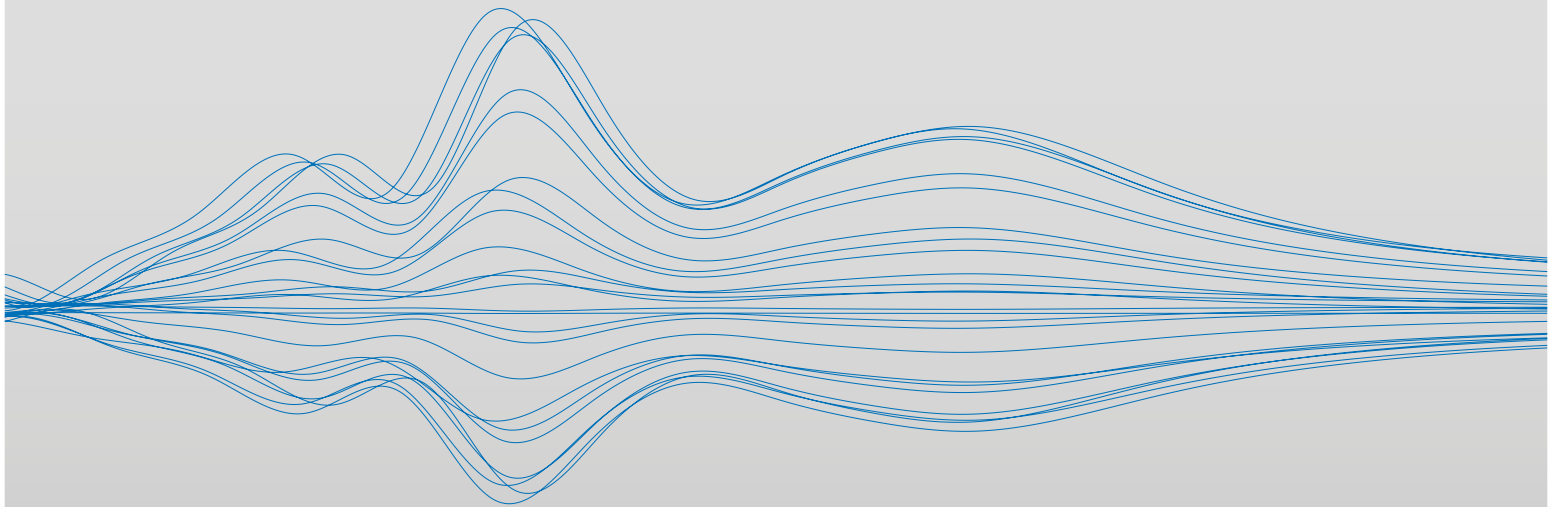


Three ESG steps to ensure
your project remains
bankable in 2021



Version four of the [Equator Principles \(EP4\)](#), the international environmental and social baseline for project finance, will take effect on 1 October 2020 following a three-month COVID-related delay from the original commencement date of 1 July 2020.

In addition to [various changes that broaden the scope of its application](#), EP4 introduces three important new requirements – human rights impact assessment, climate change risk assessment and free, prior and informed consent of affected Indigenous peoples. Because these new requirements exceed requirements for environmental and social impact assessment under domestic laws in most jurisdictions, sponsors will need to take specific steps to ensure they meet these requirements in order for projects to remain bankable in 2021 and beyond.

Human rights impact assessment

EP4 requires an assessment of human rights risks and impacts of the project, conducted with reference to the [UN Guiding Principles on Business and Human Rights \(UNGP\)](#), in particular the human rights due diligence framework under the UNGP. In order to meet this requirement, sponsors will need to identify and assess any actual or potential adverse human rights impacts of the project (including during detailed design, construction and operation), including by consultation with potentially affected groups and other relevant stakeholders, as well develop measures to integrate responses to those impacts into relevant project plans.

Any assessment will need to take into account potential impacts on human rights articulated in relevant international instruments – including rights not to be subjected to slavery, servitude or forced labour, rights to privacy, rights to work and to enjoy just and favourable conditions of work and to elimination of discrimination in respect of employment and occupation. Effective assessment of relevant impacts requires cooperation and coordination across business functions and supply chains, which can be challenging to execute during project development, particularly where detailed design, and procurement and offtake efforts are ongoing, and requires careful planning.

The assessment should be integrated into a structured internal and external stakeholder engagement program that is not only capable of meeting the requirements of domestic laws and the UNGP but which is, consistent with best practices, also suitable as an input into a project-wide materiality assessment and can underpin future sustainability monitoring and reporting efforts.

Climate change risk assessment

EP4 requires an assessment of climate change risk for all projects with potential adverse environmental and social risks, even where those risks may be limited (i.e. few in number, generally site-specific, largely reversible and readily addressed through mitigation measures). Climate change risk assessment is also required for all projects where combined scope 1 emissions (i.e. on-site emissions) and scope 2 emissions (i.e. emissions from generation of purchased energy) are expected to be more than 100,000 tonnes of CO2 equivalent annually, even if the project otherwise has no, or minimal, environmental and social risks.

The assessment is required to be aligned with the [Recommendations of the Task Force on Climate-related Financial Disclosures \(TCFD Recommendations\)](#), taking into account both transition risks (i.e. risks arising from policy, legal, technology and market changes to address climate change mitigation and adaptation) and physical risks, both acute (i.e. extreme weather events) and chronic (i.e. resulting from longer-term shifts in weather patterns). Consistent with the TCFD Recommendations, risks should be assessed under a range of scenarios, both in terms of projected warming and policy responses, to inform views in relation to the climate resilience of the project and allow for development of options to improve resilience through the design process.

The assessment for projects with combined scope 1 and 2 emissions over the 100,000 tonne CO2 equivalent threshold is required to include an alternatives analysis, evaluating technically and financially feasible and cost-effective options to reduce project-related greenhouse gas emissions during the design, construction and operation of the project. Alternative analyses will need to include evidence of options considered and justify why applicable alternatives were not selected.

In line with the TCFD Recommendations and best practices, climate risks – and opportunities – should be taken into account as early as possible in the development of the project and fully integrated into the design process, rather than left until commencement of environmental and social assessment processes or formal engagement with lenders.

Free, prior and informed consent of affected Indigenous peoples

EP4 requires that sponsors obtain the free, prior and informed consent of affected Indigenous peoples where projects impact on lands and natural resources subject to traditional ownership or under customary use, require relocation of Indigenous peoples, have significant impacts on critical cultural heritage or use cultural heritage for commercial purposes. From the commencement of EP4 this requirement will apply globally – in contrast to the position under the previous version where, in high income OECD countries (referred to as 'Designated Countries'), compliance with domestic laws was sufficient.

This change will have significant practical impacts for projects in those countries, which includes Australia, Canada, Denmark, Finland, Norway, New Zealand, Sweden and the United States. In particular, in jurisdictions where it is not a strict requirement of domestic law to obtain the consent of Indigenous peoples – which includes Australia, where rights can be obtained in land in which native title does or may exist without the consent of the relevant Indigenous peoples (for example, because tenure was granted prior to lodgement of a native title claim or by reliance on a determination by the National Native Title Tribunal in the absence of agreement) – sponsors are likely to find that their project will be unbankable without an agreement with affected Indigenous peoples, except perhaps in very limited cases.

Even where agreement has been obtained, EP4 requires independent evaluation of the consultation process. In order to meet this requirement, sponsors need to be aware that the fact of having reached agreement may not be sufficient and that they should take steps to ensure that the negotiation and consultation process is adequately documented in order to demonstrate that the agreement was the product of fully informed consultation.

Not just for new projects

EP4 applies expressly to expansions or upgrades of existing projects. This has particular implications for human rights impact assessment and free, prior and informed consent of affected Indigenous peoples because while the requirements may be notionally limited to the expansion or upgrade, in practice stakeholders are likely to expect historical impacts to be taken into account, which may be challenging for projects not previously subject to such requirements.

The changes to EP4 are reflective of the finance community's increasingly elevated expectations in relation to environmental, social and governance (ESG) performance. In a project development context, sponsors need to be live to these heightened expectations from the early design phases of the project and to take steps to embed relevant assessments into the development phase, or risk the project's bankability when it comes time to secure finance.

For further advice on fulfilling the requirements of EP4 and integrating robust sustainability and ESG practices into your business, please contact Rhys Davies, Steven Gray or Daniel D'Ambrosio.



Rhys Davies

Partner, International Sustainability & ESG Lead

rhys.davies@dlapiper.com



Steven Gray

Counsel, Climate Change

steven.gray@dlapiper.com



Daniel D'Ambrosio

Associate, Business & Human Rights

daniel.dambrosio@dlapiper.com



Natasha Luther-Jones

Global Co-Chair, Energy and Natural Resources Sector

International Co-Head, Sustainability and ESG
natasha.luther-jones@dlapiper.com



JP Douglas-Henry

Global Co-Chair, Litigation and Regulation
International Co-Head, Sustainability and ESG

jp.douglashenry@dlapiper.com

