

The Treasury

New Zealand Sovereign Green Bonds Programme Information Release

November 2022

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Treasury Report: Green Bonds: Determining Scope of Framework

Date:	24 February 2022	Report No:	T2022/132
		File Number:	DE-10-6-3

Action sought

	Action sought	Deadline
Minister of Finance (Hon Grant Robertson)	Agree to establish a green framework Refer a copy of this report to the Climate Response Ministerial Group members	4 March 2022

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Laura Browne	Senior Analyst, NZ Sovereign Green Bond Programme	[39]	N/A (mob) ✓
Chris White	Head of NZ Sovereign Green Bond Programme	N/A (wk)	[35]

Minister's Office actions (if required)

<p>Return the signed report to Treasury.</p> <p>Refer a copy of this report to the Climate Response Ministerial Group members</p>

Note any feedback on the quality of the report

Enclosure: No

Treasury Report: Green Bonds: Determining Scope of Framework

Executive Summary

In November 2021, Cabinet agreed to establish a Sovereign Green Bond Programme [CAB-21-MIN-0454 refers]. The cornerstone of a Green Bond (or other type of labelled bond) is the utilisation of the proceeds for eligible projects. Ahead of the first bond issuance, we need to develop an enduring framework which outlines broad categories of eligibility.

Decision on type of Framework

A substantive consideration is whether to establish the framework as a Green or Sustainable framework. Both frameworks include *Green* expenditure categories – allowing for the issuance of Green bonds. The key difference is that a Sustainable Framework also includes *Social* expenditure categories.

Treasury, with the endorsement of the Establishment Committee,¹ recommends establishing a Green Framework. Key reasons include:

- Green Frameworks have been the dominant focus of Sovereign issuers to date, with more established international best practice and guidelines.
- Implementing a Green Framework this year is already ambitious. Maintaining a focus on Green expenditure lowers some implementation risks.
- A Green Framework aligns with the intention to issue Green Bonds over the near term. The approach does not preclude the programme from evolving into a Sustainable framework in the future.

Possible categories of expenditure

Categories under a Green Framework could include Clean Transport, Energy Efficiency, Climate Change Adaptation, Biodiversity, Living Natural Resource and Land Use, and Sustainable Water and Waste-water Management.

As Minister, you make decisions about the categories and eligibility criteria for expenditure (as part of the overall framework development), however it is an operational decision whether a particular project meets the criteria for inclusion.

Next steps

The key milestones and planned points of engagement in 2022 are:

Timing	Milestone	Comment
April	Advice on proposed categories of expenditure and eligibility criteria	We recommend you use the Climate Response Ministerial Group as a forum to engage your Ministerial colleagues.
Late June	Advice on the near-final Framework	Subject to your agreement, we will prepare a draft Cabinet paper.
August	Cabinet process	We recommend you take the final Framework to Cabinet in early August.
Late August	Public release of the Framework	We are interested to test with your office the likely scale and scope of the announcement.
Late 2022	First bond issuance	

¹ The NZ Sovereign Green Bonds Establishment Committee has been formed to provide oversight and guidance during the project's establishment phase, with members drawn from Treasury's executive team, markets and senior leaders from key public sector agencies.

Recommended Action

We recommend that you:

- a **note** that in November 2021, Cabinet agreed to establish a Sovereign Green Bond Programme, with the inaugural bond issuance in late 2022 [CAB-21-MIN-0454 refers]

Type of framework

- b **note** that the Treasury recommends establishing a Green Bond Framework rather than including *social* expenditure categories (i.e. a Sustainable Bond Framework)
- c **agree** to establish the framework as a Green Bond Framework
Agree / Disagree.

Next steps

- d **agree** to use the Climate Response Ministerial Group through the development of the framework
Agree / Disagree.
- e **indicate** if you would like us to prepare talking points ahead of the upcoming meeting of the Climate Response Ministerial Group on 2 March 2022
Yes / No.

Update on Public Release

- f **indicate** whether you (or a different Minister) would like to lead the public announcement of the Framework in late August 2022
Yes / No.
- g **note** we will work with your office around options for the announcement
- h **refer** a copy of this report to the Climate Response Ministerial Group.
Refer / do not refer.

Chris White
Head of NZ Sovereign Green Bond Programme

Hon Grant Robertson
Minister of Finance

Treasury Report: Green Bonds: Determining scope of framework

Purpose of Report

1. In November 2021, Cabinet agreed to establish a Sovereign Green Bond Programme [CAB-21-MIN-0454 refers]. As part of the announcement, it was signalled that final details of the Sovereign Green Bond programme would be announced in mid-2022, followed by an inaugural issuance in late 2022.
2. This report seeks a decision on whether to establish the framework for the labelled bond programme as either a Green or Sustainable Bond Framework. It also provides an initial overview of potential green and social expenditure categories, clarifies decision-making responsibilities, and seeks your input on the announcement of the framework.

Context

3. The Green Bonds Project Team, within the Capital Markets directorate in the Treasury, is leading work developing the framework. Bank of New Zealand and Deutsche Bank AG were appointed as joint structuring advisers on 16 December. As well as using these advisers, the team is considering global best practice, the experience of comparable countries that have already issued green bonds, as well as considering New Zealand specific elements.
4. The New Zealand Sovereign Green Bonds Establishment Committee has been formed to provide oversight and guidance during the project's establishment phase. With members from Treasury's executive team, markets and key public sector agencies (senior leaders from Ministry for the Environment, Ministry of Transport and Waka Kotahi), the group is providing strategic guidance and enabling cross-agency perspectives and collaboration which will be crucial in establishing a workable framework.
5. We have also commenced work to explore how a Sovereign New Zealand issuance and framework could reflect our unique characteristics including the status of Māori as tangata whenua and the importance of Te Taiao environment to Māori.
6. A labelled bond programme is a financing instrument and does not provide an alternate or additional funding source, rather it is a new source of financing. Projects that could be included in the bond will need to have first secured approval for funding either through the Budget process or from within agency baselines.

Decision on type of Framework

7. The cornerstone of a labelled bond is the utilisation of the proceeds for eligible projects. Ahead of the first issuance, we need to develop an enduring framework which outlines broad categories of eligibility (Use of Proceeds categories). A substantive consideration is whether to establish the framework as a Green or Sustainable Bond Framework. Both allow for issuance of Green Bonds.
8. Green and Sustainable Bond Frameworks both include *Green* categories of expenditure. The key difference is that Sustainable Frameworks include additional *Social* expenditure categories. Social categories require the identification of target populations that benefit from eligible expenditures. Examples of social categories include affordable basic infrastructure, employment generation, and access to essential services.

We recommend establishing a Green Framework

9. Treasury, with the endorsement of the Establishment Committee, recommend establishing a Green Framework. There are a number of considerations in reaching this recommendation.
10. **Green Frameworks have been the dominant focus of developed nation Sovereign issuers to date.** There are clear precedents, with established international best practice and guidelines – particularly around impact reporting. Most developed nation Sovereigns that have issued labelled bonds have established Green Frameworks including the United Kingdom and Ireland. However, Sustainable Frameworks have been issued by Luxembourg, Slovenia and South Korea.
11. **Implementing a Green Framework this year is already an ambitious project** in terms of the scope of activity required for establishment and implementation. This includes developing, testing and agreeing reporting and monitoring requirements with a range of different agencies and projects. While key agencies including Ministry of Transport, Waka Kotahi and crucially Ministry for the Environment are supportive and active in the programme Establishment Committee, we are aware there is considerable activity in the system this year including publication of the Emissions Reduction Plan by May 31, implementation of CERF funding and completion of the National Adaption Plan due in August.
12. **Maintaining a focus on Green expenditure lowers some implementation risks.** Expanding the breadth of the programme to include social expenditure would require involvement and coordination across a wider group of agencies. There are also risks in placing new monitoring and reporting requirements at a time where we are aware the system is largely already at capacity (particularly given the system pressures stemming from the response to COVID-19).
13. **Establishing a Green Framework aligns with the intention to issue Green Bonds over the near term.** It supports the work of the ERP and NAP and aligns to the Government's stated commitment to address Climate Change. NZDM has also indicated that consideration should be given to whether splitting our Bond offering into further slices (e.g. Social bonds and Green Bonds in addition to conventional NZ Government Bonds and Inflation Indexed Bonds) is desirable given the size of our funding programme.
14. **This approach does not preclude the programme from evolving.** Part of the ongoing role of implementing the framework is identifying opportunities for development and supporting the broader system to be ready if the decision is taken to extend the framework to include social expenditure. Evolving the programme later would also allow us to build on experience with reporting and monitoring Green Bonds and provide more mature guidance around Social Bonds.
15. We acknowledge however that there are merits to both approaches. A Sustainable Framework could provide an opportunity to show market leadership, would allow greater flexibility (i.e. could issue either Green, Social or Sustainability bonds²), and encompass a broader pool of expenditure.
16. Electing for a Sustainable framework at this stage will likely push out the timelines for the release of the framework and given the additional complexity involved additional resource will be required. The first bond issuance would still likely be feasible in late 2022.

² Sustainability bonds include both green and social expenditure.
T2022/132 Green Bonds: Determining Scope of Framework

Categories of expenditure

17. The decision to proceed with a Green or Sustainable framework is critical for the development of expenditure categories and eligibility criteria, and in turn reporting and monitoring. Other aspects of the Framework such as governance arrangements would largely be the same under either approach.
18. The scope of either programme is likely to be significant. We have discretion around which categories of expenditure to include, however the International Capital Market Association (ICMA) provides detailed guidance around ten established green categories and six social categories.
19. As we develop the categories, we will need to balance factors particular to the New Zealand context and what will be acceptable to domestic and international investors.
20. From a practical sense, the categories must be sufficiently broad to generate enough eligible expenditure which can be tracked, with the ability to measure impacts. Agencies will have additional reporting and monitoring obligations to demonstrate the impact of the expenditure on defined environmental or social metrics. This will be published as part of the allocation and impact reporting for the bond.
21. As part of the process to determine the categories, we will also develop eligibility criteria, which will help shape the types of projects that could be included in the bond.
22. In terms of where decision-making responsibilities sit:
 - a **Defining the categories of expenditure and the eligibility criteria** requires Ministerial endorsement as part of the Framework.
 - b **Deciding whether specific projects meet the eligibility criteria** to be included in the pool of expenditure for the Bond is an operational decision determined by officials and an inter-agency board. The structure and role of this group will be agreed as part of the Framework.

Potential Green Categories

23. There are some common themes amongst sovereign issuers in terms of Green categories. Ireland and the UK both selected five green categories – four of which overlapped. Due to the significant quantum of spend, Clean Transport expenditure has formed a significant share of the overall issuance in many examples.
24. Potential green categories and possible eligible expenditure that we are exploring span a broad range of agencies and Ministerial portfolios. Areas to work through include, for example, whether to include a separate category around sustainable water and wastewater management or whether to include water related expenditure in a broader category.

Potential Green categories of expenditure	Likely Ministerial Portfolios
Clean Transport	Transport
Energy efficiency Climate change adaptation	Climate Change; Energy and Resources; Foreign Affairs; Building and Construction; Emergency Management; Research, Science and Innovation
Terrestrial and aquatic biodiversity conservation projects Environmentally sustainable management of living natural resources and land use Sustainable water and waste-water management	Environment; Agriculture; Conservation; Biosecurity; Forestry; Local Government (water); Oceans and Fisheries

Potential Social Categories

25. Social categories are less established than their green counterparts. As such, guidance around methodology is still developing. According to ICMA, *“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). A social issue threatens, hinders, or damages the well-being of society or a specific target population.”* (ICMA – Social Bond Principles June 2021)
26. Examples of target populations include people living in poverty, people with disabilities, unemployed people, aging populations or vulnerable youth. The guidance however notes that in some circumstances, target populations may also be served by addressing the general public (e.g. through building a hospital).
27. The following table outlines four social categories that we could explore, alongside the Ministerial portfolios likely to contain eligible expenditure.

Potential Social categories of expenditure	Possible Ministerial Portfolios
Affordable basic infrastructure (e.g. clean drinking water, sanitation, transport, energy)	Social Development and Employment; Education; Health; Housing
Access to essential services (e.g. health, education and vocational training, healthcare, financing and financial services)	Children; Disability Issues; Seniors; Women; Youth
Employment generation	Māori Development; Pacific Peoples; Whānau Ora
Socioeconomic advancement and empowerment (e.g. equitable access to and control over assets, services, resources, and opportunities; equitable participation and integration into the market and society, including reduction of income inequality)	Business, Science and Innovation; Digital Economy and Communications; Small Business

28. The potential scope of the social categories may allow some expenditure that would otherwise be included in green categories to instead be included in a social category. An example of this may be expenditure relating to public transport.
29. One practical limitation when looking at social categories is that Kāinga Ora issues their own Sustainability bonds. This constrains the scope of Social Housing expenditure that could be included in any Sovereign bond (to avoid double counting). There could be a similar consideration in relation to expenditure included in Auckland City Council’s Green Bond programme.

Next Steps

30. The key milestones and planned points of engagement in 2022 are:

Timing	Milestone	Comment
April	Advice on proposed categories of expenditure and eligibility criteria	We recommend you use the Climate Response Ministerial Group as a forum to engage your Ministerial colleagues.
Late June	Advice on the near-final Framework	Subject to your agreement, we will prepare a draft Cabinet paper.
August	Cabinet process	We recommend you take the final Framework to Cabinet in early August. Note that the timeline to report back to Cabinet is slightly later than originally signalled in November 2021, however the timeframe for public release remains consistent.
Late August	Public release of the Framework	We are interested to test with your office the likely scale and scope of the announcement.
Late 2022	First bond issuance	

Potential role of the Climate Response Ministerial Group

31. Given the importance of determining categories and eligibility, we think it will be important to engage your Ministerial colleagues as the categories of expenditure develop. The Climate Response Ministerial Group membership covers the ministerial portfolios that are most likely to have expenditure included in green categories. Broader engagement for the social expenditure categories would also be required if you elect to develop a sustainable framework at this stage.
32. We recognise that the Climate Response Ministerial Group has a busy programme of work. However, we recommend the following – relatively light touch – engagement to ensure any views on the proposed categories can be considered as the framework develops.
- a *March* – provide a short update on the programme at an upcoming meeting. We can provide suggested talking points if required.
 - b *Early May* – seek feedback on proposed categories of expenditure given the likely implications for agencies (additional monitoring and reporting). Note that the focus of this discussion should be on the *categories* rather than the *expenditure*. The advice we provide you in April could form the basis of a paper for this group.
 - c *Early July* – provide a short update on the near-final Framework ahead of the Cabinet process.

Public announcement

33. We are interested to explore with your office the likely scale and scope of framework announcement. Public launch of the framework could occur in late August and presents an opportunity for ministerial announcement or for announcement by NZDM. We would appreciate your consideration of whether you would make the announcement (potentially with other Ministers) and if so whether you have a preference on timing.

34. Announcement materials will be developed in any announcement scenario. We have commenced work on brand and visual identity to create a credible product able to be marketed internationally while reflecting the unique aspects a New Zealand Aotearoa programme brings.
35. As well as announcement of the framework, there is a further opportunity to announce the first issuance later in 2022.