Response to Consultation Paper on EIB's approach to supporting climate action

16 March 2015

1) Scope of the revision

a) Climate Policy encompassing the whole portfolio

The draft version of the new EIB Climate Policy recently presented for consultation with the public to which this submission is a response states that the aim of this process is to "conduct a formal review of its approach to climate action".

In June 2014, the European Council confirmed the validity and importance of the EU 2050 objectives for greenhouse gases emission reductions. At the European Council in October 2014 it was further agreed that by 2030 the EU will increase energy efficiency by at least 27 percent (compared to projections based on PRIMES 2007), cut emissions by at least 40 percent (compared to 1990 levels) and provide at least 27 percent of the EU's energy

consumption from renewable sources. The EU cannot follow this path unless the EIB both addresses the total climate impact of its financing operations within and outside the EU and drastically reduces the GHG impact of its loans in the short, medium and long-term.

We would like to refer to the executive summary of the report released on 3rd March 2015 by the European Environment Agency (EEA)1 taking stock of the state of the EU climate and environmental policies and providing a science based outlook for the next decades (up to 2050). The EEA observes that Europe needs to introduce farther-reaching policies if it wants to achieve its long-term climate target.

The EIB lending criteria should also be responsive to sector-specific EU climate policy, such as the Transport White Paper which calls for an emissions reduction from the sector of 60% by 2050 compared to 1990 levels.

In our opinion such a review should result in a development of a fully fledged Climate Policy encompassing all sectors and lending instruments of the EIB, including direct lending to projects, the EIB's participation in investment and equity funds as well as the lending to financial intermediaries for on-lending to small and medium enterprises and Mid-Caps.

b) Policy coherence

The EIB needs a Climate Policy that will ensure its portfolio is compatible with the EU 2030 and EU 2050 climate objectives at the project level as well as taking into account the cumulative climate implications of its entire portfolio and of some of the sectors within it.

The above mentioned political priorities of the EU which the EIB identifies in two paragraphs of the consultation paper:

"[…] the limits imposed by other policy priorities covered by the Bank, which are sometimes in conflict with the objective of supporting low carbon emission projects (for example, innovation in energy-intensive industries or strategic infrastructure addressing energy security of supply and/or growth, SMEs, employment and cohesion goals) (A.21, p. 16);

and

[…] " maintaining the balance with other policy goals such as creating jobs and promoting EU competitiveness and growth" (A36 p. 20) do not have to be conflicting but the ways for

1 European Environmental Agency, "The European environment — state and outlook 2015", March 2015, http://www.eea.europa.eu/soer-2015/synthesis/report/0c-executivesummary

reaching those objectives can be more or less compatible with all the other goals at the same time. The EIB as the house bank of the EU is fully guided by EU law and is thus by its mandate prohibited from following those interpretations of any policy that would result in undermining any other EU policy. In effect the EIB should follow the lending trajectory that combines the policies. For example, lending to EE and RES combine the political priorities of supporting low-carbon emission trajectory of the EU economy while improving the innovation in the energy-intensive industries (they are forced to use less GHG intensive production technologies or look for material substitute, i.e. if steel cannot be produced within the GHG emission limits than a material that has the physical parameters of steel but requires much less GHG emissions to produce will be favoured).

The EIB needs a Climate Policy that will help to interpret EU objectives related to energy security or transport infrastructure as these can often appear contradictory due to vague definitions. The EIB needs to make order in this chaos, otherwise it will finance investments that contradict one another or cancel out each other's effects. For example, EIB support for airports development or motorways network developments may undermine emissions reductions generated via other bank support extended to public transport.

c) The need to establish the EIB's carbon budget and review its carbon footprint assessment

As a part of the EIB Climate Revision the Bank would be expected to define its intentions for financing, with examples of some types of projects (like energy efficiency) that do contribute to all the policy objectives of the EU but also provide some that clearly do not (effectively limiting or halting lending to these sectors based on the climate imperative). This list should include the most polluting sources of energy generation, the most climate harmful mining practices (i.e. oil, lignite and coal extraction) and processing (refineries) as well as clearly defined limits for the amount of LNG terminals, highways and airports that the EIB is able to finance between 2015 and 2020 while still staying within the 2030 and 2050 GHG reduction commitments of the EU. This could take the form of the carbon budget at the disposal of the EIB for all their projects financed with the division into specific sector and a margin for the jokers (projects that are not easily categorised like public infrastructure including hospitals and roads) or a roadmap for decreasing the GHG absolute emissions financed by the EIB. An assessment of the emissions from fossil fuel power plant should be compared with the least GHG emitting energy source able to produce the required amount of electricity or heat and similarly this approach should be applied in transport: the highway emissions should be compared with the emissions of the rail transport powered by renewable energy etc.

The currently used methodology for assessing projects' carbon footprint needs further review and strengthening. For example the EIB doesnot count the whole project's CO2 emissions, but only a proportion according to how much of the project it financed although its financing often determines a project's realisation. This should be changed. Also it should be considered to examine as the baseline (for accounting absolute and relative project

emissions) the most environmentally acceptable alternative which would also be economically feasible, rather than a fossil fuel baseline. For gas pipelines, the exclusion of the actual combustion of the gas delivered by the new section of pipeline is a clear weakness. The usual objection here is that double-counting should be avoided and that the gas combustion should be counted with the facility which burns it. However double-counting is only a problem in country-level reporting for global GHG emissions calculations, not for financial institutions seeking to get a feel of the amount of GHG-emitting infrastructure they are contributing to.

It is also necessary to cover the EIB's support to financial intermediaries with the carbon footprint methodology.

Only by changing the current appraisal practices of the Bank would it be possible change the lending portfolio with the speed needed and channel the resources that under the current portfolio end up supporting oil refineries, airports and highways to those sectors that are absolutely crucial for increasing the EU-28's energy transformation, local employment and reduction of GHGs such as energy efficiency in the housing sector or locally-owned renewable energy projects (i.e. small scale locally used biogas plants).

d) The Climate Action eligibility criteria

As far as the EIB Climate Action program may be considered artificial it should be welcomed however that the bank established a concrete financial target (performance indicator) for projects in climate change mitigation and adaptation, which can be considered as a part of integrating climate change consideration into bank lending policies. However we see a need to review the Climate Action eligibility criteria, including raising the criteria for energy efficiency and introducing environmental sustainability criteria for renewable energy projects. We call for excluding the automotive industry from Climate Action eligibility projects as individual transport, even when electric cars are used, will not be environmentally sustainable. Nuclear energy should be excluded from the project types that can be classified as climate change projects. While the carbon emissions might be relatively low, this energy is not sustainable and prevents the needed energy transition. Also only fully transparent projects financed through financial intermediaries should be counted as Climate Action.

e) Ensuring total actual emissions reductions

There is a need to ensure an outcome from climate reduction that actually results in emissions reductions. For example in the area of e-mobility, lending should be targeted at issues such as off-peaking charging and smaller and lighter vehicles such as e-bikes rather than simply provided to the automotive industry in the hope that emissions reductions will result. Industries should only be provided with R&D support if they are bound by meaningful emissions reduction targets, for example the aviation industry should not receive R&D

support for efficiency development until the International Civil Aviation Organisation has agreed a technology-forcing CO2 standard for aircraft.

f) Coherence with the 2030 and 2050 trajectory of GHG emission reductions

The result of an ambitious and thorough revision of the Bank's approach to climate protection would be to align the Bank with the 2050 GHG reduction goals of the EU and the internationally agreed trajectory of reducing GHGs emissions worldwide in a way allowing for the mean increase of the Earth's temperature rise to stay below 2 degrees Celsius (which in itself is already a gamble as it provides only a 50% certainty that the irreversible runaway climate change can be prevented in this way). This translated into the EIB Climate Policy would mean an absolute (not relative) emissions reduction of the whole EIB financed portfolio[2] at the very least in line with the 2030 and 2050 EU targets as well as the absolute emissions reduction should be taking place in all the sectors where the EIB is most present (transport, energy generation, energy transmission, industry, SMEs, intermediary lending) and both within and outside the EU-28. Ambitious as it may sound, it is the only rational policy that the EIB can adopt that would ensure both the short as well as the medium and long-term benefits to the EU economy and an increase in the wellbeing of the EU citizens without decreasing the wellbeing of the non-EU citizens.

2) Risks of the business as usual approach or continuation of the lending with the current tools, policies and methodologies

a) Carbon intensive infrastructure increases the risk of a new market bubble – this time, a carbon bubble

Currently, companies involved in oil and gas extraction and coal and lignite mining are valued based on the assumption that all the reserves on their books will be burned. This is at odds with the science of climate change and with the EU 2050 climate objectives, thus creating a risk of a so-called carbon bubble. If the EU's climate commitments are upheld and other global players agree to stabilise the rise of GHG emissions to below 2 degrees, then 80 percent of the fossil fuel reserves now on the books of fossil fuel companies cannot be burned – their de facto value should thus be zero, whatever the current valuations may be.

This poses a systemic risk not only to these companies that will face a loss of value but also to any financial institutions holding their assets in the form of equity or bonds, or that are exposed to these companies in any other form.

2 As opposed to the current approach of treating climate action as a separate part that encompasses just around 25% of the EIB lending

Further loans to companies extracting fossil fuels, constructing or operating fossil fuel enabling infrastructure (including refineries, roads, airports, rails and ports) or using fossil fuel generation or heating facilities only exacerbate the risk of a carbon bubble further. The EIB must address this risk in its Climate Policy and it must devise a new pattern of lending that reduces the carbon bubble risk.

We would like to address the EIB to the Carbon Tracker Carbon Bubble reports available at:

http://www.carbontracker.org/report/carbon-bubble/

and the Risk of Doing Too Little Too Late report published last year by the Greens/EFA and researched by Profundo (the European Carbon Bubble study) available at:

http://sustainablefinancelab.nl/files/2014/03/SFL-GND-Carbon-Bubble.pdf

b) The need to divest from fossil fuels

In addition, the EIB must also recognise the movement for divestment from fossil fuels , which is increasingly becoming an international phenomenon. The EIB should include fossil fuel investment data in its reports and oblige its financial intermediaries to do the same. The EIB must also declare its target for divesting the Bank's funds from fossil fuels and assist financial intermediaries institutions with developing a divestment target and disclosure practices.

c) Ensuring resilience of crucial infrastructure investment

The EIB should also recognise the need to ensure investment in infrastructure is forward-looking with regards to energy independence. At present, 94% of Europe's transport relies on oil products, of which 90% is imported. EIB lending should not exacerbate this dependence on imported fossil fuels, which is the consequence of investment in carbon intensive infrastructure such as airports and motorways.

3) Suggested tools to achieve policy coherence through the Climate Policy

a) Analysing the cumulative impacts of already existing projects in a given sectoral category together with the EIB projects proposed for financing on the 2030 and 2050 GHG emission reduction goals of the EU-28

These type of calculations cannot be made via project by project assessment. Nor are the member states themselves able to assess how their own specific development choices affect the EU as a whole. The EIB, however, is uniquely placed to have an overview of the financing sought by specific types of project promoters across the EU over time – when excessive levels of GHG intensive infrastructure appear in its project pipeline and on its books, it would be able to take concrete steps to restrict further lending of this kind.

In effect the EIB would have to look beyond project finance and take responsibility for assessing medium and long-term implications of the group of projects it finances (i.e. assessing the climate impact and the coherence with the 2030 and 2050 transport GHG emissions of Europe-28 as a whole of all the projects it finances) and de facto preparing an assessment of how many emissions or infrastructure of a certain category type (i.e. LNG terminals or airports) is compatible with the EU 2030 and 2050 GHG reduction goals. This is actually much easier to be done from the EU level than from individual Member States level and thus the subsidiarity principle fully applies legitimising the EIB role in this regard.

The new Climate Policy requires an obligatory macroeconomic analysis into the impact of EIB lending on the EU member states' decarbonisation trajectories. This is a positive first step, but would need to include not only the impact of projects on a single country's emissions but also giving due consideration to the GHG emissions produced by transboundary projects – such as oil and gas pipelines – that affect more than one EU country, as well as taking into account the emissions produced by the EIB financed projects outside the EU, which often serve the energy needs of the block.

The best example of why this is crucial is the current focus of diversifying gas supply routes and thus the political pressure from both the EC and the Member States to fund and construct new gas import infrastructure. Decisions made now by the EIB to finance new import infrastructure risk being uneconomic and will cement fossil fuels dependence for the next 40-60 years. Preventing the use of public money for massive fossil fuel projects such as Southern Gas Corridor can open space for more serious efforts on energy efficiency and sustainable forms of renewable energy.

This is all the more important given that the real need is to decarbonise energy supplies. In 2013 the International Energy Association concluded that "No more than one-third of proven reserves of fossil fuels can be consumed prior to 2050 if the world is to achieve the 2 °C goal"[3]. What is more In all scenarios of the EU's Energy Roadmap2050 impact assessment[4] shows that decarbonisation decreases the EU's energy import dependence. In all of the EU's five decarbonisation scenarios there is also a decrease – at least to some extent – in natural gas imports by 2050 compared to 2010[5].

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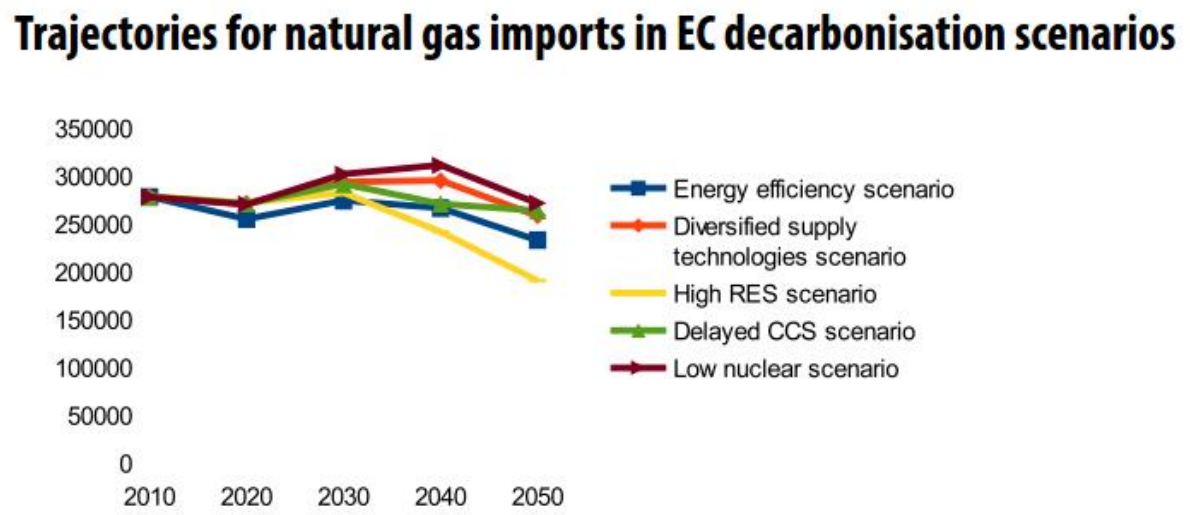
3 https://www.iea.org/newsroomandevents/pressreleases/2012/november/name,33015,en.html

4 Commission Staff Working Paper: Impact Assessment accompanying the document: Communication From The Commission To The European Parliament, The Council, The European Economic And Social CommitteeAnd The Committee Of The Regions Energy Roadmap 2050, December 2011, http://ec.europa.eu/energy/energy2020/roadmap/doc/sec_2011_1565_part2.pdf

5 In some of the scenarios there is a temporary increase around 2030 and 2040, however these seem to be some of the least realistic scenarios currently, given that they assume quite wide usage of CCS. In any case, these temporary import increases amount to less than the current import capacity



Source: No Public Money for Mega-Gas Pipelines[6]

Climate Policy should provide sustainable and long term guidelines for the current financial decisions in order to avoid undermining the medium and long-term climate goals by a wrong interpretation of the short-term reactions and fund projects that combine the different benefits and deliver positively on all the EU political priorities.

Such an analysis is needed to minimise the risk of generating 'stranded assets' both at member state level and, more widely, at EU level. It would also contribute towards ensuring maximum benefit from EIB loans for the EU economy and the wider public.

b) The EIB Climate Policy addressing and aimed at the long-term perspective would lay the ground for the introduction of tools and instruments that would not only serve climate objectives but also ensure long-term financial stability

A long-term climate perspective, enshrined in the new EIB Climate Policy, would have consequences for the way in which project finance is conducted, especially when it comes to infrastructure projects that do not result in significant *direct* GHGs yet still result in high-carbon economic development, i.e. airports, highways, oil pipelines, certain industrial facilities, oil refineries, major gas supply pipelines and LNG terminals. A long-term perspective would duly consider indirect GHG emissions in total project costs, helping in turn to promote more rational use of EU funds.

Thus the EIB Climate Policy must include an obligation to periodically review Carbon Footprint Methodology, Emission Performance Standards of power plants, it must put a cap

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would be able toprovide for. http://bankwatch.org/news-media/for-journalists/press-releases/pipe-dreams-why-southern-gas-corridor-will-not-reduce-eu-d

6 http://www.counter-balance.org/wp-content/uploads/2014/06/PCI-June2014-webnew.pdf

on the EIB's annual emissions from projects and must establish a trajectory – or a road map – for a gradual but constant increase of investments in demand side energy efficiency and dispersed renewable energy technologies that benefit local economies and communities

c) The EIB needs a Climate Policy to be able to improve the effectiveness of its financing and must address the problem of disadvantaged regions within the EU

This especially refers to smart grids enabling demand-side energy efficiency, with a particular focus on the housing sector, as well as small-scale dispersed community-owned renewable energy sources.

In order to do so the EIB should focus on systematic support of local level energy planning which is the only way to shift energy development towards sustainability, efficiency and self-sufficiency. This is the essence of intelligent energy.

The EIB Climate Policy is a unique opportunity to include the systematic support of intelligent energy into banks operations.

Investment needs in energy efficiency, renewable energy and sustainable transport across Europe are huge, particularly in Central and Eastern Europe (CEE) – the EU region where most clean energy progress needs to be made.

The EIB is best placed to fill this financing gap and develop tailored solutions for the renewables and energy efficiency markets in the CEE region. The added value of the EIB is in blending Cohesion and Structural Funds with financial instruments that enables support of the whole project lifecycle including the planning and capacity building phases that are not suitable for standard commercial financing but are crucial for intelligent energy development.

The EIB can help to overcome current barriers for financing sustainable energy projects, in particular, high up-front investment costs, lack of financial guarantee, high loan related costs, lengthiness and complexity of permission procedures.

Other important aspect is the active involvement of local communities into local energy planning and project implementation. Community led energy projects are the best example as they present opportunity for local citizens and stakeholders to plan, develop and own energy infrastructure or utilise existing energy savings potential collectively and directly satisfy their energy needs. This type of enterprises combines multiple positive elements such as creation of capital by using local means, investment of the capital within the region that stimulates its economic development or formation of the basis for long term enterprising with active involvement of citizens. At the same time, as community energy promotes

sustainable RES and energy savings it brings decreasing of the environmental pollution and greenhouse gas emissions.[7]

Scale, ownership, sustainability of resource utilisation and efficiency of energy consumption are key elements in intelligent energy economy. That is why the EIB should condition any support for renewable energy and energy efficiency projects on strict binding sustainability criteria.

d) Energy efficiency needs to be treated as an energy source of its own

The European Commission, in its recent communication on the Energy Union (COM(2015)80) calls for a fundamental rethinking of energy efficiency, treating it as an energy source in its own right, representing the value of energy saved. The Commission will ensure that energy efficiency and demand side response can compete on equal terms with generation capacity.

The EIB needs to get on par with the Commission efforts in this area. Ensuring energy efficiency is treated equally to any other sources of energy means that measures to reach efficiency potential needs to be taken into account before any new energy generation or distribution project is started. This is ensured by strict application of the efficiency first principle.

Efficiency First is an organizing principle by which demand-side measures are considered on comparable economic terms with supply-side resources in energy sector planning, investing, and purchasing. It also ensures that whenever demand-side measures are shown to be less expensive or more valuable than their supply-side alternatives, they should be deployed first. In this way, an Efficiency First approach avoids the lock-in of unnecessary and more expensive resources, and ensures that energy needs are met with the cheapest and cleanest alternatives available.[8]

Efficiency First also recognizes that there are barriers to efficiency that prevent its uptake – even where efficiency is cost-effective for consumers or society as a whole. Overcoming these barriers requires a combination of public funding incentives, regulatory mechanisms and codes & standards. Achieving the efficiency potential requires a high-level commitment to systematically identify the multiple decision points where efficiency is overlooked or

7 In CEE countries in comparing to Germany or Great Britain there is a lack of knowledge related to the citizen-led EE and RES projects which is directly linked to a lack of legitimacy of the cooperative as a real market player and viable economic alternative in front of the financial operators, the governments and citizens. Source:http://rescoop.eu/report-financial-barriers-and-existing-solutions

8 Edith Bayer: Efficiency First: Key Points for the Energy Union Communication. RAP 2015. Online: http://www.raponline.org/document/download/id/7507

undervalued, and put in place concrete policies and measures to ensure that investments happen wherever efficiency is more cost-effective or valuable than equivalent supply-side resources.

The EIB needs to set the efficiency first as one of the guiding principles in its Climate Policy. Further on, the principle must be practically implemented into decision making about energy projects on various levels of their assessment.

An important part of implementation of the efficiency first principle is consideration of and support for demand-side management measures. The role of the EIB here is especially prominent in lending to energy infrastructure projects. Pursuing the efficiency first principle the EIB must ensure that demand side management is a main feature of design of any such project. While many grid projects can claim they comply with this criterion already now, the EIB must ensure that its financing requires significant added value and pushes for additional measures focused at demand side management. The EIB should develop a methodology to assess such added value is in place.

e) Mainstreaming energy efficiency

Project lending can bring significant energy efficiency improvements, namely projects in areas such as transport, industry, agriculture, SMEs or urban and regional development.

Especially in case of lending to individual projects, the bank should screen the potential of each of the projects to achieve additional energy savings. On one hand, it should require the investors to undertake such measures, i.e. through demanding an energy audit to be undertaken and measures resulting from it implemented. On the other hand, it should adjust the lent volume in order to meet financing needs for such measures to take place and clearly earmark part of the loan for them.

In case of lending to financial intermediaries, these should work together with the intermediary to develop measures and procedures that will be implemented by them in order for final recipients' projects to improve their energy efficiency. Where possible, such as in case of loans and other instruments dedicated to building construction and reconstruction, minimum energy efficiency requirements of the final projects should be set.

In both cases, technical assistance of the bank should be used to mainstream energy efficiency measures in the projects.

f) Focused approach to financial instruments for energy efficiency

Financing from the European Structural and Investment Funds dedicated for energy efficiency has significantly increased in the 2014 – 2020 period compared to the previous one. Despite of this, available funding and other measures will not be sufficient to ensure countries achieve their end-use energy savings targets set under the Energy Efficiency Directive (EED).

In Slovakia, for example, ESI funds under the OP Quality of Environment will only cover 20% of investment needs for energy efficiency of buildings owned or occupied by central authorities as required by the EED. Overall, measures presented in the Slovak National Energy Efficiency Action Plan (NEEAP) will only cover 85% of the binding target.

In the Czech Republic, ESI funding for energy efficiency in public and multiapartment buildings is only sufficient to achieve a slow, non-ambitious energy renovation scenario. The National Building Renovation Strategy, part of the NEEAP, however recommends a fast, deep renovation scenario as the most effective both in terms of economic benefits and energy savings.

At the same time, financial instruments provided so far by the EIB have had only limited success in the CEE countries. While some of JESSICA schemes – like in the case of Lithuania – have marked significant success, in other cases – such as the Czech Republic – they face difficulties both in the preparation and implementation phases. In case of ELENA, uptake of technical assistance has been very limited in the CEE countries with only 3 schemes running in the new member states so far.

The EIB needs to significantly increase its presence in energy efficiency funding in the CEE countries. As interest in energy efficiency financing can be lower in the new member states, the bank needs to increase promotion of its instruments in these countries. In 2015, a single conference dealing with urban development taking place in the CEE countries (Nitra, Slovakia) is organized by the EIB. In 2014, there was no such event.

One of the barriers for implementation of financial instruments in energy efficiency are different administrative and legal setups across the countries and even institutional habits. Planning in the cities often does not focus on the area of low-carbon development which undermines the attractiveness of the ELENA scheme, connected to the existence of low-carbon plans. Still, these cities would benefit from both technical assistance and financing of energy efficiency measures. It is necessary to build closer ties with cities and other stakeholders in the CEE countries in order to overcome such barriers.

Use of innovative financial instruments in energy efficiency is planned in most of the CEE countries in the 2014 – 2020 period. While revolving instruments can be well used for these purposes as efficiency measures create return on investment through the savings, it is necessary to analyse closely the situation of final beneficiaries. In many cases, both in the household and public sectors, taking an extra loan, even for measures with a payback, is not viable. Low income and unemployment, over indebtedness, rules on public debt and many other reasons may put the potential beneficiaries off the possibility to use the financial instruments.

In these cases, it is necessary to offer a subsidy or a combination of subsidy and loan. Finance from the ESIF, which can be used in both ways, should be used for the non-

returnable subsidies always when the situation of the beneficiaries would not allow a loan. EIB financing, on the other hand, should be used to capitalize the revolving funds in order to free the ESIF for the subsidies.

As the EIB will be active in assisting in the setup of financial instruments in the member states, it should encourage them to analyze well the situations of various groups of potential beneficiaries in order to ensure financial instruments in a form of loan are only used where there is an absorption potential for them, while in cases where loan is not an option, subsidy is used.

g) Volume-based lending target should be viewed as a start only and should be accompanied by clear targets for project outcomes

For example targets for the total energy generated by renewable energy projects and per sum invested in renewable energy (this can be broken down by project type, such as wind-farms, solar panels, etc.) This can better inform the Banks' future lending targets and strategies and should also be disclosed to private commercial financial institutions thereby facilitating the development of their own climate action lending policies.

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