Green bonds: the future of equity financing?

1. A BURGEONING INDUSTRY

Green bond issuance is expected to balloon over the next few years. On a global scale, predictions for 2023 alone estimate up to $600bn will be raised from green bonds, with Europe playing a leading role in this. The European Commission will fund up to €250bn over the next few years by issuing NextGenerationEU green bonds, making the EC the largest green bonds issuer in the world. Greece is expected to raise substantial amounts through green bonds in order to reduce greenhouse gas emissions by 55% by 2030 and achieve net-zero by 2050.

The Greek government has announced that it will issue its inaugural green bond in 2023 with a view to (a) aligning its financial policy with national sustainability targets and facilitating, through regular reporting progress on the national ESG project, (b) strengthening Greece's investor base, by addressing institutional investors' rising ESG standards, and by reaching out to new types of investors, and (c) standing at the forefront of the Eurozone's sovereign issuers, by joining member states present on the sovereign green bond market, and by anticipating the growing impetus of credit rating agencies for environment-related assessment criteria.

2. THE GREEN BOND MARKET IN GREECE

To date, Greek entities have issued €3.875bn in green bonds and Bernitsas Law is proud to have advised on successful inaugural green bond issues by:

- Piraeus Bank's €500m Green Senior Preferred Bond in order to enhance its green financing and promote its ESG agenda.
- Mytilineos SA's €500m Green Senior Notes in order to fund eligible green projects within the company's Green Bond Framework.

3. APPLICABLE LEGISLATIVE FRAMEWORK IN GREECE

International guidelines

Currently, the green bond market is not governed by hard-wired legislation. Instead there are voluntary guidelines and standards issued by industry groups which set a soft minimum standard. The key guidelines observed by the industry are those of the International Capital Markets Association (ICMA) and the Climate Bond Initiative (CBI).

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> Maria Nefeli Bernitsa, Bernitsas Law

ICMA guidelines key requirements

DEFINITION

Green bonds are any type of bond instrument whose proceeds or equivalent amounts are exclusively applied to finance or refinance eligible Green Projects (see 'Use of proceeds' below on eligibility) which are aligned with the four core components of the green bond project.

4 Components of green bond project

USE OF PROCEEDS

Bond proceeds should be used for eligible Green Projects which include projects falling within the following categories: (a) renewable energy, (b) energy efficiency, (c) pollution prevention and control, (d) environmentally sustainable management of living natural resources and land use, (e) terrestrial and aquatic biodiversity, (f) clean transportation, (g) sustainable water and wastewater management, (h) climate change adaptation, (i) circular economy adapted products, production technologies and processes, and (j) green buildings.

PROCESS FOR PROJECT EVALUATION AND SELECTION

Issuers should communicate (a) the environmental sustainability objectives of their Green Projects, (b) the process followed in order to determine that the projects fit within the categories outlined above, and (c) information on the issuer's processes for identifying and managing social and environmental risks.

MANAGEMENT OF PROCEEDS

In the interests of achieving transparency, the net proceeds of the bond (or an equal amount) should be credited to a sub-account, moved to a sub-portfolio or otherwise tracked to ensure allocation to eligible projects.

REPORTING

It is recommended that the issuers will use qualitative and, where feasible, quantitative performance indicators in order to report annually on the use of proceeds.

TYPES OF GREEN BONDS

- Standard green use of proceeds bonds
- Green revenue bonds
- Green project bonds
- Secured green bonds

CBI guidelines

The CBI guidelines set out more granular requirements than the ICMA in relation to pre- and post-issuance, but always in the context of the four components of green bond projects outlined above. Crucially, a key component of the CBI scheme is the certification process.

GREEK LAW 4936/2022

Greece's recent climate change law was enacted less than a year ago in the context of Greece's goal to reach carbon neutrality by 2050. While it does not address the issuance of green bonds specifically, it sets out a number of key changes in the climate space which will likely affect the underlying investments for green bonds:

From January 2024 at least ¼ of new corporate vehicles shall be electric or hybrid.

From January 2025 the sale and installation of petrol-fuelled heaters is strictly forbidden.

From the end of December 2028 the production of electricity from lignite-powered plans is banned.

From 1 January 2030 all new privately used or corporate vehicles must produce zero emissions.

By 2030 the carbon emissions of buildings, social infrastructure (especially relating to sports, culture, public lighting and other public spaces), irrigation systems, sewage systems and state vehicles shall be reduced by 30% against the carbon emissions benchmark of 2019.

4. CHANGES EXPECTED TO THE LEGAL FRAMEWORK – EUROPEAN GREEN BOND (EuGB) STANDARD

In February 2023, the European Council announced that provisional agreement was reached on the European Green Bonds Regulation. Contrary to earlier statements by key stakeholders, the EuGB standard will be voluntary. This means that even after it enters into force, issuers will be able to continue using existing standards for the issuance of green bonds. The European Central Bank has expressed its view that EuGBs should become a mandatory standard within a reasonable time frame. The Regulation is yet to be ratified by the European Council and Parliament. It will enter into force 12 months following ratification and introduce the following key changes:

- *Green bond definition* – All proceeds of EuGBs are required to be invested in economic activities aligned with the Taxonomy. In its press announcement, the European Council stated that there will be an exception whereby some EuGBs are subject to an 85% threshold instead.
- *Supervision* – The designated national competent authorities of the home member state shall supervise that issuers comply with their obligations under the new standard.
- *Independent verification* – Alignment of the bond with the EuGB needs to be verified by an accredited verifier.
- *Enhanced reporting* – Issuers of EuGBs will be required to publish on their website a completed factsheet in the form prescribed by the legislation, the pre- and post- issuance reviews of allocations, the annual allocation reports and the impact report, which includes a description of the Green Projects, its environmental objectives and information about financing and environmental metrics.

5. TAXONOMY REQUIREMENTS APPLICABLE TO GREEN BONDS

The EU Taxonomy Regulation, which has been in force since January 2022, creates a common classification system for which products qualify as environmentally sustainable. EuGBs need to comply with the following Taxonomy requirements:

- contribute substantially to as least one of the six environmental objectives, namely: (a) climate change mitigation, (b) climate change adaptation, (c) sustainable use and protection of water and marine resources, (d) transition to a circular economy, waste prevention and recycling; (e) pollution prevention and control and (f) protection of healthy ecosystems; and
- not significantly harm any of the other five environmental objectives; and
- comply with minimum social safeguards set out in the eight fundamental conventions; and
- comply with the technical screening criteria established under the Taxonomy Regulation.

6. CHALLENGES AND POTENTIAL SOLUTIONS

Lack of clear economic benefit
For medium to smaller scale entities, the economic benefit of an environmentally sustainable bond offering is riskier and much harder to quantify. The passage of time and creation of successful precedents will lessen the perceived risk associated with these products.

Onerous reporting
The reporting requirements for complying with the Taxonomy are particularly onerous especially for smaller or less sophisticated players who struggle with the interpretation of the numerous key performance indicators in the Taxonomy. The market is creating solutions to the reporting challenge. It is expected that the hurdle will be overcome once this reporting requirement is morphed into the usual processes.

Potential reputational challenges
The potentially high reputational and monetary cost of marketing products as sustainable when in fact they do not meet the required threshold, is an important deterrent for firms. With more certainty and clarity on market practice and expectations, the deterrence will become less powerful.

7. LOOKING AHEAD

Despite the Greek economy's challenges over the last decade, Greece remains in possession of three great assets for an environmentally sustainable future: sun, wind and sea. These are key components for renewable energy and offer a fertile environment for sustainable biotech and agritech products. The ocean and existing efforts to conserve marine life, create opportunities for blue bond issuance as well. Greece's rich natural resources, coupled with the national and international targets for environmental sustainability, are expected to render Greece an important candidate for green bond issuances and sustainable investments more broadly.

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Greece Law Firm of the Year at the IFLR Europe Awards 2022 and 2021

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