Deutsche Bank position paper: standards / labels for sustainable finance

Introduction

- The EU Commission is looking at bringing more clarity around terms such as “sustainable”, “green”, “ESG”, etc. with regard to financial products.
- Deutsche Bank prefers using standards and labels (some defined by market participants, some by legal force) over widening the EU taxonomy to cover all economic activities (as suggested in Q83 of the consultation on the Renewed EU Sustainable Finance Strategy).
- Labels should be deployed where they provide useful clarity for consumers and where they can help sustainable financing products grow.

- The overall approach in this area should be based on the following principles:
    - Creation of a level playing field between all kinds of financial products, notably by including securities in the scope of the Disclosure Regulation. The discussion of product classification for the purposes of client preferences clearly shows the interdependence between the different parts of ESG regulation overall, and the problems created by the current limited scope.
    - Recognition of the central role of the ESG product nomenclature following from Articles 8 and 9 of the Disclosure Regulation. These provide “legal standards” for ESG products, and there should not be any doubt that compliance with these standards is sufficient to distribute financial products as “sustainable”, without the need for additional labels. The legal standards should form the basis in all respects, and there should not be any additional and diverging ESG product types (as proposed in the consultation on client preferences). Accordingly, there should also not be additional product-related guidance for advisors with the potential to create an additional and diverging layer of product classification.
    - There is a need for clarity about the additional merits and practical usefulness of labels in addition to the mentioned legal standards for ESG products – such clarity does not exist currently, and there is a tangible risk of confusing investors instead of promoting ESG objectives. Without such clarity, even for the Ecolabel the question of its additional value compared to the legal standards and of potentially higher negative effects in terms of confusing investors can be raised.
    - International compatibility of standards is important to make EU financial markets attractive for investors. Any rule or standard label should account for different regional taxonomies, potential non-availability of data on companies outside the EU (due to different disclosure requirements) and allow international investors to tap into sustainable financing options in Europe.

- In terms of priorities, there is already work underway to revise the Ecolabel Regulation and to promote the EU Green Bond Standard (GBS). The Commission should then prioritise standardisation of the conditions for products to receive incentivisation (through prudential incentives and/or official guarantee schemes) and to be included in a potential green securitisation framework, i.e. lending products.

Label for investment funds

- Under the conditions specified above (in particular, the legal precedence of the Art 8/9 assessment), the EU should use the Ecolabel Regulation to create a label for investment funds providing additional transparency. Under no circumstances, the label should serve as a precondition for classification of a product under Art 8/9. A label would increase transparency for issuers wishing to attract green investors and would establish minimum standards for a fund labelling itself as green/ESG.
- Such a label should spread into various sub-categories – i.e. ESG, green (aligned with EU Taxonomy) or impact investing.
- It could also serve as a classification scheme giving a "shades of green approach", e.g. various levels from dark green (100% taxonomy-compliant) to light green (20% compliant). This would move away from the current binary (green vs not green) approach.
- As the market needs to be able to adjust to changes associated with the EU Taxonomy and the Disclosure Regulation, such a label should not be introduced before 2021 at the earliest.
- If the EU Ecolabel was to be linked to the EU Taxonomy, asset managers would only have the full data from 2023, and the investment universe could be limited to EU companies only. More flexibility will be needed here.
- The investment universe should not be too restrictive to make sure there is a broad offer on the market. The first proposal for EU Ecolabel criteria was far too ambitious, giving very tight definitions and best-in-class conditions.

Green Bond Standard / sustainability-linked bonds

- The EU Green Bond Standard (GBS), as suggested by the TEG, is a useful addition to market-based solutions.
- Given the success of the ICMA Green / Social Bond Principles, we are in favour of the GBS remaining a legal guidance instrument, not to be part of a Regulation.
- As many international issuers and investors use EU financial markets to place Green Bonds (often also using the euro as currency), the EU should avoid intervening in a functioning and successful market.
- The EU GBS can be used for public issuers, and it can also entail incentives for issuers. We will respond in more detail to the targeted GBS consultation.

Corporate lending products

- Sustainability-linked loans are an important growth market with great potential to support corporate transformation. Therefore, standards should be supporting and not limiting the developing market. The EU should develop in-principle guidelines that are regularly updated, pushing the growth of the market in an orderly fashion.
- A global approach beyond the EU is necessary, taking into account that the Loan Market Association (LMA) jointly with APLMA and LSTA have issued guidance on sustainability-linked loans, and are well-placed to build up such a set of standards.
- When developing a standard, the EU Taxonomy should serve as one but not exclusive reference point. Given the bespoke character of ESG-linked structures, other guidance systems have to be considered, e.g. referring to broader SDG goals.

Retail lending products

- A broad standard / label for sustainable mortgages and loans (including wider social and environmental considerations would also be helpful.

- In particular, a green-mortgage definition will support an already growing market in the EU. This should focus on residential properties and on pre-defined, specific ESG topics.
- As necessary groundwork, the following elements should be part of a green-mortgage framework:
    - Align energy requirements for private mortgages with the Paris targets. Energy performance certificates (EPC) to be standardised across the EU;
    - EPC to be centrally available (no additional costs for customers for providing documents, bank's asset valuation to cross-check);
    - Residential mortgages are often taken out with a need for an additional loan for renovation (when buying older stock); a capital incentive for banks would help grow this component.
- For commercial real estate finance, existing certifications and industry standards can underpin a financial label.
- There should be public incentives to make it possible to offer such credit products at a discount.

Financial benchmarks

- The existing EU Climate Transition and Paris-aligned benchmarks should be complemented by an ESG benchmark.
- The definition of an ESG benchmark should follow established market standards. The market requires an ESG benchmark to overweight companies that are managing the business value risks from E&S factors better, i.e. companies in which ESG factors are considered material for business value and impact capital flow.