

Green Bond Guidelines, 2017

SUMMARY

This is a summary of the “Green Bond Guidelines, 2017” published on March 28, 2017 by the Ministry of the Environment, Japan (MOEJ). This is an unofficial translation. Translations are to be used solely as reference material to aid in the understanding of the Guidelines. The government of Japan will not be responsible for the accuracy, reliability or currency of this summary, or for any consequence resulting from use of the information in this summary.

Chapter 1 Introduction

1. Purpose of the Guidelines

In December 2015, the “Paris Agreement,” an international agreement on climate change, was adopted at the COP 21¹, held in Paris, France. In this agreement, the global long-term goal was set to hold the increase in the global average temperature to well below 2°C, and pursue efforts to limit the temperature to 1.5°C above pre-industrial levels. In order to address the long-term substantial reduction of greenhouse gas emissions in Japan, and to achieve this “2°C goal”, it is necessary to mobilize large amounts of private investment in Green Projects such as renewable energy projects.

Furthermore, the "2030 Agenda for Sustainable Development", adopted at the United Nations Sustainable Development Summit held in September 2015 in New York, lays out the Sustainable Development Goals (SDGs) which include the conservation of oceanic and terrestrial ecosystems. This has also increased expectations for the role of private investments in projects for the prevention of natural capital deterioration and other environmental purposes.

In recent years, issuances of Green Bonds —bonds issued by organizations including corporations and local governments to raise funds for Green Projects— and investments in the bonds have significantly increased at an international level. Green Bonds are becoming an effective tool to raise funds for Green Projects which contribute to the reduction of GHG emissions and the prevention of natural capital deterioration. These trends have been particularly notable since the establishment of the "Green Bond Principles" (hereinafter referred to as "the GBP") in January 2014. Although Green Bond issuances and investments have also begun to appear in Japan, they have not spread sufficiently, compared with

¹ The 21st Conference of the Parties to the United Nations Framework Convention on Climate Change

overseas.

In light of the above, this “Green Bond Guidelines” (hereinafter referred to as “the Guidelines”) have been developed with the purpose of spurring issuances of Green Bonds and investments in them in Japan. In the course of the development, in order to maintain credibility of the green characteristics of Green Bonds, the Guidelines seek to prevent “green-wash” bonds (bonds labelled as “green”, despite the fact that they have no environmental benefits, or that their proceeds² have not been appropriately allocated to Green Projects) from being issued and invested in.

The Guidelines, with due consideration to the consistency with the GBP, which is widely accepted in the Green Bond markets in the world, provide issuers, investors and other market participants with illustrative examples of specific approaches and interpretations tailored to the characteristics of the Japan’s bond market which will aid these market participants to make decisions on working-level matters related to Green Bonds. It will lead to both the establishment of credibility of the green characteristics of Green bonds and the alleviation of costs and administrative burdens for issuers, thereby spurring Green Bond issuances and investments in Japan.

2. Basic Concepts of the Guidelines

The Green Bond market, essentially, is to be developed through interaction based on sufficient information between issuers who wish to raise funds with clearly declaring that they will allocate the proceeds only to Green Projects, and investors who wish to invest in Green Projects they select. The final decision on how the appropriateness of the issuers' approaches related to their Green Bonds is evaluated, and whether these Green Bonds are invested in, would be left to the market participants.

If elements a Green Bond should have are clarified in the Guidelines, it will be the foundation of the interaction between these issuers and investors as well as the tool for explanation to their stakeholders that the proceeds of the Green Bond will surely be used for Green Projects.

In addition, it is important for these issuers and investors that credibility of the green characteristics of the Green Bond has been maintained within the market and society. Especially, preventing “green-wash” bonds from being issued and invested in is indispensable from the viewpoint of protection of Green Bond investors.

On the basis of the above, the Guidelines have been developed with due consideration to the

² “Proceeds” in the Guidelines means the “net proceeds” after issuance fees have been deducted.

consistency with the contents of the GBP (as of June 2016). The Guidelines recognize that a Green Bond is expected to be aligned with the following four components: (1) Use of Proceeds, (2) Process for Project Evaluation and Selection, (3) Management of Proceeds, and (4) Reporting, and believe that bonds which have all elements described with the word "should" in the Guidelines concerning these four components can be internationally accepted as Green Bonds³.

On the other hand, the Guidelines do not take the "all or nothing" position, that means, the Guidelines do not insist that "the issuer should not claim any environmental benefits of the bond unless the bond have all elements described with the word 'should' in the Guidelines." Considering the current immaturity of Japan's Green Bond market, it is beneficial that issuers implement "trial" issuances of "bonds" with referring to the Guidelines, as long as their proceeds are allocated with certainty to Green Projects, even if the evaluation of environmental benefit of the bonds issued in the "trial" issuances is not perfect or reporting of the result of the evaluation is a little limited. These "trial" issuances will help issuers to accumulate knowledge toward future issuances of "Green Bonds", which have all elements described with the word "should" in the Guidelines.

As for matters about which issuers, investors and other market participants have different ways of thinking, it is important to establish a mechanism in which 1) the issuers disclose information relevant to their Green Bonds in an easily understandable way 2) the investors or other market participants evaluate the appropriateness of the issuers' approaches related to the Green Bonds through the utilization of the information disclosed by the issuers, and 3) all of the participants including the issuers and the investors can take advantage of the knowledge accumulated through these interactions between the participants, rather than to filter out specific approaches related to Green Bonds from the market, unless these approaches are obviously inappropriate. By establishing the mechanism, market discipline can be exercised to avoid greenwashing, while securing the diversity of issuers' approaches.

The Guidelines are developed with a focus on the green characteristics of bonds, and therefore do not cover the inherent risks as bonds. It is important to keep in mind that Green Bonds, even if they are aligned to the Guidelines, have credit risks, price fluctuation risks, liquidity risks and other risks, like any other ordinary bonds.

3. Structure of the Guidelines

In Chapter 2, the Guidelines explain the overview and the current situation of Green Bonds. Benefits of Green Bond issuances and investments are also explained, as references for

³ However, it is necessary to keep in mind that an individual Green Bond is to be evaluated and selected by each investors and other related participants based on their own ways of thinking.

issuers who are considering to issue Green Bonds and for investors who are considering to invest in them.

Chapter 3 is the core of the Guidelines. In this chapter the Guidelines explain elements which Green Bonds are expected to have and examples of possible approaches that make a bond have these elements. Descriptions in this chapter have the following meaning.

- ① Sentences described with the word “should” are basic elements which bonds labelled as “green” are expected to have.
- ② Sentences described with the word “recommend” are elements which bonds labelled as “green” are considered to be better to have, although it is still acceptable that a bond which does not have these elements is labelled as “green”.
- ③ Sentences described with the word “to be considered” are examples of possible approaches and interpretations related to Green Bonds.

It should be noted that the Guidelines are legally non-binding. No legal penalties, etc. will be imposed if a certain action does not comply with the elements described in the Guidelines (including elements described with the word "should"). However, it is necessary to keep in mind that, if a certain action infringes upon any laws and regulations, legal penalties, etc., may be imposed on the basis of these laws and regulations, even though the action complies with the elements described in the Guidelines.

Depending on the characteristics of the issuers and the Green Projects in which Green Bond proceeds will invest, practical application of the Guidelines is considered to vary significantly. Thus, in order to facilitate the understanding of readers, several patterns of Green Bond issuances are provided as model cases in Chapter 4.

Chapter3 Elements which Green Bonds are expected to have and examples of possible approaches (Excerpt)

1. Use of proceeds

○Green Bond proceeds should be allocated to Green Projects with clear environmental benefits, which will be assessed by the issuer.

These Green Projects include, but are not limited to:

1)Renewable energy

- Renewable energy generation
- Renewable heat supply
- Renewable energy storage, supply and demand control etc.

2)Energy efficiency

- Constructing energy efficient buildings, such as net-zero-energy house/building
- Remodeling buildings for energy efficiency etc.

3)Pollution prevention and control

- Projects contributing to circular economy
(e.g. recycling, heat recovery, and inverse manufacturing)
- Controlling release of hazardous chemical substances
- Soil remediation etc.

4)Sustainable management of living natural resources

- Environmentally sustainable agriculture, fishery, and forestry
- Integrated pest management (IPM) etc.

5)Terrestrial and aquatic biodiversity conservation

- Protection of coastal, marine and watershed environments
- Conservation of Sato-yama/Sato-umi etc.

6)Clean transportation

- Development or manufacture of clean energy vehicles such as EV or FCV
- Installing infrastructure for clean energy vehicles
- Improving efficiency of a logistics system by modal shift or joint delivery etc.

7)Sustainable water management

- Conservation of water cycle
- Countermeasure for floods etc.

8)Climate change adaptation

- Enhancing urban-infrastructure capability to prevent weather-related disasters etc.

9)Eco-efficient products, production technologies and processes

- Development and introduction of environmentally friendlier products
- Resource efficient packaging and distribution etc.

- It is recommended that issuers, where feasible, quantify the environmental benefits of the Green Projects to which Green Bond proceeds will be allocated.
- Issuers should provide investors in advance with information on the use of Green Bond proceeds through legal documents (e.g. the prospectus), or other documents.
- This information should include the Green Project categories.
- In the case that individual Green Projects to which Green Bond proceeds will be allocated have been specified, it is recommended that issuers add information on these projects to the explanation to investors.
- Green Projects to which Green Bond proceeds will be allocated may have negative environmental impacts as well as environmental benefits. “Green Projects with clear environmental benefits” described above mean the projects whose negative environmental impacts are expected to be limited compared to their environmental benefits. These negative environmental impacts include, but are not limited to:
 - disruptions of ecosystem caused by massive land development
 - light pollutions
 - bird strikes
 - damages from low frequency noise
 - noises and vibrations caused by the construction
 - air pollutions
 - water pollutions

In the case, the issuers should add information on these negative impacts (e.g. how they are assessed, what the issuers do to curb them) to the explanation to investors.
- In case that the use of Green Bond proceeds includes refinancing of existing Green Projects, it is recommended that the issuers add information on 1) the amount (or the share) of bond proceeds being used for refinancing, and 2) which Green Projects (or Green Project categories) may be refinanced to the explanation to the investor.

2. Process for Project Evaluation and Selection

- Issuers should provide investors in advance with information on the “environmental sustainability objectives” (e.g. environmental benefits to be realized through the Green Bond issuance).
- Issuers should provide investors in advance with information on the “criteria” for evaluating and selecting specific Green Projects to which Green Bond proceeds will be allocated according to the “environmental sustainability objectives” described above.

- Issuers should provide investors in advance with information on the “process” (e.g. “the reason why the issuers determine the Green Projects evaluated and selected as the use of Green Bond proceeds can provide environmental benefits properly in light of the above objectives and criteria,” “by whom and how the above criteria are applied” and “who determine whether Green Projects are eligible in light of the above objectives.” etc.).
- It is recommended that whether the “process” works appropriately from an environmental point of view be checked by involving any internal departments with environmental expertise or external institutions with the “process” .

3. Management of Proceeds

- Issuers should track and manage the net Green Bond proceeds in an appropriate manner. These tracking and managing activities should be controlled by the issuer’s internal process.
- As long as the Green Bonds are outstanding, the issuers should periodically adjust to match the amount of the total Green Bond proceeds to the sum of the amount of the proceeds allocated to Green Projects and the amount of the unallocated proceeds.
- Issuers should provide investors in advance with information on how Green Bond proceeds will be tracked and managed.
- It is recommended that issuers keep evidenced documents which show they tracked and managed Green Bond proceeds appropriately.
- Issuers should provide investors in advance with information on how unallocated Green Bond proceeds will be managed.
- It is recommended that issuers manage unallocated Green Bond proceeds in assets with high liquidity and safety.

4. Reporting

- After issuance of a Green Bond, issuers should disclose publicly up to date information on the use of Green Bond proceeds.
- The disclosure should be made at least once a year until full allocation of the proceeds, and as necessary thereafter in the event of new developments.
- Disclosed information should include the following items.
 - A list of Green Projects to which Green Bond proceeds have been allocated
 - A brief description of each Green Project (including up-to-date progress)

- The approximate amount allocated to each Green Project
 - The expected environmental benefits of each Green Project
 - Information on unallocated Green Bond proceeds (The approximate amount of the unallocated proceeds or the share of the amount of the unallocated proceeds to the total amount of the proceeds, when the unallocated proceeds are expected to allocate to Green Projects, and how the unallocated proceeds will be managed until allocation)
- In case that Green Bond proceeds have been allocated to refinancing of existing projects, it is recommended that disclosed information include 1) the approximate amount (or the share) of the allocated proceeds to refinancing, and 2) a list of the Green Projects (or the project categories) refinanced.
- It is recommended that the disclosure be made on a project-by-project basis. In case it is difficult, for example due to confidentiality agreements, the disclosure can be made on an aggregate basis.
- Issuers should use appropriate indicators consistent with characteristics of the Green Projects etc. when disclosing information on environmental benefits.
- It is recommended that issuers, where feasible, use quantitative indicators and disclose information on methodologies and/or assumptions as well as these indicators in the quantitative determination.

5. External Review

- It is recommended that issuers use an external review in case that they need an objective assessment of the Green Bond.
- It is recommended that external institutions who give external reviews on Green Bonds show clearly which components of the bond they have reviewed, and, which evaluation criteria they have employed to review it in their review reports, etc.
- In case that issuers have their Green Bonds reviewed, it is recommended that they disclose documents showing the results of the review.
- It is recommended that external institutions who give external reviews on Green Bonds have expertise relevant to the components of the bond they review.
- It is recommended that there are no personal relationships and capital relationships between the issuers and the external institutions who give external reviews on their Green Bonds.
- It is recommended that external institutions who give external reviews on Green Bonds

show clearly their relevant expertise to the components which they have reviewed, and, their independence of the issuers.