UNEP FI Workshop on Environmental Credit Risk

4 May 2006, Copenhagen

Welcoming remarks and presentations:

Keynote Presentations:
Christian Brandt, Finansraadet (The Danish Bankers Association), welcomed participants and gave an introduction on the work of the Danish Bankers Association. Its members consist of commercial banks, savings banks, cooperative savings banks and the Danish branches of international banks.

Essentially, the mission of the Danish Bankers Association is to influence the political decision-making process. This is achieved through direct contact with politicians and authorities, and through participation in social and political debates.

Chris Bray, Barclays Bank & UNEP FI Steering Committee Member, gave a presentation on UNEP FI and its work programme. UNEP FI is the oldest in the public private partnership with 160 members in 44 countries, of which 8% are from Scandinavian countries. He announced that UNEP FI has two new projects: Biodiversity and Property.

Knut Rørbakken, Nordea AB, presented on Nordea's approach to Corporate Social Responsibility (CSR): addressing social issue is part of the group's daily business practice and for them CSR is spelled with three R's:

- Risks
- Reputation
- Relations

For Nordea CSR is equal to dialogue and multi- stakeholder approach is equal to Interdependence. As Nordea is a large corporation, regional presence, financial solidarity and prestigious brand are the base for its stakeholder relations.

Sustainability and CSR issues are now permanent strategic factors. It's more focus on structural commitment than ticking boxes.

Environmental issues are divided into the following categories: Risk Management, Internal Operations, Community Responsibility, Marketing and Products. The UN millennium development goals for financial institutions have seen an increase in shareholders activism.

Today the strategic commitments for Nordea are as follows: Corporate Citizenship, Principles, UNEP FI, and the Global Compact.

Summary

- Corporate Social Responsibility (CSR): a way for a company to maintain and develop relations with stakeholders
- CSR spelled with three Rs: Risks, Reputation and Relations
- "Building Bridges is better than building fences": Open, honest, respectful, and dynamic

Knut finished the presentation by describing UNEP FI as **U**niquely k**N**owledgeable **E**nvironmental **P**artner for **F**inancial **I**nstitutions.

Frederik Reumert, Danske Bank A/S, presented on Environmental Management at Danske Bank. Environmental profile is not high in the Danish agenda but as Danske Bank is an international organization and the international profile calls for environmental profile. Danske Bank is mainly a retail bank.

Dankse Bank's Environmental profile consist of the following:
Clear communication internally before communicating outside it has no CSR report as of yet. KMPG conducted a survey, which indicated that there is a significant trend in the financial sector environmental reporting especially in the last 3 years.

Environmental impacts fall under two categories:

- Direct environmental impacts are getting more specific such as disclosing CO2 emissions.
- Indirect environmental impacts- policy making versus risk management i.e. among commercial banks there seems to be a tendency that banks should not become policy makers; in countries without a proper regulatory framework there is a moral obligation; in the western world indirect environmental impacts should be managed from a risk management perspective and the challenge is to set up procedures to systematically manage environmental risks.

Environmental way of thinking is a priority within the organization. Internally and externally communication is very important.

The main goal for 2006 is to focus on direct environmental impacts. For Dankse bank environmental management is part of its CSR commitment.

Eva Sandberg, Alecta, gave an account of the Nordic informal network and its strategies and objectives as follows:
The purpose of meeting is to exchange experience and information regarding CSR; identify news and reports that might be of interest to the network; raise awareness of SRI and CSR within the community and companies themselves.

The network would like to discuss the following topics:

- Corporate Governance;
- News from UNEP FI and the various working groups and taskforces
- Global compact;
- ISO 26000;
- Principles for Responsible Investment.

Key outcomes are as follows:

- The duties of host alternates;
- Two annual meetings;

Carina Lundberg, Folksam, spoke as a signatory to the Principles for Responsible Investment (PRI). She explained the following:

- What is PRI?
- Why do we need PRI?
- Who is the target audience?

Chris Bray, Barclays Bank, presented on Environmental Credit Risk Assessment (ECRA). A third of Barclay's employees are based in Africa. He went on to describe Environmental Risk Management (ERM) at Barclays. ERM has been practiced at Barclays for over 10 years. The unit reports directly to the Group Credit Risk Director. The responsibilities of the unit are as follows:

- Protect the Group from material environmental risk worldwide; research is done to understand where risk will be coming from and then refer to the UK risk team;
- Integration of environmental risk into credit appraisal process: Environmental Risk is fully integrated into mainstream Business;
- Seek to influence risk related environmental legislation: a survey was conducted in the UK called the Banana skin survey. It pointed out the risks facing banks. The survey showed that ERM is normally low but now the rating has increased significantly.

Some points highlighted included the business drivers:

- Social Awareness: Climate change in every news headline
- Legislation: UK Statutory Guidance notes on contaminated land- Responsible for local government;
- Political Drivers: Environmental reporting; Naming and shaming was introduced by the UK environmental officer and Green taxation: more taxation for the environment;
- Stakeholders recognise that a bank's lending practices represent its most significant environmental impact;
- Mainstream investors (Morley, L & G, Henderson, F & C) scrutinise our approach to sustainability issues;
- Socially responsible rating agencies e.g. FTSE4Good, Dow Jones Sustainability Index
- Increasing environmental legislation;
- The rise of "corporate social responsibility" and pressure to report publicly on our "CSR" progress;
- Increasing scrutiny from NGOs, media and customers;
- Political interest.

Explanation of the types of environmental risk were given as follows:

- Direct Risk: …the potential for a lender to become legally responsible to pay for the clean-up of land or water which has been contaminated or polluted by a customer.
- Indirect Risk: …environmental costs and liabilities weaken a borrowing customer's ability to honor their financial liabilities to the bank.
- Reputational Risk: …damage to the brand may arise through association with projects deemed, or perceived, to be environmentally harmful.

Some Direct Risk examples: Bad debt, devalued or worthless security, potential costs of remediation

Some Reputational Risk examples:

- Perception is reality;
- NGOs and the media will not always let the facts get in the way of a good story or campaign.

Risk Management Tools:

- Land Use Investigation
- Environmental Impact Assessment (Equator Principles): Equator Principles are a consistent framework for establishing a robust understanding of environmental and social impacts of projects; Projects are categorised according to the perceived degree of risk/impact; Environmental and Social Impact Assessments (ESIA) are undertaken by independent environmental consultants.
- IFC Performance Standards and World Bank Guidelines provide the basis for the management standards expected in the project
- For more sensitive projects, an Environmental and Social Management Plan (ESMP) will be required to address those impacts raised in the ESIA
- Adherence to the ESMP by the project sponsor will be covenanted in the loan documentation
- Consistent and comprehensive environmental and social due diligence, improving effectiveness and efficiency in transaction
- Common framework/terminology, transparent to banks, project sponsors, legal and technical advisers, Greater certainty in 'bankability' of project financingsEnvironmental Risk Sector Guidance Notes: For business development and risk managers, Generic, i.e. worldwide application, Non-technical
- Key issues addressed: Potential Pollutants, Regulation, Environmental Risks, Social Risk Considerations.

In closing Chris Bray commented on the possible opportunities that could result in environmental credit risk assessment as identifying clients needs for capital spend, e.g. upgrading equipment to comply with permit; major corporates may seek out environmentally aware banks which understand and face similar business drivers and stakeholder expectations.

Contact
Ms. Kiki Lawal
kiki.lawal@unep.ch