GREEN BONDS
FINANCING A SUSTAINABLE FUTURE

Aaron Franklin, Paul Davies, Michael Green, Francesco Lione, and Lee Irvine of Latham & Watkins discuss the growth of green bonds and their key characteristics.

Green bonds are debt instruments with similar characteristics to traditional bonds, which issuers use to implement and finance their environmental, social and governance (ESG) strategies. Over the past decade, a diverse array of green bonds has been issued but the predominant type of green bond is where the issuer tells the market that it is going to use the proceeds of the bond to finance projects meeting certain disclosed environmental sustainability criteria. Investors interpret the green designation as suggesting that the bond , and possibly the issuer, might meet the investors' environmental sustainability investment criteria.

This article discusses:

- The growth in the market for green bonds.
- The key components of green bonds.
- Risks relating to the marketing of green bonds and to the issuer's obligations after the issue.
- Practice points
- Future trends to watch

GROWTH AND MOMENTUM

Green bond issues have increased rapidly since they were first issued in 2007 and they are estimated to continue to grow in 2017. In 2007, $0.8 billion of green bonds were issued while, in 2016, that figure had grown to between $81 billion and $93 billion. As of 1 March 2017, of the $202.6 billion raised so far through issues of green bonds, $188.5 billion remained outstanding. An important subset of this growth has come from issuers based in China, which issued $30.5 billion of green bonds in 2016; approximately one-third of total issues for the year.

The structural force driving growth in this market is investor demand for assets perceived as environmentally beneficial. In some cases, this demand is based on an asset manager having a mandate to focus on environmental sustainability in its own right. In other cases, the demand is based on an investor seeking assets that are less exposed to risks associated with changes in the economy related to reduced fossil fuel use. Businesses are increasingly reducing the prominence of fossil-fuel-intensive activities in their strategic plans and investing instead in more environmentally-friendly substitutes. This shift signals to some investors that, aside from their preference for environmental sustainability, there is a strong risk avoidance argument for investing in green bonds.

The demand for environmentally beneficial assets can be seen through the rapid growth in the green bond market, with anecdotal evidence of perpetual undersupply and

oversubscription of green bonds. It is also illustrated by the fact that investors with over $45 trillion in assets under management have publicly committed to environmentally friendly finance; for example, by participating in the United Nations' Principles for Responsible Investment, joining the Paris Green Bonds Statement or becoming a member of the Institutional Investors Group on Climate Change. Investors are not only showing a willingness to buy green bonds, they are also shaping the product by participating in the market-led standards known as the Green Bond Principles (*see box "Green Bond Principles"*).

Investor demand creates a powerful incentive for potential issuers to create a supply of green bonds. This incentive is not necessarily financial: in general, green bonds have not had a lower interest rate than their non-green comparators. Rather, the main advantage of a green bond is furthering an issuer's sustainability strategy. It does this by signalling to stakeholders, not just investors, the issuer's willingness to sacrifice flexibility and undertake additional costs to further sustainability goals. Although difficult to quantify, market participants frequently cite this advantage.

An additional benefit of issuing a green bond can be attracting investor interest. Asset managers increasingly operate with environmental-sustainability criteria or priorities and the green label communicates that the bond may be a potential fit or worth a second look. The involvement of green-constrained investors in an order book may not change the coupon but, at least in certain cases, has enabled a larger offering size. The green label can also communicate a strong overarching approach to ESG issues, which can provide assurance to investors reticent to invest in a challenging jurisdiction.

Growth in the green bond market has been further accelerated by the rapid development of market infrastructure that is intended to standardise and simplify the new product (*see box "Market infrastructure development"*).

DEFINING GREEN BONDS

Green bonds are debt instruments with similar characteristics to traditional bonds, which issuers use to implement, emphasise and finance their ESG strategies. This definition is necessarily broad and imprecise because what the market and regulators recognise as a green bond includes a range of different securities. Green bonds can be analysed as debt instruments with three necessary components:

- A green label
- An underlying environmentally beneficial activity.
- A connection or relationship between the bond and the underlying environmentally beneficial activity.

Green label

The first component of all green bonds is that, as a matter of definition, they are labelled as green by the issuer. By applying the green label, the issuer distinguishes its bond as green and allows investors to more easily identify the bond as meeting investment criteria related to environmental sustainability.

Underlying green activities

Green bonds universally relate to an underlying activity that purports to be environmentally beneficial (*see box "Environmentally beneficial activities"*). In practice, the use of proceeds for approximately half of all green bond issues relate to renewable energy or energy efficiency, although this trend decreased significantly in 2016, with uses of proceeds related to sustainability in water usage recording the most notable increase.

While most market participants are able to agree at a high level on categories of activity that are environmentally beneficial, questions often arise at a more detailed level. Examples include when one objective, such as carbon dioxide emissions reduction, trades off against another objective, such as biodiversity conservation, or when there are disputes about whether a technology, such as clean coal or nuclear energy, qualifies. A certain degree of uncertainty with respect to the boundary around what activities qualify as environmentally beneficial may be inevitable, as the priorities of stakeholders differ depending on geography, risk exposure and ideology. This uncertainty prompts the question of who decides what is permitted to be labelled as a green bond. There is no universal answer and it is helpful to think of two competing regimes: market-driven regulation and central regulation.

Market-driven regulation. In most of the world, except China, the market decides what is permitted to be labelled as a green bond. This means that an issuer is free to label any bond as green if investors will agree with that label. Market stakeholders such

Green Bond Principles

The Green Bond Principles were created in 2014 by a coalition of investment banks, issuers and investors and have been updated annually, most recently in June 2017, based on feedback from stakeholders designated as members or observers (*www.icmagroup.org/Regulatory-Policy-and-Market-Practice/green-bonds/green-bond-principles/*). Although the Green Bond Principles are the predominant voluntary green bond standard, they provide only an indicative and non-exhaustive list of activities expected to be supported by the green bond market.

The Green Bond Principles provide more specific guidance through four core components that govern certain procedural aspects of a green bond issue. These core components recommend transparency with regard to how the bond's proceeds will be managed, used and reported, including with respect to any environmental benefits achieved. The four key components encourage the issuer to:

- Disclose in what type of projects the green bond proceeds will be invested.
- Describe the process to determine what projects will receive financing.
- Describe how proceeds will be managed in the interim period before they are invested or during the period after they are repaid but before they are reinvested.
- Report how the proceeds were used as well as, if possible, outcomes related to environmental key performance indicators of the issuer's selection.

as non-governmental organisations and environmental consultants act as de facto gatekeepers, and may punish dubious green bonds by claiming that an issuer is engaging in "green washing" or by excluding an issue from green bond databases.

The market-driven approach allows for flexibility but permits a degree of uncertainty around what qualifies as a green bond. This uncertainty is, in many cases, mitigated through voluntary measures, such as by complying with the Green Bond Principles or obtaining an external review. External reviews are typically performed by third-party consultants. The most popular form of external review is the second opinion, in which a consultant provides an opinion for the benefit of investors in support of the green bond (*see box "Second opinions"*). The substance of second opinions varies depending on the issue and the particular third-party consultant involved, ranging from assessment of compliance with the Green Bond Principles's process guidelines, to the issuer's overall ESG compliance, to compliance of the issuer's activities with the consultant's in-house criteria for what constitutes a green bond.

Another form of external review consists of third-party verification against a defined standard, which can take place either concurrently with or subsequent to an issue. Specialised ratings are also available, where the issuer's green bond and underlying activities can be assigned a credit-like rating.

Central regulation. Some central authorities publish binding rules to identify what qualifies as a green bond. For example, several different organisations in China have issued binding rules. The regulation of green bonds in China is divided primarily on the basis of the type of issuer, with the People's Bank of China regulating green bonds issued by financial entities, the National Development and Reform Commission (NDRC) regulating bonds issued by other companies that do not have listed equity, and the China Securities Regulatory Commission regulating bonds issued by non-financial corporate issuers with listed equity. In addition, both the Shanghai and Shenzhen stock exchanges have issued pilot guidelines applying to bonds issued on their exchanges.

In certain cases, Chinese green bond guidelines have been more flexible compared to typically-acceptable green bonds in Europe.

Market infrastructure development

A number of developments in the market infrastructure for green bonds have increased growth in the green bond market, including the following:

- In 2014, a coalition of issuers, investors, and underwriters created voluntary process guidelines known as the Green Bond Principles, which have heavily influenced the market's development.
- Investment funds and exchange-traded funds that are focused on green bonds and environmental investing have proliferated.
- Index providers have launched indices to track the green bond market, such as the S&P Green Bond Index and Barclays MSCI Green Bond Index.
- Several stock exchanges have launched dedicated segments for listing green bonds, including the London Stock Exchange, Luxembourg Stock Exchange and Oslo Børs.
- Moody's and Standard & Poor's have announced green ratings.
- Non-governmental organisations, such as the Climate Bond Initiative, have developed certification standards.

This flexibility applies to what activities are sufficiently environmentally beneficial. For example, certain guidelines accept clean coal or fossil fuel retrofittings, which would not generally qualify in the European market. This flexibility also applies to the connection between the bond and the underlying activity. For example, certain guidelines permit a bond to be labelled green if greater than 50% of proceeds are used for eligible purposes, whereas European standards would require a much higher threshold.

The connection

The third component of all green bonds is the connection or relationship between the bond and the underlying green activity. Bonds are often characterised as green where the proceeds are used to finance green projects. In reality, the manner in which the green bond relates to the activity is diverse and often the same green bond will operate in multiple ways. To understand how green bonds operate, it is helpful to consider three categories: future use, immediate use and credit support. These categories are indicative and often overlap, but facilitate analysis of the different types of green bonds.

Future use. The original and predominant green bond structure is future use. Here, the green bond issuer, which is typically a bank, states in the offering disclosure for the bond that it commits to lending the proceeds from the bond issue to third parties that will use the borrowed funds to finance projects that meet the green bond issuer's eligibility criteria. These projects are typically referred to as eligible green projects. The green bond issuer typically selects which borrowers and projects to fund only after the green bond has been issued and investors will only learn after the fact, if at all, how their funds were eventually used.

The meaning of eligible green projects will be detailed in the disclosure, and often includes financing and refinancing ongoing or new operations, or acquiring assets. Typically, issuers of future-use green bonds state in their offering disclosure that they will periodically report with regard to how much of the proceeds have been loaned to eligible green projects, the characteristics of those projects and, in some cases, the environmental outcomes associated with those projects.

The future-use structure was used for the first green bond, issued by the International Finance Corporation in 2007, and remains the dominant structure. The most common type of issuer is a financial institution; often supra-national or quasi-governmental development banks. However, municipalities, utilities companies and large corporates, among others, have also issued future-use green bonds. In these cases, rather than lending

green bond proceeds on to third parties, the green bond issuer will allocate the proceeds to internally selected eligible green projects.

Future-use green bond structures allow investors to invest in an asset that they can characterise as green from the moment of first buying the bond, while transferring to the issuer the burden of reviewing potential projects, administering loans and monitoring ongoing creditworthiness and compliance. The issuer is often a bank and well-equipped to perform these functions. Investors are insulated from direct exposure to the credit risk of the ultimate borrowers and rely on the issuer's balance sheet. The ultimate borrowers are able to borrow from bank lenders without the burden of undertaking a securities issue, which involves extensive legal review and typically requires a sufficiently large sum that may disqualify many potential borrowers.

The Green Bond Principles and the practice of obtaining second opinions help facilitate the future-use structure. The Green Bond Principles' core components are tailored to improving the reliability of an issuer's promise to use proceeds to support unidentified environmentally-beneficial projects, covering such matters as providing adequate disclosure on what types of projects will be eligible for funding, how projects will be selected, the management of the proceeds of the bond before lending those proceeds to the ultimate borrowers and the future reporting on how the proceeds were used. Similarly, the practice of obtaining external review in the form of a second opinion allows the external reviewer to assess the issuer's project eligibility criteria for compliance with a green bond framework.

Most future-use green bonds have been low-risk, low-interest rate instruments that are typically rated as investment grade. This results both from the fact that most future-use green bond issuers are investment-grade rated financial institutions and from the risk preference of many investors that are focused on ESG compliance.

Immediate use. Immediate-use green bonds are where the particular use of proceeds is disclosed to investors at the time of issue. Investors in immediate-use green bonds can assess for suitability the particular project in question, rather than, in the case of future-use green bonds, the suitability of the issue's project eligibility criteria. For example, a corporate issuer would issue an immediate-use green bond by explaining to investors that the use of the proceeds would be to finance the construction of a specific new solar power electricity generation facility or to refinance debt facilities related to ongoing recycling operations. Immediate-use green bonds have also been issued to acquire assets and to finance bolt-on and leveraged acquisitions.

Immediate-use green bonds require and allow the investors to assess both the environmental appropriateness of the underlying activity and the creditworthiness of the issuer. Accordingly, green bonds in this category rely to a lesser extent on green bond infrastructure, such as the Green Bond Principles and external review.

The credit profile of immediate-use green bonds is more varied than with respect to future-use green bonds, and includes most sub-investment grade green bonds. One potential explanation for the increased diversity in credit profile for this category is that it includes bonds issued for single projects or for single end users, which can lead to smaller issue sizes by smaller issuers.

Credit support. Credit support green bonds are characterised by the business activities or assets that provide the credit support for the bond, such as the cash flows to support interest payments, rather than how the bond's proceeds will be used. Most prominently, this category would include "pure play" green bonds, which are issued by companies that are predominantly involved in environmentally-beneficial activities. For example, this category of green bond would include a bond issued by a renewable power generation corporation where the use of proceeds are "general corporate purposes." This category of green bond would also include securitisations of cash flows from environmentally-beneficial contracts, such as leases of hybrid automobiles.

As with immediate-use green bonds, credit support green bonds require and allow investors to assess both the environmental appropriateness of the underlying activity and the creditworthiness of the issuer.

Environmentally beneficial activities

At a high level, there is little dispute that activities related to the following would qualify as environmentally beneficial:

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

RISKS AND CONCERNS

The advantages conveyed by green bonds may also carry additional legal and reputational risks relating to the process of marketing and selling the green bond and to the issuer's obligations after the issue.

Marketing and sale

Certain risks are inherent to marketing and selling any bond, green or otherwise, such as the risk that investors or regulators will claim that the issuer's disclosure related to the bond was misleading. Different risks apply depending on the relevant jurisdictions and legal regimes, and whether the bond

is subject to regulatory approval. When marketing and selling a green bond, the issuer will somehow communicate that the green label applies to that bond, which opens the issuer to arguments that the issuer's green label was misleading in several ways.

Nature of the underlying green activities. The green label may be subject to challenge on the grounds that it implies that certain or all of the associated underlying green activities are environmentally beneficial. The boundaries for what qualifies as green are often unclear and it is not hard to imagine disputes about whether a particular project would be environmentally beneficial. For example, a dispute could arise regarding whether a water desalinisation project that relied on fossil fuel-derived electricity had a net benefit to the environment. This issue may be exacerbated by regional differences; for example, clean coal operations do not, in general, qualify as a green activity in the European green bond market whereas clean coal qualifies as a pollution prevention measure under certain standards in China. This issue may also be complicated for future-use green bonds, where the actual use of the bond is not determined until after the green bond has been issued.

Relationship-based challenges. The green label may be subject to challenge if the bond does not sufficiently relate to the underlying green activity. For example, the green label could be challenged as misleading unless applied to a bond where the proceeds are used for particular green projects, thereby excluding the credit support green bond (including pure play green bonds). Although credit support green bonds have been accepted by the green bond market in the past, the Green Bond Principles call these bonds into question to the extent that they do not adhere to certain procedural norms that are more appropriate for immediate-use and future-use green bonds.

Another example of a relationship-based challenge is that the green label is misleading unless the bond's proceeds finance new or additional green projects. This argument is undercut by the sweep of market practice and, in particular, by the express reference to "refinancings" in the Green Bond Principles. Nevertheless, this additionality challenge retains currency with a certain segment of those who monitor and comment on developments in the green bond market.

Second opinions

Issuers frequently support the characterisation of their bond as green by commissioning a second opinion by an environmental consultant. The content of these opinions varies depending on the format of the second opinion provider. In most cases, these opinions will assess the procedural aspects of the green bond such as whether the issuer has adequately disclosed the use of proceeds, whether the issuer has explained how it will select projects and how the issuer expects to report.

Second opinions often assess the underlying performance of an issuer on environmental, social and governance matters, determining whether the company's history and internal controls are consistent with the green label. In certain other cases, the opinion will address the environmental sustainability of the underlying green activity. Certain second opinion providers develop proprietary ratings such as "shades of green" or "scales of assessment."

Second opinions are typically treated like reports published by credit rating agencies. Second opinions are typically:

- Neither included nor incorporated by reference in the offering memorandum, although it is not uncommon to reference that a second opinion is provided.
- Provided for the benefit of the public, in contrast to auditor comfort letters, which are addressed to the underwriters.
- Made available to the public through the issuer's website.
- Subject to review before publication to ensure that factual descriptions of the issuer's green bond framework and ESG performance are consistent with the issuer's offering disclosure.

The Green Bond Principles recommend that issuers use some form of external review but do not include this as a core component. A second opinion is, however, required by certain of the green bond-specific stock exchange listing segments, such as the Luxembourg Green Exchange.

A further example of a relationship-based challenge is that the green label is misleading in the context of a future-use or immediate-use green bond unless applied to a bond where 100% of the proceeds are to be deployed for green purposes. Many European green bond issues allot a certain portion of the proceeds, typically between 1% and 5%, to cover transaction expenses. Certain green bonds will allot a specific portion of the proceeds to "cash on the balance sheet" or "general corporate purposes"; again, typically not more than 5%. According to NDRC guidelines applicable to certain Chinese issuers, up to 50% of the proceeds may be used for non-green purposes.

Issuer disqualification. The green label may be subject to challenge on the grounds that the issuer of the green bond disqualifies the issue. The theory of this challenge would be that issuing a green bond implies that the issuer's business is operated in an environmentally friendly manner. This implication could be considered misleading where an issuer's business operations are antithetical to environmental sustainability or where the issuer has a history of causing environmental damage or non-compliance with relevant norms. The widespread attention to a spring 2017 issue of a green bond by an oil and gas company demonstrated this type of challenge. The proceeds of this issue were to be invested in, among other things, energy efficiency projects, and a leading green bond non-governmental organisation and database declined to include this in its listing. Nevertheless, this issue was bought by investors in large numbers, whether for its green credentials or for its credit profile. Despite the attention garnered by this issue, many market participants continue to express support for the idea that any company should be able to issue a green bond if it plans to use

the proceeds in an environmentally beneficial way. Relatedly, guidelines applicable to certain Chinese issuers suggest that issuers involved in high-pollution, high-energy consumption industries are not eligible to issue a green bond regardless of the bond's use of proceeds.

Obligations after the issue

Green bonds differ in three ways from traditional bonds with respect to the issuer's obligations after issue. An issuer's failure to adapt to these different obligations could impose additional risks.

Firstly, for future-use green bonds the issuer will need to consider carefully whether the actual allocation of the bond's proceeds conforms to the expected use of proceeds as disclosed at the time of issue. For example, an issuer that sold its green bond based on the promise of using the proceeds to finance water conservation projects to be selected in the future may expose itself to legal and reputational risks if it then finances biodiversity projects. To make matters more difficult, many issuers include in their eligibility criteria concepts that are open to interpretation such as "sustainability" and "environmentally friendly."

Secondly, green bonds often involve reporting on the green aspects of the bond, beyond the normal financial reporting involved in a traditional bond. For future-use and immediate-use green bonds, the issuer will typically promise to provide certain information about, among other things, how the proceeds of the bond are used and what environmental results are the outcome of this use. In substantially all green bonds to date, these promises were not legally binding, meaning that they were included only in the disclosure and not in the bond contracts.

Thirdly, mandatory securities law imposes on most bond issuers (both traditional and green) certain fair disclosure obligations, which relate to promptly disclosing material developments to the market as a whole and avoiding situations whereby certain investors have access to important information not available to the market as a whole; often referred to as inside information or material non-public information. The point of these obligations is to prevent those with material information from profiting at the expense of those without this information. To meet these obligations, issuers need to assess the materiality of information in their possession and whether public disclosures are required. For example, issuers may post a press release if a major counterparty declares bankruptcy because that information will affect the issuer's future revenue. For green bond issuers to comply with these obligations, they may need to take into account environmental outcomes and risks in determining what information is material or potentially inside information.

PRACTICE POINTS

The green label can be applied to different types of bond, such as government, corporate, mortgage and municipal bonds. These different types of bonds have their own set of practices and norms that do not necessarily change due to the green label. Even for the aspects unique to the green bond, practice varies and remains in flux.

Labelling the bond as green

Issuers will often state in the bond offering disclosure that they consider the bond to be a green bond. They can do this by including "green" in the title of the bond. For example, instead of a new bond being referred to as "Senior Notes due 202X", the new bond would be referred to as "Senior Green Notes due 202X." They may also, or alternatively, include a statement to the same effect, such as: "the Notes are being issued as green bonds in accordance with our green bond framework." Multilateral investment banks and established issuers tend to adopt this approach.

Other issuers have relied on a less direct statement or no statement at all. In some instances, issuers will include disclosure with respect to a second opinion provider characterising the bond as green. In other instances, the issuer will rely on the implication of a use of proceeds related to financing eligible green projects. Corporates or less established issuers tend to adopt this approach.

In either case, the green label may be bolstered by reference to the green nature of the bond in other offering communications, such as press releases, Bloomberg announcements and investor presentations used for the roadshow. Green bonds then receive additional publicity from blogs and green bond databases that publicise new issues.

Key green disclosures

In the past three years, many green bonds have been issued in compliance with the Green Bond Principles, which provide voluntary guidance on the process and disclosure involved in issuing a green bond (*see box "Green Bond Principles"*). Another element of the disclosure included in many recent green bonds involves disclosing as a risk factor that the bond will not meet the environmental investment criteria of every investor or will cease to be considered a green bond in the future.

Green promises

Issuers typically include all relevant green promises, such as on the use of proceeds and future reporting, as disclosure in the bond offering document. With few exceptions, these promises are not included as elements of definitive contracts. In other words, failure to fulfil a green promise does not generally trigger an event of default and the right to demand immediate repayment of the bond.

Certain bonds, however, include as a matter of course a covenant that applies generally but has the effect of creating an enforceable green promise: the covenant to use the proceeds as specified in the bond disclosure. This covenant may appear in underwriting or purchase agreements between the issuer and its investment banks, but is not often a covenant enforceable by the noteholder for European bonds. In contrast, certain Asian bonds, including sub-investment grade bonds, include this as a right of the noteholders.

Environmental due diligence

The general bond process includes due diligence, which is meant to uncover any material concerns that should be disclosed to potential investors so as to minimise securities law risks. The due diligence process involves investigations of the issuer's affairs by the underwriters and legal counsel, usually through a series of question and answer sessions with company management, a review of key company documents, and discussions with accountants and auditors. This process is weighted towards uncovering matters that could significantly affect the topics that an investor is likely to find material, such as the financial results or condition of the issuer.

The due diligence process generally includes the review of an issuer's compliance with relevant regulations, including environmental regulations, and any liabilities for environmental remediation, but the emphasis is generally on how these matters could affect the bottom line. Due diligence on ESG

matters for the purpose of ensuring adequate disclosure is clearly more important for green bonds than for non-green bonds.

There needs to be a comprehensive approach to addressing ESG issues and this will require the legal and technical environmental teams to work together closely. The increasing concerns around ESG issues also mean that there is now more focus on supply chain risks and climate change risks. More particularly, depending on the industry sector of the issuer and the information made available, the scope of ESG diligence will need to be tailored to the specific risks. For example, for green bond issuers with a portfolio of renewable energy assets, particular attention will be required to consider any government incentives that are provided to renewable energy producers, and the general stability and predictability of renewable energy regulations in the relevant countries.

Therefore, when undertaking ESG due diligence, it is essential that the necessary questions are raised and that the green bond issuer makes available the necessary resources (whether internal expertise or external advisors) to provide accurate and complete answers. This process will be the key opportunity to verify and obtain comfort that the statements in the offering disclosure are accurate and address the material ESG risks facing the issuer.

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FUTURE TRENDS TO WATCH

Green bonds have continued to evolve through the recent period of rapid growth in new issues. One evolution is the expansion of "sustainability" bonds, which look to broader sustainability criteria, such as labour and social effects, more directly, rather than exclusively to traditional environmental or climate change concerns. The "sustainability" or "social" bond market is still in its infancy, but the frameworks established for green bonds, in particular future-use green bonds, is being applied directly to this growing area. Demonstrating this trend, the same group that developed the Green Bond Principles are tailoring analogous Social Bond Principles, [that were publically announced in June 2017].

A trend yet to reach maturity is the overlap between green bonds and another area of strong growth in the past decade: Islamic finance, such as sukuk (*see Focus "Islamic finance: rising above the downturn?", www.practicallaw.com/0-384-7915*). Standard and Poor's has estimated that approximately $77.1 billion of sukuk were issued by corporations, sovereign entities and government related entities in 2016, amounting to more than double the $33.6 billion raised in 2006. Commentators have frequently noted the overlap between green bonds and Islamic finance in that both entail explicit requirements around non-financial investment criteria. By incorporating environmental requirements into a traditional sukuk, issuers may be able to help to facilitate broader participation of the sukuk market by conventional investors, who are already showing an increasing appetite for Islamic financial products, and allow Islamic investors access to a wider range of Sharia-compliant investment products.

A number of governments and affiliated bodies have, however, started recognising the potential benefits of a green sukuk and are, in some cases, working to ensure a stable and supportive framework for issuers and investors and, in other cases, considering issuances themselves. In January 2014, the Securities Commission Malaysia published guidelines for the issuance of sustainable and responsible investment sukuk as part of a highly anticipated expansion of the country's existing sukuk framework (*www.sc.com.my/wp-content/uploads/eng/html/resources/guidelines/bondmkt/sukukGuidelines_08012014.pdf*). These guidelines are intended to allow Islamic institutions to capitalise on the growing demand for social and environmental-focused investments. In the Gulf Cooperation Council region, the Dubai Supreme Council of Energy has announced a partnership with the World Bank to develop a green investment strategy, which could incorporate sukuk.

A green sukuk could be used for many of the same purposes as a green bond and, from a structuring perspective, the structuring of a green sukuk would not be different from the structuring of a conventional sukuk, being largely dependent on the assets that are available to support the sukuk and the projects to be financed.

Paul Davies and Francesco Lione are partners, Michael Green and Lee Irvine are counsel, and Aaron Franklin is an associate, at Latham & Watkins.