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EU Ecolabel criteria for Financial Products

*Preliminary report
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ABREVIATIONS AND ACRONYMS

AIF	Alternative Investment Funds
AIFMD	Alternative Investment Fund Managers Directive
BIC	Bank Identifier Code
CAB	Climate Awareness Bonds
CBI	Climate Bonds Initiative
CVA	Credit Valuation Adjustment
EC	European Commission
EEA	European Economic Area
EIB	European Investment Bank
ESMA	European Securities and Market Authority
ESRB	European Systemic Risk Board
ESG	Environment, Social, Governance
ETD	Exchange-Traded Derivatives
ETF	Exchange-Traded Funds
EURIBOR	Euro Interbank Offered Rate
FNG	Forum Nachhaltige Geldanlagen (Sustainable Investment Forum Germany)
GBP	Green Bond Principles
GBS	Green Bond Standard
GHG	Greenhouse Gas
HNWI	High Net Worth Individuals
ICMA	International Capital Markets Association
IDD	Insurance Distribution Directive
IDFC	International Development Finance Club
IF	Investment Fund
IPID	Insurance Product Information Documentation
IMD	Insurance Mediation Directive
JRC	Joint Research Centre
KID	Key Information Document
KPI	Key Performance Indicator
LIBOR	London Interbank Offered Rate
MDBs	Multilateral Development Banks
MiFID	Market In Financial Instrument Directive
MS	Member States
MTF	Multi-Lateral Trading Facility
NFID	Non-Financial Information Directive
OTC	Over-The-Counter
OTF	Operational Trading Facility
PIE	Public Interest Entity
PRIIPs	Packaged Retail Investment and Insurance Products
RM	Regulated Markets
RWA	Return Without Action
SME	Small and Medium Enterprises
SNAT	Supranational Authority
SPV	Special Purpose Vehicle
SRI	Socially Responsible Investment
UCITS	Undertakings For Collective Investment In Transferable Securities
TEEC	Transition Energétique Et Ecologique Pour Le Climat (Law on Energy and Ecological Transition for the Climate (France))
TMI	Total Market Index

EXECUTIVE SUMMARY

Policy context

In the Action Plan on Sustainable Finance (hereafter, the Action Plan) adopted in March 2018 in the context of the Capital Markets Union, the Commission proposed the creation of a voluntary EU-wide labelling scheme through the extension of the EU Ecolabel to financial products: Action 2.3 of the Action Plan stipulates that the Commission will "*explore the use of the EU Ecolabel framework for certain financial products, to be applied once the EU sustainability taxonomy is adopted.*"

This innovative solution would enable investors to directly channel their funds into sustainable investments. Following the preliminary positive feedback expressed on the subject by EU Ecolabelling Board members in February and November 2018, the Commission has started the work on developing criteria for extending the EU Ecolabel to selected green financial products.

The EU Ecolabel Regulation No 66/2010 permits the label to be awarded to "goods and services" (together "products"). It was concluded that financial products can be considered as services for distribution or use within the scope of the label. On this basis, the Commission initiated the policy-making process towards the development and implementation of EU Ecolabel criteria for PRIIPs ('packaged retail and insurance-based investment products') governed by Regulation (EU) No 1286/2014 and other financial products addressed to retail investors, which can be considered as services for distribution or use under the Administrative Agreement between the Directorate General Joint Research Centre (DG JRC) and Directorate General for the Environment (DG ENV) both of the European Commission on "EU Ecolabel for Financial Products".

The EU Ecolabel for Financial Products will allow retail investors concerned with the environmental impact of their investment to rely on a trusted and credible (third party verified) label when investing in green financial products and avoid "greenwashing". It will stimulate the comparability of investments, facilitate and enhance green investment, and support a stable and sustainable financial market at the European level, and beyond. Most importantly, it will contribute to the achievement of the EU climate and energy targets by 2030.

Process and methodology

This draft preliminary report is aimed at providing the background information for the development of EU Ecolabel criteria for retail financial products and "other" financial products. The study has been carried out by the Circular Economy and Industrial Leadership Unit (JRC-B5) and the Finance & Economy Unit (JRC-B1) of the DG JRC. The work is being developed for the DG ENV and in collaboration with the Directorate General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA) of the European Commission.

This preliminary report addresses the requirements of the Ecolabel Regulation for technical evidence to inform criteria development presenting an analysis of the scope of financial products, definitions and description of the legal framework, an overview of existing national and/or regional financial labels or schemes, a market analysis and providing information on the definitions of "green" or environmentally sustainable financial products. It also provides background information on the relevance and application of the EU Taxonomy, investment portfolio greenness, environmental exclusions, social and ethical exclusions, reporting requirements or assessment systems. This preliminary report therefore supports the criteria proposals which are to be made in the first Technical Report. The latter will provide the background information required for the first Ad-hoc Working Group (AHWG) meeting, scheduled to take place in April 2019.

An important part of the process for developing EU Ecolabel criteria is the involvement of stakeholders through surveys and questionnaires, publication of and consultation on draft technical reports and working group meetings. This preliminary report also includes the inputs from an extensive online stakeholder survey and bilateral interviews with label and scheme operators and will be closed after the first AHWG meeting.

Main findings

The EU Ecolabel criteria for retailed financial products aims at facilitating the identification and comparison among retail investments towards green investments and supporting a sustainable financial market. As institutional investors are more sophisticated and can request specific and granular information, thus a label might not be the best tool for their needs. However, the EU Ecolabel would be particular helpful for retail investors that are typically interested in investing in products covered by the Regulation on Packaged Retail Investment and Insurance-based Products (PRIIPs) or simpler savings products.

The number of products that could potentially be included in the scope of the EU Ecolabel is very large. Therefore, based on the information resulting from the market analysis, the revision of the existing national labels and the stakeholders' questionnaire and interviews, it is suggested that the EU Ecolabel criteria for retailed financial product should be developed for investment funds and insurance based products with an investment component for the first set of financial products¹.

An assessment of existing national and regional labels for green financial products indicates that they differ considerably in their interpretations of "green investments" or "sustainable investments" due to the application of different methodologies and taxonomies (with varying degrees of detail and definitions). The results suggest that the EU Ecolabel criteria could rely on the "EU Taxonomy" proposed in the Action Plan. Therefore, the assets underlying the retailed financial products should be evaluated regarding their link to green or environmentally sustainable economic activities as established under the EU Taxonomy.

In addition, the background information collected suggests the need for the inclusion of social and ethical aspects into the EU Ecolabel criteria and the need of a high level of transparency when reporting and verifying the proposed EU Ecolabel requirements.

Finally, some issues related to the operational and legal implications for a new product will need to be considered.

¹ Although a broad scope is necessary, a the first set of financial products that will be covered by the EU Ecolabel criteria will result from the market analysis, the stakeholder online questionnaire survey and bilateral interviews. It might be necessary to enlarge or restructure the product scope at a later stage to allow retail investors with a preference for other environmentally sustainable financial products to choose among several types of financial products.

1. INTRODUCTION

Governments from around the world chose a more sustainable path for our planet and our economy by adopting the United Nations 2030 Agenda for Sustainable Development and the 2015 Paris Agreement on climate change. Sustainability has long been at the heart of the European project and the EU is fully committed to reaching the EU 2030 climate and energy targets and to mainstream sustainable development into EU policies. Achieving EU sustainability goals requires major investments. A substantial part of these financial flows will have to come from the private sector and this requires redirecting private capital flows towards more sustainable investments as well as comprehensively rethinking the European financial framework.

In this context, in December 2016, the Commission established a High-Level Expert Group to develop an overarching and comprehensive EU strategy on sustainable finance. This group published its final report in January 2018. As a follow-up, on 7 March 2018, the Commission published an Action Plan on Financing Sustainable Growth (hereafter, the Action Plan)². The Action Plan puts forward ten actions whose main objectives are

- 1) reorienting capital flows towards sustainable investments to achieve sustainable and inclusive growth;
- 2) managing financial risks stemming from climate change, resource depletion, environmental degradation and social issues; and
- 3) fostering transparency and long-termism in financial and economic activity.

To achieve these objectives, the Action Plan includes a series of key actions covering all actors in the financial system such as:

- 1) To establish a common language for sustainable finance through the EU taxonomy.

There is a current patchwork of classification systems for green/sustainable activities across the EU. This creates uncertainty for investors who want to invest with sustainability objectives in mind. An EU sustainable taxonomy would mean a uniform and harmonised classification system that is essential to determine which activities can be regarded as sustainable across the EU. Further information can be found in section 4.

- 2) To create standards and labels for green financial products. An EU ecolabel for green financial products will help to guide investors and flag financial products in line with the transition towards a sustainable economy

The Action Plan proposes to widen the scope of the EU Ecolabel to financial products because consumers are increasingly interested in investing in products with a positive sustainability impact. However, the lack of well-defined standards makes it more difficult for investors to channel their funds into financial products and that invest in sustainable assets. Labelling schemes for sustainable financial products would be very useful for non-professional investors to easily identify investments that comply with green or low-carbon criteria and will contribute to raise awareness about these products.

As follow-up to the Action Plan, the Commission adopted a package of legislative proposals in May 2018 ("the May 2018 Package") a proposal for a Regulation on the establishment of a framework to facilitate sustainable investment³ (hereafter "the Taxonomy Proposal").

The Commission sees merit in the use of the EU Ecolabel Regulation 66/2010⁴ (hereafter, the Ecolabel Regulation) to create a voluntary EU-wide labelling scheme. Criteria would have to be identified for specific financial products offered to retail investors (such as Packaged Retail Investment and Insurance Products). Such a labelling scheme will be applied to certain financial products once the EU Taxonomy is adopted.

² European Commission. 2018. Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Economic and Social Committee and the Committee of the Regions Action Plan: Financing Sustainable Growth. Available from: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097>

³ Proposal for a Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment of 24 May 2018 (COM(2018) 353 final 2018/0178).

⁴ Regulation (EC) No 66/2010 of the European Parliament and of the Council of 25 November 2009 on the EU Ecolabel (OJ L 27, 30.1.2010, pp. 1-19. Available from: <http://data.europa.eu/eli/reg/2010/66/oj>

The EU Ecolabel promotes the production and consumption of products with a reduced environmental impact throughout their life cycle and it is awarded to the best environmentally performing products available in the market. The EU Ecolabel Regulation addresses the main issues relating to a labelling scheme, namely the general principles and rules of the voluntary EU Ecolabel scheme, the procedures for developing/revising criteria, the mechanisms for awarding the ecolabel, the supervision mechanism as well as the set-up of promotional activities. EU Ecolabel criteria for specific product groups are developed in line with the principles and methodology contained in the EU Ecolabel Regulation. In particular, the criteria are defined based on the environmental information derived from Life Cycle Assessment (LCA) and product oriented environmental performance assessment studies. Different environmental, safety and functional aspects are also considered.

The EU Ecolabel is part of a broader EU Action Plan on Sustainable Consumption and Production⁵ and Sustainable Industrial Policy, which was adopted by the European Commission on 16 July 2008⁶ and links the EU Ecolabel to other EU policies such as green public procurement (GPP) and the ecodesign of energy-related products. It is also part of the EU Action Plan for the Circular Economy.

According to the Ecolabel Regulation, the label may be awarded to "goods and services" (together "products") which are supplied for distribution, consumption or use on the Community market whether in return for payment or free of charge. A preliminary analysis concluded that financial products would fall within the scope of the Ecolabel Regulation where they can be considered *services* for distribution or use.

The European Commission launched the development of the EU Ecolabel criteria for financial products at the end of 2018, which will be in line with both Action Plans: the Action Plan on Sustainable Consumption and Production and the Action Plan on Sustainable Finance. The process is coordinated by DG ENV in collaboration with DG FISMA. The DG JRC is providing the environmental and techno-economic analysis, as well as scientific support to the political process. The development of the criteria follows the methodology outlined in Annex I of the EU Ecolabel Regulation, being included in this preliminary report, the reasoning for choice and scope of the product group, an analysis of other environmental label's criteria, the current laws and ongoing legislative initiatives related to financial products, the intra-community market data for the sector and the reference data and information collected and used for issuing the report. Additionally, this report also includes inputs from stakeholders and experts in order to discuss on key issues and to develop wide consensus.

This report will be provided as working document prior to the first ad-hoc working group (AHWG) meeting to be held in April 2019. This working group is composed of experts from Member States, industry, NGOs and academia that have registered as stakeholders of the study and will support JRC work along this process. The preliminary report will be closed after the 1st AHWG meeting but will still be available on the project website at: http://susproc.jrc.ec.europa.eu/Financial_products/index.html

⁵ http://ec.europa.eu/environment/eussd/escp_en.htm

⁶ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the Sustainable Consumption and Production and Sustainable Industrial Policy, Action Plan {SEC(2008) 2110}{SEC(2008) 2111}Available at <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2008:0397:FIN:EN:PDF>

2. LEGAL REVIEW, SCOPE AND DEFINITION

This chapter provides a brief overview of financial products held by retail investors, legislation on instruments held by European retail investors and a review of existing labels and schemes operating both in the EU and internationally. Further supporting market data on the composition of financial assets held by retail investors can be found in Chapter 3.

A retail investor is a retail client who is not a professional client, or a customer not qualified as a professional client, i.e. a client who possesses the experience, knowledge and expertise to make its own investment decisions and properly assess the incurred risks.⁷ Since a retail investor has a limited capacity for information processing compared to an institutional investor, a EU Ecolabel on financial assets could be useful for this type of investor.

2.1 Overview of financial assets held by retail investors

This section provides a brief introduction to the wealth allocation of European retail investors across several investment products.

Retail clients are mostly households. EU-28 households, which are the major contributors to the net financial wealth of the EUR area, own about EUR 34 tn of cumulated assets, and their financial liabilities are equal to 30% of their financial assets. Across the EU-28, households' financial assets mainly comprise the following⁸:

- **Currency and deposits**, including notes and coins issued by monetary authorities, and deposits (i.e., transferable deposits and others), both in national currency and in foreign currencies.
- **Equities**, including listed, unlisted shares and other equities.
- **Investment fund shares**, i.e. shares of collective investments.
- **Life insurance and annuity entitlements**, including pure protection life insurances, products linked to investment funds, as well as voluntary pensions (not linked to employment).
- **Non-life insurance** technical reserves, i.e. assets against outstanding risks in respect of non-life insurance policies.
- **Pensions funds and standardized guarantees**.
- **Debt securities**, including both plain debt securities and convertible and exchangeable bonds (i.e. structured products).
- **Loans**, including loans for consumption, for house purchases and other loans.
- **Financial derivatives** and employee stock options, including e.g., options, forwards, swaps, and credit derivatives.
- **Other accounts receivable/payable** (i.e., trade credits and advances).

The composition of households financial assets is rather stable over time. Approximately 70% are composed by currency and deposits, pension funds, and (life and non-life) insurance products. More details on the breakdown of household holdings can be found in section 3.1.

2.2 Financial market legislation

For financial products offered to retail investors, a number of related directives and regulations exist and need to be considered. A short description of each of these pieces of legislation is provided below.

⁷ See Regulation n. 1286/2014 of PRIIPs Regulation, Article 4(6) for the definition of "retail investor"; see, also, Directive 2014/65/EU, Article 4 (1), point (11), Directive 2014/65/EU, Article 4(1), point (10) and Annex II, and Directive 2011/61/EU, Article (4)(1)(aj).

⁸ Definition of the categories and sub-categories of financial assets are provided by European System of Accounts (ESA 2010, Chapter 5).

Regulation (EU) No 1286/2014 – Regulation of package retail investment and insurance products

Packaged retail investment and insurance products⁹ (PRIIPs) are investment products that banks typically offer to retail investors. PRIIPs includes:

- i. packaged retail investment product (PRIIP), i.e. investment, including instruments issued by special purpose vehicles, where the amount repayable to the retail investor is subject to market fluctuations;
- ii. insurance-based investment product, i.e. insurance product for which its maturity or surrender value is exposed to market fluctuations.

The PRIIPs Regulation shall not apply to the following products¹⁰:

- a) non-life insurance products as listed in Annex I to Directive 2009/138/EC;
- b) life insurance contracts where the benefits under the contract are payable only on death or in respect of incapacity due to injury, sickness or infirmity;
- c) deposits other than structured deposits as defined in point (43) of Article 4(1) of Directive 2014/65/EU;
- d) securities as referred to in points (b) to (g), (i) and (j) of Article 1(2) of Directive 2003/71/EC;
- e) pension products which, under national law, are recognised as having the primary purpose of providing the investor with an income in retirement and which entitle the investor to certain benefits;
- f) officially recognised occupational pension schemes within the scope of Directive 2003/41/EC of the European Parliament and of the Council or Directive 2009/138/EC;
- g) individual pension products for which a financial contribution from the employer is required by national law and where the employer or the employee has no choice as to the pension product or provider.

The PRIIP category is broad and intended to cover all financial products sold on the retail market that have exposure to underlying assets (stocks, bonds, etc.), provide a return over time and have an element of risk.

The EU has adopted a regulation on PRIIPs, which obliges those who produce or sell these investment products to provide investors with key information documents (KIDs). KIDs should include the following information:

- the name of the product and the identity of the producer;
- the types of investors for whom it is intended;
- the risk and reward profile of the product, which includes a summary risk indicator, the possible maximum loss of invested capital and appropriate performance scenarios of the product;
- the costs investors have to bear when investing in the product;
- information about how and to whom an investor can make a complaint in case there is a problem with the product or the person producing, advising on or selling the product.

The main goal of the PRIIPs Regulation is to increase transparency in the market. The regulation is applicable from 1st January 2018

Directive 2011/61/EU on alternative investment funds managers

This directive establishes a legal framework for the authorisation, supervision and oversight of managers of a range of alternative investment funds (AIFM), including hedge funds and private equity.

This directive sets up the possibility that the AIFMs can ‘passport’ their services in different EU countries on the basis of a single authorization. Once an AIFM is authorised in one EU country and complies with the rules of the directive, the AIFM is entitled to manage or market funds to professional investors throughout the EU. AIFMs are required to assure the competent authority of the robustness of their internal arrangements with respect to risk management. This includes a requirement to disclose, on a regular basis, the main markets and instruments in which they trade, their principal exposures and their concentration of risk.

⁹ See Regulation n. 1286/2014 of PRIIPs Regulation, Article 4(1)-(3).

¹⁰ See Regulation n. 1286/2014 of PRIIPs Regulation, Article 2(2).

Additionally, AIFMs are required to provide a clear description of their investment policy, including descriptions of the types of assets and the use of leverage. An annual report for each financial year has to be made available to investors on request.

The passport may at a later point in time be extended to non-EU AIFMs and to the marketing of non-EU funds, managed by either EU and non-EU AIFMs. EU countries may choose not to apply the directive to smaller AIFMs (i.e. <€100 million if they use leverage and with assets below €500 million if they do not). Smaller funds are however subject to minimum registration and reporting requirements.

Directive 2009/65/EC consolidated and Directive 2014/91/EU on undertakings for collective investment in transferable securities (UCITS)

The main aims of the directive are to:

- offer investors a wider choice of products at lower cost through a more efficient UCITS market in the EU, better investor information and more efficient funds supervision and
- keep the EU's investment sector competitive by adjusting the rules to market developments.

In particular, this directive lays down rules on:

- investor information via a standardised summary information document to make it easier for the consumer to understand the product
- a genuine EU passport for UCITS management companies which will allow a management company located in one EU country to manage funds in other EU countries
- marketing of UCITS in other countries, e.g. by simplifying administrative procedures
- mergers of UCITS in other countries
- stronger supervision of UCITS and of the companies that manage them, e.g. through enhanced cooperation between national financial services supervisors.

Directive 2009/65 was amended by Directive 2014/91/EU (UCITS V) which introduced new rules on UCITS depositaries (the asset-keeping entity), e.g. the entities eligible to assume this role, their tasks, delegation arrangements and the liability of depositaries, remuneration and sanctions.

Directive 2009/138/EU on the taking-up and pursuit of the business of Insurance and Reinsurance

This directive acts as a prudential framework for insurance firms and replaces several rules in the areas of life insurance, non-life insurance and reinsurance. It introduces requirements tailored to the specific risks which each insurer bears. They promote transparency, comparability and competitiveness in the insurance sector.

The Solvency II directive (amended by the Omnibus 2 directive), covers 3 main areas, related to capital requirements, risk management and supervisory rules. The directive requires insurance companies to hold capital in relation to their risk profiles to guarantee that they have enough financial resources to withstand financial difficulties. Insurance companies have to put in place an adequate and transparent governance system and conduct their own risk and solvency assessment on a regular basis. Finally, the directive enables supervisors to review and evaluate whether insurance companies comply with the rules and requires these companies to report to supervisory authorities and disclose information publicly.

Under the Solvency II directive the European Commission can adopt delegated and implementing acts, including technical standards and information for the calculation of technical provisions and basic own funds.

Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading

This directive seeks to improve the quality of information provided to investors by companies wanting to attract external investors to raise capital in the EU to finance their growth. It aims to ensure that adequate and equivalent disclosure standards are in place in all EU countries in the event that the securities are offered to all

EU investors. It lays down rules on the prospectus¹¹, a document that EU companies are required to publish when they issue securities to attract investments. By virtue of these rules, once a prospectus has been approved in one EU country, it is valid throughout the EU (single passport for the issuers).

Issuers are obliged to publish a prospectus on offers of securities, unless the offer:

- is addressed solely to qualified (professional) investors; and/or
- is addressed to fewer than 150 persons, other than qualified investors (e.g. individuals), per EU country; and/or
- is addressed to investors who acquire these securities for a total consideration of at least €100 000 per investor; and/or
- covers securities (shares or bonds) with a denomination per unit of at least €100 000;
- has a total value in the Union of less than €100 000.

The prospectus must contain a summary document, produced in a standard format, providing key information on:

- the essential characteristics of the issuer of the securities (e.g. the issuing company), of any guarantors (e.g. the bank) and of the securities offered or admitted to trading on a regulated market, as well as the main risks associated with them;
- the general terms of the offer, notably an estimate of the expenses invoiced by the issuer to the investor.

The issuer is civilly liable vis-à-vis the information provided in the prospectus. This information must be in accordance with the facts and contain no omissions. Once the prospectus has been approved by the competent authority of the EU country of origin, it must be published (in a widely-circulated national newspaper or on the website of the issuer, for example) and a copy must be sent to the European Securities and Markets Authority (ESMA). A prospectus remains valid for up to 12 months following its approval, provided it is updated and supplemented with the required items.

Directive (EU) 2016/97 on insurance distribution

Under the new directive on insurance distribution¹², consumers and retail investors buying insurance products or insurance-based investment products will benefit from:

- greater transparency of insurance distributors in regard to the price and the costs of their products, so that it is clear to consumers what they are paying for;
- better and more comprehensible information, so that consumers can take more informed decisions, with a simple, standardised Insurance Product Information Document (IPID) for non-life insurance products;
- where insurance products are offered in a package with another good or service, for example when a new car is sold at a bargain price together with motor insurance, consumers will have the choice to buy the main good or service without the insurance policy;
- rules on transparency and business conduct to prevent consumers from buying products that do not meet their needs.

These rules now also apply when a product is bought directly from an insurance company, and not only (as in the past) when products are bought via intermediaries such as agents or brokers. There are stronger safeguards for the sale of life insurance products with investment elements, such as unit-linked life insurance contracts. Insurance distributors selling such products have to make sure that the product is suitable with regard to the customer's financial situation, investment objectives and experience in the investment field. Insurance distributors will benefit from fair competition on a level playing field and an improved legal framework for cross-border business.

Directive 2014/95/EU on disclosure of non-financial information

¹¹ Prospectus: a disclosure document that contains information enabling investors to make investment decisions in full knowledge of the facts

¹² Insurance distribution: to sell, propose to sell, advise on or carry out other work before concluding an insurance contract including dealing with claims after an insurance event

EU law requires large companies to disclose certain information on the way they operate and manage social and environmental challenges. This helps investors, consumers, policy makers and other stakeholders to evaluate the non-financial performance of large companies and encourages these companies to develop a responsible approach to business. Directive 2014/95/EU lays down the rules on disclosure of non-financial and diversity information by large companies. This directive amends the accounting directive 2013/34/EU. Companies are required to include non-financial statements in their annual reports from 2018 onwards.

EU rules on non-financial reporting only apply to large public-interest companies with more than 500 employees. This covers approximately 6,000 large companies and groups across the EU, including listed companies, banks, insurance companies and other companies designated by national authorities as public-interest entities.

Under Directive 2014/95/EU, large companies have to publish reports on the policies they implement in relation to environmental protection, social responsibility and treatment of employees, respect for human rights, anti-corruption and bribery and diversity on company boards (in terms of age, gender, educational and professional background)

Directive 2014/95/EU gives companies significant flexibility to disclose relevant information in the way they consider most useful. Companies may use international, European or national guidelines to produce their statements, for instance, they can rely on the UN Global Compact, the OECD guidelines for multinational enterprises or ISO 26000.

2.3 Review of existing Ecolabels and Schemes

2.3.1 Introduction

The following sections provide an overview of the existing ecolabels and schemes available in the market for financial products. It details their scope, criteria for awarding of the label or scheme and verification procedures. Exclusion and evaluation criteria are also presented and explained. Additionally, the sections provide the rationale for how the national and regional labels are awarded and describe what are the post-award requirements in terms of reporting and examine compliance are. Following a description of the individual schemes, a comparison of the labels is presented in Table 1.

National and private financial ecolabel schemes adapt the broader Social Responsible Investment (SRI) framework, which considers both environmental and social sustainability while aiming at financial return and encompassing transparency and reporting practices. Nevertheless, if a scheme focuses more on environmental sustainability by either including more environmental requirements or by weighting more heavily the importance of environmental aspects, then this scheme is rather characterised as environmentally sustainable or green. One should note that a green scheme could also include social aspects in the criteria.

2.3.2 The Nordic Ecolabel (Investment Funds)

Context: The Nordic Swan Ecolabel (NS Ecolabel)¹³ provides consumers with guidance about investment funds that have taken on a role and function in influencing companies and capital markets to act in a more sustainable way.

The label sets out exclusion, inclusion and transparency criteria, developed through a stakeholder consultation process, and endorses investments in (i) companies with a strong sustainable rating and (ii) those in transition to more sustainable business activities.

What the Nordic Ecolabelling intends to achieve with ecolabelled funds is to:

- Reduce investments in non-sustainable companies
- Increase investments in companies with good sustainability performance

¹³ <https://www.svanen.se/en/Newsarchive/2017/10/The-worlds-first-Nordic-Swan-Ecolabelled-funds/>

- Influence and encourage companies to show greater accountability concerning the UN's agenda 2030 through active ownership
- Increase visibility and engagement in sustainability issues from the financial industry through transparency and dialogue with investors
- Stimulate increased traceability between the investor's capital and concrete investments in sustainable projects.

Scope: The NS Ecolabel can be awarded to all funds, provided that they comply with UCITS regulation and are registered for distribution in one or more of the Nordic countries. Additionally, no more than 50% of their assets should be based on non-corporate credits, such as governmental bonds. From February 2018, qualified non-corporate green bonds were added to the product group definition. The applicant needs to prove compliance with exclusion criteria and fulfil inclusion, transparency and ownership and quality requirements as defined in the evaluation framework.

Exclusions: The scheme defines exclusion criteria which exclude, among others, the following economic activities: extracting and refining fossil fuels, generating power, controversial weapons, conventional weapons, GMO crops, no compliance with international norms and conventions, governmental bonds – sanctions and governmental bonds – corruption ,and in the case a holding does not meet the obligatory exclusions. Additionally, the scheme sets exclusion thresholds for specific economic sectors or activities beyond which an investment cannot be awarded the NS Ecolabel. Exclusion criteria are also set as regards indirect holdings requiring their percentage to remain below 5% of the investments. There is an "*indicative but shifting taxonomy*" which indicates that funds may include companies, which might not be considered as highly sustainable, but could contribute to the transition to sustainability at some point in the future.

Criteria: Other criteria categories include active ownership, reporting, transparency, quality and regulatory requirements. Additionally, the fund must have an active management system, perform an internal annual check for compliance, take into account the laws and regulations in the Nordic region, release sustainability reports, etc.

The label encompasses inclusion criteria, which need to be fulfilled and reported in an Environmental Social Governance (ESG) analysis report. This can be carried out by an external provider and has to be updated on an annual basis. The analysis can also be performed internally, however in that case, a corporate responsibility report is also prerequisite, especially for equities and corporate bonds. The ESG analysis should cover at least 90% of the direct holdings of the fund. The environmental performance of the holdings and the percentage of investment in a particular holding is part of the evaluation. In line with the evaluation, the application can achieve a maximum of 16 points indicating an outstanding performance, though, it needs six points to be eligible for the ecolabel. As regards bond funds, the minimum amount of points for the NS Ecolabel to be awarded is five. The label does not cover financial risks or returns.

Taxonomy: The NS Ecolabel does not explicitly refer to the Green Bond Principles (GBP)¹⁴ in its documentation. Nevertheless, in the section on inclusion criteria, it provides a list of business areas and activities that may be included in a fund with an environmental objective. Some of these (renewable energy such as producer/service/maintenance of windmills, solar cells, biogas production etc.) are aligned with the project categories of ICMA's GBP. An extensive overview of the existing taxonomies including the broad categories of eligibility for green projects covered by the GBP is available in Chapter 4..

Verification: The scheme validates the performance of the fund during the application. Next to the verification ESG annual reporting is required by the scheme. Additionally, the Competent Body for the Nordic Ecolabel may decide to do a random check (including a possible on-site visit), to verify whether a fund continues to fulfil the label requirements during the licence period. The licence validity is subject to meeting the criteria requirements and the licence can be revoked if the fund cannot adequately document compliance. The NS Ecolabel authorities can also gather random samples from the fund's website, and analyse them against exclusion criteria. No compliance with exclusion requirements can lead to a more thorough check in which case the derived costs must be met by the applicant.

¹⁴ <https://www.icmagroup.org/green-social-and-sustainability-bonds/green-bond-principles-gbp/>

2.3.3 The Austrian Ecolabel (Sustainable financial products)

Context: The Austrian Ecolabel belongs to the Socially Responsible Investment (SRI)-Fund labels. The Austrian ecolabel evaluates whether an investment fund qualifies for an award in the following sectors: 1) climate, 2) water, and 3) renewable energy and environmental technologies. Two types of investment funds qualify:

- Thematic funds with focus on specific industries (e.g. clean energy)
- Investment funds with a socially responsible investment strategy

The Austrian Ecolabel for financial products consists of three main pillars.

- Selection criteria that allow for identifying the positive environmental and social performance of companies or issuers of the financial products.
- Criteria related to the qualification and integrity of the organisation which performs auditing and criteria about quality of auditing and documentation of the process.
- Criteria related to transparency. Transparency criteria focus on information about sustainability (including environmental and social aspects) according to European sustainable and responsible investment forum (EUROSIF)¹⁵. They aim to provide customers with a clear vision of the investment strategy of the financial product. The investment quality of the financial product is assessed by means of the self –regulation of the Austrian investment funds branch ("Selbstregulierung der Österreichischen Investmentfondsbranche")

Scope: The scope of the label covers financial products whose investment strategy is based on sustainable, ethical, social and environmental measures. The fund can entail investments made by companies, public entities or real estate actors. Funds of funds and financial products based on sustainable indexes are also included under the scope of the scheme. The scheme requires the fund to be a diversified open-ended fund and the funds can also include bond funds.

The financial products that apply for the Austrian Ecolabel are fall in one of the following categories:

- Sustainable financial products – ethics and environment (NF). They are financial products that invest in assets which in comparison to other assets of the same industry or sector show a better environmental performance (Best in Class principle applies). The exclusion of certain economic sectors, industries and activities ensures the value of those products.
- Sustainable financial products related to the topics: climate, water, renewable energy and environmental technology (TF). They are financial products that invest in activities with an environmental performance above the average, or in companies which produce or handle products to reduce environmental impacts
- Sustainable financial products for real estate. They invest in real estate activities with an environmental and social performance above the average according to the best-in-class principle.

Exclusions: The Austrian Ecolabel does not permit investments in some specific economic sectors or projects including nuclear power, coal, genetic engineering, natural gas or mineral oil extracted via fracking or from tar sands, and weapons and armaments if the percentage investment is more than 5% of the fund's total. However, percentages in different exclusion sectors do not sum-up. The scheme does not stipulate the use of a specific taxonomy and places diverse criteria depending on the sector invested with the intention to cover as broadly as possible the relevance of the different activities. The fund is eligible for the Austrian Ecolabel if it reaches a predefined percentage of the maximum possible score. The latter is subject to the number of criteria and evaluation procedure.

Criteria: The scheme defines inclusion criteria in three areas as outlined in the scope. Beginning from the company-related criteria, environmental aspects and corporate management issues are set. The criteria refer to biodiversity, land protection, climate mitigation, air and water protection, waste management and resource efficiency. Management related criteria concern employees, suppliers, investments and social responsibility aspects. The scheme also sets country relevant criteria in the areas environment, society and economy similar to those at corporate level. The same applies for real estate-related funds. The scheme evaluates the application using the best in class approach and awards the label if the applicant achieves more than 65% of the total score.

¹⁵European Sustainable and Responsible Investment Forum. <http://www.eurosif.org/>

Verification: The scheme adopts a standard protocol concerning the verification process, which examines compliance with the auditing procedure. Specialised auditors who have been examined and registered by the scheme carry out monitoring and compliance assessment. The license is valid for four years but annual updates are required. These are to be conducted by an external auditor. The monitoring procedure examines possible changes in the investment strategy. If the latter applies, the fund has to inform the scheme on how extensive these changes are and if the fund still complies with the criteria. The annual update is the most important monitoring step. The scheme strongly encourages internal audits and demands an established internal monitoring procedure.

2.3.4 Energy and Ecological Transition for the Climate Label

Context: The “Energy and Ecological Transition for Climate” (TEEC)¹⁶ is a recent label published in March 2016 in France. Its primary objective is to encourage the creation of “green” funds by awarding certification to investments, to steer savings towards energy and ecological transition and to help address climate change. It is the outcome of one of the public policies called for by Article 2 of Energy Transition for Green Growth Law of August 2015. This label aims at drawing attention to existing investment funds or at giving rise to the creation of such funds.

Types of criteria: The label sets out criteria for the labelling of candidate funds. For each criterion and sub-criterion there are qualitative or quantitative indicators, making it possible to evaluate whether the criterion has been met. The criteria focus on the following concepts:

- a) Eligibility criteria in terms of scope
- b) Pillars – label criteria
- c) Definition of the activities falling within the scope of the energy and ecological transition and the fight against climate change
- d) Strict and partial exclusions
- e) Requirements for the use of derivative instruments within the framework of “energy and ecological transition for the climate” management

Scope / financial criteria: Regarding the scope of the TEEC label, the first set of criteria is related to the eligibility of the financial products, there are three main criteria. The first one “*eligible funds*” considers products that can be awarded with the label which are:

- funds failing under UCITS Directive¹⁷:
- AIFs having no major leverage effect as defined in the AIFM Directive¹⁸
- in formation private equity and infrastructure AIFs

The second criterion called “*Funds’ assets*” specifies the origin of the financial instrument. According to this criterion fund assets that are “*comprised of securities issued by issuers or claim on issuers of which at least 75% have their registered head office in the European Union, with the exception of bond funds to which the geographical constraint does not apply*” can be eligible for this scheme.

Additionally, this criterion mentions “*debt securities issued by States, local and regional authorities and government or international public agencies can be included in eligible funds*” if they fulfil the requirements of the previous criteria.

Environmental criteria / criteria related to environmental performance: Finally, the third criterion includes special cases and criteria that are to be fulfilled. These special cases include the following:

- a) Funds of funds that must be invested 90% at minimum in funds having the “*energy and ecological transition for the climate (EETC)*” label. The remaining 10% should not be invested in non-label funds but in transferable securities or money market instruments as defined in Article 50(2)(a) of UCITS Directive
- b) Feeder funds that are eligible for the label given that the master fund is labelled.

¹⁶ https://www.ecologique-solidaire.gouv.fr/sites/default/files/Label_TEEC_Criteria%20Guidelines.pdf

¹⁷ Directive 2009/65/EC of the European Parliament and of the Council of the 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS).

¹⁸ Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 Text with EEA relevance

Regarding the requirements to be fulfilled by the financial products, there are mainly three groups of criteria. The first one refers to objectives and methodologies for the selection of assets contributing to the energy and ecological transition; the second one refers to ESG criteria reflexion in the portfolio, and the third one to the positive impacts on energy and ecological transition.

Exclusions: The TEEC label completely excludes investments in business activities that are active in fossil fuels exploration, production and exploitation and nuclear sector activities. Additionally, it partially excludes service companies, and those involved in distribution and/or transportation and the production of equipment if 33% or more of their turnover comes from clients from strictly excluded sectors. They are also partially excluded companies that are making 33% or more of their turnover from storage and landfill centres without GHG capture, incineration without energy recovery, energy efficiency for non-renewable energy sources and logging, unless managed in sustainable fashion and peatland agriculture.

Taxonomy: The TEEC label applies a taxonomy of "green activities" which is an adaptation of the Climate Bond Initiative (CBI)¹⁹ taxonomy (See Chapter 4). Activities defined within the scope of the energy and ecological transition are those directly or indirectly contributing to "green growth". The taxonomy lists eight eligible sectors. These include energy, buildings, industry, waste (including pollution control and sequestration), transport, information technology and communication, agriculture and forestry, and adaptation.

Further "areas" (e.g. solar energy), "specific categories and activities" (e.g. "PV solar electricity") and descriptions are provided for each of the broad sectors provided above.

The TEEC taxonomy reflects similar sectors to those available in the CBI taxonomy yet with some differences. For example, activities such as fuel-efficient vehicles and broadband which are listed in the taxonomy of the CBI (see Chapter 4) are omitted. Moreover, the TEEC taxonomy includes a "services" category within its "energy", "buildings" and "industry" sectors. The TEEC has strict and partial exclusions, which apply to certain types of business activities.

Reporting: The TEEC label sets out additional requirements on transparency in financial management. Derivatives must be limited to techniques enabling the sufficient management of the securities portfolio and must not impair the fund's investment policy. The fund should also calculate the turnover rate of its portfolio and its contribution to energy and ecological transition. Reporting is one of the aspects requested within the transparency criteria, and it is a requirement that reports should include at least one measurable result among the environmental aspects of climate change, water, natural resources or biodiversity by setting appropriate indicators.

Verification: The auditing processes can be performed internally and also by external verifiers. As regards the external verifiers, there are currently three institutions that can act so in France. The scheme can also perform checks to examine the degree of implementation of the fund strategy and goals. The scheme anticipates a list of documents to be filled and submitted by the applicant which includes information about the fund, the KID, marketing material, reporting and management report, the itemised portfolio statement, a summary document addressing information as requested in the scheme's criteria and the technical documents about derivative instruments and rotation rate. TEEC label is allowed to examine the implementation of the funds goals, as described in the application, 4-5 years after the labelling.

2.3.5 Luxflag Climate Finance Label

Context: The primary objective of the Luxflag Climate Finance Ecolabel is to reassure investors that funds invest in sustainable activities in the majority of their investment portfolio. Luxflag also targets sustainable development goals as defined by the United Nations SDG strategy²⁰. Therefore, it sets eligibility criteria that consist of exclusion, inclusion, transparency and monitoring requirements.

Scope: The investment fund should demonstrate an investment portfolio in which 75% of the total assets are related, with certain and clear link, to mitigation and/or adaptation of climate change or cross-cutting activities while it defines which activities are classified as climate mitigation/adaptation related. Furthermore, the fund should prove that 25% of the total assets are in the form of cash, liquid assets or other investments. Other

¹⁹ <https://www.climatebonds.net/2018/09/launch-major-update-climate-bonds-taxonomy-expansion-international-guide-climate-aligned>

²⁰ <https://www.un.org/sustainabledevelopment/sustainable-development-goals/>

investments encompass any financial instrument related to climate finance, investments in listed and non-listed entities which turnover is generated at least 50% from climate finance activities. Bonds funds should invest at least 75% of the total assets in green bonds. The latter should be compliant with the GBP or ICMA, CBI or any other internationally recognised initiative (see Chapter 4). Direct investments may include those in climate-related infrastructure.

Exclusions: The LuxFlag climate label features an exclusion criterion that requires the applicant investment fund to provide evidence that its exclusion policy is applied across 100% of its portfolio in accordance with the exclusion list. The exclusion list covers activities /categories, such as new construction of electric and thermal coal-fired plants, nuclear projects, large geothermal plants located in protected forest areas, biofuel projects, oil production from oil sands and others²¹.

Criteria: LuxFlag sets eligibility criteria. Three scope-related eligibility criteria are described in the respective paragraph. Further on, the Luxflag label requires transparency on Climate Finance objectives and portfolio compositions towards investors. A monitoring mechanism should also be provided along with the evaluation of ESG standards. The fund should also respect the regulatory framework of the EU authorisation country.

Taxonomy: The Luxflag Climate Finance Label has embedded within the framework of its criteria a taxonomy which closely reflects that of the International Development Finance Club (IDFC) (See Chapter 4). It presents a list activities, categories, associated sub-categories as well as accompanying examples that are eligible for classification as climate finance activities. These activities are related to the mitigation and adaptation of climate change or cross-cutting activities according to the classification as defined under the Common Principles for Climate Mitigation Finance Tracking²². An extensive overview of the existing taxonomies including the IDFC taxonomy is available in Chapter 4..

Verification: LuxFlag label accepts and reviews applications after the applicant submits the application form along with a series of documents which among others involve the prospectus of the investment vehicle, the latest audited annual financial statement, a full list of assets of the investment fund, ESG/SRI climate investment policy etc²³. Luxflag label informs the applicant about the application receive and engage an auditor for the completion of Agreed Upon Procedures, empowering him/her to examine the report as provided by the applicant. The completed application is presented to the Climate Finance Label Eligibility Committee for analysis and recommendations to the board of directors. Based on the committee's recommendations the LuxFlag board approves or rejects the application in one month time. The Luxflag label award is valid only for one year and must be renewed. Each labelled fund has to submit a compliance letter after six months. The fund should be fully compliant otherwise, the application is frozen.

2.3.6 The FNG Label for sustainable mutual funds

Context: The FNG Label²⁴ label is managed by an industry association and aimed at facilitating sustainable investment in German speaking countries (Germany, Austria, Lichtenstein and Switzerland). The label principally focuses on mutual funds of all asset classes. The label does not feature a definition of "green" since it seeks to award funds with the best ESG performance, therefore it requires issuers are screened against ESG criteria.

The FNG label for sustainable mutual funds also aims at offering to consumers, institutional investors and marketing organisations a transparent standard for funds which pursue a consistent and rigorous sustainability strategy. It is based on minimum requirements in accordance with the internationally recognized standards and guarantees scrutiny by an independent auditor and grading criteria. The minimum requirements it stipulates are defined in a similar way to the exclusion criteria of other national labels. The label's main goal is to establish a continuous improvement of quality standards for sustainable investment products.

Scope: Eligible for the FNG label are mutual funds or equivalent investment vehicles. The label is intended for all asset classes that are compliant with the UCITS regulation or an equivalent standard. However, structured, guarantee, microfinance, synthetic exchange-traded funds and funds of funds cannot apply for the label on

²¹ <https://www.luxflag.org/labels/climate-finance/>

²² <http://www.worldbank.org/en/news/feature/2015/04/03/common-principles-for-tracking-climate-finance>

²³ <https://www.luxflag.org/labels/climate-finance/useful-information4/documents.html>

²⁴ <http://www.fng-siegel.org/en/>

account of their specific fund characteristics. The use of derivatives must be limited to instruments which have a stable leveraging effect and are used to hedge certain market risks.

In a first step the applicant has to prove compliance with the following mandatory criteria:

- A fully completed and publicly available FNG sustainability profile, which is no more than one year old at the date of submission.
- A fully completed and publicly available Eurosif transparency code declaration, also no more than one year old. The declaration should clearly and accurately reflect the analysis of the selection steps
- Proof that at least 90% of the fund portfolio in terms of number of issues and assets under management underwent ESG screening (excluding cash holdings). The ESG analysis must show the applicant evaluates environmental and social and governance criteria.

Exclusions: The FNG label incorporates exclusion criteria which outline investments in activities that cannot be considered in the ecolabelling process, such as manufacturing of controversial weapons, manufacturing of conventional armaments, operators of nuclear power plants, coal mining companies, companies which exploit concentrate sands and companies which use and/or produce hydraulic fracking technologies. The applicant should not violate human and labour rights, environmental and bribery and corruptions laws.

Similar to other financial labels, the FNG label also specifies exclusion criteria in the case the issuer is a country. To ensure that for government bonds, the portfolio does not contain securities issued by countries which are classified as "not free" according to the currently valid Freedom House²⁵ ranking, countries which have not ratified the UN Convention on Biological Diversity²⁶ and or have not ratified the Kyoto Protocol²⁷, countries which are listed within the bottom 40% of countries in the currently valid Transparency International's Corruption Perceptions Index²⁸, and countries which are in violation of the Nuclear Non-Proliferation Treaty²⁹ and countries which fulfil the "Possession of Nuclear Weapons" criterion within the criteria. In addition to these, the exclusion criteria also reject issuers who are in violation of the ten Key Principles of the UN Global Compact³⁰ or are active in manufacturing controversial and conventional weapons and operators of nuclear power plants. As regards the two latter, a threshold of 5% is set up below which the fund is eligible for ecolabelling even if invests in these sectors.

Taxonomy / Criteria: The FNG label awards points within its grading section for products standards for the quality of sustainability analysis which assesses the sustainability character of the industry the financial product is to be invested. Industries with strong environmental impacts are defined in the FNG label based on the CBI taxonomy (see Chapter 4). In addition to the latter list, it also classifies the following as sustainable:

- Companies financing in their core business activities according to the list defined by the Climate Bond Initiative (based on a case-by-case review),
- Fair trade,
- Sustainable education (operators of universities), and
- Sustainable medicine (genetics).

The FNG Siegel apart from the minimum requirements applies a grading model to distinguish the performance of the ecolabelled funds. Hence, it involves three criteria categories of different weighting. Further on the category 'Impacts' includes three sub-criteria. The applicant is ranked in a star label scale beginning with zero up to three stars.

Verification: The auditing and evaluation of the application is handled by an independent verifier, which has to demonstrate international experience in the certification of sustainable funds. The scheme requires the sustainability strategy of the fund to be communicated and also detailed information on the investment company and the sustainable fund, the ESG evaluation of companies (countries), the fund management process, ESG reporting and control.

²⁵ <https://freedomhouse.org/report/freedom-world/freedom-world-2018>

²⁶ <https://www.cbd.int/convention/text/default.shtml>

²⁷ <https://unfccc.int/process/the-kyoto-protocol>

²⁸ <https://www.transparency.org/research/cpi/overview>

²⁹ <https://www.un.org/disarmament/wmd/nuclear/npt/>

³⁰ <https://www.unglobalcompact.org/what-is-gc/mission/principles>

2.3.7 Green Funds Scheme

Context: The Dutch Green Fund is a scheme for funding environmental projects, under which various stakeholders work together, improving the environment by funding innovative environmental technologies and investing in nature and the environment. The scheme only refers to the Netherlands and its key element is a tax incentive. Everyone who invests in green bonds or green funds is eligible for a tax advantage of 2.5% on his or her green capital. However, the interest rate of the investment is lower than the market interest rate, and therefore the tax incentive compensates the latter making the project attractive for investors and financial institutions.

Scope: Projects considered for investment are those related to nature, forest and landscape, and agriculture. Other sectors reflected are energy, sustainable construction and sustainable mobility. The scheme can also invest in further sectors as long as they generate major environmental benefits and are innovative. The majority of the projects that obtained green certificates as proof of a green investment are in organic farming, green label greenhouses and renewable energy³¹

Exclusions: There are not extensive exclusion requirements. The main prerequisite is the project to provide a significant and immediate environmental benefit.

Criteria: The Green Fund Scheme does not apply environmental criteria apart from obtaining the green certificate. In the frame of the green certificate, the government sets criteria applying to green projects and assures compliance with those criteria for evaluating "green". Following the green certificate issuance, the financial institution can release the investment, yet it has to allocate 70% of the proceeds, labelled as green, to certified green projects.

Verification: The procedural flow for funding green projects entails the economic assessment of the project and the application for a green certificate to the government, which is a prerequisite for financing the project. The government certifies the greenness of the project and issues the certificate, which remains valid for the following ten years. For implementing the green fund scheme, diverse Dutch governmental institutions are working closely together. Additionally, the government has created a list of approved green institutions, which are then described as green funds or banks with a green fund.

Next to the application for funding, the bank applies for a green certificate to the government. The green certificate is necessary if the investment is to be realising through a green fund. The government checks whether the project meets all the conditions of the Green Funds Scheme and, if so, it issues the green certificate is valid for ten years. Thereafter, the procedure is completed and the project, which is officially characterised as green, is eligible for green funding.

2.3.8 Bond related schemes/initiatives

2.3.8.1 Climate Bonds Standard & Certification Scheme

Context: The Climate Bonds Standard and Certification Scheme³² is a Fairtrade-like labelling scheme for bonds operated by the Climate Bond Initiative³³ which is an investor-focused not-for-profit organisation, promoting large-scale investments aiming to deliver a global low carbon and climate resilient economy. The scheme allows investors, governments, industry and other stakeholders to prioritise 'low carbon and climate resilient economy' by certified climate bonds. The scheme can be used by bond issuers, governments, investors and the financial markets to boost investments that can address climate change. Its mission is to 'Mobilise debt capital markets for climate change solutions'.

Scope: The scope is outlined to ensure consistency with the 2 degrees Celsius warming limit in the Paris agreement and specifies which bonds can be certified. The scheme embraces a variety of bonds and also certifies debt instruments that do not fall within the strict definition of a 'bond', such as green bond funds, loan facilities and a wide variety of other debt instruments as defined by the Green Bond initiative.

³¹ The Green Funds Scheme. A success story in the making. NL Ministry of housing, Spatial Planning and the Environment

³² <https://www.climatebonds.net/standard>

³³ <https://www.climatebonds.net/>

The standard represents a certification system whose key features can be summarised as follows:

- Full alignment with the latest versions made up of the GBP
- Clear mandatory requirements for use of proceeds, tracking and reporting
- Specific eligibility criteria for low carbon and climate resilient projects and assets
- An insurance framework with independent verifiers and clean procedures
- Certification by an independent Climate Bonds Standard Board.

The requirements of the standard are divided into pre-issuance requirements that need to be fulfilled ahead of issuance and post-issuance requirements necessary to be met by issuers striving for continued certification that follows the issuance of the bond.

Pre-issuance requirements: The selection of Nominated Projects & Assets defines the obligation of the issuer to establish, document and maintain a decision-making process to determine the eligibility of the Nominated Projects & Assets. Internal processes & controls criteria refer to systems, policies and processes to be used for managing bond funds and investments. They include tracking of the proceeds, managing unallocated proceeds and earmarking funds to nominated projects & assets.

Reporting prior to issuance entails the bond disclosure documentation that in turn describes the investment areas into which the Nominated Projects & Assets fall, the intended types of temporary investment instruments for the management of unallocated proceeds, and also should be specified whether a periodic assurance engagement will be undertaken during the term of the bond. If so, the expected frequency of the periodic assurance needs to be set.

Post-issuance requirements: the post-issuance requirements are split into three parts. The first part refers to the reporting process and sets requirements concerning the continuous eligibility of the Nominated Projects & Assets and a statement on the environmental objective of the bond. Additionally, use and non-contamination of proceeds is also included in this specific part along with the reporting obligations. As concerns the latter, the issuer should provide a report to the bond holder and the Climate Bonds Initiative at least annually, containing the list of Nominated Projects & Assets to which proceeds of the bond have been allocated. The report should also include a brief description of the projects, the amounts disbursed, and the expected impacts.

The second part of the scheme requirement refers to Projects & Assets and lays out a two-step process to determine their eligibility. It includes a Climate Bond Taxonomy (see Chapter 4) and sector-specific technical criteria. Firstly, specifying the project/requirements, an asset should fall into one or more of the investment areas contained in the latest version of the Climate Bond Taxonomy, and then the Nominated Projects & Assets shall meet the most updated sector-specific eligibility criteria.

The third part of post-issuance requirements sets out prerequisites for specific bond types. Definitions for the bond types are also provided in the standard. Criteria related to specific bond types; project holding, settlement period and earmarking to be eligible for certification are also outlined.

The Climate Bond Standard & Certification Scheme can certify bonds in the areas of energy, transport, utilities and buildings and develops criteria for further sectors, such as natural resources and industry, and sub-sectors corresponding to hydropower, recycling, disposal, IT, communication and others.

Verification / certification: The standard includes a Climate Bond Certification process with two distinct phases. The pre-issuance certification phase includes assessment and certification of the internal processes of the bond issuer, entailing selection for projects & assets, internal tracking of proceeds, and the allocation system of the funds. A verifier assesses the readiness of the issuer and the proposed bond to conform to the standard. On the other hand, the post-issuance certification phase assesses and certifies the conformity of the issuer and the bond with all the post-issuance requirements. Post-issuance periodic certification is not mandatory, but an option, in the case issuer wants to reaffirm ongoing conformity with the standard during or after the term of the bond. Internal process & controls should be carried out by the issuer and disclosed to the verifier.

An approved verifier has to be involved in the certification procedure as mentioned above. The verifier has to be supplied with all relevant information by the issuer to conceptualise a report giving assurance that Climate Bonds Standard requirements are met. Next to certification, the bond receives a special mark and can be traded as a certified climate bond. Following the label award, the issuer needs to provide annual reports to the CBI and the market throughout the term of the bond. These reports should confirm that the bond still complies with the requirements of the Climate Bonds Standard. If any change is made to the nominated assets/projects

or proceeds of the bond, these changes can also be disclosed in the annual internal report. External verification of the report is not required by the label.

There are two types of costs involved with Climate Bonds certification: internal and external. The issuers incur the internal costs when establish the required internal processes and controls to meet the requirements of the certification. They may also include costs associated with tracking and performance of the projects & assets tied to the climate bond. On the other side, external costs firstly include engagement of the verifier and secondly a certification fee. The latter is paid once immediately after the issuance of the bond.

CBI maintains a list with registered and approved verifiers. To become a verifier, one must demonstrate competence and experience in three thematic areas as follows:

- Issuance of debt instruments in the capital markets and management of funds within issuing organisations
- Technical characteristics and performance of low carbon projects and assets in the areas covered by the specific criteria available under the Climate Bonds Standard.
- Provision of Assurance Services in line with the International Standards on Assurance engagements ISAE 3000³⁴

Additionally, the approval of verifiers is specific to the location where they operate and their technical expertise.

2.3.8.2 Green Bond Principles (GBP)

Context: The International Capital Market Association (ICMA) published the GBP, which aim to promote integrity in the Green Bond market through guidelines, which recommend transparency and disclosure. With a focus on the use of proceeds, the GBP intend to support issuers in transitioning their business model towards greater environmental sustainability through specific projects.

Scope: They specify high level categories for eligible Green Projects in recognition of the variety of current views and of the ongoing development in understanding of environmental challenges and consequences, and allow market participants for developing their own robust procedures while referencing a broad set of complementary criteria as relevant.

GBP are voluntary process guidelines that recommend transparency and disclosure and promote integrity of the market by clarifying the approach for issuance of green bonds. They provide issuers with guidance on the key components involved in launching a credible green bond and aid investors by promoting availability of information necessary to evaluate the environmental impact of their Green Bond investments.

The GBP guidelines suggest a clear process and disclosure for issuers, investors, banks, underwriters, placement agents and several others which may be used to understand the features of any given bond. The GBP emphasise transparency, accuracy and integrity of information that will be disclosed and reported by issuers to stakeholders.

The GBP outline four core components

- Use of Proceeds
- Process for Project Evaluation and Selection
- Management of Proceeds
- Reporting

Criteria: The use of proceeds is the basis of the GBP. All designed green projects should be assessed and where feasible quantified by the issuer and provide environmental benefits. The GBP requires the project to contribute to environmental objectives, such as climate change mitigation and adaptation, natural resources and biodiversity conservation, and pollution prevention and control. The GBP define several broad categories for eligibility for green project which include renewable energy, energy efficiency, pollution prevention and control related projects, environmentally sustainable management of living natural resources and land use, circular economy etc.. Definitions for green may also vary depending on sector and geography.

³⁴ <http://www.ifac.org/system/files/downloads/b012-2010-iaasb-handbook-isae-3000.pdf>

Reporting: The issuer should communicate to investors the environmental sustainability objectives, the justification that the projects fits to eligible green projects categories, the criteria and their evaluation as regards environmental and social risks associated with the project. Encouraging transparency, GBP recommend an external review as regards the process for project evaluation and selection.

The net proceeds of the Green Bond, or an amount equal to these net proceeds, should be credited to a sub-account or moved to a sub-portfolio or otherwise tracked by the issuer in an appropriate manner. It should also be attested to by the issuer in a formal internal process linked to the issuer's lending and investment operations for green projects.

Issuers should carry out and record readily available up to date information on the use of the proceeds to be renewed annually until full allocation, and on a timely basis in the case of material developments. The GBP recommend the use of qualitative performance indicators and, where feasible, quantitative performance measures. It also suggests the disclosure of the underlying methodology and assumptions made in the quantitative determination.

Verification: Compliance with the four core GBP components can be carried out by an external reviewer. The reviews may differ in scope and can cover full or part of the four GBP components. They are grouped into the following types.

- Second party Opinions are normally carried out by an institution with environmental expertise which is independent from the issuer. The assessment examines the alignment with GBP, yet it can also include the assessment of the issuer's overarching objectives, strategy, policy and/or processes related to environmental sustainability, and the evaluation of the environmental features of the type of projects intended for the Use of Proceeds.
- An issuer can obtain independent verification against a designated set of criteria. The verification process focuses on alignment with internal or external standards.
- An issuer can have its green bond framework or Use of Proceeds certified against a recognised external green standard or label. The certification is normally carried out by a qualified, accredited third party.
- The green bond can be evaluated or assessed by qualified third parties, such as specialised research providers or rating agencies according to an established scoring/rating methodology.

An external review may be partial, covering only certain aspects of an issuer's Green Bond or associated Green Bond framework or full, assessing alignment with all four-core components of the GBP. The timing of an external review may depend on the nature of the review. Its publication can be constrained by business confidentiality requirements. The GBP encourages external review providers to disclose their credentials and relevant expertise and communicate clearly the scope of the review conducted. In turn, the GBP can provide with guidelines and promote best practice. The guidelines provide information and transparency on the external review processes.

2.3.8.3 The European Investment Bank Climate Awareness Bonds

Context: The European Investment Bank (EIB) issues Climate Awareness Bonds (CABs) considering the EU and EIB climate policy. The EIB is world leader in Climate Finance lending USD 21bn in 2016³⁵. The vast majority of that amount was lent in advanced economies while the rest in emerging and developing economies. The share of CABs allocations from 2007 to the end of 2016 was 87% in the EU and 13% outside the European Union.

The first CAB was issued in 2007 and since then the EIB participates in different activities as regards sustainable finance, for example the coordination of the High Level Expert Group (HLEG) for the climate mitigation taxonomy and the comparison of China/MDB taxonomies. It has also edited various sustainable finance related reports, including the first allocation report, first comprehensive impact report, first allocation report by project and bond, first post-completion project report and the first independent reasonable assurance report including external review form.

³⁵ MDB Joint report on Multilateral development banks' Climate Finance and internal sources for 'Advanced Economies'
<http://www.eib.org/attachments/press/2016-joint-report-on-mdbs-climate-finance.pdf>

In 2017, the EIB has achieved its target to exceed 25% of its annual lending toward Climate Action³⁶. The total loans signed for Climate Action reached EUR 150 bn in the period 2010-2017. A large proportion of the CABs (36%) is lent to low carbon transport projects, 26% in energy efficiency, 23% renewable energy, 6% other climate mitigation, 5% research development and innovation, and 4% climate adaptation. The forecast for Climate Action lending in 2015-2020 is about USD 100 bn.

Scope: Apart from CABs, the EIB, as a climate finance pioneer, provides with other climate-related investment schemes³⁷. Equity funds are also established and provide a "quality stamp" to encourage and attract new investors, enable investment into new asset classes (e.g. biodiversity, soil decontamination etc.), and mobilise additional public and private capital for climate action projects.

The eligible projects are focusing on two main sectors namely renewable energy and energy efficiency. The former entails projects such as wind, hydropower, wave, tidal, solar and geothermal energy. The latter comprises projects on district heating, cogeneration, building insulation, energy loss reduction in transmission and distribution and equipment replacement with significant energy efficiency improvements.

Exclusions: Nuclear and coal based energy generation are excluded. Similarly, equity and intermediated investments are disqualified. The threshold for GHG emissions is set at 550g CO₂e/kWh.

Criteria: The general EIB practise considers environmental, social, economic and technical aspects. It also requires CAB eligibility assessment and quality checks. The EIB 2015 Climate Strategy³⁸ aims to implement the Paris Agreement inside and outside the EU by focusing on three key areas:

- Reinforcing the impact of climate financing
- Building resilience to climate change
- Further integrating climate change considerations across EIB standards, methods and processes

The EIB is the world's largest climate financier. Its target for 2018 was at least 26% of overall annual financing is committed to Climate Action. Its Climate Action contributed to savings of 2 to 3 million tonnes CO₂-equiv. over the past years.

Taxonomy: CABs are aligned with the GBP. Additionally, the particular EIB CAB strategy and its key features can be summarised as follows:

- Scale of issuance with benchmark-size green bonds
- Building a green bond curve in EUR
- No premium charged for green bonds
- No refinancing of projects

Reporting: The EIB recommends transparency and accountability by deciding followings

- Alignment with the GBP
- Eligible sectors: Renewable Energy and Energy Efficiency
- Reporting project impacts and linking bonds to projects
- External review/audit of the CAB programme

Verification: The CAB processes can be a matter of an external review through an audit. The audit elements include allocation of proceeds, impact indicators, such as GHG emissions and savings, and heat and electricity metrics. The internal tracking and management of proceeds should also be included in the audit process. Moreover, any potential disbursement-related change affecting the project's CAB eligibility should be publicly disclosed. As a result of the alignment of CAB strategy with the one of the GBP, the external review can be based on GBP recommendations.

³⁶ <http://www.eib.org/en/projects/priorities/climate-and-environment/climate-action/index.htm>

³⁷ European Investment Bank. www.eib.org/climate

³⁸ EIB Climate Strategy. Mobilising finance for the transition to a low-carbon and climate-resilient economy. <http://www.eib.org/infocentre/publications/all/eib-climate-strategy.htm>

2.3.9 Examples of private schemes

2.3.9.1 Rabobank green and sustainable bonds framework

Context: The Rabobank Green and Sustainability Bond Framework³⁹ is a commercial private sector initiative aimed at facilitating two types of funds to be labelled according to the sector they are invested in. Rabobank can issue bonds under the combined Green and Sustainability Bond Framework. Thus, they can be labelled as either 'Green Bonds' or 'Sustainability Bonds'.

Scope: The Rabobank Green Bonds are only applicable to funds allocated to financing of renewable energy projects, specifically wind and solar. The Rabobank Sustainability Bonds refer to funds allocated to loans, which are provided to SMEs with sustainability certifications on products, processes or buildings. Under the "green" component of the framework as provided by Rabobank, any new or ongoing renewable energy project is eligible to be funded entirely or partially by the allocation of the bonds proceeds. Rabobank can also issue Green and Sustainability Bonds in a combined portfolio.

Inclusions: A number of restricted activities are excluded from benefitting from the funds available under the scheme and are registered in a specific exclusions list.

Taxonomy: The framework applied for assessing "green" bonds follows the GBP (see Chapter 4) of the ICMA. Judging by the guidelines to be followed in assessing renewable energy projects for funding, it is quite clear that the framework aims to minimise risks and impacts and support IFC⁴⁰ business activities with the following attributes:

- potential significant adverse environmental or social risks and/or impacts that are diverse, irreversible, or unprecedented.
- potential limited adverse environmental or social risks and/or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures.
- minimal or no adverse environmental or social risks and/or impacts.

Reporting: Reporting will be available to investors within one year from the date of the green bond issuance and annually thereafter until the proceeds have been fully allocated. The report informs on the total amount of loans for wind and solar projects on a portfolio basis. Rabobank discloses a list of projects as far as client confidentiality allows it. Rabobank is also responsible for reporting on the installed energy generation capacity for the size of the bond and has to report in a similar manner as regards Sustainability Bonds. However, due to confidentiality reasons it will not be able to disclose information on individual SME loans. Concerning the impact reporting of the SME funding, a breakdown of the amounts per selected certification scheme, and sectors will be provided. On top of that, the report should include details about the objectives of the certification and performance indicators. The project can also report on positive impacts as far as the client allows for that.

Verification: All renewable energy projects to be funded are evaluated according to Equator Principles⁴¹. Additionally, Rabobank requires that the eligible SMEs possess certifications that are based on predefined criteria, have an independent control mechanism and meet minimum legal standards. To demonstrate its environmental commitment, Rabobank defines eligibility criteria, demonstrating a structure and transparent selection process, management of proceeds, and reporting on an aggregate level. The Rabobank framework is subject to an external assessment of the use of proceeds, project evaluation and selection, management of proceeds and quality of reporting. On top of that, an eligibility committee evaluates the provided sustainability certifications and decides on their eligibility based on best practices, performance of the sector and scope of the certification.

³⁹ <https://www.rabobank.com/en/investors/funding/greenandsustainabilitybond/index.html>

⁴⁰ https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/policies-standards/es-categorization

⁴¹ Reporting can be found on <https://equator-principles.com/members/rabobank>

2.3.9.2 Triodos Socially Responsible Investment Fund

Context: The Triodos Socially Responsible Investment (SRI) fund is an UCITS that aims to generate long-term capital growth for its investors through a diversified portfolio of listed sustainable companies, which covers various economic sectors and geographical areas. Triodos is an open-ended investment fund with variable capital.

Scope: Triodos distinguishes between two fund categories:

- Sustainable equity fund is a global impact fund, investing across a diversified portfolio of large listed companies that are selected for their financial as well as sustainability performance
- Sustainable pioneer fund, which invests in global equities of innovative small and medium sized companies that are active on the forefront of ground-breaking solutions in the field of sustainability. This scheme also requires total transparency.
- The fund invests in specific environmental, social and cultural activities. The environmental sectors for investment are organic farming, renewable energy, ecological development and organic food.

The value of the fund reached EUR 951 million with 70% to be sourced to the Equity fund and the rest to Sustainable Pioneer fund.

Exclusions: The institution's sustainable investment strategy follows a two-step procedure for exclusions. Firstly, the companies selected should derive revenues from products and services that contribute towards a transition to a sustainable world. In a second step, the companies that do not meet the minimum standards are excluded from funding. In turn, minimum standards are established and required for the environmental, social and governance criteria. Among others, the fund screens out investments in products and services related to arms, fossil fuels, tobacco, gambling and animal testing.

Criteria: Positive screening is adopted to identify companies that positively contribute towards a more sustainable future using seven transitions themes that are tracked against the UN Sustainable Development goals (SDG) and entail sustainable food and agriculture, circular economy, sustainable mobility and infrastructure, renewable resources, innovation for sustainability, prosperous and healthy people and social inclusion and empowerment. Additionally, the fund invests in equity companies worldwide and requires at least 67% of its net assets⁴² are invested in shares of large companies and the rest 33% in shares of small and mid-cap companies. They are selected because of their financial, social and environmental performance.

Reporting: The scheme offers total transparency as regards the companies selected for investment and publishes the actual portfolio of both fund schemes and a justification for the inclusion of each company. The fund's strategy is based on active engagement and dialogue that aims at promoting sustainability awareness and supporting action.

Verification: Selecting listed companies for inclusion in the Triodos investment fund is a systematic process. To ensure compliance with social, environmental and governance requirements, companies are screened against a range of criteria, in a three-stage process⁴³. Triodos offers total transparency about the companies selected for investment and publishes the actual portfolio of both fund categories and the rational for the inclusion of each company. At least once each year, the scheme evaluates all companies in the portfolio to confirm their products continue to support the transition to sustainability. The fund applies an initial fee at 0.5% of the investment and an annual service charge of 0.4% per year based on the value of the holdings, which is charged monthly.

2.3.1 Conclusions

A number of legislations regulate the financial sector in Europe. However, sustainable finance investing in Europe is voluntary and mostly self-regulating. A number of voluntary labels and schemes are available on the market but they are diverse in their scope, coverage, strategies as well as mechanisms for assessing and mitigating environmental, social and governance factors. The existing market based approaches are

⁴² Triodos Bank <https://www.triodos.co.uk/ethical-investments/sustainable-equity-fund>

⁴³ www.triodos.co.uk/sri

inconsistent and exposes investors to risks. There is therefore a need for a framework for environmentally sustainable or green investment, to be applied across EU-28 and developed in line with existing financial regulations that stimulates not only the comparability of investments but also facilitates and enhance sustainable investment at EU level and boosts consumer confidence.

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Table 1: Overview of labels

	TEEC label	Luxflag Climate finance	FNG Siegel	Nordic Swan	Austrian label	Green Funds Scheme
Date of launch	01/12/2015	01/09/2016	01/05/2015	15/06/2017	Established in 1990	It was implemented in 1995
Number of labelled funds or value	4 green bonds, 3 equity, 8 infrastructure App. EUR 2 Md	4 funds EUR 450 M	5 Environmental thematic funds (equity and green bonds) among 40 applicants	13 (EUR 3 Md) [All in equity: 8 focus on Sweden, 3 Global, 1 Frontier, 1 Energy]	more than 100 labelled financial products	Since the implementation of the program, more than 234,400 individuals have invested, more than EUR 6.8 billion in green funds, financing more than 5.000 projects.
Time to audit an application	4 to 6 weeks (depending on the type of fund)	1 month	4 months	About 30 hours over a 6-9 week period. (Can be much longer depending on the fund companies eagerness and adaptability)		N/A
Legal basis	Secondary & tertiary legislation	None	None	None	None	None
Eligibility criteria	UCITS/AIFM (at least 50% invested in Europe)	An investment fund authorised by a Member State or be subject to supervision equivalent to that in EU Member States	UCITS funds	UCITS funds	Sustainable Funds/Investment Certificates - Ethics-Ecology, Thematic Funds /Investment certificates	The Dutch "Green Fund" is not a label but a tax scheme. In green savings accounts, 70% of deposits are invested in green projects.
Decision on the evolution of the scheme	A multi-stakeholder committee chaired by the French Ministry of Environment	Luxflag in conjunction with a dedicated multi-stakeholder industry working group led by the Association of Luxembourg Fund Industry	An independent expert committee	The Nordic Ecolabelling Board, an independent external organisation.	Government sponsored: Federal Ministry of Agriculture and Forestry, Environment and Water Management	Government sponsored Ministries of the Environment, Finance and Agriculture.
Institution granting the label	Accredited (by the National Accreditation body COFRAC) auditors	LuxFlag Board upon the recommendations of the Eligibility Committee and LuxFlag secretariat	GNG, the operational labelling body of FNG, advised by an independent expert committee, who review the audit results	Nordic Swan Ecolabel	Federal Ministry of Agriculture and Forestry, Environment and Water Management	Ministries of the Environment, Finance and Agriculture.
Labelling costs	None	EUR 3,000 (once labelled)	EUR 3,000 (application)	To generalize, an application fee of 3,000 EUR and an annual license fee of 0.0015% of AUM in the fund. Please follow link for all details	The annual royalties depend on the specific turnover of the branch and/or product group of the applying enterprise.	N/A

	TEEC label	Luxflag Climate finance	FNG Siegel	Nordic Swan	Austrian label	Green Funds Scheme
<i>Audit costs</i>	Depending on auditor	0	Included into labelling costs	See labelling costs	See labelling costs	N/A
<i>Labelling period</i>	1 year (renewable)	1 year (renewable)	1 year (renewable)	Same as the criteria document. Current criteria are valid until 2020-06-30. The criteria are updated every 3-5 years.	1 year (renewable)	The Government checks whether the project meets all the conditions of the Green Funds Scheme and, if so, it issues a green certificated that remains valid for ten years.
<i>Intermediate verification</i>	Yes	Compliance verification after six months	None	Annual	None	None
<i>Green taxonomy</i>	CBI based, however slightly adjust to reflect national priorities	Common Principles for Climate Change Mitigation and Adaptation and Adaptation Finance Tracking (IDFC (International Development Finance Club)+MDBs)	CBI based	Based on ICMA's GBP.	The scheme does not stipulate the use of specific external taxonomy.	The scheme does not stipulate the use of a specific external taxonomy. It contains a definition of green projects providing a significant and immediate environmental benefit.
<i>Transparency requirements</i>	Some of the fund's financial management practices must be transparent. Investor's documents must present the environmental strategy of the fund	The applicant must publish full investment portfolio at least once a year. Additionally, it must describe its Climate Finance objectives (environmental and financial) and be transparent towards investors in its portfolio composition and documentation by providing categories and/or sub-categories of its Climate Finance investments	Signatory of the Eurosif Transparency Code required - FNG Matrix (a framework developed by FNG questioning the RI approach of the fund) required - Impact reporting assessed by the auditor (Points are granted depending on the quality of the KPIs reported)	Mandatory: Annual Fund sustainability report All holdings, updated quarterly Point Score: Detailed engagement information Voting records	Information on the sustainability or ecological/social concept of Ecolabelled products should be presented in line with the European Sustainable and Responsible Investment Forum's Sustainability Fund Transparency Guidelines.	There are no reporting obligations
<i>Control & monitoring</i>	Control and Monitoring plan Guidelines. 1. Process of certifying a candidate investment fund 2. The methods for monitoring a certified fund 3. The management of any observations made on the Control and Monitoring Plan in force	Compliance monitoring at six months	Included into the Label's rules of procedures and FAQs	An on-site visit is performed in connection with the application and once a year during the validity of the license. Sample checks are made on a regular basis.	The environmental and social evaluation of companies, public issuers and real estate is carried out by funds or external organisations.	Green projects are subject to the same economic examination by banks as non-green projects.

3. OVERVIEW OF THE REFERENCE MARKET FOR THE EU ECOLABEL FOR FINANCIAL PRODUCTS

As proposed in the European Action Plan on Financing Sustainable Growth (COM/2018/97), the EU Ecolabel Regulation 66/2010 could be applied to specific financial products offered to retail investors. Packaged Retail Investment and Insurance Products (PRIIPs) could be a starting point set of financial product for which EU Ecolabel criteria can be developed. However, the scope of the EU Ecolabel could be wider allowing retail investors with a preference for environmentally sustainable financial products to choose among several types of financial assets, while considering also their risk-profile return profile. Against this background, this chapter first analyses retail investors' holdings. Then, it focuses on PRIIPs, reporting definitions for each of the main PRIIPs categories based on the relevant EU Regulations. This section also includes a more detailed analysis of the sustainable investment fund market in Europe. Non-PRIIPs which may be included in the scope of the Ecolabel criteria for Financial Products, as bonds and stocks, as well as pension funds, are also covered in this chapter. Finally, a schematic classification of considered financial products is developed, based on their structure.

3.1 Overview of financial assets held by retail investors

This section covers the wealth allocation of European retail investors, non-professional investors⁴⁴, across several investment products (PRIIPs and Non-PRIIPs).⁴⁵ This section also provides an overview of the composition of financial assets held by public authorities, that are the major consumer category together with retail investors.

As shown by Figure 1, the composition of household's financial assets is relatively stable over time.⁴⁶ Currency and deposits, pension funds, and (life and non-life) insurance products constitute around 30%, 20%, 18%, respectively, of household's wealth. The share of equities in households' financial portfolios is also around 18%. Investment fund shares increased from 6% in 2012 to 8% in 2017. Turning to the least represented asset categories, less than 1% of households' wealth is invested in financial derivatives.

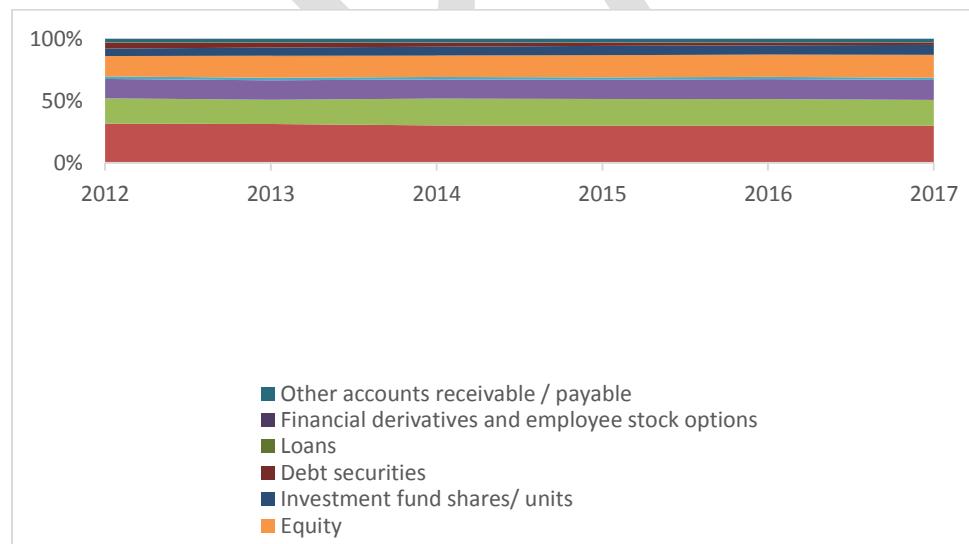


Figure 1 – Share of total financial assets held by households by financial instrument, EU-28, from 2012 to 2017. Total financial assets held by EU households: EUR 34 tr in 2017. Source: EUROSTAT.

⁴⁴ See Directive 2014/65/EU, Article 4 (1), point (11).

⁴⁵ This section provides an update to the analysis on retail investment products available in section 2.1 of the report on "Distribution systems of retail investment products across the European Union", European Commission.

⁴⁶ See the definitions of financial assets in section 2.1.

Figure 2 provides the distribution of households' financial assets across EU Member States (MS). With reference to 2017, more than half of EU-28 financial assets are held by households located in three countries, namely the United Kingdom (21.5%), Germany (17.1%) and France (15.6%). As shown in Figure 2, there are differences across MS in the way households allocate their financial wealth. Currency and deposits represent more than 50% of financial assets in the Czech Republic (53%), Greece (61%), Cyprus (62%) and Slovakia (60%). On the other hand, currency and deposits represent less than 25% of financial assets in Denmark (15%), Netherlands (17%), Sweden (14%) and the United Kingdom (24%). Households in Ireland, Netherlands and United Kingdom invest more than 30% of financial assets in pensions and standardized guarantees; on the opposite, Greece, Luxemburg, Hungary, Finland invest less than 5% in this asset class. The share of life insurance and annuity entitlements in households' portfolios is significantly larger in France (36%) and Denmark (28%) than in other MS. Life insurance products are much less popular in Eastern MS (e.g., Bulgaria, Czech Republic, Estonia, and Romania). As for the share of equity investment, households in Bulgaria (45%), Estonia (53%), Finland (39%) and Sweden (37%) are well above the EU average (24%). At the other end of the spectrum in terms of investment in company shares there are households in Germany (11%), Ireland (12%), Netherlands (11%) and the United Kingdom (10%). Finally, investment fund shares are proportionally mostly held by households in Belgium (15%), Spain (15%), Italy (13%) and Luxemburg (12%).

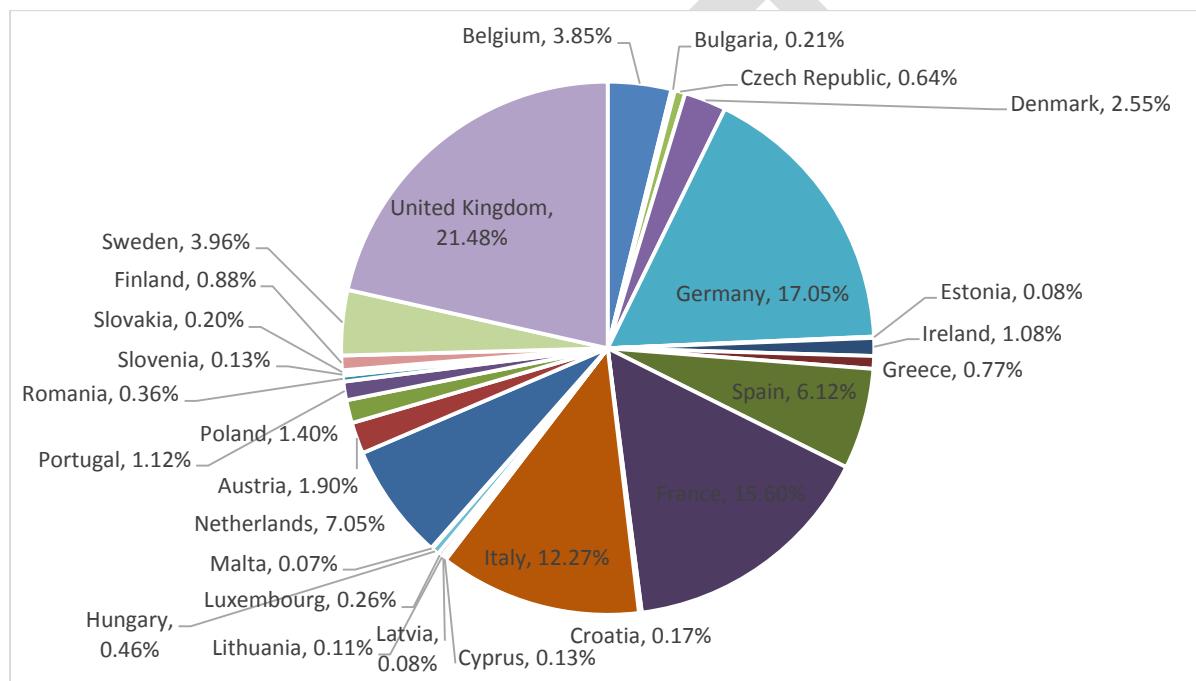


Figure 2 – Share of total financial assets held by households in 2017 across MS. Source: EUROSTAT.

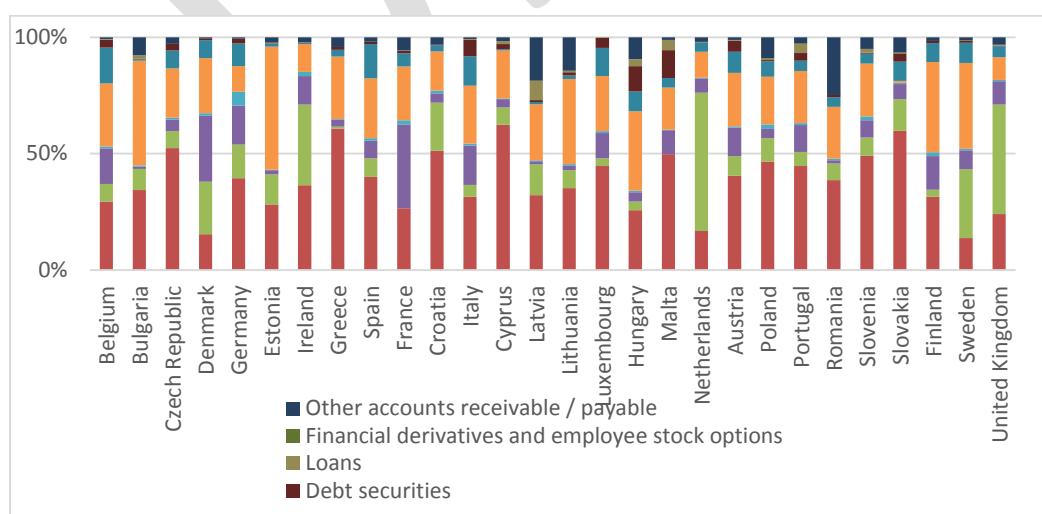


Figure 3 – Share of total financial assets of households across countries, by financial instruments in 2017. Source: EUROSTAT.

In addition to retail investors, public authorities are major consumers in Europe and can also significantly contribute to sustainable consumption and production.⁴⁷ Figure 4 shows the composition of financial assets held by EU Governments as a whole, over time. The general Government sector consists of institutions which are engaged in the redistribution of national income and wealth, and whose output is intended for individual and collective consumption. Government financial assets are mainly held in equity (40%) and in currency and deposits (17%). Investment fund shares increased from 3% in 2012 to 5% in 2017. Related to public authorities, Green Public Procurement (GPP) is worth mentioning. This is an instrument aiming at stimulating a critical mass of demand for more sustainable goods and services. It is a voluntary process whereby public authorities seek to procure goods and services with a reduced environmental impact throughout their life cycle when compared to goods, services and works with the same primary function that would otherwise be procured.⁴⁸ GPP criteria have not yet been developed for financial products .

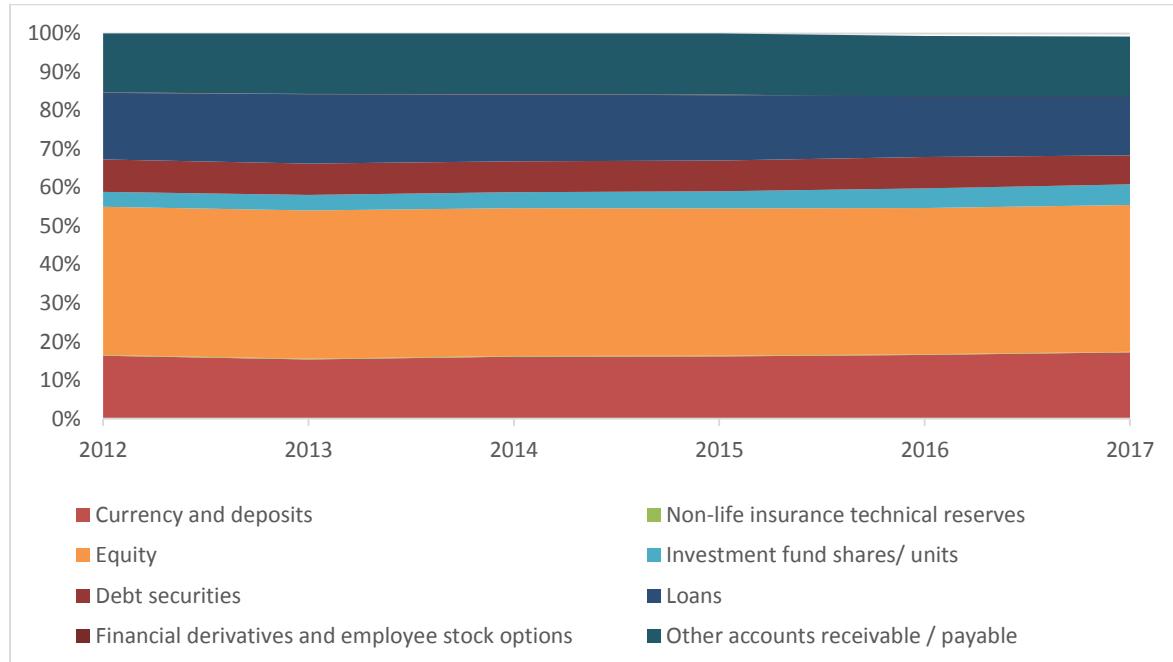


Figure 4 – Share of total financial assets held by general Government by financial instrument, EU-28, from 2012 to 2017. Total financial assets held by EU general Government: EUR 6 tr in 2017. Source: EUROSTAT.

3.2 Packaged Retail Investment and Insurance Products (PRIIPs)

PRIIPs cover a range of investment products which, taken together, make up a market in Europe worth up to EUR 20 tn⁴⁹. Figure 5 shows that the outstanding capital invested in investment funds, insurance contracts, structured retail products and deposits held by households has been broadly increasing until the end of 2017, when it peaked at above EUR 20 tn, to then slightly decrease in 2018Q1. Note that the figure provides only a rough estimation of the PRIIP market size. In particular, the Alternative Investment Fund (AIF, see Section 2.1) category includes both retail AIFs (RAIFs) and other AIFs (AIFs addressed to professional investors)⁵⁰. Deposits held by households and non-profit institutions serving households include both structured deposits, which are PRIIPs, and traditional deposits. Finally, data for structured retail products, not including derivatives, is available only for leading markets (i.e. Austria, Belgium and Germany).

⁴⁸ Reference Communication COM (2004) 400.

⁴⁹ The coverage of PRIIPs was estimated about EUR 10 tn in 2007 (see Impact Assessment final report SEC(2009)556).

⁵⁰ The EU Alternative Investment Fund Managers Directive (AIFMD) allows an AIF manager to market the shares of an AIF only to professional investors. It is important to note that the AIFMD Passport does not extend to marketing to retail investors. However, the AIFMD leaves the regulation of RAIFs to national discretion. Member States permit the marketing of AIF to retail investors imposing stricter requirements.

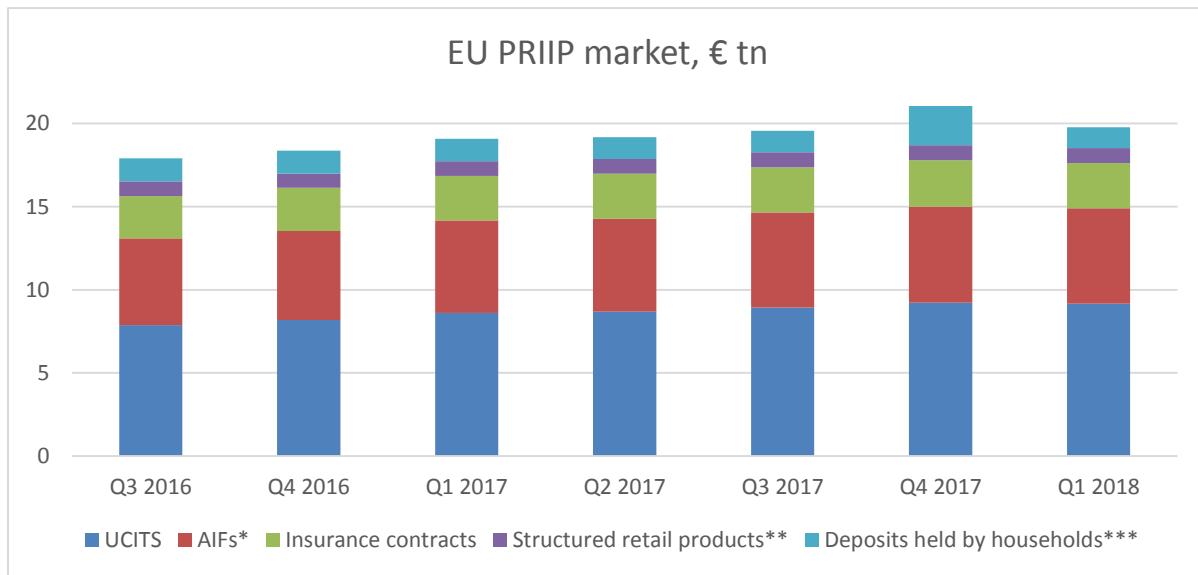


Figure 5 – Notes: for investment funds (UCITS and AIFs), the Net Asset Value is reported.

*Not all AIFs are PRIIPs. **Includes only leading markets (Austria, Belgium and Germany). ***Includes also traditional deposits, which are not PRIIPs. Sources: EFAMA (investment funds), EIOPA (insurances unit-linked and index-linked contracts), EUSIPA (structured retail products excl. derivatives), ECB (deposits).

3.2.1 Investment Funds

Investment funds (IFs) are collective investment undertakings that invest in financial and/or non-financial assets. Investment funds allow (i) investment strategies that could not otherwise be feasible owing to e.g. the large denominations; (ii) economies of scale; (iii) risk reduction through portfolio diversification. Investment funds can be classified by asset classes or by other characteristics of the fund. Considering asset classes, some examples of how the investment funds can be classified are the following:

- Equity funds: invest predominately in the stock market.
- Bond funds (also referred to as fixed income funds): invest in bonds. They can invest in one type of bond only, either government (sovereign) bonds or corporate bonds, or they can invest in both.
- Hybrid funds (also referred to as mixed or balanced funds): invest both in stocks and bonds.
- Real Estate funds: invest on tangible real estate assets.
- Commodity funds: invest in commodities (e.g., metals, energy, etc.), either tangible or through the use of derivative strategies.

Some other examples that reflect other characteristics of investment funds, can also include the following:

- Open End Funds: do not have restrictions on the amount of shares the fund can issue.
- Closed End Funds: are based on issuing a fixed number of shares. These funds generally issue shares to the public only once.
- Exchange-traded funds (ETF): are traded on a stock exchange (i.e., they are quoted on the stock exchange in the same way as shares and bonds). An ETF tracks the benchmark, i.e., the reference index (e.g., a stock index, a fixed income index, or a commodity index). An ETF holds assets such as stocks, commodities, or bonds.
- Hedge funds: apply a range of investment strategies and risk management techniques (e.g. emerging market funds, market neutral funds).
- Funds of funds: investment funds investing in other funds.

The EU legislation, distinguish the following two categories of investment funds:

1. UCITS Funds: these funds can be registered in Europe and sold to investors EU-wide using unified regulatory and investor protection requirements. UCITS funds are perceived as safe and well-regulated investments. As the UCITS framework is considered solid and safe UCITS are not only popular in

Europe, but also in South America and Asia among investors who prefer not to invest in a single company, but rely on diversified investments. UCITS funds have reached an outstanding amount of EUR 9,7 bn at the end March 2018. UCITs are PRIIPs. Among the EU 28 countries, UCITS are domiciled mainly in Luxemburg (38%), Ireland (20%), United Kingdom (13%) and France (10%).

2. **AIFs:** The managers managing these funds are regulated by the EU Alternative Investment Fund Managers Directive (AIFMD). The definition of AIF captures a broad range of funds, including all non-UCITS investment funds, including hedge funds, private equity funds and real estate funds. Some of this funds are sold to retail investors upon a national discretion, although such funds are in principle designed for professional investors. AIFs are domiciled mainly in Germany (29%), France (18%), Netherlands (14%), Luxemburg (12%) and Ireland (10%).

Between 60-80K investment funds are active in the EU, with net assets amounting to around EUR 15 tn. In Figure 6 investment funds are classified with respect to the asset class of investment. 72% of the total net assets of investment funds in Europe is held by equity, bond and mixed funds.

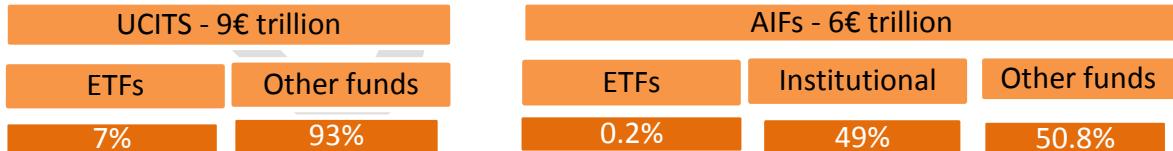
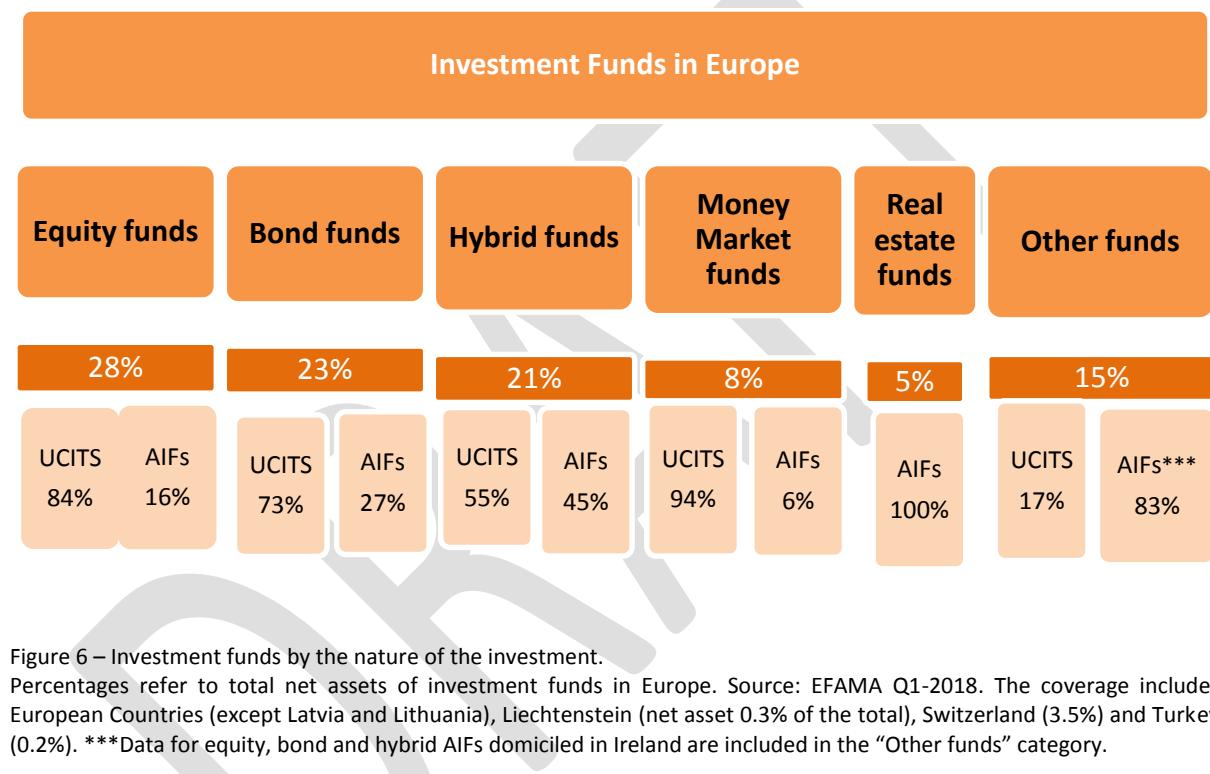


Figure 7 – Investment funds classified by UCITS and AIFs. Source: EFAMA Q1-2018, percentages w.r.t. the total net assets by category.

Figure 7 classifies investment funds in UCITS and AIFs. Net assets of UCITS ETFs reached EUR 632 bn in 2018Q1, up from EUR 19 bn in 2017Q4. They amount to 7% of the total net assets of UCITS. The vast majority of UCITS ETFs are domiciled in Ireland (56%) and in Luxemburg (24%). Net assets of institutional AIFs, which are AIFs reserved for institutional investors and do not fall under the definition of PRIIPs, amount to 49% of the total net assets of AIFs. The Ecolabel eligibility criteria for investment funds should foresee verifications at two distinct levels.

The first level is in most cases the ‘greenness’ of each of the companies in which the fund invests. In the case of bonds, it can be related to the company, or to the project which is being financed through the bonds. This should be based on the EU Taxonomy of green economic activities (see Section 4.1.2 below). The second level is the portfolio composition. In this respect, one could foresee methodologies to assess the overall ‘greenness’ of a portfolio, e.g. by computing a weighted average of the percentage of companies’ turnover deriving from green business and setting or threshold. It may e.g. also take into account the number of bonds issued in accordance with the GBS.

3.2.1.1 The European Sustainable Fund Market

Based on Bloomberg data, out of more than 80,000 active funds domiciled in the EU28, 421 funds are green or sustainable⁵¹. 86% of these funds are UCITS. These 421 funds are further classified as follows (one fund can be classified into more than a category):

- Clean Energy (40): Funds investing in securities of companies contributing to less carbon intensive energy production and consumption.
- Climate Change (20): Funds investing in securities of companies facilitating adaptation to the impacts of climate change.
- Environmentally Friendly (173): Funds investing in securities of companies contributing in improving the quality of the environment.
- ESG (290): Environmental, social, and corporate governance funds investing in companies compliant with ESG criteria.

As showed in Figure 8 most sustainable funds are domiciled in Luxembourg or France. In fact, almost all funds domiciled in Luxembourg, as well as in Ireland, are offshore funds.

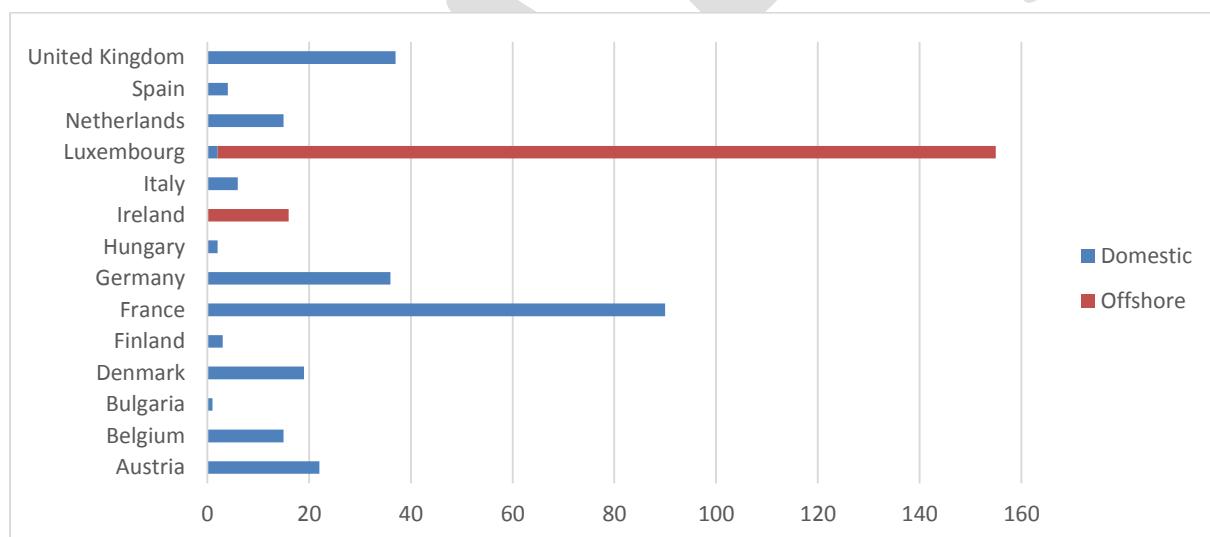


Figure 8 – Number of investment funds in each country for domicile type. Source: Bloomberg.

Figure 9 provides the distribution of total assets of sustainable investment funds based on asset classes⁵². Almost half of total assets is invested in equities. Figure 8 provides evidence of the heterogeneity in the asset allocation of sustainable funds by country of domicile. However, equities funds, fixed funds and mixed funds are the mainly classes characterizing the sustainable investment funds. The asset allocation in France is characterized also by a relevant share (more than 30%) of money market funds.

⁵¹ The Bloomberg Fund Classification System provides a fund classification grouping and compares funds with similar investment objectives. Bloomberg classifies funds based on public documents including prospectuses, fund fact sheets, and annual/semi-annual reports to determine the intended investment objective of the fund manager. The characteristics of the objective relate to both asset class specific dimensions (e.g., strategy, type of investment, etc.) and non-asset class specific dimensions (e.g. industry focus, geographic focus, general attributes, etc.).

⁵² See the definition of asset classes in Section 2.1.

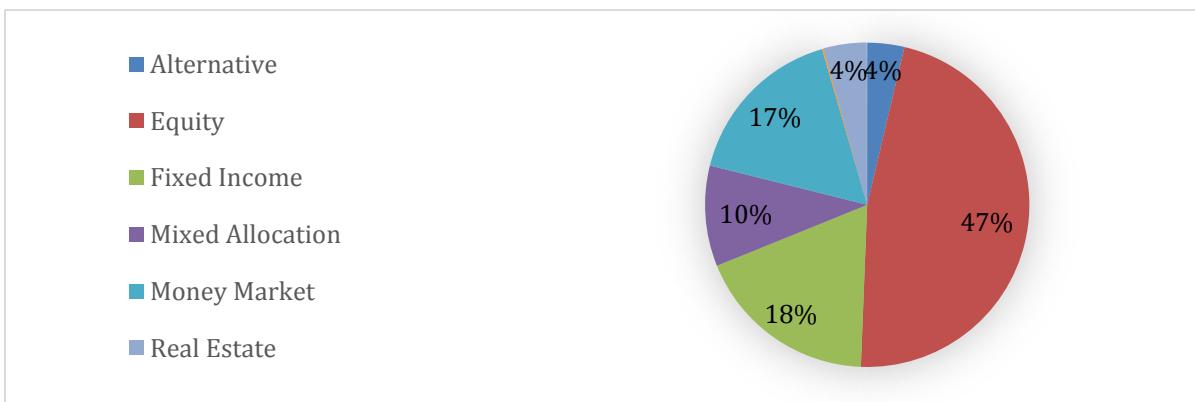


Figure 9 – Breakdown by asset class. Source: Bloomberg.

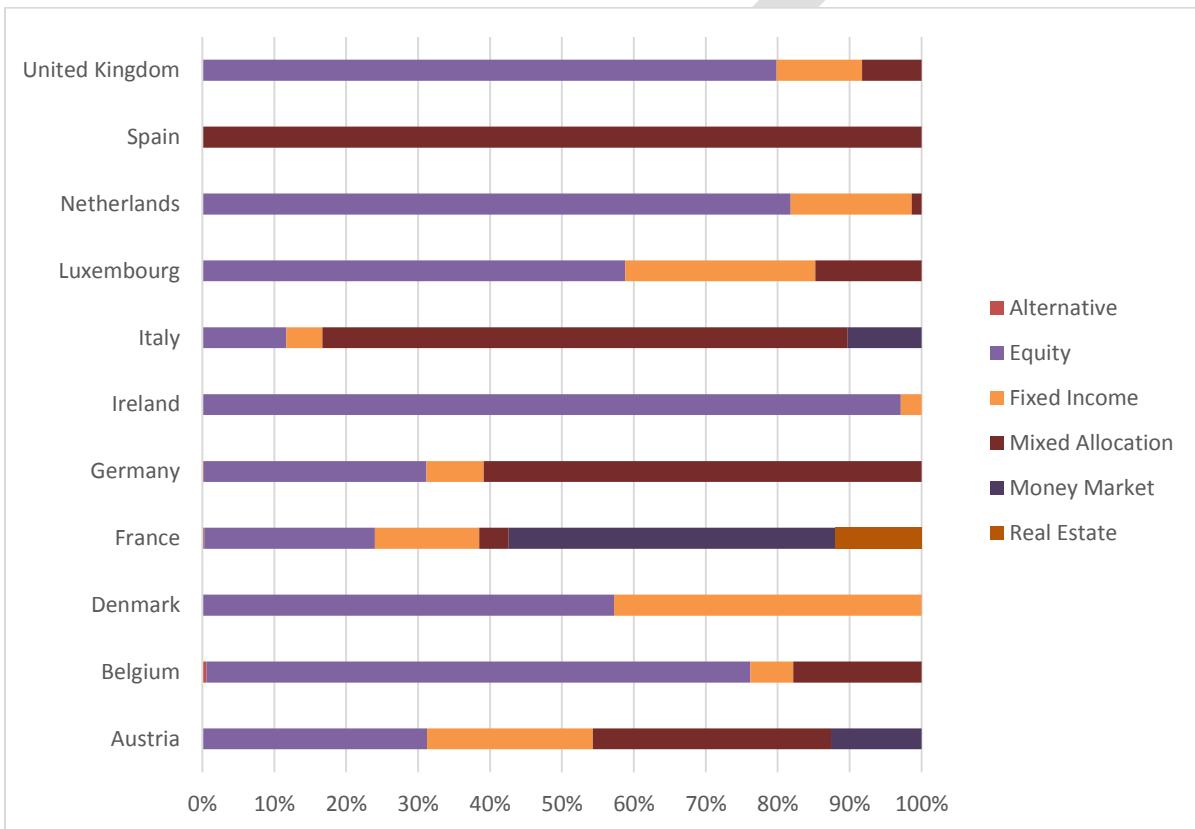


Figure 10 – Class of asset allocation of investment funds by country of domicile, for selected MS. Source: Bloomberg.

3.2.2 Life Insurance Products: unit-linked and index-linked plans

Life insurance products provide assurance on survival to a stipulated age only, assurance on death only, assurance on survival to a stipulated age or on earlier death, life assurance with return of premiums. Life insurance products offer a wide range of investments based on the following categorization:

- guaranteed return products (i.e., pure protection life insurance);
- non-guaranteed products linked to either (i) investment funds, i.e. unit-linked contracts, or (ii) structured products (mainly structured bonds), i.e. index-linked contracts;
- a combination of non-guaranteed and guaranteed return products.

Non-life and pure protection life insurances are excluded from PRIIPs. All non-guaranteed products and hybrid life insurance contracts are included in PRIIPs. As shown in Figure 11, France, the United Kingdom and Germany are the largest EU markets for insurance products. Figure 12 shows the distribution of total assets held by

insurers across countries, distinguishing between assets held for index- and unit-linked contracts and other contracts. In Luxembourg, the United Kingdom and Ireland index-linked and unit-linked contracts are more popular than other type of contracts, while they are less common in all other countries.

About 25% of the total insurers' investment is associated to index-linked and unit-linked contracts. The unit-linked contracts grew rapidly (15.2%) from 2015 and 2016. On the opposite, the non-linked contracts registered a sharp decrease in 2016.⁵³ As showed in Figure 13 65% of this is invested in UCITS.

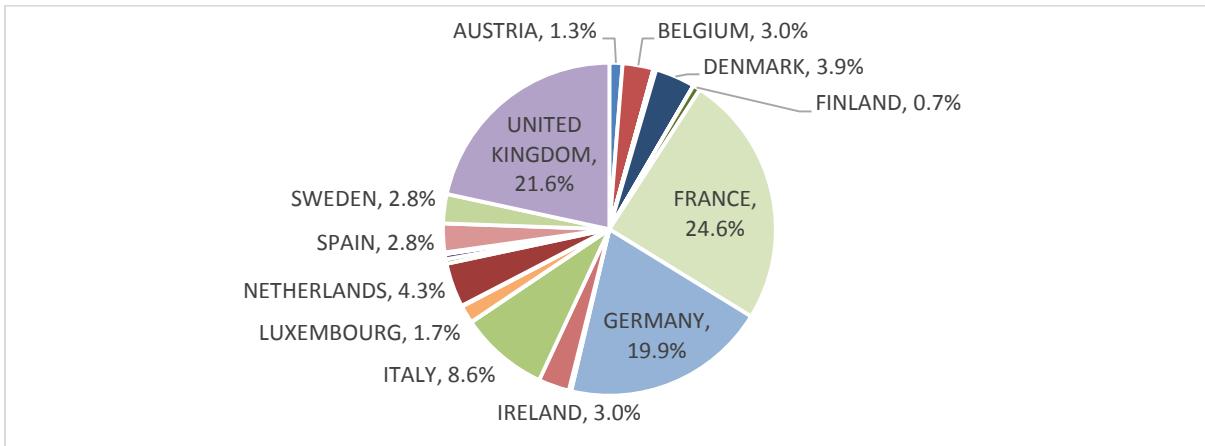


Figure 11 – Total of assets held by insurers, reported under Solvency II, per countries. Source: EIOPA Q1-2018.

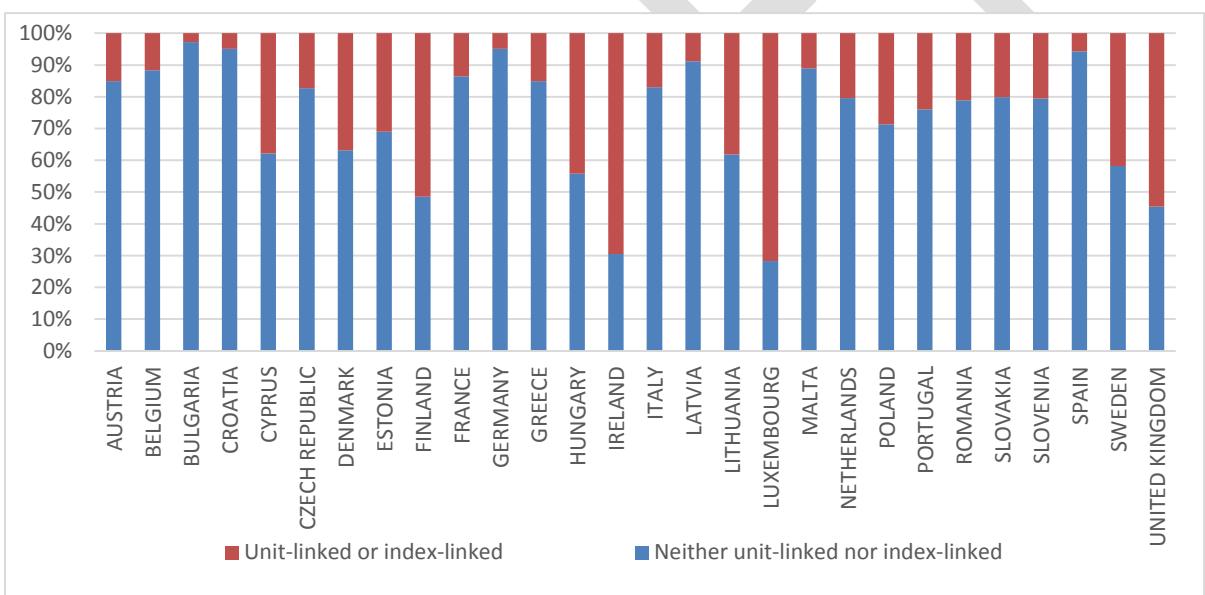


Figure 12 – Total of assets held by insurers and reported under Solvency II, distinguishing unit- and index-linked contracts and other contracts. Source: EIOPA Q1-2018.

⁵³ Source: www.insuranceeurope.eu.

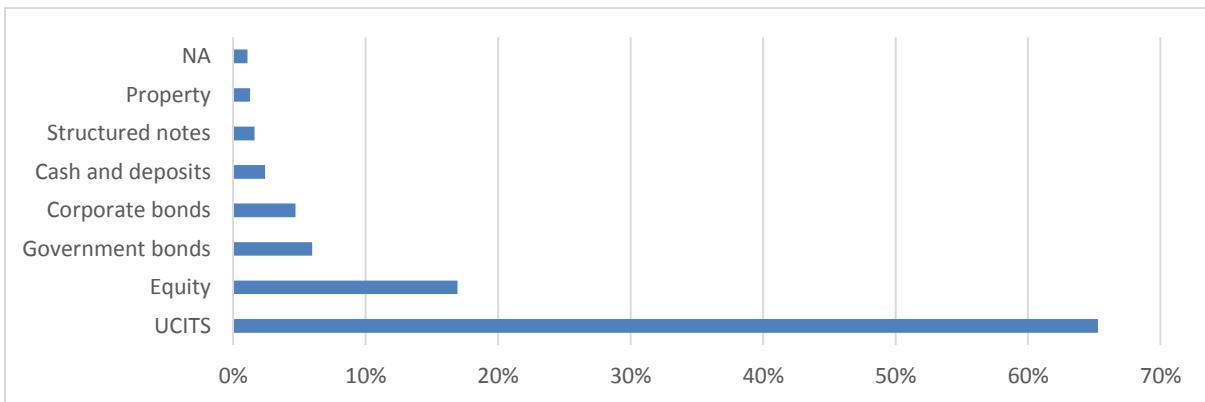


Figure 13 – Underlying assets of unit-linked and index-linked contracts.

The figure reports the percentage of the total assets held by insurers for unit- and index-linked plans. Source: EIOPA, Q1-2018, data covers the EU28.

3.2.3 Derivative Instruments

A derivative is a financial instrument whose value depends on (or derives from) the value of other, more basic, underlying assets. Financial derivatives are used for several purposes, including risk management, hedging, arbitrage between markets, and speculation. Derivative contracts are traded in the following markets:

1. Over-the-counter (OTC): these contracts are traded (and privately negotiated) directly between two parties, without going through an exchange or any other intermediary.
2. Exchange-traded-derivatives (ETD): standardized derivatives, e.g. linked to interest rates or indexes, are traded on exchange platform (Eurex, in the EU).

Derivative contracts can be classified as follows:

- Options: contracts which give the holder the right, but not the obligation, to purchase from or sell to the issuer of the option an asset at a predetermined price within a given time span or on a given date.
- Forwards: contracts under which two parties agree to exchange a specified quantity of an underlying asset at an agreed price (the strike price) on a specified date.
- Futures: similar to forward contracts, they are normally traded on an exchange.
- Swaps: contractual arrangements between two parties who agree to exchange, over time and according to predetermined rules, streams of payment on an agreed notional amount of principal. The most common types are interest rate swaps, foreign exchange swaps and currency swaps.

Derivatives can be linked to a financial or non-financial asset, to a group of assets or to an index. The main categories of derivatives with respect to the underlying assets are the following:

- Interest rate derivatives;
- Credit derivatives;
- Equity derivatives;
- Commodity derivatives;
- Foreign exchange derivatives.

Table 2 reports examples of the most common derivatives in the market, with an indication of their market share.

Table 2. Classification of the main derivatives w.r.t. the underlying^a.

Underlying	ETD		OTC		
	Futures	Options	Swap	Forward	Option
<u>Equity</u>	European Single Stock Futures traded on Eurex	Equity Options traded on Eurex (options on 750+ stocks, from 13 countries)	Equity swap	Repurchase agreement	Stock option

Underlying	ETD		OTC		
	Futures	Options	Swap	Forward	Option
<i>Transactions: 16.8mn Value: Euro 36tn</i>	Exchange (800+) <i>20% of transaction ETD</i>			<i>80% of transaction OTC</i>	
<u>Interest rate</u> <i>Transactions: 5.4mn Value: Euro 282tn</i>	EURIBOR future, EONIA future <i>6% of transaction ETD Counterparties: only between 50% EEA</i>	Option of EURIBOR future <i>6% of transaction ETD Counterparties: only between 50% EEA</i>	Interest rate swap <i>94% of transaction OTC Counterparties: 50% only between EEA</i>	Forward rate agreement <i>94% of transaction OTC Counterparties: 50% only between EEA</i>	Bond option
<u>Credit</u> <i>Transactions: 1.2mn Value: Euro 13.8tn</i>	Bond future (e.g., Corporate bond index future) <i>3% of transaction ETD</i>	Options on bond future. <i>3% of transaction ETD</i>	Credit default swap (CDS) <i>97% of transaction OTC Counterparties: only between 40% EEA</i>	Repurchase agreement <i>97% of transaction OTC Counterparties: only between 40% EEA</i>	Credit default option
<u>Foreign exchange</u> <i>Transactions: 6.5mn Value: Euro 112tn</i>	Currency Futures (e.g., EUR/CHF futures, EUR/JPY futures) <i>1% of transaction ETD</i>	Options on currency futures. <i>1% of transaction ETD</i>	Currency swap <i>99% of transaction OTC Counterparties: only between 40% EEA</i>	Currency forward <i>99% of transaction OTC Counterparties: only between 40% EEA</i>	Currency option
<u>Commodity</u> <i>Transactions: 5mn Value: 9.1tn</i>	Bloomberg Commodity Indexes (e.g., Bloomberg Energy Futures, Bloomberg Agriculture Futures) <i>54% of transaction ETD</i>	Weather options <i>54% of transaction ETD</i>	Commodity swap <i>46% of transaction OTC</i>	Commodity forward <i>46% of transaction OTC</i>	Gold option

^a Data on daily transaction of all derivative contracts open at the end of day (24 Feb 2014). Source: European Securities and Markets Authority (ESMA), Report on trends, risks and vulnerabilities 2017. Data used in the report are based on the mandatory reporting under EMIR and are aggregated across six trade repositories authorized in the EU.

3.2.4 Structured Products

Structured products are instruments whose pay-outs are linked to an exposure to reference values or the performance of one or more assets which are not directly purchased by the investor. Structured investments may be used as an alternative to, or to complement, equity investments. The main example of structured products is the convertible bonds, i.e. debt that could be converted to equity under certain circumstances, and other securities linked to derivatives. Figure 14 shows the top EU issuers of structured products.

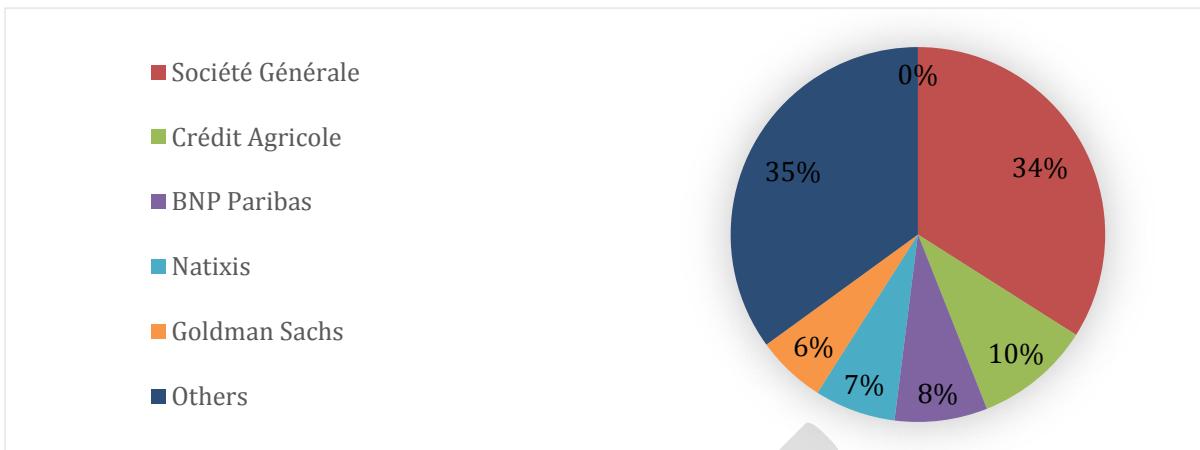


Figure 14 – Top European issuers of structured products. Market shares by volume. Source: structuredretailproducts.com

Most of the structured products consist of two components:

1. Basic financial instrument (e.g. bond),
2. Derivative (e.g. option).

Given their components, structured products are riskier than a government bond and less risky than derivatives. The payoff, risk-level and general characteristics of a structured product are determined from these two components. Structured products can be classified by payoff types, which refer to the strategy or return profile they expect to generate at maturity, by underlying instrument, by risk level or by market (i.e. OTC or organized markets). EUSIPA classified the structured retail products by risk level:

- Capital protected products: protect the initial investment at the maturity, and can also generate a return to the investor. These products (mostly) consist of a traditional bond plus an option.
- Yield enhancement products: provide a larger return than traditional bonds; however, the capital is not protected. These securities are linked to an underlying stock, index or a basket of securities. Most of these products have a predetermined limit on the return.
- Participation products: similar to yield enhancement products, but with no cap on the return.
- Leverage products: allow investors to participate in the performance of the underlying asset to an extent that is more than proportional to the changes in the underlying.

According to their underlying, structured products can be categorized as followed:

- Foreign Exchange linked structured products;
- Commodity linked structured products;
- Equity-linked structured products;
- Interest rate linked structured products;
- Hybrid-linked structured products;
- Credit linked structured products;
- Fund linked structured products;
- Inflation linked structured products.

Structured deposits are the combination of a deposit and an investment product. Thus, the return on a structured deposit depends on the performance of the underlying investment product. Structured deposits can be used as alternatives to cash deposits. Structured deposits “directly” linked to an interest rate index, such as EURIBOR or LIBOR, are excluded from PRIIPs. All other structured deposits linked to an underlying asset different from interest rates (e.g., equities, commodities, etc.) are PRIIPs.

3.3 Other financial instruments (Non-PRIIPs)

This section covers a set of non-PRIIPs which may be included in the scope of the EU Ecolabel, as evaluation criteria. Non-PRIIPs that could rather straight forwardly be covered by the EU Ecolabel are stocks, bonds and pension funds, because they are underlying assets of PRIIPs.

3.3.1 Stocks

A stock represents a fraction of the ownership of the corporation. Shares of an issuer can be traded on a stock exchange. For an overview of the European stock market, one can refer to the STOXX Europe Total Market Index (TMI), which includes 1235 companies and covers approximately 95% of the free float market capitalization⁵⁴. It includes large, mid and small capitalization companies from 17 European countries. In terms of sectoral composition, the most represented sectors are the manufacturing industry, with 35% of listed companies, and the financial sector, with about 17% of listed companies, as shown in Table 3. With respect to fossil-intensive sectors, i.e. 3.5% of listed firms are active in mining and quarrying, 4.2% in transportation and storage, while 3.3% in electricity, gas, steam, and air conditioning supply.⁵⁵ In terms of market capitalization, manufacturing firms have an overall capitalization of about EUR 12 tn, while financials market capitalization is around EUR 5 tn.

The eligibility criteria for the EU Ecolabel of a particular stock would be based on the composition of the business of the issuing company, in terms of ‘green’ economic activities, as defined by the EU Sustainability Taxonomy (see section 4.1.2)

Table 3. Classification of companies included in the STOXX Europe.

TMI based on activity sectors, defined as in Nomenclature statistique des activités économiques dans la Communauté européenne (NACE). Source: Bloomberg.

NACE categories	% of companies	Market Cap (EUR bn)
MANUFACTURING	34.90%	12,117
FINANCIAL AND INSURANCE ACTIVITIES	16.76%	4,828
INFORMATION AND COMMUNICATION	9.39%	1,607
REAL ESTATE ACTIVITIES	6.96%	635
WHOLESALE AND RETAIL TRADE; REPAIR OF MOTOR VEHICLES AND MOTORCYCLES	6.64%	902
TRANSPORTATION AND STORAGE	4.21%	788
CONSTRUCTION	3.72%	340
MINING AND QUARRYING	3.48%	743
PROFESSIONAL, SCIENTIFIC AND TECHNICAL ACTIVITIES	3.40%	553
ELECTRICITY, GAS, STEAM AND AIR CONDITIONING SUPPLY	3.24%	644
ADMINISTRATIVE AND SUPPORT SERVICE ACTIVITIES	2.11%	403
ACCOMMODATION AND FOOD SERVICE ACTIVITIES	1.70%	106
ARTS, ENTERTAINMENT AND RECREATION	0.97%	94
HUMAN HEALTH AND SOCIAL WORK ACTIVITIES	0.89%	94
AGRICULTURE, FORESTRY AND FISHING	0.73%	273
WATER SUPPLY; SEWERAGE, WASTE MANAGEMENT AND REMEDIATION ACTIVITIES	0.57%	31
OTHER SERVICE ACTIVITIES	0.16%	1
EDUCATION	0.08%	5
Total market capitalization		24,164

3.3.2 (Green) Bonds

A bond is a fixed income instrument that represents a loan made by an investor to a borrower (typically corporate or governmental). While all standard bonds could be suitable for the EU Ecolabel, based on the ‘greenness’ of the issuing companies, Green Bonds are a type of bonds that would be particularly relevant. During the last ten years, the green bond market has grown significantly and the value of issuances is about EUR 118 bn in 2018⁵⁶. However, the European green bond market is very small in size compared the market of conventional bonds, corresponding to approximately 1%⁵⁷.

⁵⁴ The free-float market capitalization is the share of a stocks’ total market capitalization that is available for trading and it is approximately EUR 8 tn (source: www.stoxx.com).

⁵⁵ Based on EUROSTAT data, utilities, infrastructure, transportation and construction accounted for 67% of total greenhouse gas emissions in the EU in 2015.

⁵⁶ Source: Report “The green bond market in Europe 2018” by Climate Bonds Initiative. See also Figure 15.

⁵⁷ Source: ICMA and Dealogic data.

Green bonds finance or re-finance in part or in full new and/or existing eligible green projects⁵⁸. One the relevant subgroups of the TEG on Sustainable Finance is preparing recommendations for an EU GBS, including an explicit definition of an EU green bond and the principles on which the process of project evaluation and selection is based.

Should the EU Ecolabel be extended to bonds, the work undertaken by the European Commission on the development on an EU green bond standard should be carefully considered in order to ensure consistency as far as possible. The ‘greenness’ of bonds should be evaluated according to criteria based on the EU taxonomy of economic activities.

In 2017, about 36% of the global amount of green bonds was issued by EU companies. The number of green bonds issued increased significantly over the last years, as shown in Figure 15. Green bonds can be issued by governments, financial institutions, or corporations. Figure 16 shows the breakdown by issuer type in the EU green bond market from 2012 to 2018. The European Investment Bank (EIB) was the first green bond issuer in 2007. The Nordic Investment Bank issues green bonds that invest in Northern European countries. The EIB and the Nordic Investment Bank are defined supranational authorities (SNATs) and the bonds issued by them enjoy a high credit rating. The amount of green bonds issued by SNAT is about EUR 5 bn in 2018. France is one of the earlier issuers of green bonds, it dominates the green bond market in Europe (about EUR 7 bn issued in 2018) and is the third largest globally. Nordic countries are the second largest European green bond market, with Sweden being the largest market among them. As shown in Figure 16, financial issuers have grown over time and currently account for slightly less than half of the total amount issued in 2018. Governmental issuers account for approximately one-third of the green bond market as of 2015.

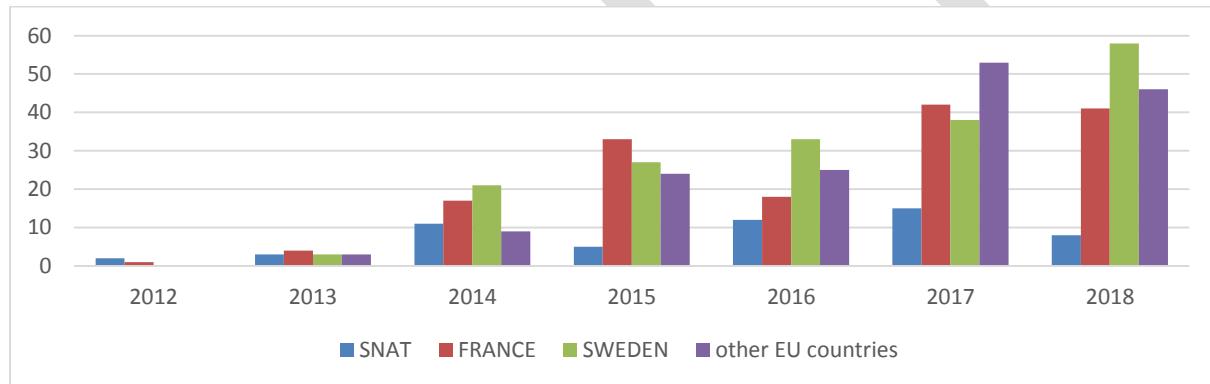


Figure 15 – Number of green bonds issued from 2012 to 2018. Breakdown by issuer country. Source: Bloomberg.

⁵⁸ See “Technical expert group on sustainable finance subgroup: EU Green Bond Standard (GBS)”, progress report, available at https://ec.europa.eu/info/publications/sustainable-finance-technical-expert-group_en.

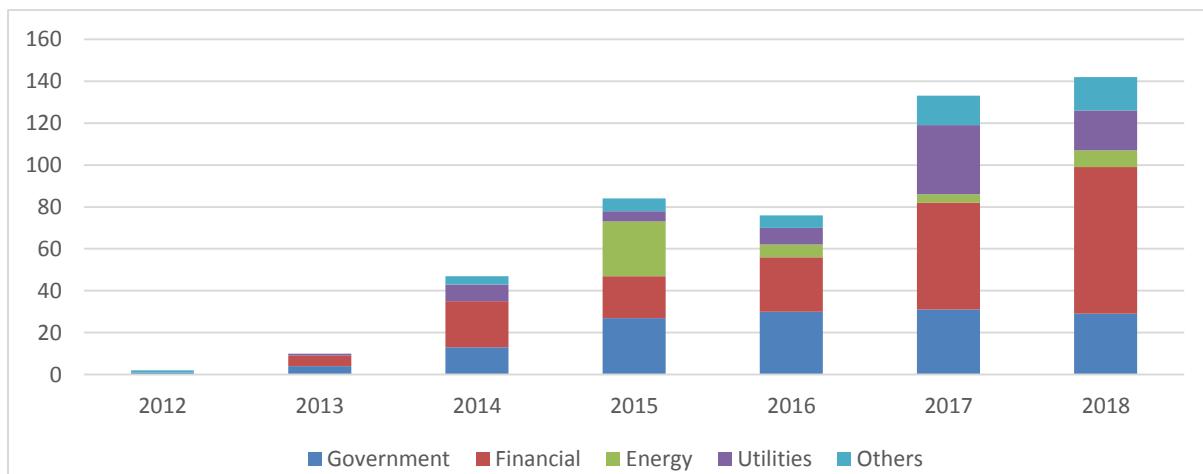


Figure 16 – Number of green bonds issued in EU countries from 2012 to 2018. Breakdown by Bloomberg Classification Industry Standard (BICS) of issuers. SNAT are excluded in this sample. Source: Bloomberg.

3.3.3 Pension Funds

A pension fund is a plan that provides retirement income. Pension funds are a complementary resource and do not substitute the public pension system. In the fourth quarter of 2016, the outstanding amount of pension entitlements was EUR 2,2 bn.⁵⁹

In analogy with unit-linked life insurances, unit-linked pension products include an investment fund component and therefore the latter falls under the PRIIPs regulation. These are products where the investment and protection components are combined, as a fraction of the premium is invested in stocks, UCITs, bonds, and other financial instruments.⁶⁰ As shown in Figure 18 pension fund managers invest mainly in government and corporate bonds (about 50% of their total assets) and in UCITS, (20% of assets).

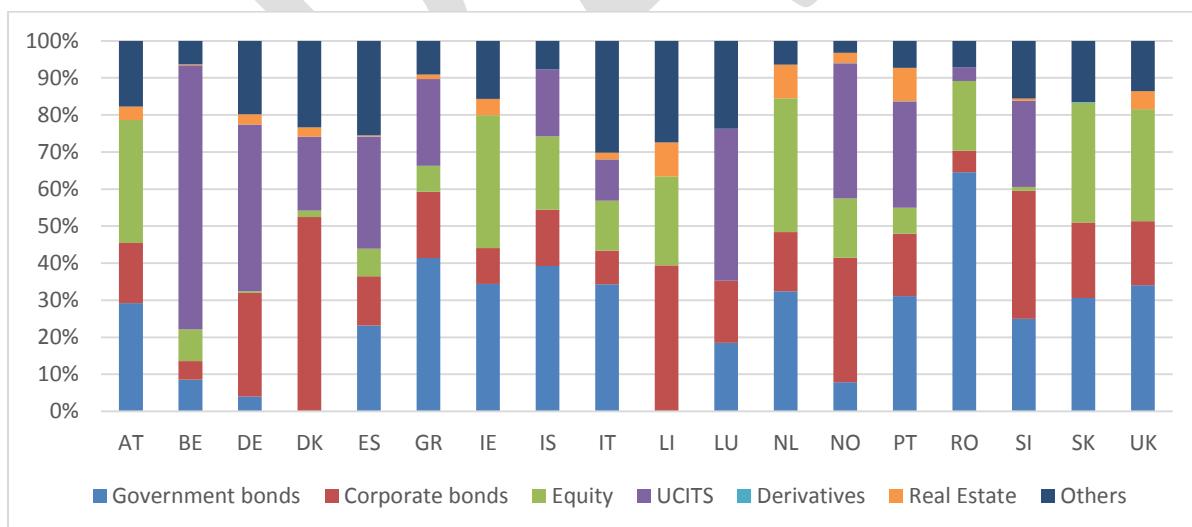


Figure 17 – Allocation of total assets held by pension funds. Source: EIOPA, 2016.

⁵⁹ Source: ECB press release on insurance corporations and pension funds, 2017.

⁶⁰ The data available from EIOPA do not distinguish between assets held for unit-linked plans and other plans.

3.4 The complexity of financial instruments

A relevant aspect in the context of the EU Ecolabel for financial products would be the degree of complexity of structure and underlying assets of the financial products in terms of verification. Complex products are characterized by complicated structures, involving for example the presence of underlying assets, or even multiple layers of underlying assets. There may be several underlying assets that are particularly difficult to verify because they cannot be directly related to specific economic activities or capital investments. Table 4 provides a schematic analysis of the structure of most common financial instruments. Based on the complexity of the instruments, one can identify the following classes:

- Bonds and stocks: they can act as primary financial assets or as underlying assets of more complex financial products. The level of "greenness" of stocks and bonds can be defined considering the business mix of the issuer company, also based on the information it discloses
- Investment funds: Two levels of analysis are involved in the assessment of the "greenness" of investment funds: the portfolio allocation of the fund and the measure of the "greenness" of each of the investee corporates. Moreover, among investment funds there are funds that are more complex and funds that are less complex. For example, a hedge fund or a fund of fund could invest in derivatives or other hedge/investment funds. In that case, in order to verify whether the fund is compliant with EU Ecolabel criteria, one should be able to assess the "greenness" of the underlying derivatives and of the underlying hedge/investment fund, respectively – which will be practically very difficult because of the short term and liquidity of this instrument.
- Unit-linked contracts: they are similar to investment funds, as their "greenness" can be defined based on the greenness of the underlying assets, or of the portfolio of the investment fund to which the product is linked.
- Derivatives, structured products and structured deposits: these instruments can become very complex, as they are constructed based on one or multiple underlying layers. In the simplest cases, the "greenness" of these products would reflect the greenness of the underlying assets. However, for most derivatives and structured products their verification would be very challenging.

Table 4. Analysis of financial instruments based on their level of complexity.

Financial instruments in bold are those for which setting EU Ecolabel criteria would be more straightforward.

Base Instruments:		Underlying assets:	
level 0	level 1	level 2	level 3
<i>Primary financial assets</i>			
Cash, Deposit account			
Bonds:			
Government bonds			
Corporate bonds			
Stocks			
Investment funds:			
Equity funds	Stocks		
Fixed income funds	Bonds		
Hybrid funds	Stocks and bonds		
Money market funds	Short-term debt securities, i.e. government bonds		
Real estate funds	Real estate		
Commodity funds	Commodities		
ETF	Stocks, bonds, commodities		
Hedge funds	Stocks, bonds , commodities, currency, futures*, options*, swaps*	* underlying of derivatives	
Fund of funds	Investment funds	asset allocation of the fund: stocks, bonds, hedge funds**	** asset allocation of hedge funds
Unit-linked contracts	Investment funds, stocks, bonds	asset allocation of the fund: stocks, bonds, etc.	
Index-linked contracts	Structured product***	***underlying of the structured product	
Derivatives:			
Options	Equity, Interest rate, credit, foreign exchange, commodity		
Futures	Equity, Interest rate, credit, foreign exchange, commodity		
Forwards	Equity, Interest rate, credit, foreign exchange, commodity		
Swaps	Interest rate swap, currency swap, equity swap, credit default swap (CDS)		
Options on futures	Future contract	Equity, Interest rate, credit, foreign exchange, commodity	

Base Instruments:	Underlying assets:		
level 0	level 1	level 2	level 3
<u>Structured products:</u>			
Foreign Exchange linked	Currency		
Commodity linked	Commodities		
Equity-linked	Share linked (single equity) or index linked (basket of shares)		
Interest rate linked	Interest rate		
Hybrid-linked	Currency, commodity, equity		
Credit linked	Debt instruments (e.g., Credit default obligations)		* underlying of derivatives
Fund linked	Hedge funds	Stocks, bonds, commodities, currency, futures*, options*, swaps*	
Inflation linked	Inflation rates		
Structured deposits	Equity, index of equities, commodity, interest rates, bond, currency or a combination of these investment products.	<i>Deposit + Investment product = Structured deposit</i>	

3.5 Conclusions

The scope of the Ecolabel criteria should be based on considerations of different nature. Based on the design and purpose of the Ecolabel, which intended to support investors in their decision-making process, it makes sense to include in its scope those financial products that are intended to be sold to retail clients. A natural starting point would be PRIIPs.

A second element that should be taken into account is the relevance of the Ecolabel within the reference product class. In other words, it is important not to target niche markets and instead seek to promote green finance. In this respect, investment funds, unit-linked life insurance products and pension funds taken together account for a large part of the PRIIPs market.

A third consideration relates to the need to maintain a level playing field across product categories, avoiding that particular products may derive an advantage from being included in the scope of the Ecolabel, compared to competing products that are excluded from the scope.

A fourth point relates to the feasibility of setting verifiable EU Ecolabel criteria for particular product categories. In this respect, derivatives and structured products are in most instances too complex to verify and in fact as underlying assets, it will be difficult to relate them to economic activities or capital investment.

Finally, consistency across various EU regulations should be ensured. In this respect, the development of an EU GBS shall be taken into account. At the same time, the inclusion of bonds as such in the scope of the EU Ecolabel for bonds as such needs to be considered carefully so as to avoid that the EU Ecolabel and the GBS became competing frameworks..

4. TECHNICAL ANALYSIS

An EU Ecolabel focusing on requirements relating to environmental sustainability issues but also taking into account social and governance issues could ensure that issuers consider these factors in a uniform manner in their investment decision process and minimise the risks of greenwashing for clients. Initial evidence suggests that a range of strategies^{61,62} are employed in order to make portfolios more attractive to customers seeking green or environmentally sustainable financial products. These strategies include but are not limited to community investing, sustainability-themed investing, corporate engagement, ESG, and exclusionary screening. These approaches are embedded in the criteria of some existing regional schemes and labels (see Chapter 2). In addition, fund managers may also take a positive approach to the identification of green sectors or economic activities, possibly with reference to screening criteria or a Taxonomy. This section introduces each of the main taxonomies adopted by regional and national labels and schemes, and identifies the sustainable investment strategies prevalently applied by fund managers.

4.1 Taxonomy

Taxonomy is a classification system that categorizes different economic activities and provides criteria as to what an environmentally sustainable economic activity is.

4.1.1 Summary of the existing taxonomies

The concept of taxonomy is embedded within green finance, which has been defined as "*financing of investments provided for economic activities that provide environmental improvement, climate change mitigation and more efficient resource utilization benefits in the broader context of environmentally sustainable development*". These economic activities could be projects or activities in specific economic sectors of any economy in areas such as renewable energy, green transportation or green buildings amongst others.

The existing labels and certification schemes available in Europe for sustainable finance (see Chapter 2) certify the "greenness" of financial products using one of the three commonly available taxonomies. These include:

- The GBP of the International Capital Markets Association (ICMA)
- The Climate Bonds Taxonomy of the Climate Bonds Initiative (CBI)
- The International Development Finance Club (IDFC) taxonomy

4.1.1.1 The Green Bond Principles Taxonomy

The GBP (see Chapter 2) is an industry-led initiative, which offers a voluntary and process oriented guideline for evaluating the best practice with reference to the use of proceeds, processes for project evaluation and selection, management of proceeds and reporting on use of proceeds. The GBP explicitly recognises several broad high-level project categories of eligibility for green projects that may be included in a fund, which contributes to environmental objectives such as:

- climate change mitigation
- climate change adaptation
- natural resource conservation
- biodiversity conservation
- pollution prevention and control

⁶¹ Inderst, Georg; Stewart, Fiona Elizabeth. 2018. Incorporating environmental, social and governance factors into fixed income investment (English). Washington, D.C. World Bank Group. <http://documents.worldbank.org/curated/en/913961524150628959/Incorporating-environmental-social-and-governance-factors-into-fixed-income-investment>

⁶² The Principles for Responsible Investment.2013. Building the capacity of investment actors to use environmental, social and governance (ESG) information. Available from: <https://ec.europa.eu/docsroom/documents/21441/attachments/1/translations/en/renditions/pdf>

4.1.1.2 The Climate Bonds Initiative

The Climate Bond Initiative (CBI) (see Chapter 2) is a climate-focused standard and certification scheme with performance-based minimum standards for a broad range of sectors. These minimum standards define green economic sectors or activities within a predefined taxonomy that is continuously being revised. The taxonomy of the CBI is designed principally to certify climate and green bond issuances and possess three levels, with additional sector-specific eligibility criteria. Within the CBI definitions, a number of sectors which do not qualify as "green" are also listed. Specifically the taxonomy lists the following eight eligible sectors:

- Energy
- Building
- Industry
- Waste, pollution control and sequestration
- transport
- Information Technology and Communications
- agriculture and forestry
- adaptation

Further "areas" (e.g. solar energy), "specific categories and activities" (e.g. "PV solar electricity") and descriptions are provided for each of the broad sectors provided above, or are currently under development.

4.1.1.3 International Development Finance Club (IDFC) taxonomy

The International Development Finance Club (IDFC)⁶³ taxonomy presents a list activities, categories, associated sub-categories as well as accompanying examples that are eligible for classification as climate finance activities which are defined as activities related to mitigation and adaptation of climate change or cross-cutting activities according to the classification defined under the Common Principles for Climate Mitigation Finance Tracking. The IDFC taxonomy classifies any activity climate change mitigation related as long as it encourages the reduction of GHG emissions or enhances carbon sequestration. Also available within the taxonomy is a list or categories of activities that are eligible for climate change adaptation finance. The taxonomies included in the IDFC Common Principles for Climate Mitigation Finance Tracking (see Table 5) possess a high level of detail and are up to three levels.

Table 5. Climate change categories in the IDFC Common Principles for Climate Mitigation Finance Tracking Taxonomy

Mitigation	Adaptation
Renewable energy	Water and wastewater systems
Lower-carbon and efficient energy generation	Crop production and food production
Energy efficiency	Other agricultural and ecological resources
Agriculture, forestry, land-use	Industry, extractive industries, manufacturing and trade
Non-energy GHG reductions	Coastal and riverine infrastructure (including built flood protection infrastructure)
Transport	Energy, transport and other built environment and infrastructure
Waste and wastewater	ICT
Low carbon technologies	Financial services
Cross cutting issues	Institutional capacity support or technical
	Cross cutting sectors

⁶³ <http://www.worldbank.org/en/news/feature/2015/04/03/common-principles-for-tracking-climate-finance>

4.1.2 The EU Taxonomy⁶⁴

The EU-wide classification system, or EU Taxonomy (see section 1.1), which will provide businesses and investors with a common language to identify which economic activities can be considered environmentally sustainable or not, for the purposes of establishing the environmental sustainability of an investment is being developed as a part of the Action Plan of the Commission⁶⁵.

The EU Taxonomy is not a mandatory list to invest in. It is also not a standard, nor an exclusion list. It does not harmonise the existing market practices and strategies with regards to sustainable finance. A key expectation is that the EU Taxonomy would address the complications created by “greenwashing” and confusing fragmentation within the financial sector which undermines investors' confidence.

Under the Commission's proposal for a sustainability classification system, for economic activities to qualify as environmentally sustainable, they would have to fulfil the following requirements:

- contribute substantially to at least one of the six environmental objectives⁶⁶ articulated within the Action Plan, comply with Technical Screening Criteria
- not significantly harm any of the other environmental objectives
- comply with Minimum Social Safeguards

The EU Taxonomy is expected to be applied by financial market actors involved in the manufacture and distribution of all types of financial products, and also by EU Member States setting out national rules on labelling investment products. As the EU Taxonomy will only contain activities that contribute substantially to environmental objectives i.e. “green”, some activities might be included in it. However, the activities which are excluded are not necessarily considered “brown” i.e. having a significant negative impact on the environment. They are simply not categorized. The EU Taxonomy will also include activities in economic sectors that have an impact on the environment as long as they manage to reduce their impact substantially. This will enable polluting sectors to transition and move onto greener pathways.

An EU Taxonomy would be the reference point for an EU label for green financial products. Green financial products obtaining the EU Ecolabel would need to select their investments included in their portfolio on the basis of green activities listed in the EU Taxonomy. The framework established by the EU Taxonomy Proposal should be used as guidance in the development of the EU Ecolabel criteria, and the link with the EU Taxonomy would be established by taking a “look-through” approach for the development of the EU Ecolabel criteria which entails assessing (as one of the many requirements that must be fulfilled before a financial product can be awarded the label), if the assets underlying such products are linked to environmentally sustainable economic activities, as established under the EU Taxonomy (see Figure 20).

⁶⁴ <http://ec.europa.eu/transparency/regdoc/rep/1/2018/EN/COM-2018-353-F1-EN-MAIN-PART-1.PDF>

⁶⁵ Communication from the Commission Action Plan: Financing Sustainable Growth (COM(2018) 97 final). Available from: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52018DC0097>

⁶⁶ The six environmental objectives as defined in the proposed regulation are: (1) climate change mitigation; (2) climate change adaptation; (3) sustainable use and protection of water and marine resources; (4) transition to a circular economy and waste prevention and recycling; (5) pollution prevention and control; and (6) protection of healthy ecosystems

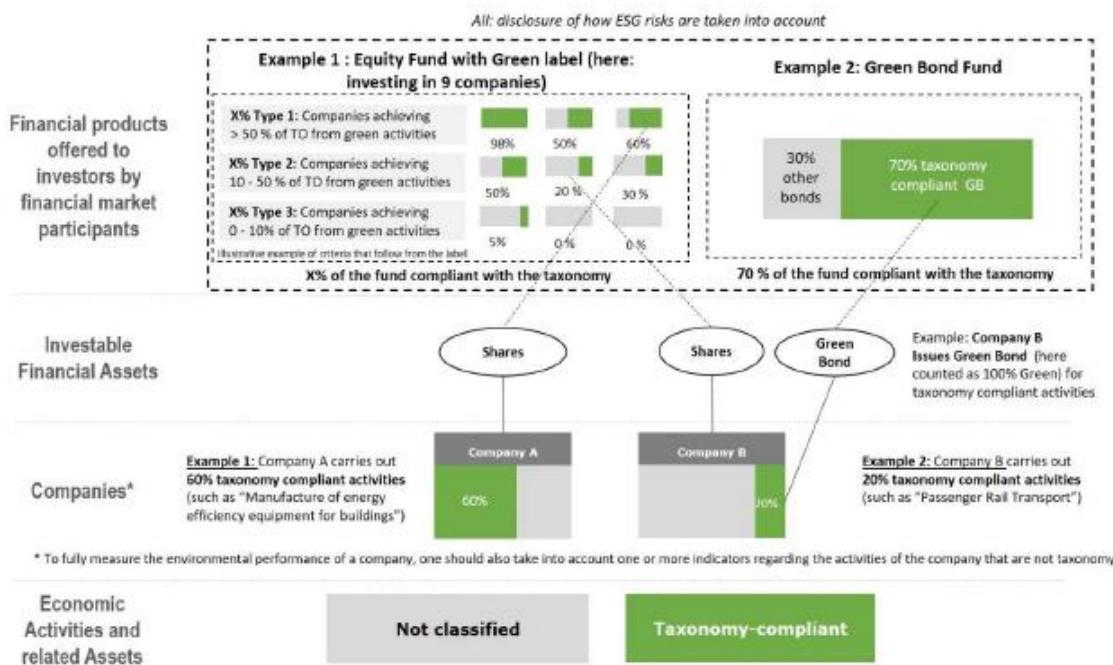


Figure 18⁶⁷ - Linkages between the EU Taxonomy and the green investing

4.1.3 Analysis of existing taxonomies and application in existing labels

An examination of the three main taxonomies, the CBI, the GBP project categories and the IDFC indicates that there are differences in the manner the taxonomies have been defined— as an example, the ICMA GBP provides guidance on high-level or otherwise broad categories of potentially eligible green projects but it does not define the type of projects under the general categories that could qualify as “green”. Instead it refers to other independently developed standards and criteria for guidance on defining eligible green projects. However, the CBI project categories are linked to detailed qualification criteria⁶⁸, and it is reportedly the only current industry effort that provides a detailed definition of “green” within each of the broader asset categories provided by the GBP project categories.

The CBI, the GBP project categories and the IDFC taxonomy are employed in a number of national and regional labelling initiatives for financial products as shown in Table

Table 6. Taxonomy of regional and national labels and schemes

Financial Label	Taxonomy
TEEC Label	Adaptation of the Climate Bonds Initiative taxonomy
FNG Siegel	Climate Bonds Initiative
Nordic Swan Ecolabel	ICMA's GBP
Luxflag Climate Finance Label	IDFC
Austrian Ecolabel	Do not mention a specific taxonomy but outline criteria which include exclusion and restricts investments in certain economic sectors based on specified social and ecological standards

⁶⁷ Illustrative example and does not pre-empt any policy decision by the commission on labels and schemes.

⁶⁸ https://www.bourse.lu/sustainability_standards_and_labels

4.2 Sustainable Investment Strategies

A range of strategies are available and currently being applied in the financial sector to ensure investment in assets and projects that have a positive impact in terms of mitigating climate change and contributing to the Paris objectives. The main sustainable investment strategies applied in Europe are reviewed in the following section.

4.2.1 Exclusion

Exclusions otherwise known as negative screening is one of the most common strategies for defining what is green or environmentally sustainable. It entails the restriction of companies or sectors from their portfolio based on one or a number of ESG attributes. There are several forms of exclusions. Value-based exclusion criteria are those used to make decisions based on investors' own values. They include for example when considering the environmental aspects, the exclusion of chlorine-based chemicals and agrochemicals, genetic engineering and biocides, etc. However, the necessity of monitoring the portfolio as different exclusions can have very different impacts on investment strategies has been pointed out.⁶⁹

Available information indicates that negative screening (exclusion) is currently the dominant strategy applied of the total European professionally managed assets with a growth rate of around 48% between 2014 and 2016.

4.2.2 Positive screening or best-in-class approach

Alternate to negative screening is the positive screening or best-in-class approach. This consists in choosing the companies which are rated or evaluated as having the best ESG score in a particular sector. This approach does not lead to the exclusion of economic sectors or industries, such as tobacco or mining, but instead invests in the companies that have the best performance in terms of meeting the ESG criteria that are relevant for their respective industries. This approach makes it difficult to compare performances across differing sectors (for example when an oil exploration company is compared against an information technology company).

Best-in-class investments are increasingly becoming popular in Europe. Investment in leading companies deploying the strategy grew from approximately EUR 58 billion to nearly EUR 500 billion between in 2005 and 2015⁷⁰. However, this growth represents roughly about 4% of the all the total strategies employed in Europe.

4.2.3 Norms-based screening

The norms based screening approach entails the screening of investments of business practice against international/global norms such as environmental protection, human rights, labour standards, and anti-corruption. These norms or standards are publicly available in international initiatives and guidelines such as the Kyoto Protocol⁷¹, OECD Guidelines for Multinational Enterprises⁷², the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy⁷³, and the UN Global Compact⁷⁴ amongst others.

According to the Global Sustainable Investment Alliance⁷⁵, the norms-based screening is the second most dominant investment approach in Europe with over \$5.55 trillion in assets, and a growth rate of 40% between 2014 and 2016.

⁶⁹ Schroders 2017. Demystifying negative screens: The full implications of ESG exclusions

December 2017. Available from: <https://www.schroders.com/el/sysglobalassets/digital/insights/2018/thought-leadership/demystifying-negative-screens---the-full-implications-of-esg-exclusions.pdf>

⁷⁰ <https://www.statista.com/statistics/425765/socially-responsible-investments-europe-best-in-class/>

⁷¹ <https://unfccc.int/process/the-kyoto-protocol>

⁷² <http://www.oecd.org/investment/mne/1922428.pdf>

⁷³ <https://www.ilo.org/empent/areas/mne-declaration/lang--en/index.htm>

⁷⁴ <https://www.unglobalcompact.org/>

⁷⁵ http://www.gsi-alliance.org/wp-content/uploads/2017/03/GSIR_Review2016.F.pdf

4.2.4 ESG integration

The methodological and explicit inclusion of information on material ESG factors into financial analysis by investment managers in decision making is known as ESG integration. This is hinged on the premise that sustainability can have a material impact on companies' performance. Therefore, materiality is a key component of the ESG integration. ESG integration entails an initial assessment of a variety of sustainability information, to determine which ESG information is financially relevant. If they are found relevant, they are then considered during the assessment of the corporate performance and investment performance. However it has been noted that the approach is very difficult to assess due to several issues including too many unknown variables which significantly influence the practices of integration.

Globally the integration of ESG factors is the second largest investment strategy, and although it exhibited an overall growth rate of 39.3% between 2014 and 2016, it was deployed in only 12% of the invested assets in Europe in 2016, and according to the HLEG Report⁷⁶ despite their rapid growth, ESG funds represent less than 2% of the overall European retail funds market.

4.2.5 Sustainability themed investing or thematic investing

Sustainability themed investment strategy encompasses a variety of subjects which enables investors to select investment in any number of topics closely linked to sustainability or sustainable development (e.g. clean energy, sustainable transportation, land use, etc.). This strategy is growing very fast in Europe, as although it contributed only 1% of the total assets invested in 2016, it experienced a growth rate of 146% between 2014 and 2016, second only to the impact investing strategy.

4.2.6 Impact/community investing

Impact investing refers to investments made into companies, financial assets and sectors of the economy aimed at promoting specific positive social or environmental benefits to the community in tandem with the financial returns expected from the investments. Impact investing is the fastest growing strategy in Europe. Although the assets employing this strategy is small (\$107.2 billion), between 2014 and 2016 it experienced a growth of 385%.

4.2.7 Corporate engagement and shareholder action

According to the GSIR 2016, this strategy "relies on the participation of corporate stakeholders to deploy their shareholder power to influence corporate behaviour, including through direct corporate engagement (i.e., communicating with senior management and/or boards of companies), filing or co-filing shareholder proposals, and proxy voting that is guided by comprehensive ESG guidelines".

4.3 Green Investment Definition

Although numerous definitions abound, "green" finance (also often used interchangeably with green investment) is generally associated within the financing of investments that provide environmental benefits. Furthermore, green investment has also been defined as the investment needed to enable a reduction in GHG and air pollutant emissions, without crucially reducing the production and consumption of non-energy goods⁷⁷. Summarily, financial products or investments in themselves cannot be green. Greenness is derived from the uses to which they are being put in underlying assets or activities.

The prevailing and overlapping concepts of "green" are developed around three main types of investment strategies:

⁷⁶ Financial Stability, Financial Services and Capital Markets Union. 2018. Final report of the High-Level Expert Group on Sustainable Finance. Available from: https://ec.europa.eu/info/publications/180131-sustainable-finance-report_en

⁷⁷ Eyrard, L et al., 2011. Who's going green and why? Trends and determinants of green investment. IMF Working Paper, International Monetary Fund, Washington D.C.

- Socially-responsible investing (SRI)
- Environmental, social and governance (ESG) investing
- Impact investing

In SRI, the approach is usually to avoid investments in industries through negative screening according to some defined ethical guidelines. Impact investing on the other hand entails investing in projects or companies with articulated interest in attaining social or environmental change. The third concept which is commonly applied globally is the ESG investing. This is essentially integrating ESG factors into fundamental investment analysis so that they in effect are able to impact investment performance⁷⁸. Green investments can also be based or defined using a number of other sustainable investment strategies such as exclusion (also known as divestment approaches), best-in-class approach, etc., as explained in section 4.2.

The review of the labels and schemes (see section 2.2) indicates that most of them consider green a sub-set of ESG, SRI, Impact investing or any other overarching strategy that they employ. This is because although they appear to be thematic due to the use of taxonomies to define environmentally sustainable economic activities, and stipulating requirements on impact reporting which are linked to climate change mitigation reporting, some of them also require the incorporation of ESG standards in the investment process. In addition, they also have criteria which limits investments in economic activities or sectors not deemed environmentally sustainable through negative screening.

The collection of all the products or services offered by any organization or company is termed the product portfolio. In the financial industry, an investment portfolio is a commonly applied terminology which encompasses assets such as stocks, bonds, cash and real estate, amongst others. The most common asset classes in any portfolio are equities (stocks), fixed-income securities (bonds), real estate, and cash equivalents and the share/proportion of each asset class in a portfolio is the asset allocation of that portfolio. These could be directly or indirectly invested.

Various forms of metrics have been developed and are available in the industry for defining "greenness". Some of these take the form of thresholds where a specific proportion (in percentage) of a portfolio's total assets under management is required/mandated to be invested in climate change mitigation and/or climate change adaptation activities. For example, the LuxFLAG Climate Finance Label is a certificate for funds that invest at a minimum, 75% of their total assets in projects with a clear link to climate change mitigation and/or climate change adaption activities as well as other interlinked operations. Activities deemed as climate change mitigation and adaptation of climate change or cross-cutting activities are defined and listed in the IDFC Taxonomy. .

The share of companies based on the percentage of revenues of the company(s) that can be attributed to "green" activities by assessing to what degree (quantified as a percentage), the company engages in sustainable economic activities using clearly identified taxonomies⁷⁹ is also employed in practice to define 'greeness'. As an example, a company with 65% of return on revenue from environmentally sustainable activities, could be deemed as 65% environmentally sustainable.

Green investment financing could also take the form of making financing available for companies whose revenues are generated largely from green/neutral activities. To be eligible, companies need to generate a certain percentage of their revenues from environmentally friendly activities. The cut-off point varies widely. Although some green equity indexes do not specify any green revenue threshold, others range from 20% - 50% depending on the rating agency⁸⁰

Depending on the financial actors (banks, associations, institutional investors, etc.), various definitions of greenness exist. As detailed in Chapter 2, the available national labels and certification schemes for financial products also apply different criteria to certify the "greeness" of financial products. As an example, the Dutch Green Funds Scheme awards green certificate to projects that demonstrate environmental benefits in at least

⁷⁸ Commonfund. 2013. From SRI to ESG: The Changing World of Responsible Investing. Available from: <https://files.eric.ed.gov/fulltext/ED559300.pdf>

⁷⁹ 2degrees-investing (April 2016), Measuring progress on greening financial markets - briefing note for policymakers. <http://degreesilz.cluster023.hosting.ovh.net/wp-content/uploads/2017/04/Measuring-progress-on-greening-financial-markets-briefing-notes-for-policymakers-2016.pdf>

⁸⁰ Kahlenborn et., al., 2017. Defining green in the context of green finance. Available from: <https://vfu.de/ressourcen/sustainable-finance-dossiers/dossie-sfs/kahlenborn-2017-defining-green-in-the-context-of-green-finance.pdf>

one of a number of categories, which together provide a comprehensive overview of "green". These categories include activities such as nature conservation, organic farming, sustainable agriculture, waste management and recycling, renewable energy, energy efficiency, sustainable building, sustainable mobility, sustainable water management and climate change adaptation⁸¹. This approach is similar to that employed adopted in the banking industry where financing is provided to projects deemed as contributing to a shift towards more sustainable infrastructure, cleaner energy supply, clean air, etc. Some financial institutions, in addition to mandating compliance to these banks' overall green objectives, set requirements on the minimum proportion of investment to be fulfilled to qualify. As an example, the EIB requires at "*least 25% of its investments are committed to climate change mitigation and adaptation annually invested goals*"⁸²

These approaches to defining/identifying "greenness" are not mutually exclusive as investors often use a combination of different green and ESG approaches. A combination of ESG integration, screening and corporate engagement and shareholder action, is commonly employed in and can be described as a "*form of ESG or green overlay in the general investment process*" that allows investors to select the most sustainable industries or companies, exclude "dirty" companies and/or motivate "polluters" to improve their ESG performance over time. These investment strategies are quite popular and have very high market shares compared to other investment strategies as shown in Figure 19.

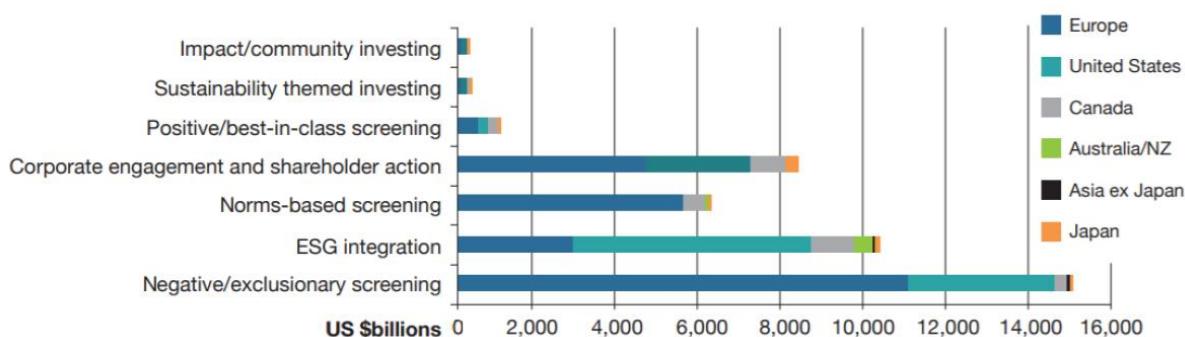


Figure 19 – Sustainable investment strategy by assets and region (Kahlenborn et. al., 2017)

Impact investing and green themed investing can provide important information for the definition of green. However, their share in the market is extremely low.

The "greeness" of investments can also be established across different asset classes (equities, bonds and alternative investments) with the objective of differentiating the "greeness" of entire asset classes so that investment policies can be amended.

Interest in this form of green investment, practiced through green private equity and infrastructure funds, has grown in renewable energy or clean technology companies over the years. However, there appears to be no consistent definition of what is "green" nor are green investment policies applied uniformly to all asset classes.

The main "green" asset classes currently available in the European market are equities and bonds⁸³. Term loans, mainly infrastructure and real estate complement these. However, other classes such as structured equity and bond investment solutions (e.g., green repacking and equity-linked), securitisation and revolving credit facilities which integrate ESG factors in their margin grids are developing. Equity funds take the largest share of European green funds (around 85% by number and volume). However, the market is gradually diversifying into bonds and has recorded a three-fold increase in the bond fund segment since 2015. Therefore,

⁸¹ Netherlands Enterprise Agency (2018). Green Project Categorization. <https://www.rvo.nl/subsidies-regelingen/regeling-groenprojecten/voorwaarden-regeling-groenprojecten/projectcategorie%C3%ABN>

⁸² EIB: Climate and environment for everyone's future, <http://www.eib.org/en/projects/priorities/index.htm?f=search&media=search>

⁸³ Novethic, 2017. The European green funds market. Available from: https://www.novethic.com/fileadmin/user_upload/tx_ausnovethicetudes/pdf_syntheses/Green-funds-study-Novethic-Ademe-2017.pdf

green bond funds are products whose environmental nature are easy to explain and because they also clearly - identified projects, they are also much easier to sell⁸⁴.

The definition of greenness is also available from rating agencies or indices such as MSCI, Nasdaq, etc. These organizations provide investment managers and asset owners with a benchmark (known as an index or rating) which are meant to help them in identifying and making active investment decisions. It is believed that such green indices or environmental rating systems that incorporate an environmental component can increase visibility into the relationship between environmental and financial performance, as well as incentivising environmental responsibility.

However, as the available equity indices employ varying methodologies, definition, composition, and coverage. In addition, their selection and weighting of the index constituents also differ with three basic approaches being applied – screening, best in class and reweighting as presented in Table .

Table 7. Green equity indices and selection approaches (non-exhaustive)

	RI / SRI / ESG/ SI	Green thematic	Sectors	Carbon related
FTSE	FTSE4Good Series ¹	FTSE Environmental Market ¹		FTSE CDP Carbon Strategy ³
Dow Jones	DJ Sustainability ²			
S&P		S&P Eco	S&P Clean Energy, Alternative Energy	S&P Carbon Efficient ³
MSCI	MSCI ESG / SRI ²	MSCI Climate; Environmental ¹		
HSBC			HSBC Climate Change ¹	
Bloomberg			Bloomberg Clean Energy ¹	
NASDAQ		NASDAQ OMX Green Economy ¹		

Selection approach: 1. Screening, 2. Best-of-class, 3. Re-weighting; Source: ⁸⁵

A number of labels and schemes are also available in Europe to help investors assess and select from a range of financial products, which are labelled as sustainable or green. One major concern of investors is that the labels and schemes, even those providing a "very high assurance of greenness" such as the French TEEC label and the LuxFlag label for Climate Finance are difficult to compare because they employ different philosophies, taxonomies and in addition, define "greeness" differently in through the criteria they apply (see Chapter 2).

4.4 Verification

4.4.1 Summary of the current verification procedures

The existing labels and schemes available in Europe for financial products apply verification procedures of a similar core structure with small divergences to each other. Next to the auditing of the documents and examining compliance with the specific criteria by an auditor, the scheme or external verifiers check for compliance with the verification procedure. This demands the auditor to disclose all relevant documents to the verifier. Apart from compliance with the procedure, verification may also refer to other issues, such as tracking the use and or allocation of proceeds (e.g. GBP). The verification can set diverse requirements depending on the type of assets and on average takes one month to be accomplished.

It can be carried out partially, covering only certain aspects, or fully and thus assesses alignment with all specific requirements for verification. The timing of verification precedes the award of the label and can be randomly chosen or linked to a specific period of the year. Particular schemes may also adopt verification requirements of other schemes (e.g. EIB for CABs refers to GBP). In some cases, the verification procedure is

⁸⁴ Natixis. A view on the green and sustainable assets market. Available from: https://www.natixis.com/natixis/jcms/lpa5_65797/en/a-view-on-the-green-and-sustainable-assets-market

⁸⁵ Inderst, G., Kaminker, Ch., Stewart, F. (2012), "Defining and Measuring Green Investments: Implications for Institutional Investors" Asset Allocations", OECD Working Papers on Finance, Insurance and Private Pensions, No.24, OECD Publishing.

limited to examining the existence of other certificates, which demonstrate compliance with the scheme's prerequisites (e.g. Dutch Green Funds Scheme).

Verification can also refer to pre-issuance and post-issuance auditing process (e.g. Climate Bond Standard) and might require periodical certifications additionally. In most of the cases, the schemes involve annual update reports, which cover the validity period of the investment. Thus, any occurring changes are subject to reporting and verification. Many of the schemes reserve the right to perform random checks to certify compliance either by a site visit or by examining the webpage of the fund to assure compliance. In the case of no compliance, the scheme can perform more exhaustive inspections or the licence can be revoked.

4.4.2 Cost of verification

Costs can be divided into internal and external. Issuers incur the former when they establish and carry out internal processes and controls to meet the obligations of the certification. External costs include involvement of a verifier, the certification fee and the annual usage fee. The application fee covers the time spent by the scheme processing the application while the annual fee is for examining compliance on a yearly basis. Some schemes include an inspection to the application fee (e.g. Nordic Swan). Fees for the initial application may differ across the EU countries and are subject of the scheme's policy (Table 1). Indicative, application fees can range between EUR 3,000 - 4,000. The applicant should also consider an annual usage fee and the costs to involve an external verifier; the respective costs are also subject to local conditions.

4.4.3 Conclusions

The existing labels and schemes consider green a sub-set of ESG, SRI, Impact investing or any other overarching strategy that they employ. They also use different strategies to define green economic activities or sectors with varying degrees of granularities. Depending on the financial sector, varying definitions and qualities of green also exist, often measured or assessed through the application of different criteria as well. Depending on the strategies embedded within a label or scheme, social and ethical issues are also considered.

It is therefore necessary to develop a consistent definition of "green", through the EU Ecolabel, which should be built upon the EU Taxonomy, and would make use of process criteria to strengthen the environmental impact of investments.

5. Feedback from stakeholders: questionnaire and bilateral interviews

In December 2018, a questionnaire was circulated by the study team to gather input and opinions from stakeholders for the preparatory study of EU Ecolabel for financial products. Additionally, this information was complemented by concurrently held bilateral interviews with representatives of the existing labels and schemes available in the EU-28 for financial products.

117 stakeholders replied to this questionnaire by end of January 2019. The questionnaire focused on several aspects of the EU Ecolabel criteria under development. It included close and open questions. The main findings of this questionnaire, complemented by the information obtained in parallel bilateral interviews with relevant representative of the existing labels is presented in this section. A full analysis of the feedback of the stakeholders is provided in Annex I.

5.1 Product group definitions and scope of financial products information

The scope of this product group is proposed by the Commission to initially encompass the financial products covered by the PRIIPs Regulation (EU) No 1283/2017 and other financial products addressed to retail investors, which can be considered as services for distribution or use.

Regarding the scope, most of the respondents agreed that UCITS should be included in the first product group scope. Additionally, they selected life insurance policies with an investment element and pension funds as products that could also be covered.

Finally, stakeholders provided other factors that should be taken into account in defining the initial scope of products. The majority of respondents identified the "*potential for the product to deliver environmental benefits*" and the "*objective to mainstream sustainable finance*" as the most relevant factors. The factors that were cited most were: ESG label/social benefits, simple products, mainstream/significant products and the possibility for traceability/transparency.

5.2 Strategies and green definitions

An EU Ecolabel focusing on requirements relating to environmental issues, but also taking into account social and governance issues, could ensure that issuers consider these factors in a uniform manner in their investment decision process and minimise the risks of greenwashing for clients. In order to achieve this, a range of different strategies and definitions can be adopted.

In this section, a brief overview of the feedback of the stakeholders regarding the types of strategies and definitions of green portfolios that could be reflected in the EU Ecolabel criteria is provided.

Regarding **investment strategies**, initial evidence suggested that fund managers adopt a range of strategies to make their portfolio more attractive to customers seeking green or sustainable products. Stakeholders pointed out that the main strategies that should be reflected in the EU Ecolabel Criteria are the thematic approach (44%), the exclusionary approach (36%) and the impact investing (36%).

Stakeholders widely supported that "*a wide range of social criteria should also be included so that there is a proper balance between environmental and social sustainability in line with the best market practice of integrating ESG and with the Paris agreement on a just transition*". Among the social aspects that were clearly pointed out as relevant were the *human and labour rights and the health and safety*.

Likely, stakeholders widely supported that *a wide range of governance issues should be included in the EU Ecolabel criteria* and that the most relevant governance aspects were *transparency, anti-corruption, sustainability report, dialogue with stakeholders and risk management including due diligence*.

Regarding the compliance for the award of the EU Ecolabel for this product group, financial products could be required to attain a certain minimum number of points based on different aspects of the investment strategy (e.g. social, environmental, governance) or to pass a set of criteria to be awarded the label (**point criteria**)

system or pass/fail system). Some EU Ecolabel criteria for services adopt a number of mandatory criteria and a portion of optional criteria out of which a minimum number of points need to be obtained to qualify.

Stakeholders considered that a *point system could be moderately to highly appropriate* for the EU Ecolabel criteria and regarding the weighting, it stems that *green activities* should have the heaviest weight followed by *excluded criteria and the social and governance screening criteria*.

5.3 Sustainable investment and economic activities

An EU-wide classification system (taxonomy) is being developed, which will provide businesses and investors with a common language to identify in a first step economic activities that can be considered environmentally sustainable. In later steps, it is planned to address social and ethical aspects. The taxonomy will facilitate the assessment of whether investments are green on the basis of their contribution to environment objectives, but it will not attempt to define the degree of “greenness”. In addition, the taxonomy will only define “green” economic activities, not “brown” ones.

An **exclusion** requirement implies that the EU Ecolabel criteria could not be granted to financial products that are linked to certain economic activities. Such activities could be excluded on their “brown” nature (e.g. fossil fuel exploration) or owing to other consideration related to social and governance aspects.

Stakeholders *supported with a wide majority the use of exclusions* for specific activities based on environmental, social and corporate governance considerations, such as *coal mining, the fossil fuel energy generation, deforestation, petroleum extraction or natural gas or shale gas extraction, human and labour rights violation or corruption*.

The exclusions could be total, in which case the product that could be awarded the EU Ecolabel would be those that have no investments in companies that are active in specific economic sectors. Alternatively, they could be partial, which would allow a portfolio to have a comparatively small investment share in companies (partially) active in specific economic sectors.

The opinion of stakeholders was *equally divided between the use of total and partial exclusions*. In support of the partial exclusions, stakeholders commented the better adaptation of the investment to the market conditions and global economy, the enhancement of the credibility of the label and the better consideration of indirect investment. Most of the stakeholders proposed a threshold between 5% and 10% for the partial exclusions. The reasons underpinning the use of total exclusions include the transparency and easiness of understanding by the consumers and the significant harm of the excluded activities and the risk of greenwashing of the label.

The verification of **the thresholds related to the greenness of the portfolio** can be carried out at different levels. Stakeholders pointed out the *importance of performing the verification at portfolio level, company level and activity and use of proceeds level*. Additionally, stakeholders provided information on the minimum percentage that should be invested in green activities so that the financial product qualifies for the EU Ecolabel. *At least 50%* was suggested as the preferred option for a threshold at portfolio, asset class, company and activity and use of proceeds. The main reasons that supported this threshold were that this threshold enhances the credibility of the label, prevents greenwashing and is strict enough while does not reduce too much the financial market and the choices of the fund managers.

When assessing the greenness of shares, a threshold should be identified based on the greenness of the underlying business that has issued them. To be eligible for the EU Ecolabel, issuer companies may be asked to generate a minimum proportion of their revenue from green activities. Stakeholders considered *a minimum share of green turnover (or revenue) required for each of the companies or a minimum threshold applying to the (weighted) average of companies' green turnover share* should be applied.

5.4 Assessment and verification methods.

This section presents the inputs from the stakeholders on how the verification could work and where the main challenges can be found.

Given that **portfolios** may have investments in a number of different types of financial assets this could have implications for the assessment and verification processes. Stakeholders considered that *structured deposits, structured products, bonds and pension funds* would require *a very specific form of verification while investment funds, life insurance policies with an investment element and saving schemes/account could be verified by a generic verification form.*

Similarly, stakeholders identified *real state, money market instruments and financial derivatives as those financial assets* that would require *a very specific verification form while shares and bonds could be verified by a more generic verification form.*

A key consideration for the EU Ecolabel is the **cost and complexity of assessment and verification** for applicants. Stakeholders proposed that in order to streamline the process the EU Ecolabel criteria should *build on existing national schemes having harmonized criteria/structure and defining clear and general standards.* Other suggestions were the *creation of a web-based application tool* for submitting the application, *shortening the reporting of the results* and making them understandable for all stakeholders *and encouraging the cooperation of competent bodies.* The *involvement of a third party verification, the inclusion of mutual recognition* for those criteria already verified by other labels/organizations and the *provision of historical information* were other initiatives suggested by the stakeholders. *Private verifiers are welcome* by the stakeholders due to the complexity of the financial products and the dynamic market evolution as well as to the reduction of costs and the increase in the reliability that they can bring.

6. CONCLUSIONS

This preliminary report aims at providing the background information for the development of the EU Ecolabel criteria for retail financial products. The study has been carried out by DG-JRC.B1 and B5 units in cooperation with DG ENV and DG FISMA. This work was initiated as a result of the Commission proposal included in the Action Plan on Sustainable Finance of creating a voluntary EU wide labelling scheme that enables investors to directly channel their funds into sustainable investments.

The financial market is a sector highly regulated. The main regulations linked to the EU Ecolabel criteria for retail financial products would be those related to PRIIPs and UCITs as they regulate the retail financial products with the highest market shares.

A revision of the existing national schemes identified a variety of labels that are competing on the market. Each existing label differs in terms of context, scope, strategies, taxonomy used, and ways for assessing and verifying their performance.

The market analysis carried out in this study identified that the composition of household financial assets is relatively stable over time. Currency and deposits, pension funds, and (life and non-life) insurance products constitute around 30%, 20% and 18% respectively of household wealth. In addition to retail investors, public authorities are major consumers in Europe and can significantly contribute to sustainable investments. Government financial assets are mostly held in equity (40%) and in currency and deposits (17%).

Based on the above information, the scope of this product group is initially proposed to encompass the financial products covered by PRIIPS Regulation (EU) No 283/2017 and other financial products addressed to retail investors, which can be considered as services for distribution or use such as those covered by UCIT Regulation and insurance based products with an investment component.

This preliminary report also identified the lack of harmonized criteria for defining greenness of the financial products because there are non-uniform requirements on transparency or on the quality of reporting. There is therefore a need for a framework that stimulates not only the comparability of investments but does also facilitate and enhance sustainable investment at EU level and beyond. The Action Plan promised to deliver an EU wide classification system or EU taxonomy that could provide the basis for developing the EU Ecolabel criteria.

The development of the EU Ecolabel criteria will require careful consideration of all the existing strategies as well as the aspects to be included. The revision of the existing labels and the feedback from the stakeholders identified the exclusion criteria, thematic approach and impact investment as the most suitable strategies to follow. Further analysis is still required to decide on their appropriate thresholds.

Social and governance aspects are suggested to be included in the EU Ecolabel criteria to get a proper balance between the environmental, social sustainability and governance issues in line with the market practice of integrating ESG and the Paris agreement. Among these aspects to be included human and labour rights, health and safety, transparency, anticorruption, sustainable report and risk management including due diligence were identified as the most relevant ones.

The EU Ecolabel criteria should also foresee verification at two distinct levels. The first level is the greenness of each of the invested companies in case of stocks being in compliance with the EU Taxonomy. The second level is suggested to occur at investment portfolio composition. In this respect, alternative methodologies could be applied what would require further evaluation and additional information.

This preliminary report supports therefore the EU Ecolabel criteria proposals which are to be made in the first Technical Report and that will provide the background information required for the 1st AHWG meeting to be held April 2019. This preliminary report also includes the inputs from an extensive stakeholder survey and bilateral interviews with label and scheme operators and will be closed after the first AHWG meeting.

7. ANNEX I. detailed results from the questionnaire and bilateral interviews

Between December 2018 and January 2019, a questionnaire was circulated to gather input and opinions from stakeholders for the use on the preparatory study of EU Ecolabel for financial products. Additionally, the information was supported with information obtained from bilateral interviews held concurrently with representatives of the most ecolabel and schemes available in the EU-28 for financial products.

Q1. Scope

The EU Ecolabel criteria are aimed to correspond to “*the best 10-20% of financial products available on the Community market*” within a certain product group and a preliminary market analysis has identified investment funds, in particular listed funds classified as UCITs as potentially the first set of financial products that should be covered by the EU Ecolabel criteria.

Q1.1. Would you agree that UCITs should be included in the first product group(s) based on your understanding of the current state of the financial market?

This question was aimed at testing whether one of most common types of investment fund could form the starting point for the product group. 22 out of 29 responses received agreed that UCITS should be included in the first product group scope.

Q1.2. Which other products should be included first?

This question provided a list of products that fit broadly within the scope of PRIIPs regulation together with others that are of market significance. The majority of respondents selected investment funds (84%), life insurance policies with an investment element (58%) and pension funds (58%). Also notable were bonds (42%) and savings accounts/products (31%).

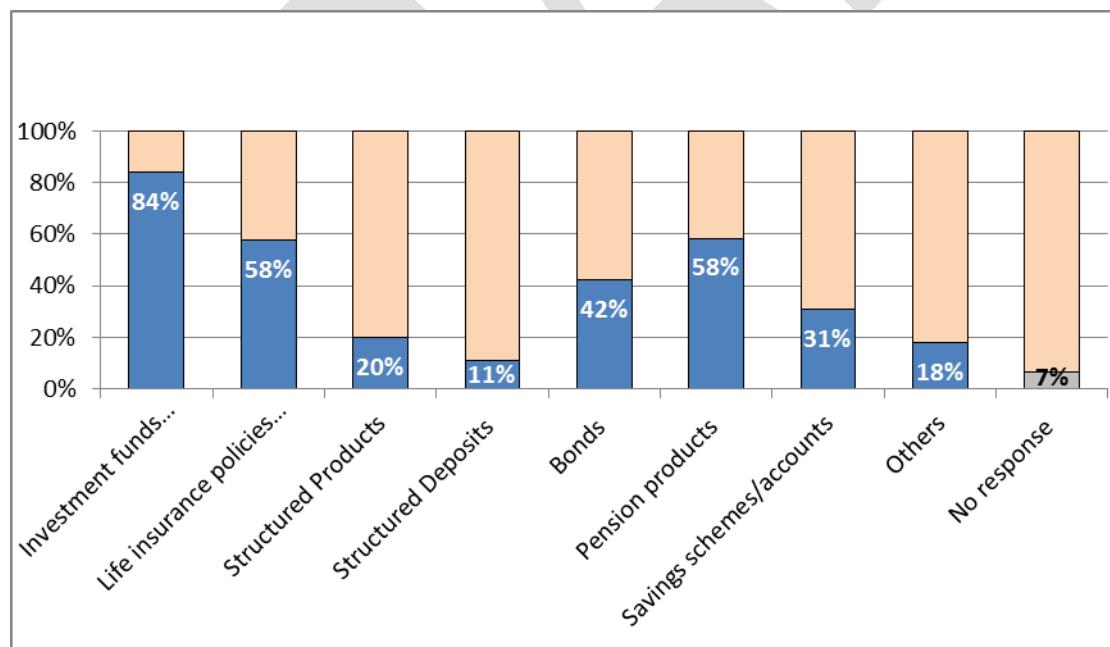


Figure 20 – Retail financial products that should be included within the 1st Ecolabel scope

23 respondents provided an open response to the invitation to elaborate on which products should be included within the scope.

A diversity of responses was provided, with no one response reaching a majority. These included the potential to include real estate funds, employee savings schemes, simple (non-structured) products, competing products, green bonds, green mortgages, exchange-traded funds, funds-of-funds.

Interestingly, three respondents described the potential for the Ecolabel to focus on the labelling of the underlying assets rather than portfolios. Included within two of their responses was the potential to label 'green' bonds as this could both stimulate the issuers market and make it easier for investment funds to verify their performance.

Q1.3. Other than market share, what factors should be taken into account in defining the initial scope of products?

The majority of respondents identified '*Potential for the product to deliver environmental benefits*' (74%) and '*Objective to mainstream sustainable finance*' (58%) as factors to take into account.

25 respondents provided an open response to the invitation to elaborate on which factors should also be taken into account in defining the product scope.

A diversity of responses was provided, with no one response reaching a majority. They can be categorised under the following broad headings:

- Technical focus: it should be ESG themed, it should demonstrate environmental benefit, and it should demonstrate social benefit, scope based on feasibility of verification, traceability and transparency of investments, sustainable asset allocation.
- Market focus: long-term products, products of significance in the market, simple products, mainstream products, co-existence with existing labels, level playing field amongst competing products.
- Investor focus: provide investor protection, scope should be based on investor literacy and feedback, minimise the expense ratio for sustainable investments.

Those that were cited most were: ESG label/social benefits (5), simple products (4), mainstream/significant products (4), possibility for traceability/transparency (4).

Two negative opinions about the factors to be considered were also expressed.

Q2. Strategies and green scope

Initial evidence suggests that fund managers adopt a range of strategies in order to make their portfolio more attractive to customers seeking green or sustainable products.

Fund managers may take a positive approach to the identification of green sectors or economic activities, possibly with reference to screening criteria or a taxonomy.

Available information indicates that an increasing proportion of assets are currently managed using ESG strategies. ESG strategies include but are not limited to community investing, sustainability-themed investing, corporate engagement, and exclusionary screening. This is reflected in the criteria of existing schemes and labels too.

An EU Ecolabel focusing on requirements relating to environmental issues, but also taking into account social and governance issues, will ensure that issuers consider these factors in a uniform manner in their investment decision process and minimize the risks of greenwashing for clients.

Q2.1 What types of strategies should be reflected in the EU Ecolabel criteria?

This question aims at providing an overview of how the criteria set can be configured. 30 responses were received in this section, which clearly supported some of the strategies already used in other existing schemes such as the thematic approach (44%), exclusionary approach (36%) and impact investing (36%).

Figure 21 shows the distribution of the strategies proposed.

Additionally, one stakeholder considered that it is important to provide some flexibility around the strategies so that higher adoption of the label will be possible. According to this stakeholder, a combination of ESG integration and corporate engagement as well as certain exclusions and thematic strategies should be included. A separate label for impact investing and purely thematic strategies can be considered since these strategies will likely remain as a niche in the future market.

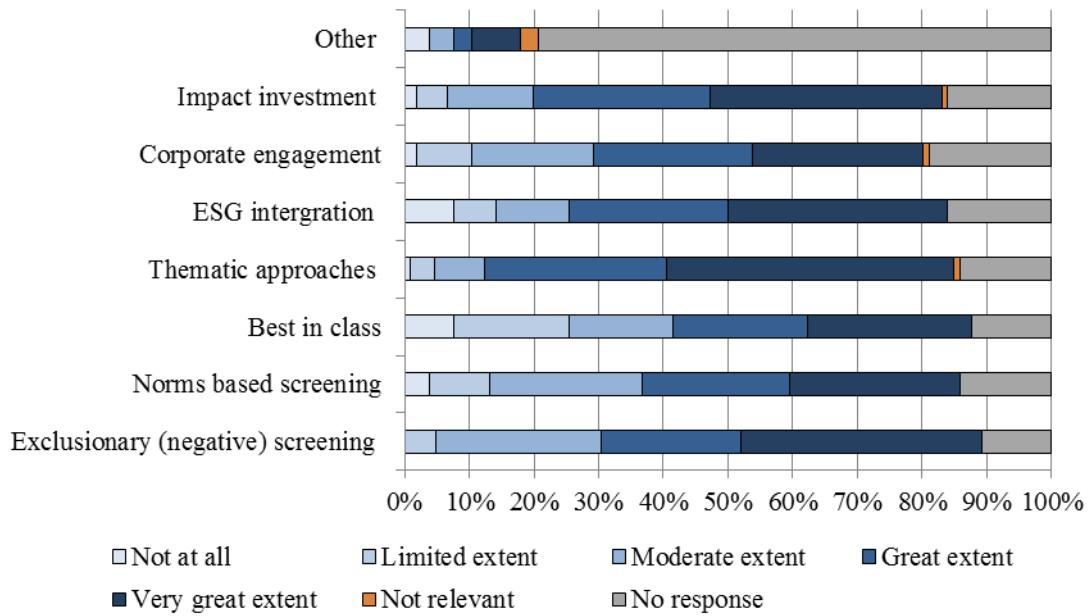


Figure 21 – Types of strategies to be reflected on the EU Ecolabel criteria.

Q2.2 To what extent do you consider that the EU ecolabel should have criteria that address social issues?

This question aims to get a first indication about the extent in which social criteria should be integrated in the EU Ecolabel. 29 responses were received split among the four options provided as possible replies:

- social issues should not be addressed in the ecolabel because environmental issues are the most important to address (7%)
- social issues should not be addressed at this stage in the first set of criteria development. They could be considered later on (7%)
- only key social factors should be included to ensure that social objectives are not jeopardised while the focus should be on environmental issues (38%)
- a wide range of social criteria should be included so that there is a proper balance between the environmental and social sustainability in line with the best market practice of integrating ESG and with the Paris agreement on a just transition (48%)

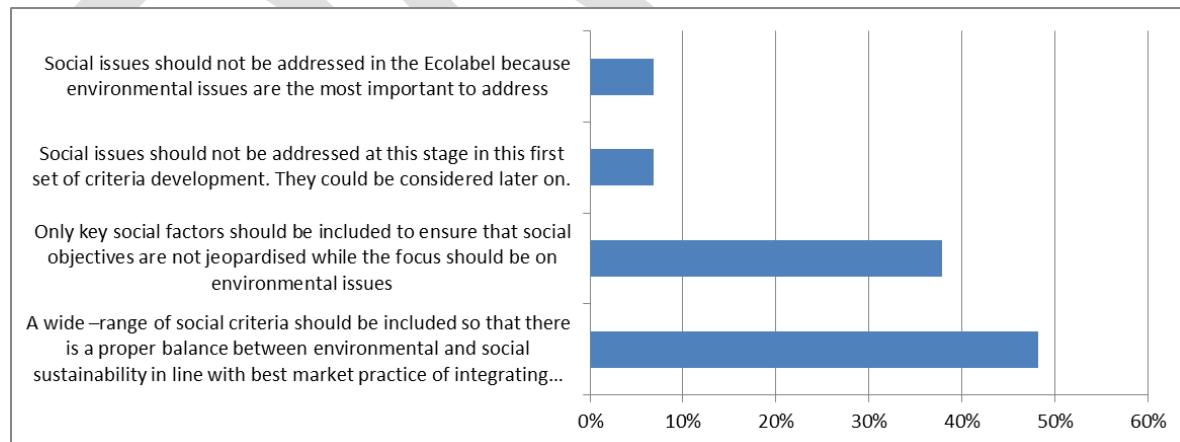


Figure 22 – extend to which EU ecolabel should have criteria that address social issues.

As observed, stakeholders widely supported the inclusion of social criteria aiming to get a proper balance between the environmental and social suitability. 5 respondents provided an open response to the invitation to support their views. A diversity of responses was obtained, supporting each of the four statements included as replies.

Three stakeholders commented that leaving aside social criteria is a mistake because they are considered as key factors of success in the fight against climate change. Environmental criteria cannot be addressed without taking into account their associated social impacts and vice versa.

On the other hand, a couple of stakeholders considered that neither social nor ecological criteria should be attached to financial products because investment is made to harvest interests or profits or that it is important to maintain the focus so that the essence of the label can be easily understood and explained by the retail investors/financial advisors. The social factors can be developed at a later stage.

Stakeholders were asked about the relevance of the following social aspects. Most of them considered that aspects related to human rights, labour rights and health and safety are of key importance. The diversity of the responses is showed in Figure 1.

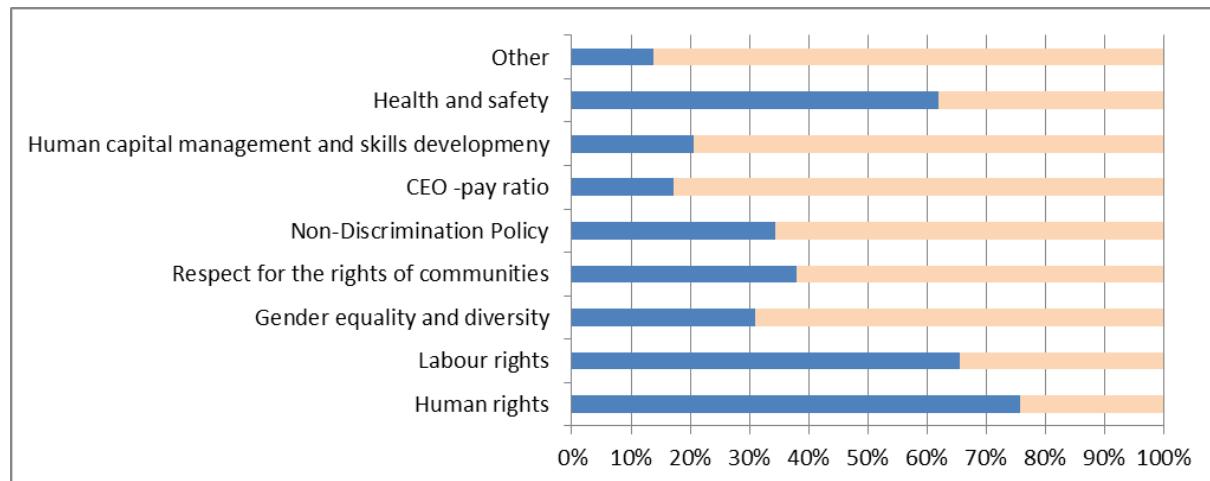


Figure 23 – Breakdown of the relevance of the social aspects to be considered in the EU Ecolabel

Four stakeholders elaborated further on “other aspects”. Aspects suggested were the job creation, the differentiation among the production and sales of conventional and unconventional weapons and the need of deciding further aspects on the particularities of each investment strategy and its ability to address social aspects.

One stakeholder reiterate that social aspects should not be included in the EU Ecolabel due to the lack of interest from the investors.

Q2.3 To what extent do you consider that the EU Ecolabel should have criteria that address governance?

Likely as in the previous question, this question aims to get a first indication about the extent in which ethical corporate and governance aspects should be integrated in the EU Ecolabel. 29 responses were received split among the four options provided as possible replies:

- A wide-range of governance issues should be included so that there is a proper balance between environmental and social sustainability in line with best market practice of integrating ESG and with the Paris agreement on a just transition (50%).
- Only key governance issues/factors should be included to ensure that governance objectives are not jeopardised while the focus should be on environmental issues (37%).
- Governance issues should not be addressed at this stage in this first set of criteria development. They could be considered later on (10%)
- Governance issues should not be addressed in the Ecolabel because environmental issues are the most important to address (0%)
- Other (3%)

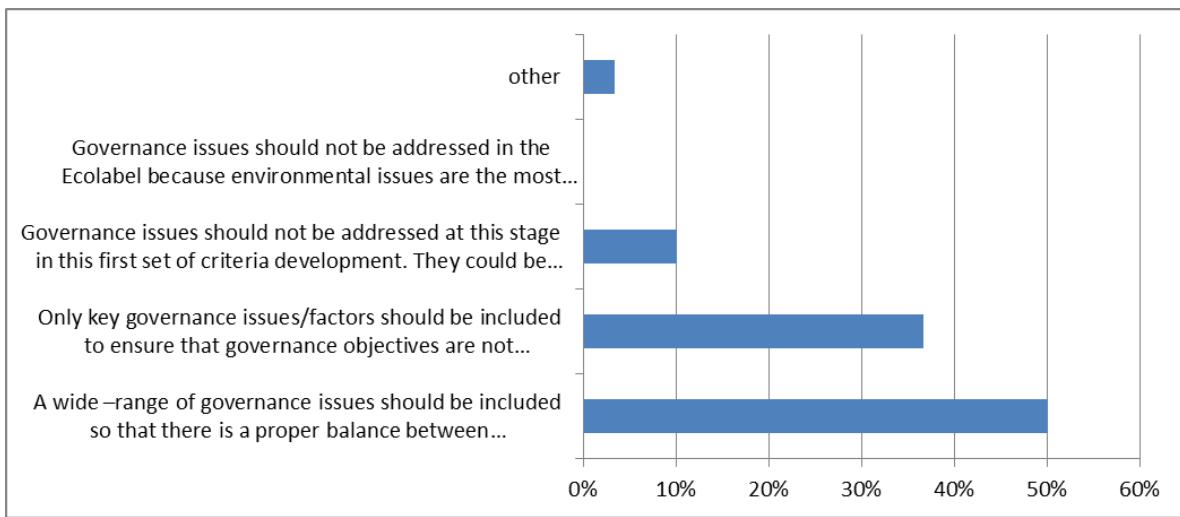


Figure 24 – Extension to which governance aspects should be included in the EU Ecolabel

As observed the majority of stakeholders support the inclusion of a wide range of governance issues. Only one stakeholder elaborated further under the “other” option. This stakeholder considered that governance should be a key concern to ensure that corporations properly allocate all resources and pay the taxes in the countries where they operate, supporting the achievement of the SDGs.

Stakeholders were asked about the relevance of the following governance aspects. Most of them considered that aspects related to anti-corruption (90%), transparency (86%), sustainability report (62%), dialogue with stakeholders (62%) and risk management including due diligence (62%).

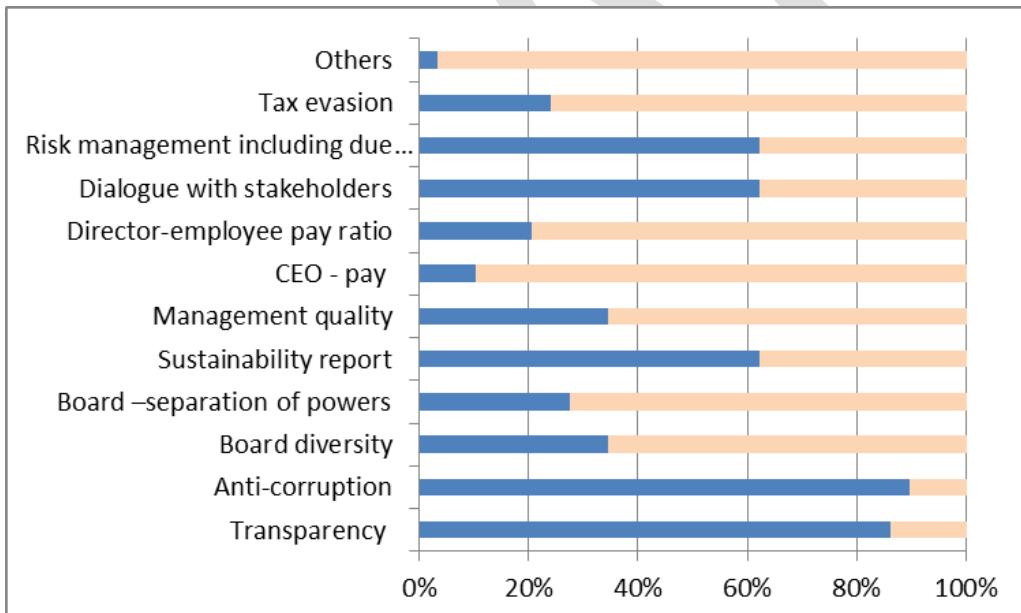


Figure 25 – Breakdown of the relevance of the governance aspects to be considered in the EU Ecolabel

Only one stakeholder elaborated further under the “other” option pointing out that the specific governance aspects should be decided depending on the investment strategy and the ability to address governance issues.

Q2.4 Given the range of possible investments in a portfolio and the different combinations of criteria, it might be beneficial to examine a point system for the Ecolabel. To what extent would this be appropriate for this product group?

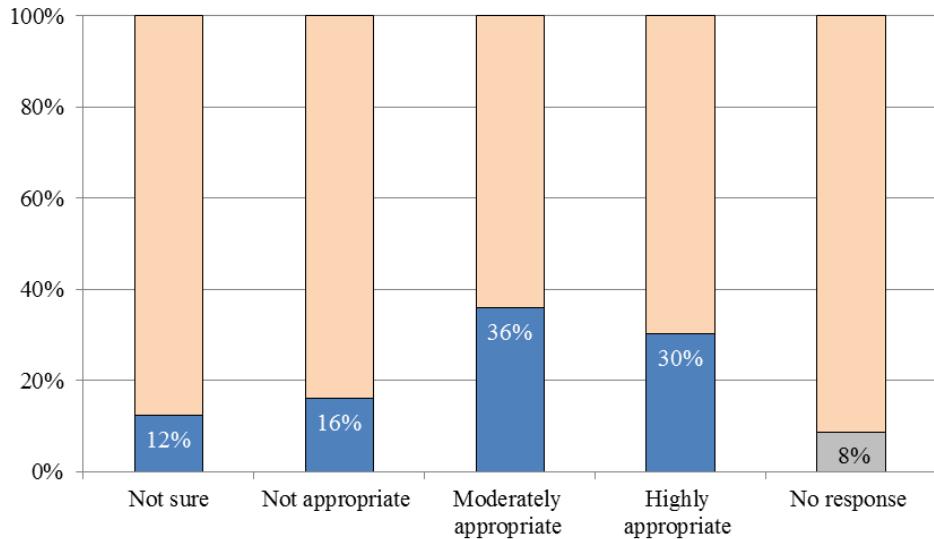


Figure 26 – Significance of establishing a point system for awarding the EU Ecolabel.

Most of the stakeholders considered that the inclusion of a point system can be either moderately appropriate or highly appropriate.

Q4.7 If there were to be a points system, what weighting would you attribute to each of the following possible components that contribute to the total score for a financial product?

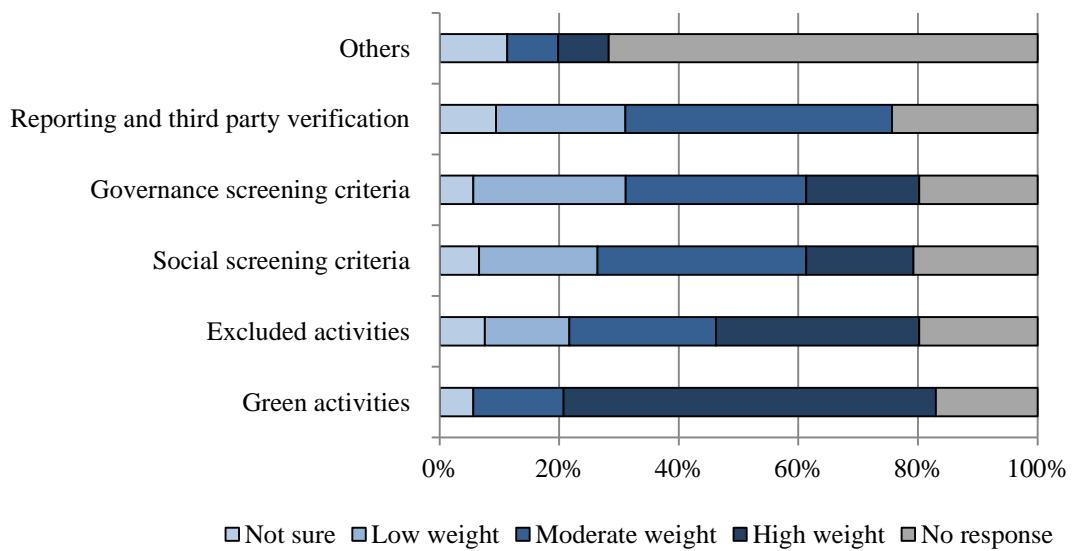


Figure 27 – Weighting of the point system components.

According to the results, green activities should have a heavier weight than other aspects followed by those excluded activities and the social screening criteria. Regarding the information provided by the stakeholders under “other” aspects, stakeholders commented that research quality setting standards or criteria must be met by research and or rating agencies should be included.

Q3. Sustainable investment and economic activities

An EU-wide classification system (taxonomy) is being developed, which will provide businesses and investors with a common language to identify in a first step economic activities that can be considered environmentally sustainable. The first delegated act under the taxonomy will focus on climate change mitigation and adaptation activities and some environmental activities. It will define technical screening criteria relating to “substantial contribution” to mitigation or adaptation and containing requirements for “do not significant harm” to other environmental objectives, this means:

- sustainable use and protection of water and marine resources
- transition to a circular economy, waste prevention and recycling
- pollution prevention and control
- protection of healthy ecosystems

The taxonomy will facilitate the assessment of the degree to which investments contribute to environmental objectives but it will not attempt to define the greenness of financial assets. In addition, the taxonomy will only define green economic activities, not brown ones.

Exclusions

An exclusion requirement implies that the ecolabel could not be granted to financial products that are linked to certain economic activities. Such activities could be excluded based on their brown nature (eg fossil fuel exploration) or owing to other considerations related to social and governance assets.

A non-exhaustive review of the existing labelling schemes and initiatives in Europe indicates common environmental exclusions based on economic activity, such as but not limited to: nuclear energy, genetic engineering, fossil fuels, coal mining, natural gas, crude oil or uranium, etc

Portfolio thresholds for greenness / sustainability

A review of existing schemes and labels indicates that they tend to work at three main levels; portfolio, company and economic activity. However, other levels may be necessary

Q3.1 Should the EU Ecolabel have exclusions for specific activities on the basis of their environmental/social impacts or based on corporate governance considerations?

Stakeholders supported with a wide majority (93%) the use of exclusions for specific activities based on environmental, social or corporate governance considerations. Those environmental aspects that were considered especially relevant by the stakeholders are those related to the fossil fuels such as coal mining, fossil fuel energy generation, petroleum, natural gas or shale gas extraction. Deforestation plays also an important role according to the stakeholders (see Figure 30Error! Reference source not found.)

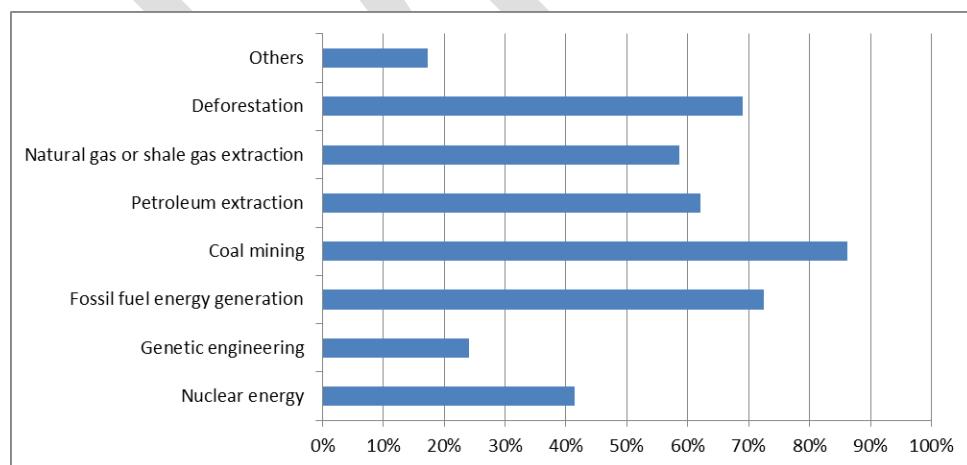


Figure 28 – Relevance of the environmental exclusions

Several stakeholders provided more information under the aspect “other”. For example stakeholders pointed out other aspects that could be included such as a bad management of waste landfills, the extraction of

unconventional fossil fuels, water-intensive activities in water-stressed regions or activities related to fracking and oil sands.

One stakeholder pointed out that simple exclusions will likely not result in a higher adoption by fund managers and that an alternative approach could be to link technology exposure (i.e. fossil fuel energy generation) to corporate environmental strategy (i.e. a low-carbon transition plan) to form the basis for exclusions. This means exclusion criteria could be determined for companies involved in brown technologies that fail to demonstrate a clear decarbonisation strategy. This type of exclusion criteria might align better to fund managers' investment process.

A special remark was submitted regarding the possible exclusion based on genetic engineering aspects. The stakeholder commented that genetic engineering can be used for activities that are sustainable, bringing positive contribution to the environment. For example, genetic engineering is one tool that enables the transition towards a sustainable bio-economy or a society based on renewable bio-resources, replacing fossil fuels. Several examples of the use of genetic engineering to develop sustainable solutions were provided including its use for sustainable agriculture, reduction of the environmental impact from meat production and reduction in the use of antibiotic in farming, reducing the environmental impact of household chores such as laundry or cleaning and finally helping to produce renewable fuels (i.e. ethanol).

A lower support was provided by the stakeholders to the use of social and governance exclusions (approx. 77%). Among those social and governance exclusions considered relevant were the human and labour rights violation followed by the corruption.

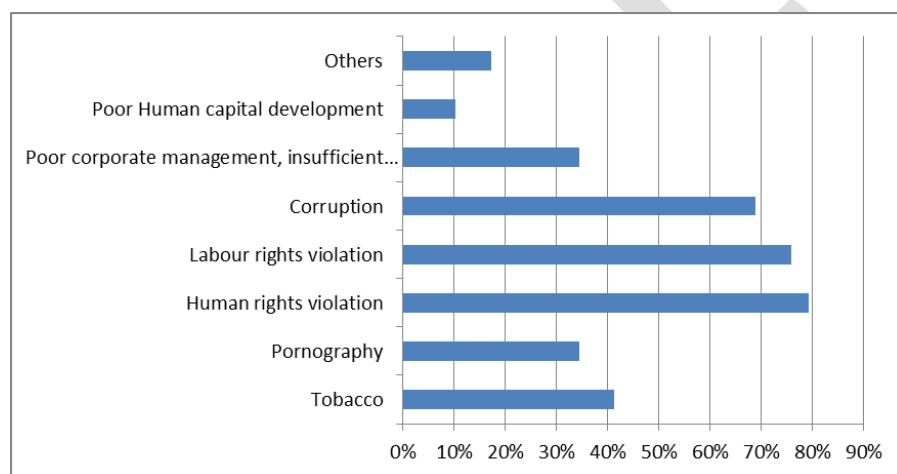


Figure 29 – Relevance of the social and governance exclusions

Stakeholders were invited to suggest more aspects that could be included as social and governance exclusions. They suggested the exclusion of manufacturing and sales of conventional and unconventional weapons and mines. One stakeholder suggested following the UN Global Compact guidelines.

Q3.2 If exclusions are included in the EU Ecolabel, should they be total or partial?

The opinion of the stakeholders was equally divided between the use of total or partial exclusions.

The reasons supporting partial exclusions were that:

- better adaptation to market conditions: partial exclusions allow the economy and the companies to adapt to different production processes, markets and alternatives for raw materials
- credibility of the label: a total exclusion limits the possibilities of investment and therefore it could damage or make difficult to maintain the credibility of the label. It is difficult to guarantee that 0% of company revenues as there might be a large amount of suppliers, business partners or other links/associations.
- better reflection of the complexity of the global economy: the partial exclusions give companies involved in controversial activities time and incentives to move away from those activities. This move away should result from ongoing investor engagement.
- Better consideration of indirect investments that could take place on the companies

Most of the stakeholders proposed a threshold limit between 5% and 10%. It was stated that according to the experience gained by the existing labels, a threshold of 5% to 10% on the revenue or the turnover will do the job on sector-based industries. Additionally, stakeholders provided some examples of possible partial exclusions and their associated thresholds, e.g. maximum 1% revenue in gambling, maximum 5% revenue in nuclear power, maximum 5% of the portfolio that are free investment, maximum of 10% of revenue in fossil fuels, etc.

The reasons supporting the use of total exclusions are:

- transparency and easy to be understood by the consumers: total exclusions are easier to be understood by the consumers and bring a higher level of transparency to the label. The awarded financial product will have a larger effect on the market as it communicates a clear message to the consumers
- sectors with high environmental or social impacts should be excluded: aspects such as deforestation, fossil fuel extraction (coal, oil and gas) and nuclear energy should be totally excluded due to the large environmental impacts associated with these activities. Regarding social aspects, human and labour right violation, manufacturing and sales of controversial weapons
- significant harm of the excluded activities and greenwashing: relevant companies may only have a small share of their activities related to the excluded activities, but this activity could still do significant harm. This is especially true for diversified multinational. Furthermore, it is feared that the partial exclusion will not be visible to the retail customer in the marketing and thus this approach would risk greenwashing

Q4. Portfolio greenness for thresholds

A review of existing schemes and labels indicates that they tend to work at three main levels - portfolio, company and economic activity. However, other levels may be necessary.

Q4.1 At what level do you consider the EU Ecolabel will need to work in order to verify the product's greenness?
 This question aims to find out the level of verification. Stakeholders pointed out the importance of carrying out the verification at portfolio level, at company level or at activity and use of proceeds level. Additionally, they pointed out that there could be also interesting to have a minimum threshold at investing manager or at fund company level in the sense that when applying to the EU Ecolabel the whole company should fulfil certain criteria.

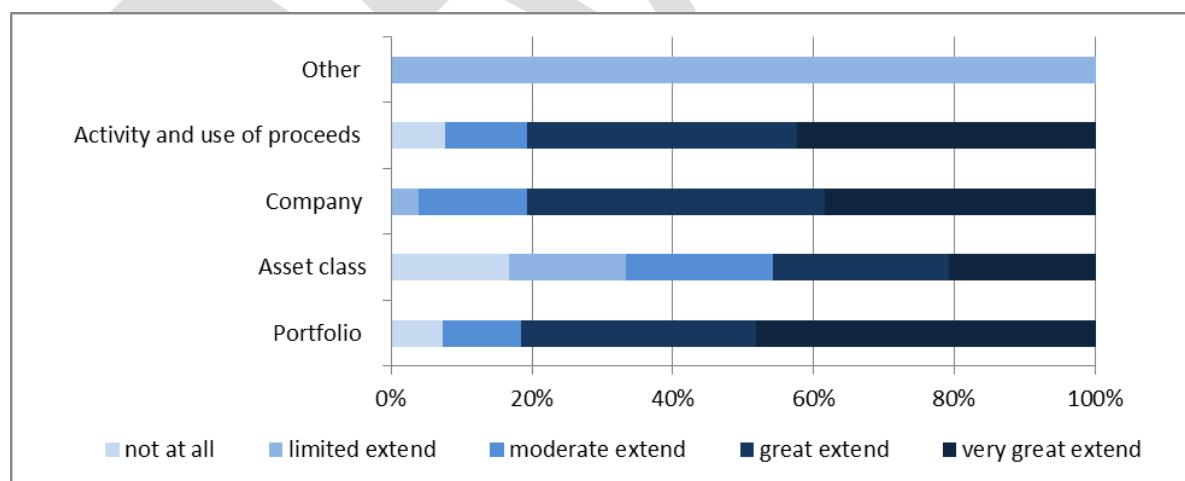


Figure 30 – Types of verification to be carried out in the EU Ecolabel.

Additionally, stakeholders provided information on the minimum percentage that should be invested in green activities for product to qualify for the EU Ecolabel when the verification is carried out at portfolio, asset class, company or activity and use of proceeds levels. As seen in Figure 31 at least 50% of the investment is the most popular option regardless the level of verification.

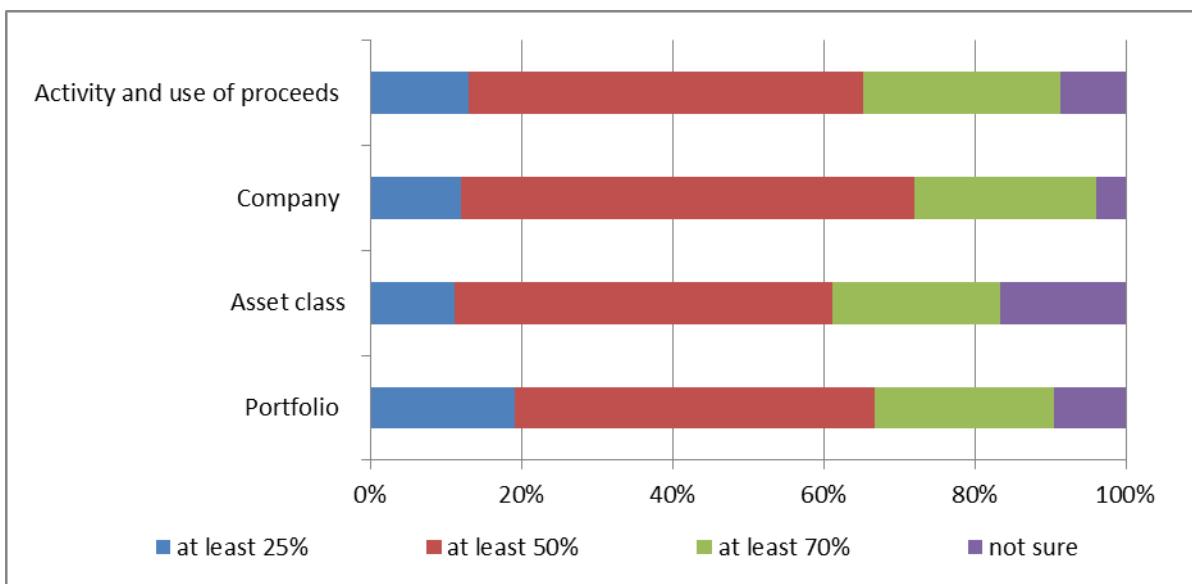


Figure 31 – Minimum percentage that should be invested in green activities for each of the verification levels.

Stakeholders considered that the reasons for suggesting these minima values for investments are:

a) at least 25%

- Any type of a service or a product is generated from usage and management of human or natural resources. These two are always engaged in any type of market distribution.

b) at least 50%

- Credibility of the label: on the one hand at least 50% of the investment should be pre-selected and on the other hand this level will have a direct and even stronger effect than exclusion criteria on the fact in which companies invest in funds
- It will set the minimum requirement quite high but also allows for companies in serious transition to greener future activities
- It prevents greenwashing but allows sufficient diversification
- The market of green activities, depending on how the EU taxonomy defines them, may be not large enough to justify a higher allocation.
- This is the minimum requirement to classify an activity as green

c) at least 70%

- Credibility of the label: EU ecolabel should be awarded only to the “best” performing financial products available on the market in terms of greenness.
- A threshold at the level of the portfolio or asset class would again risk a certain degree of greenwashing, as it will be unclear to retail customers that a certain part of the portfolio can happily be invested in companies/assets that don't have to adhere to the Ecolabel criteria. The company turnover threshold is very important, but should be exceeding already existing best practices and be
- As we try to find a minimum standard - at least 70 % should be claimed sustainable

Finally, stakeholders suggested other methodologies or improvements to the presented methodology such as

- work with ranges instead of fixed thresholds (i.e. 25 - 50%)
- use the weighted holding in the fund, defined as the percentage of the fund's investment in a company relative to the total revenue in such business areas that are aimed to be promoted (according to the EU taxonomy)
- a point system as implemented in Nordic Ecolabel.

Stakeholders were asked for technical criteria that could apply to the following financial products:

a) Transferable securities

a.1) shares

- requirements on minimum threshold on ESG rating, exclusion criteria in combination with selection criterion (best-in class)
- at least 50% of company revenue in green activities
- verification level: product and production process of the company
- the intrinsic value is proposed as main characteristic of this financial product.

a.2) bonds

- minimum requirement concerning the issuer (e.g. compliance with the exclusion criteria)
- minimum requirement concerning the emission (e.g. use and management of proceeds, project categories, etc).
- minimum requirements on transparency and reporting (e.g. which projects are financed to what extent), if it is refinancing (secondary market) or impact investing (primary market).
- at least 50% of company revenue in green activities
- verification level: product and production process (company) and legislation and policies (sovereign bonds)
- the pay-out risk is proposed as main characteristic of this financial product.

b) Financial derivative instruments

- the nature of the financial derivative instruments makes difficult to identify the environmental performance associated with. Therefore, the use of derivatives should be limited, although it is recognized that they are important hedging instruments.
- the leverage risk is proposed as main characteristic of this financial product.

c) Money market instruments

- the liquidity risk is proposed as main characteristic of this financial product.

d) Real state

- criteria concerning the environmental performance of the building such as energy efficiency, GHG emissions, impacts on biodiversity and the social performance such as aspects of the renters, infrastructure, accessibility, etc. should be considered. These criteria should include the materials used and their ecological footprint.
- criteria for the refurbishment of the buildings
- exclusion criteria related to deforestation and water pauperization
- the energy certificate is proposed as main characteristic of this financial product.

e) Others

Q4.2 When assessing the 'greenness' of shares, a threshold should be identified based on the 'greenness' of the underlying business that has issued them. To be eligible for the EU Ecolabel, issuer companies may be asked to generate a minimum proportion of their revenue from green activities. How should be the greenness of several companies weighted?

Stakeholders selected that a minimum share of green turnover (or revenue) required for each of the companies (52%) could be the most relevant way of assessing the greenness of several companies. Additionally, one stakeholder commented another approach used in the climetrics. This approach is based on sector overlay and used to adjust the portfolio weights regarding the climate change impacts.

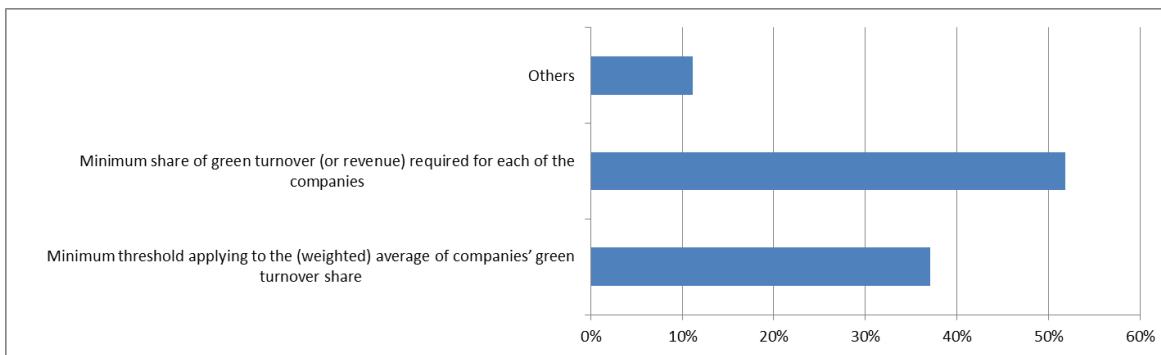


Figure 32 – procedures for assessing the greenness of a portfolio.

When assessing the greenness of bonds, be eligible for the EU Ecolabel issuer companies may be asked to ensure that a minimum proportion of the proceeds of the bonds are invested in green activities. Stakeholders considered that greenness of the issuers of the bonds should be taken into account to great extent or to moderate extent (see Figure 35**Error! Reference source not found.**).

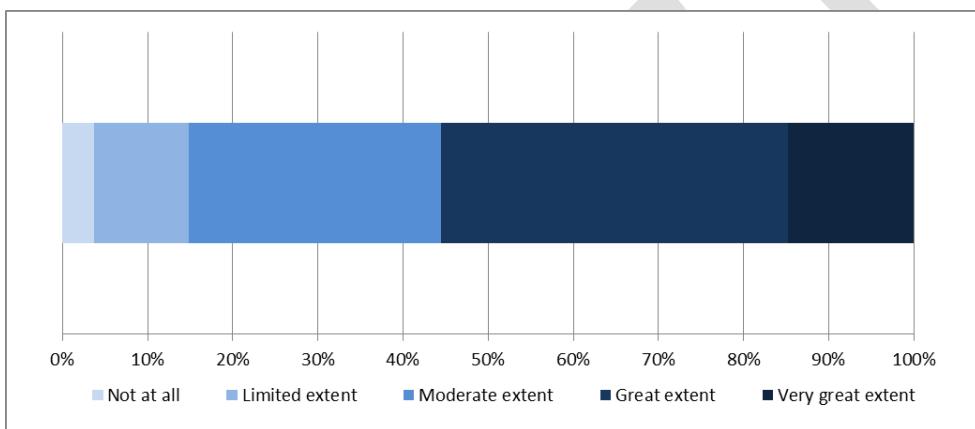


Figure 33 – Importance of considering the greenness of the issuers of the bonds.

Q5. Assessment and verification methods

Various assessment systems exist. Some labels evaluate conformity of products using a pass or fail criteria linked to a specific issue. If the product does not meet the criteria, it fails. If it does, it passes. A point system is used to evaluate compliance and may incorporate totals, percentages, averages or other types of calculations. Existing EU Ecolabel criteria for services adopt a number of mandatory and a portion of optional criteria out of which a minimum number of points need to be obtained to qualify.

Points systems

To be deemed “compliant” for the award of the EU ecolabel for the product group, financial products could be required to attain a certain minimum number of points based on different aspects (e.g. social, environmental, governance) of a product to be awarded the label.

Portfolio verification

Given that portfolio may have investments in a number of different types of financial assets this could have implications for the assessment and verification processes.

Given that portfolios may have investments in a number of different types of financial assets this could have implications for the assessment and verification processes. Stakeholders were requested to provide their views on:

Q5.1 To what extent would the following financial products require their own specific form of verification? In general stakeholders considered that products should be verified following a very specific form of verification. This opinion is stronger for the structured deposits and structured products followed by the pension products, bonds and investment funds addressed to retail clients.

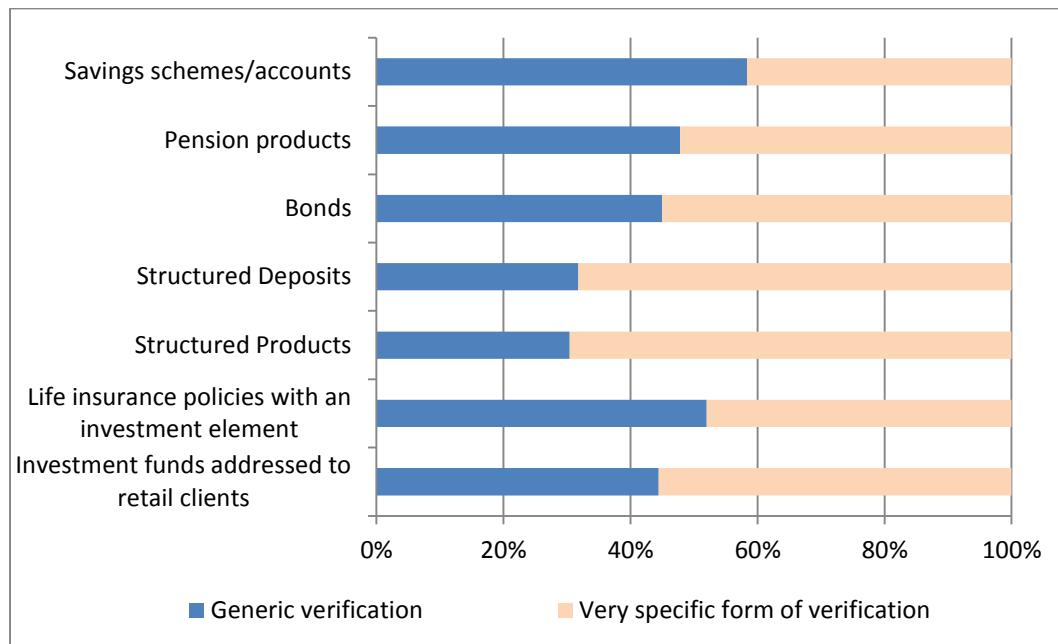


Figure 34 – Generic or specific form of verification for selected financial products

Additionally, some stakeholders elaborated further on this issue with split opinions.

On one hand, they pointed out that in some national schemes, there is only one assessment sheet for different kinds of products. In this way, a standardised assessment is ensured as well as a reduction of the work, time and costs of the auditors.

On the other hand they commented that the actual content of the financial products will vary in and between the listed products and that in their experience it is rather difficult to compile generic criteria for product groups that do not have the same underlying functional mechanisms (i.e. investment funds and structured products are designed in quite a different manner). Each product has different asset classes and holding periods, which make it relevant to take into account specific verification process.

The same question was addressed in the case of the financial products. Stakeholders corroborated the idea of having specific verification forms for real state, money market instruments and financial derivatives. They considered that generic verification could be used for shares and probably bonds. They elaborated more on this aspect pointing out that there is no one size for all verification process for different types of asset classes, because each one has different proceedings and markets for placements, which make it relevant to take into account these specific while developing a verification process. Moreover, they commented that the listed instruments are quite unique in character, apart from shares, bonds and to some extent money market instruments, which can be verified at the same issuer level. On the other hand, debt market instruments can

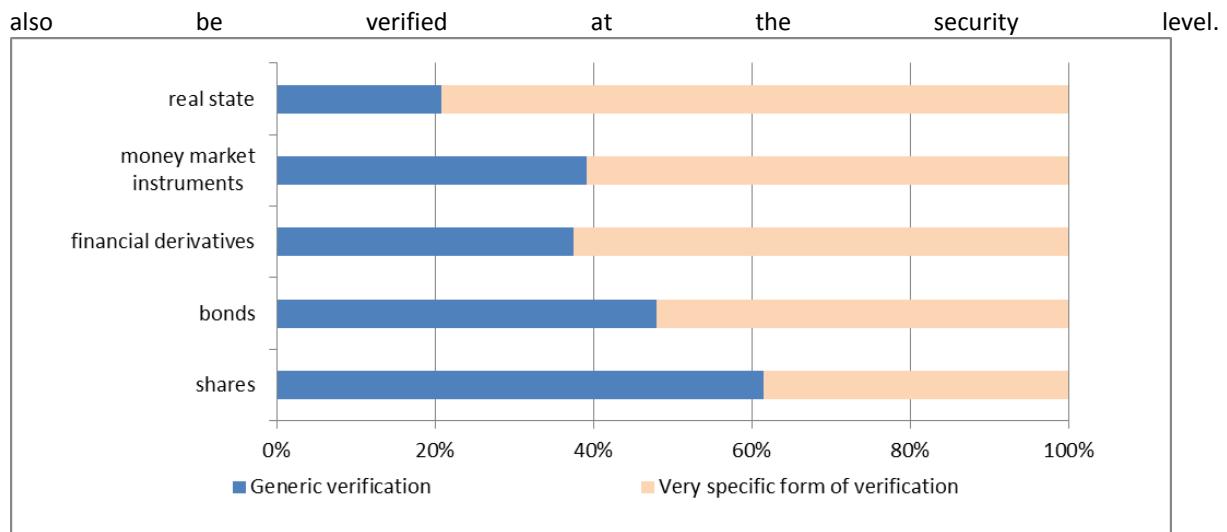


Figure 35 – Generic or specific form of verification for selected financial products

A key consideration for the EU Ecolabel is the cost and complexity of assessment and verification for applicants, therefore stakeholders provided with some examples on how this can be streamlined and minimised effectively:

a) building up on the existing national schemes in terms of:

- harmonization with criteria/structure of existing labels to reduce the cost for applicants who wish to apply
- defining clear and general standards to lower the costs due to the scale effects
- As there is a broad spectrum of ESG strategies and understandings across Europe, there should be a minimum level implemented and only special cases should be valued extraordinary.
- development of a web-based application tool so that the applicants fill in the details on their investment fund and upload documentation.
- Shortening the reporting of results and making them understandable for all parties involved.
- Encouraging the cooperation of competent bodies to a greater extent for the sake of capacity building or reducing the number of assessor across Europe.

b) streamline/simplify the verification process by

- involving a third party verification
- including mutual recognition for those criteria that are verified by other label/third party organization or standard.
- harmonizing the methodology for all certified verifiers
- developing a verification process based on a multi-stakeholder process, with a maximum degree of transparency so that other stakeholders can review it and if needed comment on the verification results
- provision of a practicable (compact) audit record
- provision of historical information on the full portfolio of holdings. However, financial product providers will likely have to rely on external sustainability rating data for portfolio management. This data might not be easily shared with verifiers as the data are confidential. Self-reporting can be a solution that increases transparency, however, third party verifiers will have to rely on this self-reported data.

Q5.2 To what extent and under what conditions, should private verifiers be permitted to assess compliance with the EU Ecolabel criteria?

Stakeholders expressed that private verifiers should be permitted to assess compliance with the EU Ecolabel criteria to a great extent or very great extent (50% and 19% respectively).

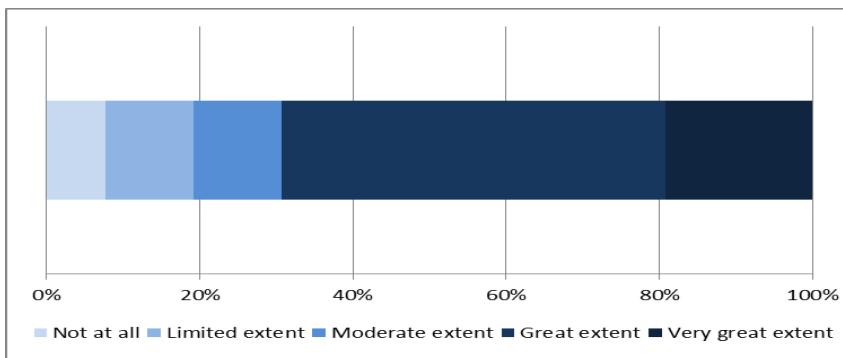


Figure 36 – Permission for verifying EU Ecolabel criteria to private verifiers.,

Additionally, they provided further rationale on this point, suggesting that:

- private verifiers should be supervised by an official entity or a certification body
- private verifiers should be certified and free from any conflict of interest. They could be members of an independent and international, non-profit association
- private verifiers from well-reputed labelling schemes in the financial area could be used to some extent in the verification process to reduce costs and reliability concerns. However, the possibility itself of opening the verification to private entities could bring concerns regarding the costs and reliability of the verification.
- private verifiers will increase the costs of the verification, increase a risk of no harmonization or different interpretation of the criteria and not increase the knowledge of sustainable financial products in the competent bodies of the EU Ecolabel board
- the complexity of the verification and the dynamic market evolution might make private verifiers necessary for assessing compliance in a reasonable timeframe

Finally, stakeholders were requested to provide any other suggestion or recommendation for the assessment and verification process. In the final remarks, they suggested that

- an annual update-audit should be mandatory because the portfolios may change rapidly. This update-audit shall only assess if the portfolio is compliant with the criteria, if possible obligations are met or if anything fundamental (e.g. change of sustainability model) has changed since the assessment and verification.
- The number of certified verifiers should be limited and the cost of the verification should be predefined by EU and partially be subsidised. This will limit the competition between verifiers and will encourage product owners to apply. The choice of the verifier should be at the discretion of the product owner
- Criteria should make sure that the labelled financial product can deal with holding/companies when breaches occur in a standardized way
- The EU Ecolabel should be awarded for a fixed period (i.e. 2-3 years) and only if there is a change in strategy, a statement to the verifier should be made.
- The application fee must be discussed and determined outside the general fee structure for the EU ecolabel