

## ***Enhancing the role of European promotional and public banks under the EU Taxonomy and EU Green Bond Standard***

### **EAPB recommendations for the European Commission and the Platform on Sustainable Finance**

#### **Introduction - The EAPB and its members**

The European Association of Public Banks (EAPB) represents national and regional promotional and public banks, including municipality funding agencies and public commercial banks. EAPB members provide financial services and funding for projects that support sustainable economic and social development. Activities range, amongst others, from the funding of companies and the promotion of a greener economy to the financing of social housing, health care, education, and public infrastructure at national, regional and local level. For promotional and public banks capital markets are the most important funding source. Because of the characteristics of their business model, promotional and public banks are early adopters of sustainable bonds issuance. In 2020, members of the EAPB issued over €120 bn in corporate bonds, of which around 15% were sustainable bonds. In the period between 2017 - 2020 the issuance of sustainable bonds by promotional and public banks increased by 56%.

#### **The limited usability of the current EU Taxonomy and EU GBS for promotional and public banks**

EAPB members support the aim of the EU Taxonomy Regulation (“EU Taxonomy”) and EU Green Bond Standard (“EU GBS”), which is to direct more capital towards sustainable economic activities. Due to their specific business model, European promotional and public banks are well positioned to play a key role in a fair and social transition to a more sustainable society. This is recognized by the European Commission which stated that “*National promotional banks play an important role in catalysing long-term finance*” in policy areas including climate change<sup>1</sup>.

Promotional and public banks have been early adopters of green bonds, providing stable funding for the public sector, thereby enabling public policy objectives with respect to a more sustainable society. It is therefore unfortunate that many EAPB members experience difficulties applying the EU Taxonomy and the EU GBS. It seems that when developing the EU Taxonomy and EU GBS, the business models of commercial banks have been taken as a starting point and those of the promotional and public banks have not been duly considered. As a result, both the EU Taxonomy and the EU GBS in their current form are not well-suited for promotional and public banks. In this context, it is important to point out that the limited usability of the EU Taxonomy for promotional and public banks has consequences for regulatory reporting, as credit institutions are also required to report the GAR in their Pillar 3 disclosures on ESG risks.

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<sup>1</sup> Communication from the Commission to the European Parliament and the Council: “Working together for jobs and growth: The role of National Promotional Banks (NPBs) in supporting the Investment Plan for Europe”: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:52015DC0361>

## Difficulties with the EU Taxonomy and the EU GBS and corresponding EAPB solutions

To enhance the role of European promotional and public banks under the EU Taxonomy and EU GBS, the EAPB would like to address the difficulties that these banks currently face when applying them, while at the same time proposing solutions to overcome these difficulties. With these recommendations, we hope to make the EU Taxonomy and EU GBS a usable tool for both commercial as well as promotional and public banks, to leverage their potential for achieving our shared European mission to direct more capital towards sustainable economic activities.

### 1. Lack of data for the GAR due to non-disclosing public sector and SME clients

For many promotional and public banks, the majority of clients are governmental and other public sector entities. In addition, many promotional banks support SMEs with special loan programs. Most of these entities are not required to report under the NFRD or in the future, CSRD. Hence, they will not report on their green economic activities under the Disclosures Delegated Act (“DDA” - Article 8 of the EU Taxonomy). This poses a challenge for those EAPB members that report under the NFRD and the EU Taxonomy. To calculate their Green Asset Ratio (“GAR”), the taxonomy alignment ratio of their assets, banks must use the most recently available data of their counterparties. In the absence of information due to non-disclosing clients, promotional and public banks will need to request clients to disclose the information voluntarily, which would be burdensome, or alternatively, make use of estimates.<sup>2</sup> We welcome the clarification in the Commission Notice of 21 December 2023<sup>3</sup> that exposures to regional and local public authorities should be included in the GAR where the use of proceeds is known. Hence, use of such voluntarily reported data is allowed for mandatory EU Taxonomy reporting (the ‘mandatory GAR’). However, voluntarily reported SME data, estimates and proxies are not allowed to be used for the ‘mandatory GAR’ and may only be used for additional and voluntary reporting (the ‘voluntary GAR’) which does not carry the same significance for capital markets.

In its report of October 2022, the Platform on Sustainable Finance advised the European Commission to examine and review how the EU Taxonomy could be applied to general-purpose sovereign debt, and more broadly to the public sector beyond green bonds and use-of-proceeds. It was noted that this required further thorough study and a full impact assessment. The priority of the recommendation was however qualified as ‘low’.<sup>4</sup>

The usability of the EU Taxonomy for public sector exposures is crucial for the GAR to be representative and enables promotional and public banks to issue taxonomy-aligned bonds and hence help to pursue public policy objectives, especially at the local level.

### The EABP recommends:

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<sup>2</sup> Commission Notice on the interpretation of certain legal provisions of the DDA under Article 8 of EU Taxonomy Regulation on the reporting of eligible economic activities and assets, FAQ 20, [Publications Office \(europa.eu\)](https://publications.ec.europa.eu/publication-detail/-/publication/11111111-1111-1111-1111-111111111111)

<sup>3</sup> Draft Commission Notice on the interpretation and implementation of certain legal provisions of the Disclosures Delegated Act under Article 8 of the EU Taxonomy Regulation on the reporting of Taxonomy-eligible and Taxonomy-aligned economic activities and assets (third Commission Notice), [link](#)

<sup>4</sup> Platform Recommendations on Data and Usability, October 2022, p. 15 and 83, [Platform on Sustainable Finance's recommendations on data and usability of the EU taxonomy \(europa.eu\)](https://platformon.sustainablefinance.europa.eu/recommendations-on-data-and-usability-of-the-eu-taxonomy)

- That the usability of the EU Taxonomy for (general purpose) public sector exposures must be given full priority to enable promotional and public banks to assess the taxonomy alignment of their exposures. This would in turn foster the issuance of bonds in line with the EU GBS.
- We note an inconsistency between Level 1 (Recital 21 EU Taxonomy)<sup>5</sup>, in which the assessment of taxonomy-aligned exposures of non-reporting customers by financial market participants is allowed, and the DDA article 7 paragraph 7<sup>6</sup>, which excludes this possibility for the mandatory Green Asset Ratio. We request the EU Commission to correct this inconsistency and to explicitly allow such an option also in Level 2 for the mandatory GAR. At least for exposure to non-reporting counterparties, estimates based on standardized models should be allowed (opt-in).

As stated above, promotional and public banks are early adopters and major issuers of green bonds. However, considering the absence of information due to non-disclosing counterparties and the assumption that -with the exception of known use of proceeds exposures to local and regional governments- an EU green bond cannot be issued on the basis of voluntarily reported alignment information (based on proxies and estimates), EAPB members foresee that it will be challenging to issue green bonds in line with the EU GBS. Therefore, as stated above, the usability of the EU Taxonomy for (general purpose) public sector exposures needs to be given full priority.

#### The EABP welcomes:

- The voluntary nature of the EU GBS, which enables the coexistence with well-established market standards. This shall allow public and promotional banks (including major current issuers of green bonds) to continue financing the required sustainable economic activities of the European public sector through the issuance of green bonds, even beyond the scope of the EU GBS. In this context, special attention should be paid to any distortions on the green bond market and specifically on the current market standards arising from the optional disclosures (opt-in regime) provided in Art. 13g and 13h of the EU GBS for use of proceeds bonds or sustainability-linked bonds. Having said that, it is of utmost importance for promotional banks to be able to secure future access to funding by accommodating (potentially shifting) investor preference to EU taxonomy aligned bonds. Therefore, we emphasize the relevance of a workable framework for the target groups public sector and SMEs which will enable promotional and public banks to issue taxonomy aligned bonds on a large scale.
- The statement made in measure 4 of the “Commission staff working document: Enhancing the usability of the EU Taxonomy and the overall EU sustainable finance framework”<sup>7</sup>. The SFDR Q&A has clarified that the use of estimates concerning taxonomy alignment is permitted for disclosures under SFDR in certain cases (e.g., non-NFRD undertakings such as unlisted SME, referring also to recital 21 of Taxonomy regulation). Moreover, the European Commission stated it would assess the feasibility of issuing guidance on taxonomy-estimates. We would welcome such a guidance. The use of estimates is crucial in order to support market participants of all kinds in their transition towards sustainable economic activities, without overburdening undertakings, especially SMEs. We encourage the inclusion of a SME opt-in to the GAR numerator, a legal permission to use estimates not only under SFDR but also under the taxonomy regulation as well as the DDA and a guidance for a pragmatic approach on how to assess Do No Significant Harm (DNSH) and minimum safeguards in the context of SME financing.

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<sup>5</sup> Regulation (EU) 2020/852 of the European parliament and of the Council (EU) on the establishment of a framework to facilitate sustainable investment, and amending Regulation (EU) 2019/2088: [EUR-Lex - 32020R0852 - EN - EUR-Lex \(europa.eu\)](#) Recital 21

<sup>6</sup> Commission Delegated Regulation (“Disclosures Delegated Act”), Art. 7 paragraph 7. [Publications Office \(europa.eu\)](#)

<sup>7</sup> Commission staff working document: Enhancing the usability of the EU Taxonomy and the overall EU sustainable finance framework: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52023SC0209>

Some promotional and public banks support clients via promotional lending with the use of proceeds known and another bank as direct counterparty. The end-customer (ultimate beneficiary) can be a counterparty which is not required to report against NFRD/CSRD and therefore do not disclose taxonomy data (e. g. unlisted SME). According to the new wording of DDA, Annex V 1.2.1.2, the public bank must use the information of the counterparty which in fact - for the ultimate beneficiary - is not available or cannot be made available with a reasonable effort and especially not for every reference date/existing portfolio.

### The EABP recommends:

- That exposures to financial undertakings (DDA, Annex V 1.2.1.2) with use of proceeds known might be assessed using the overall green asset ratio of the direct counterparty in case the information for these specific exposures is not available.

### **2. Further guidance needed on lending to regional and local governments and Public Sector Entities (PSE)**

We welcome the clarification in the Commission Notice of 21 December 2023 that when financing or lending to regional or local governments, ‘known use of proceeds’ exposures should be included in the GAR of financial undertakings and ‘unknown use of proceeds’ exposures should be excluded from the GAR of financial undertakings. However, further guidance is needed on where to reflect the unknown use of proceeds exposures to regional and local governments in the reporting template for credit institutions (Annex VI to the DDA). We recommend to add these exposures to the list of “Assets not covered for GAR calculation”, pending the development of an appropriate methodology for the use of the EU Taxonomy in public spending.

Furthermore, guidance is needed on the treatment of other Public Sector Entities (PSE). Including these exposures in the denominator disadvantages all promotional and public banks in comparison to other banks with much smaller exposures to such entities. Therefore, we recommend to add these exposures to the list of “assets not covered for GAR calculation”.

### The EAPB recommends:

- As proposed by the Platform of Sustainable Finance in its report on data and usability of the EU Taxonomy in November 2022, to develop in the short term “*a framework, including a set of principles for the use of the Taxonomy in public spending, when it is intended to protect the environment, that determine for which types of expenditures these investments may deviate from it, why and how. (...)*” This would allow for an appropriate methodology for assessing the taxonomy alignment of general loans to local and regional governments as well as other PSE to enhance the role of promotional and public banks;
- Until the EC develops such a methodology, to include the exposures to PSE in the “*Assets not covered for GAR calculation*” rows of Annex VI to the DDA.

- In line with the Commission Notice, to include the unknown use of proceeds exposures to regional and local governments in the “*Assets not covered for GAR calculation*” rows of Annex VI to the DDA.

### 3. Public housing is not always financed by municipalities

The DDA assumes that financing public housing always takes place through municipality lending, which is incorrect. In Europe, public housing is provided by municipalities but also by specific social housing entities or municipality-controlled entities. The debt of these special social housing entities is either fully guaranteed by (local) governments or the special social housing entities are subsidized or owned by the central government. Due to such guarantee or subsidy, the exposures of credit institutions towards social housing associations are *de facto* sovereign exposures. A large portion of this financing is used to renovate or build houses which are taxonomy-aligned. However, since this financing is not provided directly to a municipality, promotional and public banks are not able to include these exposures in their GAR as specialised lending to local governments.

As long as the use of proceeds is known and these economic activities are taxonomy-aligned, these exposures should be eligible for the GAR of credit institutions.

#### The EAPB recommends:

- That public housing financing is eligible for the GAR of credit institutions if these exposures are fully guaranteed by a ‘sovereign’<sup>8</sup> guarantor, also when the financing is not provided to a municipality, but to a public/social housing association directly.

### 4. Promotional and public banks have a less granular overview of financed activities.

The primary goal of promotional and public banks is to pursue public policy objectives. Hence, promotional and public banks face the same difficulties as sovereigns when it comes to reviewing the taxonomy-alignment of the economic activities financed, as loan proceeds are often used for carrying out general public tasks. In the Netherlands for example, water authorities have an exclusive legal mandate to carry out certain climate adaptive economic activities. When taxonomy aligned economic activities are carried out by clients pursuant to a legal mandate, it should be sufficient to assess the taxonomy alignment of such legal mandate, instead of the economic activity funded. Such limited review should only apply to clients that have a legal mandate to carry out specific public tasks that are in line with the EU Taxonomy. In that respect, we are concerned with the requirement stated in the EC notice abovementioned that specifies that “*credit institutions should obtain adequate documentary evidence (...) by the respective producers of goods and service providers, ascertaining that undertakings producing goods and providing services that are purchased by retail clients and public authorities comply with the relevant TSC and with minimum safeguards (...)*”. Such provision clearly introduces additional burden for promotional and public banks with a category of counterparties not subject to non-financial disclosures. It is not in line with the flexibility that was originally proposed for sovereign green bond issuers<sup>9</sup>.

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<sup>8</sup> ‘sovereign’ means an entity referred to in Article 1(2), point (b) of Regulation (EU) 2017/1129: Member State, one of a Member State’s regional or local authorities, public international bodies of which one or more Member States are members, the European Central Bank or the central banks of the Member States.

<sup>9</sup> With regard to the taxonomy alignment of ‘sovereign’ green bonds, it has been argued that flexible review requirements should apply since sovereign issuers have a less granular overview of the activities funded with green bond proceeds, compared to financial and non-financial

## The EAPB recommends:

- That exposures to local governments and PSE with a legal mandate to carry out specific public tasks in line with the EU Taxonomy are taxonomy aligned “by default” and the review of taxonomy alignment could be limited to an assessment of the taxonomy alignment of such legal mandate.

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undertakings issuing green bonds. It is argued that where proceeds of those bonds are allocated to tax expenditures, transfer programmes or subsidies, it is not required to assess the taxonomy-alignment of each economic activity funded by such programmes. Instead, it should be sufficient to assess the taxonomy alignment of the terms and conditions of the programmes themselves. While the original European Commission’s proposal for the EU GBS proposed such lighter taxonomy alignment review requirements for sovereign issuers, the text of the provisional agreement on the EU GBS between the European Parliament and the Council does not contain such lighter review requirements for sovereign issuers.