

# THE EU GREEN BOND STANDARD: A WELCOME LEAP FORWARD FOR SUSTAINABLE FINANCE?

## The EU Green Bond Standard: a welcome leap forward for sustainable finance?

*Following a lengthy period of negotiation between the co-legislators, the long-awaited EU green bond standard (the “EU GBS”) has been approved by the European Parliament and is set to be published shortly. First put forward as part of the European green deal investment plan, the standard forms part of the EU sustainable finance agenda which aims to leverage financial markets to support sustainable economic growth in Europe. The EU GBS is the first attempt to regulate the green bond market which has so far operated on the basis of voluntary adoption of the ICMA Principles. In this briefing, we look at key elements of the EU GBS and how it will shape the sustainable finance market.*

### A voluntary standard open to all issuers

The voluntary nature of the EU GBS has been the subject of much discussion following the European Parliament’s initial proposals for a mandatory standard, which caused concern amongst market participants for having the potential to stifle the market.

The agreement to proceed with a voluntary standard is welcome as it gives issuers the flexibility to choose to issue EU GBS bonds or continue to issue green bonds in line with existing market labels, such as the ICMA Principles (which the vast majority of existing green bonds are aligned with). It will also allow seasoned ESG issuers time to test the market first - the European Investment Bank for example has already committed to aligning its green bond programme over time with the EU GBS - as well as allowing the co-legislators the opportunity to test issuer uptake and overall market reaction.

### Scope of the label

The EU GBS label is for ‘use of proceeds’ green bonds and does not cover other types of ESG bonds such as social or sustainable bonds (although see ‘Voluntary disclosure requirements for the wider market’ below). Compliance with the various requirements will allow issuers to use the label “European Green Bond” or “EU GB” in their green bond prospectus, provided that the prospectus is published pursuant to the EU Prospectus Regulation (the “EU PR”) (i.e. for the purposes of the wholesale debt capital markets, a listing has been obtained on a EU regulated market).

## The EU GBS - At a Glance

The EU GBS is a voluntary “gold standard” available to all green bond issuers (in and outside the EU) to help the financing of sustainable investments. The EU GBS emerged out of a desire to harmonise the European sustainable bond market and to improve transparency and market integrity. There are four key requirements under the standard:

**Taxonomy Alignment:** The proceeds of the bond should be allocated to projects aligned with the EU Taxonomy (subject to a 15 per cent. flexibility pocket). The EU Taxonomy Regulation (the “EU Taxonomy”) is part of the EU’s sustainable finance framework and aims to provide a robust, science-based classification system, setting out criteria for economic activities aligned with achieving net zero by 2050, as well as broader environmental goals. For an economic activity to qualify as “environmentally sustainable” under the EU Taxonomy, the activity must (i) contribute substantially to at least one of the environmental objectives, or be an enabling activity, (ii) “do no significant harm” to any of the other environmental objectives, (iii) be carried out in compliance with minimum social and governance safeguards, and (iv) comply with detailed technical screening criteria to be adopted under the EU Taxonomy.

**Factsheet and Reporting:** The EU GBS requires an issuer to publish a green bond ‘factsheet’ prior to issue as well as comply with various pre- and post-issuance reporting requirements. External reviewers must provide a pre-issuance review of the factsheet as well as post-issuance review of the allocation reports.

**External Review:** All EU GBS bonds must be checked by an external reviewer to ensure compliance with the EU GBS and that funded projects are aligned with the EU Taxonomy.

**Supervision of External Reviewers:** The EU GBS sets out detailed rules for external reviewers including registration with and supervision by the European Securities Markets Authority (“ESMA”).

## Use of Proceeds

One of the hallmarks of the EU GBS is that the proceeds of the green bond must be invested in economic activities that are aligned with the EU Taxonomy. The proceeds can be allocated to finance the following: (i) fixed tangible or fixed intangible assets that are not financial assets, provided that they relate to economic activities that meet the EU Taxonomy requirements, (ii) financial assets, provided that the proceeds are directly, or indirectly, through subsequent financial assets, allocated to economic activities that meet the EU Taxonomy requirements (subject to certain conditions), (iii) the assets and expenditures of households, (iv) capital and operating expenditure that relate to economic activities that meet the EU taxonomy requirements or that will meet those requirements within a reasonably short period from the issuance of the bond, provided that the issuer has published a Capex plan (see below). Issuers may also allocate proceeds from a portfolio of one or more outstanding European green bonds to a portfolio of fixed assets or financial assets provided that they demonstrate in allocation reports that the total value of fixed assets or of financial assets in their portfolio exceeds the total value of their portfolio of outstanding European green bonds.

The taxonomy alignment aspect of EU GBS bonds is likely to be helpful to in-scope investors seeking to align such investments with their reporting obligations under the EU Sustainability Related Disclosures Regulation (“SFDR”).

## Flexibility in EU Taxonomy Alignment

Whilst the link to the EU Taxonomy is integral to the desire to maintain a high level of ambition for EU GBS bonds, there is recognition of the fact there are economic activities that are not yet covered by the EU Taxonomy’s technical screening criteria, which is still a work in progress. Therefore, the EU GBS provides a flexibility pocket of up to 15 per cent. of the net proceeds for (i) when there is no technical screening criteria available at the time of issue and (ii) certain activities in the context of international support reported in accordance with internationally agreed guidelines, including climate finance reported to the EU and United Nations Framework Convention on Climate Change (UNFCCC). In the case of (i), issuers must comply with the Do No Significant Harm principle under the EU Taxonomy and, in the case of (ii), issuers must comply with the technical screening criteria on a “best efforts” basis.

## Capex Plans

Where the use of proceeds relates to capital expenditure and operating expenditures that meet the EU Taxonomy requirements, the issuer is required to publish a ‘Capex plan’ in accordance with Commission Delegated Regulation (EU) 2021/2178. The Capex plan must (i) specify a deadline for taxonomy alignment of all the capital and operating expenditures funded by the EU GBS bond (before the bond reaches maturity), (ii) be subject to assessment from an external reviewer regarding taxonomy alignment, and (iii) be summarised in the bond prospectus.

## Factsheets

Issuers of EU GBS bonds must prepare a ‘green bond factsheet’ which must be reviewed pre-issuance by an

external reviewer. The EU GBS sets out a prescribed template for the factsheet and content requirements include (i) information on how the bond is expected to contribute to the issuer’s broader environmental strategy, (ii) where the issuer is subject to Article 8 of the EU Taxonomy, a description on how bond proceeds are expected to contribute to the issuer’s taxonomy-aligned assets, turnover, capital expenditure and operating expenditure, (iii) detail on how the bond proceeds are intended to contribute to funding and implementing transition plans (for issuers who are required to prepare them (for example, under the EU Corporate Sustainability Reporting Directive (“CSRD”)) or who choose to do so voluntarily), (iv) information on the intended allocation of proceeds to taxonomy-aligned economic activities, (v) detail on the environmental impact of the bonds (where available), and (vi) information on reporting. Factsheets will be considered ‘regulated information’ for the purposes of the EU PR and may be incorporated by reference in the bond prospectus.

Factsheets are not dissimilar to existing ‘green bond frameworks’ but go further in requiring a high level of detail in a prescribed format. It will be interesting to how the two interact and whether the content and format of the factsheet has an impact on how frameworks are prepared in the wider sustainable finance market as well.

## Reporting

There are detailed requirements and templates for reporting under the EU GBS. Until full allocation of proceeds (and, where applicable, until the completion of the Capex Plan), issuers must prepare an annual allocation report, which is subject to post-issuance review by an external reviewer. Issuers must also publish an impact report after full allocation of proceeds and at least once during the lifetime of the bonds, which may be subject to review by an external review at the option of the issuer.

// “This Regulation creates a gold standard that green bonds can aspire to. It ensures that the money raised must go to green activities and that bonds are vetted by professional and independent third-party reviewers. This is a world apart from current market standards.” //

Paul Tang, rapporteur

## Limited Grandfathering

The delegated acts adopted as part of the EU Taxonomy are to be subject to review and amendment, reflecting the need for the technical screening criteria to be dynamic and to allow for technological and scientific advances to be reflected. So the question of whether a European Green Bond should maintain its designation until maturity regardless of updated EU Taxonomy criteria has been discussed at length.

The European Council advocated full grandfathering on the basis that it is the simplest option, providing legal certainty for issuers. However, the final agreement has ended up in a more complex place: issuers are able to apply the technical screening criteria applicable at issue when allocating the proceeds to eligible fixed assets or expenditures, however, where the relevant technical screening criteria are amended, unallocated proceeds and

proceeds covered by a Capex plan that have not yet met the EU Taxonomy requirements must comply with the amended technical screening criteria within seven years. Proceeds covered by a Capex plan that are not yet taxonomy aligned are also subject to detailed rules which apply when the technical screening criteria has been amended.

Issuers at risk of not complying with the amended technical screening criteria within seven years are allowed to publish a plan (to be reviewed by an external reviewer) within the seven-year period for “how to align the economic activity to the amended technical screening criteria and to mitigate the negative consequences to the extent possible.”

### Green Securitisation

The EU GBS also contains specific provisions in relation to green securitisations. See our [briefing](#) ‘Green Securitisations in Europe: Fifty Shades of Green’ for further details.

### Sovereign issuers

Whilst the application of the EU GBS to sovereign issuers is not the focus of this briefing, it is worth noting that the EU GBS allows EU and third-country sovereigns to issue EU GBS bonds to finance public assets or expenditures that meet or are expected to meet the EU Taxonomy requirements within a reasonably short period from issuance, such as tax relief, subsidies, intermediate consumption, current transfers within a general government and current international cooperation.

### Voluntary disclosure requirements for the wider market

The EU GBS also separately includes voluntary sustainability disclosure requirements for bonds ‘marketed as environmentally sustainable’ (i.e. use of proceeds green bonds and sustainability-linked bonds (“SLBs”) with environmental key performance indicators and targets). These voluntary disclosure templates can be used by issuers even if they do not intend to use the EU GBS label and are intended to facilitate comparison of green bonds and sustainability-linked bonds for investors in the wider market as well as addressing greenwashing concerns.

The full detail is expected to be set by the Commission in due course but the templates will at a minimum require detail on, amongst other things, transition plans (where applicable), and further requirements for SLBs (such as details of the bond structure and the rationale, level of ambition, materiality, and calculation methodology of the KPIs) as well as for use of proceeds green bonds (such as the minimum proportion of bond proceeds to be used on activities that are environmentally sustainable under the EU Taxonomy).

Under the current EU prospectus regime, there are no specific disclosure requirements for ESG bonds, although ESMA has recently made a [public statement](#) on expected sustainability disclosure in prospectuses, noting that the forthcoming EU Listing Act will envisage sustainable disclosure requirements under the EU prospectus regime. It will be important to ensure the template requirements are consistent with the EU Listing Act reforms as well as other EU sustainable finance legislation. If well calibrated,

the templates could provide a useful steer to issuers on what minimum disclosures ought to be included in ESG bond prospectuses, particularly given the emerging investor expectations of more granular detail.

### Sanctions

As mentioned above, issuers of EU GBS bonds will need to have their prospectus approved by a national competent authority in the relevant Member State. Competent authorities have wide-ranging powers under the standard to ensure compliance including the ability to require publication of factsheets or reports in line with the EU GBS, impose fines, suspend trading and also make public the fact that the issuer is not in compliance with its obligations and require the issuer to publish that information on its website.

### Regulation of External Reviewers

The EU GBS establishes a new supervisory regime, providing regulatory oversight over second party opinion providers and external reviewers for the first time. The new regime requires reviewers of European Green Bonds to register with ESMA and meet various organisational and governance conditions for registration and ongoing supervision (with an equivalence assessment, recognition or endorsement mechanism available for third country reviewers).

To allow time for reviewers to adapt to the new regime, the EU GBS allows a limited transition period of 18 months where reviewers are able to provide their services as long as they notify ESMA and comply with certain requirements on a “best efforts” basis.

ESMA is also empowered to develop draft regulatory technical standards specifying a number of detailed requirements relating to registration (including the management of conflicts of interest) within 24 months of the EU GBS Regulation coming into force.

The new supervisory regime is likely to be well received by market participants given the importance of external reviews to investors and the need for consistency and transparency across providers. However, it is likely to be some time before we see changes in the market given the transitional period and that detailed regulatory technical standards from ESMA are not yet available.

### Future of the label?

There is no doubt that the EU GBS is an ambitious standard and goes well beyond existing guidelines and labels in the green bond market. The co-legislators have made it clear that their intention is for the standard to be for high quality green bonds, integrating European green bonds within the wider remit of the EU sustainable finance regulatory framework and tackling greenwashing concerns.

This raises the question of which issuers are in a position to use the standard. At the outset at least, the EU GBS is likely to be used by EU institutions as well as ‘pure play’ issuers. The key concern around take up of the label more broadly is linked to usability of the EU Taxonomy. There are concerns in a number of areas including in respect of the assessment of the Do No Significant Harm and Minimum Safeguards requirements including data unavailability and heavy reliance on EU legislation and criteria (which has an



impact on the ability to assess non-EU projects) as identified in a [report](#) of the Commission's Platform on Sustainable Finance and an [ICMA Report](#). In particular, there are concerns around a current lack of taxonomy assets which has led market participants to question whether the 15 per cent. flexibility pocket provides sufficient leeway for many issuers to be able to utilise the EU GBS at all.

There is also the question of whether the label (whilst intended for all), will in practice be primarily relevant for EU issuers who will need to report in line with CSRD (which includes reporting on annual taxonomy alignment), and are more likely to list their debt securities on an EU regulated market. Issuers outside the EU may be more incentivised to consider the voluntary disclosures available for the wider sustainable finance market if they evolve into market standard disclosures and enhance comparability for bond investors, particularly for SFDR purposes.

Ultimately, whilst the EU GBS will enhance transparency and promote harmonisation in the European green bond market, the question of how successful the label will be will depend on a number of factors including investor demand ('dark green funds' for example will find EU GBS bonds an attractive option), pricing advantages and if issuers can be otherwise incentivised to move away from an existing well-functioning market based on voluntary best practice.

The tougher sanctions under the EU GBS will also weigh heavily on the minds of issuers who are increasingly cognisant of reputational and litigation risks when preparing their ESG bond prospectuses.

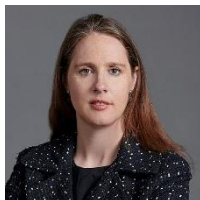
What is clear is that while the EU GBS represents the first formal attempt to regulate the green bond market, the increasing focus on accountability and transparency will mean that other regulators are not far behind. In the UK, the Financial Conduct Authority has indicated that it will consider various approaches to ESG disclosure in prospectuses as part of UK prospectus reforms (see our briefing [here](#) for further details). It will be interesting to see how this evolving regulatory landscape, together with shifting investor expectations, impacts the global sustainable bond market and if the EU GBS does, over time, spur issuers to be ambitious when seeking funding for their green projects.

### Next steps

The final text is expected to be published shortly with the EU GBS due to apply 12 months after its entry into force (likely late 2024/early 2025).

*For more information, please speak to your usual Slaughter and May contact or one of the lawyers listed below.*

## CONTACT



**Caroline Phillips**  
Head of Debt Capital Markets  
Partner  
T: 0207 090 3884  
E: [caroline.phillips@slaughterandmay.com](mailto:caroline.phillips@slaughterandmay.com)



**Matthew Tobin**  
Head of Financing  
Partner  
T: 0207 090 3445  
E: [matthew.tobin@slaughterandmay.com](mailto:matthew.tobin@slaughterandmay.com)



**Guy O'Keefe**  
Partner  
T: 0207 090 3299  
E: [guy.okeefe@slaughterandmay.com](mailto:guy.okeefe@slaughterandmay.com)



**Kevin Howes**  
Partner  
T: 0207 090 3173  
E: [kevin.howes@slaughterandmay.com](mailto:kevin.howes@slaughterandmay.com)



**Sabine Dittrich**  
Head of EU Financial Regulation  
T: 0207 090 5786  
E: [sabine.dittrich@slaughterandmay.com](mailto:sabine.dittrich@slaughterandmay.com)



**Minolee Shah**  
PSL Counsel  
T: 0207 090 5491  
E: [minolee.shah@slaughterandmay.com](mailto:minolee.shah@slaughterandmay.com)

**London**  
T +44 (0)20 7600 1200  
F +44 (0)20 7090 5000

**Brussels**  
T +32 (0)2 737 94 00  
F +32 (0)2 737 94 01

**Hong Kong**  
T +852 2521 0551  
F +852 2845 2125

**Beijing**  
T +86 10 5965 0600  
F +86 10 5965 0650

Published to provide general information and not as legal advice. © Slaughter and May, 2023.  
For further information, please speak to your usual Slaughter and May contact.

[www.slaughterandmay.com](http://www.slaughterandmay.com)