EU Platform on Sustainable Finance 2.0 going forward. Accordingly, the Commission and other EU regulators have been providing additional guidance on the application of the EU Taxonomy, most notably a December 2022 [Commission Notice](#) on the interpretation of the Climate TSC.

The wider challenge of aligning with the EU Taxonomy

The current lack of Taxonomy aligned assets and projects will be a further significant and structural barrier to the wider uptake of the EU GBS. A recent Danske Bank [research presentation](#) indicated that the actual Taxonomy alignment numbers reported by corporates in the Nordics – arguably one of the most advanced regions in environmental regulation – is negligible. Looking at the alignment data reported by 75 companies, the research found that the average Taxonomy alignment for CapEx was 14%. 39 out of 75 companies reported 0% revenue alignment while 56 reported below 10%.

Another recent [study](#), this time relying on a top-down estimation methodology (and excluding the DNSH and MS tests) found the overall Taxonomy alignment of Euro area investor portfolios to be at 2.8%. The study also shows that Taxonomy alignment may differ considerably depending on sectors:

NACE code	Sector	Total investment (EUR bn)	Taxonomy eligible (EUR bn)	Taxonomy aligned (EUR bn)	Transition exposure (EUR bn)	Taxonomy eligible (%)	Taxonomy aligned (%)	Transition exposure (%)
A	Agriculture, forestry and fishing	5.6	0.6	0	0	10.9%	0.0%	0.0%
B	Mining and quarrying	123	0	0	110.8	0.0%	0.0%	90.1%
C	Manufacturing	1909.7	765	15.5	438	40.1%	0.8%	22.9%
D	Electricity, gas, steam, airco	515.5	454	206.3	178.6	88.1%	40.0%	34.6%
E	Water supply, sewerage, waste	31.7	30.2	4	0	95.3%	12.6%	0.0%
F	Construction	155.3	155.3	29.1	20.8	100.0%	18.8%	13.4%
G	Trade, repair of motor vehicles	384.3	0	0	6.8	0.0%	0.0%	1.8%
H	Transport and storage	315.3	208.3	5.1	294	66.1%	1.6%	93.3%
J	Information and communication	557.3	476.6	0	0	85.5%	0.0%	0.0%
L	Real estate	237.3	237.3	35.6	166.1	100.00%	15.00%	70.00%
M	Professional, scientific, technical	1706.7	73.6	0	0	4.3%	0.0%	0.0%
N	Support services	101.7	25	0.1	26.3	24.6%	0.1%	25.9%
...
	Total	10 635.9	2425.9	295.7	1241.4	22.8%	2.8%	11.7%

Source: [Two sides of the same coin: Green Taxonomy alignment versus transition risk in financial portfolios \(Nov. 2022\)](#)

Among other things, the low Taxonomy alignment is linked to the fact that the current EU economy is far from being on a clear Paris-aligned trajectory. This highlights the need to finance new Taxonomy aligned projects as well as transform existing assets with CapEx including via brownfield investments. Beyond its uptake, we believe the use of the EU GBS for transition should be seen as an important success metric in line with the Commission's [policy priority](#) for transition.

On this point, the successful outcome would also depend on how practical and encouraging the EU GBS' rules on CapEx plans will be (including their timeline, interaction with bond maturity, and grandfathering treatment). Consistency between the CapEx plan rules under the EU GBS and [Article 8 Delegated Regulation](#) would be an important factor. This would avoid fragmentation and disincentives against the use of the EU GBS for transition purposes.

Potential timeline

We expect that the technical details of the text will require several weeks to be worked out. It is also reported that the final text may stipulate a one-year gap period between the entry into force and the application of the regulation.