Options for Mitigation and Offset Financing

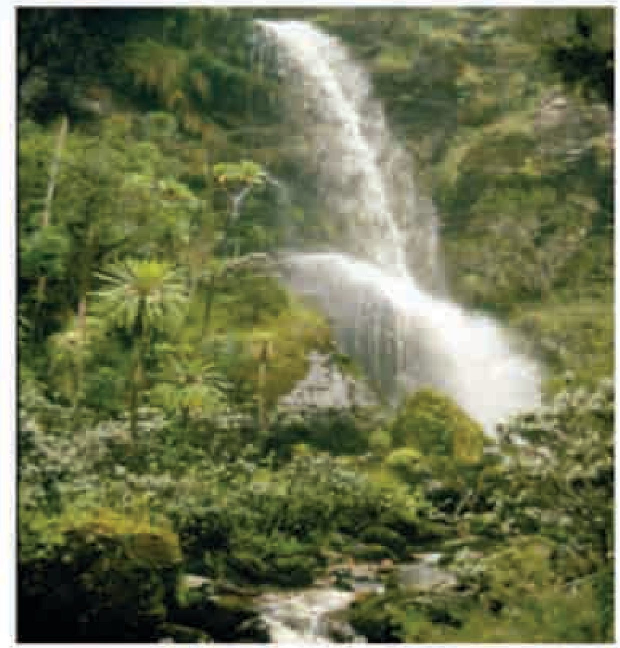
Mainstreaming the Mitigation Hierarchy in Impact Assessment
IAIA Washington, DC
November 2017

Biodiversity Offsets – Growing opportunity

- Increasing uptake of mitigation hierarchy

- Growing regulation requiring offsetting

- Institutional funding beginning to target offsets



Some Challenges for Offset Financing

- Inadequacy of funding
- Insecurity of funding
- Timing of funding to address impacts
- Stringent requirements and conditions for funding (additionality, permanence)

Three finance pillars

- **UPFRONT FINANCE:** Complete lump sum funding early on

- **ONGOING FINANCE:** Regular ongoing payments

- **FINANCIAL GUARANTEES:** Financial safeguards to protect against non payment risk

Upfront Finance

BALANCE SHEET FINANCE

- Project developer utilises their own balance sheet capital – simple and straight-forward

PROJECT LOANS

- Wrapping mitigation & offset costs into general project finance

FREESTANDING LOANS

- Bespoke loans issued solely for the purpose of financing an offset

BONDS

- "Green" Bond collateralized with annual revenues

On-going Finance

ANNUAL PAYMENTS

- Annual payments over the life of projects

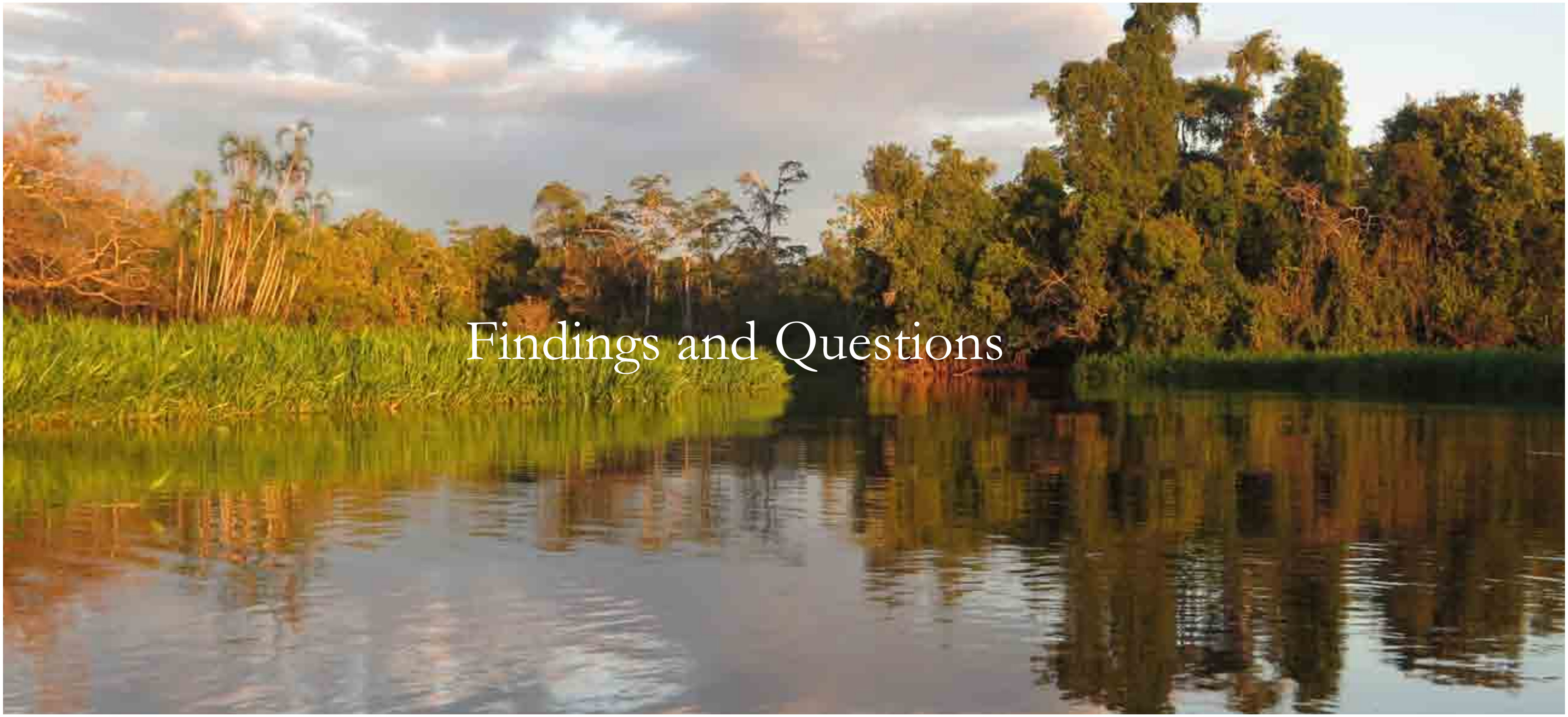
REVENUE-BASED FUDNING - ROYALTIES

- Retained percentage revenue stream from company income source

Finance Guarantees

Financial safeguards to protect project finance reduce investor risks and protect against failure

- Insurance products
- Captive insurer
- Performance bonds
- Irrevocable letters of credit



Findings and Questions

Upfront versus Variable Funding

- Securing upfront capital to fully finance an offset reduces systemic and specific risks
- Ensures against temporal losses
- Institutionally sourced upfront financing should be prioritised
- Need for accurate and consistent valuations to ensure the offset is fully financed through to delivery

The importance of regulation - Building offset requirements

- **Regulation** increases the ability to mobilise finance
- Requires adherence to **the mitigation hierarchy** - - creates demand
- Create **compliance and liability framework** as a template for regulated offsets

Some Constraints Under Current Conditions

- Voluntary offsets offer **insufficient certainty** for investors
- No **on-demand** offsets (aggregation/banking); Time and cost lag.
- Development and Equator banks are committed to apply standards but generally lack dedicated financing options

Further Analysis

- Promising application of offset covenants to finance agreements should be expanded
- Options for different financial instruments
- Some standards should be relaxed to stimulate greater upfront funding – offsets in PA's?
- Will ability to transfer liability increase interest in early financing?
- Development of insurance products remains challenging and requires further study
- Need reliable, effective, third-party institutions to ensure financing, permanence, additionality and equivalence (CTFs)