Meek Principles for a Tough Climate

Why the Carbon and Climate Principles will not stop the melting of the ice

BANKTrack

A tough climate

In December 2009, the world community will convene in Copenhagen, Denmark to try to hammer out a new post-Kyoto global framework to combat climate change.[1] The UN Climate Summit will take place in a context of growing public concern and a near universal scientific consensus on the severity of the threat posed by anthropogenic climate change. Contrary to earlier summits, few at the table will question the need to act swiftly and boldly as a world community, so as to avoid catastrophic climate change from unfolding.

Whatever the outcome of the summit, much of the wrestling between the parties will focus on where the massive funds for mitigation and adaptation measures are to be found, and how they are to be allocated. Public funds will not be sufficient to cover the astronomical bill alone, so the private finance sector will be expected to play a key role in mobilizing necessary resources. The questionable assumption here is that banks and private investors are part of the solution, rather than the problem.

Time for Principles

In response to this growing expectation about the role of private finance in combating climate change, two groups of prominent financial institutions last year adopted two different sets of voluntary frameworks for managing the climate impact of their operations.

In February 2008, a group of US banks released the 'Carbon Principles' a common procedural approach for assessing carbon risks faced by companies building new coal-fired electric power plants in the United States.[2] The principles were designed to address the risks associated with regulatory uncertainty, and were also a direct response to growing public concern over the proliferation of plans for more than one hundred new coal-fired power plants that, if built, will lock the United States into a carbon-intensive, coal-dependent future with millions of tons of new and additional CO2 emissions every year.

Then in December, a second group of international banks and insurance companies, under the auspices of the Climate Group, released the 'Climate Principles'.[3] Broader in scope and ambition than the Carbon Principles, the Climate Principles seek to 'establish best-practice standards for financial institutions to address the implications of climate change across their entire range of advisory, lending, investing, and insurance services'. While the Climate Principles were endorsed by only three leading international banks and two insurance companies,[4] its proponents hope the Principles become the leading climate policy standard for the finance sector.

[1] http://en.cop15.dk/

[2] Citi, JPMorgan Chase and Merrill Lynch, Later joined by Bank of America, Credit Suisse and Wells Fargo, see www.carbonprinciples.org

[3] The climate Group is a UK based initiative bringing governments and business together to 'set the world economy on the path to a low-carbon, prosperous future'. http://www.theclimategroup.org/about/corporate_leadership/climate_principles

[4] Credit Agricole, HSBC, Munich Re, Standard Chartered, Swiss Re

A meek response

BankTrack welcomes the fact that the signatories to the Carbon Principles and the Climate Principles acknowledge that they must do their part in combating climate change. Given the potential climate impacts -- both positive and negative -- of the finance sector's role in mobilizing and allocating capital and investment, there is a compelling need for a robust sector-wide climate safeguard standard or code of conduct for the banking sector.

However, rather than a bold new initiative, both the Climate Principles and the Carbon Principles are deeply disappointing. While they both contain elements that are useful, neither in its present form addresses climate change risks with the rigor, urgency or ambition that the challenge at hand plainly requires. To appropriately respond to this challenge, financial institutions must adopt strong climate protection performance policies and strategic objectives and climate management tools and oversight mechanisms that are as comprehensive and rigorous as those that they already use to ensure compliance with other corporate policies and strategic objectives, such as their credit rating and risk management frameworks or their human resources policies.

Both the Climate Principles and the Carbon Principles fall short of this basic test. Too often, they contain vague or aspirational procedural provisions where substantive, outcome-oriented standards are required. The Carbon Principles are not a performance standard; they are primarily a set of due diligence procedures. More troubling, the existence of the Carbon Principles has not stopped signatory banks from financing new coal plants. The Climate Principles aspire to establish climate performance standards for their financing, but have not yet established a formal process to do so. As a result, both principles do not provide any performance benchmarks for evaluating whether signatories –or their clients- are actually changing their business practices and portfolio decisions to reduce their climate impacts.

In many cases, these frameworks also do not address the risk that their services will actually exacerbate the climate crisis. Rather, they focus on the risks posed to the banks by potential climate change and the uncertainty around anticipated regulatory responses to climate change. Since these issues should already be considered in the exercise of prudent business practice and existing fiduciary duties, it is often not clear that the Climate and Carbon Principles prescribe any action that would differ from business as usual.

Both the Climate Principles and the Carbon Principles appropriately emphasize the wide range of attractive business opportunities that financial institutions will have in helping to facilitate the implementation of low carbon solutions to the climate crisis. But neither initiative recognizes what climate science and common sense clearly tell us: certain other greenhouse gas (GHG) intensive activities are so inherently destabilizing that they can no longer be responsibly funded. No bright lines are drawn, no technologies are excluded, nothing is off the table.

Both the Carbon Principles and the Climate Principles fail to acknowledge that moving *towards* a low carbon economy also implies taking steps towards phasing out and *abandoning* the fossil fuel-based economy; such an acknowledgement would by necessity redirect the finance sector away from its continuing financing for the expansion of the oil, gas and coal industry, and fully commit itself to finance the transition towards safe, low and no carbon energy options.[5] While the signatories recognize that they will be operating in an increasingly carbon-constrained business environment going forward, they continue to finance the dirtiest, most backward carbon-intensive technologies.

The inevitable conclusion from reviewing both sets of principles is that even if they were to be adopted tomorrow by every financial institution in the world, they would only result in, at best, a moderate departure from existing business practices. The financing of oil, gas and coal exploration projects from the Arctic to the Antarctic, the construction of pipelines crisscrossing every continent, and the installation of hundreds of new fossil-fuelled power plants that will cast a deep carbon shadow over the planet for decades to come would continue unabated. This is not the response needed to the alarming situation at hand.

Ambition needed

BankTrack calls upon leading financial institutions to develop a robust framework of climate policies and practices whose ambition is commensurate with the scale of the challenge at hand. BankTrack calls on the Carbon Principles banks, and the Climate Group and its partners, to dramatically ratchet up their ambitions for the finance sector if either of these sets of Principles are to develop credibility as a leading initiative. Such a framework must recognize:

- the scientific consensus on the urgency of the climate crisis and the need to dramatically reduce the level of greenhouse gas emissions as quickly as possible;
- the need for the wide-scale phase-out and replacement of existing carbon-intensive technologies and practices over relatively short-time horizons;
- the urgent need for strong, comprehensive, performance-based climate policies in priority greenhouse-gas intensive sectors;
- the need for a clearly-defined time-bound program of work to develop rigorous performance standards for avoiding, minimizing, and publicly reporting on all financed emissions;
- the need to incorporate appropriate mechanisms for external stakeholder participation.

A different approach; the Kiribati Principles

In 2007 BankTrack called upon banks to abandon window dressing efforts and start developing climate policies and practices that make a real difference to the climate. BankTrack urged banks to do the following:[6]

[5] In the vision of BankTrack this would also exclude nuclear energy and large hydro as viable energy options. See position paper mentioned in footnote 8.

[6] This outline of bank policies was subsequently dubbed 'the Kiribati Principles', after one of the many low-lying land areas in the world about to be submerged as a result of climate change, and to emphasise the urgency of the situation. For the paper see

First, banks must take steps to disentangle themselves from activities and projects that substantially contribute to climate change. Towards this end, they should:

- Phase out their support for all new coal, oil and gas extraction and delivery projects;
- Phase out their support for all new coal-fired power plants;
- Phase out their support for the most harmful practices in other Greenhouse Gas (GHG)-intensive sectors;

Second, banks should minimize the extent to which their remaining lending activities and investments contribute to climate change. Towards this end, they should:

- Assess and report on the GHG emissions associated with all their loans, investments and other financial services (financed emissions); this to develop a baseline on which to base reduction targets;
- Establish portfolio and business-unit emissions reduction targets in line with what is considered necessary to stop climate change from unfolding, as based on current scientific consensus on climate stabilization;
- Develop a set of tools and policies that allow them to effectively address climate issues and reduce emissions across their full range of operations and services.

Third, banks should drastically increase their lending and support for the development and use of climate-friendly technologies and production processes. Accordingly, they should:

- Increase support for GHG emissions reduction technology, renewable energy production and energy efficiency in all business lines;
- Develop products and services to help retail customers address climate change.

Engagement required

The two annexes to this statement provide our detailed comments on the Carbon Principles and the Climate Principles as they are now formulated. They are submitted to the signatories in the spirit of fostering a debate between the finance sector and civil society groups -- such as BankTrack -- on how to make these principles, or another sufficiently ambitious standard truly deliver on combating climate change.[7]

Nijmegen, Netherlands
March 2009

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http://www.banktrack.org/download/a_challenging_climate_what_banks_should_do_to_combat_climate_change/0_0_071212_a_challenging_climate_final.pdf

[7] Unfortunately, no such debate or indeed any consultation process has taken place during the drafting process of the Principles. This already cast doubt on the stated commitment of Carbon Principles signatories to “Engage with our customers, suppliers and wider society to seek opportunities for a low carbon economy”.

Annex 1 Comments on the Climate Principles

*BankTrack comments on the Climate Principles are included in original text in **blue***

THE CLIMATE PRINCIPLES:

A framework for the finance sector

VISION

There is international scientific consensus that greenhouse gas (GHG) emissions from human activities are a critical contributor to changes in the world's climate. Failure to reduce these emissions is likely to result in widespread, irreversible changes to the climate, which leading scientists and economists predict will have negative consequences for human society, the global economy and the world's natural systems.

We agree with this statement as far as it goes. However, it fails to convey the urgency of the challenge and the growing consensus in the scientific community and the public that considerable action must be taken immediately to prevent the most dangerous impacts of global climate change. It also fails to reference commonly-accepted targets that can guide policy objectives --such as a stabilization pathway that takes us back to atmospheric levels of maximum 350 ppm of CO2 or that provides reasonable assurance of keeping global temperature increases below 1.5 degree Celsius.

In our capacity as advisors, lenders, investors and insurers, we are in a position to play a stewardship role by assisting the individuals, companies and projects we help finance, and clients that we offer insurance cover to, to understand and manage the risks, opportunities and adaptation needs relating to climate change. This stewardship role requires us to develop the expertise, products and services necessary to equip our clients and partners to address these challenges. We also recognise we must minimise our operational GHG emissions. We believe that climate change presents a series of risks and opportunities to which:

Again, we agree with this statement as far as it goes. Financial institutions can play an important stewardship role in helping their clients minimize their climate impacts and risks. But collectively, the finance sector also serves as a critical "gatekeeper" function in determining who gets access to capital and on what terms. Financial institutions must also discharge this function in ways that are consistent with the urgency of the climate crisis. The Climate Principles should address this issue explicitly by specifying a set of technologies and activities that are too inherently dirty or risky to be responsibly supported.[8]

1. Governments should respond by taking an integrated approach to energy and climate policy; setting targets for reducing carbon emissions and developing

[8] Bank of America, for example, recently announced that it would phase out its support for companies that practice mountaintop removal coal mining.

mechanisms to support their achievement, giving due consideration to action recommended by leading global scientists to ensure GHG emissions in the atmosphere can be stabilised at safe levels.

2. Businesses should respond by understanding and managing their carbon and climate risks and seeking opportunities to support the transition to a low carbon economy; and,
3. Individuals should take responsibility and change their behaviour and purchasing decisions to reduce their personal carbon footprint.

Once again, BankTrack does not disagree with this statement, but finds it lacking in vision and ambition. It understates the response to the climate crisis that society should expect from its business leaders. Surely, the business community must do more than "understand and manage risks" and "seek opportunities" to facilitate the transition to a low-carbon economy; Just like individuals they must change their behaviour and refrain from supporting activities that exacerbate the climate crisis or impede progress toward climate solutions.

The principles contained in this document set out our commitment to:

1. Minimise our operational carbon footprint;
2. Make business decisions that will reduce climate change risks and allow the development of climate-change related opportunities
3. Develop products and services that enable our customers to manage their climate change related risks and business opportunities;
4. Engage with our customers, suppliers and wider society to seek opportunities for a low carbon economy;
5. Support the development of sound energy and climate change policy; and,
6. Disclose progress against our commitment.

It is not clear whether the "climate change risks" addressed in Point 2 include the risks that business decisions will have adverse climate impacts, or if it is intended only to refer to risks climate change may have for profitability and shareholder value. We think this point should be clarified to explicitly include a commitment to avoid support for the most greenhouse gas intensive technologies and activities, and to reduce the carbon footprint of lending, investment and other financial services.
We appreciate that signatory banks commit to minimise their operational carbon footprint but consider this in 2009 an absolute minimal commitment of every business, hardly worth mentioning.

We believe that taking a proactive approach to climate change will position us as a leading financial institution in a low carbon economy.

OUR ACHIEVEMENT

1.0 We have a robust low carbon strategy or position and are managing our operational carbon emissions

1.1 We have issued a strategy or position that indicates how we undertake our business in a way that reduces the climate and operational carbon impact of our activities.
1.2 We have board level commitment for the strategy or position and a named senior executive who has responsibility for implementing it across our organisation and for ensuring that decisions taken are consistent with it. This executive has the necessary resources to meet the commitments contained in our strategy or position.
1.3 We have measured a significant proportion of our operational GHG emissions using an internationally recognised or equivalent domestic standard and we disclose this information.
1.4 We have issued clear and challenging, yet achievable, targets for making reductions in our operational GHG emissions.
1.5 We engage our employees on our commitment to addressing climate change and support them in playing an active role in meeting this commitment.

These initial steps demonstrate our commitment to addressing climate change and managing our own operational impacts. However, we recognise we must go further, as we have significant influence on the management of climate change risks and the opportunities for the development of a low carbon economy through the deployment of capital. We also commit to engaging with our customers, suppliers and wider society as appropriate to do this.

BankTrack welcomes the signatory's commitment to reduce operational emissions from business operations. We are unclear, however, why these provisions are characterized as "achievements" while all of the other provisions are labelled as "commitments". One could interpret this distinction to imply that demonstrated action on direct operational emissions is the only concrete prerequisite for new membership, and that a mere commitment to act on other issues is sufficient. If that is the case, we feel that inappropriately prioritizes reducing direct, operational emissions over steps to reduce indirect, financed emissions.

BankTrack appreciates that signatories recognise that they must go beyond operational emissions and acknowledge their influence over clients in managing climate risks. BankTrack believes however that the responsibility of banks goes beyond merely 'engaging as appropriate to do this' and must include action to reduce banks financed emissions.

OUR COMMITMENT

2.0 We will develop commercially viable approaches to ensure climate and carbon issues are addressed where these apply to our business strategy and activities.

While we understand the importance of seeking commercially viable approaches to deal with climate issues, the formulation above precludes any approaches that are deemed not commercially viable in the short term but that may nevertheless be *necessary to pursue for the greater good of society. It is out of the question that every necessary step that must be taken to combat climate change will also be commercially viable; solid principles will recognise the inherent tension between commercial and societal interests and provide guidance in dealing with these tensions.*

2.1 Research Activities

2.1.1 We will incorporate climate and carbon issues into our research activities and, where relevant, will utilise the findings to develop products and services that benefit our customers and clients.

We find this provision to be rather vague and aspirational. Further guidance should be provided regarding the kinds of climate-related research that signatories will pursue, and the products and services that they will seek to develop.

2.2 Asset Management

2.2.1 We will enable our analysts to incorporate carbon and climate risks and opportunities into their research and investment decisions where relevant.

This commitment should be clarified and expanded. If it is intended to refer only to the risks to investments posed by climate change or regulatory interventions, it does little more than restate existing fiduciary duty to consider material risks in making investment decisions.

If, on the other hand, it requires analysts to consider the climate impacts of their investments, and presumably to weigh social costs and the economic costs of climate change against potential rates of return, then this commitment represents an important innovation that BankTrack fully supports. In doing so, the limits of this approach must be recognised: certain aggregate social costs, like a planetary catastrophe cannot be weighed against the rate of return of individual investments. Further elaboration on how analysts will be expected to integrate climate implications into their research and investment decisions is therefore welcome.

2.2.2 We will engage our clients to understand the carbon and climate change risks and opportunities relevant to them and we will develop products and services that support them in managing those risks and exploiting those opportunities.

Again, this provision can be interpreted simply to restate common-sense business practice and fiduciary obligation. We would not have thought it necessary for signatories to make an additional commitment to understand their clients' needs and concerns and to develop products and services that are responsive to their clients' interests. Accordingly, we believe that this provision could be strengthened by a clearer articulation of best practices and benchmarks for evaluating performance. Furthermore, it could be improved by including a greater emphasis on client and bank responsibilities for minimizing and mitigating climate and carbon-related risks and impacts.

2.2.3 Where consistent with our fiduciary responsibilities, we will engage with the companies our clients invest in to understand how they are minimising the risks and maximising the opportunities presented by climate change and climate policy. We will also encourage these companies to improve their governance and disclosure of climate risks and opportunities.

Once again, this provision does not appear to require anything more than is already required by traditional fiduciary duty. It elides the critical questions of what kind of engagement is expected under the principles, and what interventions signatories believe are actually precluded by their fiduciary responsibilities. Further clarification on the nature of his commitment and how it differs from existing obligations is therefore warranted.

Overall, we think that this section on asset management fails to acknowledge the need to have clear reduction or exclusion policies based on climate and energy criteria. Such policies are essential to give credibility to shareholder activism practices and to avoid investment in false solutions to climate change (nuclear, biofuel, carbon capture and sequestration etc.)

The section should also recognise the need to calculate and reduce financed emissions in the case of asset management.

2.3 Retail Banking

2.3.1 We will undertake research to understand:
1) The potential impacts of climate change and climate change policy for our customers;
2) The willingness of our customers to address these impacts;
3) The products and services that customers need to address these impacts and the barriers to addressing them;
4) The approaches needed to raise awareness of how our customers manage their GHG emissions and reduce their carbon footprint.

2.3.2 Based on our understanding of our customers, we will develop products, services and communication and engagement strategies to enable them to address potential impacts and reduce their carbon footprint.

BankTrack welcomes initiatives to develop products and services that will assist customers to avoid, address, minimize, mitigate and adapt to climate change. While specialized products and services may serve important functions, climate considerations should not be relegated to niche markets; rather they should be integrated into the broadest possible range of products and services.

2.4 Insurance and Reinsurance

2.4.1 We will develop the necessary knowledge, skills and tools to assess carbon and climate risks associated with our transactions and the financial implications they have for our business.

2.4.2 We will develop risk assessment techniques to assist our clients to understand better and respond to climate change.

2.4.3 We will develop insurance products and services that encourage our customers to reduce their carbon and climate risks, assist the development and adoption of GHG mitigation technologies and strategies and take advantage of the carbon market.

Paragraphs 2.4.1 and 2.4.2 may be interpreted to simply restate common-sense business practice and fiduciary obligation. For example, we would already expect insurance companies to integrate the risk of increased losses due to more extreme weather events into their risk assessment methodologies. Clarification regarding what else is expected of signatories would therefore be useful.

Paragraph 2.4.3's commitment to "assist the development and adoption of GHG mitigation technologies" is more promising, but further clarification here would also be useful. Again, there must be inclusion of an emphasis on "avoiding" carbon emissions, including the development and adoption of "avoidance" technologies and strategies.

In addition, to meaningfully be called "Climate Principles", there must be some principle involved that calls for clients to reduce not only their carbon and climate risk, but also to reduce their climate and carbon impacts. Furthermore, we are concerned that Paragraph 2.4.3 does not recognize the problem that certain products and services may create a moral hazard of facilitating greater investment in greenhouse gas intensive technologies. For example, instruments that might help the sponsors of a new coal-fired power plant "take advantage of the carbon market" may fit within this provision, but would obviously be counterproductive in terms of reducing carbon emissions. Signatories should agree not to develop or market such products.

2.5 Corporate Banking

2.5.1 We will develop and implement a process to consistently assess the financial implications of carbon and climate risks relevant to our clients and will train employees to implement this assessment.

2.5.2 We will consider practical ways to assess the carbon and climate risks of our lending and investment activities. Where a feasible and relevant methodology can be found, we will develop and implement this approach.

2.5.3 We will engage our clients to understand the carbon and climate risks and opportunities associated with their business. This might include encouraging them to develop a strategy to manage these risks; to measure and disclosure their carbon footprint; and, to set meaningful targets to reduce carbon emissions.

2.5.4 We will develop financing solutions to facilitate investment in low carbon technologies and GHG reduction projects.

Again, the meaning of "carbon and climate risks" needs to be clarified. It is not clear whether the phrase refers to "risks to climate change caused by the client," or "risks to the client caused by climate change." If it is the latter, paragraphs 2.5.1 and 2.5.2 *do little more than restate common sense business practices and existing fiduciary obligations. If it is the former, expectations and performance benchmarks must be developed and specified. BankTrack also believes that an active approach is required to develop and adopt common methodologies to account for financed emissions.*

Paragraph 2.5.3 raises the importance of having clients disclose and reduce their carbon footprints (though using very weak language such as 'this might include'). However, it falls well short of suggesting that support from the signatories should be conditioned on accomplishment of any meaningful carbon footprint performance standards. In the absence of such standards, compliance with paragraph 2.5.3 requires very little.

This paragraph should be strengthened by requiring signatories to make a good faith effort to encourage their clients to at least adopt sectoral best practices for reporting avoiding and minimizing greenhouse gas emissions. It should also incorporate an exclusion list of activities that would render a company ineligible for support from signatory institutions.

2.6 Investment Banking & Markets

2.6.1 *Corporate Advisory*
We will develop the knowledge, tools and skills necessary to advise our clients of the potential financial implications of carbon and climate risks and opportunities associated with their business transactions.

2.6.2 *Structured Lending & Venture Capital*
We will develop viable financing solutions to facilitate investment in low carbon technologies and GHG reduction projects.

Paragraphs 2.6.1 and 2.6.2 simply restate common sense practices for assisting clients and remaining competitive in a climate-constrained business environment.

Paragraph 2.6.2 should require signatories to develop a priority strategy for investments in low carbon and GHG reduction projects.

As with corporate banking, these provisions should be amended to incorporate an exclusion list of activities that would render a company ineligible for support from signatory institutions and set performance targets reducing the GHG intensity of financing.

2.6.3 *Trading*
We will develop expertise to support emissions trading, weather derivatives, renewable energy credits and other climate related commodities, and look for ways to play a constructive role in promoting these.

Paragraph 2.6.3 seems to assume that these trading schemes and instruments will develop in ways that are socially beneficial and will improve our ability to manage climate change by creating new incentive structures and reducing the economic costs *of mitigation efforts. However, the way in which cap-and-trade schemes have been structured so far, and initial experiences with carbon trading, have proven that this assumption is very problematic.*

For example, the widespread reliance and use of offsets has allowed business-as-usual emissions levels to continue, while delaying incentives to make needed, immediate investments in new technologies and infrastructure. In addition, the offset market, especially in Clean Development Mechanism projects, have become increasingly problematic. After years of experience, it is now clear that it is impossible to reliably prove that offsets are additional, leading to real GHG emission reductions. Moreover, too many offset projects have created unacceptably high environmental, social and human rights impacts.

Another major flaw which has been exposed in carbon trading schemes relates to the windfall profits that many companies "earned" due to the give-away of emissions permits during the earlier phases of the EU Emissions Trading Scheme. More recently, companies that have cut production due to the economic downturn have cashed in some Euro 1 billion of emissions permits, resulting in a collapse in carbon prices. Using carbon credits as a source of easy cash has no positive impact on, and in fact inhibits real action on climate change.

Finally, carbon trading is impossible to regulate on every level. The offset market faces insurmountable challenges with verification, including problems relating to additionality and leakage. The primary market for carbon trading is beset with current and potential difficulties, such as the problem of windfall profits, and concerns relating to the transparency of over-the-counter derivatives trading. The secondary carbon market, which will eventually dwarf primary markets, will be dominated by speculative investors, paving the way for the kinds of financial innovation that can be become excessively risky in bubble economy. As the current economic crisis has demonstrated, the "originate-and-distribute" model creates deep interlinkages between financial markets, and a potential collapse in the carbon markets would have severe environmental and financial consequences.[9]

Given the above, BankTrack thinks that banks should not assume 'trading' to be part of the solution. Instead, they should focus their attention on other activities which will more demonstrably lead to real reductions in carbon emissions.

2.7 Project Finance

For projects that release or are likely to release 100,000 tons CO_2 equivalent per year (aggregate emissions of direct sources and indirect sources associated with purchased electricity for own consumption), except where justified deviation is provided, we will request the client to:

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[9] See the recent report of FoE US 'Subprime Carbon? Re-thinking the World's Largest New Derivatives Market', available on BankTrack website; publications

Project finance is not the only source of financing for projects. Adequate principles should apply to any lending with known use of proceeds as well as corporate financing to single purpose companies that are failing to control carbon emissions.

The minimum threshold of 100,000 tons of CO2 equivalent used in this section is too high. Substantial emissions reductions can be achieved from lower emitting projects. Given the severity of the global climate crisis, we recommend that this threshold figure be modified downwards. [10]

2.7.1 Seek opportunities to reduce project-related GHG emissions in a manner appropriate to the nature and scale of project operations and impacts.
2.7.2 Quantify and disclose direct GHG emissions and indirect GHG emissions associated with the offsite production of power used by the project.
2.7.3 Monitor and report GHG emissions annually in accordance with internationally-recognised methodologies.
2.7.4 Evaluate technically and financially feasible options to reduce or offset project-related GHG emissions during the design and operation of the project.

This section also fails to recognize that certain projects are so dirty or greenhouse gas intensive that they are fundamentally incompatible with responsible climate stewardship, and should not be financed by institutions that aspire to a leadership role on climate issues. Under this section, even the dirtiest projects such as unconventional oil development and mountaintop removal coal mining apparently would still be eligible for support if their proponents evaluate marginal process improvements and report on emissions. This is incrementalism ad absurdum, and essentially indistinguishable from business as usual.

BankTrack believes that the Climate Principles should therefore exclude at least all new coal, oil and gas extraction and delivery projects and all new coal-fired power plants.[11] *The section -– or an annex -- should either (1) specifically exclude the most harmful existing and emerging practices in other GHG-intensive sectors, or (2) articulate a set of best practices in each sector that will be prerequisites for financing. These standards should then tighten over time.*

In addition, the emphasis only on quantifying and disclosing, and monitoring and reporting project-specific GHG emissions neglects the need to seek net reductions in GHG emissions at both the project and corporate levels. For example, in the Carbon Principles, the signatories look for commitments "at the corporate or project level to reduce net greenhouse gas emissions within specific timetables or for new capacity, making a commitment not to increase net emissions." A similar requirement should be included in this section.

As stated above, these provisions should not only apply to strict project finance but to any lending in which the specific use of the proceeds can be identified.

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[10] We note for example that the EBRD has adopted a minimum of 20.000 tons.
[11] We refer to the BankTrack position paper for a comprehensive list. See footnote 6

3. We will engage others to support the growth of a low carbon economy, where consistent with our corporate policies on public engagement

3.1 We will disseminate information through our network of customers, suppliers, staff and other stakeholders to raise awareness about climate change and the opportunities for reducing GHG emissions.

3.2 We will engage our significant suppliers on climate change issues and work with them to enable us to reduce GHG emissions throughout our supply chain.

3.3 We recognise that tackling climate change cannot be solved through voluntary action alone and we support the adoption of effective and efficient regulation and policy to reduce GHG emissions. Such support may include engaging policy makers and/or key stakeholders on an individual basis or through relevant industry and multi-stakeholder initiatives.

This section could be strengthened through recognition of the scientific imperative of the need for stringent and immediate reduction of greenhouse gas emissions, and a pledge to support public policy that is consistent with that scientific imperative.

DISCLOSURE REQUIREMENTS

SECTION 1.0 of the Climate Principles

The Climate Principle Achievement Public Disclosure Requirement

1.1 We have issued a strategy or position that indicates how we undertake our business in a way that reduces the climate and operational carbon impact of our activities.

- Climate change strategy or position that outlines how the organization is addressing the relevant items covered by the Principles

1.2 We have board level commitment for the strategy or position and a named senior executive who has responsibility for implementing it across our organization and for ensuring that decisions taken are consistent with it. This executive has the necessary resources to meet the commitments contained in our strategy or position.

- Named senior executive responsible for the organization's strategy or position
- Overview indicating responsibilities for implementing the strategy or position and for achieving targets set by the organization
- Overview of how climate change issues are managed across the business

1.3 We have measured a significant proportion of our operational GHG emissions using an internationally recognized or equivalent domestic standard and we disclose this information.

- Operational GHG emissions
- Reduction targets, revisions thereof and timeframes
- Annual reporting of progress towards targets
- GHG footprint is verified by an independent party (e.g. external auditors)

1.4 We have issued clear and challenging, yet achievable, targets for making reductions in our operational GHG emissions.

- Quantitative and qualitative targets for reducing operational GHG emissions.

1.5 We engage our employees on our commitment to addressing climate change and support them in playing an active role in meeting this commitment.

- Employee awareness raising and/or training programme and methods to assess success of that process
- Approaches used to support employees take action on climate change at work and/or at home

SECTION 2.0 & 3.0 of the Climate Principles

1 All financial institutions adopting the Principles are required to disclose what has been achieved on all aspects of the Principles applicable to their business activities.
2 Where financial institutions have not fully implemented the relevant requirements, they will be encouraged to disclose a timeframe for achieving full implementation.
3 Information should be disclosed on an annual basis.
4 The Climate Group will review disclosure against the Principles on an annual basis using publicly available information, (eg. Carbon Disclosure Project response, Corporate Reports and website).
5 The Climate Group will develop a framework for reviewing disclosure and for identifying emerging consistent and best practice which will be agreed by the group of adopting organizations.

These reporting requirements are useful as far as they go. However, they do not provide an adequate basis to assess the performance of the Climate Principle signatories in reducing their financed emissions.

BankTrack believes that it is essential that the signatories measure and report on GHG emissions associated with all their loans, investments, and other financial services. They should also establish and disclose portfolio and business-unit emissions reduction targets consistent with current science on climate stabilization, and report on progress in achieving those objectives.

Furthermore, the Climate Group and the signatories should work to establish, and publicly share, consistent methodologies for measuring financed emissions and tracking and reporting on efforts to reduce these emissions over time.

Annex 2 Comments on the Carbon Principles

BankTrack comments are included in original text in blue. This critique focuses on the Carbon Principles itself, not on the due diligence process that is also part of the principles.[12]

The Carbon Principles

The Intent

We the adopting financial institutions have come together to advance a set of principles for meeting energy needs in the United States (US) that balance cost, reliability and greenhouse gas (GHG) concerns.[13] The principles focus on a portfolio approach that includes efficiency, renewable and low carbon power sources, as well as centralized generation sources in light of concerns regarding the impact of GHG emissions while recognizing the need to provide reliable power at a reasonable cost to consumers. The Carbon Principles ("the Principles") represent the first time that financial institutions, advised by their clients and environmental advocacy groups, have jointly committed to advance a consistent approach to the issue of climate change in the US electric power industry.

We advance these Principles to create an industry best practice for the evaluation of options to meet the electric power needs of the US in an environmentally responsible and cost effective manner. When evaluating the financing of new fossil fuel generation we will be guided by the Principles and employ the accompanying Enhanced Environmental Diligence Process (the "Enhanced Diligence Process") to assess project economics and financing parameters related to the uncertainties around current climate change policy in the US. The Enhanced Diligence Process will evaluate the ability of the proposed financing to meet financial requirements under a range of potential GHG emissions assumptions and parameters. These assumptions will include policies regarding CO_2 emission controls and potential future CO_2 emissions costs as well as the costs and feasibility of mitigating technologies or other mechanisms. Due to the uncertainties around many of these factors, the Enhanced Diligence Process will encourage consideration of assumptions that err on the side of caution until more clarity on these issues is available to developers, lenders and investors. Financial institutions that adopt the Principles will implement them with the accompanying Enhanced Diligence Process, while consulting with environmental groups and energy companies.

This approach explicitly focuses on regulatory risks associated with potential government interventions to mitigate climate change. As such, it simply restates common sense business practices and existing fiduciary obligations. It does not necessarily address the increased risks to climate stability, or the impediments to

[12] See http://www.carbonprinciples.org/documents/Carbon%20Principles%20Diligence%20Final.pdf

[13] We consider all Greenhouse gases but refer to CO2 which is the most significant

more climate friendly energy solutions that may be created by the project.

Moreover, the Carbon principles are a process standard, not a performance standard. Therefore, banks have made no commitment one way or the other in terms of their ongoing financing of new conventional coal fired power plants. In fact, financing for construction of a number of new conventional coal fired power plants in the US from Carbon Principle signatories has occurred since the Carbon Principles have come into effect.

While an initial focus on the United States may have been justified, BankTrack believes that the Carbon Principles should be expanded to include potential new coal fired power finance in any jurisdiction.

The Carbon Principles

Energy efficiency. An effective way to limit CO_2 emissions is to not produce them. We will encourage clients to invest in cost-effective demand reduction, taking into consideration the potential value of avoided CO_2 emissions. We will also encourage regulatory and legislative changes that increase efficiency in electricity consumption including the removal of barriers to investment in cost-effective demand reduction. We will consider demand reduction caused by increased energy efficiency (or other means) as part of the Enhanced Diligence Process and assess its impact on proposed financings of new fossil fuel generation.

We agree that energy efficiency measures are critical to solving the climate change crisis. The Carbon Principles should more explicitly prioritize energy efficiency and demand reduction measures as the preferred solution for satisfying energy demand, and consider investment in increased production capacity only where demand reduction alternatives are shown to be inadequate to meet energy needs.

While it is understandable in this context that emphasis is placed upon the 'cost effectiveness' of investments, we note that this may lead to the obstruction of a energy shift that may not be cost effective in short term, conventional terms but nevertheless necessary from the perspective of avoiding a global climate catastrophe.

Renewable and low carbon energy technologies. Renewable energy and low carbon distributed energy technologies hold considerable promise for meeting the electricity needs of the US while also leveraging American technology and creating jobs. We will encourage clients to invest in cost-effective renewables, fuel cells and other low carbon technologies, taking into consideration the potential value of avoided CO_2 emissions

We will also support legislative and regulatory changes that remove barriers to, and promote such investments (including related investments in infrastructure and equipment needed to support the connection of renewable sources to the system). We will consider production increases from renewable and low carbon generation as part of the Enhanced Diligence Process and assess their impact on proposed financings of new fossil fuel generation.

Conventional or Advanced generation. In addition to cost effective energy efficiency, renewables and low carbon generation, we believe investments in other generating technologies likely will be needed to supply reliable electric power to the US market. This may include power from natural gas, coal and nuclear[14] technologies. Due to evolving climate policy, investing in CO_2-emitting fossil fuel generation entails uncertain financial, regulatory and environmental liability risks. It is the purpose of the Enhanced Diligence Process to assess and reflect these risks in the financing considerations for fossil fuel generation. We will encourage regulatory and legislative changes that facilitate carbon mitigation technologies such as carbon capture and storage (CCS) to further reduce CO_2 emissions from the electric sector.

New fossil fuel generation constructed with conventional technology, if not accompanied by mitigation measures, will increase the emission of CO_2 into the atmosphere at a time when federal and state level emissions controls seem likely and, in some regions of the country, are already mandated. An important aspect of the Enhanced Diligence Process will be to evaluate the mitigation strategy and plan of the developer to address the risks posed by the increased CO_2 emissions from new sources when future emissions controls are uncertain. For projects proposed in jurisdictions that already have controls on emissions in place, the developer will need to show how the new generation will be consistent with the existing rules and potential changes going forward. However, in the absence of regional or federal regulations, the development plan will need to account for the added risks due to the uncertainties around future emissions limits.

This approach fails to recognize that certain projects are so dirty, greenhouse gas intensive that they are fundamentally incompatible with responsible climate stewardship, and should not be financed at all. BankTrack is therefore opposed to financing for new nuclear power facilities due to their high costs, long-term radioactive waste management, risk of accidents and potential to contribute to nuclear weapons proliferation.

BankTrack believes that when the costs of carbon capture and storage (CCS) for coal power are internalized into financial analysis, as well as the other high social and environmental costs associated with coal mining, transportation and use, that renewable energy and energy efficiency offer much better and more profitable investment opportunities than CCS while meeting energy service needs.

Every plausible greenhouse gas emission reduction strategy includes dramatic reductions in reliance on coal. Yet coal generation is not excluded from financing under the Carbon Principles and their Enhanced Diligence Process. The Carbon Principles should therefore be amended to include an exclusion list of the dirtiest power sources --including new coal generation-- and performance benchmarks for other types of projects to ensure that they meet best practice standards.

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[14] It is recognized that nuclear plants carry a host of risks that financial institutions must consider, but which are outside the scope of these principles.

The Commitments

Adopters commit to:

Encourage clients to pursue cost-effective energy efficiency, renewable energy and other low carbon alternatives to conventional generation, taking into consideration the potential value of avoided CO_2 emissions.

Ascertain and evaluate the financial and operational risk to fossil fuel generation financings posed by the prospect of domestic CO_2 emissions controls through the application of the Enhanced Diligence Process. Use the results of this diligence as a contribution to the determination whether a transaction is eligible for financing and under what terms.

Educate clients, regulators, and other industry participants regarding the additional diligence required for fossil fuel generation financings, and encourage regulatory and legislative changes consistent with the Principles.

BankTrack supports these commitments as far as they go. However, we believe that they must be supplemented with additional requirements if the Carbon Principles are to provide an appropriate framework for addressing climate change drivers in the power sector. First, as noted, the signatories should agree to forego consideration of projects that rely upon the most greenhouse gas intensive technologies. Second, signatories should agree to measure and report on GHG emissions associated with all the loans, investments, and other financial services they provide to power sector clients in the US and all other countries. They should also establish and disclose portfolio and business-unit emissions reduction targets consistent with current science on climate stabilization, and report on progress in achieving those objectives.

BankTrack wishes to thank Steve Herz for the initial analysis, and Larry Lohmann, Michelle Chan, Yann Louvel, Bill Barclay, Dana Clark and Johan Frijns for additional comments on the draft version of this paper.

For more information on the climate and energy campaign of BankTrack see: http://www.banktrack.org/show/focus/banks_climate_and_energy

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