‘Second Opinion’ on Sunndal Sparebank´s Green Bond Framework

December 21th, 2018

Summary

Sunndal Sparebank's Green Bond Framework (GBF) together with its climate and environmental policies provide a good base for climate-friendly investments. Overall, CICERO finds the framework to be aligned with the Green Bond Principles.

The green bond framework lists eligible projects which promote the transition to low carbon, climate resilient growth and a sustainable development in Norway. Proceeds will fund renewable energy and clean transportation. Green bond proceeds can be used to finance both new loans as well as to refinance existing loans. Sunndal Sparebank has informed CICERO that the aim is to allocate about 70 % of the proceeds to the refinancing of loans connected to existing run-of-river hydropower plants. CICERO is encouraged to see that about 30 % of the proceeds in Sunndal Sparebank's green bond framework will be allocated to clean transportation solutions, such as electric vehicles. According to the issuer, all bonds issued under this framework will meet two Sustainable Development Goals (SDGs), goal 7, Affordable and Clean Energy, and goal 13, Climate Action.

Sunndal Sparebank's green bond framework is compliant with the Green Bond Principles and has good governance and management structures in place. CICERO considers it a strength that the issuer has green loan products in its lending policy in order to use its lending activities to contribute to sustainable electricity and transport solutions. CICERO takes note that, regarding the process for the selection of eligible projects, there is no formal environmental competence involved, which would be relevant especially regarding the financing of hydropower projects. These concerns are, however, reconciled by the clarity and narrow definition of the project categories, and by the issuer's confirmation that controversial hydropower projects will lose their eligibility to receive green bond financing. In general, it would be a benefit to have environmental competence as part of the bank's team. The framework includes transparent reporting on green bond projects to investors and the public. This will include third party verification of the reported installed renewable electricity capacity. CICERO encourages the issuer to formalize ambitions and intentions regarding the raising of awareness of environmental and climate issues inside the bank and towards its customers.

Based on the overall assessment of the project types that will be financed by the green bonds as well as governance and transparency considerations, CICERO rates Sunndal Sparebank's Green Bond Framework as Dark Green.

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1 Introduction and background

The global Expert Network on Second Opinions (ENSO), a network of independent non-profit research institutions on climate change and other environmental issues, was established by CICERO (Center for International Climate and Environmental Research – Oslo) to broaden the technical expertise and regional experience for second opinions. CICERO works confidentially with other members in the network to enhance the links to climate and environmental science, building upon the CICERO model for second opinions. In addition to CICERO, ENSO members include Basque Center for Climate Change (BC3), International Institute for Sustainable Development (IISD), Stockholm Environment Institute (SEI), and Tsinghua University's Institute of Energy, Environment and Economy.

This Second opinion was produced by SEI and CICERO on behalf of ENSO. SEI is an independent international research institute that has been engaged in environment and development issues at local, national, regional and global policy levels for more than 25 years. CICERO is an independent, not-for-profit, research institute, focused on providing reliable and comprehensive knowledge about all aspects of the climate change problem. A more detailed description of each of these institutions can be found at the end of this report. SEI and CICERO are both independent of the entity issuing the bond, its directors, senior management and advisers, and is remunerated in a way that prevents any conflicts of interests arising as a result of the fee structure.

The CICERO-led ENSO provides second opinions on institutions' framework and guidance for assessing and selecting eligible projects for green bond investments, and assesses the framework's robustness in meeting the institutions' environmental objectives. The second opinion is based on documentation of rules and frameworks provided by the institution themselves (the client) and information gathered during meetings, teleconferences and email correspondence with the client. ENSO encourages the client to make this Second Opinion publicly available. If any part of the Second Opinion is quoted, the full report must be made available.

ENSO's Second Opinions are normally restricted to an evaluation of the mechanisms or framework for selecting eligible projects at a general level. ENSO network members do not validate or certify the climate effects of single projects, and thus, has no conflict of interest in regard to single projects. Network members are neither responsible for how the framework or mechanisms are implemented and followed up by the institutions, nor the outcome of investments in eligible projects.

This note provides a Second Opinion of Sunndal Sparebank Green Bonds Framework and policies for considering the environmental impacts of their projects. The aim is to assess the Sunndal Sparebank Green Bonds Framework as to its ability to support Sunndal Sparebank`s stated objective of promoting the transition to low-carbon and climate resilient growth.

This Second Opinion is based on the green bond framework presented to ENSO by the issuer. Any amendments or updates to the framework require that ENSO undertake a new assessment. ENSO takes a long-term view on activities that support a low-carbon climate resilient society. In some cases, activities or technologies that reduce near-term emissions result in net emissions or prolonged use of high-emitting infrastructure in the long-run. ENSO strives to avoid locking-in of emissions through careful infrastructure investments, and moving towards low- or zero-emitting infrastructure in the long run. Proceeds from green bonds may be used for financing, including refinancing, new or existing green projects as defined under the mechanisms or framework. ENSO assesses in this Second Opinion the likeliness that the issuer's categories of projects will meet expectations for a low carbon and climate resilient future.

Expressing concerns with 'shades of green'

CICERO/ENSO Second Opinions are graded dark green, medium green or light green, reflecting the climate and environmental ambitions of the bonds and the robustness of the governance structure of the Green Bond Framework. The grading is based on a broad qualitative assessment of each project type, according to what extent it contributes to building a low-carbon and climate resilient society. The shading methodology also aims at providing transparency to investors when comparing green bond frameworks exposure to climate risks. A dark green project is less exposed to climate risks than a lighter green investment.

This Second Opinion will allocate a 'shade of green' to the green bond framework of Sunndal Sparebank:

- **Dark green** for projects and solutions that are realizations today of the long-term vision of a low carbon and climate resilient future. Typically, this will entail zero emission solutions and governance structures that integrate environmental concerns into all activities.
- **Medium green** for projects and solutions that represent steps towards the long-term vision, but are not quite there yet.
- **Light green** for projects and solutions that are environmentally friendly but do not by themselves represent or is part of the long-term vision (e.g. energy efficiency in fossil-based processes).
- **Brown** for projects that are irrelevant or in opposition to the long-term vision of a low carbon and climate resilient future.

Assessing governance

In assessing the governance quality of the issuer, four aspects are studied: The policies and goals of relevance to the green bond framework; the selection process used to identify eligible projects under the framework, the management of proceeds and the reporting on the projects to investors. Based on these aspects, an overall grading is given on governance strength falling into one of three classes: Fair, Good or Excellent.

Overall shading

The project types that will be financed by the green bond primarily define the overall grading. However, governance and transparency considerations are also important because they give an indication whether the institution that issues the green bond will be able to fulfil the climate and environmental ambitions of the investment framework. Hence, the governance assessment plays a role in the overall shading of the framework. Investments in all shades of green projects are necessary in order to successfully implement the ambition of the Paris agreement. The overall shading reflects an ambition of having the majority of the project types well represented in the future portfolio, unless otherwise expressed by the issuer.

2 Brief Description of Sunndal Sparebank's Green Bond Framework and rules and procedures for climate-related activities

Sunndal Sparebank is a local savings bank from Sunndalsøra in Western Norway. Sunndal Sparebank was established in 1892, to support the agricultural activities in the local community. The bank is able to lend to private customers across Norway while lending to corporate customers is restricted to its local country of Møre and Romsdal.

According to the issuer, Sunndal Sparebank is committed to contribute to the goal of achieving a sustainable future. In this context the bank refers to the UN Sustainability goals and the Paris climate agreement. The bank is aware of the future challenges related to climate change. The bank has informed CICERO that it intends to raise awareness of climate and environmental related issues in the future, especially among customers in the small and medium sized enterprise segment. As of today, there are no formalized routines in place to enact this ambition.The bank's headquarter building was certified under the "Miljøfyrtårn" standard, a Norwegian certification scheme for environmental management. In this context, energy efficiency and waste management improvements have been undertaken in the main building. The heating system has been switched to use waste heat from Hydro Aluminum's Sunndal plant. Moreover, the bank prepares annual reports on its direct climate and environmental impacts, tracking a.o. the number of flights and amount of sorted waste.

Sunndal Sparebank currently does not have any systems to track the greenhouse gas emissions of its loan portfolio. Therefore, the bank has adopted climate friendly loan products for private and corporate customers that are clearly framed within the bank's lending policy. These loans can only finance electric vehicles, vehicles powered by hydrogen, and hydro-, solar and wind power projects. Regarding hydropower projects, the bank will finance run-of-river projects only. The Bank has informed CICERO that under its green loan policy, private customers can be offered a lower interest rate compared to non-green loans, provided a positive credit risk assessment of the individual loan is available.

Sunndal Sparebank has informed CICERO that all bonds issued under this framework will support the Sustainable Development Goals (SDGs). The Green Bond Framework targets two SDGs, namely goal 7, Affordable and Clean Energy and goal 13, Climate Action.

Use of proceeds:

The net proceeds will be used to finance or re-finance eligible projects in part or in full. The framework specifies two categories within the field of climate mitigation: Renewable energy and clean transportation. The issuer has informed CICERO that approximately 70 percent of the funds will be allocated to the refinancing of loans connected to five existing run-of-river hydropower plants. The issuer informed us that all these plants have an installed capacity of under 5 MW each, and a total combined capacity of under 10 MW. These plants were constructed in the period 2004-2014. For potential future projects connected to green bonds under this framework, the bank will finance small run-of-river projects only. The remaining 30 percent of green bond proceeds will be allocated to new loans in the clean transportation category.

Green bond proceeds will not be allocated to projects that contribute to serious environmental damage, corruption, violate human and labor rights or involve other acts that may be perceived as unethical. The assessment of what constitutes projects that fall under these criteria is carried out by the bank itself. Under this Green Bond Framework, Sunndal Sparebank will not fund nuclear or fossil energy generation, mining or the oil and gas industry.

Selection:

The selection process is a key governance factor in the Green Bond Principles. CICERO considers how climate and environmental considerations are taken into account when evaluating whether projects can qualify for green bond funding. The Sunndal Sparebank's green bond framework outlines a transparent selection procedure.

According to Sunndal Sparebank, a two-step approach will be applied in selecting the projects for green bond funding.

In a first step, the bank's loan officers assess and approves whether a loan to a private or corporate client qualifies as a green loan. Loans need to comply with the project categories described in the green bond framework and the bank's lending policy for green loans. All approved green loans are added to a green registry in order to track which projects or assets have been financed by green loans. This applies to both new and refinanced loans. According to the framework, the loan officers will receive training in order to identify, register and track green loans.

In a second step, the registry of selected loans will be presented to a newly established green bond committee on a quarterly basis. The committee consists of three members: Chief Executive Officer, Risk and Compliance Officer and Chief Operating Officer. These members represent the treasury, lending and credit units. The committee will check the eligibility of each loan, remove loans that do not fulfill the requirements, and approve the green registry. The committee will also remove projects that have provoked a controversy from the green registry, e.g. controversial hydropower projects, according to the issuer. All decisions in connection with this process are documented and filed together with the final green registry. According to the issuer, the environmental expertise lies with the Chief Operating Officer, who has been responsible for following up the environmental certification "Miljøfyrtårn" process. CICERO was made aware that the Chief Operating Officer does not have formalized environmental competence.

Management of proceeds:

Sunndal Sparebank will transfer all net proceeds from Green Bonds to a designated account. The net proceeds in this account will be directly linked to the predetermined eligible loans and, by extension, projects. The Finance Department is responsible for ensuring that the net proceeds are financing eligible green projects in accordance to the Green Bond Framework. The portfolio of green loans will be reviewed on a quarterly basis and the issuer will document all transfers to and from the portfolio and insure that there are sufficient green projects in it. Unallocated proceeds will be temporarily placed preferably in green funds / Green Bonds listed at Oslo Børs or in an ordinary bank account.

Transparency and Accountability:

Transparency, reporting, and verification of impacts are key to enable investors to follow the implementation of green bond programs. Procedures for reporting and disclosure of green bond investments are also vital to build confidence that green bonds are contributing towards a sustainable and climate-friendly future, both among investors and in society.

Sunndal Sparebank commits to regular reporting at least on an annual basis until full allocation of proceeds is accomplished. The report will be available on Sunndal Sparebank's website. The report will include, but is not limited to, the number of outstanding green bonds, the allocation of proceeds between project categories, the amount of unallocated proceeds and impacts achieved by the green bond. For renewable energy projects, the amount of installed Mega Watt (MW) will be reported. For the clean transportation category, the issuer will report on the number of electric and hydrogen vehicles financed. Reporting on both project categories may include further indicators than those stated here. The bank will not report on all individual projects due to confidentiality concerns. In this context, the bank's auditor will verify the physical existence of reported installed renewable generation capacity. This verification will be included in the reporting, according to the issuer.

In addition to the green bond report, the issuer will make the green bond framework and this second opinion publicly available on its website.

The table below lists the documents that formed the basis for this Second Opinion:

Document Number	Document Name	Description
1	Sunndal Sparebank's Green Bonds Framework, 2018	This document comprises Sunndal Sparebank's Green Bonds Framework and how it intends to use proceeds, how it plans to evaluate and select eligible projects, manages the proceeds and reports to investors.
2	Sunndal Sparebank's Credit Handbook (Kredithåndbok) 08.11.2018	This document elaborates on Sunndal Sparebank's credit policy and details related to personal and corporate loans.
3	Annual Climate and Environmental Report 2017	This document reports on the Miljøfyrtårn certification criteria future health, environment and safety targets.
4	Miljøkartlegging Sunndal Sparebank, 2017	This document outlines the criteria for Miljøfyrtårn recertification and explains how Sunndal Sparebank addresses them.

Table 1. Documents reviewed

3 Assessment of Sunndal Sparebank's Green bond framework and environmental policies

Overall shading

Based on the project category shadings detailed below, and consideration of the issuer's sustainability work, governance structure and transparency considerations, the Sunndal Sparebank green bond framework is rated **CICERO Dark Green**. The renewable energy category is shaded Dark Green. The clean transportation category is shaded Dark to Medium green.

Eligible projects under the Green Bond Framework

At the basic level, the selection of eligible project categories is the primary mechanism to ensure that projects deliver environmental benefits. Through selection of project categories with clear environmental benefits, green bonds aim to provide certainty to investors that their investments deliver environmental returns as well as financial returns.

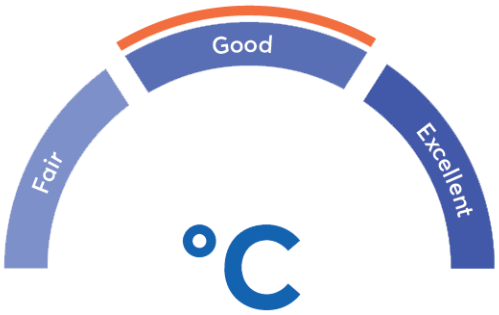
Category	Eligible project types	Green Shading and some concerns
Renewable energy 	• Small scale run-of-river hydropower projects, wind- and solar power projects • Supportive infrastructure, e.g. ○ Access roads, intake, turbine houses etc.	**Dark Green** ✓ Only run of river plants with without dam reservoirs are eligible for financing. In general, however, care should be taken to minimize any negative impacts on wildlife, biodiversity and landscapes. ✓ To the extent of the issuers influence, construction or upgrading of access roads for new projects should be kept to a level that ensures the proper functioning of the project but that does not encourage increased car use by the local population, and emissions from construction of potential new projects should be minimized ✓ Mind land-use issues that may arise from building wind and solar plants. Mind potential negative impacts on biodiversity linked to wind power plants.
Clean transportation 	• Light and heavy electric vehicles	**Dark to Medium Green** **Dark Green** ✓ Due to a high share of hydropower in Norway's electricity mix (ca. 94%), the charging of electric vehicles is based on largely fossil free electricity.

	• Light and heavy hydrogen vehicles	**Medium Green** ✓ The production of hydrogen in Norway as of now involves the use of natural gas and thus emits greenhouse gasses. ✓ An alternative method to produce hydrogen using renewable electricity exists. This is currently not price competitive. The increase in renewable intermittent capacity raises the feasibility of the application of this method in the future.

Table 2. Eligible project categories

Governance assessment

In assessing the governance quality of the issuer, four aspects are studied: The policies and goals of relevance to the green bond framework (1), the selection process used to identify eligible projects under the framework (2), the management of proceeds (3) and the reporting on the projects to investors (4). Based on these aspects, an overall grading is given on governance strength falling into one of three classes: Fair, Good or Excellent.



The overall assessment of the governance structure of Sunndal Sparebank gives it a rating of Good. Sunndal Sparebank has appropriate policies and strategies to support the green bond framework. The bank conducts annual climate and environmental reporting for its own premises, in line with Miljøfyrtårn certification. The project categories are specific and clear. Sunndal Sparebank's team would benefit from having formal environmental competence, especially regarding the financing of hydropower projects. However, the issuer has confirmed that the green bond committee will remove controversial projects from the green loan registry. We welcome that unallocated proceeds will, to the extent feasible, be invested in green bonds at the Oslo stock exchange. The issuer commits to annual reporting to investors that includes the financed amount of renewable electricity generation capacity and the number of financed electric or hydrogen powered vehicles. Reporting will be done on a best-effort basis, however not on individual projects due to confidentiality considerations. The issuer has confirmed that, in order to provide assurance, the bank's external auditor will verify the physical existence of the reported total amount of installed renewable capacity. The auditor's verification will be included in the green bond reporting, according to the issuer.

Strengths

Governance

CICERO is encouraged to see that Sunndal Sparebank has green loan products in its lending policy in order to use its lending activities to contribute to sustainable electricity and transport solutions. We take note of the announcement that Sunndal Sparebank intends to use its position to raise awareness of climate and environment related issues especially among its SME clients. We encourage the issuer to formalize these ambitions.

The issuer will not report on single projects due to confidentiality considerations and the availability of data. Sunndal Sparebank has confirmed that third part verification of the reported installed renewable capacity will be included in the green bond reporting, thereby giving assurance to investors.

Project categories

CICERO takes a long-term view on climate change, and thus recommends excluding projects that support prolonged use of fossil fuel-based infrastructure that will contribute to emissions in the long run. The issuer has explicitly stated in their green bond framework net proceeds will not be allocated or linked to fossil energy generation, nuclear energy generation or potentially environmentally negative resource extraction.

Project categories under Sunndal Sparebanks green bond framework are clearly defined. Norway has committed to a 40 percent reduction in emissions by 2030 as part of its contribution to the Paris Agreement. Emissions from the transportation sector have gradually increased in Norway since 1990 and the greatest source of greenhouse gas emissions is road traffic, mostly related to private vehicles. CICERO is encouraged to see that a 30 % share of the proceeds in Sunndal Sparebank's green bond framework will be allocated to clean transportation solutions, such as electric vehicles.

Investments in renewable energy are key to the low-carbon transition. Increased electrification of previously fossil driven sectors, such as transport, and emergence of new sectors, such as data centers, are expected to increase demand for electricity.

Weaknesses

There are no apparent weaknesses in the framework.

Pitfalls

Governance

CICERO considers the issuer's broad climate and environmental policies, goals and achievements to support the context of the green bond framework. Sunndal Sparebank's green bond framework shows that appropriate and relevant intentions and ambitions are in place. However, CICERO encourages the issuer to formalize these ambitions, to improve the environmental competence in the bank and to consider defining environmental targets and resilience policies. In this context, we see it as encouraging that the bank is planning to increase the competence of the lending department in environmental and climate matters through courses.

The issuer does not apply any environmental or social scrutiny of hydropower projects beyond the requirements defined by the regulatory authority NVE. We consider NVE's standards to be sufficient regarding the management of environmental and social impacts. However, opposition to single projects may arise. The issuer has therefore assured us that projects which provoke a controversy will be removed from the green loan registry by the green bond committee.

Project categories

An investment category that includes technologies that are realizations today of the long-term vision of a low carbon and climate resilient future is considered dark green. Typically, this will entail solutions such as zero emission public transportation like trains and trams. Sunndal Sparebank's green bond proceeds allocated to renewable energy projects and electric vehicles would also be examples of such dark green solutions.

The upgrading and construction of hydropower assets and related infrastructure are currently considered to be activities that are consistent with a transition towards a low-carbon world. However, as technologies continue to evolve in the energy sector, it is important to consider potential lock-in of obsolete technologies. Run-of-river hydropower projects are often located in pristine environments and any unnecessary interventions should be avoided. The issuer has informed CICERO that around 70 percent of the proceeds from the renewable energy

category will be allocated to refinancing small hydropower projects. CICERO encourages Sunndal Sparebank to include environmental competence within its team, especially regarding the financing of new hydropower projects.

The Norwegian electricity system is mostly powered by renewable hydropower and regulations for the rollout of electric vehicles have been very successful. Developing transport technologies that imply higher emission levels may be seen as a setback. In this context, medium green covers technologies that represent steps towards the long-term vision but are not quite there yet since they partly still run on fossil fuels. Examples of such technologies are hydrogen production from natural gas.

Hydrogen production in Norway relies to a large extent on natural gas, but cleaner alternatives are developing and hydrogen production from renewable energy sources has the potential to expand in the future. It is uncertain whether CO_2 emissions generated from natural gas based hydrogen production and its use in transportation today are significantly lower when compared to CO_2 emissions from petrol- and diesel-powered cars. If the production of hydrogen adopts existing techniques that do not use natural gas, emissions from the use of hydrogen in transportation can be drastically reduced. In the meantime, hydrogen is a positive alternative fuel for currently diesel-powered heavy transportation, a.o. due to the absence of exhaust gasses affecting local air quality, like NOx emissions, and since electric alternatives in this segment are only just emerging.

Impacts beyond the project boundary

Due to the complexity of how socio-economic activities impact the climate, a specific project is likely to have interactions with the broader community beyond the project borders. These interactions may or may not be climate-friendly, and thus need to be considered with regards to the net impact of climate-related investments.

Appendix:
About CICERO

CICERO Center for International Climate Research is Norway's foremost institute for interdisciplinary climate research. We deliver new insight that helps solve the climate challenge and strengthen international climate cooperation. We collaborate with top researchers from around the world and publish in recognized international journals, reports, books and periodicals. CICERO has garnered particular attention for its work on the effects of manmade emissions on the climate and the formulation of international agreements and has played an active role in the UN's IPCC since 1995.

CICERO is internationally recognized as a leading provider of independent reviews of green bonds, since the market's inception in 2008. CICERO Second Opinions won several international prizes, including an award from Climate Bonds Initiative for being the biggest second opinion provider (2017) and two awards from Environmental Finance for being the best external review provider (2017, 2018).

CICERO Second Opinions are graded dark green, medium green and light green to offer investors better insight in the environmental quality of green bonds. The shading, introduced in spring 2015, reflects the climate and environmental ambitions of the bonds in the light of the transition to a low-carbon society.

CICERO works with both international and domestic issuers, drawing on the global expertise of the Expert Network on Second Opinions. Led by CICERO, ENSO is comprised of trusted research institutions and reputable experts on climate change and other environmental issues, including the Basque Center for Climate Change (BC3), the Stockholm Environment Institute, the Institute of Energy, Environment and Economy at Tsinghua University and the International Institute for Sustainable Development (IISD). ENSO operates independently from the financial sector and other stakeholders to preserve the unbiased nature and high quality of second opinions.

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