

Green Bond Principles

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1. Executive Summary

Green Bonds are fixed-income instruments that finance green projects with environmental benefits. Green Bonds have been largely influenced by the Green Bond Principles (“the Principles”), but the lack of a regulatory body for Green Bonds has been questioned. This paper seeks to inform potential investors about the Green Bond Principles and address some of the issues raised.

1.1 Green Bond Principles¹

The Principles are a set of guidelines that recommend transparency and disclosure and promote best practices in the Green Bond market. The Principles have acted as an industry standard for structuring Green Bonds even though they are not a regulatory body. The Green Bond Principles comprise four pillars:

Use of Proceeds	Process for Project Evaluation and Selection	Management of Proceeds	Regular Reporting
<ul style="list-style-type: none"> • Declare the eligible Green Project categories that the proceeds of the bond will go to • Projects should provide clear environmental benefits that will be assessed and, when feasible, be quantified by the issuer 	<ul style="list-style-type: none"> • Outline the process to determine how the project fits within the eligible Green Project categories • Establish the environmental sustainability objectives • May take into consideration the quality of the issuer’s overall environmental sustainability profile 	<ul style="list-style-type: none"> • Move the proceeds of the Green Bonds to a sub-account or otherwise track the proceeds of the bonds by a formal internal tracking process • As long as the bonds are outstanding, the balance of the tracked proceeds should be periodically adjusted to match the allocations to Green Projects during that period • Should make known the intended types of temporary placement for unallocated proceeds 	<ul style="list-style-type: none"> • Report at least annually on the list of projects invested from the proceeds with the amounts allocated to each one • Qualitatively and/or quantitatively measure the impact of the investments

Furthermore, the Principles recommend that issuers undergo an external review to confirm the alignment of their Green Bonds with the four pillars of

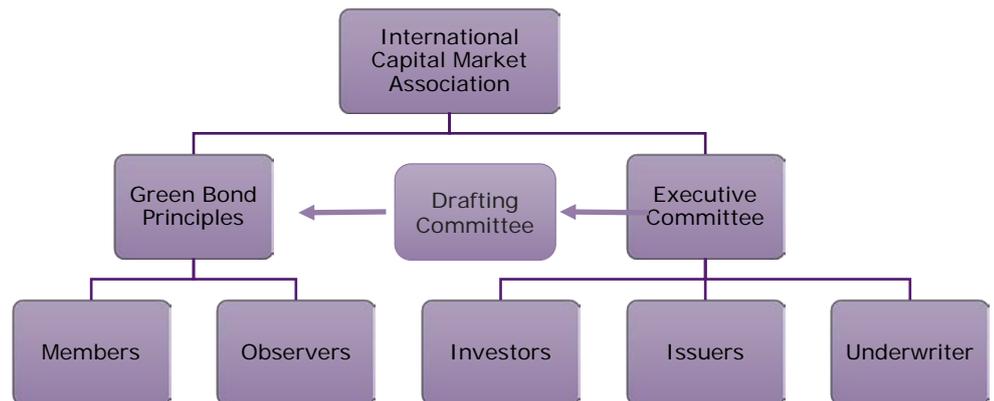
¹<http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/green-bonds/green-bond-principles/>

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the Principles and, in some cases, verify the environmental benefits (most commonly known as a second opinion).

The Principles have a governance structure that allows stakeholders to provide input on the decision making process with respect to: 1) updates to the Principles; 2) oversight of a Secretariat; and, 3) all other matters that may arise in regards to the Principles. The governance structure comprises two levels of participation: Members and Observers. Green Bond issuers, investors, and underwriters are qualified to apply for membership to the Principles. Observers consist of organizations active in the field of green finance but don't qualify for members such as Non-Government Organizations ("NGOs"), universities, auditors, and service providers.



The International Capital Market Association acts as the Secretariat for the Green Bond Principles. The duties of the Secretariat includes: 1) host the principles; 2) receive and approve Member and Observer applications; 3) maintain a web-page with a list of Members, Observers, the Executive Committee, and the Drafting Committee; 4) organize and run general meetings of the Members and Observers; 5) manage other meetings and calls, including maintaining minutes; 6) advise on governance issues; and, 7) handle other administrative matters. The Secretariat shall not be a regulatory body for the Principles.

1.2 Executive Committee²

Investors	Issuers	Underwriters
<ul style="list-style-type: none"> •ACTIAM N.V. •BlackRock, Inc. •California State Teacher's Retirement System (CalSTRS) •KfW •Mirova •Standish Mellon Asset Management Company LLC •TIAA-CREF Asset Management •Zurich Insurance Group 	<ul style="list-style-type: none"> •European Bank of Reconstruction and Development (EBRD) •European Investment Bank (EIB) •ENGIE •International Finance Corporation (IFC) •Nordic Investment Bank (NIB) •Unibail-Rodamco SE •Unilever •World Bank 	<ul style="list-style-type: none"> •BofA Merrill Lynch •BNP Paribas •Coöperatieve Rabobank U.A. •Credit Agricole CIB •HSBC •JPMorgan Chase & Co. •Morgan Stanley and Co International PLC •Skandinaviska Enskilda Banken AB (SEB)

The Executive Committee ("EC") is elected by the general members of the Principles and comprises eight investors (including Mirova), eight issuers, and eight underwriters. The EC has the authority to address matters regarding the Principles including voting on amendments to the Principles and appointing the Drafting Committee ("DC"). The DC comprises one to

²<http://www.icmagroup.org/Regulatory-Policy-and-Market-Practice/green-bonds/executive-committee/>

three previous Green Bond investors; one to three previous Green Bond issuers; and one to three Green Bond underwriters but cannot exceed six total members. The Drafting Committee reviews feedback from Members and Observers, provides the EC with recommendations for changes to the principles, and provides a revised draft for approval by the EC.

2. Investor Concerns

The Green Bond Principles have historically been the market standard definition for what constitutes a Green Bond, but a few entities, such as the Climate Bond Initiative, have developed their own variations. The Principles have provided a definition of Green Bonds that has promoted issuances while maintaining a high standard of what is considered “green.” For example, “pure play” bonds, bonds issued by green companies (e.g. a wind turbine manufacturer) that are used for general corporate purposes, are not acknowledged as Green Bonds by the Principles due to the lack of a clear use of proceeds and limited transparency. To ensure the legitimacy of the Green Bond, the Principles recommend a second-party external review to objectively evaluate its environmental benefit.

We believe standardization would help the growth and credibility of the Green Bond market but requires a delicate balance. The Green Bond market may lose credibility if it implemented standards that were too relaxed and could result in new Green Bonds that provide little to no environmental benefit. On the other hand, stringent standards could be a deterrent for potential Green Bond issuers. Transparency is a large component of the Green Bond market but developing standards that are too strict could discourage potential issuers and therefore hurt the Green Bond market.

Skeptical investors could criticize the Green Bond market for not implementing a regulatory body that verifies the authenticity and tracks the proceeds of Green Bonds. The Principles are a market-driven organization that acts to promote green finance but does not act as a regulator. In its infancy, the Principles perceived regulation as a force that could restrain innovation or fix an inadequate definition of Green Bonds. Mirova believes that it is unlikely for a corporation to deliberately mislead investors with a weak Green Bond issue because the issuer would face significant reputational damage due to the level of transparency a Green Bond issue demands. The market has achieved a lot on its own initiative but following the Paris Agreement in 2015³, it is time for policy makers to create a positive environment in which Green Bonds can thrive and assist in the global challenge of energy transition and carbon reduction. A regulatory framework and the potential reputational risk should prevent weak Green Bond issuances and further ensure the legitimacy of the Green Bond Market.

Mirova believes the use of an active Green Bond manager may alleviate some of the concerns regarding the legitimacy of the Green Bond Market. Active Green Bond management may add value in many ways including but not limited to:

- 1) providing an independent review of the risks and opportunities of linked projects;
- 2) seeking meaningful impact and analyzing impact reporting; and

³ http://ec.europa.eu/clima/policies/international/negotiations/paris_en

- 3) engaging with issuers at the “roadshow” stage, or when and if concerns arise.

Mirova believes an active manager should analyze the financial criteria of a Green Bond as well as the environmental, social, and governance (“ESG”) criteria before investing. Once invested, the manager should review the Green Bonds on a regular basis and track the proceeds with the bond issuers. This seeks to mitigate the chance of any misuse of proceeds, ensure that the Green Bonds are abiding by the Green Bond Principles and contribute to the integrity of the Green Bond Market.

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