



Designing the Model Framework Structure and Content for the issuance of Green Bonds in Armenia (Green Bond Framework)

D4 - Report on
recommendations of
integrating
framework with
existing governance
structures

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Designing the Model Framework Structure and Content for the issuance of Green Bonds in Armenia (Green Bond Framework) - D4 - Integrating framework with existing governance structures

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1. Background / introduction

The Government of Armenia through the Ministry of Environment (Designated National Authority) has requested support of Green Climate Fund (GCF) within the framework of “Readiness and Preparatory Support Programme” to implement comprehensive assessment of the constraints for further expansion of “green finance” practices, mapping of available instruments and to come up with comprehensive set of methodological, awareness raising and capacity building interventions. The main objective of the Readiness Project is to achieve paradigm shift in design and utilization of “green finance” instruments through incorporating into policies, operational modalities of national banks and non-banking financial institutions the climate-resilient approaches and guidelines, as well as regulatory simplification and introduction of policy incentives for designing respective on-lending facilities.

As part of the Readiness Project, the assignment “**Designing the Model Framework Structure and Content for the issuance of Green Bonds in Armenia (Green Bond Framework)**” is being carried out by the Consultant. The objective of the Assignment is to contribute towards advanced utilisation by Armenian banks and non-banking financial institutions of the opportunities to attract financing through issuance of the Green Bonds through design of the Model Framework Structure and Content for the issuance of Green Bonds in Armenia (Green Bond Framework) and assistance to 2 competitively selected entities¹.

In order to ensure full alignment with the green bond framework, certain procedures of the issuer have to be reviewed and potentially existing procedures within the organisation will need to be adjusted. This report describes the key elements that need to be included in processes when launching a credible green bond which would be aligned with the *International Capital Markets Association (ICMA) Green Bond principles*. These include aspects such as the use of proceeds, project selection and reporting. This report also provides recommendations to beneficiaries on how to improve internal processes in line with Green Bond processes and describes how to use a tool developed within this assignment for:

- Screening investments as to whether they are aligned with ICMA Green Bond Principle
- Calculating estimated greenhouse gas (GHG) emissions reductions.

¹ Could be either banks willing to finance/refinance its green portfolio or private sector entity seeking attraction of funds for implementation of the green project/s

2. Green bond framework integration - core components

ICMA's Green Bond Principles (GBP) provide guidance to ensure transparency and promote integrity in development of the green bond market. The GBP recommends a clear process and disclosure for issuers, which investors, banks, underwriters, arrangers, placement agents and others may use to understand the characteristics of any given green bond. The GBP guidelines stipulate key elements that must be covered while launching a credible green bond.

There are four core components for alignment with the ICMA's GBP:

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

The key elements that ensure heightened transparency are the following:

- (i) Green Bond Frameworks
- (ii) External Reviews (carried out by the SPOs)

These components are described in the chapters below. *Alignment with all the four core components of the GBP must be explained in the Green Bond Framework or in other legal documentation when a bond is issued.*

2.1. Use of Proceeds

First, a use-of-proceeds approach (and the subsequent verification) allows for transparency - clarity on use-of-proceeds tends to facilitate impact reporting that aligns real economy investments and outcomes with financing.

All designated eligible green projects should provide *clear environmental benefits*, which will be assessed and quantified by the issuer (or in the case of more complex projects, the project applicant submits extensive technical documentation from which the environmental and climate impacts are visible) and demonstrated to investors.

Moreover, in case some of the proceeds are intended for *refinancing of projects*, the issuer must provide an estimate of the share of financing vs. refinancing, and if possible, also clarify which investments or portfolios may be refinanced, and which would be the maximum look-back period for refinanced eligible green projects.

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The GBP explicitly recognise several broad categories of eligibility for Green Projects, which contribute to environmental objectives such as:

- climate change mitigation
- climate change adaptation
- natural resource conservation
- biodiversity conservation
- pollution prevention and control.

Green projects may include assets, investments and other related and supporting expenditures such as R&D that may relate to more than one category and/or environmental objective. Also, green projects definition may vary depending on sector and geography.

While the GBP's purpose is not to take a position on which green technologies, standards, claims and declarations are optimal for environmentally sustainable benefits, it is noteworthy that there are several current international and national initiatives to produce taxonomies and nomenclatures, as well as to provide mapping between them to ensure comparability. These may give further guidance to green bond issuers as to what may be considered green and eligible by investors. These taxonomies are currently at various stages of development - see for example the EU Taxonomy description in the box below. Issuers and other stakeholders can refer to examples in the sustainable finance section of ICMA's website.

Box: EU Taxonomy - an emerging issue for green investments

An emerging framework for green investments is the *EU Taxonomy*² which is expected to be linked to an upcoming important standard for green bonds. The EU Taxonomy is classification system, establishing a list of environmentally sustainable economic activities. It is to be used to provide companies, investors and policymakers with appropriate definitions for which economic activities can be considered environmentally sustainable. According to the EU Taxonomy, a project is classified green when it meets one or more of the following characteristics:

- Reduces greenhouse gas emissions or removes greenhouse gases from the atmosphere,
- Promotes climate resilience and/or adaptation,
- Promotes the sustainable use and protection of water and marine resources,
- Aids in the transition to a circular economy / improved waste management,
- Promotes pollution prevention and control, and
- Aids in the protection and restoration of biodiversity and ecosystems.

2.2. Management of Proceeds

The net proceeds of green bond should be credited to a sub-account, moved to a sub-portfolio or otherwise tracked by the bank in an appropriate manner. Also, green bond proceeds will need to be attested to by the issuer in a formal internal process linked to the issuer's lending and investment operations for eligible green projects.

² See https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance/eu-taxonomy-sustainable-activities_en

As long as the green bond is outstanding, the balance of the tracked net proceeds should be periodically adjusted to match allocations to eligible green projects made during that period. The issuer should notify investors of the intended types of temporary placements for the balance of the retained net proceeds.

The proceeds of green bonds can be managed in two ways: 1) per bond (bond-by-bond approach) or 2) on an aggregated basis for multiple green bonds (portfolio approach).

The GBP recommends that an issuer's management of proceeds is supplemented by the use of an external auditor, or SPO, to verify the internal tracking method and the allocation of funds from the green bond proceeds (see Key Recommendations section below).

2.3. Process for Project / Sub-Investment Evaluation and Selection

The process for evaluation of sub-investments to be included in the use of proceeds should be formally described within the Green Bond Framework. This process could involve, for example:

- Establishment of an investment committee to decide upon specific investments which have been appraised to ensure that they comply with the Green Bond Framework / Green Bond Standard. In principle, banks issuing green bonds should have an internal team responsible for technical appraisal, including eligibility and environmental and social safeguarding.
- Establishment of Standard Operating Procedures which can be followed for smaller investments - including by retail bankers.

The issuer of a green bond (bank) should clearly communicate to investors:

- The environmental sustainability objectives of the eligible green projects;
- The process by which the issuer determines how the projects fit within the eligible green projects categories and
- Complementary information on processes by which the issuer identifies and manages perceived social and environmental risks associated with the relevant project(s).

Issuers are also encouraged to:

- Position the information communicated above within the context of the issuer's overarching objectives, strategy, policy and/or processes relating to environmental sustainability.
- Provide information, if relevant, on the alignment of projects with official or market-based taxonomies, related eligibility criteria, including if applicable, exclusion criteria; and also disclose any green standards or certifications referenced in project selection.
- Have a process in place to identify mitigants to known material risks of negative social and/or environmental impacts from the relevant project(s). Such mitigants may include clear and relevant trade-off analysis undertaken and monitoring required where the issuer assesses the potential risks to be meaningful.

Most of the above should be communicated through the **green bond framework** and **impact (or also allocation) reporting**. There are many institutions and companies that provide independent

analysis, advice and guidance on the quality of various green solutions and environmental practices. In addition to Second-Party Opinion providers, which conduct verification, banks can rely on internal capacity or external institutions and companies.

2.4. Reporting

2.4.1. Allocation reporting

Issuers should keep readily updated information on the use of proceeds to be renewed each year until full allocation, and on a timely basis in case of material developments. The annual report should contain a list of the projects to which green bond proceeds have been allocated, as well as a brief description of the projects, the amounts allocated, and their expected impact. The Investment screening tool (described in later sections) for investment evaluation and selection can be used to for collection of this information.

In cases where the amount of detail available for presentation is limited by confidentiality requirements, competitive considerations, or a large number of underlying projects, the GBP recommend that information is presented in generic terms or on an aggregated portfolio basis (e.g. percentage allocated to certain project categories).

2.4.2. Impact reporting

The GBP suggest the use of qualitative or, where feasible, quantitative performance metrics. Also, the key underlying methodology or assumptions used for quantification shall be elaborated.

Issuers can decide whether they should report on the impact at the project or portfolio level, which can depend on the type and size of the project. Moreover, the issuers should refer to and adopt, where possible, the guidance and impact reporting templates provided in the [Harmonised Framework for Impact Reporting](#).

The use of a summary, which reflects the main characteristics of a Green Bond or a Green Bond programme, and illustrates its key features in alignment with the four core components of the GBP, may help inform market participants. To that end, a template can be found in the sustainable finance section of ICMA's website which once completed can be made available online for market information.

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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 Report³¹:

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

2.5. External Reviews

The international and European green bond market has developed with the help of an ecosystem of organisations known as external reviewers providing advisory services on the environmental benefits of underlying projects.

The issuer must appoint (an) external review provider(s) to assess through a pre-issuance external review the alignment of their Green Bond Framework with the four core components of the GBP (i.e. Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds and Reporting) as defined in Section 2 above.

Post issuance, it is recommended that an issuer's management of proceeds be supplemented by the use of an external auditor, or other third party, to verify the internal tracking and the allocation of funds from the Green Bond proceeds to eligible Green Projects. There are a variety of ways for issuers to obtain outside input to their Green Bond process and there are several types of reviews that can be provided to the market (e.g. Second-Party Opinion, Certification, Verification, Scoring/Rating). External reviews shall be made publicly available on issuer's website or through any other accessible communication channel as appropriate. Using the [template for external reviews](#) available in the sustainable finance section of ICMA's website is also recommended.

3. Investment screening tool for investment evaluation and selection

To support bank's staff in project selection, an investment screening tool based on the ICMA standard with a GHG calculator for various types of investments has been developed (elaborated in the following subsections). The outputs of this tool could also be reused for allocation reporting (if required) and impact reporting, by aggregation of different deal sheets.

This subsection aims to present the tool for screening and evaluating green investments that are nominated for participation in the green bond issuance system. According to the ICMA Green Bonds Principles, selected investments may belong to the following sectors:

- Renewable energy
- Energy efficiency
- Pollution prevention and control
- Sustainable management of living natural resources
- Terrestrial and aquatic biodiversity conservation
- Clean transportation
- Sustainable water management (including clean and/or drinking water)
- Climate adaptation and
- Eco-efficient products, production technologies and processes.

The developed tool consists of:

1. A general sheet with basic investment data
2. Sector project eligibility sheets intended for the evaluation of investments.

3.1. General sheet

The general sheet contains general information about the company applying for the investment and the investment itself, as follows:

- Name, address, telephone, email and description of the company's activities,
- Name and description of the investment,
- Investment value in EUR and AMD,
- Shares of financing by project owners, banks and other sources,
- Investment start and end dates.

The layout of the general sheet is shown below.

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GREEN BONDS QUESTIONNAIRE					
INVESTMENT SCREENING					
<i>This is a checklist to see if investments are in line with green bonds standards</i>					
GENERAL DATA					
Name of client/applicant (company):					
Address:					
Phone:					
Email:					
Description of activities of the company:					
INVESTMENT DATA					
Name of investment:					
Purpose of investment - environmental objectives: (select maximum three)					
Investment description:					
Currency of investment	AMD				
Value of investment:	EUR		AMD		-
Financing from project owner	EUR		AMD		-
Financing from bank	EUR		AMD		-
Financing from other sources:	EUR		AMD	-	Name of source
	EUR		AMD	-	Name of source

In addition, there are several groups of questions in the general sheet that need to be answered based on the drop-down lists in which the offered answers are ordered. Below are the following questions with offered answers:

- The investment belongs to the following eligible green project categories (ICMA) (select maximum three):
 - climate change mitigation
 - climate change adaptation
 - natural resource conservation
 - biodiversity conservation
 - pollution prevention and control

- The investment belongs to the following eligible areas (ICMA):

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- Energy production, transmission, appliances and products,
 - Energy transmission,
 - Appliances and products,
 - New buildings,
 - Refurbished buildings,
 - Energy storage,
 - District heating,
 - Smart grids,
 - Reduction of air emissions,
 - Greenhouse gas control,
 - Soil remediation,
 - Waste prevention,
 - Waste reduction,
 - Waste recycling,
 - Energy/ emission-efficient waste to energy,
 - Environmentally sustainable agriculture,
 - Environmentally sustainable animal husbandry,
 - Climate smart farm inputs such as biological crop protection or drip-irrigation,
 - Environmentally sustainable fishery and aquaculture,
 - Environmentally sustainable forestry, including afforestation or reforestation,
 - Preservation or restoration of natural landscapes,
 - Protection of coastal, marine and watershed environments,
 - Electric or hybrid transportation,
 - Public transportation,
 - Rail transportation,
 - Non-motorised transportation,
 - Multi-modal transportation,
 - Infrastructure for clean energy vehicles and reduction of harmful emission,
 - Sustainable infrastructure for clean and/or drinking water,
 - Wastewater treatment,
 - Sustainable urban drainage systems and river training and other forms of flooding mitigation,
 - Efforts to make infrastructure more resilient to impacts of climate change, as well as information support systems, such as climate observation and early warning systems,
 - The design and introduction of reusable, recyclable and refurbished materials, components and products,
 - Circular tools and services,
 - Certified eco-efficient products,
 - Buildings that meet regional, national or internationally recognised standards or certifications for environmental performance, and
 - None of the above areas;
- Form of financing:
 - New investment/financing green projects,
 - Refinancing green projects, and
 - Other forms (this is flexible as various inputs could be valid);

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- Nature of what is being financed:
 - Physical assets,
 - Financial green assets (mortgage loans)
 - Research and development,
 - Operational expenses
 - Leasing - real estate, and
 - Refinancing.

Below that is a list of types of investments/sectors. *By clicking on one of them, the user will enter directly into the sheet dedicated to the respective type of investment.* The types of investments are as follows:

- Industry - efficient processes and reduction of CO2 emissions,
- Energy efficiency in new buildings,
- Renewable energy sources - solar photovoltaic installations,
- Renewable energy sources - solar water heating installations,
- Renewable energy sources - bioenergy,
- Renewable energy sources - geothermal energy,
- Renewable energy sources - small hydro power plants,
- Renewable energy sources - wind,
- Transport - electric vehicles - passenger cars and commercial vehicles,
- Transport - electric buses,
- Industry - efficient processes and reduction of CO2 emissions,
- Water infrastructure,
- Sustainable agriculture,
- Forestry, and
- Waste - sustainable waste management.

Within the general sheet, the alignment with the Nationally Determined Contribution (NDC) objectives is also checked through the questions given below.

Alignment with Nationally Determined Contribution (NDC) objectives:

- Is this investment aligned with central objective of the Paris Agreement?
("Holding the increase in the global average temperature to well below 2°C above preindustrial level and pursuing efforts to limit the temperature increase to 1.5°C above preindustrial levels, recognizing that this would significantly reduce the risks and impacts of climate change")
- Is this investment aligned with national NDC objectives?
(40 % reduction from 1990 GHG emission levels by 2030)
- How is it aligned? (Through which of the following sector?)
- Please specify:

The end of the general sheet is reserved for the result of screening in which the answer to the question "Does this investment meet requirements for green bonds standards? YES/NO" arising from the analysis of individual investments through sector sheets is entered.

3.2. Sectoral sheets

In the sheets aimed at analysing the compliance of investment with the green bonds (GB) standards, the response to the question "Does this investment meet the requirement for green bonds" is obtained by answering several questions.

Objective	Question/criteria	Answer	
Reduction of energy consumption	Does this investment reduce energy consumption by more than 30% compared to the baseline?	Yes/No	Yes
Reduction of GHG emissions	Does this investment reduce GHG emissions by more than 30% in compared to the baseline?	Yes/No	Yes
Purpose of building	The investment / building is not intended for the extraction, storage, transport or production of fossil fuels?	Yes/No	Yes
Reduction of fossil fuels	Does this investment reduce the use of existing / installed (fossil) energy production capacity by more than	Yes/No	Yes
EE measures	Does this investment include efficient envelope?	Yes/No	Yes
	Does this investment include use of efficient heating or cooling system?	Yes/No	Yes
	Does this investment include use of efficient appliances/equipment?	Yes/No	Yes
	Does this investment include use of efficient lighting?	Yes/No	Yes
Use of renewable energy	Does this investment include use of renewable energy sources by more than 20% of the total energy consumption? (biomass, biofuel, geothermal energy, solar energy)	Yes/No	Yes
Potential for waste reduction	Does this investment recycle waste from demolition or construction?	Yes/No	Yes

The questions are divided into **green**, for which if the answer is "no" the investment is eliminated and questions marked in **yellow**, which are optional. **Only one answer "no" to green questions is sufficient to generate the answer "no" to the question of compliance with GB standards.** The answers to the yellow questions have no impact on this result. The yellow questions are there to provide additional information on the project and make it possible to assess how "green" they are - which could be potentially useful in the case of competing projects for limited resources.

The drop-down list allows you to select the "yes" or "no" answer for each question. If the answer to all green questions is "yes", the answer to the question of compliance with GB standards becomes "yes" automatically.

Specific measurable ICMA indicators were used wherever they exist. For types of investments where the ICMA indicators are only general in nature, criteria have been developed in line with ICMA standards, i.e. they are not the opposite of them.

For most potential mitigation investments, a relatively simple model for calculating GHG emissions has been developed so that a bank / investor can estimate the expected impact of investments. Depending on sectors/types of investment, mandatory criteria mainly relate to GHG

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emissions, reduction of fossil fuel use, sustainability, impact on climate change and the environment. Some criteria are very specific, and some are only descriptive.

In principle, GHG emissions are calculated by comparing the pre-investment situation with the investment situation. Fields that depend on investment data are marked in **blue** and are entered by the bank. The **orange** colour marked fields represent the assumptions given by the consulting team, but they can be changed if a bank has access to different data.

GHG calculations are developed for:

- renewable sources
- buildings and
- transport sector

The calculation of GHG emissions takes into account the total emission savings over the entire life cycle of the investment.

There is potential for the development of tools for additional sectors, with or without GHG emissions calculations, depending on the bank's policies and intentions. However, most of these types of investments will involve bespoke analysis and calculations (for example for investments in industrial processes).

4. Recommendations for integration of green bond framework in internal processes

For financial institutions in Armenia interested in issuing a Green Bond, the following specific recommendations for processes are relevant.

1. COMMUNICATE WHAT ARE ELIGIBLE GREEN PROJECTS TO THE INVESTORS

In order to avoid later harmonization of projects with "green criteria", the bank should communicate green projects eligibility to the investors and potentially with clients early on.

- For example, in the event that the bank wants to increase the demand for a certain type of projects, it can launch campaigns that target potential circle of clients (or inform them directly).
- The bank should make a list of acceptable green projects and corresponding criteria public, so that clients can use it as an input before preparing the project. Also, the bank may distribute project-related questionnaires or checklists to help clients with self-assessments.
- Bank's staff, across all departments shall be informed about green projects, especially the staff working directly with clients.

2. BUILD TECHNICAL APPRAISAL TEAM (FOR LARGE / COMPLEX PROJECTS)

Given that the evaluation of projects, as well as reporting, will require certain level of technical knowledge, it is expected that the bank has its own internal team of engineers or sector experts. However, in addition to this team, the bank can request (procure) help from external experts/specialists for e.g., complex GHG calculations, field visits and other checks.

3. PREPARE CHECK-LISTS AND REPORTING FORMS (FOR SMALLER INVESTMENTS)

In order to simplify the work and reduce the level of effort required for interaction with clients, the bank should prepare checklists and forms for the assessment of eligibility, as well as for reporting, which potential clients or retail bankers can first fill out themselves. Also, the bank should do training for internal staff on how to use these checklists and forms. If possible, one person should be central in providing support to other staff and investors in case of ambiguities.

4. REINFORCE / BUILD OFF OF EXISTING ENVIRONMENTAL AND SOCIAL SAFEGUARDING SYSTEM

In general, Green Bond frameworks should build off of already adopted environmental and social governance (ESG) policies. Typically this will mean that the institution has a separate team that has the knowledge necessary to review projects for relevant issues. However, given that the issuance of green bonds requires the application of slightly more stringent Environment and Social Safeguard (ESS) criteria, it is possible that the existing ESG system will have to be reinforced or upgraded (e.g. new environmental and social criteria should be added to the list of activities excluded from potential investment). The bank can refer to already implemented technical assistance projects, study and apply available materials, or request external assistance in establishing appropriate criteria and a qualified team.

5. KEEP EVIDENCE

In principle, the client is expected to provide all information / documentation that is required for a full project assessment. Technical documentation (excerpts) or sheets from the investment review tool must be stored by the bank and kept at least for the duration of the bond repayment.

6. EMBED GREEN PROJECT CRITERIA AS OBLIGATION WITHIN THE LOAN CONTRACT

In order to ensure that clients comply with the initially promised "green criteria" during the construction or operation phase (and maybe the entire lifecycle) of green projects, it is highly recommended to incorporate provisions (criteria) of green projects into the contract (in order to oblige the client to implement the project as stipulated in the contract). An annex containing prescribed elements can be added to the loan agreement.

7. FOLLOW UPDATES ON GB STANDARDS AND NATIONAL REGULATIONS

Though the ICMA standards are well-established, green bond standards in general are still being shaped. And in general, green project standards and criteria are considered a process that will continue to evolve. Furthermore, the green bond framework eligibility criteria could be adapted to local regulations, demand, and practices. Therefore, a green bond issuer must always be aware of developments and changes in green criteria by the creators of green bond standards, as well as sectoral / legal changes within their country which may be relevant for the investments.