



**LEGAL**

# **Public debt and climate change: selected legal issues**

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# How could climate affect public debt legal framework?

- Borrowing objectives
- Borrowing purposes
- Borrowing authorization
- Natural disaster management
- Public investment
- Green/social/sustainable bonds
- Reporting requirements
- Debt transparency



*"Yes, the planet got destroyed. But for a beautiful moment in time we created a lot of value for shareholders."*

CartoonStock.com

***Strong underlying legal framework for PDM: definitions and coverage, borrowing authority, reporting and disclosure, accountability mechanisms***

## **Relevant legal instruments**

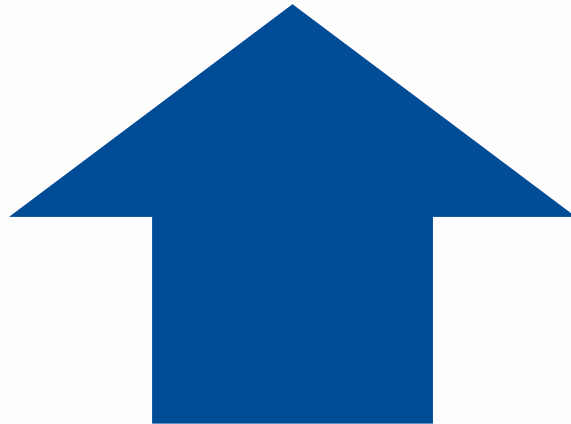
**PDM / PFM / debt  
transparency laws**

**Climate change,  
environmental laws**

**Related secondary  
legislation**

# Balancing borrowing objectives and principles with climate considerations

*“The main objective of public debt management is to ensure that the government’s financing needs and its payment obligations are met at the lowest possible cost over the medium to long run, consistent with a prudent degree of risk.”*



## Climate Change Act

*Financial policies, financial management, support for capitalization and borrowing, by the State and private entities, must adopt the following guiding principles on climate matters:*

*a) Principle of **prioritization**, aiming that financial programming, in the public and private sector, **consider and contribute to climate policy objectives**;*

*...*

*d) Principle of accountability and prudence, aimed at **incorporating climate risks in the assessment of assets and liabilities**...*



## Public Debt Management Act

*The management of direct public debt shall be guided by **principles of discipline and efficiency**, ensuring the availability of the financing required by each budgetary period, in line with the following objectives:*

*a) Minimization of direct and indirect costs from a long-term perspective*

*...*

*d) non-exposure to exaggerated risks*

*...*

# Referring to climate-related aspects in borrowing purposes

*“state loans” may be used for “creating new jobs and improving **social and ecological conditions** in the country” or “**liquidation of the consequences of natural disasters** and other exceptional situations”*

*“Government debt shall be incurred and used for ... **protection against or elimination of consequences caused by natural and environmental disasters**”*

# Coordinating climate institutions borrowing powers and borrowing authority framework

## National Council on Climate Change

### Nigeria Climate Change Act 2021 Sections 3 and 17

- National Council on Climate Change is charged, i.a., with ensuring “the mainstreaming of climate change into the national development plans and programmes” and mobilizing “financial resources to support climate change actions.”
- The Council may “**borrow money** from financial organisations or other institutions **for the purpose of executing its mandate** under [the Climate Change] Act.”

## Borrowing under the PDM framework

### Nigeria Fiscal Responsibility Act 2007 Section 44

- Any Government in the Federation or its agencies and corporations must specify the purpose for which the borrowing is intended and **provide a cost-benefit analysis**
- Borrowing must comply with the condition of the “existence of **prior authorization in the Appropriation or other Act or Law** for the purpose for which the borrowing is to be utilized...” and is **subject to limits**
- DMO shall maintain **electronic database** of internal and external public debts

# Safeguarding public finance in the context of natural disaster management spending

- **Conditions for the declaration of emergency**
- Consequences of the declaration of emergency
  - ▶ “bypassing” normal requirements
  - ▶ spending categorization, controls
  - ▶ fiscal rules escape clauses
  - ▶ exceptional invocation of monetary financing by the CB (CB as the emergency lender of the State)
- **Flexibility in using budgetary resources with ex post safeguards (controls, audits, reporting)**

Climate, natural disaster/emergency funds, contingency reserves

- contingency allocations
- climate funds: purpose and objective; geographical scope
- objectives, governance, investment of resources

# Integrating climate aspects into public investment

## Selected legal considerations



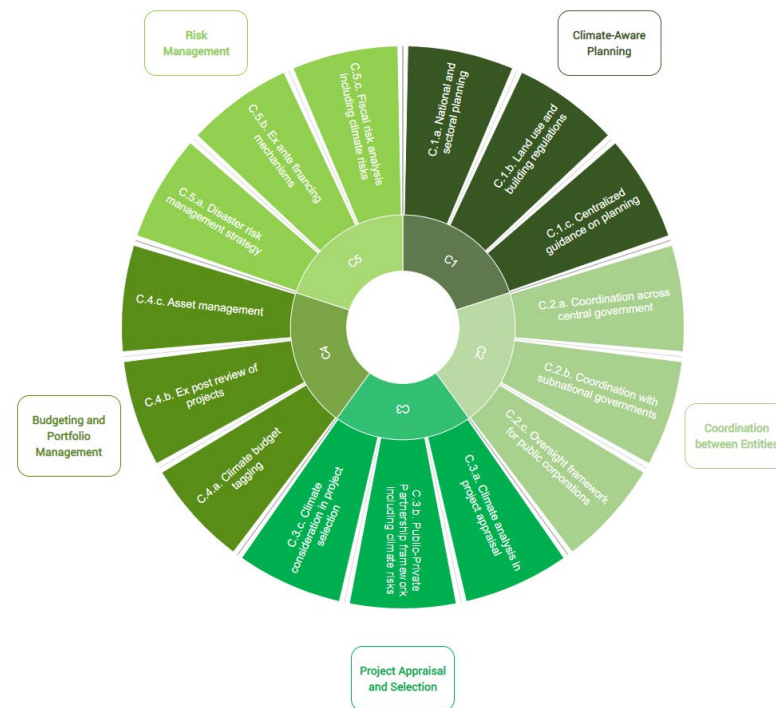
**Criteria for project consideration and appraisal**

**Investment planning**



**Reporting / oversight**

## C-PIMA





## “Green” bonds

- Green, social or sustainable bonds are usually referring to use of proceeds bonds
  - This means the entirety of the bond proceeds will be used for specific, qualifying expenditures and projects
  - Over sixty series of use of proceeds bonds have been issued by sovereigns from Poland's inaugural issuance in 2016 through the end of 2021, with twenty-one of these issuances in 2021 alone.
- Sustainability-linked bonds tie the interest rate of the bond to the issuer's fulfilment of a pre-defined sustainability target within an agreed timeframe
  - SLBs do not require that the proceeds of the bond be used for specific eligible projects or in a certain manner
  - First sovereign issuance was by Chile in 2022

## Use of proceeds bonds: definitions

### Green bonds

Green bonds are debt securities issued to raise capital exclusively to fund new or existing environmental projects

### Social bonds

Social bonds are debt securities issued to raise capital exclusively to fund new or existing projects with positive social outcomes

### Sustainable bonds

Sustainable bonds are debt securities issued to raise capital for a mix of environmental and social projects

### ICMA Principles

ICMA's Green Bonds Principles and Social Bond Principles are voluntary process guidelines intended to provide issuers with guidance on key components involved in launching a credible green or social bond and standardizing disclosures for underwriters and investors

## Use of proceeds bonds

- Green, social or sustainable bond framework published in advance of its first GSS bond issuance
  - Structured in line with ICMA Principles
  - Reviewed by an external verifier with expertise in environmental, social and sustainable issues
- Offering document for each GSS bond offering will include:

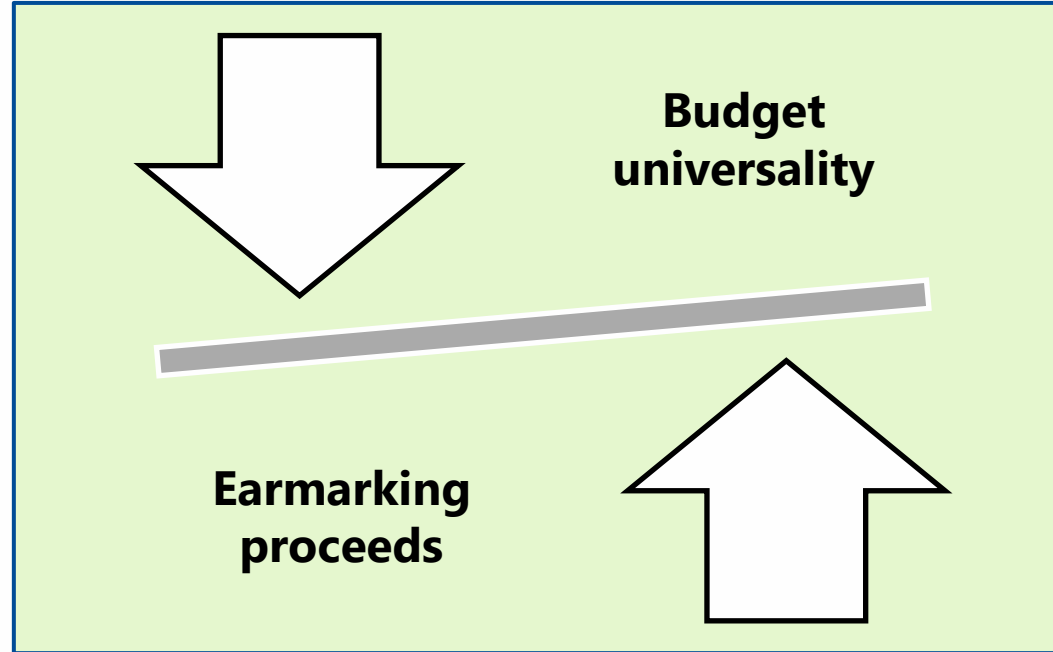
Use of proceeds	Project evaluation	Management of proceeds	Reporting
Bond issuance labelled as green, social or sustainability bonds by including eligible projects in its use of proceeds disclosure	The issuer defines the kind of projects it seeks to support	The issuer discloses how it will separate bond proceeds and make periodic allocations to eligible investments	The issuer chooses how it and/or third parties will monitor and report on the use of proceeds and expected impacts

# UoP bonds management of proceeds – PFM issues

## Poland Green Bond Framework

*“All proceeds from Ministry of Finance, Poland Green Bond are **set aside in a designated account** for funding exclusively projects as defined in the Eligible Sectors disclosed in this Green Bond Framework.*

*The proceeds are credited to a separate “Green Cash Account” and disbursed to Green Bond Eligible Projects.”*



## Germany Budgetary Principles Act (Section 7):

*“All revenues shall serve as cover for all expenditures. Revenues may be restricted to usage for specific purposes insofar as this is prescribed by a law or permitted in the budget.”*

**Germany Green Bond Framework**  
Green bonds proceeds “will be part of the overall funding of the Federal Republic of Germany. Consequently, the German Finance Agency will manage proceeds of the issued Green German Federal securities **in line with the treasury policy of the German Federal Government.**”

## India Framework for Sovereign Green Bonds

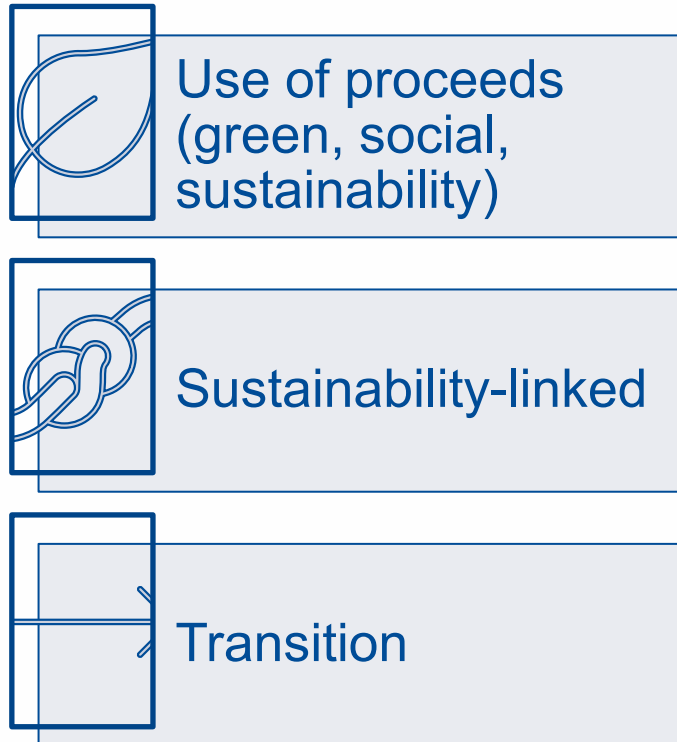
*“The proceeds will be **deposited to the Consolidated Fund of India (CFI)** in line with the regular treasury policy, and then **funds from the CFI will be made available for eligible green projects**. For the purposes of ensuring that the proceeds’ allocation and accounting is transparent, clear and beyond doubt, **a separate account will be created and maintained by the Ministry of Finance Government of India**. Public Debt Management Cell (PDMC) will keep a track of proceeds within the existing guidelines regarding debt management, and monitor the allocation of funds towards eligible green expenditures.”*

# Reporting

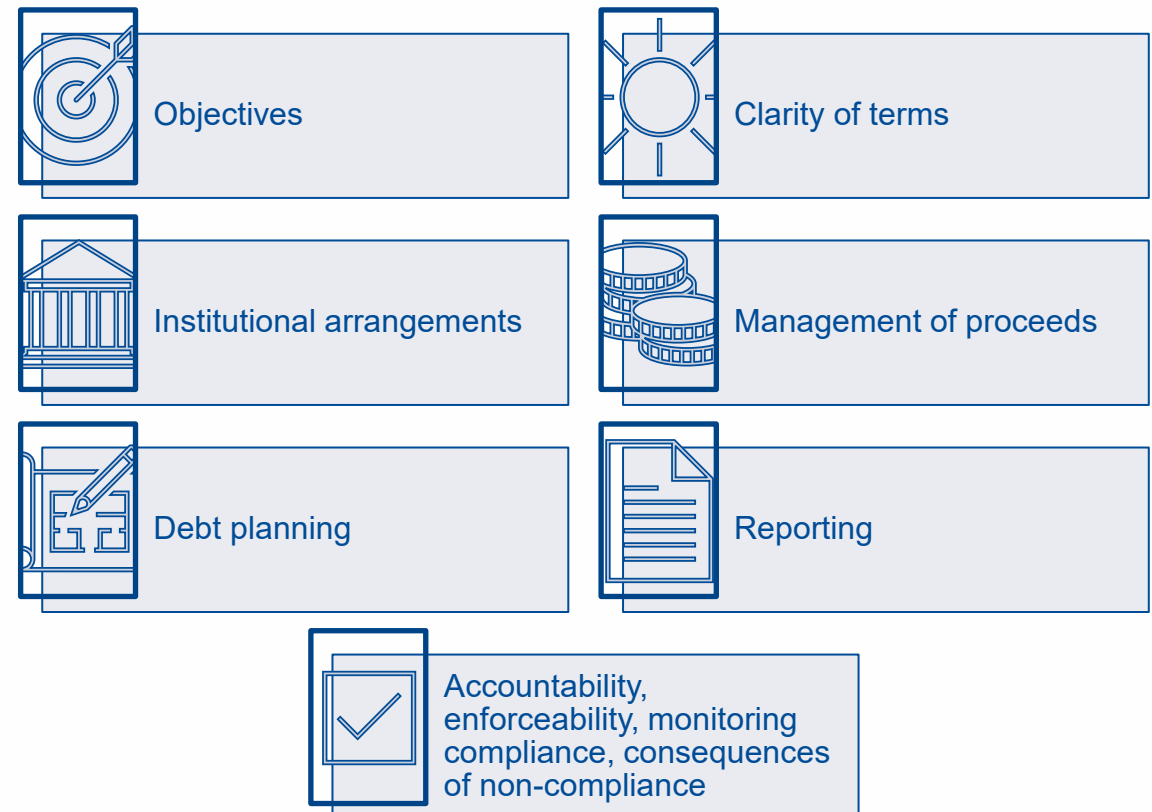
- Issuers will generally, within one year of issuance, publish information about the allocation of the net proceeds of the notes on a designated website
- Website disclosure on the issuer's website is the typical market practice and is consistent with ICMA's emphasis on transparency
- This information is typically updated annually, or when there are material developments, until the net proceeds of the notes have been fully allocated to eligible projects
- The reports often include the allocation of net proceeds of notes to eligible projects, the projects funded, management's assertion that the proceeds have been invested in eligible projects and a report from an independent accountant examining management's assertion
- Some issuers publish "impact reports" detailing the environmental impact of the selected project

# ESG bonds - summary of selected legal PFM considerations

## ESG bonds types\*

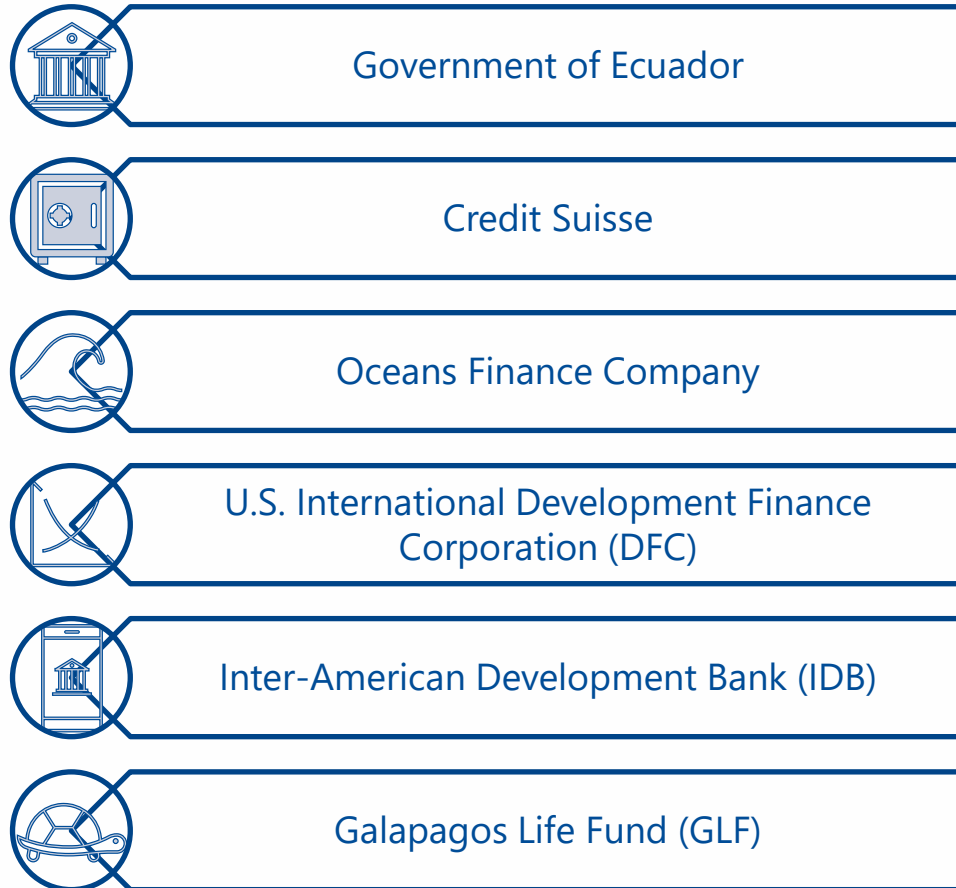


## Integration into the PDM framework



\*by the type of expenditures targeted and the way in which ESG goals are achieved  
for more information see Lindner, P., and Chung, K. Sovereign ESG Bond  
Issuance: A Guidance Note for Sovereign Debt Managers (IMF WP 2023/058),  
available [here](#)

# Ecuador debt-for-nature swap



USD 656 mln Galápagos marine conservation-linked bond



debt conversion to exchange USD 1.628 bn of Ecuador international bonds for a USD 656 mln loan

USD 656 mln political risk insurance

USD 85 mln guarantee

Source: <https://www.dfc.gov/media/press-releases/financial-close-reached-largest-debt-conversion-marine-conservation-protect>

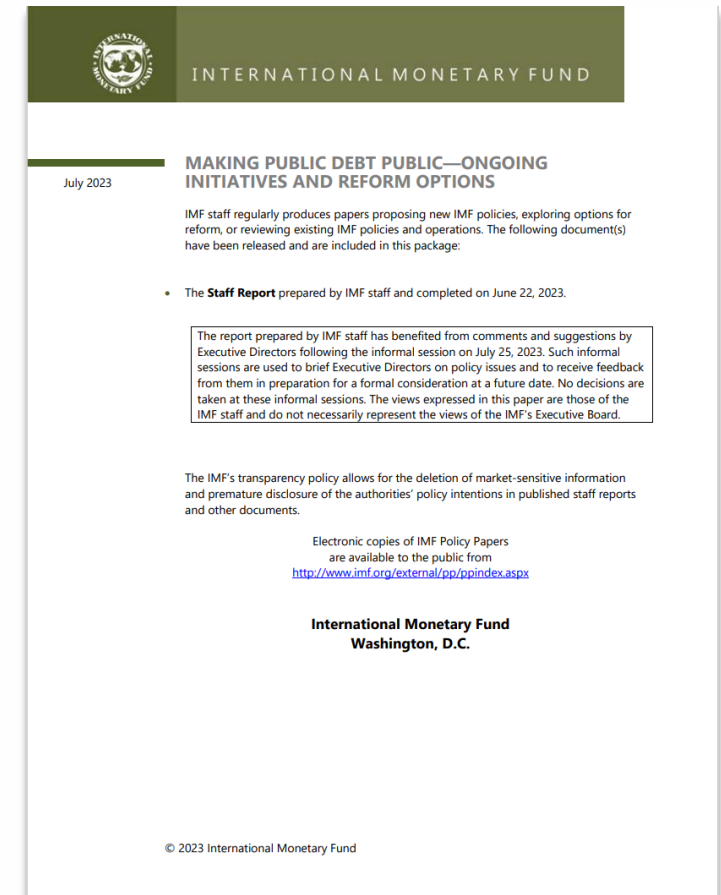
# Debt transparency has emerged as a prominent topic

Increased calls for debt transparency, due to a significant rise of public debt and increased use of complex forms of financing (collateralized borrowing, SOE and PPP debt, government guarantees, etc.)

Last July the IMF, in the context of the MPA, published a Board Paper entitled ***Making Public Debt Public***.

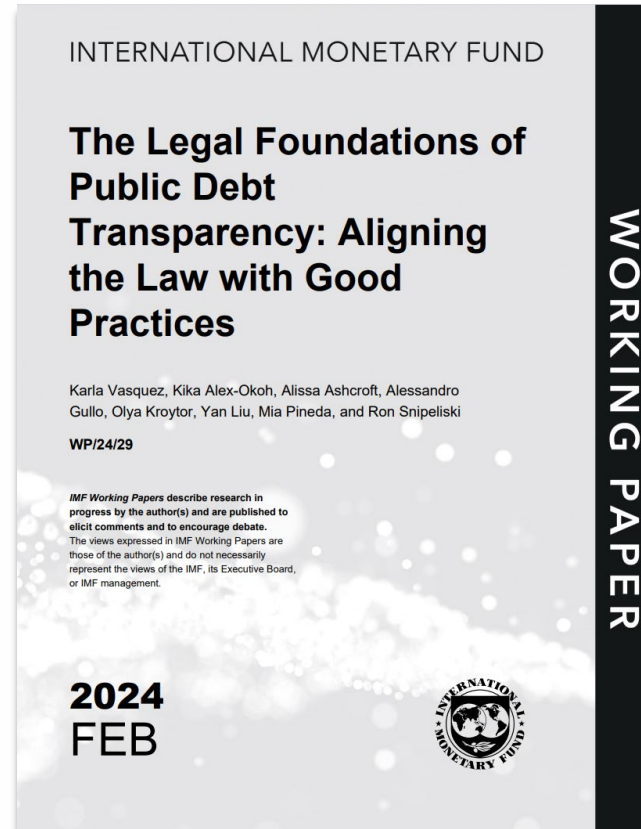
**Opaque debt is the consequence of inadequate institutions and capacity (“underlying drivers”) as well as “adverse incentives”...**

- Limited information and accountability make it easier for the authorities to skirt fiscal rules or to divert public funds.
- Poor transparency may help creditors to achieve better contract terms than their competitors.





# Strengthening domestic legal frameworks: a critical gap



No other publication has examined comprehensively the role domestic law plays in promoting debt transparency.

## Law is important!

- **Primary laws provide permanency.** Strengthening the domestic laws of debtor countries help align practices with international standards by entrenching good borrowing practices, adequate institutional arrangements, and proper accountability.
- **Clear and unambiguous debt disclosure requirements** for the contracting of public debt create an incentive to disclose debt transactions and bind the discretion of policy makers and public debt managers on what, when and how to disclose debt data.
- Laws can also help **enhance the control on borrowing** by entities outside the central government, **strengthen institutional arrangements** for debt data collection and disclosure, and **support monitoring and oversight** of public debt.

# Key findings

*Accountability mechanisms, from SAI mandates to oversight by the legislature, are insufficient...*



## Recommendations:

### Supreme Audit Institutions

- **Broad mandate to audit public debt**, which may derive from the powers to audit the government's financial statements.
- **Legal authority to audit the whole public sector** as SOEs, though broadening the authority of the SAI should be commensurate with its institutional capacity.
- **Sufficient powers to obtain information and report audit results.**

Contingent liabilities:  
climate-related risks

### Oversight by the Legislature

- **Sound procedures, institutions, and staff** with technical capacity.
- Level of **transaction approval authority may be needed** for complex transactions.
- **Confidential debt information** should not be exempt from legislative oversight.