European Investment Bank

The EIB and Carbon Finance
Frequently Asked Questions (FAQs)

General	The scientific evidence of climate change is now widely accepted, as is the need to urgently address its causes, notably Greenhouse Gas (GHG) emissions. The EU is at the forefront of international efforts to combat climate change and has played a key role in the development of the two major treaties addressing the issue, the 1992 United Nations Framework Convention on Climate Change and its Kyoto Protocol, agreed in 1997. Protection and improvement of the environment, including tackling climate change, are key priorities for the European Union (EU) and for the European Investment Bank (EIB), the Bank promoting European objectives. In support of the EU's objectives on Climate Change, the EIB has established financing objectives that give priority to Renewable Energy; Energy Efficiency; Security and Diversity of Energy Supplies; Research into new Energy Technologies as well as Carbon Finance.
Q	**What is Carbon Finance?**
A	Carbon finance is the general term applied to resources provided to a project to acquire appropriately certified greenhouse gas (GHG) emission reductions ("carbon" for short). The purchaser can then use these reductions to meet, for example, obligations to reduce carbon emissions which may have been incurred under EU or national legislation. Commitments of finance for the purchase of carbon have grown rapidly since the first carbon purchases began in 1996. Carbon funds are financial entities which facilitate the operation of carbon finance.
Q	**What is the EIB involvement in Carbon Finance?**
A	The carbon finance activities of the EIB, through its sponsoring of carbon funds, are a natural extension of the Bank's mission to further the climate change objectives of the EU. The EIB is currently involved with (4) carbon funds. The pioneering EU Emissions Trading Scheme (EU ETS), launched on 1 January 2005, is a system for trading carbon credits or "allowances" between the installations bound by the enabling legislation. It has become the cornerstone of EU efforts to reduce emissions cost-effectively. The carbon credits which the EIB´s carbon funds are concerned with are of the types which are eligible for meeting EU ETS obligations.

Q	Why does the EIB sponsor carbon funds?
A	The EIB decision to support carbon funds (in close collaboration with the EU Commission; International Finance Institutions (IFIs); governments and corporates) is in recognition of the contribution that these funds can make to reducing Climate Change through the development of the carbon market. Climate change is a prime example of a global market failure – in this case, the costs of GHG emissions are ignored by households and businesses in taking everyday consumption and investment decisions. It is the responsibility of the EU and its Member States to act where appropriate to address such market failures. EIB has a key role to play in support of European efforts to tackle climate change. The EIB sponsors carbon funds by investing in the establishment of new funds, thereby creating additional organisational capacity and expertise; providing risk capital and developing new financial instruments to meet the needs of the developing carbon market. The aim of these carbon funds is to support the EU's climate change policy and assist Member States meet their obligations under the Kyoto Protocol through: • financing of environmentally beneficial projects; • supporting the project based carbon credit mechanisms established by the Kyoto Protocol; • assisting compliance purchasers of carbon credits to meet their legal obligations under EU legislation; • reinforcing the EU ETS market mechanism.
Q	**Which Carbon Funds does the EIB sponsor?**
A	• The Multilateral Carbon Credit Fund (MCCF) – with EBRD • The Carbon Fund for Europe (CFE) – with IBRD • The EIB-KfW Carbon Programme – with KfW • The Post-2012 Fund – EIB led – under preparation
Q	**Can the EIB acquire carbon credits from projects?**
A	As an Institution, the EIB does not purchase carbon credits directly from projects. Project promoters interested in selling their carbon credits should contact the Carbon Funds directly.
Q	**How can I contact these Carbon Funds?**
A	Contacts for each Carbon Fund are available in the Fund's brochures.
Q	**How much is the EIB investing in these funds?**
A	It is expected that about EUR 500 million in capital will be invested in these four EIB sponsored Carbon Funds by Sovereign States, Corporates and IFIs (including EIB). No cash support was required for the MCCF and the CFE, but the EIB has invested EUR 50 million in the EIB-KfW Carbon Programme and expects to invest the same amount in the Post-2012 Fund; EIB's principal contribution is through the catalytic effect it has achieved by taking the initiative with other parties to establish new organisational capacity and expertise to meet the needs of the Carbon Finance market. At the same time, the EIB's

	involvement leverages substantial additional capital from other participants to complement its own contribution. This contribution arise not only from its investment capital, but also from its project pipeline around the world, its AAA credit rating and reputation/standing or less tangible items such as its project appraisal experience and due diligence capacity.
Q	**Why does the EIB support these particular carbon funds? Is there any duplication of effort between these funds?**
A	Though each of the four EIB sponsored Funds is expected to make a distinct contribution to the development of the EU Carbon Market, they have been designed to complement each other as they are based either on different carbon mechanisms, or serve different geographic areas and client groups or cover different time periods. Each of these four EIB sponsored Funds has a distinct value added which is described in their brochures (see also the Briefing Note on Carbon Funds)**.**
Q	**Why is there a link with developing countries? Aren't carbon reductions in developed countries just as worthwhile?**
A	Yes - they are just as worthwhile, but are subject to different policy mechanisms. In the EU these include notably national and EU caps on CO_2 emissions, feed-in tariffs or green certificates for renewables and combined heat and power, and EU targets for energy efficiency and transport biofuels. The financing requirements for new investments are equally supported by EIB, notably through special loan conditions available under its Climate Change Finance Facility (CCFF). The countries targeted by the Kyoto Protocol and the EIB Carbon Funds are generally those where finance is less available, expertise to develop credits is most scarce and the need for new investment is substantial. By concentrating in these areas, the EIB therefore acts in accordance with the objectives of Kyoto and adds significant value in its own right. Under MCCF, for example, credits can only be acquired from EIB or EBRD financed investments, and therefore are subject to the EIB/EBRD due diligence process. The Banks are, therefore, financing the underlying projects as well as providing a means to support the development and verification of credits, and their sale.
Q	**Doesn't the Bank have a conflict of interest in both financing underlying projects and buying the credits generated through its Carbon Funds?**
A	No. It is important that new "low carbon" projects are financed on the most efficient terms. EIB's lending decisions for investment projects are taken independently from any possible purchase of carbon credits by an EIB backed Carbon Fund. Project promoters always have the option to sell credits to the buyer of their choice – there is no exclusivity for EIB Carbon Funds.
Q	**How do EIB's carbon activities differ from those of the private sector?**
A	The four EIB sponsored Funds are being implemented in partnership with various public and private sector organisations and have focused on building up organisational capacity, expertise and risk capital resources necessary to meet the needs of the Carbon market. These Funds differ from the standard Private Sector "Trading Funds" as they clearly focus on the less developed areas of the Carbon Market. They also differ in that they need substantial 'patient and catalytic public sector capital' to support their long term development, partly because they act to various degrees in anticipation of market and regulatory developments, partly because they cover geographic areas, markets and timescales that the private sector is not yet prepared to meet on its own.

	The intention of the EIB, through its overall investment activities, is to leverage, to the extent possible, the use of private sector capital in supporting low carbon projects and to meet compliance obligations of the participants. In addition, it is also prepared to take such other steps as are necessary in collaboration with the relevant public and private sector institutions to ensure the development of an EU Carbon Market that is capable of meeting EU policy needs.
Q	**What types of carbon credits do EIB Carbon Funds buy? Do they buy only Kyoto Protocol based credits?**
A	The EIB funds buy only the highest quality credits. EIB sponsored funds will purchase mainly project based credits under the Joint Implementation (JI) and Clean Development Mechanisms (CDM) of the Kyoto Protocol, some EU Allowances (under the MCCF), project based Verified Emissions Reductions (VERs), and possibly Assigned Amount Units (AAUs) through "greening" schemes. Joint Implementation refers to projects in industrialised countries which have emission reduction obligations under Kyoto. The Clean Development Mechanism refers to projects in developing countries that do not have greenhouse gas reduction obligations under Kyoto. This concentration ensures that the EIB funds acquire the highest quality (highly regulated and verified) carbon credits.
Q	**What volume of CO_2 transactions will EIB Carbon Funds enable?**
A	This will depend on when credits are delivered and the market prices at this time. However, purely to give an indication, the current market price for credits for delivery in December 2008 (the 'forward contract' with currently the highest volume of trading) is EUR 19 per tonne. At this price, EUR 500 million would buy over 26 million tonnes of carbon. The actual volume achieved, however, may be more or less than this.
Q	**Doesn't the Kyoto Protocol come to a close in 2012? How does the participation in the carbon market contribute to a long-term solution to the long term problem of climate change?**
A	It is true that the current Kyoto period closes in 2012 – and it is undeniable that uncertainty about the post 2012 situation is constraining the development of the market. It is because of the absence of formal, regulated market structures beyond 2012 that the EIB is leading preparation of the path breaking Post-2012 Carbon Fund. This Fund will exclusively acquire highest quality Post-2012 credits. Moreover, it will do so at prices reflecting the longer-term prospects of the market, i.e. above the low prices that apply in the voluntary market which is currently virtually the only basis of selling post 2012 credits. The Fund will therefore considerably enhance market value and certainty for post 2012 credits – and in part set the scene for the post-2012 system. For this reason, the development is welcomed by the private as well as the public sector.
Q	**Do any EIB funds purchase carbon credits from a voluntary or unregulated market? If so, what standards are applied to those credits?**
A	None of the EIB funds have bought voluntary credits to date. The CFE Fund may purchase Verified Emission Reductions (VERs) on the voluntary market subject to the World Bank's due diligence, including the voluntary market's equivalent to compliance grade credits (e.g. WWF Gold Standard). This due diligence is the guarantee of highest quality.

Q	**Do any of the EIB Funds sell carbon credits to non-compliance buyers**
A	The principal purpose of the EIB Funds is to meet purchasers´ compliance obligations under the EU ETS and Member States' commitments under the Kyoto Protocol, but voluntary buyers are not excluded if and when capacity is available.
Q	**What standards will the Bank Funds apply to carbon credits acquired for the regulated market?**
A	The highest standards. The regulated market is generally defined as carbon credits that comply with the requirements of the "flexible mechanisms" of the Kyoto Protocol. The carbon credits purchased under the Bank funds will strictly adhere to the Kyoto Protocol under the UNFCCC, an international Treaty binding on all signatories, which regulates the detailed, rigorous methodologies, and a detailed documentation trail and transaction log, all overseen by the UNFCCC Secretariat as well as the provisions of the EU ETS. These credits are universally recognised as the highest quality credits available in the market.
Q	**What mechanisms exist to ensure that the above UNFCCC standards are met?**
A	Each fund is managed by permanent, dedicated staff to ensure respect of the applicable UNFCCC standards and supported by the resources, experience and processes of the EIB and one or more additional International Financial Institutions.
Q	**How does the Bank make sure that the greenhouse gas reductions would have not taken place anyway?**
A	The UNFCCC verification and registration process is designed to ensure that carbon credits are not granted for greenhouse gas reductions that would have taken place anyway and that the carbon reducing investments do actually take place. The highest standards in the voluntary market are intended to do the same. (e.g. WWF Gold Standard)
Q	**What environmental and other standards does the Bank require of the underlying carbon credit generating projects?**
A	The Bank requires that the underlying carbon credit generating projects meet the standards set under the Kyoto Protocol treaty, as well as the standards required under the EU ETS. In addition, projects have to undergo the rigorous economic, financial, environmental and social due diligence of the EIB and its partner institutions (World Bank, EBRD, KfW) to ensure that the highest international standards are achieved.
Q	**Do the Bank Funds buy carbon credits from forestry and other sink projects, and from large dams; and, if so, what standards must be met?**
A	Yes, as long as they meet the necessary eligibility criteria for carbon credits as dictated by the rules of the UNFCCC and the CDM and JI mechanisms. The MCCF Fund's range of eligible projects is limited in that it may only purchase carbon credits generated from projects financed by the EIB or EBRD and are therefore subject in addition to their respective due diligence process.

Q	**Do the bank Funds purchase carbon credits resulting from projects reducing HFC (hydrofluorocarbon) emissions?**
A	With the exception of the CFE, the EIB funds do not purchase this type of carbon credit.
Q	**How does the Bank determine a "fair" price for carbon credits acquired by its funds?**
A	The responsibility to determine a fair price is that of the Funds themselves and not that of the EIB, which maintains an arms length management relationship with them. As the Carbon Market is currently a young market, regulatory and structural factors play a key role at present, but over time the market balance of supply and demand should determine the appropriate price.
Q	**Does the Bank make a profit from its carbon funds?**
A	The EIB is a not-for-profit public bank with a public policy mission. Its partners in the carbon market have a similar public policy orientation. Whilst recovering its costs, the EIB is able to pursue policy-based objectives, in this instance including development of market capacity to the benefit of all players in the market, and facilitating the financing and implementation of environmentally beneficial projects.
Q	**What is the Bank's reaction to recent media reports critical of the carbon market?**
A	Media reports are making a useful contribution to the public debate and market transparency by looking into recent market developments. It is also helpful that the media highlights controversial or doubtful practices and segments, as this should improve market practice and inform potential customers, to the benefit of overall market credibility and integrity. Part of the recent criticism has focused on some carbon offsetting practices offered on the voluntary market. The criticisms relate primarily to verification and additionality procedures in the voluntary sector which, if correct, need to be addressed. However, the EIB's Funds are NOT involved in such voluntary schemes. All EIB Funds operate in the Kyoto "regulated market" – this part of the market does not suffer from problems of additionality or verification. Other appropriate standards, e.g. the "Gold Standard", would be applied for any "voluntary market" carbon credits purchased. the regulated Kyoto based market is enjoying growing success and gaining credibility every day, as reflected in the price premium for its credits as compared with the voluntary market.
Q	**Some recent commentators have argued that carbon trading is largely discredited as a means of fighting climate change – why is the Bank getting involved?**
A	Carbon trading is an innovative and powerful initiative which European governments and many others worldwide believe has an important role to play in the fight against climate change. But the carbon market is new, and as with any new market, the extent and level of regulation will need to be adjusted in light of experience in order to eliminate unsatisfactory practices and make carbon offsetting a reliable and credible tool to fight climate change.

Q	Has not the European Emissions Trading System already failed? – Why is the Bank endeavouring to prop it up?
A	It is recognised, with hindsight, that the distribution of national allowances under the first phase under the ETS was too generous. This led to considerable price volatility and subsequently low prices within Phase I (2005-2007). In contrast, post-2008 prices in Phase II are much stronger. The Commission has also imposed much more stringent allocations in its assessment of second phase National Allocation Plans. This should ensure that, going forward, the EU ETS will deliver an ambitious and meaningful environmental contribution in the fight against climate change, underlining the EU's leadership in this field.
Q	**Carbon credits are a poor second best to actually reducing CO2 emissions. What is EIB doing about that?**
A	The most significant contribution that the Bank can make to implement the EU policy on Climate Change will be through the implementation of the EU Climate Change Policy objectives, in particular by supporting "low carbon generation" project investments. EIB has already taken a series of initiatives such as the financing of carbon funds as well as the introduction of new financial instruments such as RSFF (to finance research into Energy Technologies); CCFF (the Climate Change Finance Facility) and CCTAF (the Climate Change Technical Advisory Facility) to reinforce its effectiveness in meeting these EU objectives. In 2006, the EIB signed loan agreements for 96 environmental projects, amounting to EUR 10.9bn, which represents 23.7% of its total lending.
Q	**Has the EIB assessed its own impact to the environment? What does it do to minimise it?**
A	The EIB's impact as an organisation is minimal as compared to its contribution in mitigating climate change through its financing activities. Nevertheless, EIB is particularly attentive to the impact of its own organisation as shown through the environmental considerations that played an important role in the construction of its new extension. More details are in the Bank's 2006 Social Corporate Responsibility report.
Q	**What is the EIB's carbon footprint? How is it being managed?**
A	The EIB is currently examining its overall carbon footprint, including effects of its project financing on carbon emissions. In the meantime it is in the process of developing and applying an improved internal carbon management system (housekeeping), which inter alia involves the purchase of its internal energy requirements from renewable energy resources.