

LMA Publishes "External Review Guidance for Green, Social and Sustainability-Linked Loans"

Introduction

The rapid evolution of sustainable finance products has led the LMA to provide further guidance; we wrote recently on its Guide to Sustainability-Linked Leveraged Loans¹. Now the LMA, together with the APLMA and the LSTA, has published a second edition of its external review guidance², replacing that provided in 2022.

This new edition is intended to provide clarity around the different types of external review through the adoption of common terminology and more standardised review processes.

The Guidance considers the forms that reviews may take and examines:

- Ethical and Professional Standards for External Reviewers;
- Organisation of External Reviewers;
- Content of External Reviews; and
- Disclosure for External Reviewers.

Each of these points is covered below.

The Purpose of an External Review

As part of our previous update referred to above, we examined the specialised roles that arise at different stages in the lifecycle of a loan. One such role involves external review, by which the loan is awarded an ESG score / rating.

There continues to be no single set form of external review that a borrower can obtain, so the LMA Guidance clarifies the different forms, namely:

- Second Party Opinions ("SPOs"); and
- Verification.

The method of external review to be adopted will usually follow from the nature of the loan.

SPOs

An SPO typically involves an assessment of the loan and / or wider financing with regard to the overarching principles of green, social and sustainability-linked financing at a pre-execution stage. The approach taken by the SPO to this assessment will differ depending on whether the loan is a green or social loan or a sustainability-linked loan.

Verification

Verification involves a review of financial and non-financial information prepared by a third party against a detailed ethical standard. The level of detail contained in such assessments is more extensive than that for an SPO.

The new guidance aims to establish common definitions, which may otherwise vary. The LMA explores the methodology of both SPOs and Verification in detail with a view to encouraging consistency and an understanding of the need for differences in presentation.

¹ <https://maples.com/en/knowledge-centre/2023/11/lma-guide-to-sustainability-linked-leveraged-loans>

² Sustainable Lending Microsite: LMA

Ethical and Professional Standards for External Reviewers

The five fundamental principles underpinning all external reviews are:

- Integrity;
- Objectivity;
- Professional competence and due care;
- Confidentiality; and
- Professional behaviour.

The LMA acknowledges that some external reviewers may, in addition, be subject to existing professional standards, but encourages them to ensure consistent application in approach to the five principles listed above.

This, in turn, will help to increase clarity, consistency, and transparency in the market. The independence of the external reviewer is paramount and the LMA also recommends putting in place appropriate safeguards where necessary to protect the independence of the external review.

Organisation of External Reviewers

The updated Guidance outlines the infrastructure required by companies supplying external review services. In keeping with the theme of promoting consistency, the LMA sets out a four-part list of 'must-haves' for external review providers that includes reference to, for example, appropriate staff with necessary experience.

In addition, providers of SPOs should have the expertise in:

- the eligible Green or Social Project categories, together with any associated exclusion criteria under appropriate international, national or industry level guidance in respect of green and/or social loans;
- the selected key performance indicators and sustainability performance targets, along with any associated benchmarks,

baselines and sector standards in respect of sustainability-linked loans; and

- where necessary, an awareness of science-based trajectories and / or climate change strategy.

The LMA then links this list to methods of assessment, noting that the above can also be included in such assessments, depending on the methodology and standards being applied.

Content

The guidance provides a detailed list of points to be included that can be used to structure an external review, ranging from (i) "*details of definitions, analytical approach, criteria and / or methodologies used*" to (ii) "*...the level of verification and a description of any relevant international professional standards to which such verification will be aligned*".

In doing so, the guidance seeks to remove confusion arising from the inconsistent application of common terms by connecting how / when these terms are used in (i) SPOs and (ii) Verification.

This outline as to content is combined with a short note on the common scoring/rating of these green, social, and sustainability-linked loans.

Disclosure for External Reviewers

The guidance concludes with brief comment on the (i) timing of and (ii) parties to the disclosure of an external review, noting that this may need to be tailored to the nature of the review and any confidentiality provisions underpinning such review.

Conclusion

We are pleased to see this further guidance, which should result in more clarity in the market. We will continue to monitor further developments.

For further information, please reach out to your usual Maples Group contact or any of the persons listed below.

Dublin

Sarah Francis

+353 1 619 2753

sarah.francis@maples.com

Alma O'Sullivan

+353 1 619 2066

alma.o'sullivan@maples.com

Louise Sharkey

+353 1 619 2733

louise.sharkey@maples.com

February 2024

© MAPLES GROUP

This update is intended to provide only general information for the clients and professional contacts of the Maples Group. It does not purport to be comprehensive or to render legal advice.