

Capital Markets

INSIGHT

THE EU GREEN BOND STANDARD

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The Council of the European Union and the European Parliament announced, on 28 February 2023, that provisional agreement on the European Green Bond Standard (the **EU GBS** and the **Regulation**) had been reached. More recently the consolidated legal text (including the relevant annexes) has been made available. Whilst the general direction of the EU GBS has been known for some time, the newly available text clarifies a number of questions as to how the EU GBS will work. We provide an overview in this briefing.

Key Takeaways

Timing – The agreement is provisional as it is subject to legal and linguistic checks and still needs to be confirmed by the Council and the European Parliament before it is final. However, that is expected later in 2023 and it will apply c. 12 months after publication in the Official Journal. Market participants can therefore look at the current text with a degree of certainty.

Core Principles – The EU GBS remains a voluntary standard where the net proceeds of the issuance must be used to finance sustainable economic activities in alignment with Regulation (EU) 2020/852 (the **EU Taxonomy**). There are, however, a number of caveats and complexities to this general requirement. For those sectors not yet covered by the detailed technical screening criteria (**TSC**) of the EU Taxonomy and for certain very specific activities connected with the support of international green finance there will be a “flexibility pocket” of 15% of proceeds that do not need to be fully aligned. Further, for operating and capital expenditures that will be EU Taxonomy aligned within a “reasonably short” period of time post issuance, the Issuer may publish a “CapEx plan” outlining a pre maturity deadline by which those expenditures will be Taxonomy aligned. In addition, where the TSC are amended after issuance, unallocated proceeds and proceeds covered by a CapEX plan that have not yet met EU Taxonomy requirements should be allocated in line with the amended TSC within 7 years. A pre-issuance “European green bond fact sheet” and post-issuance allocation and impact reports must be provided by the issuer in line with standardised templates. EU GBS bonds will require review by an external reviewer subject to a registration system maintained by the European Securities and Markets Authority (**ESMA**).

By way of reminder, EU Taxonomy alignment means that the activity (i) substantially contributes to at least one of 6 environmental objectives set out in the EU Taxonomy (i.e. climate change mitigation, climate change adaptation, sustainable use and protection of water and marine resources, transition to a circular economy, pollution prevention and control and protection and restoration of biodiversity and ecosystems), (ii) does no significant harm to any of the other 5 environmental objectives, (iii) meets minimum safeguards relating to human, labour and consumer rights, corruption, taxation and fair competition, and (iv) complies with the TSC.

EU Prospectus Regulation – The designation “European green bond” or “EuGB” will only be available for issuers that publish a prospectus compliant with Regulation (EU) 2017/1129 (the **EU Prospectus Regulation**) and EU sovereign or quasi-sovereign issuers that are exempt from the EU Prospectus Regulation. National competent authorities of the home member state of the issuer will supervise compliance. EU GBS bonds will therefore be subject to the EU Prospectus Regulation liability regime and potential sanction by competent authorities. Additional disclosure items must be included in an EU GBS prospectus such as a summary of the CapEX plan (if used) and a statement that the bonds are issued in accordance with the Regulation.

Voluntary disclosures for sustainability linked bonds (SLBs) and non-compliant green bonds – In addition, use of proceeds bonds “marketed as environmentally sustainable” that are not EU GBS bonds and SLBs with “environmental sustainability objectives” may also provide voluntary pre-issuance and post-issuance disclosures based on templates to be developed by the European Commission. The templates will include disclosure of transition plans and EU taxonomy aligned turnover, capital and operating expenditure where the issuer is subject to the EU Corporate Sustainability Reporting Directive and Article 8 of the EU Taxonomy. For SLBs, the voluntary templates will require further detail relating to the rationale and ambition of the key performance indicators of the bond. Post-issuance voluntary disclosures will be subject to competent authority supervision.

INSIGHT: KEY FEATURES OF THE EU GREEN BOND STANDARD

Use of Proceeds

Net proceeds – Subject to limited exceptions, net proceeds must be allocated in alignment with the EU Taxonomy. Further, issuers must use the proceeds for financing or refinancing, **fixed assets, capital expenditure, operating expenditure, financial assets created not later than 5 years post issuance, or “assets and expenditures of households”**. 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 aligned with the EU Taxonomy**.

Flexibility Pocket – Up to **15% of proceeds** may be allocated to EU Taxonomy compliant activities where no TSC have been developed or for specific activities related to international support of green finance (e.g. specific types of climate finance reported to the United Nations Framework Convention on Climate Change).

CapEX Plan – Proceeds may also be used to finance **capital expenditures and operating expenditures** that will meet the requirements of the EU Taxonomy within a “reasonable period of time” subject to the publication of a CapEX plan (and inclusion of a summary of the CapEX plan in the prospectus).

Grandfathering – Proceeds should be allocated in line with the TSC at the time of issuance. Where the TSC are amended after issuance, unallocated proceeds and proceeds covered by a CapEX plan that have not yet met EU Taxonomy requirements should be allocated in line with the amended TSC within **7 years**.

Reporting

Pre Issuance report – The issuer is required to complete a **“European green bond factsheet”** pre issuance which must be verified by an external reviewer. The form of the report is set out in **Annex I** to the Regulation.

Allocation reports – An allocation report must be published for every 12 month period until the full allocation of proceeds and, if applicable, until completion of the CapEX plan. Issuers must obtain a post-issuance review from an external reviewer after full allocation of the proceeds and on an annual basis where proceeds are allocated in that year on a portfolio basis. Allocation reports and reviews, must be published within 270 days following the end of the annual period. The form of the report is set out in **Annex II** to the Regulation.

Impact reports – An impact report must be published after full allocation of proceeds and at least once during the lifetime of the bond. The form of the report is set out in **Annex III** to the Regulation. A review of the impact report by an external reviewer may be obtained, but is not mandatory.

CapEX Plan – CapEX plans, if used, will also require an external review, which must be published within 60 days of the deadline by which the capital and operating expenditures are to be EU Taxonomy aligned.

External Review

Independent external reviewer – Issuers will be required to obtain external reviews on the European green bond fact sheet and certain allocation reports (see **“Reporting - Allocation Reports”**). Issuers may also contract an external reviewer to provide an impact report review. The forms of these external reviews are set out in **Annex IV** to the Regulation.

ESMA Registration System – External reviewers will be subject to a **registration system and supervisory framework** and will need to provide their independent opinion on whether the issuer has aligned with the EU Taxonomy criteria. ESMA will be tasked with establishing the register and supervision regime for EU and third-country external reviewers.

Transitional regime – Will apply for the first 18 months following the entry into force of the Regulation to enable issuance before the registration system is fully on-stream.

EU Green Bond Standard

Other Features

EU Prospectus Regulation – The EU GBS can only be used by issuers that publish a prospectus under the EU Prospectus Regulation with the exception of those EU sovereign and quasi sovereign entities that are exempt from the EU Prospectus Regulation.

Sovereigns and public bodies – EU sovereign and quasi sovereign entities that are exempt from the EU Prospectus Regulation and third-country equivalent entities, may allocate proceeds to various types of public expenditure provided that the proceeds are allocated in alignment with the EU Taxonomy. Post-issuance reviews of the allocation of proceeds may be provided by a “state auditor” not subject to ESMA supervision.

Securitisation – The use of proceeds requirements will apply to the originator. Synthetic securitisations are excluded as are certain sectors such as exposures financing the exploration, mining, extraction, production, processing, storage, refining or distribution, including transportation, and trade of fossil fuels.

Voluntary disclosures – Issuers of use of proceeds bonds “marketed as environmentally sustainable” that are not EU GBS bonds and environmental sustainability linked bonds may provide voluntary pre-issuance and post-issuance disclosures based on templates to be developed by the European Commission.

KEY CONTACTS

LONDON


PETER PEARS

Partner | London
E: ppears@mayerbrown.com
T: +44 20 3130 3297


JAMES TAYLOR

Partner | London
E: jtaylor@mayerbrown.com
T: +44 20 3130 3136


BERND BOHR

Partner | London
E: bbohr@mayerbrown.com
T: +44 20 3130 3640


ROBERT M. FLANIGAN

Partner | London
E: rflanigan@mayerbrown.com
T: +44 20 3130 3488


LOLA ADEKOYA

Associate | London
E: LAdekoya@mayerbrown.com
T: +44 20 3130 3226


WHITNEY JOSEPH

Senior Associate | London
E: wjoseph@mayerbrown.com
T: +44 20 3130 3116


SERENA MUSSONI

Lawyer (Milan) | London
E: smussoni@mayerbrown.com
T: +44 20 3130 3196

FRANKFURT


PATRICK SCHOLL

Partner | Frankfurt
E: pscholl@mayerbrown.com
T: +49 69 7941 1060


SUSANNE LENZ

Partner | Frankfurt
E: slenz@mayerbrown.com
T: +49 69 7941 1066


DUŠAN STOJKOVIĆ

Counsel | Frankfurt
E: dstojkovic@mayerbrown.com
T: +49 69 7941 1073


ALEXEI DÖHL

Counsel | Frankfurt
E: adoehl@mayerbrown.com
T: +49 69 7941 1105


MARCEL HÖRAUF

Counsel | Frankfurt
E: mhoerauf@mayerbrown.com
T: +49 69 7941 2236

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