



## The Sheppard Mullin Six SOCIAL LOAN PRINCIPLES

Investors are increasingly focused on Environmental, Social, and Governance (ESG), and more companies are reporting on these statistics. Reporting on ESG metrics is challenging because there is a lack of consistency in the market as to what ESG is, how to measure whether ESG is successful, and how that success is rewarded. In the debt capital markets, industry trade groups are working to provide market participants with ESG reporting frameworks in order to unite these ESG reporting efforts and move towards a more uniform reporting standard. The latest proposed framework is the Social Loan Principles published by the Asia Pacific Loan Market Association, the Loan Market Association and the Loan Syndications & Trading Association.

### Here are six key items to be aware of today regarding the Social Loan Principles:

**What are They?** Social Loan Principles (SLP) are voluntary guidelines issued in April 2021 by several prominent loan market associations to provide a framework for borrowers and lenders to identify, measure and report on loans used to finance or re-finance a “Social Project” (as described in the SLP). The SLP aim to promote transparency, disclosure and reporting, with the ultimate goal of encouraging growth of loans targeted at Social Projects by providing investors a means to verify that their investments are being utilized effectively.

**Why do They Matter?** Demand is booming for investments that expressly support positive outcomes for society as a whole, as well as marginalized demographics. The International Capital Market Association (ICMA) has published for a number of years its Social Bond Principles (SBP). Issuance of bonds that expressly identify themselves as being “social bonds” of a type identified by the SBP grew eightfold to \$154 billion in 2020, according to Bloomberg. The loan market has followed ICMA’s lead and created the SLP. The demand, and the response by the industry groups, is part of the widely-reported trends towards a broader Environmental, Social, and Governance (ESG) focus from investors and reporting by an increasing number of companies. The scope of what constitutes ESG and how it is measured remains a challenge for market participants. The SLP are one attempt to move towards a consistent methodology for use in the social loan market.

### What are the core principles of the SLP?

1. The borrower must use the proceeds of such loan for a Social Project.
2. The borrower of a social loan must clearly communicate to lenders the (a) Social Objectives, (b) Process to determine how the project fits into an eligible category of Social Project, and (c) Eligibility criteria for borrower to determine an eligible Social Project.
3. The borrower should credit proceeds to a specific account and track them clearly and appropriately.
4. The borrower should keep updated records on the use of proceeds and how funds are allocated for each Social Project. Where feasible, the reporting should include quantitative performance measures and the impact of the social project on the Target Population.

**What is a Social Project?** The SLP describe Social Projects as projects that “directly aim to address or mitigate a specific social issue and/or seek to achieve positive social outcomes especially but not exclusively for a target population(s). A social issue threatens, hinders or damages the well-being of society or of a specific target population.” The SLP provide a non-exhaustive list of potential target populations, and acknowledge that the definition of a target population can vary, and may be the general public in some cases.

**Does a Social Loan Require 3rd Party Review?** The SLP recommend a third-party external review where appropriate, but Borrower self-certification may be enough in many cases to certify that a borrower’s project meets the requirements of a Social Project under the SLP. A consultant with recognized expertise may be able to verify the process of choosing a Social Project or provide an opinion to that effect. Auditors or independent ESG rating providers may be able to verify that certain projects align with internal company standards as well. In some cases, there may be a certification process the borrower can undergo in order to confirm its internal processes or reporting procedures. When following other frameworks that operate in a similar way as the SLP, many participants have found that investors and lenders highly value (and often require) independent third party verification and public reporting of both the use of funds and the progress made toward achieving stated goals.

**Are There Other Options if My Company Does Not Have an Eligible Social Project or Social Loan?** Yes. The SLP are the latest addition to a group of frameworks published by industry groups active in the debt capital markets. The SLP are structured similar to the Green Loan Principles (February 2021) and the Sustainability-Linked Loan Principles (May 2020), which were both previously published by the same working group of industry associations as published the SLP. If your company does not have an eligible Social Project under the SLP, it may have a Green Project or may be a candidate for setting sustainability-linked goals that can be tied to the pricing of a sustainability-linked loan. The SLP, the Green Loan Principles and the Sustainability-Linked Loan Principles also have parallel frameworks that can be used by bond issuers.

## Key Contacts - Social Loan Principles



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Ben helps developers, utilities, infrastructure funds, banks and institutional investors finance, buy and sell infrastructure projects, and advises the companies that develop and own those projects, across the United States. While his experience spans asset classes and transaction types, he focuses on tax credit monetization transactions and renewable energy generation facilities.



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