Green, Social and Sustainability Bonds Standard

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Contents

Clarification note
This document contains the essentials of NN Group's Green, Social and Sustainability Bonds Standard for Proprietary Assets.

This Policy is part of the Responsible Investment Framework policy of NN Group N.V. (NN Group). Last update: April 2023.

1 Introduction to the NN Green, Social and Sustainability Bonds Standard

This standard provides insight into how we put NN's ambition and the defined impact themes into practice through investments in green,
social and sustainability bonds. NN has defined three key themes where
we can make the most environmental and social impact concerning all
our business activities and create long-term value:

- Sustainable planet
- Healthy living
- Inclusive economy

The purpose of this document is to provide the first Green, Social and Sustainability Bonds Standard for NN Group, so that current (and future) eligible investment exposure can be classified as such. As the market and regulatory standards in this area continue to evolve[1], we will regularly update this standard to keep up with best practices. This standard needs to be applied in addition to the basic responsible investment (RI) criteria as described in NN's RI Framework policy and related standards.

This standard contains the minimum requirements that external asset managers managing NN proprietary assets need to meet when classifying bonds as green, social and sustainability (GSS) bonds in NN's proprietary asset portfolio. For client assets, NN business units are encouraged to use the standard where possible and feasible.

When NN Group's proprietary assets are invested through an external asset manager, and this asset manager classifies a bond as a GSS bond, the asset manager needs to verify that the instrument is compliant with the International Capital Markets Association's (ICMA) Green Bond Principles (GBP), Social Bond Principles (SBP) and Sustainability Bond Guidelines (SBG)[2]. Asset managers are therefore advised to analyse and keep, in a readily accessible format, a Second Party Opinion (SPO) for any bond that is deemed to be a GSS bond.

Additionally, asset managers are expected to apply further assessments at the issuer level and project or sector level, to ensure GSS bonds align with NN's RI Framework policy. More on this can be found in sub-chapter 2B), Project evaluation and selection.

What are green, social and sustainability bonds?
Green bonds and social bonds are any type of bond instrument where the proceeds, or an equivalent amount, will be exclusively applied to finance or re-finance, in part or in full, new and/or existing eligible green and/or social projects.[2]

Green projects include assets, investments and other related and supporting expenditures such as research and development that provide clear environmental benefits and may relate to one or more green project categories listed in the ICMA GBP. Preferably, green projects fund EU Taxonomy eligible activities, that is, activities that substantially contribute to one or more of the six environmental objectives of the EU Taxonomy[3].

Table 1 Thresholds for classifying GSS bonds

NN classification	% of proceeds used for green projects	% of proceeds used for social projects
Green bond	>90%	<10%
Social bond	<10%	>90%
Sustainability bond	10–90%	10–90%

1 We closely follow the developments around the EU Green Bond Standard for which the final text is expected at a similar time as this standard is published.
2 Source: Green Bond Principles ICMA version June 21 (Green-Bond-Principles_June-2022-280622.pdf (icmagroup.org); Social Bond Principles ICMA version June 22 (Social-Bond-Principles_June-2022v3-020822.pdf (icmagroup.org); Sustainability Bond Guidelines ICMA version June 21 (Sustainability-Bond-Guidelines-June-2021-140621.pdf (icmagroup.org)
3 For projects to substantially contribute to environmental objectives of the EU Taxonomy they need to meet the Technical Screening Criteria (TSC) specified in Annex I of the EU Taxonomy regulation. At the moment, the TSC are specified for only two out of six environmental objectives. As the TSC are further developed, green bonds will always need to meet the TSC in order to be classified as green.

In expectation of a similar standard for activities contributing to social objectives, social projects directly aim to address or mitigate a specific social issue and/or seek to achieve positive social outcomes, especially, but not exclusively, for a target population(s).

Sustainability bonds are any type of bond instrument where the proceeds, or an equivalent amount, will be exclusively applied to finance or re-finance a combination of both green and social projects.

For bonds to be classified as green or social bonds by NN Group, the issuer needs, at a minimum, to meet the GBP or SBP criteria published by ICMA and described below. NN classifies sustainability bonds as bonds where proceeds are dedicated to both green and social projects if the issuer meets both the GBP and SBP, respectively.

Different types of green, social and sustainability bonds are defined further in relevant ICMA principles.

Important notes
Bonds that are mapped to (one of) the UN Sustainable Development Goals (SDGs), or sustainable themes or similar initiatives, do not necessarily meet the GBP or SBP criteria as mentioned in this document and the ICMA guidelines. The same applies for bonds that have a EU Taxonomy alignment goal or a sustainable investment objective under the Sustainable Finance Disclosure Regulation (SFDR). It is important that the asset manager always verifies whether all the criteria described in chapter 2 of this standard are met.

2 Green, social and sustainability bond due diligence

For NN to classify a bond as a green, social or sustainability bond, the issuer of the GSS bonds needs to adhere at least to the core components of ICMA GBP and SBP. These core components are:

a. Use of proceeds
b. Project evaluation and selection
c. Management of proceeds
d. Issuer's reporting

Asset managers that classify a bond as a GSS bond within NN's proprietary assets need to assess the GSS bond on these four core components. The ICMA GBP and SBP recommend a clear process and disclosure for issuers, for investors to fully understand the characteristics of any given GSS bond. If requested by NN Group or its business units, the asset manager is responsible for providing information on the framework used by the issuer and any legal documentation related to the security or fixed income instrument in a timely manner and a readily accessible format.

a. Use of proceeds

The asset manager needs to ensure that the issuer allocates the amount equal to the net bond proceeds to financing or re-financing of eligible green and/or social projects, as indicated in Table 1. All designated eligible green and/or social projects need to provide clear environmental and/or social benefits, which will be assessed and, where feasible, quantified by the issuer. With the social benefits of social projects, they need to preferably be targeted towards populations listed in, but not limited to, the ICMA SBP. The above needs to be appropriately described in the legal documentation of the bond.

To prevent the proceeds of GSS bonds financing projects that are in conflict with the environmental and social objectives of such bonds, the asset manager needs to ensure that the proceeds are not allocated to any assets directly linked to activities that violate NN's norms-based criteria highlighted in NN's RI Framework policy as well as activities linked to:

- Fossil fuel energy
- Nuclear energy
- Gambling
- Alcohol

b. Project evaluation and selection

Asset managers need to check the following aspects of the GSS bond[4], and explain how they conducted the checks on:

a. The environmental and/or social objectives of the green and/or social projects, including the target population of social projects.
b. The process and criteria by which the issuer determines how the projects fit within the eligible green and/or social project categories (examples are identified above), including any references to international sustainability standards and certifications.
c. Complementary and any supplementary information on processes by which the issuer identifies, manages and addresses any known, and perceived, environmental and social (sustainability) risks and adverse impacts on environmental, social and governance (ESG) factors associated with the relevant project(s), for example, environmental degradation and employee rights.
d. The bond's fit within the issuer's overarching objectives, strategy, policy and/or processes relating to environmental and/or social sustainability. It is highly encouraged that the assessment of any past issuer controversies and issuer ESG ratings supports the findings on this aspect.

4 Asset managers are also encouraged to ask issuers to have their process for project evaluation and selection supplemented with an opinion of an independent third party, preferably one with environmental and/or social expertise. Evidence of an extensive review of the issuer's process for project evaluation and selection performed by the asset manager would also suffice.

With green projects, the activities financed by the projects mentioned in aspect 2 above preferably meet EU Taxonomy eligibility requirements. That is, they should be in line with the most recent technical screening criteria (TSC) listed in the Technical Annex to the EU Taxonomy[5]. The asset manager is also encouraged to supplement its green bond analysis with criteria developed by the Climate Bonds Initiative[6].

Furthermore, in relation to aspect 2, asset managers need to describe the criteria they use in assessing whether the underlying projects achieve, or will achieve, the desired impact of the investment. These need to be put within a geographical, legal, economic and any other context relevant to the desired impact, being in line with the current market standard or establishing the best practice.

If the issuer does not meet the stipulations above, or when information is missing, the asset manager is expected to engage with the issuer. Asset managers need to provide information on whether they engage with issuers, details about the content and outcome of these engagements, and any escalation points arising from them.

c. Management of proceeds

Asset managers need to make all possible efforts to verify whether an amount equal to the net proceeds of the GSS bond is credited to a sub-account, moved to a sub-portfolio or otherwise tracked by the issuer in an appropriate manner, and attested to by the issuer in a formal internal process linked to the issuer's lending and investment operations for green or social projects. The asset manager needs to ensure that the issuer provides transparent access to the balance of proceeds at the asset manager's request.

Since it concerns internal processes, it is required that this part of the GSS bond structure is verified by an external auditor, or other third party, to sign off on the internal tracking method and the allocation of funds from the GSS bond proceeds.

It is further encouraged that the asset manager seeks transparency on the balance and investment instruments of the unallocated proceeds.

d. Issuer's reporting

For due diligence and monitoring purposes, asset managers need to verify that the issuer, at minimum annually and for the entire period the bond remains outstanding, provides readily available and up to date information on the use of proceeds, and on a timely basis in the case of material developments. This annual reporting needs to include:

- An analysis of the allocated amount versus the amount still left to be allocated, including, but not limited to, breakdown of allocated amounts per region, green and/or social categories, new versus existing projects, financing versus refinancing part of the allocation of proceeds, et cetera.
- A list of the projects to which GSS bond proceeds have been allocated and a brief description of
  - These projects;
  - The performance of green and social projects against the EU Taxonomy TSC and green project criteria, and social project criteria, respectively
  - The amounts allocated to them;
  - Their expected impact;
  - Their achieved impact.

In special circumstances, such as due to confidentiality considerations or a large number of projects, it is possible that the issuer aggregates the above information per green and/or social category.

The reporting on the expected and achieved impact needs to be supported by qualitative performance indicators, at least one quantitative performance measure (e.g. number of beneficiaries, especially from target populations) per green and/or social category and disclosure of the key underlying methodology and/or assumptions used in the quantitative determination.

Asset managers need to keep the issuer's allocation and impact reporting in a readily accessible format.

5 See further at EU taxonomy for sustainable activities (europa.eu)
6 See further at Sector Criteria | Climate Bonds Initiative

3 Other pre- and post-issuance reporting and requirements

External reviews

Pre-investment, it is highly recommended that the asset manager asks the issuer for an external review (SPO) on the GSS bond, to assess the alignment of the GSS bond with the four components mentioned in chapter 2.

Post-issuance, it is required that the issuer's management of proceeds (see sub-chapter 2C) be supplemented by the use of an external auditor, or other third party, to verify the internal tracking and the allocation of funds from the GSS bond proceeds.

Monitoring

The asset manager needs to, in line with the reporting frequency of the underlying GSS bond, but at least semi-annually, monitor whether the GSS bond instrument is still meeting NN Group's RI criteria, including the criteria mentioned in this standard.

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