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External Review & reporting for Sustainable Bonds

15 May 2024

Bhutan

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External Review

Need for an external review

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» **Issuers seek external reviews for the same reasons more traditional external assurance is sought. For example, to demonstrate:**

- Adherence to certain principles and/or standards such as ICMA's Green Bond Principles
  - "Am I following market practices?"
- The environmental and/or social integrity of the financial product
  - "Are the activities I am financing green/social/sustainable?"
- Adequacy of internal controls and procedures
  - "Are my processes aligned with market practices?"
- Adequacy of Key Performance Indicators (KPIs) chosen
  - "Are my reporting indicators descriptive of actual environmental/social performance"?
- Improve overall credibility





EXTERNAL REVIEW

External review providers

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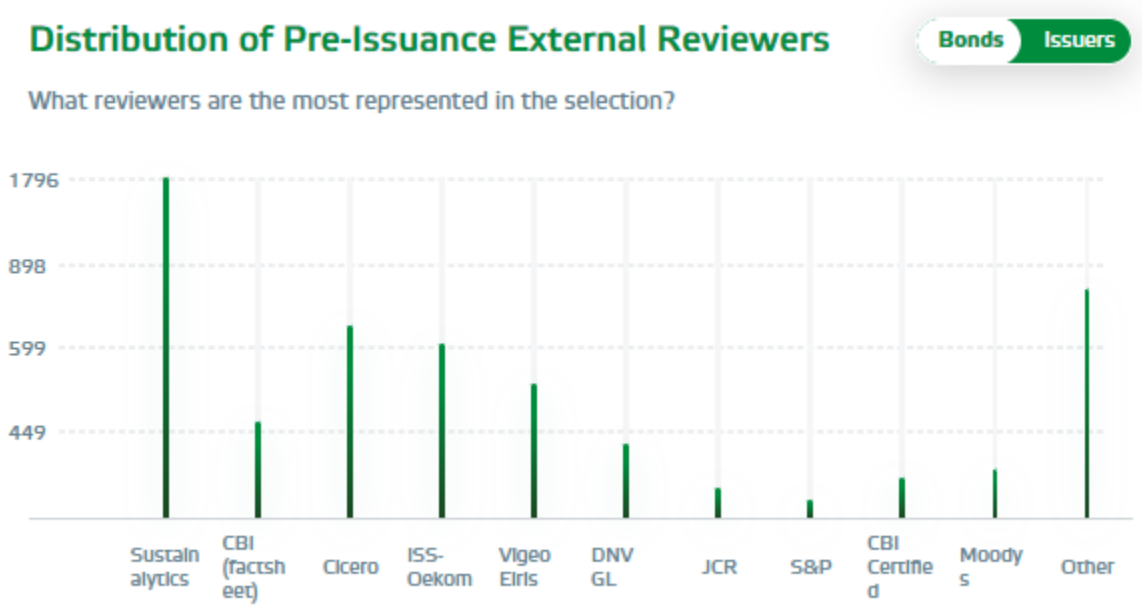
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SynTao Green Finance
联合赤道
China Lianhe Equator
瑞景通途
Make Green Achievable

Statistics on external review

» **There are a variety of ways for issuers to obtain an external review on the environmental and/or social credentials of their bond, or bond framework:**



Source: LGX DataHub, a universe of 7000+ sustainable debt instrument as per 01/09/2022

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Types of External Review

Types of external review

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» **There are a variety of "products" external reviewers can provide to issuers on the environmental and/or social credentials of their bond, or bond framework:**

- Second Party Opinion (SPO)
- Certification
- External verification (Assurance)
- Rating



TYPES OF EXTERNAL REVIEW

Second Party Opinion (SPO)

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- Most widely used form of external review provided by independent organisations
- Usually issued based on a bond framework (validity: n-years)
- It evaluates the bond framework against a specific principle/standard
- Most commonly against the ICMA principles if use of proceeds bond or an SLB
- Generally, includes an assessment of the issuer's overarching objectives, strategy, policy and processes relating to the environmental and social features of the type of projects that the issuer intends to finance with the proceeds



S&P Global
vigeo eiris
SUSTAINALYTICS
CICERO Center for International Climate Research
DNV·GL
ISS-oekom

Advantages and limitations of SPO

ADVANTAGES

- It is a valuable improvement on issuer disclosure as it provides some additional comfort to investors on the validity of the issuer's claims
- The second party providers work with the issuer to ensure the information investors are looking for is included

LIMITATIONS

- Relatively high transaction costs for investors, limiting scaling of the market
- Reviews can lack independence
- Reviews often provide limited disclosure of environmental performance criteria



Source: OECD

Certification

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- An issuer can have its green, social or sustainability bond (or associated framework) certified against a recognised external standard or label
- That standard or label defines specific criteria
- Alignment with such criteria is normally tested by qualified third parties which verify the consistency of the relevant bond (or framework) with such criteria

CLIMATE BONDS STANDARD CERTIFIED

Climate Bonds Standard



Source: CBI

Advantages and limitations of certification

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ADVANTAGES

- Reducing transaction costs through standardisation
- Certification providers are less reliant on internal environmental expertise of the issuer (Independence from issuer increased compared to second party review model)
- Science-based criteria
- **Diversifying investor base:** Certification signals the integrity of a particular type of investment (e.g., low-carbon). May be important for investors looking for specific types of investments, in addition to other green bond investors

LIMITATIONS

- It is time-consuming and resource intensive to develop robust sector-specific criteria



Source: OECD

TYPES OF EXTERNAL REVIEW

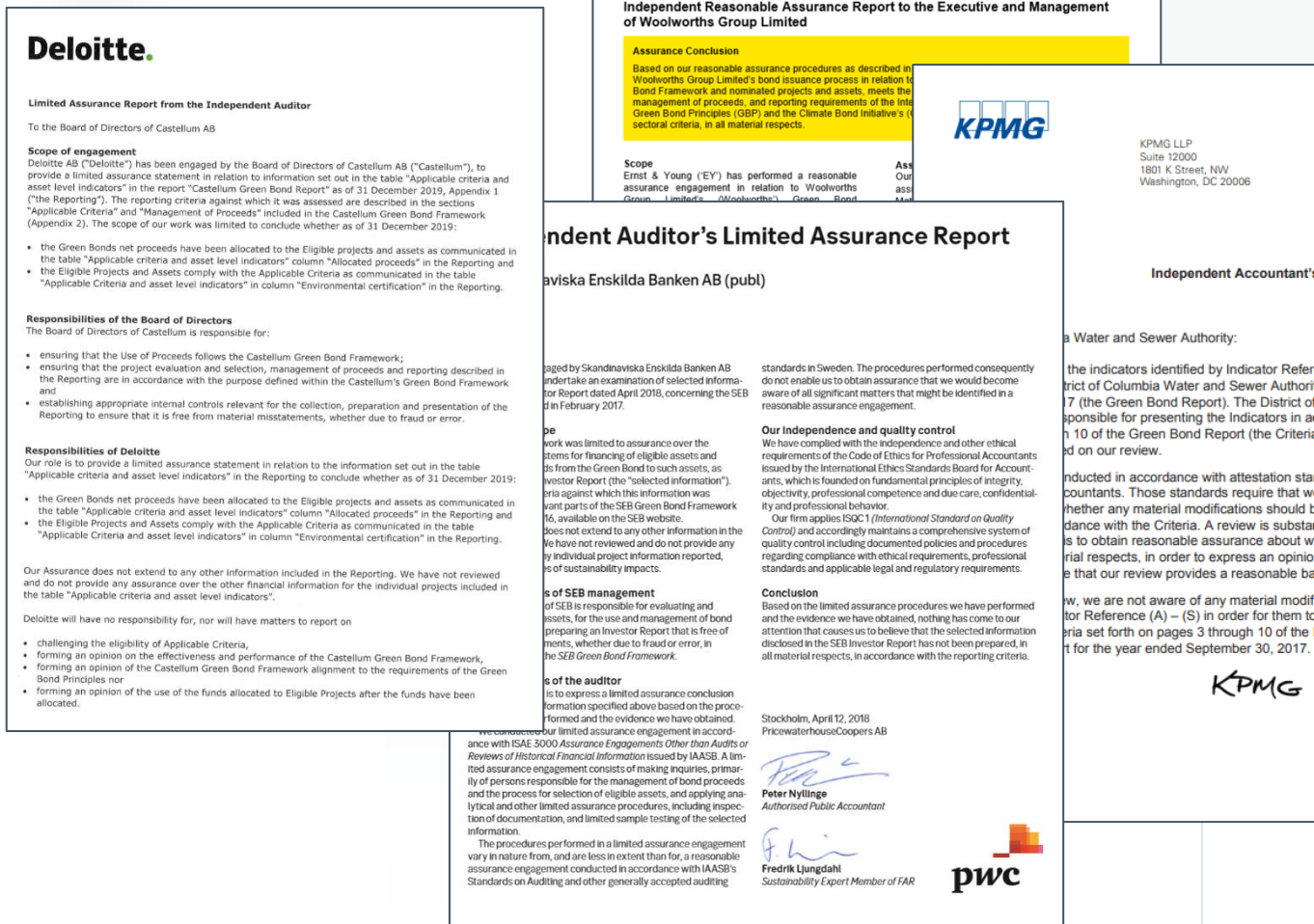
External verification

WHAT DO WE MEAN BY THIS?

- An external verification is typically made based on an annual green or social of sustainability bond post-issuance report, or information
- A few established issuers, such as the EIB, go this route

WHY SEEK AN EXTERNAL VERIFICATION?

- Larger institutions already commit to an audit of the sustainability/green credentials and decision-making
- The audit report will contain the necessary assurances required for green bond issuances, so a separate opinion is not necessary
- For organisations who already have a second opinion, external verification provides investors with extra assurance on reporting, for example



Advantages and limitations of external verification

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ADVANTAGES

- Transaction costs can be lower than those for an SPO as the assurance can be integrated with general financial audits for the issuer
- More independence than the second party opinion; adherence to international assurance standards

LIMITATIONS

- Assurance does not cover the environmental/social impacts of the projects funded by the bond
- Post-issuance auditing might result in a requalification of the green bond and the risk of investors seeing their investments classified as not green



Source: OECD

Rating

ADVANTAGES

- Rating agencies could integrate the offering with their credit rating services
- The green bond reviews could benefit from rating agencies' credibility in the mainstream financial markets



LIMITATIONS

- Certain rating agencies are currently exploring green bond assessments that are focused on rating the process (management of proceeds, disclosure and reporting) rather than providing detailed rating on how green the projects funded by the green bonds are
- Investors may want more on green asset quality, which rating agencies do not directly have the expertise to assess
- As for second party providers, rating agencies might face lack of independence issues

Source: OECD

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Reporting

Why is GSS bond reporting important?

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» **For the same reasons traditional financial reporting is undertaken, but especially important for a nascent market, to build investor trust in non-traditional activities**

- Allow the organisation (and investors) to set benchmarks and environmental/social performance goals
- Measure, control and monitor green and social activities
- Demonstrate compliance to certain standards/international goals
- Improve communication among investors, issuers and project owners

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Allocation vs. Impact reporting

What is allocation reporting?

- Mandatory components of ICMA's GBP, SBP, SBG and almost all other standards
- Issuers should make and keep readily available up to date information on the use of proceeds to be renewed annually until full allocation and on a timely basis in case of material developments
  - The annual report should include:
  - List of projects with a brief description of the projects
  - The amounts allocated and their expected impact
- If details cannot be provided (confidentiality issues, big number of projects…) information should be presented in generic terms or aggregated portfolios

Source: ICMA GBP

What is impact reporting?

- Recommended components of ICMA's GBP, SBP, SBG and almost all other standards
  - GBP recommend the use of qualitative performance indicators
  - Where feasible, quantitative performance measures and disclosure of the key underlying methodology and/or assumptions
- Issuers with the ability to monitor achieved impacts are encouraged to include those in their regular reporting
- Different voluntary guidelines have been published in an attempt to standardise impact reporting
  - Goal: Create a harmonised framework for impact reporting that issuers can adapt to their own circumstances
- Mandatory pillar of the draft EU GBS



Source: ICMA GBP

ICMA Harmonised Framework for Impact Reporting

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- Provides issuers with a reference as they develop their own reporting
- Recommends the use of both qualitative performance indicators and, where feasible, quantitative performance measures with the disclosure of the key underlying methodology and/or assumptions
- Offers impact reporting metrics and sector-specific guidance for the project categories
- Reporting templates are included for issuers to use and adapt to their own circumstances

V. Reporting Templates

Renewable Energy

Illustrative Summary Template for Project-by-Project Report:

Renewable Energy (RE)	Signed Amount a/	Share of Total Project Financing b/	Eligibility for green bonds	RE component	Allocated Amount c/	Project lifetime d/	#2) Annual generation (electricity / other)		#3) a) Renewable energy capacity added	#3) b) Renewable energy capacity rehabilitated	#1) Annual GHG emissions reduced/avoided e/	Other Indicators
Project name f/	currency	%	% of signed amount	% of signed amount	currency	in years	MW/ GWh	GJ/ TJ	MW	MW	in tonnes of CO_2 equivalent	
e.g. Project 2	XX	XX	XX	XX	XX	XX	XX	XX	XX	XX	XX	Capacity of RE plant(s) to be served by transmission systems (MW) XX t CO_2 eq. Absolute annual project emissions.

Illustrative Summary Template for Portfolio-based Report[35]:

Renewable Energy (RE)	Signed Amount a/	Share of Total Portfolio Financing b/	Eligibility for green bonds	RE component	Allocated Amount c/	Average portfolio lifetime d/	#2) Annual generation (electricity/other), possibly per unit of financing		#3) a) Renewable energy capacity added (possibly per unit of financing)	#3) b) Renewable energy capacity rehabilitated (possibly per unit of financing)	#1) Annual GHG emissions reduced/avoided (possibly per unit of financing) e/	Other Indicators (possibly per unit of financing)
Portfolio name	currency	%	%	%	currency	years	MWh/ GWh	GJ/TJ	MW	MW	in tonnes of CO_2 equivalent	
e.g. Portfolio 2	XX	XX	XX	XX	XX	XX	XX	XX	XX	XX	XX	Capacity of RE plant(s) to be served by transmission systems (MW) XX t CO_2 eq. Absolute annual portfolio emissions

Source: [ICMA Harmonised framework for impact reporting]

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Best practice for post-issuance reporting

Example: What does a best practice post-issuance report look like?

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- Availability: Public
- Frequency: Annual, until maturity of the bond/full allocation
- Content: Use of proceeds (allocated and unallocated), environmental/social impact with appropriate metrics
- Complete project list
- Accuracy: Figures specific to each bond and project

ISIN	Total proceeds allocated	Total proceeds not allocated	Proceeds allocated to eligible activity X	Proceeds allocated to eligible activity Y	Proceeds allocated to eligible activity Z	Etc.
XS123456789	EUR 400 million	EUR 100 million	EUR 85 million	EUR 10 million	EUR 5 million	Etc.

Source: Luxembourg Green Exchange observations

Example: What does a best practice post-issuance report look like?

Project/ Portfolio name	Project/ portfolio description	Eligible activities category	Tangible or intangible asset (private or public)	ISIN of Green Bond(s) proceeds used	Total project/ portfolio investment	Amount of green bond proceeds allocated
Northeast Wave Power One	Construction, installation and operation of 10 wave power units	Renewable energy	Tangible	XS12345689	EUR 100 Million	EUR 75 Million

Project start date/end date	Share of proceeds used for direct financing vs. refinancing	Share of co-financing by others	Share of proceeds allocated	Impact metric (absolute, annually)	Impact metric (relative)	Qualitative impact description
2016 ongoing	100% direct	25%	90% CAPEX 10% OPEX	0 kt CO2e	-25kt CO2e	Replacement of local gas-fire combined heat and power

Source: Luxembourg Green Exchange observations

USE OF PROCEEDS CASE STUDIES

Philippines sustainability bond: Reporting

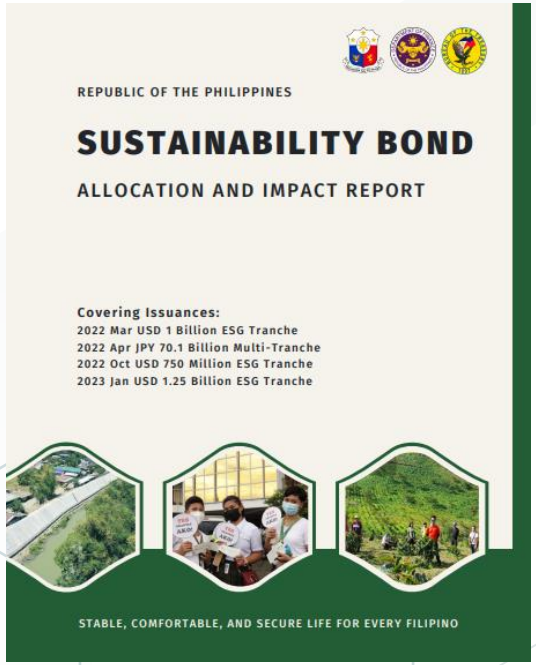
ALLOCATION & IMPACT REPORTING COMMITMENTS AT FRAMEWORK LEVEL

The Allocation Report may include:
- Amount of net proceeds raised
- Balance of unallocated net proceeds
- Total amount of net proceeds allocated per Eligible Expenditure
- Details of the split between financing and refinancing

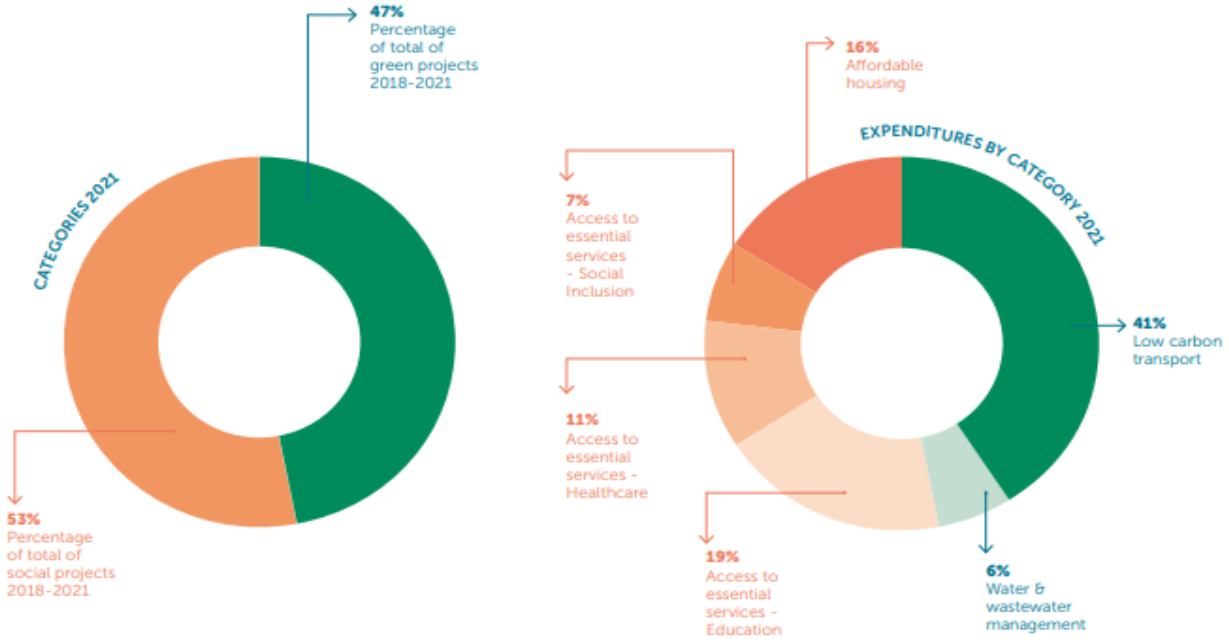
The impact report:
Where feasible, it will aim to report on on the estimated environmental and social impacts arising from the implementation of the Eligible Social Projects and/or Eligible Green Projects, in coordination with the concerned implementing NGAs

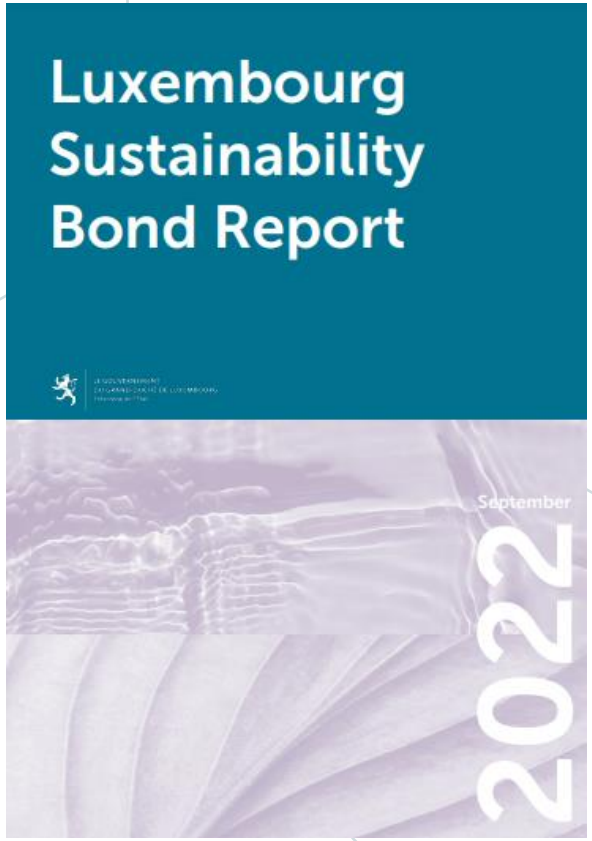
[Philippines Sustainability Bond Report]

ACTUAL REPORTING : PUBLICLY AVAILABLE ON THE WEBSITE OF THE BUREAU OF TREASURY (BTr)



Example on allocation reporting





Source: [Luxembourg sustainability bond report]

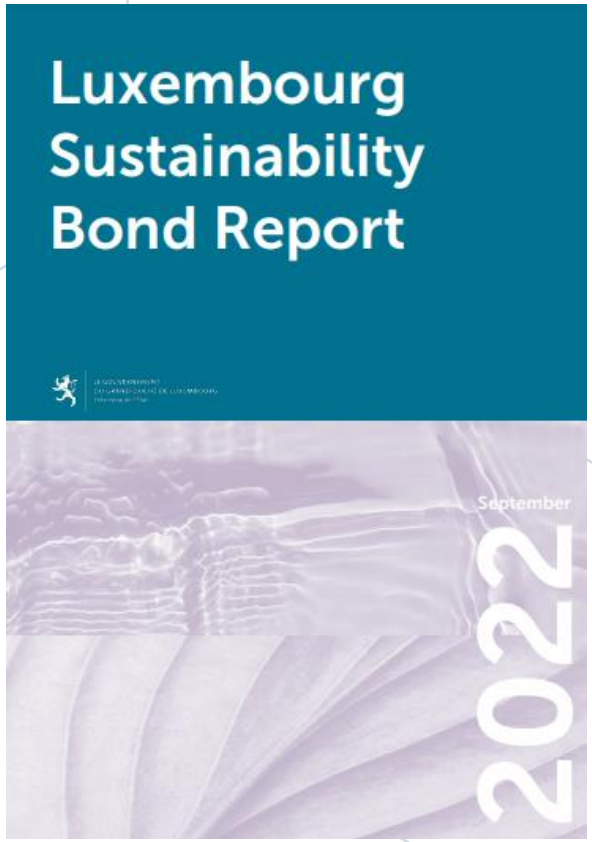
Example on impact reporting

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Low Carbon Transport

PROJECT TARGET	Investments in **7 low carbon transport projects**	30 Deploy **30 low carbon vehicles** by 2030 (tram)	31 mil. Serve **31 million users on tramlines (max.)** per year by 2030	Build **36 km** of new tram & rail lines by 2030
LSB REALISED BY/IN 2021	Invested in **7 low carbon transport projects**	17 Deployed **17 low carbon vehicles** (tram)	15 mil. Served nearly **15 million users on tram lines** (in 2021)	Built **18.6 km** of new tram & rail lines

PROJECT TARGET	469 mil. Enable **469 million passenger-kilometres (pkm)** per year by 2025	Enable **2.7 billion tonne-kilometres** per year of rail transport	600 000 Transfer **600 000 ITUs (max.)** per year from road to rail transport	Transfer **3.4 million tons of freight** per year from road to rail transport
LSB REALISED BY/IN 2021	88.8 mil. Enabled **88.8 million passenger-kilometres (pkm)** (in 2021)	Enabled **2.6 billion tonne-kilometres** of rail transport (in 2021)	163 500 Transferred **163 500 ITUs** from road to rail transport (in 2021)	Transferred **> 4 million tons of freight** from road to rail transport (in 2021)



Source: [Luxembourg sustainability bond report]

ICMA Harmonised Framework for Impact Reporting

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THE OBJECTIVE IS TO ENHANCE THE USABILITY OF THE INITIAL DOCUMENTS AND TO AVOID REPETITIONS

» Voluntary guidelines, unites the already existing harmonised frameworks in one document

» Existing harmonised frameworks are:

- The first Harmonised Framework for Impact Reporting by 7 MDBs (2015) on renewable energy and energy efficiency sectors
- Sector specific guidelines under ICMA GBP:
- Sustainable Water and Wastewater Management Projects (June 2017)
- Sustainable Waste Management and Resource-Efficiency Projects (February 2018)
- Clean Transportation Projects (June 2018)
- Green Building Projects (February 2019)
- Biodiversity (April 2020)
- Climate change adaptation (December 2020)



Source: [ICMA Harmonsied framework for impact reporting]

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Thank you!

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