

JRC TECHNICAL REPORTS

Development of EU Ecolabel criteria for Retail Financial Products

(Draft) Technical Report v1.0:
Draft criteria proposal for the
product scope and ecological criteria

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March 2019



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1 INTRODUCTION

The main objective of this study is the development of EU Ecolabel criteria for financial products. The study has been carried out by the Circular Economy and Industrial Leadership and the Finance & Economy Units of the Joint Research Centre (JRC) of the European Commission. The work is being developed for the European Commission's Directorate General for the Environment (ENV) and in collaboration with the Directorate General for Financial Stability, Financial Services and Capital Markets Union of the European Commission (FISMA).

The EU Ecolabel criteria are designed to promote the use of the most environmentally friendly products as articulated by Regulation on the EU Ecolabel (Regulation (EC) No 66/2010 of the European Parliament and of the Council of 25 November 2009 on the EU Ecolabel), hereafter, the 'EU Ecolabel Regulation'. According to Article 2 this Regulation applies to “products” (either goods or services) that are supplied for distribution, consumption or use on the Community market.

As part of the study this Technical Report is intended to provide the background information for the first Ad-hoc Working Group (AHWG) meeting on the development of EU Ecolabel criteria for this product group scheduled to take place in April 2019. The main purpose of this Technical Report (TR) is to present proposals for future criteria, which can be feasible for the product group under study. The proposals presented take into account the results of the Preliminary Report (PR) which provides the legislative, market and technical analysis to support the criteria proposals. For the proposed scope and each criterion proposal, questions that require further consultation with the stakeholders are also listed.

1.1 THE EU ECOLABEL CRITERIA DEVELOPMENT PROCESS

A typical process of developing the EU Ecolabel criteria for any product group is set out in Article 7 and Annex I of the Ecolabel Regulation. This entails the management of a process of stakeholder consultation to be supported by the development of the following documents by the party which is leading the process: (1) a Preliminary Report; (2) a proposal for draft criteria; (3) a Technical Report in support of the proposal for draft criteria; (4) a final report; and; (5) manuals for potential users of the EU Ecolabel and Competent Body (CBs), and for authorities awarding public contracts.

Moreover the EU Ecolabel Regulation also stipulates that a minimum of two Ad-Hoc Working Group (AHWG) stakeholder meetings shall be held along the criteria process, the first of which will take place in April 2019. At these meetings the material contained in the Preliminary Report, together with the scope and criteria proposals contained in the supporting Technical Report, shall be tabled for discussion. The feedback from these meetings, together with associated rounds of written consultation, shall be used by the party leading the process to further adapt the scope and criteria proposals.

This TR has been drafted in accordance with Article 7 of the EU Ecolabel Regulation and will be updated during the criteria development process based on new information, stakeholder feedback and input from the AHWG meetings. The final TR will incorporate all relevant scientific arguments substantiating the final criteria proposal.

In addition to the above-mentioned first AHWG meeting in April, a second AHWG meeting is foreseen in October 2019.

1.2 SUMMARY OF THE PRELIMINARY REPORT

The PR was drawn up based on an analysis of information and data available on green financial products. This encompassed several sources including academic literature, industry or consumer association reports, results from the first stakeholder questionnaire survey, and consultation (in the form of bilateral interviews) with selected financial label and scheme operators. The PR focusses on the following main aspects:

- Scope, definition and relevant EU legislation
- Market analysis
- Technical analysis of existing taxonomies and the definitions of "green" financial products
- Identification of the need for an EU Ecolabel for financial products (as a conclusion of the preliminary report)

1.2.1 Background

Sustainability has long been at the heart of the European project and the European Union (EU) is fully committed to reaching the EU 2030 climate and energy targets and to mainstreaming 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 European Commission established a High-Level Expert Group (HLEG) 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 European Commission published an Action Plan: Financing Sustainable Growth (hereafter, the 'Action Plan')¹. This Action Plan puts forward ten actions whose main objectives are to

(i) reorienting capital flows towards sustainable investments to achieve sustainable and inclusive growth;

(ii) managing financial risks stemming from climate change, resource depletion, environmental degradation and social issues; and

(iii) fostering transparency and long-termism in financial and economic activity.

Actions i and ii of the Action Plan refer to: “Establishing an EU classification system for sustainable activities” (“EU Taxonomy”), and “Creating standards and labels for green financial products” (report on an EU green bond standard; the use of the EU Ecolabel framework for certain financial products). Specifically, the Commission sees potential merits in the use of the EU Ecolabel Regulation for a new EU-wide labelling scheme for certain financial products.

As follow-up to the Action Plan, the Commission adopted a package of legislative proposals in May 2018 (“the May 2018 Package”). This package inter alia included a proposal for a “Regulation of the European Parliament and of the Council on the establishment of a framework to facilitate sustainable investment” (hereafter “the Taxonomy proposal”)².

A further follow-up is the preparation of a Commission decision defining criteria to be fulfilled by financial products in order to qualify for the EU Ecolabel. This happens in the framework of the EU Ecolabel Regulation, which provides guidance as to how criteria should be developed and implemented for products and services. It is also a part of a broader EU Action Plan on Sustainable Consumption and Production and Sustainable Industrial Policy (European Commission, 2008). This Action Plan was already adopted by the European Commission on 16 July 2008 and links the EU Ecolabel to other EU policies such as green public procurement (GPP), the ecodesign of energy-related products, and the EU Action Plan for the Circular Economy.

The EU Ecolabel is a voluntary ecolabel award scheme intended to promote products with a reduced environmental impact during their entire life cycle and to provide consumers with accurate, non-deceptive, science-based information on the environmental impact of products.

¹ 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>

² 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).

According to the EU Ecolabel Regulation, the label may be awarded to "goods and services" which are supplied for distribution, consumption or use on the Community market whether in return for payment or free of charge. Financial products would fall within the scope of the EU Ecolabel Regulation where they can be considered as services for distribution or use. **It is important that consequently, it is the financial service as such being provided by the product manufacturer of the green financial product which would be ecolabelled, while the EU Ecolabel logo may figure on the promotional material of the green product itself.** The EU Ecolabel criteria can therefore be particularly useful for retail investors who would like to express their investment preferences in relation to the environmental sustainability of the activities funded by their money.

For financial services provided and products offered in this context to retail investors, a number of Regulations and Directives exist and need to be considered. For example, the Packaged Retail Investment and Insurance Products (PRIIPs) Regulation (EU) No 1286/2014 seeks to enable investors to better understand and compare the key features, risks, rewards and costs of different PRIIPs. The definition of the products in the scope and out of the scope of the PRIIPs Regulation is provided in the next section. Directive 2009/65/EC regulates and stipulates provisions on undertakings for the collective investment in transferable securities (UCITS) that are a popular product among retail investors. Directive 2011/61/EU (AIFMD) regulates the managers of alternative investment funds, such as hedge funds and private equity³. The non-financial and diversity information Directive 2014/95/EU is relevant in regards to the disclosure of information about environmental protection and social responsibility by certain large undertakings and groups.

1.2.2 Market analysis

The market analysis carried out in support of the first scope and criteria proposals has focussed on retail clients as investors. A retail client is one that is not a professional client, i.e. a client who does not possess the experience, knowledge and expertise to make its own investment decisions and properly assess the incurred risks.⁴ Retail clients are mostly composed of households, being the major contributors to the net financial wealth (i.e., all financial assets minus all financial liabilities) of the Euro Area.

Statistics show that EU-28 households own about EUR 34 tn of cumulated assets, and their financial liabilities are equal to 30% of their financial assets. Currency and deposits, pension funds, and (life and non-life) insurance products constitute around 30%, 20%, 18%, respectively, of the EU-28 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.

Many of the above mentioned products are covered by the PRIIPs Regulation. PRIIPs products are packaged retail and insurance-based investment products that e.g. banks, insurances and asset managers typically offer to retail clients. PRIIPs⁵ include:

- (i) packaged retail investment product (PRIP), 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.

³ This Directive is only of relevance, where Member States decided to allow the marketing to retail investors on their territory.

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

⁵ See Regulation n. 1286/2014 of PRIIPs Regulation, Article 4(1)-(3) and the Discussion Paper "Key Information Documents for Packaged Retail and Insurance-based Investment Products (PRIIPs)" n. JC/DP/2014/02.

The following products are out-of-scope of the PRIIPs Regulation:⁶

- (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 scope of the PRIIP Regulation 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. PRIIPs cover a range of investment products which, taken together, make up a market in Europe worth up to EUR 20 tn at the end of 2017. Investment funds, unit-linked life insurance products and unit-linked pension funds taken together account for a large part of the PRIIPs market.

Depending on the source there are understood to be between 60k and 80K investment funds domiciled in the EU (EFAMA Q1 2018 and Bloomberg, October 2018), with net assets amounting to around EUR 15 tn⁷. About 72% of the total net assets of investment funds are invested predominately in equities and/or bonds. EU legislation distinguishes between UCITS funds and AIFs. UCITS and AIFs funds reached an outstanding amount of about EUR 9 tr and EUR 6 tr, respectively, at the end March 2018. Some AIFs are sold to retail investors following regulation at the national level, although such funds are in principle designed for professional investors.

According to Bloomberg, 421 funds are currently marketed as green or sustainable⁸. These funds are further classified as clean energy, climate change, environmentally friendly and environmental, social and corporate governance (ESG) funds⁹. This represents about 0.01% of the total active funds (see Kahlenborn et. al., 2017, on the very low market shares of sustainability or environmentally themed investing and green impact investing).

As for other PRIIPs categories, the market for life insurance products offering non-guaranteed products linked to either investment funds (i.e. unit-linked contracts), or structured products (i.e. index-linked products) amounts to about EUR 3 tn. Approximately 25% of households' financial assets are composed by stocks and debt securities. A particular category among bonds are "Green bonds", which finance or re-finance in part or in full new and/or existing eligible green projects. This specific product has received attention both at EU level and by private initiatives. However, the European green bond market is still very small in size compared the

⁶ See Regulation n. 1286/2014 of PRIIPs Regulation, Article 2(2).

⁷ Source: EFAMA Q1 2018.

⁸ 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.).

⁹ One fund can be classified into more than a category, and approximately 35% of these funds are also classified as Socially Responsible Funds. For example, 49 funds belong in the category "Socially Responsible and ESG".

market of conventional bonds, corresponding to approximately 2.5% of the total bonds market in 2018. It is worthy of note that about 36% of the global amount of green bonds was issued by EU companies in 2017.

1.2.3 Technical analysis

Initial evidence suggests that a range of strategies are employed in order to make investment portfolios more attractive to customers seeking green or environmentally sustainable financial products. An increasing proportion of assets are currently managed based on a number of sustainable investment strategies including:

- exclusionary screening,
- positive screening or best-in-class approach,
- norms based screening approach,
- ESG integration,
- sustainability themed investing or thematic investing,
- impact/community investing, and
- corporate engagement and shareholder action.

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. The share of each asset class in a portfolio is referred to as the asset allocation of that portfolio. These could be directly or indirectly invested in.

A number of labels and schemes are available in Europe to help investors assess and select from a range of financial products which are described as sustainable or green. These include the TEEC Label¹⁰, FNG Siegel¹¹, Nordic Swan Ecolabel¹², Luxflag Climate Finance Label¹³ and the Austrian Ecolabel¹⁴ amongst others. Some of these labels and schemes define the "greenness" of an investment portfolio either by setting a requirement or threshold on:

- 1 the minimum proportion (in percentage) of a portfolio's total assets under management mandated to be invested either in climate change mitigation and or climate change adaptation activities or;
- 2 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 which are defined in the taxonomy applied by the label or scheme.

The existing labels and schemes also make use of taxonomies to define green sectors or economic activities, in some cases with reference to screening criteria.

The different strategies, criteria and taxonomies employed by the prevailing labels and schemes, create uncertainties for investors as they are unable to compare different type of information for different financial products. It also represents an obstacle to the flow of capital towards more environmentally sustainable economic activities.

A Taxonomy is a classification system that categorises different economic activities and provides criteria as to what can be considered an environmentally sustainable economic activity. These economic activities could be projects or activities in specific economic sectors of any economy in areas such as renewable energy and green buildings amongst others. Regional and

¹⁰ Energy and Ecological Transition for the Climate. Available at https://www.novethic.com/fileadmin/user_upload/divers/labels/1605-LabelTEEC_Referentiel-ENG.pdf

¹¹ FNG – Siegel. Available at <https://www.fng-siegel.org/en/siegelkriterien-en.html>

¹² Nordic Swan. Available at <https://www.nordic-ecolabel.org/>

¹³ Luxflag, <https://www.luxflag.org/labels/climate-finance/>

¹⁴ The Austrian Ecolabel (January 2016). Eco-label Guideline UZ 49 for Sustainable Investment Products. Version 4.0. Available at: https://www.umweltzeichen.at/file/Guideline/UZ%2049/Long/Ec49_R4a_sustainable_Investment_products_2016.pdf

national labels as well as schemes available in Europe certify the “greenness” of financial products using any one of the following taxonomies:

- 1 the Climate Bond Initiative (CBI) taxonomy;
- 2 the Green Bond Principles (GBP) project categories; and
- 3 the International Development Finance Club (IDFC) taxonomy.

These taxonomies differ in the manner in which they categorise different economic activities as environmentally sustainable. They also differ in their levels of granularity (see the PR for information).

This analysis of existing national and regional labels for green and environmentally sustainable financial products suggests that EU Ecolabel criteria could rely to some degree on a taxonomy. However as the existing taxonomies are incomparable and have varying degrees of granularities, a harmonised taxonomy at the EU level is needed. The framework established by the EU Taxonomy proposal will therefore be used as guidance in the development of the EU Ecolabel criteria, and the link with the EU Taxonomy will be established by taking a “look-through” approach. This will entail 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.

The EU Ecolabel will, moreover, define criteria for determining whether financial products offered to retail investors are sufficiently “green” to be awarded with the label. This will require careful consideration of the following aspects:

- The scope of financial products to which the EU Ecolabel criteria is applicable.
- The potential for the product to deliver environmental benefits and to attract retail investors.
- Operational issues and product verification.
- Identification of optimal strategies to be considered in the EU Ecolabel criteria in order to promote environmentally sustainable investments based on definition of “greenness” provided by the criteria.
- How the EU Taxonomy will be used in the context of the EU Ecolabel.
- Options for compliance with the requirements of proposed EU Ecolabel criteria for the purpose of awarding the label e.g. mandatory requirements, or optional requirements with a point-based scoring system.

1.2.4 Towards the EU Ecolabel criteria

This section provides an overview of how the criteria set could be configured. This includes the identification of the environmental themes that should be covered by the criteria, the structure of the criteria and the assessment and verification possibilities. The structure of the criteria is initially described here in terms of broad criteria areas so that the overall design and coverage of the proposal can be discussed with stakeholders. Then the technical scope of each specific criterion is developed further in subsequent sections of this paper.

Green investment is generally associated within the financing of investments that provide environmental benefits such as a reduction in greenhouse gas and air pollutant emissions, without reducing the production and consumption of non-energy goods. Financial products or investments are therefore green as a result of the uses to which the money is put in terms of the underlying assets or economic activities.

The prevailing and overlapping concepts of “green” used to date by investors have been developed around four main types of investment strategies: (1) Socially-responsible investing (SRI); (2) Environmental, social and governance (ESG) investing; (3) Impact investing, and (4) thematic investing.

Of these strategies, impact investing and thematic investing specifically focus on activities that will deliver a specific and measurable social or environmental performance or improvements. Green thematic investing will address specific environmental objectives or problems and can provide important information for the definition of green.

The criteria proposals for the EU Ecolabel are aimed at enhancing the environmental benefits of investments and thus "greenness" in the context of the EU Ecolabel is proposed to be defined via criteria which set requirements covering:

- Green economic activities,
- Green investment thresholds,
- Exclusions based on compliance with one or more of the environmental objectives of the EU taxonomy, and
- Exclusions based on social and ethical aspects (see Table 1).

To facilitate the identification of economic activities and sectors that qualify as "green", in a harmonised and consistent manner, a criterion requiring the use of the EU taxonomy is proposed. In this sense, "green" will mean economic activities that contribute to the achievement of the environmental objectives as described in the EU Taxonomy. Currently, the EU Taxonomy focuses on identifying the economic activities that significantly contribute to climate change mitigation and climate change adaptation while not harming any of the other four criteria such as water use, circular economy, etc. In the future, the EU Taxonomy will identify any economic activity that significantly contributes to the achievement of any of the six EU Taxonomy objectives.

In addition to the identification of green economic activities through reference to the EU Taxonomy, the use of exclusions which limit the flow of investments into economic activities or sectors which are considered as not to be environmentally friendly or sustainable, or that do not fulfil the level of ambition of the EU Ecolabel will ensure that the EU Ecolabel is awarded to the best environmental performing products.

Another aspect to take into account when linking the EU Ecolabel criteria to the Taxonomy is that the Taxonomy will cover minimum social safeguards, while the EU Ecolabel requires taking into account "where appropriate, social and ethical aspects". These aspects have been identified through both the stakeholder survey and reviews of the existing schemes and labels as being important issues for investors. Therefore, the set of criteria proposed for the EU Ecolabel will also consider these aspects.

The first proposal for the structure of the EU Ecolabel criteria for discussion at the 1st AHWG meeting is presented in Table 1.

1st criteria proposal and criteria structure**Table 1 – Proposed structure for the EU Ecolabel criteria for financial products**

Criteria area	Criteria	Technical scope
Environmental aspects	1. Thresholds on green investment portfolio and economic activities <i>1.1 Green investment minimum thresholds</i>	<ul style="list-style-type: none"> Portfolio threshold for minimum % investments in activities and sectors qualifying as "green" according to the EU Taxonomy Threshold for minimum % turnover from company engagement in activities and sectors qualifying as "green" according to the EU Taxonomy For bonds: compliance of bonds contributing to meeting the portfolio threshold with the EU Green Bonds Standard
	<i>1.2 Green economic activities</i>	<ul style="list-style-type: none"> List of economic activities and sectors qualifying as "green" according to the EU Taxonomy
	2. Exclusions based on environmental aspects	<ul style="list-style-type: none"> List of specific sectors to which exclusionary thresholds will apply
Social and ethical aspects	3. Exclusions based on social & ethical aspects	<ul style="list-style-type: none"> List of social and ethical aspects to which exclusions will apply
Information	4. Retail investor information	<ul style="list-style-type: none"> List of information requirements to be provided/made publicly available to retail investors
	5. Information appearing on the EU Ecolabel	<ul style="list-style-type: none"> Information on the EU Ecolabel logo, registration number and statements that could appear on the EU Ecolabel.

1.2.5 How the criteria set could work

This section discusses the possible approaches to how the applicant would need to fulfil the criteria requirements and then subsequently formally assess and verify a retail financial product in order to obtain an EU Ecolabel license. The EU Ecolabel is a pass or fail system, meaning that to get the label awarded to their products, applicants have to fulfil a set of criteria. Failing to fulfil the criteria means that the EU Ecolabel cannot be awarded. There are basically two options for setting the criteria: making them all mandatory, or setting optional criteria with a point-based system. The two options are presented and analysed below.

1.2.5.1 Mandatory vs Optional Criteria set

Depending on the product group, both mandatory criteria sets and optional with point-based systems have been used for EU Ecolabel criteria, including a combination of the two. The potential advantages and disadvantages of the two approaches are briefly evaluated in this section.

A point-based system may be used for some or all of the criteria. In a point-based system, a number of points is attributed to each optional criterion. The product receives a number of points depending on which optional criteria it complies with. Then, the total number of points is calculated and there is a minimum threshold that needs to be achieved in order to be awarded the label. A point-based system can be used as a stand-alone system or in combination with mandatory minimum criteria.

The main benefit of a points-based approach is that it allows for flexibility, i.e. there will be various ways in which the green financial product can be awarded the EU Ecolabel. This may allow for a greater volume of products to be potentially eligible and encourage mainstream financial actors to apply for the label¹⁵.

When all criteria are mandatory, if the product does not fulfill all of the criteria requirements, it fails and cannot be awarded the EU Ecolabel. On one hand, the fact that all criteria are mandatory and all EU Ecolabel products fulfil all of them in the same way can be perceived as a more transparent system and could enhance investor confidence. On the other hand, this type of system has the disadvantage of not providing flexibility to the applicant to comply with the criteria. This could result in a smaller market for the EU Ecolabel. An overview of the advantages and disadvantages of both systems is briefly presented in Table 2.

The feasibility of applying the point-based system to the EU Ecolabel for financial products was explored with the stakeholder questionnaire survey. However, it did not appear that stakeholders considered "highly appropriate" that the EU Ecolabel should adopt a point-based system as only 30% of the respondents voted in favour of the approach. 36% of the respondents considered a point-based system moderately appropriate. Based on the response and considering the risks that this approach could result in different levels of importance being applied to varying aspects of the criteria, this option is not proposed to be pursued further.

A system with all mandatory criteria is therefore proposed, except for the criterion on EU Ecolabel information, that refers to the text that can be displayed with the EU Ecolabel logo, and is an optional requirement according to the EU Ecolabel Regulation.

Table 2 Summary evaluation of pass/fail and point-based EU Ecolabel systems

System	Advantages	Disadvantages
Pass/fail	Strict compliance to all requirements /no flexibility	Difficulty of prioritisation of the most relevant criteria
Point-based	Possibility of prioritising criteria and flexibility in the application of criteria	If unsupported by some mandatory could result in very poor performance in environmental aspects

Question to Stakeholders

1.1 Do you agree with the proposal of a set of mandatory criteria for the EU Ecolabel for this Product Group?

1.2.5.2 Assessment and verification

In order to simplify and reduce the costs of assessment and verification the EU Ecolabel criteria for financial products could consider recognising the commonalities that each criteria share with those of national and regional schemes. This aspect is still being investigated within the assessment and verification of each criteria.

The specific assessment and verification requirements are indicated within each criterion. Where the applicant is required to provide declarations, documentation, analyses, or other evidence to show compliance with the criteria, these may come from the applicant and/or their supplier(s) and/or their subcontractor(s). As a pre-requisite, the 'financial product services' shall meet all legal requirements related to the place of product manufacture, registration and authorisation.

¹⁵ Product volume in this context refers to the number of EU Ecolabel licences for the product group

Competent bodies shall give preference to attestations that are issued by bodies that are accredited under the relevant harmonised standard for bodies certifying products, processes and services. Accreditation shall be carried out in line with Regulation (EC) No 765/2008 of the European Parliament and of the Council. Competent bodies may require supporting documentation and may carry out independent checks.

After being awarded the EU Ecolabel licence, the applicant is required to inform the relevant Competent Body of any changes pertaining to their licensed product(s). Because of the dynamic nature of financial products the current practice within other labels and schemes is to provide updated information on a financial product every six months. Such information related to any changes or deviations should include the following:

- Investor information and investment policy,
- The methodology for computing the portion of turnover in accordance with Criterion 2,
- The environmental objectives of the portfolio,
- The financial objectives,
- Corporate activities and governance structures of the company managing the portfolio,
- Management and internal control procedures for addressing risks of excluded activities in the investment portfolio.

The competent body may perform follow-up assessments of the applicant's financial product annually during the award period.

2 PRODUCT SCOPE AND DEFINITION

This section introduces the proposal for the scope of the Financial Product group together with the supporting background discussion and rationale. Additionally, the key definitions that underpin the scope proposal the EU Ecolabel for Financial Product group are also presented in this section. A summary of the results of the stakeholder questionnaire is provided at the end of the section.

2.1 Scope

2.1.1 Target clients for the EU Ecolabel

European financial services regulations make a distinction between 'professional clients' and 'retail clients'. In the context of the EU Ecolabel, which is aimed primarily at consumers, the attention is therefore focused on the possibility to label financial products that are targeted at non-professional retail clients.

Regulation also recognises that a non-professional retail client would, in general, tend to have a more limited knowledge of the potential risks and the underlying investments associated with different financial instruments into which their money may be invested. Therefore, they would benefit the most from an EU Ecolabel for financial products. If, as emphasised by the findings from the questionnaire (see the box below), the intention should be to use the EU Ecolabel to 'promote green finance' it would therefore also seem logical to focus most attention on those financial products that are typically offered to retail customers, such as those under the PRIIPS Regulation and some products which do not fall in the scope of the PRIIPS Regulation.

2.1.2 Retail products in the scope of the EU Ecolabel

The preliminary report to this study identified the main financial assets held by retail clients. In 2017 the majority (68%) of household money in the EU was held in a combination of currency and deposits, pension funds and insurance products. However, how households allocate their financial wealth varies across the EU Member States (see Figure 1):

- In the Czech Republic and Greece currency and deposits account for over 50% whereas in others this share can drop to as low as 14%.
- In Ireland and the Netherlands pension funds are more prominent, with more than 30% share, whereas in others this share can drop to as low as 5%.
- In France and Denmark life insurance and annuities are more prominent (28 – 36%)

The scope of the EU Ecolabel should recognise the differences in allocation choices made across the EU, so as to ensure that the most prominent products have the potential to be labelled.

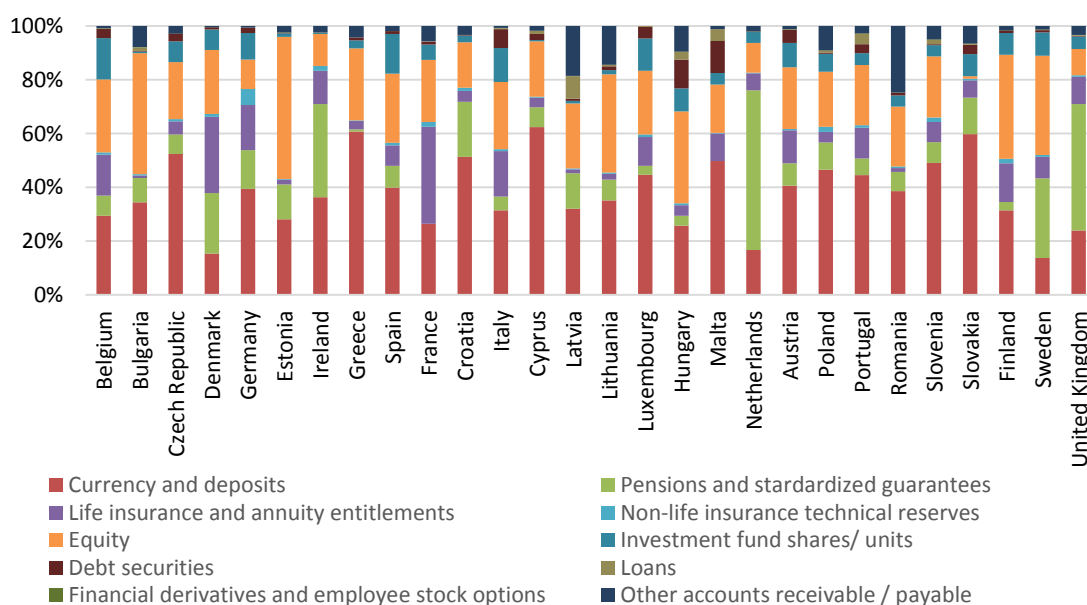


Figure 1 – Share of total financial assets of households across countries, by financial instruments in 2017. Source: Eurostat (2018)

Of those products that are within the scope of the PRIIPs Regulation, investment funds and unit-linked life-insurance products¹⁶ are of particular relevance for the scope of the EU Ecolabel both in terms of market importance and the potential to verify their underlying assets. Q3.2 of the stakeholder questionnaire identified these two products as the most popular for inclusion within the first ecolabel product scope, with 84% of respondents selecting investment funds and 58% selecting ‘life insurance with an investment element’ and ‘pension funds’ respectively. Moreover, their inclusion within the scope would be broadly consistent with those that are addressed by current labels and schemes, as the majority of them do not include directly held assets.

Investment funds, which can take a number of different forms, stand out from the market analysis in the preliminary report to this study as an important mainstream product made available to retail clients and would therefore be a good fit for the first scope of the ecolabel. They provide an alternative to simpler products for retail clients seeking to obtain a better short to medium term return from their savings and investments.

In terms of products that target similar retail clients, those insurance products that have a unit-linked investment component – such as some types of individual pensions as well as annuities – can be seen to target a similar market for income in retirement, so if these products were to be included in the scope they should be included together. Pension products have since the 1980s been a focus for the development of more responsible investment policies by fund managers. In particular, public and private institutional funds are understood to have played the most significant role and could, moreover, be considered of relevance to public procurement in cases where the service is outsourced¹⁷.

Also highlighted by stakeholders in the response to Q3.2 of the stakeholder questionnaire were bonds (42%) and savings accounts/products (31%). While both public and privately issued bonds are likely to feature within the underlying assets of a product such as an investment fund, they can also be purchased by a retail client via a retail broker. If bonds were considered within a future possible scope of the ecolabel this would have the benefit of allowing for a ‘green’ bond product to be directly identified by retail clients. However, careful consideration would be

¹⁶ including unit-linked pension products

¹⁷ Global Sustainable Investment Alliance, Global Sustainable Investment Review 2016.

needed as to how bonds awarded the ecolabel would co-exist with and complement the proposed EU Green Bond Standard. This aspect is discussed further in section 3.1.2. Bonds issued by public authorities could be relevant in so far as they would need to stipulate compliance with the EU Ecolabel requirements for underlying assets in any procurement carried out using the proceeds from green bonds.

Although 31% of respondents suggested that savings accounts could be considered within the scope, this could include a variety of simpler savings products, potentially also including deposits. While deposit accounts were identified in the preliminary report to this study as being of significance in terms of household financial assets, one of the types of deposit that is a PRIIPs product – namely structured deposit accounts which combine a deposit with an investment element – are from the limited market information available not understood to currently be of significance across the EU¹⁸. Moreover, verification of greenness for savings accounts that do not have a structured investment element could be difficult because of the variety of ways in which the money may be used. For example, money may be used to provide loans to companies or specific projects.

Whilst it may potentially be feasible to verify the savings products of specialist banks such as Triodos, who conduct a strict screening of all loans and investments they make, it is to be discussed with stakeholders which of the savings account products of high street banks could be possible to ecolabel. A possible model is the Green Funds Scheme in the Netherlands, which was referred to in the preliminary report to this study. The fund supports the identification and certification as green of projects that can then be funded by both green investment funds and green savings accounts¹⁹.

2.1.3 Verification of the underlying assets

In order to allow for verification of ‘greenness’, it will therefore be important to understand how each product is developed by the product manufacturer and what the underlying financial assets are that would need to be verified. Criteria for the most readily verifiable underlying assets - shares, bonds and real estate holdings - should be developed so that those retail financial products, which may include these assets in their portfolio, can be awarded with the EU Ecolabel. The potential to verify these underlying assets is addressed further in section 3.1.1

Based on the experience of existing labels and schemes, and as also highlighted in the market analysis, investment funds also may hold indirect investments in other alternative funds that also comprise equities, bonds and real estate. This creates challenges related to the traceability and consequently verification of performance due to the complexity of such fund structures. This issue is considered further in section 3.1.1

2.1.4 Place of product manufacture, registration and authorisation

In line with the EU Ecolabel Regulation (EU) 66/2010 art 2.1 the EU Ecolabel criteria for Retail Financial Products shall apply to any retail financial product which is supplied for distribution in the Community market. Additionally sectoral EU legislation applies that will already define the rules for manufacture and distribution of a product in the EU. This aspect may differ from some existing schemes and labels that allow for products that are subject to third country regulatory requirements that are considered by the label or scheme to be equivalent to those of EU Member States.

¹⁸ European Banking Authority (2018) *EBA report on cost and past performance of structured deposits*.

¹⁹ Netherlands Ministry of Housing, Spatial planning and the Environment, *The Green Funds Scheme – Focus on environment*, https://www.rvo.nl/sites/default/files/bijlagen/SEN040%20DOW%20A4%20Greenfunds_tcm24-119449.pdf

2.1.5 Rationale of the proposed retail financial product scope

As this is the first development of EU Ecolabel criteria for Financial Products, the analysis suggests that it may be appropriate to start with a narrower product scope that could be extended in future revisions.

For this first stage, the objective is to cover financial products typically offered to retail investors. This is because the EU Ecolabel is mainly intended to support retail investors in their decision-making process. It therefore makes sense to include in its scope the service provided by the product manufacturer in relation to those financial products that are meant to be sold to retail clients. This includes PRIIPs products.

As PRIIPs are the core of the retail investment market, it is therefore in turn also proposed to start the development of EU Ecolabel criteria by focusing on a number of specific PRIIPs products.²⁰ Moreover, in order to ensure the relevance of the EU Ecolabel for the investors, it is important not to target only niche markets but instead to seek to promote mainstream green finance. In this respect, investment funds and unit-linked insurance products taken together account for a large part of the PRIIPs market. In addition to the market share of products the following considerations have been made in formulating the first scope proposal:

- That the products are substitutable i.e. that they encompass competing offers that may be made to retail clients;
- That they have to some extent already been possible to label by existing EU schemes; and
- That they include, with reference to the criterion 1 proposal, verifiable underlying asset classes i.e. that consist primarily of equities and bonds.

Based on these considerations investment funds together with insurance-based products that have an investment element analogous to investment funds have been included within the first proposed scope. Insurance-based products can include unit-linked insurance sold as individual pension or annuity products.

In later stages, and based on the market analysis and feedback received from stakeholders, other products covered by the PRIIPs Regulation as well as products outside the scope of the PRIIPs Regulation could be included. For example, savings accounts were highlighted in the survey response and deposit accounts were identified within the market analysis as important. However, for both savings and deposit products the potential to identify and trace specific underlying assets or the economic activities financed with loans will be important and will require further discussion with stakeholders. This is because they will need to be verifiable according to the proposed criterion 1.

In regards to the relevance of the scope for public procurement, those services that provide an income in retirement as well as bonds for which the use of proceeds is for specific projects could be of greatest potential relevance. In particular, public pension funds are an important service provided by public authorities and have played an important role in the development of greener financial products over the last few decades.

²⁰ Definition of PRIIPs products in section 1.2.2.

1st proposal for the Retail Financial Products scope:

This product group shall comprise the following financial products that are provided as a service by a fund manager and have been packaged for retail investors in accordance with the requirements laid down in Regulation (EU) No 1286/2014 on packaged retail and insurance-based investment products (PRIIPs):

- Investment funds, to include those referred to as Undertakings for the Collective Investment in Transferable Securities (UCITS) and, where applicable²¹, Retail Alternative Investment Funds (RAIFs);
- Insurance-based products with an investment component, such as individual unit-life insurances.

The retail financial product shall be registered or authorised for marketing or distribution in a member state of the European Union.

Questions to stakeholders

- 2.1 Do you agree with initial proposed scope for the EU Ecolabel?
- 2.2 Do you think other financial products/services should be included that are not covered in the initial proposed scope?
- 2.3 To what extent could savings and deposits be included within the scope in the future given the need to be able to identify specific uses of the money held in them as being 'green'?
- 2.4 While bonds are included as underlyings to investment funds, to what extent could retail bond products themselves be included within the scope in the future, with verification of their greenness based on the Green Bond Standard?
- 2.5 Are there any other financial products or retail investment opportunities that could be considered for a future scope?

²¹ AIFs may be marketed to retail investors upon a national discretion (art. 43 of AIFMD).

Summary of the results from the 1st stakeholder questionnaire

Here the responses to questions of relevance to the retail product scope are briefly summarised in order to identify the main findings.

Q3.1 Based on your understanding of the current state of the financial market would you agree that UCITS should be included in the first product group(s)?

This question was aimed at testing whether one of the types of funds where retail investors invest the most (UCITS) could form the starting point for the product group scope. 83% of respondents agreed that UCITS should initially be included in the product group scope. An extension of the product group could be carried out in subsequent revisions of the Decision.

Q3.2 More broadly, which retail financial products should be included in the EU Ecolabel first?

This question provided a list of products 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%).

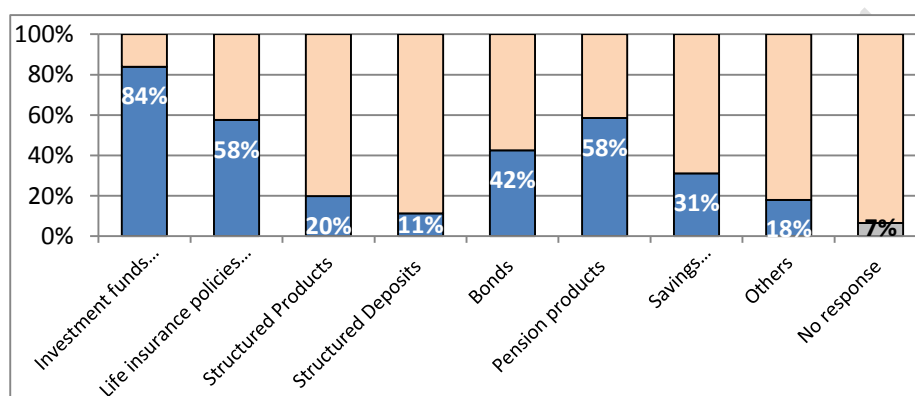


Figure 2 – Retail financial products that should be included within the 1st Ecolabel scope

23 respondents provided an open response to the invitation to elaborate on which products should be included within the scope. A diversity of responses were 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 EU 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.

Q3.3 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 were 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, 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).

2.2 Definitions

In the Commission Decisions establishing EU Ecolabel criteria, there is a possibility of providing term definitions.

Some of the definitions proposed here are specific to a single financial product while others have been developed in order to simplify and clarify the reading of the EU Ecolabel criteria, as well as to ensure a consistent understanding of the technical terms to which it refers. Overall, the proposed text is aimed to be in line with other EU legislation such as PRIIPs Regulation, UCITS or AIFM Directives.

1st proposal for the Retail Financial Products definitions:

For the purposes of this Regulation, the following definitions apply

1. ‘packaged retail and insurance-based investment product’ or ‘PRIIP’ means a product that is one or both of the following:
 - a) a packaged retail investment product (PRIP)
 - b) an insurance-based investment product;
2. ‘packaged retail investment product’ or ‘PRIP’ means an investment, including instruments issued by special purpose vehicles as defined in point (26) of Article 13 of Directive 2009/138/EC or securitisation special purpose entities as defined in point (an) of Article 4(1) of the Directive 2011/61/EU of the European Parliament and of the Council (19), where, regardless of the legal form of the investment, the amount repayable to the retail investor is subject to fluctuations because of exposure to reference values or to the performance of one or more assets which are not directly purchased by the retail investor;
3. ‘insurance-based investment product’ means an insurance product which offers a maturity or surrender value and where that maturity or surrender value is wholly or partially exposed, directly or indirectly, to market fluctuations;
4. ‘retail investor’ means:
 - a) a retail client as defined in point (11) of Article 4(1) of Directive 2014/65/EU
 - b) a customer within the meaning of Directive 2002/92/EC, where that customer would not qualify as a professional client as defined in point (10) of Article 4(1) of Directive 2014/65/EU;
5. ‘alternative investment funds’ (AIFs) means collective investment undertakings, including investment compartment thereof, which:
 - a) raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and
 - b) do not require authorisation pursuant to Article 5 of Directive 2009/65/EC
6. ‘undertaking collective investment transferable securities (UCITS)’ means an undertaking for collective investment in transferable securities authorised in accordance with Article 5 of Directive 2009/65/EC
7. ‘transferable securities’ means:
 - a) shares in companies and other securities equivalent to shares in companies;
 - b) bonds and other forms of securitised debt (debt securities);
 - c) any other negotiable securities which carry the right to acquire any such transferable securities by subscription or exchange;
8. ‘share or stock’ means a type of security that signifies ownership in a corporation and represents a claim on part of the corporation’s assets and earnings;

9. ‘bond’ means a fixed income instrument that represents a loan made by an investor to a borrower (typically corporate or governmental).

10. ‘investment fund’ means a supply of capital belonging to numerous investors used to collectively purchase securities while each investor retains ownership and control of this own shares. Types of investment funds include mutual funds, exchange-traded funds, money market funds and hedge funds.

11. ‘portfolio’ means a grouping of financial assets.

12. ‘asset’ means a resource with economic value that an individual, corporation or country owns or controls with the expectation that it will provide a future benefit.

13. ‘verification’ means a procedure to certify that a product complies with specified EU Ecolabel criteria.

14. ‘portfolio management’ means managing portfolios in accordance with mandates given by clients on a discretionary client-by-client basis where such portfolios include one or more financial instruments;

15. ‘deposit’ means a credit balance which results from funds left in an account or from temporary situations deriving from normal banking transactions and which a credit institution is required to repay under the legal and contractual conditions applicable, including a fixed-term deposit and a savings deposit.

16. ‘structured deposits’ means a deposit as defined in point (c) of Article 2(1) of Directive 2014/49/EU of the European Parliament and of the Council (1), which is fully repayable at maturity on terms under which interest or a premium will be paid or is at risk, according to a formula.

17. ‘Unit-linked’ means that the financial benefits provided by an insurance contract are directly linked to the value of assets contained in an investment fund.

18. ‘Revenue’ means this is the amount of money that is brought into a company by its business activities.

19. ‘Turnover’ is also used as a synonym for investments. In the investment industry, turnover is defined as the percentage of a portfolio that is sold in a particular month or year.

3 CRITERIA PROPOSALS

This section presents the proposed criteria for the EU Ecolabel for Financial Products together with the rationale explaining their relevance and an explanation on how these criteria should be assessed and verified.

A summary of the results of the stakeholder questionnaire is provided at the end of each section. A full set of results for the portfolio level questions are provided in Annex 4.2.

3.1 Criteria area: Environmental aspects

3.1.1 Criterion 1: Thresholds on green investment portfolio and economic activities

This first criterion proposal consists of two interrelated components, the background to each of which is introduced before presentation of the first proposal text:

- 1 definition of the thresholds for the greenness of an investment portfolio based on verification of the underlying assets,
- 2 definition of the greenness of the underlying economic activities invested in by the portfolio manager or management company,

In particular the proposals envisage a link with two other initiatives that stem from the Sustainable Finance Action Plan - the EU Taxonomy proposal and the EU Green Bond Standard.

Rationale of the proposed sub-criterion 1.1 related to the thresholds for the greenness of an investment portfolio

Various methodologies can be used to describe the greenness of financial products. Some of these take the form of thresholds where a specific proportion (in percentage) of a portfolio's total assets under management is required to be invested in economic activities that strongly contribute to the objectives of the EU taxonomy.

The PR for this study identified that current practices on the market are for thematic investments in climate change mitigation and adaptation. For example, the LuxFLAG Climate Finance Label is a certificate for funds that invest at a minimum 75% of their total portfolio assets in projects with a clear contribution to climate change mitigation and/or climate change adaptation activities. The label in turn defines the activities deemed as contributing strongly to these environmental objectives as defined by the activities listed in the IDFC Taxonomy.

Verification of the underlying assets

Once this portfolio level threshold has been established, it needs to be linked to verification of the greenness of each of the underlying assets held within the portfolio. This could include verification for, as for instance:

- equities based on a proposed threshold of 50% of companies revenue that can be attributed to 'green' activities defined with reference to the EU Taxonomy (quantified as a percentage),
- bonds where 100% of the value of the proceeds can be attributed to 'green' activities, again with reference to the EU Taxonomy.
- bonds that have been issued in order to raise general finance for public or private organisations where the proportion of greenness will need to be verified.

If the scope of financial products is expanded at a later stage then other underlying assets may require verification.

The investment portfolios for different products will consist of different asset classes with, as an example, those most commonly held by investment funds comprising company shares (equities), bonds (issued by private corporations, governments and other public authorities), real estate and fund units or shares. Funds may also hold other more complex assets such as derivatives as well as a proportion of cash as liquidity. It is therefore to be determined what proportion of the total investment in these underlying assets should be verified as green.

To ensure consistency and complementarity between EU initiatives, the development of an EU Green Bond Standard (GBS)²² is considered. In particular, it may be possible to require that the EU Ecolabel could only be obtained if portfolios are invested in ‘green bonds’, as defined by the EU GBS. At the same time, the inclusion of bonds as an underlying asset to be verified would need to be done in a way that avoids creating competing frameworks.

In terms of the scope of assets that could be verified within a portfolio, financial derivatives were considered in the PR to this study and by the stakeholders (questionnaire response Q5.5) to be technically complicated to be addressed within the framework of the EU Ecolabel, especially in the context of their verification. This is because their return is based on the value of other assets. So whilst an EU Ecolabelled financial product might necessarily still include derivatives within the portfolio it may not be necessary to verify their greenness. In relation to derivatives, some stakeholders also emphasised that the label should have a long term focus, therefore, securities that only meet short term needs would not be compatible. Existing regional and national labels and schemes either exclude them from their scope or, in the case of the French EETC scheme, they lay down criteria to ensure they are used only for effective management of the investments and that no improper practices take place e.g. short selling.

The review of existing labels and schemes also highlighted that some investment products hold a proportion of the money invested in cash (liquid) form. This cash may be placed in a holding account and/or may also be used on a short term basis to adjust the rate of return provided to investors. Some labels explicitly state that this cash is not subject to any criteria, as in the example of Luxflag. Alternatively specific criteria could apply to the holding account or to the short term use of this cash as, for example, the French EETC scheme does. Given that not all schemes operate criteria on cash and that no clear message emerged from the stakeholder questionnaire, it is not proposed to apply at this stage any specific criterion or requirements.

Determining the portfolio investment threshold and level

National labels and scheme operators consider thresholds for greenness a better instrument than exclusion criteria to channel more investments into activities that are green and environmentally sustainable. A review of existing schemes and labels indicates that such thresholds tend to work at three main levels: (1) portfolio; (2) company; and (3) economic activity.

The stakeholders were asked to react to proposed percentage thresholds for the definition of a green investment portfolio at the different levels at which they could work. The options provided to them included the portfolio level, the asset classes, the company level and activity.

The review of the labels and schemes indicated that some set thresholds at the portfolio level (e.g. the LuxFlag specifies 75% at the portfolio level) in order to assure that investments have a considerable input to sustainability, and also provide fund managers with the possibility to diversify. Moreover for green bonds, a 75% threshold is quite easily attainable as each individual bond is designed to be 100% green. According to experts, a lower threshold (i.e. 50%) might provide more flexibility on creating the investment fund strategy and a diversified portfolio and minimise risks. However, it would not guarantee that investments are strongly contribute to sustainability.

²² EU Green Bond Standard Subgroup. 6 March 2019. Interim Report of the Technical Expert Group (TEG) subgroup on Green Bond Standard - Proposal for an EU Green Bond Standard. Available from: https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190306-sustainable-finance-teg-interim-report-green-bond-standard_en_0.pdf

The majority of respondents to the questionnaire survey on this aspect were of the opinion that it is important for the EU Ecolabel to be able to work to a very great extent to verify the greenness of financial products at the portfolio level. This opinion was shared by more than half of the experts consulted during bilateral interviews.

As a threshold is required at the portfolio level, the responses to the question on what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel were analysed. A slim majority (31%) considered at least 50% of the portfolio should be invested in green activities for the product to qualify for the EU Ecolabel. 30% suggested that at least 70% should be minimal portfolio threshold.

Based on the stakeholders' responses as well as analysis of existing labels and schemes and the information obtained during the first bilateral interviews with experts, the criterion is proposed to work at two levels:

- considering the need to assure that a sufficient number of products can comply with the threshold at the portfolio level, it is proposed that a minimum of 70% of the portfolio should be required to be invested in green activities.
- at the company in relation to equity shares (50% turnover or revenue in green activities)

Relying on a single portfolio level threshold would create a risk of a certain degree of greenwashing, as it may be not clear to retail customers that a certain part of the portfolio can be invested in companies/assets that do not have to comply with the EU Taxonomy. However, the risk of greenwashing is considered to be limited as the exclusions will cater for economic activities that are considered as unsustainable. The difficulty of this approach would rely on classifying a company according to a single economic activity, because most of them are acting in more than one business area.

Identification of green economic activities or sectors.

The identification of economic activities or sectors that qualify as "green" should be done in a harmonised and consistent manner and therefore the EU Taxonomy proposal should form a component of the Criterion 1. A major way in which financial market actors can contribute to environmental goals is by channelling investments into real activities in the economy that are modified to reduce the emissions coming from the activity itself (e.g. "greening of steel manufacturing" deals with minimising the emissions from the manufacturing of steel) and investing in economic activities that contributes to environmental impact reductions in other sectors of the economy (e.g. "greening by ICT" activities include those services provided by ICT companies that e.g. reduce energy consumption in buildings or reduce travel demand).

The EU Taxonomy is a classification system that aims to create a common language for defining environmentally sustainable activities. It 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. Based on the Commission's proposal, financial market actors involved in the manufacture and distribution of green (packaged) investment products will have to disclose to what extent their products have used the EU taxonomy. In addition, the EU taxonomy will have to be used by EU Member States (MS) for setting out national rules on labelling investment products.

A comprehensive background to the EU Taxonomy has been provided in Sections 1.2.1 and 1.2.3. These sections provide the background based on technical analysis for the need for an EU Taxonomy that will facilitate the comparability of investments, address the complications created by "greenwashing" and confusing fragmentation within the financial sector and restore investors' confidence.

Under the Commission's proposal for an EU Taxonomy, 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 objectives²³ defined in the Taxonomy proposal by complying with technical screening criteria (where defined)
- not significantly harm any of the other environmental objectives
- comply with minimum social safeguards; and

As the EU Taxonomy will only contain activities that contribute substantially to one or more environmental objectives, some other activities may be left out. The activities that are not included are not necessarily considered “brown” or having a significant negative impact on the environment. They are simply not categorized. The EU Taxonomy will also include activities that have an impact on the environment, but only those companies that manage reduce their impact substantially will be classified as green. This will enable polluting sectors to transition and move onto greener pathways.

At the time of this report the development of the EU Taxonomy focusses on climate change mitigation and climate change adaptation activities. The Technical Expert Group (TEG) on Sustainable Finance is currently tasked with advising technical screening criteria for determining when an activity makes a substantial contribution to climate change mitigation and adaptation and when there could be significant harm to the other four environmental objectives. The sectors selected for screening include agriculture, buildings, energy generation, forestry, information and communication technologies, manufacturing, transport and water and waste management. In the future, the EU Taxonomy will be gradually expanded to cover the other four environmental objectives

The TEG on Sustainable Finance is also at the same time developing recommendations for a draft EU GBS to ensure consistency in the assessment and verification of bonds to be used for green projects. For the verification of the greenness of economic activities, the envisaged EU GBS will be closely linked to the proposed EU Taxonomy. The current EU GBS proposal as of March 2019 is summarised in the box below.

²³ 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

Table 3. Proposed EU Green Bond Standard requirements for Green Projects**Proposed EU Green Bond Standard requirements for ‘Green Projects’ (as of March 2019)**

Proceeds from EU Green Bonds, or an amount equal to such proceeds, shall be allocated only to finance or refinance Green Projects defined, subject to confirmation by an accredited External Reviewer (see section 4.4 of the TEG interim report of 6 March), as:

(a) contributing substantially at least one of the EU’s Environmental Objectives namely

- (i) climate change mitigation,
- (ii) climate change adaptation,
- (iii) sustainable use and protection of water and marine resources,
- (iv) transition to a circular economy, waste prevention and recycling;
- (v) pollution prevention and control and
- (vi) protection of healthy ecosystems, while

(b) not significantly harming any of the other objectives and

(c) complying with the minimum social safeguards represented by the principles and rights set out in the eight fundamental conventions identified in the International Labour Organisation’s declaration on Fundamental Rights and Principles at Work.

When the EU Taxonomy Framework will be in force and where technical screening criteria have been developed in the Taxonomy for specific environmental objectives and sectors, Green Projects shall align with these criteria allowing however for exceptional cases where these may not be directly applicable as a result among other of the innovative nature, the complexity, and/or the location of the Green Projects.

An accredited External Reviewer shall then either confirm alignment with the technical criteria, or alternatively that the projects nonetheless meet the requirements under the EU Taxonomy framework i.e. that they (a) contribute substantially to at least one of the EU’s Environmental Objectives (b) do not significantly harm any of the other objectives and (c) comply with the minimum social safeguards.

The issuer shall provide a description of such Green Projects in their Green Bond Framework (see section 4.2 of the TEG interim report of 6 March) and in the Green Bond legal documentation. In case that the Green Projects are not identified at the date of issuance, the issuer shall describe the type and sectors and/or environmental objectives of the potential Green Projects.

Green Projects may include:

- 1 eligible green assets (including physical assets and financial assets such as loans), as well as the share of the working capital that can reasonably be attributed to their operation and, for the avoidance of doubt, including potentially both tangible and intangible assets;
- 2 eligible green capital expenditures;
- 3 eligible green operating expenditures related to improving or maintaining the value of eligible assets;
- 4 eligible green expenditures from sovereigns, sub-sovereigns and public agencies.

Eligible green expenditures (items 2,3 and 4) shall qualify for refinancing with a maximum three [3] years look-back period before the issuance year of the bond. Eligible assets shall qualify without a specific look-back period. For the avoidance of doubt, a specific green asset or expenditure can only qualify as a Green Project for direct financing by one or several dedicated green financing instruments (such as bonds or loans) up to the combined equivalent of its full value. It is understood that green financing instruments can be refinanced by other such green financial products.

The EU GBS has the potential for use by the EU Ecolabel for the pre-verification of bonds, being already based on the EU Taxonomy.

Rationale of proposed "Assessment and verification"

An analysis of the regional and national schemes indicates that they assess and verify compliance (both pre-issuance and post-issuance) to their respective criteria requirements through a review of applicable documentation which provides information about the fund, including the Key Investor Information Document (KIID) and investment regulations, marketing materials, reporting and management reports, annual financial statement reports, and portfolio statements itemizing the assets contained (see the PR).

Generally the application fee across the different regional labels and schemes is roughly EUR 3,000 (depending on the label, an annual licence fee which is usually a percentage of the Assets under management (AUM)²⁴ may apply). The applicant may also have to pay an annual usage fee and the costs to involve an external verifier; the respective costs are also subject to local conditions. Additionally, the existing schemes and labels initially award their licenses for a 12 month period during which on-site compliance checks are regularly conducted (every 6 months for some existing schemes or labels). Once a year during the validity of the license, a prolongation²⁵ is possible following demonstration of compliance to the label scheme requirements in an audit. This would allow for changes in a portfolio composition, which are understood to be dynamic.

The link with the EU Taxonomy would be established by taking a “look-through” approach for the operation 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.

An assessment and verification which does not vary significantly from current market practice is proposed. As a result, this is not expected to create operational issues nor result in a significantly higher cost associated with the EU Ecolabel compared to existing schemes.

1st Proposal for Criterion 1: thresholds on green investment portfolio and economic activities

1.1 Investment portfolio greenness thresholds

The investment portfolio of the financial product shall meet the below mentioned threshold for the proportion of total portfolio asset value invested in green activities. This proportion of total portfolio asset value shall be verified based on the company economic activities related to the equities or bonds that are held and the use of proceeds of the bonds that are held.

Portfolio holdings

70% of the total portfolio asset value shall be invested in green economic activities as defined in point 1.2. All portfolio assets must be included in the total.

Assets held by the portfolio

Equities and bonds shall comply with the following thresholds:

- a. Equities: At least 90% of the direct holdings (in terms of number of issuers) of the company have a turnover of at least 50% from green economic activities as defined by point 1.2
- b. Bonds: At least 70% of value of all the bonds held in the portfolio shall be green and those bonds that contribute to greenness thresholds must be fully compliant with the EU GBS

Verification of greenness is not required for any other assets but they must still be included in the total portfolio asset value that must meet the portfolio threshold²⁶.

1.2 Green economic activities

For an economic activity within an investment portfolio to be considered green it shall meet the following requirements:

- (a) It shall contribute substantially to at least one of the EU Taxonomy's Environmental Objectives, for which technical screening criteria are available:
 - (i) climate change mitigation,
 - (ii) climate change adaptation,
 - (iii) sustainable use and protection of water and marine resources,
 - (iv) transition to a circular economy, waste prevention and recycling;

²⁵ Some labels and schemes apply the term 'extension' synonymously

²⁶ Other assets may include as an example, derivatives or money held as cash.

1st Proposal for Criterion 1: thresholds on green investment portfolio and economic activities

- (v) pollution prevention and control and
- (vi) protection of healthy ecosystems,
- (b) while not significantly harming any of the other objectives, and
- (c) it shall comply with the minimum social safeguards represented by the principles and rights set out in the eight fundamental conventions identified in the International Labour Organisation's declaration on Fundamental Rights and Principles at Work ²⁷

Assessment and verification

The applicant shall provide the following documentation showing the minimum percentage to be invested in green activities:

- the green investment policy of the applicant,
- portfolio statement and prospectus including:
 - a) complete listing of the portfolio assets for the financial product, and
 - b) evidence that at least 70% of the listed portfolio assets are invested in green activities,
 - c) an audit report on the latest annual financial statements.

EU GBS certificates shall be accepted as proof of compliance to criterion 1.

Questions to stakeholders

Relating to green economic activities

- 3.1 Is there a way to address economic activities not yet featured in the current version of the EU Taxonomy and its technical criteria?

Relating to green investment portfolio value

- 3.2 How could the revenue for a parent group with number of daughter companies and their share be handled?
- 3.3 How should assets held in other investment funds be treated within this criteria? Do they require any special form of verification?
- 3.4 To what extent should real estate also be considered as a specific asset within the portfolio verification? If so, how could its performance be verified?
- 3.5 Should assets for which verification of greenness is not required be included within the total portfolio asset value?
- 3.6 Should any type of criteria on trading practices and/or use of funds be applied to derivatives and cash?
- 3.7 Does the assessment and verification require any specific parts to be tailored to individual products within the scope?

²⁷ The scope of the social safeguards under the EU Taxonomy may be expanded to include other references such as the OECD Guidelines for Multinational Enterprises and UN Guiding Principles on Business and Human Rights.

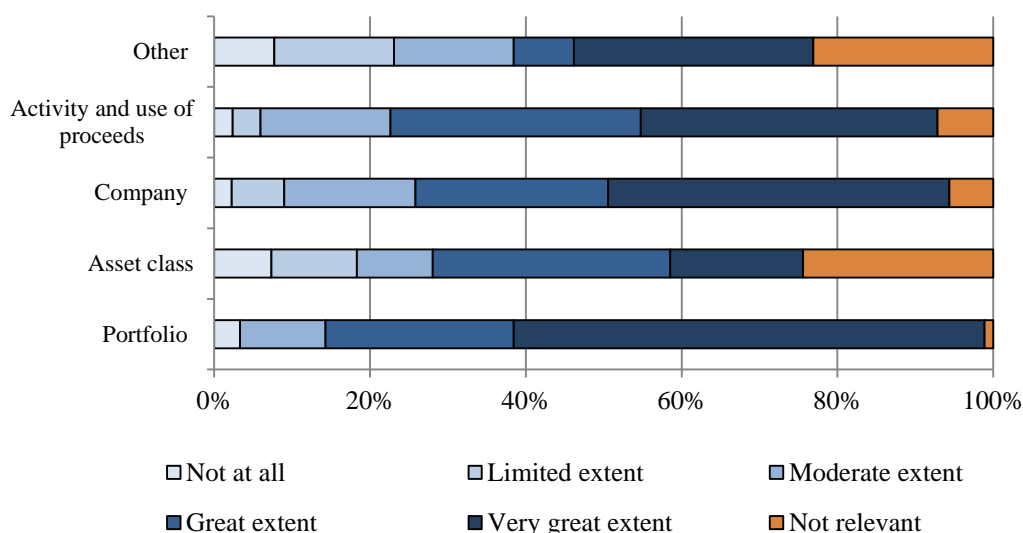
Summary of the results from the 1st stakeholder questionnaire

This section presents results for a small selection of the questions. The complete results for at the portfolio level can be found in Annex 4.2.

Q5.5 At what level do you consider the EU Ecolabel will need to work in order to verify the product's greenness?

60% of the respondents considered it important for the EU Ecolabel to work to a very great extent to assess the greenness of products at the portfolio level. Others (44%) considered the company level as the most appropriate.

Figure 3 – Level of verification of greenness.



It was argued by those proposing the company level that a threshold at the level of the portfolio or asset class would create a risk of a certain degree of greenwashing, as it will be unclear to retail customers that a certain part of the portfolio can be invested in companies/assets that do not have to comply with the Ecolabel criteria.

Q5.6.1 Based on your selection of 'portfolio' in Q5.5, what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel?

In defining investment threshold in green activities for portfolio to qualify for the EU Ecolabel, the responses from the survey was analysed. The results indicated that 31% of the participants, who responded to this survey question favoured criteria which would require that at least 50% of the portfolio should be invested in green activities for the product to qualify for the Ecolabel. 30% took the view that at least 70% should be the minimal portfolio threshold.

Q5.9 Focussing on specific asset classes, please describe technical criteria that could apply to the following:**a). Transferable Securities.****i) Shares**

Similar to Q5.8, a range of responses was obtained. While 3 respondents specifically referred to the use of the EU Taxonomy, another 2 suggested criteria based on the TEEC Label. Another suggested a criterion which combines the EU Taxonomy in combination with thresholds and exclusions but ensure that economic activities and sectors transitioning towards sustainability are not sanctioned. Other notable responses (5) were specific on the need to consider exclusion criteria in combination with selection criteria (best in class) together with minimum ESG ratings.

ii) Bonds

Roughly 50% of the respondents recommended to simply adopt the TEEC thresholds and corresponding to the GBP requires the use of proceeds, process for project evaluation and selection, management of proceeds, reporting and additionally (additionally criteria concerning the emitter). The remaining responses were varied and included the suggestion that the greenness of the issuers should be a selection criterion as it automatically determines the greenness of the bond.

These responses indicate that the EU Ecolabel criteria concerning bonds should consider current practice. However as work is underway on the development of the EU GBS, the criterion therein is put forward in the criterion on climate change mitigation thresholds.

Q5.9 Focussing on specific asset classes, please describe technical criteria that could apply to the following:**b) Financial derivative instruments**

A large majority (44%) of the 25 respondents to the question were unified in their opinion that the use of this instruments should be restricted due to their complexity making their underlying assets difficult to track and the assessment of greenness almost impossible. There was no consensus on the remaining responses. The results of the market analysis and a review of the operation of the national labels and schemes support this recommendation. It is proposed that the EU Ecolabel adopt a similar approach.

c) Money market instruments

It was not possible to gain an understanding of the technical criteria that could be applied to money market instruments no consensus could be found from the divergent responses provided by stakeholders to the questionnaire survey..

d) Real Estate

25 responses were provided of which 10 recommended criteria on energy efficiency and greenhouse gas emissions but with the suggestion to also include social criteria. Another 3 suggested the application GRESB – the ESG Benchmark for Real Estate Assets.

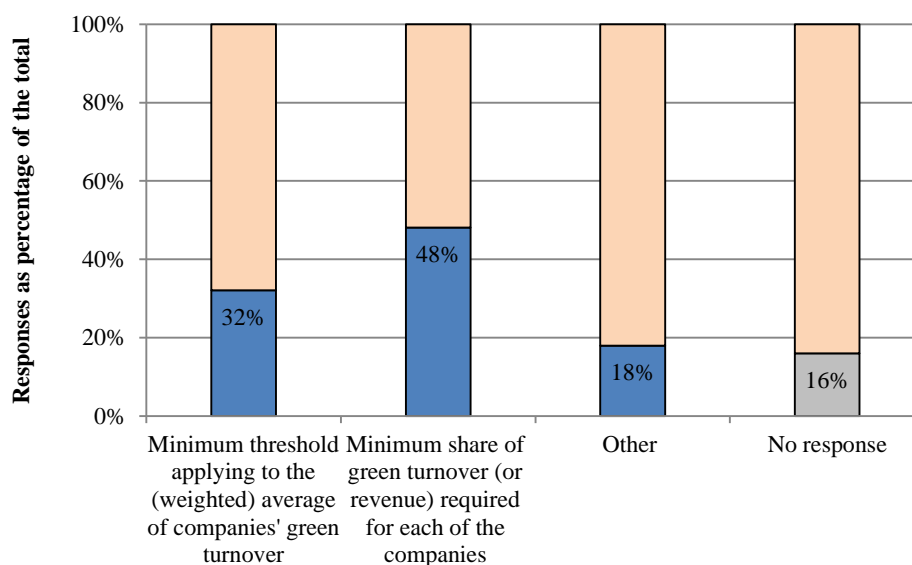
Q5.10 When assessing the greenness of a portfolio, how should the 'greenness' of the various companies be weighted?

Figure 4 – Companies weighting in a portfolio greenness assessment.

48% responded in favour of the minimum share of green turnover (or revenue) required for each of the companies should be considered when weighting the greenness of various companies, 32% supported the minimum threshold applying to the (weighted) average of companies' green turnover.

3.1.2 Criterion 2: Exclusions based on environmental aspects

The existing schemes and labels reviewed to date include exclusions that reflect, amongst other factors, legal requirements on environmental, social and ethical performance. This section discusses the benefits of including an exclusion based criterion in the EU Ecolabel criteria for financial products. Although the criterion presented below focused on exclusions based on environmental aspects, the discussion is carried out broadly and includes examples of exclusions based on social and ethical aspects, that are proposed in criterion 3.

Rationale of the proposed Criterion text

The exclusion criteria considered in this section aim to avoid economic activities with potential environmental harm, while exclusion criteria addressing social and ethical issues such as anti-corruption and transparency are covered in the next section. Exclusions may differ across the schemes mainly due to a different perception, values, policies and the specific scope of the scheme.

Strict exclusion criteria should be applied carefully because they can rapidly reduce the available investment opportunities (i.e. the underlying assets that count as green under the label), at least for equity / general corporate finance (rather than use of proceeds). Indeed, due to the complexity of fund structures, the diversity of activities that a company (or any of its daughter companies) undertake and the highly interconnected nature of global supply chains, it can be difficult to find companies who are completely disconnected from an excluded activity.

In order to make a first proposal for excluded sectoral activities, the sectoral environmental impacts and potential environmental risks have been taken into account. Additionally, the market of existing labels and schemes on fund portfolio composition²⁸, and the stakeholders' opinion as expressed in the survey have also been considered. As regards sovereign bonds, which are addressed further later in this section, the current experience and the opinion of stakeholders have contributed to form the preliminary list of exclusions.

The possible role of partial exclusions

A possible solution to this issue alongside careful definition of the scope of the exclusions is to use partial exclusions. These accommodate or allow for some proportion of excluded activity, the most common threshold is 5% in terms of revenues of any company that is part of the portfolio or in terms of the total amount invested by the fund. According to managers of the existing financial product labels in Europe, this is a realistic threshold based on the potential for excluded activities to be present in any mainstream investment portfolio, and regardless of the efforts made to verify the greenness of the portfolio.

Some differences can be observed in the way that exclusionary thresholds are implemented. For instance, some schemes do not sum up individual thresholds if a fund invests in different sectors falling under partial exclusions while others prefer to set strict exclusions and apply a threshold for portfolio value invested in excluded activities. Some of the national labels suggest that a threshold of more than 5% could affect the credibility of the EU Ecolabel. One label has higher thresholds for certain activities, for example in the fossil fuel sector, because they consider it important to encourage a gradual transition period towards more environmentally sustainable investments.

Analysis and formulation of the exclusions

In order to establish a list of possible exclusions, sectoral environmental issues and activities that are commonly cited by existing labels and schemes as well as some requirements at corporate and state level have been included in Table 4 and Table 5, respectively. The stakeholders' opinion as expressed in a survey has also been taken into account. An overview of

²⁸ Personal communication with national schemes in Europe January 2019

the relevant sources for use in formulating the criterion are portrayed in Figure 5.

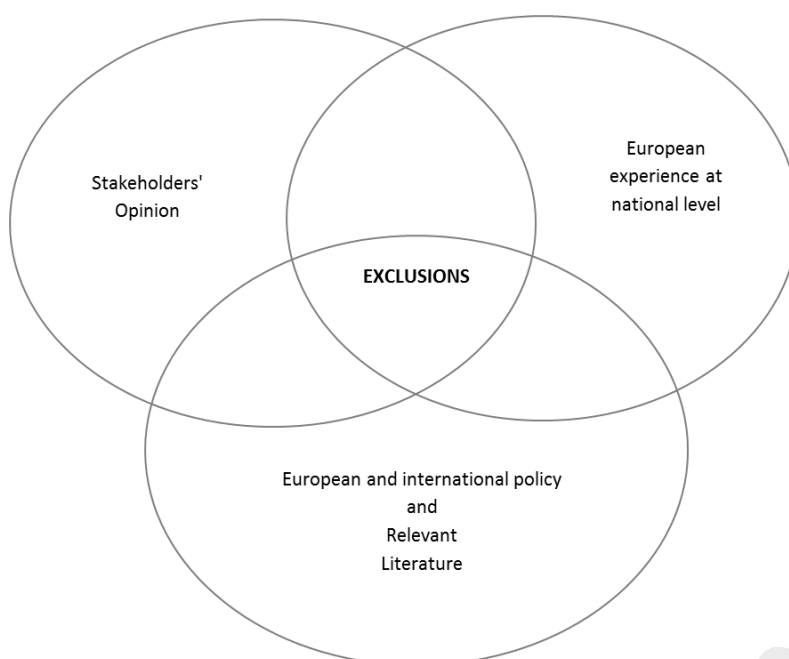


Figure 5 – *Relevant sources for formulating exclusions.*

A proposal has then been formulated by screening these two lists against current EU environmental policies and the EU Taxonomy proposal. This suggests that some of the listed activities will have technical screening criteria for green-ness within the EU Taxonomy and therefore may not fit within an exclusionary approach. For example, 9.4 existing forest management could be understood to require the protection of existing carbon sinks. The sector ‘Electricity, gas, steam and air conditioning supply’ may include technical screening criteria for Combined Heat and Power (CHP) as a low carbon transition technology that could use fossil fuels such as natural gas.

The stakeholders' responses did not provide a clear picture about which activities or economic sectors could be potentially partially excluded. Nonetheless, stakeholders strongly suggest a threshold limit at 5% for all exclusions. This reflects the partial exclusion thresholds of existing national labels and schemes. The only difference is that some only apply the threshold to certain sectors that have exclusions. Consequently, the first criteria proposal is to adopt this limit for investments in excluded sectors, thereby reflecting the current market practice to allow for some exclusionary activity without compromising the shift to more sustainable investments.

Table 4 – *Environmental-related exclusions at sectoral level in existing labels.*

Environmental- related exclusions at sectoral level

- Coal mining
- Fossil fuel energy generation
- Natural gas extraction
- Oil extraction
- Deforestation
- Pesticide production
- Unsustainable vegetable oil production
- Industrial gas production
- Waste management facilities without materials or energy recovery
- Fracking
- Oil sand exploitation
- Nuclear exploitation and energy generation
- GMO crops

Fossil fuel extraction and refining as well as subsequent fossil fuel energy generation are proposed to be excluded on the basis of the efforts to decarbonise the European economy²⁹. This could encompass newer sources of fossil fuel extraction such as fracking or oil sands. Member states are developing their own policies and permitting requirements for these newer fossil fuel resources. Because of concerns about the environmental impacts associated with these new sources permitting requirements are a focus of discussions at EU level within the frame of the emissions limits and best practices required under the Industrial Emissions Directive.

With regards to fossil fuel energy generation, the current proposal for the EU Taxonomy includes for some fossil fuel energy generation activities that are considered as transitional low carbon technologies, such as Combined Heat and Power (CHP). It is proposed therefore that exclusions for fossil fuel power generation do not include these activities.

For the nuclear fuel cycle and nuclear power generation decisions related to the energy mix are left to Member States. Some Member States are still developing new capacity as a low carbon element of their electricity generating mix – including the UK, Finland, France and Slovakia - but in general the role of nuclear power has been called into further question following the Fukushima disaster. There are currently divergent views amongst Member States on this technology. Amongst the existing labels, the French TEEC has an exclusion criterion which covers nuclear power. Nuclear power is not at the moment proposed in the list of excluded activities, but a final view on whether to exclude it or not will be taken following further dialogue with stakeholders.

Deforestation (often driven by land use change³⁰) can significantly contribute to climate change and also have a negative impact on biodiversity. Existing forestry management is currently proposed to be addressed by the EU Taxonomy, with a focus on criteria addressing maintenance of the carbon stock, including the protection of old growth forests, and legal harvesting. It is therefore considered that sustainable forestry management is already defined as a green economic activity. Related to this illegal logging is a very specific issue that may be linked to the deforestation of old growth forests and is the subject of the EU Timber Regulation legislation^{31 32}. An exclusion could therefore be proposed to as a means of protecting carbon stocks, thereby complementing the EU Taxonomy focus on existing forestry management, and with the potential for verification to be provided by the FLEGT licensing arrangements.

Industrial gases can also affect the environmental, mainly due to the high relative contribution of some gases towards the ozone depletion potential and global warming. The exclusion criterion of one major label reviewed focuses on the production of hydrofluorocarbons (HFCs),

²⁹ European Commission, “Action Plan: Financing Sustainable Growth,” 8 March 2018 available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0097&from=EN>. and the EU Long Term Strategy for reducing GHG emissions (2050 Strategy)

³⁰ BSI 2011: PAS 2050- Specifications for the assessment of the life cycle greenhouse gas emissions for goods and services.

³¹ Regulation (EU) No 995/2010 of the European Parliament and of the Council of 20 October 2010 laying down the obligations of operators who place timber and timber products on the market

³² A Commission Action Plan on combatting deforestation is upcoming and may have implications for the EU Ecolabel proposals

nitrous oxide (N₂O), perfluorocarbons (PFCs) and sulphur hexafluoride (SF₆). Fluorinated gases are controlled by Regulation (EU) No 517/2014 (the F-Gas Regulation)³³ which specifies requirements to prevent leakages and to phase down the use of F-Gases. It requires the phase down of HFCs with the highest Global Warming Potential. N₂O is included within the European Emissions Trading System (EU ETS) in relation to emissions from the production of nitric, adipic and glyoxylic acids and glyoxal. Additional impacts of fluorinated as well as other halogenated gases addressed by the Montreal Protocol³⁴ are their contribution to depletion of the ozone layer³⁵ while often also having high global warming potential. An exclusion could therefore seek to avoid investment internationally in the production of gases with a high GWP and ODP.

Pesticides use can impose a range of adverse effects on human health and increase environmental eco-toxicity. The type and extent of these effects vary according to the pesticide used. EU policy promotes the use of Integrated Pest Management and organic agriculture as means to reduce harmful pesticide use. The most harmful pesticides are identified on the Rotterdam Conventions Prior Informed Consent (PIC) list, which seeks to restrict the import of specific hazardous pesticides that are banned or subject to severe restriction at an international level, as well as with reference to EU authorisations and the WHO classification system. At this stage, the EU Taxonomy does not specifically address agricultural production systems or the manufacturing of harmful products. However, since this is still considered by stakeholders as an issue which requires attention internationally it could be possible to develop a specific exclusion for harmful pesticide production.

The use of genetically modified (GMO) crops is licensed at EU level, so it is not explicitly prohibited, but the decision to authorise their use is left to each member state. This is a difficult exclusion to apply because there are conflicting views across member states and a limited outlook on any potential detrimental environmental impacts now and into the future. Their use internationally is also linked to social and ethical issues, for example the dependency of farmers on a limited number of seed varieties and their suppliers. Because of the divergent views of Member States on this topic and the lack of a clear scientific consensus it has been decided at the moment not to propose the use of GMOs in the list of excluded activities.. A final view on whether to exclude them or not will be taken following further dialogue with stakeholders.

Screening criteria for waste facilities or resource recovery operations are currently being investigated under the EU Taxonomy, but they are not yet established. However, pending these criteria the EU Waste Framework Directive and the Action Plan for circular economy³⁶ supports a shift towards resource and energy efficiency while reducing environmental impacts by promoting environmental friendlier products, services and technologies. Therefore, it could be considered that investment in conventional waste management facilities that do not promote materials and/or energy recovery according to the waste hierarchy (e.g. landfilling, incineration without energy recovery) could be proposed for exclusion.

Unsustainable vegetable oil production has been reported as contributing to a range of environmental issues, including impacts arising from land use change and related deforestation, and has already been addressed by the criteria of some EU Ecolabel product groups. However, the subject of verification is complex and may not be possible to apply consistently across different vegetable oil products. It is therefore difficult to propose a single meaningful exclusion for this type of raw material.

How to treat sovereign bonds

³³ European Commission, "Regulation No 517/2014 on fluorinated greenhouse gases", available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.150.01.0195.01.ENG

³⁴ United Nations, "The Montreal Protocol", available at <https://www.undp.org/content/undp/en/home/sustainable-development/environment-and-natural-capital/montreal-protocol.html>

³⁵ United Nations, "The Montreal Protocol", available at <https://www.undp.org/content/undp/en/home/sustainable-development/environment-and-natural-capital/montreal-protocol.html>

³⁶ European Commission, "Closing the loop – An EU action plan for the circular economy". 2 December 2015 available at <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52015DC0614>

At a national level, existing schemes also apply requirements to sovereign bonds for awarding the label. The requirements mainly refer to acceptance of international treaties by the country issuing the bonds. Some of the labels require ratification of internationally recognised conventions, such as the Paris Agreement and the UN Convention for Biological Diversity. Social and financial constraints can also exclude a country's sovereign bonds. The latter may require the state not to be subject of EU or UN financial sanctions, and to have signed international conventions, such as the ILO convention, protect human rights, and support anti-corruption and bribery.

In addition to the stakeholders' proposals and based on the experience of national schemes, European policy frameworks were also taken into account when analysing the possible exclusions. For example, the Paris agreement³⁷ on climate change is endorsed by the European Commission and included in its action plan for sustainable growth³⁸. Therefore, its ratification is proposed as mandatory requirement for sovereign bonds. The UN Convention for Biological Diversity should also be ratified as should international conventions on environmental protection. Projects that could damage valuable or protected areas are also excluded in some schemes. This could be understood to relate to internationally funded development projects such as hydroelectric dams. Verification could be possible based on Environmental Impact Assessments (EIAs) carried out for planning and due diligence purposes.

Finally, it is recommended that investments flowing into countries which are not in compliance with the international laws or conventions listed in Table 5., be excluded.

Table 5 – *Exclusion criteria at national level.*

International environmental commitments
<ul style="list-style-type: none"> – Non ratification of the Paris Agreement – Non ratification of the UN Convention for Biological Diversity – Non ratification of international conventions on environmental protection – Projects that damage valuable and /or protected areas

Rationale of proposed "Assessment and verification"

The below workflow is proposed for checking compliance with both the environmental and the social and ethical exclusions criteria. Post-verification requirements are also outlined in Figure 6 and explained in the sections describing the verification procedures for exclusions.

³⁷ See conclusions agreed in December 2015 at http://unfccc.int/paris_agreement/items/9485.php

³⁸ European Commission, "Action Plan: Financing Sustainable Growth," 8 March 2018 available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0097&from=EN>.

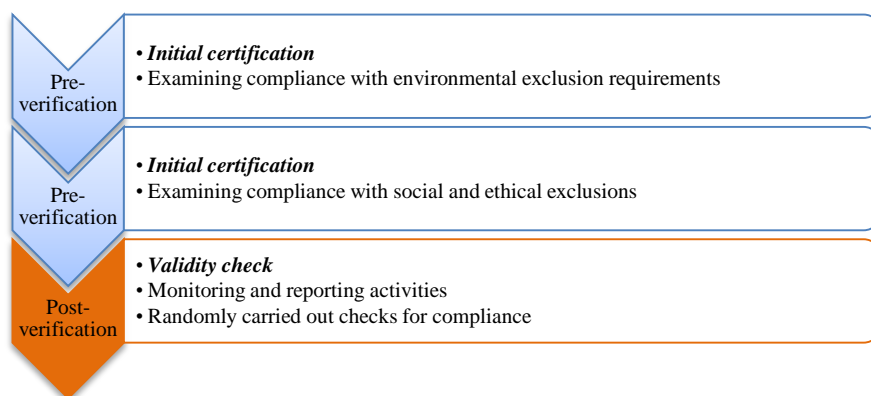


Figure 6 – Pre- and post-verification steps for examining compliance with exclusions.

In terms of the current practices of the existing labels and schemes, assessment and verification procedures consider exclusion lists when checking investment compliance. An initial assessment takes place which can be carried out by external auditors and afterwards there is verification by the respective Competent Body. Additionally, annual reports and random compliance checks can be performed to examine continuous conformity.

Apart from the initial assessment and verification, monitoring and reporting activities should be conducted internally so that any change or deviation can be reported to Competent Bodies.

The cost of assessing compliance with the exclusion criteria is difficult to estimate since it can be subject to the overall complexity of verifying the financial product.

1st Proposal for Criterion 3: Excluded activities – Environmental aspects

Companies that derive their revenue from the following activities shall be excluded from investment portfolios of the financial product:

- Coal, natural gas and crude oil exploration and extraction
- Coal, natural gas and crude oil refining for fuel
- Forms of energy generation from fossil fuels that are excluded from the EU Taxonomy
- Waste management facilities without materials or energy recovery
- Production of pesticides that are not authorised for use or import to the EU
- Production of industrial gases with a high Global Warming Potential and/or Ozone Depletion Potential
- Illegal deforestation

These exclusions shall apply to all activities within an investment portfolio. A cut off threshold 5% of the total revenue derived from each company may be associated with these excluded activities.

In the case of sovereign bonds or bonds issued by international organisations the following exclusions shall apply either to the issuing country or the economic activity:

- Non ratification of the Paris Agreement
- Non ratification of the UN Convention for Biological Diversity
- Non ratification of international conventions on environmental protection
- Internationally funded projects that could damage valuable and /or protected natural areas

Please note: The environmental exclusions included within this proposal are solely for the purpose of discussion with stakeholders and are to be further checked for their applicability and consistency.

Moreover, the exclusions will need to be further checked against the EU taxonomy to ensure there are no contradictions with the logic of how it is designed.

Assessment and verification

The applicant shall provide the investment policy, investment portfolio and the allocation of proceeds to the Competent Body. Further to the initial verification, internal checks shall be performed at least once per year and any changes communicated to the Competent Body who also retains the right to make random checks on compliance.

Question to Stakeholders

3.8 Do you think the proposed environmental exclusions should be expanded to include more economic activities?

3.9 Do you think the partial exclusions threshold should apply to each company's activities or to the portfolio as a whole? *If it should apply at portfolio level, should it be set differently for specific sectors?*

Summary of the results from the 1st stakeholder questionnaire

Here the responses to questions of relevance to environmental exclusions are briefly summarised in order to identify the main findings.

Q5.1 Should the EU Ecolabel have exclusions for specific activities on the basis of their environmental impact.

As regards the question Q5.1, the vast majority of stakeholder (87%) support the hypothesis, 9% are against it while a small percentage (4%) gave no response.

Related to the above-mentioned question, the survey provided with economic activities that could possibly be entailed in a preliminary exclusions list by stakeholders' opinions. The replies of the stakeholders are depicted in Figure 7

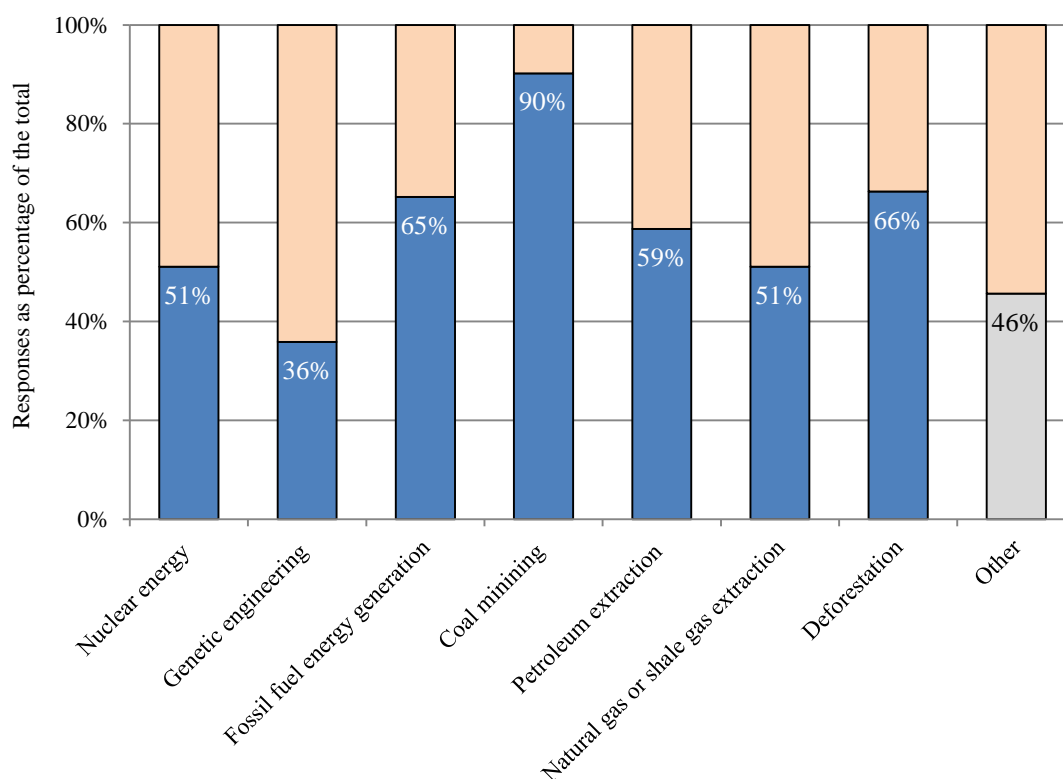


Figure 7 – Exclusion-relevant activities.

According to the results, as shown in **Figure 7**, the vast majority of the stakeholders (90%) endorse coal mining to be excluded from the scope of the EU Ecolabel for financial services. More than 60% advocate for deforestation and fossil fuel generation related investments to be disqualified. Within the range 50% to 60% are falling the sectors nuclear energy, petroleum extraction, and natural and shale gas extraction. A possible exclusion of genetic engineering is supported by 36% of the stakeholders. Additionally, they have delivered answers (46%) about other sectors that should be assessed for potentially being excluded. Between others, oil sand exploitation, pesticides production, mining, and unsustainable palm oil production were suggested.

Q5.3 If exclusions are included in the EU Ecolabel, should they be total or partial?

Stakeholders are also consulted on including partial or total exclusions (Q5.3). According to their responses, more than half support partial exclusions while more than one-third advocate for total exclusions. A small number of stakeholders (8%) did not express an opinion in that particular question. The exact percentages can be read in Figure 8

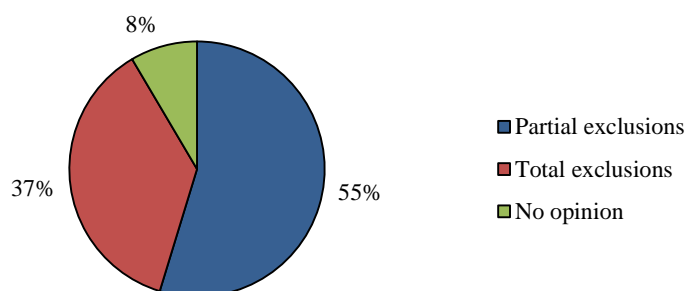


Figure 8 – Stakeholders' opinion about including partial or total exclusions

Stakeholders suggest (25%) setting up a limit of 5% as partial exclusions criterion at company level.. To a lesser percentage (12%) the responses support a threshold at 10% again in relation to particular sectors, such as electricity generation from coal, retail of alcohol and tobacco, and energy generation from fossils other than gas. If the latter is the case, the replies suggest increasing the threshold by more than 30%.

Partial exclusions refer to environmental, social and ethical issues. As mentioned above investments in fossil fuels, especially coal, and nuclear power are among the most frequently mentioned sectors on the basis of environmental aspects. On the other side, tobacco and alcohol trade belong to the social ones.

3.2 Criteria area: Social and ethic aspects

3.2.1 Criterion 3: Exclusions based on social & ethical aspects

Social and ethical criteria in existing schemes and labels respond to a number of societal concerns. The proposed strategy for the EU Ecolabel is based on exclusions for several social and ethical aspects. The benefits of this strategy are discussed in section 3.1.3.

The exclusions can be defined at sectoral and country level in the same way as for the environmental exclusions. At the national level the exclusions refer to sovereign bonds while at the sectoral level the investment portfolio may contain diverse assets as defined in the scope of this study. Some of the national schemes operating in Europe apply social exclusions while others restrict the exclusionary criteria to environmental issues and adopt social criteria as part of their inclusionary criteria³⁹.

Rationale of the proposed Criterion text

To define the framework and the lists of excluded activities at sectoral and national level, social and ethical requirements have been taken into account. The survey responses to question Q5.2 were used as a source of information along with the existing labels and schemes. European policies on social and ethical issues have also been considered in formulating this preliminary social & ethical exclusions list presented in Table 6.

Supplementary to the exclusions on sectoral level those at national level are also described in the next Table 6. These represent possible exclusions that could be applied to issuers of sovereign bonds. Additionally, this list of possible exclusions deems the economic condition of the country as a crucial element. Thus, if the country is subject to UN or EU financial sanctions for specific rights violations or activities of concern, its bonds cannot not be qualified. One should bear in mind that all requirements could be considered to be of equal importance.

Table 6 – Exclusions at corporate and national level.

Social & Ethical related exclusions at corporate and national level	
<i>Corporate level</i>	
-	Human rights violation
-	Labour rights violation
-	Corruption & Bribery
-	Tobacco
-	Conventional weapons
-	Controversial weapons
-	Poor corporate management ⁴⁰
-	Poor human capital development ⁴¹
-	Pornography

³⁹ Energy and Ecological Transition for the Climate. Available at:

https://www.novethic.com/fileadmin/user_upload/divers/labels/1605-LabelTEEC_Referentiel-ENG.pdf

⁴⁰ A poor leading, administrating and directing of a company may lead to a poor management of the resources, a lack of achievement of the company's objectives and negative effects on the human resources.

⁴¹ Corporate activities that can be considered to degrade the human capital in regards to the their workforce and/or the local context in which they operate

National level

- Human rights violation
- Working conditions violation
- Corruption & bribery
- Use of controversial weapons
- Non ratification of international conventions on social and ethical matters e.g. ILO conventions
- Country is subject to EU or UN financial sanctions for special social or ethical violations

In the survey Q5.2 human rights (90%) and labour rights (85%) were selected as the most relevant exclusions. From a social and ethical point of view, companies are proposed to be excluded if their activities violate the European convention⁴² on human rights. In relation to company activities the OECD Guidelines for Multi-National Enterprises 'Recommendations on human rights and on employment and industrial relations' and the United Nations Global Compact: 'Principles on Human rights and Labour' are also potentially relevant.

European Directives addressing working conditions and labour rights as expressed by the International Labour Organisation (ILO) also contribute to developing the framework with several exclusions⁴³. In a number of existing EU Ecolabel product groups, social criteria have been introduced that are based on compliance with the eight ILO Fundamental Conventions. These could therefore form a specific basis for verification.

Corruption was the third selection made by stakeholders in Q5.2 of the survey (81%). There exists a corruption index for countries⁴⁴. This could potentially be used to exclude sovereign bond issuers. In terms of company corruption there does not appear to be a basis for verification of an exclusion.

Tobacco was identified by more than 63% of respondents. Such an exclusion could apply to both the production of raw materials and final products.

The production of weaponry is excluded by the German, Austrian and Nordic labels. These exclusions refer to both conventional and controversial weapons such as mines. On the basis that it should be possible to identify specific divisions of companies focussed on military technology, it is proposed to be included as a specific exclusion. The identification of specific controversial weapons is to be developed further with stakeholder input.

Pornography was selected by 45% of stakeholders. This type of exclusion could be related to companies operating in the media or multimedia sectors and across a range of possible formats. Activities could also be linked to coercion, prostitution and human trafficking. This topic would appear to fit as a possible exclusion but the potential to verify it is unclear at this stage.

The topics of poor corporate management and poor human capital development were selected by few stakeholders (33% and 20% respectively). Existing labels and schemes tend to focus on positive engagement instead, for example active ownership, as opposed to exclusions.

Rationale of the proposed "Assessment and verification"

Regarding the monitoring of compliance, and in line with current practices, the applicant fund shall declare and demonstrate that the services are compliant with those requirements by using independent verification or documentary evidence that is without prejudice to the national law

⁴² European Convention on Human Rights. Available at <https://www.echr.coe.int/Pages/home.aspx?p=basictexts&c>

⁴³ International Labour Organisation (ILO). Available at https://www.ilo.org/moscow/areas-of-work/gender-equality/WCMS_249143/lang--en/index.htm

⁴⁴ Transparency International. Corruption Perception Index 2016. Available at https://www.transparency.org/news/feature/corruption_perceptions_index_2016?gclid=EAlaIqObChMI0qOikr_84AIVowrTCh2vNwajEAAYASABEgLhm_D_BwE

on data protection (e.g. copy of a written social policy, copies of contracts, statements of employee's registration in the national insurance system, official documentation/register recording the names and number of employees by the local government's employment inspectorate or agent).

1st Proposal for Criterion 3: Social and Ethical related exclusions

Companies that derive their revenue from activities that contravene the ILO's eight fundamental labour conventions and the United Nations Global Compact's 'Principles on Human rights and Labour' shall be excluded from the investment portfolio of the financial product. The following specific activities shall also be excluded:

- Tobacco production at any stage from raw material to final products for consumers
- The production of weapons

These exclusions shall apply to all activities within an investment portfolio.

In the case of sovereign bonds or bonds issued by international organisations the following exclusions shall apply either to the issuing country or the economic activity:

- The use of controversial weapons
- A corruption index reported to be less than 50
- Non ratification of international conventions on social and ethical matters e.g. ILO conventions
- Country is subject to EU or UN financial sanctions for special social or ethical violations

Assessment and verification

The applicant shall provide the investment policy, investment portfolio and the allocation of proceeds to the Competent Body. Further to the initial verification, internal checks shall be performed at least once per year and any changes communicated to the Competent Body who also retains the right to make random checks on compliance.

Question to Stakeholders

- 3.10 Do you think the proposed exclusions list on the basis of social & ethical aspects should be enriched with more activities?
- 3.11 Do you think it may be appropriate to also exclude poor corporate management practices and/or poor human capital development? If yes, how it will be possible to verify such exclusions?

Summary of the results from the 1st stakeholder questionnaire

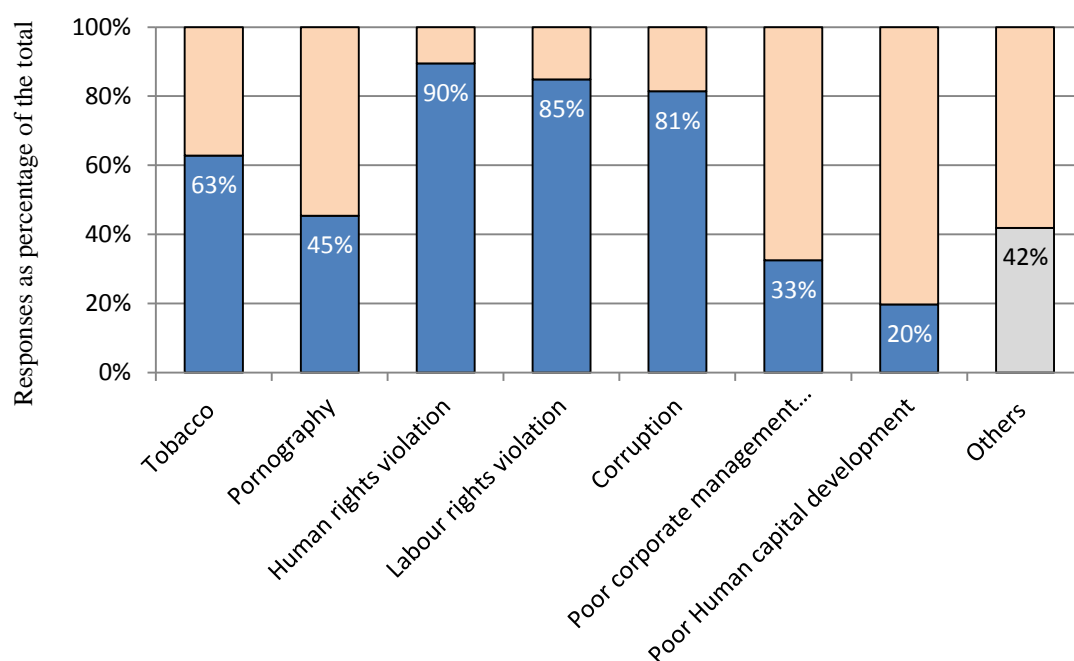
Here the responses to questions of relevance to social and ethical exclusions are briefly summarised in order to identify the main findings.

Q5.2 Should the EU Ecolabel have exclusions for specific activities on the basis of their social and ethical impact?

Questions 5.2 explored links between social and ethical impacts with exclusions. The majority of the stakeholders (>80%) agree to relate exclusions to social and ethical issues. More than 10% responded that they see no relation while less than 10% expressed no opinion. The high percentage of agreement with the social & ethical parameters signified the importance of this dimension for setting exclusion criteria.

Next Figure 9 shows specific activities that could be considered as exclusions-relevant, in line with question 5.2 of the survey.

Figure 9 – Exclusions-relevant sectors according to social and ethical performance



According to the stakeholders, human and labour rights violation and corruption (>80%) constitute significant issues for an economic sector to be excluded. Tobacco-related investment may also not qualify for an EU Ecolabel according to the responses (63%). Less than 50% of the stakeholders support pornography, poor corporate management and poor human capital development as reasons for exclusion while 42% of the respondents suggested other sectors to be considered. Investments on weapons should be considered (25%) while other sectors mentioned are alcohol, and gambling, yet the respective percentages are below 10%.

3.3 Criteria area: Information

This section proposes minimum reporting requirements that will provide retail investors with knowledge and transparency on the environmental, social and ethical performance of the financial products they are obtaining.

Additionally, a further standard criterion on information appearing on the EU Ecolabel (e.g. in the brochure or documentation of the financial product) is also included in this section. The aim of this criterion is to provide the information that should or could appear close to the EU Ecolabel logo and that informs retail investors about the outstanding environmental performance of the product.

3.3.1 Criterion 4: Retail investor information

Rationale of the proposed criterion text

The rationale is based on the need to provide consumers with clear information on the environmental and social performance of the financial product. These requirements will allow consumers to take a well-informed decision and also enhance transparency.

The consumer information requirements could somehow overlap with the information and reporting requirements required by some existing schemes and labels on aspects such as engagement and governance issues. These are complemented with responses of stakeholders to the survey which indicated that the inclusion of criteria related to corporate activities and governance structures are relevant as these would ensure that governance objectives are not jeopardised while the focus should be on environmental issues (Q4.4). Transparency and anti-corruption were also flagged as major issues to be addressed by the EU Ecolabel criteria (Q4.5) when considering governance aspects. Other factors elicited from the survey included ESG theme, demonstration of environmental benefits, demonstrated social benefits, scope based on feasibility of verification, traceability and transparency of investments, sustainable asset allocation.

Existing regional and national labels and schemes include information for the consumers and reporting requirements which can be applicable for assessment and verification at either the pre-issuance or post-issuance level. They also serve to inform the consumers about the characteristics of the financial products they are purchasing. These ensure that the market participants are provided with the right information and that the financial product remains compliant with the requirements of the respective labels. Consumer information and reporting requirements cover the climate related objectives of the applicant financial product, transparency, ownership, quality and regulatory requirements (e.g. accounting for compliance with the location or geographic specific laws and regulations). Some additionally, as in the case of bonds, require reporting project impacts.

This consumer information should be updated regularly and therefore be based on a regular monitoring of the portfolio. Such actions will enhance the credibility of the EU Ecolabel, and therefore a proposal on consumer information requirements is proposed below.

Rationale of proposed "Assessment and verification"

The assessment and verification of this criterion is proposed by providing the following documents or annual reports that contain:

- the green investment policy: the green investment policy is designed to ensure that the activities and management of the financial product are in line with green investment principles. The operation and implementation of this policy, supported by the EU Ecolabel criteria, describe in more detail the methodology and approach taken to quantifying various dimensions of the green impacts of the investments.
- portfolio statement or prospectus including a list of the portfolio assets: transparency on the allocation of the assets will enhance the credibility of the EU Ecolabel and allow

consumers to have an in-depth knowledge of the green impacts achieved by the financial product.

- management and internal control procedures to ensure the non-financial performance indicators: proper management and internal control help fund managers understand the risks the funds are exposed to, put controls in place to counter threats, and effectively pursue the objectives included in the green investment policy. They are therefore an important aspect of financial products.

1st Proposal for Criterion 4: Consumer information

The following information shall be provided by the applicant to the consumers on an annual basis:

1. Investor information and investment policy which shall detail the following:
 - the methodology for computing the portion of turnover in accordance with Criterion 2.
 - the environmental objectives of the portfolio
 - the financial objectives⁴⁵
2. Information on corporate activities and governance structures of the company managing the portfolio detailing how social and ethical issues are managed
3. Information on management and internal control procedures which detail a monitoring mechanism for reducing the potential risks of including in the investment portfolio activities included in the exclusion lists of criteria 2 and 3.

Assessment and verification

The applicant fund shall provide the latest annual reports and or documentation to the Competent Body: the green investment policy of the applicant, portfolio statement and prospectus including complete listing of the portfolio assets for the financial product and management and internal control procedures for ensuring compliance to environmental and social performance aspects.

Question to Stakeholders

- 3.12 What will be a reasonable interval for monitoring and reporting information to the consumers?

⁴⁵ The financial objectives could be indicated in the form of e.g. risk reduction policies, etc

3.3.2 Criterion 5: Information appearing on the EU Ecolabel

Rationale of Proposed Criterion text

Information on the label is useful for reinforcing messages that endorse the consumer's choice of an EU Ecolabelled product over alternatives that are not labelled. According to article 8 (3b) of the Regulation 66/2010, for each product group, three key environmental characteristics of the EU Ecolabel product may be displayed in the optional label text box. The guidelines for the use of the optional label with text box can be found in the "*guidelines for the use of the EU Ecolabel logo*" available on the EU Ecolabel website.

The first part refers to the use of the logo and the license number and the second one to the information to be provided. The sentences proposed for financial products include a reference to the reduced impact on climate change.

Rationale of proposed "Assessment and verification"

The assessment and verification of this criterion is proposed throughout a signed declaration of compliance and the provision of a sample of the product documentation where the EU Ecolabel is placed.

1st Proposal for Criterion 5: information appearing on the EU Ecolabel

The applicant shall follow the instructions on how to properly use the EU Ecolabel logo provided in the EU Ecolabel Logo Guidelines:

http://ec.europa.eu/environment/ecolabel/documents/logo_guidelines.pdf

If the optional label with text box is used, it shall contain one of the following statements:

- The chosen environmental objective for the greenness of the product selected from the following:
 - reduced impact on climate change
 - enhanced climate change adaptation
 - enhanced sustainable use and protection of water and marine resources
 - enhanced transition to circular economy, waste prevention and recycling
 - enhanced pollution prevention and control
 - enhanced protection of healthy ecosystems.

And the following statements:

- Social and ethical principles respected
- Transparent reporting on environmental performance

Assessment and verification

The applicant shall provide a signed declaration of compliance along with a sample of the product label or product documentation where the EU Ecolabel is placed that clearly shows the label, the registration/licence number and, where relevant, the statements that can be displayed together with the label.

Summary of the results from the 1st stakeholder questionnaire

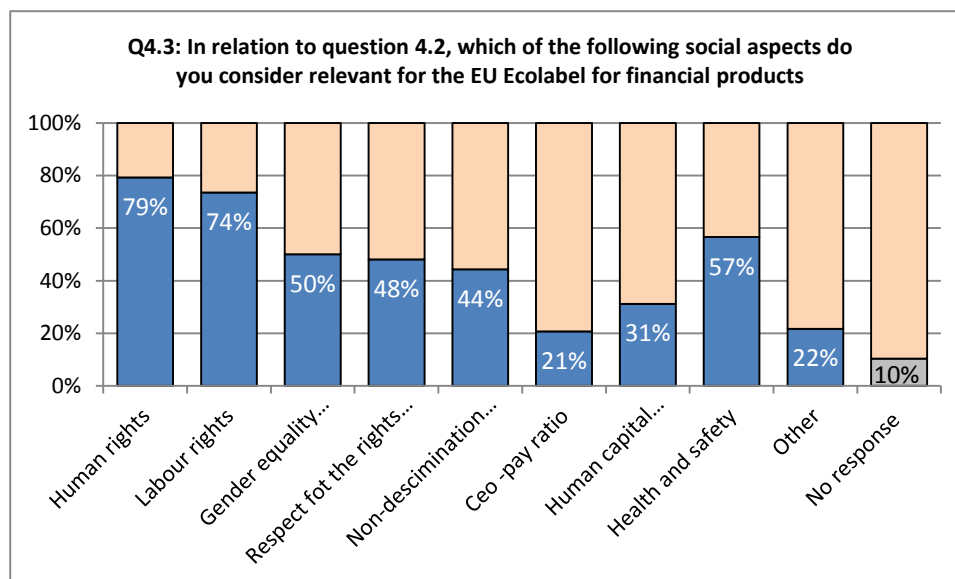
The questionnaire addresses questions related to reporting requirements which cover overlapping responses to the questions featured below.

Q4.1 What type(s) of strategies should be reflected in the EU Ecolabel criteria?

See section 3.1.

Q4.2 To what extent do you consider that the EU Ecolabel should have criteria that address social issues?

An overwhelming majority of respondents (more than 90%), although differencing on the scope of social issues which should be included, were in favour of the EU Ecolabel considering social issues.

Q4.3: In relation to Q4.2, which of the following social aspects do you consider relevant for the EU Ecolabel for financial products?

Human rights and social rights were considered by 79% and 74% of respondents respectively as important issues for the EU Ecolabel.

Q4.4 To what extent do you consider that the EU Ecolabel should have criteria that address how ethical are corporate activities and governance structures?

More than 90% of respondents agreed that the inclusion of criteria related to corporate activities and governance structures are relevant as these would ensure that governance objectives are not jeopardised while the focus should be on environmental issues.

Q4.5 In relation to Question 4.4, which of the following governance aspects do you consider should be relevant for the EU Ecolabel for financial products?

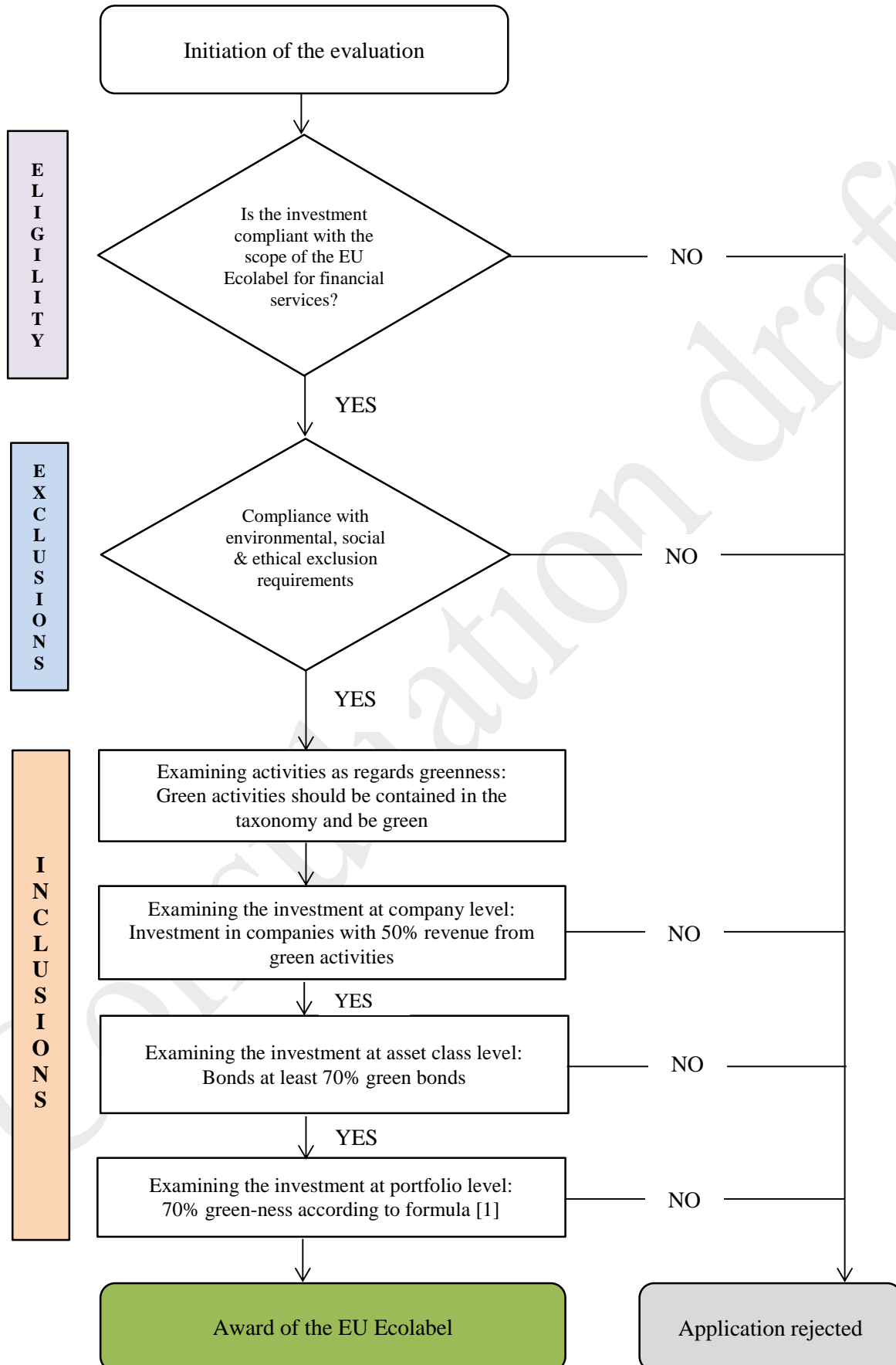
Transparency (75%) and anti-corruption (75%) were considered major issues to be addressed within any EU Ecolabel criteria addressing governance issues (Q4.5).

4 ANNEX

4.1 Evaluation flowchart and formula for the award of the EU Ecolabel

Consultation draft

Figure A1 – EU Ecolabel evaluation flowchart



The following formula [1] examines compliance of the investment portfolio with the pass/fail criterion to award the EU Ecolabel.

$$\frac{AC_1}{IP} (AC_1 \text{ Greenness in } \%) + \frac{AC_2}{IP} (AC_2 \text{ Greenness in } \%) + \dots + \frac{AC_n}{IP} (AC_n \text{ Greenness in } \%) > 70\% \quad [1]$$

AC: Value of the asset class investment

IP: Value of the investment portfolio

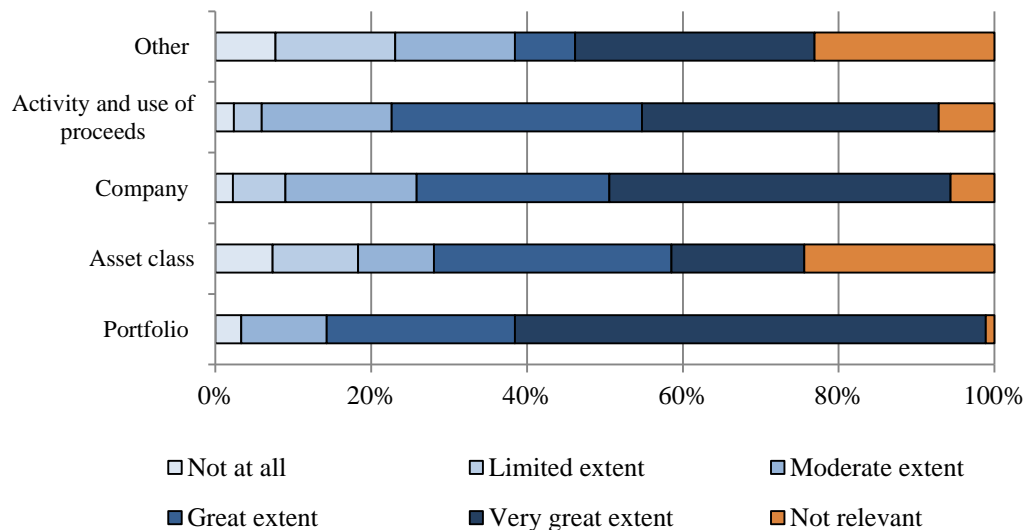
AC_{1...n} Greenness in %: Percentage of the asset class value invested in green underlying assets

4.2 Complete portfolio level results from the 1st stakeholder questionnaire

Q5.5 At what level do you consider the EU Ecolabel will need to work in order to verify the product's greenness?

60% of the respondents considered it important for the EU Ecolabel to work to a very great extent to assess the greenness of products at the portfolio level. Others (44%) considered the company level as the most appropriate.

Figure 1 – Level of verification of greenness.



It was argued by those proposing the company level that a threshold at the level of the portfolio or asset class would create a risk of a certain degree of greenwashing, as it will be unclear to retail customers that a certain part of the portfolio can be invested in companies/assets that do not have to comply with the Ecolabel criteria.

Q5.6.1 Based on your selection of 'portfolio' in Q5.5, what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel?

In defining investment threshold in green activities for portfolio to qualify for the EU Ecolabel, the responses from the survey was analysed. The results indicated that 31% of the participants, who responded to this survey question favoured criteria which would require that at least 50% of the portfolio should be invested in green activities for the product to qualify for the Ecolabel. 30% took the view that at least 70% should be the minimal portfolio threshold.

Q5.6.2 Based on your selection of 'asset classes' in Q5.5, what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel?

Of the total number of respondents, 31% favoured criteria which would require that at least 70% of the assets should be invested in green activities for the product to qualify for the Ecolabel. 26% took the view that at least 50% should be minimal asset threshold.

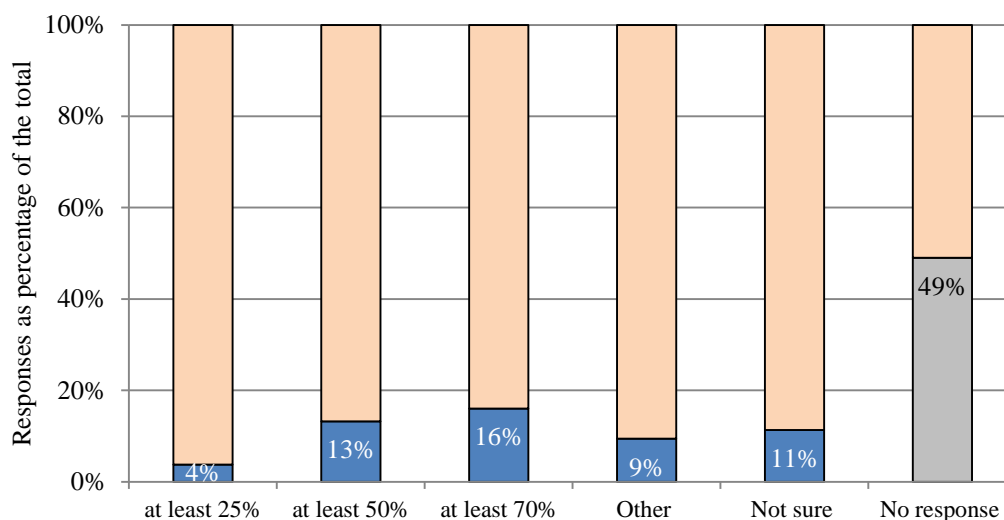


Figure 2 – Minimum investment in green activities at asset class level.

Given the relatively low rating received on whether the EU Ecolabel will need to work at the level of asset class in order to verify the product's greenness (Q5.5), and the low response rate to a minimum percentage threshold for asset classes, this option is not put forward.

Q5.6.3 Based on your selection of 'company' in Q5.5, what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel?

40% of the respondents favoured criteria which would require that at least 50% should be invested in green activities for the product to qualify for the Ecolabel. 25% took the view that at least 70% there should be minimal threshold.

Indirect holdings that employ business models which could be incompatible with the vision of the EU Ecolabel could impact the credibility of the label. Given the low percentage threshold favoured by most respondents, it is suggested that the proposal on the % turnover or revenue in green activities at the company level be complemented with a minimum percentage of the direct holdings which are under the control of the fund manager.

Given the moderate rating received on whether the EU Ecolabel will need to work at the company level in order to verify the product's greenness (Q5.5 and to Q5.6.3), this option is considered in addition to the proposal for portfolio threshold percentage.

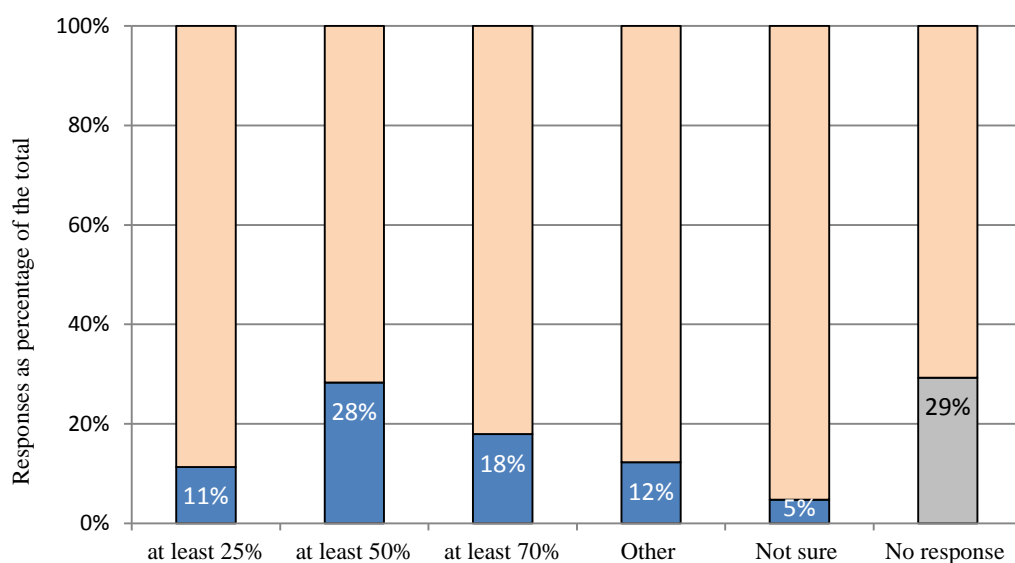


Figure 3 – Company's investments in green activities.

Q5.6.4 Based on your selection of 'activity' in Q5.5, what minimum percentage should be invested in green activities for product to qualify for the EU Ecolabel?

34% were in favour of criteria which would set a threshold of at least 50% at the activity level. Yet 29% took the view that at least 70% there should be minimal threshold at the activity level, and 7% of the respondents supported at least 25% as a minimum threshold at the activity level.

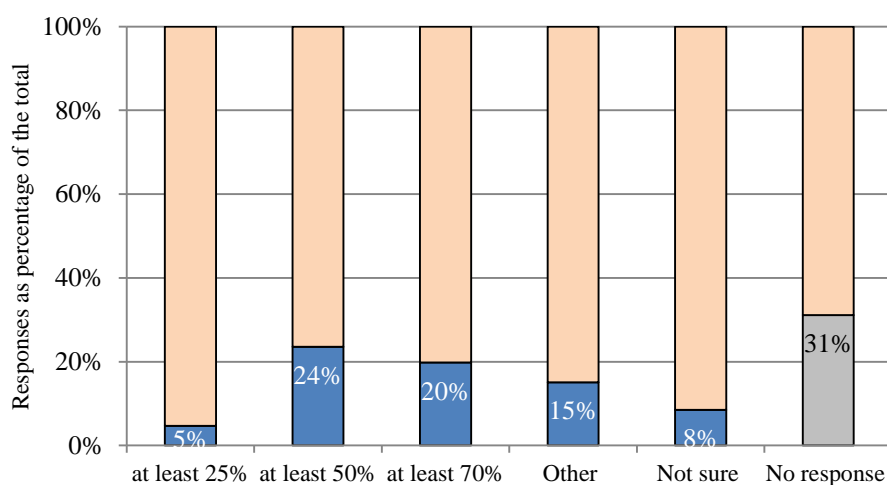


Figure 4 – Investment in green activities at activity level.

Q5.7 Please explain the reason for any of your selection in Q5.6 or provide your own proposal with a justification

Respondents who supported that the EU Ecolabel will need to work at the company (x% turnover or revenue in green activities) were mostly in favour of a minimum threshold of 50%. They viewed the company turnover threshold as very important and supported their selection based on the reasoning that the thresholds are directly linked to the credibility of the labelling scheme and that if required at the company level will have a direct and even stronger effect than exclusion criteria on the fact in which companies a fund is invested.

A few suggested that the any proposed threshold should exceed already existing best practices and be defined for each excluded activity separately. Whilst a few suggested starting thresholds of between 70% and 100% (depending on sectors)", others suggested that the percentage should be set corresponding the availability of sufficient sustainable investment opportunities, but should increase over time, increasing to at least 70%". They were of the opinion that 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 comply with the EU Ecolabel criteria.

Some respondents emphasized that the greenness requirement might not exclusively be based on a set of thresholds at activity/company/portfolio level but on a resulting combination i.e. by combining green activity/company share/portfolio composition which should be at least 50%.

About 26% of the 106 respondent to the questionnaire emphasized the importance of considering a green threshold at the portfolio level as well as the company (x% turnover or revenue in green activities) in the proposal for a climate change mitigation investment threshold. These responses were considered in the development of the criterion proposals.

Q5.8 Would you suggest any other methodology for defining the minimum portfolio allocation?

A range of overlapping responses from an equal number of respondents was received. These include:

- regardless of the level at which sustainable investment is made, the outstanding percentage cannot be invested in contradictory sectors or activities
- adopting requirement P3 of the Nordic Ecolabelling methodology
- adopting the FNG Siegel methodology
- consideration of ESG methods

The responses suggest that these aspects are of relevance to the definition and methodology for defining the minimum portfolio allocation.

Q5.9 Focussing on specific asset classes, please describe technical criteria that could apply to the following:

a). Transferable Securities.

i) Shares

Similar to Q5.8, a range of responses was obtained. While 3 respondents specifically referred to the use of the EU Taxonomy, another 2 suggested criteria based on the TEEC Label. Another suggested a criterion which combines the EU Taxonomy in combination with thresholds and exclusions but ensure that economic activities and sectors transitioning towards sustainability are not sanctioned. Other notable responses (5) were specific on the need to consider exclusion criteria in combination with selection criteria (best in class) together with minimum ESG ratings.

ii) Bonds

Roughly 50% of the respondents recommended to simply adopt the TEEC thresholds and corresponding to the GBP requires the use of proceeds, process for project evaluation and selection, management of proceeds, reporting and additionally (additionally criteria concerning the emitter). The remaining responses were varied and included the suggestion that the greenness of the issuers should be a selection criterion as it automatically determines the greenness of the bond.

These responses indicate that the EU Ecolabel criteria concerning bonds should consider current practice. However as work is underway on the development of the EU GBS, the criterion therein is put forward in the criterion on climate change mitigation thresholds.

Q5.9 Focussing on specific asset classes, please describe technical criteria that could apply to the following:

b) Financial derivative instruments

A large majority (44%) of the 25 respondents to the question were unified in their opinion that the use of this instruments should be restricted due to their complexity making their underlying assets difficult to track and the assessment of greenness almost impossible. There was no consensus on the remaining responses. The results of the market analysis and a review of the operation of the national labels and schemes support this recommendation. It is proposed that the EU Ecolabel adopt a similar approach.

c) Money market instruments

It was not possible to gain an understanding of the technical criteria that could be applied to money market instruments no consensus could be found from the divergent responses provided by stakeholders to the questionnaire survey.

d) Real Estate

25 responses were provided of which 10 recommended criteria on energy efficiency and greenhouse gas emissions but with the suggestion to also include social criteria. Another 3 suggested the application GRESB – the ESG Benchmark for Real Estate Assets.

Q5.10 When assessing the greenness of a portfolio, how should the ‘greenness’ of the various companies be weighted?

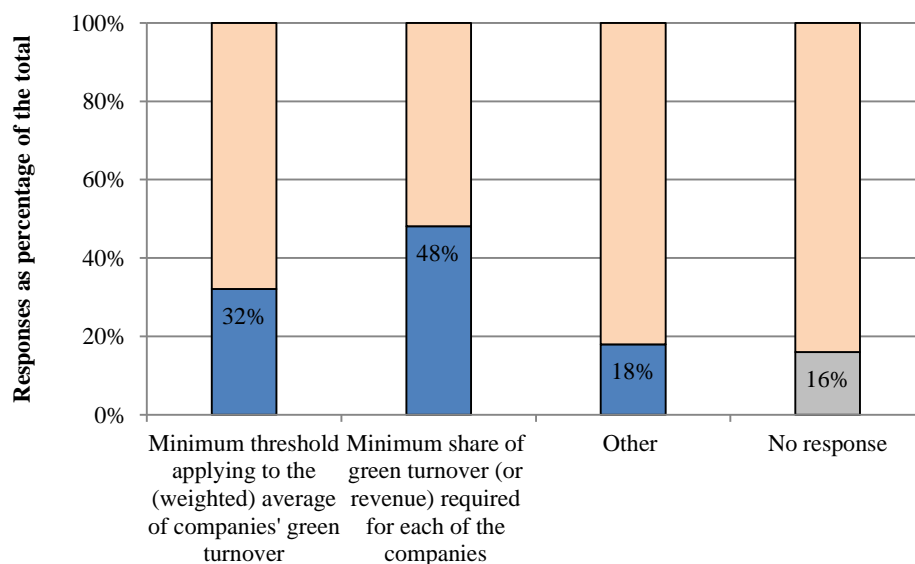


Figure 5 – Companies weighting in a portfolio greenness assessment.

48% responded in favour of the minimum share of green turnover (or revenue) required for each of the companies should be considered when weighting the greenness of various companies, 32% supported the minimum threshold applying to the (weighted) average of companies' green turnover.

Q5.11 To what extent should the greenness of the issuer of the bonds is taken into account?

Of the organizations surveyed, 12% did not provide any response. While 28% responded in favour of to a "moderate extent", 23% responded in favour of to a "great extent", and 21% responded in favour of to a "very great extent".

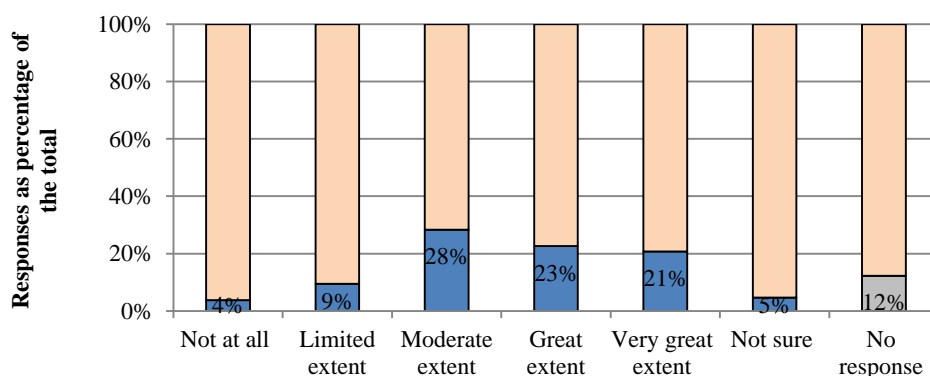


Figure 6 – Greenness of the issuer of the bonds.

Q6. Portfolio verification

Q6.1 To what extent would the following financial products require their own specific form of verification?

For investment funds addressed to retail clients, a slight majority 37% favoured generic verification while 36% requested very specific verification. For life insurance policies with an investment element, a generic approach was also favoured (38%). For structured products, and structured deposits a very specific verification was proposed by 44% and 40% of the respondents respectively. A very specific verification approach was also proposed for bonds, pension products, savings schemes/accounts.

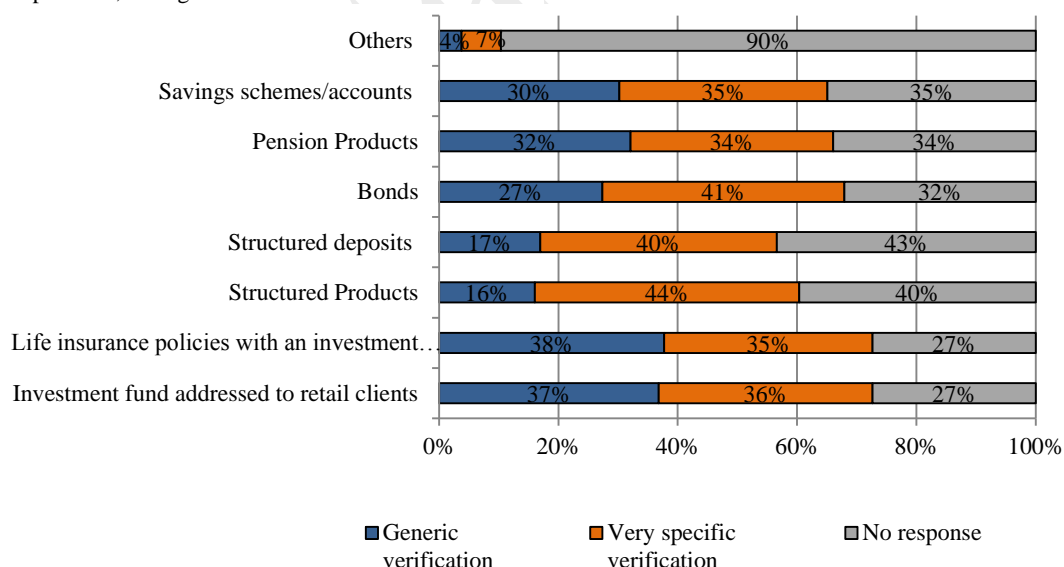


Figure 7 – Extent to which a financial product require specific form of verification.

Q6.2 To what extent would the following asset classes require their own specific form of verification?

A generic verification approach was favoured for shares but for other asset classes (bond, financial derivatives, money market instruments and real estate), a very specific verification approach was supported by the respondents.

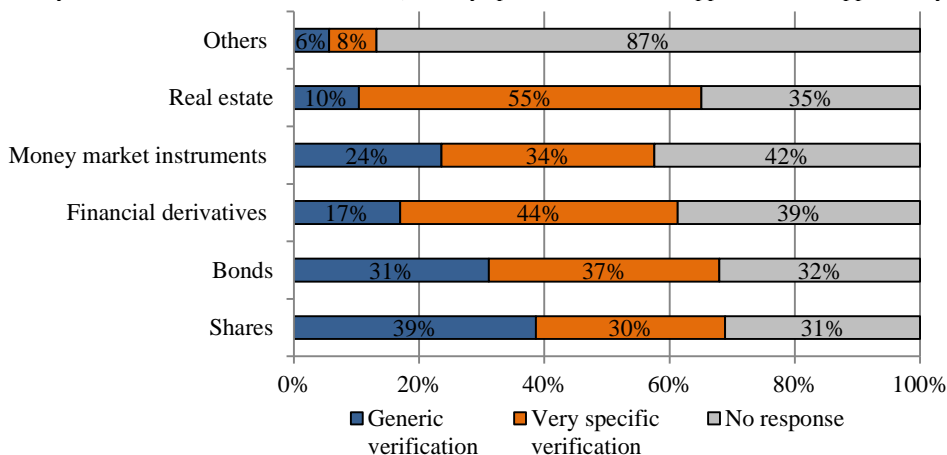


Figure 8 – Extent to which asset classes require specific form of verification.

Q6.3 How can the cost and complexity of assessment and verification be minimised?

Most respondents suggested some degree of harmonization building on existing schemes would enable financial players to work in parallel with labelling schemes. Clear, easy to understand and minimal reporting requirements were also put forward as measures to reduce the cost and complexity of the assessment and verification.

Q6.4 To what extent, and under what conditions, should private verifiers be permitted to assess compliance with the EU Ecolabel criteria?

A large share of the respondents (18%) supported permitting private verifiers to assess compliance to the EU Ecolabel criteria.

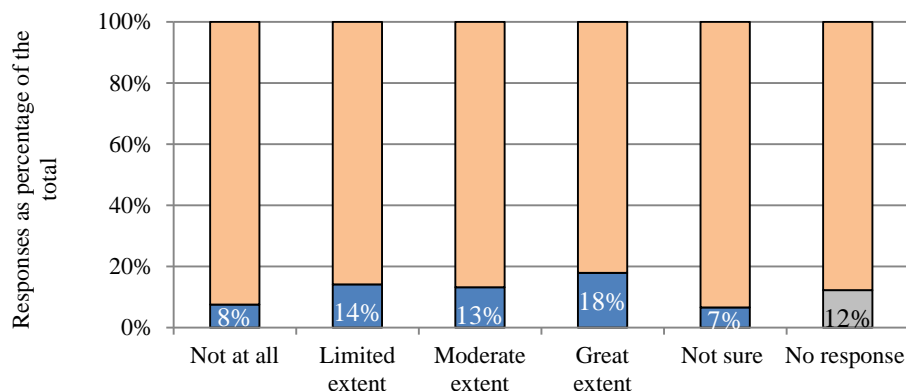


Figure 9 – Extent to which external verifiers should be permitted to assess compliance.

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