Session 2: Structural advisory and external reviews
Approaches to environmental integrity and lessons from a decade of providing second opinions on green bonds

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Kristina Alnes
Senior Advisor Climate Finance
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• About CICERO and our role in the Green Bond Market

• Green Bonds and External Reviews Principles

• Impact reporting and verification

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CICERO is Norway’s foremost institute for interdisciplinary climate Research. Our areas of expertise include: the effects of manmade emissions on the climate, society’s response to climate change, and the formulation of international agreements. We have played an active role in the IPCC since 1995. In recent years we have also been one of the pioneers of climate finance research.

**CICERO Climate Finance Center**

Estimating climate-related material risks (scenarios, Shades of Risk, detailed analysis)

Climate scientists and financial decision-makers working together

Clearing house of latest science

**Director Kristin Halvorsen**

Halvorsen was Norway’s first female Minister of Finance. Her other posts include deputy Prime Minister and Minister of Education and Research.

**CICERO Climate Finance Advisory Board**

- BlackRock
- The World Bank
- Norwegian Ministry of Finance
- Størebrand
- DNB
- SEI
- Norges Bank Investment Management
CICERO and Green Bonds

CICERO is the leading provider of independent environmental assessments (Second Opinions) of green bond frameworks. Our goal with these assessments is to provide transparent information to investors.

- the first green bond (World Bank)
- the first municipal green bond (Gothenburg)
- the first corporate green bond (Vasakronan)
- the first green sukuk (Tadau Energy)
Climate risks have financial impact

Physical climate risks and the transition to a low carbon world are associated with significant financial risks.

There is no agreed upon methodology for translating climate risk into financial risk.
Which climate scenarios are most likely?

Achieving approximately 3°C degrees in 2100 is more likely than 2°C, given current information.

Political and/or technological events can influence the temperature increase, pushing it up to 4-5°C or pulling it lower towards 2°C

**Push factors**
- India and/or China fail to implement their NDCs
  - Half of global savings due to energy efficiency happen in these two countries
- Carbon Capture and Storage (CCS) deployment is delayed due to cost and public opposition

**Pull factors**
- CCS is deployed rapidly at large-scale
  - CCS plants are built at the historical pace of coal plants in China or nuclear plants in Europe
- The US recommits to Paris and ambitious ratcheting every 5 years

Source: Based on (Clapp 2017) etc.

Notes: 2°C is considered to be somewhat more likely than 4-5°C, given the possibility of tightening ambition under the Paris Agreement design, and the possibility of deploying CCS on a large scale. No climate policy reaching approximately 4-5°C would mean that current climate policies would be rescinded or relaxed.
Investors should expect losses from extreme weather

- Flooding and extreme events can have significant impacts in combination with extreme weather and sea level rise.

- According to an estimate by WRI costs related to flooding in South Asia may be as much as $215 billion annually by 2030 and current GDP at risk in India is $14.4 billion (World Resources Institute, 2017)

- All sectors can be impacted by flooding risk. Flooding in non-urban areas can have costly indirect impacts on supply chains

“Everybody should expect more extreme storms, no matter where they live.”
- Michael Wehner, a senior staff scientist at Lawrence Berkeley National Laboratory in California
Transition to climate resilience provides investment opportunities
Expert Network on Second Opinions

iisd
International Institute for Sustainable Development

bc³
BASQUE CENTRE FOR CLIMATE CHANGE
Klima Aldaketa Ikergai

°CICERO

SEI
Södertörns International Environment and Energy Research Centre

Tsinghua University
Who defines green?

Voluntary principles for issuing a green bond that the vast majority of issuers align with *across all markets*

Country level guidelines in *some markets*

Stock exchanges with green bond lists set *criteria for listing*

Green bond indices *have criteria for inclusion*
External Review is market practice

Types of External Review 2016 (note: some overlap)

- Verification based on China Green Bond Catalogue (28%)
- Second Opinions (approx. 50%)
- CBI (9%)
Green Bonds – timeline of assessment

Second Opinion / Rating
- Should report on use of proceeds annually until full allocation, thereafter in the event of material developments. Recommends impact reporting. Best-practice to have reporting reviewed.

CBI Certification
- Pre-Issuance Certification
- Post-Issuance Certification
- Annual reporting required, annual assurance is not mandatory
The Second Opinion Process

Assessment begins

- Green Bond Framework
- Sustainability Strategy and Reports
- Other relevant documentation

Draft Second Opinion

- Green Bond Principles
- Climate Science
- Use of Proceeds
- Management of proceeds
- Governance and Transparency
- Impact Reporting
- Relevant standards

Final Second Opinion

- Clarifications with Issuer as needed

Input from Issuer

- Week 1 - 2

- Week 3 - 5

Second Opinion Report

°CICERO
Shades of Green
CICERO’s approach

1. CICERO is an independent research institution, and our second opinions are issued independently of other stakeholders’ influence. This integrity has been valued by the market.

2. CICERO takes a dynamic and flexible approach in dialogue with issuers to enhance a climate-friendly and sustainable future. Our approach is developing as science and the market evolves.
# CICERO Green Bond Rating System

<table>
<thead>
<tr>
<th>SHADES OF GREEN</th>
<th>EXAMPLES</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Dark green</strong></td>
<td>Wind energy projects with a governance structure that integrates environmental concerns</td>
</tr>
<tr>
<td><strong>Medium green</strong></td>
<td>Plug-in hybrid busses</td>
</tr>
<tr>
<td><strong>Light green</strong></td>
<td>Efficiency in fossil fuel infrastructure that decreases cumulative emissions</td>
</tr>
<tr>
<td><strong>Brown</strong></td>
<td>New infrastructure for coal</td>
</tr>
</tbody>
</table>

- **Dark green** is allocated to projects and solutions that correspond to the long-term vision of a low carbon and climate resilient future.
- **Medium green** is allocated to projects and solutions that represent steps towards the long-term vision, but are not quite there yet.
- **Light green** is allocated to projects and solutions that are environmentally friendly but do not by themselves represent or contribute to the long-term vision.
- **Brown** for projects that are in opposition to the long-term vision of a low carbon and climate resilient future.
Some categories are *typically* greener than others

Shades of Green by Project Category

<table>
<thead>
<tr>
<th>Category</th>
<th>Light</th>
<th>Medium</th>
<th>Dark</th>
</tr>
</thead>
<tbody>
<tr>
<td>Renewable Energy</td>
<td>22</td>
<td>8</td>
<td>9</td>
</tr>
<tr>
<td>Energy Efficiency</td>
<td>1</td>
<td>8</td>
<td>1</td>
</tr>
<tr>
<td>Clean Transportation</td>
<td>1</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td>Climate Adaptation</td>
<td>9</td>
<td>17</td>
<td>3</td>
</tr>
<tr>
<td>Efficient Buildings</td>
<td>1</td>
<td>11</td>
<td>6</td>
</tr>
<tr>
<td>Water Management</td>
<td>1</td>
<td>6</td>
<td>5</td>
</tr>
<tr>
<td>AFOLU</td>
<td>1</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>Waste Management</td>
<td>7</td>
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**SHADES OF GREEN**

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External reviews provide transparency to investors

- Assessment of a green bond issuer’s framework for selecting projects and investments to be eligible for green bond funding
- Investors value an independent environmental quality review highlighting strengths, weaknesses and pitfalls
- Should be produced by an independent entity with environmental expertise and no economic interests in the outcome of investment
What do you think is the key information investors want from external reviews on green bonds?
Impact reporting builds investor trust

Impact reporting is in place for 38% of bonds

Source: CBI (2017)

A wide range of metrics is being used

Emissions Intensity

Energy saving

CO₂ Emissions

Production of (clean) energy

Energy intensity

TCE Reduction

Water saving

GHG

Water

CO₂ Savings

Water quality

Water intensity

Total water consumption

Sewage

Materials used and recycled

Particulate Matter Reduction

Waste generated and/or recycled

Water recycled

Solid Waste

NOx Reduction

Waste Gas

NMVOC

SO₂ Reduction

Source: CBI (2017)
To facilitate comparison of project results, it is suggested that issuers aim to report on at least a limited number of core indicators for projects included in their green bond programs.

For energy efficiency (EE) and renewable energy (RE)
1. Annual energy savings (EE)
2. Annual Greenhouse Gas (GHG) emissions reduced or avoided (EE and RE),
3. Annual renewable energy produced (RE)
4. Capacity of renewable energy plant(s) constructed or rehabilitated (RE)
Recommendations for reporting environmental impact

- Issuers shall report on direct environmental impacts such as renewable energy production, energy savings, reduced emissions (prioritizing a reduction of CO2-equivalents), increased resilience, environmental operations and infrastructure etc.
- Issuers may choose to add social and/or economic impacts when deemed feasible and relevant.
- Reporting should also include indirect effects, such as avoided emissions, distinguishing them from reduced emissions.
- Issuers shall commit to report on expected impact (ex ante), and strive to report on actual impact (ex post).
- Reporting should target net benefits.
- Issuers shall highlight methodologies used and the potential uncertainty of environmental data to readers.
Impact Indicators

- GHG emissions is an important indicator, however, other indicators might be relevant as well depending on project type.

- In the absence of one single commonly-used standard for the calculation of GHG emissions reduced/avoided, issuers may follow their own methodologies while disclosing assumptions, data sources and applied methodologies.

- Issuers are encouraged to report GHG emissions data only when they can provide full transparency on the applicable GHG accounting methodology and assumptions, which can be referenced.
Example of a Second Opinion

Tadau Energy Green Sukuk

<table>
<thead>
<tr>
<th>Category</th>
<th>Eligible project types</th>
<th>Green Shading and some concerns</th>
</tr>
</thead>
<tbody>
<tr>
<td>Renewable energy</td>
<td>Solar power</td>
<td>Dark Green</td>
</tr>
<tr>
<td></td>
<td></td>
<td>✓ Solar power is key to a low-carbon transition. Supportive activities for solar power generation include e.g. financing, design, and interconnection.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>✓ Potential concerns regarding supply-chain emissions partially addressed through the use of life cycle criteria in supplier selection.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>✓ Potential concerns regarding site selection partially addressed through selection process and rezoning reports. An Environmental Impact Assessment (&quot;EIA&quot;) could have provided assurance to investors of the environmental soundness of the site selection and construction phase.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>✓ All construction projects can have adverse local environmental impacts.</td>
</tr>
</tbody>
</table>

Table 2. Eligible project categories

Summary

Tadau Energy’s Green Sukuk Framework provides a sound framework for climate-friendly investments. The process will support solar power development in Malaysia, which is a key technology supporting the transition to a low-carbon and climate-resilient energy system.

Tadau Energy is a private limited company involved in the special purpose of constructing and operating solar projects. Tadau Energy has two shareholders: Empyrean Energy and Eden Solar. The proceeds from the Green Sukuk will be used to finance one project comprising two solar photovoltaic power plants in the district of Tadu. The issue has no plans for additional issues under this framework.

The issue has presented CICERO with relevant pieces of documentation, but no overarching policy, or strategy of the special purpose company will follow. This lack of documentation presents some challenges when assessing the project. The issue will report on a case of proceed through several criteria, which are only available through the issuance of the sukuk by the agencies. Transparency is key to build trust in the Green Sukuk market. CICERO encourages the issue to align cases and transparent communication practices to ensure investor confidence. CICERO notes that the issue has not committed to impact reporting.

Based on the overall assessment of project type and the policies guiding the implementation Tadau Energy’s Green Sukuk Framework is rated CICERO Dark Green.
Resources


- Climate Bond Initiative list of labelled green bonds: [https://www.climatebonds.net/cbi/pub/data/bonds#](https://www.climatebonds.net/cbi/pub/data/bonds#)

Discussion

Questions from the audience and conversation on the different approaches to external reviews
### Example: Municipality

<table>
<thead>
<tr>
<th>Category</th>
<th>Eligible project types</th>
<th>Green shading and some concerns</th>
</tr>
</thead>
</table>
| **Renewable energy**         | - wind power, solar power and bioenergy from agricultural residues, forestry residues and other biological residues | Dark green  
✓ Consider negative impacts on wildlife, nature and lifecycle pollution. Avoid negative impacts on biodiversity.  
✓ Only bioenergy from local sources  
✓ Fractions of peat is included. Last year 12 percent of the energy input in the new biomass CHP came from peat, expected to be reduced this year to 8 percent. From 2019 the intend is to not use peat at all. |
| **Energy efficiency**        | - district heating/cooling, energy recovery, energy storage and smart grids.            | Dark green  
✓ Be aware of possible rebound effects. |
| **Sustainable transportation** | - public transportation, pedestrian and bicycle paths, hydrogen, biogas and electrical vehicles | Dark green  
✓ Potential for emission reduction depends on area planning and degree of urbanization, introduction |

- **Replacement of fossil raw materials**  
  - e.g. from fossil based plastics to bioplastics.  
  - Dark green

- **Energy efficient commercial and residential buildings**  
  - commercial and residential buildings that meet the energy requirements for PEZY, Sverres or Miljöbyggnad Silver.  
  - Major renovations leading to a reduced energy use of at least a 35% per m² Abetp and year.  
  - Medium green  
  ✓ Building criteria are considered adequate but may not reflect best available technology nor the highest level of standards possible in Sweden.  
  ✓ Be aware of possible rebound effects.

- **Waste Management**  
  - Dark green  
  ✓ Good practice waste management should recycle resources.  
  ✓ No investments in waste to energy, i.e. combustion of fossil fuels plastic.

- **Water and waste water management**  
  - Dark green  
  ✓ No risk of investments in existing fossil fuel or nuclear infrastructure (e.g. pipe upgrades).

- **Climate adaptation measures**  
  - Dark green  
  ✓ Important given climate change scenarios and higher frequency of extreme weather conditions.  
  ✓ Potential for good synergies with mitigation actions and opportunities.

- **Environmental measures**  
  - Medium Green  
  ✓ Max. 20 percent. Good for environment as a whole. Very broad category. No climate mitigation objective.
Green Bond Principles (GBP)

Voluntary principles for issuing a green bond. The vast majority of issuers align with the GBP. High level principles with four core components:

1. Use of Proceeds
2. Process for Project Evaluation and Selection
3. Management of Proceeds
4. Reporting

ICMA is the GBP secretariat, the principles can be downloaded from their resource center:
Use of Proceeds

The Green Bond Principles lists examples of green project categories which include, but are not limited to:

- Renewable energy
- Energy efficiency
- Pollution prevention and control
- Environmentally sustainable management of living natural resources and land
- Terrestrial and aquatic biodiversity conservation
- Clean transportation
- Sustainable water and wastewater management
- Climate change adaptation
- Eco-efficient and/or circular economy adapted products, production technologies and processes
- Green buildings

Source: CBI, Bonds and Climate Change The state of the Market 2017
Process for Project Evaluation and Selection

Example: World Bank Group

Example: SEB