Social Loan Principles

APLMA Asia Pacific Loan Market Association

LMA Loan Market Association

LSTA

Introduction

The social loan market aims to facilitate and support economic activity which mitigates social issues and challenges, and/or achieves positive social outcomes. The Social Loan Principles ("SLP") have been developed by an experienced working party consisting of representatives from leading financial institutions and law firms active in the global loan markets, with a view to promoting the development and integrity of the emerging social loan product.

The SLP aim to create a high-level framework of market standards and guidelines, providing a consistent methodology for use across the social loan market, whilst allowing the loan product to retain its flexibility and preserving the integrity of the social loan market while it develops.

The SLP comprise voluntary recommended guidelines, to be applied by market participants on a deal by deal basis depending on the underlying characteristics of the transaction, which recommend transparency and disclosure and seek to promote the integrity in the development of the social loan market by clarifying the instances in which a loan may be categorised as being "for social purposes".

The SLP build on and refer to the Social Bond Principles ("SBP") administered by the International Capital Markets Association ("ICMA"), with a view to promoting consistency across financial markets. The SBP are one of the main internationally recognised voluntary issuance guidelines that promote transparency, disclosure and reporting in the social bond market.

The SLP are intended for broad use by the market, providing a framework within which the flexibility of the loan product can be maintained, and will be reviewed on a regular basis in light of the development and growth of social loans. The SLP are designed to drive the provision of information needed to increase capital allocation to financings for social purposes.

It is envisaged that on some occasions, the SLP will be used together with the SBP. For example, an issuer may issue social bonds using the SBP, and thereafter, when it comes to using the proceeds of the bond issue, the issuer may act as a lender and use the SLP to provide social loans to one or more ultimate borrowers. In such cases, the consistency of the objectives and of the Social Project eligibility criteria of these instruments should be ensured.

In a similar way, it is envisaged that the SLP may be used by an original borrower to borrow an initial social loan, and thereafter, the original borrower may act as lender to provide social loans to one or more ultimate borrowers. This is more likely to be the case where the original borrower is a government or semi-public institution such as a municipality or a development finance institution. Each of the loans will need to comply with all the core components of the SLP to be classified as a social loan, and care will need to be taken to avoid the double counting of any such social loans.

Social Loan Definition

Social loans are any type of loan instrument made available exclusively to finance or re-finance, in whole or in part, new and/or existing eligible Social Projects (see Section 1 Use of Proceeds). Considerations for revolving credit facilities are set out in Appendix 3.

"Social Projects" will often fall within the non-exhaustive, indicative categories of eligibility set out in Appendix 1.
It is acknowledged that viable Social Projects will vary and may fall within more than one eligible project category.

Social loans must also align with the four core components of the SLP, as set out below. Social loans should not be considered interchangeable with loans that are not aligned with the four core components of the SLP.

Social Loan Principles – Core Components

The SLP sets out a clear and transparent framework, enabling all market participants to understand clearly the characteristics of a social loan, based around the following four core components:

1. **Use of Proceeds**
2. **Process for Project Evaluation and Selection**
3. **Management of Proceeds**
4. **Reporting**

1 Use of Proceeds

The fundamental determinant of a social loan is the utilisation of the loan proceeds for Social Projects (including other related and supporting expenditures), which should be appropriately described in the finance documents and, if applicable, marketing materials for the financing. All designated Social Projects should provide clear benefits of a social nature, which, where feasible, will be assessed, quantified, measured and reported by the borrower.

Where funds are to be used, in whole or part, for refinancing, it is recommended that borrowers provide an estimate of the share of financing versus refinancing. Where appropriate, they should also clarify which investments or portfolios may be refinanced, and, to the extent relevant, the expected look-back period for refinanced Social Projects.

A social loan may take the form of one or more tranches of a loan facility, and may be made by way of a term loan or revolving credit facility. Considerations for revolving credit facilities are set out in Appendix 3.

The SLP explicitly recognise several broad categories of eligibility for Social Projects. The non-exhaustive list of Social Projects set out in Appendix 1 is intended to capture the most usual types of projects supported and expected to be supported by the social loan market.

Social Projects 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. For the avoidance of doubt, it is acknowledged that the definition of target population can vary depending on local contexts and that, in some cases, such target population(s) may also be served by addressing the general public. A target population will often fall within the non-exhaustive, indicative categories set out in Appendix 2.

2 Process for Project Evaluation and Selection

The borrower of a social loan should clearly communicate to its lenders:

- the social objective(s);
- the process by which the borrower determines how the project(s) to be funded fit within the eligible Social Project categories set out in Appendix 1; and
- the related eligibility criteria, including, if applicable, exclusion criteria or any other process applied to identify and manage potentially material social and environmental risks associated with the proposed projects.

Borrowers are encouraged to position this information within the context of their overarching objectives, strategy, policy and/or processes relating to sustainability. Borrowers are also encouraged to disclose any social standards or certifications referenced in project selection.

3 Management of Proceeds

The proceeds of a social loan should be credited to a dedicated account or otherwise tracked by the borrower in an appropriate manner. Management of proceeds should be attested to by the borrower in a formal internal process linked to the borrower’s lending and investment operations for Social Projects, so as to maintain transparency and promote the integrity of the product. Where a social loan takes the form of one or more tranches of a loan facility, each tranche applicable to the Social Project must be clearly labelled, with proceeds of such tranche(s) credited to a separate account or tracked by the borrower in an appropriate manner.

Borrowers are encouraged to establish an internal governance process through which they can track the allocation of funds towards Social Projects.

4 Reporting

Borrowers should make and keep readily available up to date information on the use of proceeds, such information to be renewed annually until the social loan is fully drawn, and as necessary thereafter in the event of material developments. This should include a list of the Social Projects to which the social loan proceeds have been allocated and a brief description of the projects, the amounts allocated and their expected impact. Where confidentiality agreements, competitive considerations, or a large number of underlying projects limit the amount of detail that can be made available, the SLP recommend that information is presented in generic terms or on an aggregated project portfolio basis. Information need only be provided to those institutions participating in the relevant social loan.

Transparency is of particular value in communicating the expected impact of projects. The SLP recommend the use of qualitative performance indicators and, where feasible, quantitative performance measures, including the disclosure of the key underlying methodology and/or assumptions used in any quantitative determination. Borrowers with the ability to monitor achieved impacts are encouraged to include those in regular reports.

Review

Where appropriate, an external review is recommended. There are a variety of ways for borrowers to obtain outside input regarding the core components under the SLP and there are also several types of review that can be provided to those institutions participating in the social loan. Such guidance and external reviews might include:

Consultant review – a borrower can seek advice from consultants and/or institutions with recognised expertise in their area. **"Second party opinions"** may also fall into this category.

Verification – a borrower can have its social loan, associated loan framework, or underlying assets independently verified by qualified parties, such as auditors or independent ESG[1] rating providers. In contrast to certification, verification may focus on alignment with internal standards or claims made by the borrower.

Certification – a borrower may have its social loan or associated loan framework certified against an external assessment standard. An assessment standard defines criteria, and alignment with such criteria and is tested by qualified third parties/certifiers.

Rating or Scoring – a borrower can have its social loan or associated loan framework rated by qualified third parties, such as specialised research providers or rating agencies.

An external review may be partial, covering only certain aspects of a borrower's social loan or associated loan framework or full, assessing alignment with all four core components of the SLP. It should be made available to all institutions participating in the social loan on request. When appropriate, and taking into account confidentiality and competitive considerations, borrowers should make publicly available the external review, or an appropriate summary, via their website or otherwise.

Alternatively, given that the loan market is traditionally a relationship-driven market and therefore lenders are likely to have a broad working knowledge of the borrower and its activities, self-certification by a borrower, which has demonstrated or developed the internal expertise to confirm alignment of the social loan with the key features of the SLP, may be sufficient. Nonetheless, borrowers are recommended to document thoroughly such expertise, including the related internal processes and expertise of their staff. This documentation should be communicated to institutions participating in the loan on request. When appropriate, and taking into account confidentiality and competitive considerations, borrowers should make publicly available, via their website or otherwise, the parameters on which they assess Social Projects, and the internal expertise they have to assess such parameters.

1. Environmental, social and governance.

Appendix 1

Indicative (Non-Exhaustive) Categories of Eligibility for Social Projects

The categories, listed in no specific order, include, but are not limited to:

- Affordable basic infrastructure (e.g. clean drinking water, sewers, sanitation, transport, energy, basic telecommunications).
- Access to essential services (e.g. education and vocational training, public health/healthcare, public health emergency response energy (including electricity), financing and financial services, other governmental offices servicing select populations (and/or in low /low-middle income countries)).
- Affordable housing.
- Employment generation, and programs designed to prevent and/or alleviate unemployment stemming from socioeconomic crises, including through the potential effect of small and medium enterprise financing and microfinance.
- Food security and sustainable food systems (e.g. physical, social, and economic access to safe, nutritious, and sufficient food that meets dietary needs and requirements; resilient agricultural practices; reduction of food loss and waste; and improved productivity of small-scale producers).
- Socioeconomic advancement and empowerment (e.g. equitable access to and control over assets, services, resources, and opportunities; equitable participation and integration into the market and society, including reduction of income inequality).

Appendix 2

Target Populations

Examples of target populations include, but are not limited to, those who are:

– Living below the poverty line;[2]

– Excluded and/or marginalised populations and/or communities;

– People with disabilities;

– Migrants and/or displaced persons;

– Undereducated;

– Underserved, owing to a lack of quality access to essential goods and services;[3]

– Unemployed;

– Women and/or sexual and gender minorities;

– Aging populations and/or vulnerable youths; and

– Other vulnerable groups, including as a result of natural disasters.

Appendix 3

Application to Revolving Credit Facilities

The SLP were drafted such that they can be applied to a wide variety of loan instruments, including term loans and revolving credit facilities.

One of the fundamental determinants of a social loan is the utilisation of the loan proceeds, which should be appropriately described in the finance documents and, if applicable, marketing materials. The use of proceeds component of a term loan is often easily identifiable. Revolving credit facilities, however, may not identify in similar detail such social use of proceeds, but in any case should follow the list of eligible Social Projects set out in Appendix 1 throughout the lifetime of the revolving credit facility. The parties to any proposed social loan taking the form of a revolving credit facility will need to determine how best to evidence the flow of funds to an agreed upon social objective when applying the SLP to such a loan. A revolving credit facility may include a specific social tranche but, where not possible, a borrower may seek to report to the lenders the use of any revolving borrowings and/or identify Social Projects supported by the revolving credit facility.

Lenders may seek to monitor and validate the sustainability information provided by the borrower during the life of the loan, mindful of the need to preserve the integrity of the social loan product. In the absence of sufficient internal expertise at the lender to monitor the loan, external review is strongly recommended. Revolving credit facilities for general corporate purposes should not be categorised as "social" without satisfying the components listed in the SLP.

2. in accordance with local/regional definitions.
3. As above.