ENVIRONMENTAL LIABILITY DIRECTIVE: Impact on Companies and the Portuguese Banking System in Portugal
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1. The Environmental Liability Directive and the Environmental Risks

Historical introduction
The matter covered by the Environmental Liability Directive refers historically to the article 174 of the EC Treaty, which establishes in its number 2 that “the environment policy of the Community (…) shall be based on the precautionary principle and on the principles that preventive action should be taken, that environmental damage should as a priority be rectified at source and that the polluter should pay” and it specifies these principles.

In May 1993, the Commission published the Green Paper on Remedying Environmental Damage. Following this publication, more than 100 comments were presented by Member-States, industry, environmental organizations and other holders of diffuse interests. In November of that same year, the EP and the Commission conducted a joint prior hearing on the matter in question.

In February 2000, the Commission published the White Paper on Environmental Liability. This white paper – which preceded the Directive 2004/35/EC – describes the possible main features of a Community environmental liability regime, the most pertinent of them being: no retroactivity, coverage of both traditional damage (harm to health and property) and environmental damage; strict liability for damage caused by dangerous activities and fault-based liability caused by non-dangerous activities; some alleviation of the plaintiffs’ burden of proof and operator-focused liability.

In April 2004, the Directive 2004/35/EC of the EP and the Commission was published.

Objectives
The departure point of the normative text takes the form of a set of reasons that justify the existence of a Community environmental liability regime, the most important of them being: implementation of the environmental principles of the Treaties; the need to ensure the cleanup and remediation of the environment and the full application of the integration principle by which environmental matters must be incorporated in other Community policies.

In this context, with the publication of the Directive 2004/35/EC, the objective is the application of the polluter pays principle, since it was considered that the regime of civil liability is not an adequate instrument to cope with situations such as pollution of a diffuse character in which it becomes especially difficult to operate the relationships between cause-effect.

Key issues for companies and the financial sector
By basing its legal structure in the financial liability of operators, the Environmental Liability Directive has an immediate repercussion on companies and the financial sector.

The forecast of the directive as regards the development of financial guarantees by operators, enabling them to cope with the prevention and remedying costs of environmental damage and any imminent threat of such damage, together with a strict liability regime and a fault-based liability regime, entail important consequences to companies and to the financial sector, in particular if one bears in mind the European Union scale.

The transposition into Portuguese law – Decree-Law No 147/2008 of 29 July
The establishment of the Rule of Environmental Law was based on the prevention principle and is now being developed together with the principle of accountability. This double bottom base is the foundation of the autonomy of the new concept of environmental damage, thus considered and whose legal system is welcomed in the DL No 14/2008 of 29 July, which transposes the Directive 2004/35/EC into Portuguese law.

Some of the broad concepts used by the legislator regarding the administrative responsibility for the prevention and remedying of environmental damage, such as the concepts of “damages”, “operator” or “initial state” will cause, in a near future, the need for legal literature and case-law opinion to emerge, clearing up its sense and limiting its own content. But the backbone of the liability regime is clear, since it is based and divided between a strict liability regime for certain occupational activities and a fault-based liability regime for other activities. And it is also obvious the obligation to establish financial guarantees that allow the operator to assume environmental liability – compulsory collateral from 2010 onwards, that, in theory, may take the form of an insure
policy, bank guarantees, participation in environmental funds or provision of equity to that end.

The implications of the normative text for the State, Companies, Insurance Companies and Banks will be felt, although in a different way.

The State, although assuring the task of safeguarding the affected environmental assets, leaves the stage as a payer in most cases. At the center of the stage, at this regard, are Companies and in the backstage there are Insurance Companies and Banks. With the publication of the above-mentioned normative text, the “level of readiness” that both of them are required to have is not, after all, that different.

Insurance Companies will notice the huge window of opportunity that has been created, but in fear of difficulties arising from risk measuring, they will have to deepen the specificities of environmental matters, they ought to study a set of high complexity variables and to have finished formulas and toolkits to quantify the damage and its remediation.

The banking sector, which is responsible for financing most of the business sectors encompassed by the legal text, should note that the environmental risk assessment will be an increasingly vital tool in the risk assessment of loan portfolios. Which is particularly impressive for SMEs that do not have collateral to cover loans, should a significantly damaging situation occur, but also real for large corporations since companies face a real operational risk, which affects Banks through an increase of the under assessed credit risk according to environmental risks.
2. Environmental Risks on Banks

“The Oxford Dictionary of English defines environment as ‘what surrounds us; in particular the conditions or circumstances in which people, animals live or develop’. That is to say, everything around us. Nevertheless, a more useful definition (for risk assessment) is the one by environmental scientists, which divide the environment in three areas – earth, water and air. Environmental pollution... can be categorized as follows:

- Water pollution
- Soil contamination
- Air pollution

“Environmental pollution can be defined as the release into the environment, by human activities, of substances that have an adverse effect.” (Case, 1999, p. 4)

Since air pollution is already strongly regulated by the European Union Emission Trading Scheme under the Kyoto Protocol, the Environmental Liability Directive goes further by considering as environmental damages all those:

- “caused to protected natural species and habitats” (...)
- “caused to water” (...)
- “caused to the soil”.

One can identify three types of banking risks in light of environmental factors:

- Direct Risk
- Indirect Risk
- Reputational Risk

2.1 Direct Risk

The Direct Risk – or liability of the money lender – occurs when a bank may be hold responsible for environmental damages caused by a client.

Bank liability for the environmental damage arising from a loan to a client

The existing National legislation, as well as guidance provided by the European Commission in this matter, excludes a bank from being held responsible for environmental damages caused by a client, as a result of a loan granted by that bank. Nevertheless, while analyzing some international experiences namely in the USA, there are already cases in which banks have been held responsible for caused damages, since it was assumed that that bank participated in the financial management of that company and had the ability to influence its decisions. An often mentioned example is the American legislation developed in 1980 – Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) later known as the Superfund Law – which stated that in certain circumstances the government or a private entity could force a financial institution to pay for the cleaning of a contaminated site. At that time there was a broad notion of stakeholder, which included current and past (existing at the time of the contamination) owners and operators as well as those transporting the contaminating substance. Creditor banks may be included in one of these categories given that they partially hold those companies or because they supervise a loan and, as such, are provided with the influence over the company’s management, which includes environmental management.

Despite the existence of individual cases in the USA, in which a bank was forced to clean the contamination caused by its client, and despite similar legislation has been developed in the United Kingdom and Germany, the legal changes that since then have been made result in being more difficult for banks to be held responsible for environmental damages caused by its loans. However, it must be recognized that this is a possible scenario, and also that the environmental liability directive can become a good opportunity for appropriate legislative changes, even tough in several stages.

In practical terms and in countries where that legislation exists, though vague and controversial, there has been
certain reluctance in granting loans to certain business sectors. However, since this issue does not arise in many countries, it remains a ‘grey’ area.

Bank environmental liability arising from collateral of which it became owner and belonged to a client

While contracting a loan it is frequent to use as collateral (sometimes mortgages) of the debt some tangible assets, such as land and buildings.

In the case of land, industrial units, buildings and similar assets, it is possible that environmental damages have occurred, during present or past activities of that company. If those environmental damages have caused soil or water contamination and/or biodiversity loss, that may add an environmental liability to that asset, which reduces the financial value of that asset.

Meaning that in the risk analysis conducted by the bank there was not a concern regarding potential environmental risks of those collaterals, which in turn may indicate that the value of that real property might be overvalued, since the environmental risk pricing was not introduced in the risk analysis model. In certain situations and/or more problematic sectors, the due environmental diligences may represent key stages in the evaluation of given collaterals.

What does the European Commission say about the liability of banks

“...we must be sure that those who cause environmental damages be hold responsible for their actions. The ‘polluter pays’ principle means that the financial liability for damages caused to the environment is hold by those who pollute.”

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Picture the following example:

The Bank A grants a loan of 150.000 euros to the company Omega, using the company’s own facilities as collateral. The company Omega fails to fulfill its financial commitment and the bank makes use of the given collateral as a debt security.

However, given that the facilities are located in contaminated land its financial value is much inferior to the predicted one.

That is, the Bank A loses its 150.000 euros of loan and, besides that, it might be forced to clean up the contamination since now the land and facilities belong to the bank. How much will this clean-up cost? This means the bank may incur in costs that are superior to the granted loan.
2.2 Indirect Risk

The Indirect Risk may affect banks much more frequently than direct risks. This risk may come from two different sources:

- The inability of a company to meet its financial obligations towards the bank, due to unsecured environmental costs (cleaning, fines, equipment, etc.).
- The change of raw materials on which the production is based, as a consequence of Biodiversity losses.

The inability of a company to meet its financial obligations

Although the existence of a broad environmental legislation at European level, and also in Portugal, there are always some risks that may arise from accidents and will entail financial consequences to companies, especially in the scope of the Environmental Liability Directive. Some of those accidents might be:

- Spill of chemicals
- Storage of substances that can potentially seep into the ground
- Mismanagement of hazardous waste that can lead to contaminated soil and water
- Among others

The damages resulting from these accidents must be remedied, repaired and/or eliminated in order to restore the previously existing situation of the soil, water or natural habitats, in accordance with the Environmental Liability Directive.

Besides these potential cleaning costs and/or fines, the banks must not forget that there is also a set of additional environmental costs that must be included in the financial analysis of a company, such as:

- The need to maintain the environmental licenses and to keep up with the increasing degree of its requirements
- The need to invest in equipment to reduce their environmental impacts in order to comply with the requirements of licenses
- The need to implement a robust environmental management system with an ongoing improvement process
- The need to employ new workers focused in assuring the company meets every requirement in order to comply with legal requirements
- The need to change to environmentally friendly raw materials, and even to develop “green products”

Some of the sectors that are likely to be affected by an increasing environmental legislation are: manufacturing, chemical, pulp and paper production, refinery, food, transport and construction.

Among companies, SMEs are more likely to be subject to these risks, because:

- They are less aware of the existing environmental legislation
- They are unaware of the Environmental Liability Directive implications
- In general, these aspects are uninsured
- They face cash flow problems which contribute to perceiving environmental investment as an additional cost
- They face constant cash flow problems meaning that, should an accident that needs remediation happen, they may not have the operating fund to address that additional expense, putting into question the possibility to fulfill their payments to the Bank, becoming potentially indispensable to request another loan.
- Large enterprises, which are usually clients of SMEs, are starting to implement the so-called suppliers’ code of conduct, and requesting certain environmental behaviors from their suppliers, such as environmental certifications, among other volunteer initiatives, upon the choice of their suppliers. These increasing requirements are therefore becoming another factor to be considered while analyzing the potential market for SMEs clients and their capability to answer adequately to these requirements.
The change of raw materials on which the production is based, as a consequence of Biodiversity losses

“Biodiversity includes plants, animals and other organisms and is defined in the Convention on Biological Diversity (CBD) as the variability among organisms from all sources including terrestrial, marine and other aquatic ecosystems and the ecological complexes of which they are part; it includes diversity within species, between species and of ecosystems.

Ecosystem services are the goods and services that biodiversity provides. They include soil formation, the provision of food and fiber, air quality and climate regulation, the regulation of water supply and quality and the cultural and aesthetic value of certain plants and species.

Our understanding of the detailed interactions between biodiversity and ecosystem services is still evolving; however, it is very clear that mankind’s impacts on BES is creating material risk for the financial sector, and also rapidly increasing a range of business opportunities.”

Source: UNEP FI, in the report “Bloom or Bust”, page 4

The scarcity of natural resources is undoubtedly a strategic threat to companies. According to the UNEP FI, companies whose value chain is related to food and forest commodities and other biodiversity aspects are particularly exposed to these risks. Not only due to the changes that might take place in the sourcing of their raw material, but also because many of these companies clients are final consumers that are becoming increasingly (and will be even more) interested and demanding good environmental practices by companies.

These future changes in raw materials and preferences might also influence companies in two fundamental areas of their development: in their productive function and in the utility sense that their sales might provide to consumers in view of their new expectations.

This fact has been acknowledged by some financial leaders and companies in which they invest. Although we are witnesses of the fast growing pace of ethical investment funds and sustainability strategies in companies, there are not yet globally accepted tools capable of measuring biodiversity risks.

As such, biodiversity is a risk that the financial market does not internalize, as it happened with the climatic change issue.

Examples of ecosystem services:

- Certified products: agriculture, fisheries, wood
- Biodiversity offsets (whenever there is appropriate legislation)
- Watershed protection
- Carbon sequestration
- Biocarbon
- Biofuel
- Landscape
- Organic products
- Education
- Research

“Systems of Payments of ecosystem services are based in the principle that biodiversity provides a number of services that are economically significant.

The payments and financing must be intended to the protection of biodiversity, ensuring an ongoing provision of those services.“

Source: The Green Buck. WWF
It is worthwhile recalling that the environmental liability Directive also considers as environmental damages those “caused to protected species and habitats” [...] – that is, damages to Biodiversity.

The abundance of existing species in 2010 (OECD)

The abundance of existing species in 2050 (OECD)

Source: The Economics of Ecosystems and Biodiversity. European Communities 2008
Biodiversity loss will affect current animal, plant and forest production balances which serve as a basis for several large enterprises. It will also contribute to climate change, water advances and changes in the ecosystems as we know them. Given that large enterprises of sectors such as food, beverage, pharmaceutical, pulp and paper, among others, are mainly dependent of raw materials made available by nature, and since they have a leverage effect in a series of other economic sectors, then we might start to grasp the true dimension of this issue.

The ecological Balance is one of the pillars of sustainable development. Companies affect ecosystems, but depend on ecosystem services – such as climate, water, air, plants, food, wood, among others, most of which are consumed by all of us without ever being paid. “Us” is understood to mean consumers and companies. The non-existence of a price, has led to excessive consumption which is already having an impact in the value chain of some sectors, along with subsequent financial implications.

In Portugal there is already a simple example: the codfish in the 70s was considered the food of the poor, but nowadays it is served at the best restaurants at extremely high prices, since the abundance of this species has considerably reduced.

2.2 Reputational Risk

The Citigroup case

Thousands of credit cards were returned and destroyed by users, due to the Bank participation in investments on Finance Projects considered controversial.

In 2000 started one of the largest campaigns, which brought together several NGOs, against the financing of controversial projects, regarding the environment and human rights, by private financial institutions. The campaign objective was to influence the decision making regarding the Citigroup’s project finance.

According to the Rainforest Action Network, the NGO responsible for the campaign, the choice of institution had to do not only with the type of projects that were being financed, but also to the fact that this was the largest global financial institution, thus acting has a benchmark to every existent institution. The main pressure was held over the retail banking division, with several bank clients sending its cut card to the head-office of the institution.

Considering that the campaign counted with the adhesion of many young clients – especially students, the bank had severe losses, since a young client means a lifetime of savings and potential stable credits.
The reputational risk of banks comes from environmental aspects and it is related to the way loan money is used, or to the type of business in which banks are investing. In fact, it can be said that the banking sector is the main promoter of sustainability and environmental protection, since through financial allocation it is able to allocate natural resources to several parts of the planet. This allocation of resources is performed in an indirect way, but is intrinsically linked to the granted loans and undertaken investments.

With the growing appreciation of ethical behaviors and accountability of companies for the consequences of their actions, some banks are also experiencing a growing pressure by consumers and organizations to pay attention to the destination of their loans.

Demonstrations of citizens and NGOs against Banks lending money to build a nuclear power plant or extract oil & gas

BPN Paribas
Demonstrations due to loans related to the construction of nuclear power plants.

Royal Bank of Scotland
Demonstration due to loans granted to projects on oil and gas extraction.

The NGO BankTrack has developed reports comparing the expressed compromises and operations carried out by banks worldwide; it has disclosed “strange” businesses, identified involved banks and companies as well as the environmental impacts in question. For instance, this NGO has a website enclosing a section exclusively intending to expose the “doggy deals” undertook by those banks stating to have environmental and social commitments in Project Finance areas.

Royal Bank of Scotland
A group of NGOs wrote a parallel report on the Royal Bank of Scotland “The Oil & Gas Bank – RBS & the financing of climate change”

“It takes 20 years to build a reputation and five minutes to ruin it. If you think about that, you’ll do things differently”

Warren Buffett
In 2007, a phone survey to 1,200 consumers [1] was conducted in Portugal, having the following information been obtained:

- 60% of the population would switch to another bank if it would have seen in the news that a company that had polluted a river was financed by its bank.
- 36% would certainly choose a bank that would present a more expensive monthly payment up to 5%, if it would develop financial products and actions to support the environmental conservation. 29% would tend to choose that bank.

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[1] The phone surveys were conducted by the Center for Opinion Polls of the Catholic University of Portugal to 1,200 Portuguese consumers. With a 95% degree of belief, and a maximum sampling error of ± 2.8%, having this survey been conducted between 2 and 15 May 2007.
3. Biodiversity Risks and Banks

The biodiversity risks are therefore linked to the loss of ecosystem services by nature. The loss of those ecosystem services is closely linked to the development of economic sectors with strong impacts in ecosystems. According to the FTSE4GOOD, the sectors with a high exposure to biodiversity risks are:

- Construction, related materials and real estate
- Electricity
- Food and drug distributors
- Food producers
- Forestry & Paper
- Hotels and Tourism
- Mines
- Oil and Gas
- Utilities [telecommunications and water]

According to the OECD, it is estimated that the global biodiversity loss between 2000 and 2050 (measured according to the mean species abundance) will result from pressures in the following areas:

- Infrastructure
- Climate change
- Crops area
- Forestry
- Pasture area
- Fragmentation
- Woody biofuels
- Nitrogen deposition

Source: MNP/OECD 2007

If we take into consideration the growth expectations for the Portuguese economy in the following years, we can easily realize that all those sectors represent a major proportion of the Portuguese business sector. That is, biodiversity risks are present in every main sector of the Portuguese economy, which means that the Environmental Liability Directive has broad implications: not only for companies, but also for financing banks that must be aware of the new risks arising from legislation.

According to the UNEP FI, the loss of Biodiversity and ecosystem services entails the following implications for the financial sector:

**In the Short Term**

*The need to know potential environmental Liabilities:* It is expected that there is an increasing need to know potential environmental liabilities due to the transposition and effective implementation of different directives, such as the Environmental Liability Directive. To that effect, the UNEP FI expects that bank regulations, as well as requirements regarding the material information disclosure become more demanding in this area.

*The increase of reputational risks:* The banks involved in controversial loans or investments face reputational risks with corporate consequences, namely the switching of clients to other banks.

**In the Long Term**

*Smaller and less safe return on investment:* There might be losses of revenue from clients not being able to meet their commitments with banks, due to changes resulting from failures in ecosystem services and biodiversity losses.
4. The Implication of the Environmental Liability Directive for the Banking Sector

- **Direct Risk** since the frequently used collateral to granted loans are properties or buildings, and they might undergo serious environmental impacts or might not be in accordance to the environmental legislation in force;

- **Indirect Risk** in corporate financial capacity (in particular SMEs) in eventually being able to cope with situations in which environmental damages have to be compensated, and should the contracted insurances for those risks be inexistent;

- **Indirect Risk** through modifications underwent, at different levels, by raw materials due to changes in biodiversity; through the potential development of markets associated to natural assets (e.g. water and species reserves);

- **Reputational Risk** since the environmental awareness related to the civic awareness concerning the actions of banks is increasingly valued by citizens.
5. The Environmental Risks in Loan Portfolios of Portuguese Banks

The banking sector is responsible for financing many active companies which are covered by this directive.

It becomes interesting to realize that sectors identified as being drivers of development and future investment are those which have naturally strong environmental and social impacts (both negative and positive), such as the Tourism industry, Construction and Infrastructures, Transport and Energy.

On the other hand, and since 99.6% of our business sector is made up of small medium-sized enterprises with one of Europe’s smallest capital markets, it becomes essential to understand the importance of bank loans in our economy for the economic development of Portugal.

It is also a strong financier of Small Medium-sized Enterprises [SMEs], which represent approximately 99.6% of all companies in Portugal and are responsible for 40% of the Gross Value Added (GVA) generated by the Portuguese economy.

Source: Bank of Portugal. Monetary and financial statistics (September 2008)

SMEs represent:
- 99.6% of all existing companies
- 75% of all working positions
- 45% of turnover

and are responsible for:
- Approximately 40% of the GVA

Source: IAPMEI "Sobre PMEs em Portugal", January 2008
This situation becomes particularly relevant, when in a study conducted in 2007 to 93 Portuguese SMEs [2] the following results were obtained:

- 68% are aware of the existence of the environmental liability directive
- 60% do not know how the Directive might affect their companies
- 83% have not searched for information on environmental insurances that might enable them to mitigate an eventual accident
- 72% consider useful that banks advise on how environmental impacts might affect their business

As part of this study, a questionnaire to Portuguese banks on environmental aspects was also conducted, having been replied by 13 banks [3] that corresponded to 75% of the Portuguese banking product. Some of the conclusions are that:

- 70% of the Portuguese banking sector considers that, with the environmental liability directive, the credit risk of SMEs has increased
- 63% states that environmental risk assessment is conducted according to qualitative information

The risk of environmental damage by large corporations (depending on environmental damages) does not lead to significant increase of credit risk for banks, due to self-owned collateral and assets, provided that the due environmental diligences are ensured. The same procedures cannot be applied to most SMEs, since they do not own significant collateral or guarantors to cover loans, should a significant violation occurs.

However, whether for SMEs or large corporations, there is an increase of the real operational risk of companies, which affects banks through an increase of the undervalued credit risk depending on the environmental risks.

This fact is not new. There are already real examples of environmental damages to third parties which lead to company closures and to bad debts or contaminated collateral as a final result for supplying Banks. This directive worsens this fact, since it is not necessary that a damaging environmental impact caused by a company to affect a third party. It is sufficient for an environmental violation to occur, and as a result, to become necessary to remedy, repair and/or restore the previously existing soil, water or natural habitats situation.

[2] The questionnaires to SMEs were conducted through an online invitation to 1100 Portuguese SMEs to participate in the study, in accordance with stratification in line with companies’ sector representation by NUTS 2. Following the provided Internet address, which should be accessed in order to answer the questionnaire, several phone calls were done to acknowledge receipt of the participation application and to request the replies. Contacting these agents and obtaining their replies took place between June and September 2007.

[3] The questionnaires to banks were conducted through an online invitation to all member banks of the Portuguese Banking Association (having some stated that they were not interested). Following the provided Internet address, which should be accessed in order to answer the questionnaire, several phone calls were done to acknowledge receipt of the participation application and to request the replies. Contacting these agents and obtaining their replies took place between June and September 2007.
What Can Banks Do to Reduce Environmental Risks

The environmental impact on banks, in a first stage, will necessarily imply a reactive attitude in order to reduce the environmental risks that are not being duly compensated in the interest charged, that is, in the pricing of borrowed money. This reactive attitude may involve measures that mitigate the environmental impact, such as disclosing information to clients that are likely to experience environmental risks.

In a second stage, the sector needs to adopt a proactive attitude. Environmental risk assessment will be an increasingly essential tool in rating loan portfolios. The banks that will invest the most in this aspect will have an advantage regarding other financial institutions that did not adopt these tools of analysis. This is not only a question of corporate image but instead of operational management of loan portfolios.

Therefore, it is recommended that throughout the first operational stage intending to incorporate environmental and social risks in the lending activity, banks cover consecutively all the following stages:

• To identify a set of environmental and social general questions that must be answered by all companies. For example: Is the company registered at the EMAS?; Does it have environmental certification?; What is the number of work accidents?; Does it have fines for non-compliance of environmental and social legal aspects?; Does it have an environmental policy?; etc.

• To identify a set of environmental and social specific questions, concerning the sector in which a company operates. For example: Does the company face high additional costs to cope with environmental requirements?; Is the company management aware of its environmental impacts?; How is waste managed?; Does the company report its environmental and social performance?; Are there lawsuits resulting from citizens’ complaints regarding odors, noises or others, that may become a problem?; What are the existing procedures to control the environmental impacts in the value chain?; Does the company inventory the CO2 emissions?; Is the company subject to the Kyoto Protocol?; etc.

• To identify the potential environmental and social risks affecting loan collateral. For example: Has the property used as collateral had a previous use in the past?; Which one?; Does it have groundwater?; Is there a possibility of soil and water contamination?

To develop this methodology it is essential that the task force is aware of these issues or to include experts that, in a first stage, ensure the inclusion of relevant technical features and, constantly, encourage the knowledge disclosure to the bank’s internal team.

As a consequence, it becomes necessary that the task force on credit risk obtains specific knowledge on this issue, in order to:

a) create risk matrixes per sector;

b) develop a list of questions that must comprise loan application forms;

c) develop knowledge in order to be able to conduct an environmental and social risk assessment;

Bank cashiers must be trained so they are able to help clients to correctly answer questions on environmental issues that are included in loan application forms.

Source: Banca e Seguros, Ambiente e Sociedade – Guia para a inclusão dos riscos ambientais e sociais na concessão de crédito dos bancos Portugueses. Sustentare. 2007
According with UNEP FI, financial institutions can develop a set of tools in order to incorporate risks coming from Biodiversity issues:

**Checklists**: Sector specific checklists can be used to screen project or transaction BES risks. They are particularly useful during the initial stages of due diligence to ascertain whether a transaction deserves more in-depth BES assessment based on project (location, sector, scale) and client (capacity, commitment and track record);

**Environmental and Social Impact Assessment (ESIA)**: For project finance and other transactions where use of proceeds is known, project sponsors may be required to prepare an ESIA as part of permitting and financing requirements. For projects where significant BES risks are apparent (e.g. high-risk sectors operating in biodiversity rich environments) the ESIA process should specifically address BES risks (including direct, indirect and cumulative aspects). This may necessitate the appointment of specialists (especially where there are interactions between biodiversity and social issues). BES assessment may take time (often up to a year) and can affect decision and investment timetables;

**Client Risk Assessment (CRA)**: Most institutions will have developed CRA tools to determine a client’s credit worthiness and it may be the case that the addition of specific questions relating to a client’s commitment, capacity and track record on environmental and social issues is all that is required. Emerging industry-standard due diligence include questions around:

- **Commitment**: Evidence of policies, management systems (which reflect the full scope of BES risks – including third parties and supply chains) accountabilities and responsibilities, disclosure and reporting;
- **Capacity**: Evidence of training and head count for effective management of BES issues, and capacity for stakeholder engagement on these issues;
- **Track record**: Evidence that management of BES risks has improved over time, demonstration of compliance with regulations, effective stakeholder engagement (including local communities and, as appropriate, international NGOs).

**Environmental Audit**: For existing projects or assets, an environmental audit helps to clarify whether there are specific liabilities or risks that need to be factored into credit and other decision making. Where the asset/activity is associated with natural habitats or biodiversity (including through the sourcing of materials such as timber), it is important to specifically include BES aspects in the scope of the audit.

**Biodiversity Action Plan (BAP)**: In situations where a project has a potentially significant impact on biodiversity, a BAP may be an appropriate vehicle through which risks can be managed over the course of the transaction/life of project. A BAP serves to (i) define biodiversity impacts associated with a transaction; (ii) determine how impacts can be mitigated; (iii) establish the baseline and identify key performance indicators; and (iv) identify responsibilities and resource needs for management. BAPs are increasingly being used in loan documentation (both as conditions of disbursement and covenants) to maintain leverage over the course of the transaction.

This type of actions are gradually becoming part of the documents and approaches implemented when a loan is analysed.
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