House of Commons

Environmental Audit Committee

# UK Export Finance: Government Response to the Committee's Nineteenth Report of Session 2017–19

## Third Special Report of Session 2019

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## Environmental Audit Committee

The Environmental Audit Committee is appointed by the House of Commons to consider to what extent the policies and programmes of government departments and non-departmental public bodies contribute to environmental protection and sustainable development; to audit their performance against such targets as may be set for them by Her Majesty's Ministers; and to report thereon to the House.

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The constitution and powers are set out in House of Commons Standing Orders, principally in SO No 152A. These are available on the internet via www.parliament.uk.

### Publications



Committee reports are published on the Committee's website at www.parliament.uk/eacom and in print by Order of the House.

Evidence relating to this report is published on the inquiry publications page of the Committee's website.

### Committee staff

The current staff of the Committee are Ruth Cahir (Committee Specialist), Katie Gibbs (Committee Assistant), Laura Grant (Committee Specialist), Leoni Kurt (Second Clerk), Lloyd Owen (Clerk), Anne Peacock (Media Officer), Laura Scott (Committee Specialist), and Jonathan Wright (Senior Committee Assistant).

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# Third Special Report

The Environmental Audit Committee published its Nineteenth Report of Session 2017–19, *UK export finance* (HC 1804) on 10 June 2019. The Government's response was received on 15 August 2019 and is appended to this report.

# Appendix: Government Response

In relation to the Environmental Audit Committee's Nineteenth Report of Session 2017–19 on UK Export Finance, the Committee published thirteen recommendations. Recommendations made by the Committee are indicated in bold italicised text. Government's response is in plain text.

## UK Export Finance's support for the energy industry

**In line with recommendations by the IPCC and the CCC, and in keeping with the UK's commitments under the Paris Agreement, the UK Government should set out how UKEF will work towards net-zero emissions by 2050. Making this commitment would show climate leadership and a willingness to align the UK's domestic and international approaches to job creation and climate change**. (Paragraph 79)

In ratifying the Paris Agreement, the UK Government has signalled its continued commitment to climate action. Keeping to its commitments in the Paris Agreement, Government has legislated to ensure that the UK's carbon account reaches net zero emissions by 2050, responding to the central recommendation of the Committee on Climate Change's report on the UK's long-term emissions targets. Government has stated that it will need to determine the precise direction of future energy and climate policy in reaching this ambitious climate target. The outcome of this process may have implications for UKEF.

With its international focus, through its adoption of the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD), UKEF is laying the framework for it to assess how it can best respond to climate-related risks and opportunities, and will develop its climate strategy as it does so. UKEF is working with other government departments to ensure that UKEF appropriately takes into account the UK's international climate commitments, including the Paris Agreement, in its activities. However, the emissions released by UKEF supported projects overseas will be subject to the limitations imposed by the Nationally Determined Contributions agreed by host governments as part of their Paris Agreement commitments rather than any commitments made by the UK. The emissions from these projects are owned and managed by other countries and not the UK or UKEF.

The availability of UKEF support for renewable energy projects is not limited by its support for other types of energy projects, UKEF is taking steps to develop the breadth of its support for climate mitigation (renewable energy and decarbonisation) and climate adaptation. In the area of climate mitigation, UKEF has assessed that future demand for its support is most likely to gravitate around the 'bookends' of this activity (for example, large scale offshore wind at one end and off-grid solar at the other) given the significant private market finance capability and capacity available for established and lower capital forms of renewable energy.

As a result, UKEF will focus its efforts in promoting its support for these technologies in jurisdictions where private finance is more limited so that it can underpin and support the UK supply chains active in these climate related sectors. UKEF identified support for renewable energy as a priority sector when developing its 2017–20 Business Plan. UKEF took the strategic decision to hire renewable energy specialists in 2016 who are now leading its business development activities in this area.

UKEF's work in climate adaptation is nascent but is beginning with the potential that lies within the UK Flood and Coastal Risk Management (FCRM) supply chain to meet the needs arising from countries dealing with the impacts of increasingly prevalent climate events.

**The UK should leverage its position among other OECD Export Credit Agencies to encourage them to follow UKEF's example in aligning its work with net zero emissions by 2050, revisiting their energy support strategy in light of the IPCC's report, and introducing a strategy to end support to new fossil fuel energy projects by 2021. UKEF should seek multilateral agreement amongst OECD ECAs to join UKEF in making finance flows consistent with a pathway consistent with the Paris Agreement and net zero emissions by 2050**. (Paragraph 80)

As it has demonstrated before with the 2015 agreement between OECD Export Credit Agencies on a Sector Understanding on Export Credits for Coal Fired Electricity Generation Projects, UKEF has assumed international leadership when there has been opportunity to do so. Another such example is UKEF's appointment in June 2018 to the Steering Committee of the Equator Principles, a benchmark voluntary environmental and social risk management framework that sets a good practice framework for environmental, social and human rights due diligence and monitoring to support responsible risk decision making on project related financing. UKEF is using its position on the Steering Committee to support a review and update of the Equator Principles to consider alignment with some of the TCFD's recommendations.

UKEF will seek to work multilaterally with OECD Export Credit Agencies to encourage the further strengthening of international agreements that relate to the environment. In doing so, UKEF is conscious of the significant and increasing role that Export Credit Agencies outside of the OECD Arrangement on Officially Supported Export Credits (like China and India) are assuming and the fact that some OECD countries also operate programmes that are not subject to the OECD Arrangement. UKEF will also engage with those Export Credit Agencies in respect of issues of climate change and the environment. Until the UK leaves the EU, UKEF will also continue to engage with other member states and the EU Commission in respect of international negotiations falling under EU competence. For climate action to have impact, it is imperative that other major economies and their Export Credit Agencies act in concert. Doing so helps to ensure a level playing field for UK exports in respect of export credits so that the low carbon transition is a just transition for UK businesses and their workforces.

**In addition to considering whether UKEF subsidises fossil fuels under the "price gap" method, UKEF should publish a measure of its inventory support for fossil fuels using the OECD method. UKEF should volunteer to peer-review its fossil fuel support mechanisms, which has been effective in identifying opportunities for increased efficiency in China, Germany, Mexico and the United States**. (Paragraph 82)

UKEF's support is in line with the OECD Arrangement on Officially Supported Export Credits. It follows all OECD agreements that relate to export credits. We would note that the methodology in the OECD's report, the 2018 Companion to the Inventory of Support Measures for Fossil Fuels defines support, not subsidies, for fossil fuels and also specifically states that it makes no judgement on whether support measures for fossil fuels are inefficient or need to be reformed. No OECD Export Credit Agencies have undertaken a peer review process for their support mechanisms as they relate to fossil fuels and this is not required by the OECD Arrangement.

UKEF's support is also provided on commercial terms and it charges a premium to cover risk and operating costs. UKEF is required to operate at no net cost to the taxpayer. Therefore, UKEF does not subsidise fossil fuel projects overseas and neither could it justify the intensity of effort and resources entailed in pursuing adoption of the methodology in the OECD report. Furthermore, UKEF's support is available to exports from all sectors and is not unique to fossil fuel projects. In the last ten years, UKEF has generated over £1 billion for the Exchequer.

UKEF publishes information on all exports it supports in its Annual Report & Accounts which are presented to Parliament and published on its website. This information includes the value of its support for specific transactions. As a participant in the OECD Arrangement, UKEF already has established mechanisms for sharing information and learning from fellow participant Export Credit Agencies.

## Energy transition

**UKEF should commit to only support British businesses in projects that support the UK's climate goals. Where it is supporting a new energy project, UKEF should show how this supports transition to a low-carbon energy system and aligns with net zero emissions by 2050. Projects supported by UKEF should be able to demonstrate that they have considered a range of potential lower-carbon and renewable options, and that they have selected the option with the lowest feasible emissions. In so doing UKEF should state how its strategy will support a 'just transition' to workers in the UK who currently benefit from its support, and how this approach will support decent work in the areas affected**. (Paragraph 117)

The projects UKEF supports can have positive developmental and climate impacts, however UKEF's primary statutory mandate is to support UK exports. UKEF's support is demand-led and provided where overseas buyers have chosen to procure from the UK supply chain and are seeking financing support.

Through its adoption of the TCFD's recommendations as appropriate to an Export Credit Agency and a government department, UKEF will assess its approach to climate-related risks and opportunities and will develop its climate strategy as it does so. We envisage that this will include specifically assessing the resilience of this strategy to climate-related risk in connection to different climate-related scenarios.

When it evaluates applications to support high GHG emitting energy Projects,[1] UKEF already follows standards that require project alternatives to be considered by project developers. The OECD Common Approaches and Equator Principles which UKEF follows require that Projects must meet the relevant requirements of the International Finance Corporation (IFC) Performance Standards and World Bank Group Environmental Health Safety Guidelines (EHS Guidelines). The IFC Performance Standards includes a specific standard (Performance Standard 3) on resource efficiency, including reducing project related GHG emissions. Project alternatives must be considered and implemented where technically and financially feasible to reduce GHG emissions during design and operations. The Equator Principles specifically requires a GHG alternatives analysis to evaluate less GHG intensive options for Projects emitting more than 100,000 tonnes C02 of equivalent per year. Recognising UKEF's influence over Projects that seek its financing, UKEF will consider what additional steps it can take so that Projects it supports are designed and managed to minimise emissions .

**In the period until UKEF ends support for new fossil fuels (end of 2021) it should always explain publicly on its website why it has chosen to support a fossil fuel project, why lower-carbon alternatives were not pursued, how the project is contributing to energy transition, and what mitigating actions have been taken**. (Paragraph 118)

Although we disagree with ending the availability of UKEF's support for new fossil fuel projects by the end of 2021, there is more that UKEF can do to build on its existing transparency obligations. UKEF already discloses information regarding the environmental and social risks of Projects (including GHG emissions) which UKEF supports that have high potential of adverse environmental and/or social impacts (Category A). From the financial year 2020–21, UKEF will additionally disclose this information in respect of Projects which UKEF is asked to support which have medium potential of adverse environmental and/or social impacts (Category B).

A number of fossil fuel projects that UKEF has supported will make positive developmental impacts both through meeting energy needs in developing countries and through replacing higher carbon emitting energy sources. UKEF will consider whether it could better communicate the basis for its decisions to support fossil fuel Projects.

**UKEF should review its energy policy, as it did after the 2015 Paris Agreement, to ensure that it demonstrates climate leadership in responding to current knowledge of climate risks. We recommend that UKEF's fossil fuel investment should finish by the end of 2021. At the very least, UKEF should follow Sweden's Export Credit Corporation (SEK) in introducing a 5% cap on gross lending to fossil fuel operations (coal oil and gas) as a proportion of total support. As with the UK's domestic carbon budgets, this cap should progressively reduce in size, and should align with supporting net-zero emissions by 2050**. (Paragraph 119)

1 Civil (non-aerospace) cases within the scope of the OECD Common Approaches and/or the Equator Principles. Subsequent references to 'Projects' refer to this definition.

UKEF will continue to develop its strategy on climate-related risks and opportunities, including as it relates to the energy sector, as a central part of adopting the TCFD's recommendations. However, to end UKEF's support for fossil fuel projects by the end of 2021 would not achieve an effective or "just" transition for UK workers into the low carbon economy and would be too rapid to support the transition that the UK's oil and gas industry is beginning to make towards lower carbon and renewable energy sources. In developing countries, energy security is a key component for development and poverty alleviation and these countries will continue to need to use a mix of energy sources.

We would note that, in introducing its cap on fossil fuel support, SEK does not have the same "just transition" considerations as does the UK since Sweden does not have a significant oil and gas sector. As a recent report on Sweden's export credits has stated, "the introduction of restrictions on fossil fuels should not have a significant impact on Sweden's domestic export industry."[2] This is not the case in the UK, where over 280,000 jobs are supported by the UK's offshore oil and gas sector and UKEF's support has helped to sustain these jobs at a time of low and fluctuating oil prices, as well as supporting the transition of that industry's capabilities into offshore wind.

**UKEF returned £500m to the Treasury in the last 5 years. Noting that key technologies to achieve net-zero emissions are still to be developed fully, we recommend that Treasury ringfences at least 20% of money returned by UKEF from all historic category A (highest risk to environment) projects as well as all projects with forecast emissions of more than 25,000 tonnes of C02 equivalent per year, for at least the next ten years. This money should be invested into renewable energy and low-carbon transition research and development**. (Paragraph 120)

The Government recognises the importance of supporting renewable energy and low carbon transition research and development, but does not agree with the proposed approach. Hypothecating income in this way would restrict our ability to respond flexibly to changing priorities or react quickly to unforeseen circumstances. The current system allows the Government to allocate funding based on need and ensure that it is spent in the most effective way to provide value for money for taxpayers.

The UK is already a world leader in clean growth. Between 1990 and 2016, the UK reduced its emissions by 42 per cent while growing the economy by more than two thirds.[3] The Government has committed to conduct a review into the costs of decarbonisation, which will consider how to achieve this transition in a way that works for households, businesses and public finances, as well as the implications for UK competitiveness. Our Clean Growth Strategy sets out how we will continue to cut emissions while keeping costs down for consumers, creating good jobs and growing the economy. The Clean Growth Strategy also sets out significant investment by the Government in clean growth, including

£2.5 billion to be invested by the Government to support low carbon innovation from 2015- 2021 and £1 billion to support the uptake of ultra-low emissions vehicles. Budget 2018 set out how the Government is accelerating the shift to a clean economy, building

2 Swedish Society for Nature Conservation (2019), The world 's first fossil free export credits, p20 https ://www .naturskyddsforeningen .se/sites/default/files/dokume nt-media/the worlds first fossil free export cred its .pdf

3 Committee on Climate Change, Reducing the UK's emissions , https://www.theccc .org.uk/our impact/reducing-tl1 e-uks-em issions/

on the Industrial Strategy, Clean Growth Strategy, and 25 year Environmental Plan. We announced a package of measures to support tackling climate change, including an Industrial Energy Transformation Fund, backed by up to £315 million of investment.

UKEF has significant capacity to support UK renewable energy and low-carbon exports to a wide range of overseas markets. It has c.£20 billion in remaining capacity for exports from all sectors, including renewable energy and low carbon exports.

UKEF is actively raising awareness and developing partnerships with UK companies pursuing low carbon exports so that they can access UKEF's support where this is needed. UKEF will 'lead with finance' to incentivise overseas project sponsors to procure from the UK, connecting the UK supply chain to clean growth opportunities. UKEF is also actively enhancing sector breadth in its activities, for example deepening its capabilities in renewable energy at both ends of the technology spectrum (large scale offshore wind and small scale off grid solar photovoltaics). We also recognise there is significant private market finance available to fund renewable energy and so requests for UKEF to complement the private market are currently limited.

UKEF will look into further developing its capabilities in the area of renewable energy and decarbonisation, and will consider the needs of UK companies pursuing renewable energy and low carbon export opportunities when enhancing its product range. This will build on the commitment in the Export Strategy to analyse the full range of its statutory powers to identify where it can consider creating new products and enhancing existing ones.

## Policy, measurement and transparency

**Government should legislate to ensure compliance with the UK's obligations under the Paris climate agreement and other national and international climate and environmental commitments, including the SDGs**. (Paragraph 146)

The action that the UK Government has taken to legislate to ensure that the UK carbon account reaches net zero emissions by 2050 shows that the UK is intent on living up to its obligations under the Paris Agreement. In meeting this ambitious target and complying with its international obligations, Government will make other policy decisions as appropriate, not all of which will require legislation to achieve compliance.

UKEF's decision making takes into account domestic legislation, international agreements that the UK has ratified and wider government policy with the appropriate weighting . Its development of a climate strategy will take into account the UK's international obligations and Government's wider policy making as it evolves.

**For full transparency, UKEF should report on the forecast and actual emissions of all projects it supports, as well as the portfolio totals, in a single document, so that it is easy to access and compare projects. UKEF should also report the total emissions of its portfolio annually in its Annual Report and Accounts. This should not be challenging, as UKEF already collects this data**. (Paragraph 147)

UKEF has long been committed to reporting on greenhouse gas emissions for relevant projects it supports. Since 2008–9, it has reported through its Annual Report & Accounts on all Projects it supports where operational phase annual greenhouse gas emissions (GHG) are initially estimated to exceed 25,000 tonnes of C02 equivalent per year. UKEF agrees that there are further steps it can take to present this information in a more accessible way which allows the public to make meaningful use of emissions data. In considering the public accessibility of its emissions data, it will take account of TCFD's recommended GHG emissions disclosures.

**UKEF should report the Scope 3 emissions of all projects, and in particular of all fossil fuel-related projects where Scope 3 emissions are particularly high. The GHG Protocol provides a methodology for calculating Scope 3 emissions, and the TCFD recommendations provide a readily available source of guidance for this work. If Government considers that existing methodologies for modelling Scope 3 emissions are inadequate, it should support research to develop an agreed model, and should promote this model amongst its ECA peers**. (Paragraph 149)

The GHG Protocol is internationally recognised and UKEF does not propose developing alternative methodologies to those already in existence. The GHG Protocol is the most widely used framework by business, government and the voluntary sector. The GHG Protocol requires the accounting and reporting of Scope 1 (direct) and Scope 2 (indirect - electricity) emissions. However, it recognises the significant challenges in accounting for Scope 3 (value chain/other indirect) emissions which is an optional reporting category . As part of adopting TCFD, UKEF will consider the emission metrics it assesses, noting that TCFD only recommends disclosure of Scope 3 emissions if appropriate. UKEF is committed to transparency in respect of climate impacts and will consider whether it may invite project sponsors to disclose Scope 3 emissions on a voluntary basis. As internationally recognised methodologies for accounting for GHG emissions develop and adoption gathers pace, UKEF, in conjunction with other parts of Government, will consider at what stage it may become appropriate for it to require of project sponsors disclosure of Scope 3 emissions for their Projects. UKEF is committed to providing meaningful transparency of the support it provides, but in doing so seeks to balance the resources required with the resulting level of material insight that can be achieved.

**UKEF should commit to follow recommendations by the Task Force on Climate related Financial Disclosures (TFCD), including to quantify and report its exposure to stranded assets due to climate change and actions to support energy transition**. (Paragraph 150)

The Government recognises the TCFD's recommendations as one of the most influential international initiatives to integrate climate risks and opportunities into mainstream financial decision making. That is why, in September 2017, the UK became one of the first countries to formally endorse the TCFD's recommendations. UK Government's recently launched Green Finance Strategy announced that UKEF will further strengthen its robust capability in risk assessment by making climate-related financial disclosures in its accounts, in line with the TCFD's recommendations, as soon as practicable following the close of the 2020/21 financial year.

The TCFD's recommendations provide UKEF with a framework through which it can systematically consider the risks and opportunities related to climate change, including transition, physical and price risk. In line with those recommendations, UKEF will develop its strategy in respect of climate-related risk and opportunities, embed this in its governance and determine the management processes, targets and metrics it will use to identify, assess and manage climate-related risks. In view of its adoption of TFCD, UKEF has already begun to build on its risk assessment capability through launching a pilot training programme for staff in climate change and by drawing on industry best practice to inform the updating of its risk analysis tools. In implementing the TCFD's recommendations, UKEF will do so as appropriate to its role as an export credit agency and a government department with a statutory role to support UK exports. This demand led public function distinguishes it from the financial model generally adopted by the private sector in its capital allocation decisions.

**UKEF should report on the GHG emissions profile of each of its energy projects, including its net emissions and the difference between modelled emissions for alternative energy generation methods. The alternative energy generation methods should include the incumbent generation method (when the UKEF-supported project is substituting a more emissions-intensive energy production method) as well as any feasible renewable energy alternatives. UKEF should also calculate and report the net difference that it makes to emissions in export countries across its portfolio**. (Paragraph 152)

As UKEF determines what climate-related targets and metrics it will use to manage climate-related risks under TCFD, it will also consider whether it might request additional emissions profile data from energy project sponsors and other recipients of its support, including those of alternative energy sources. UKEF is committed to providing emissions data which is meaningful and which provides transparency around the impact its support has.

**The remit of the Export Guarantees Advisory Council (EGAC) should be expanded to include assessing how UKEF's activities contribute to the UK's climate commitments and greenhouse gas net zero targets. The EGAC should report regularly on this progress to the Secretary of State for International Trade**. (Paragraph 153)

EGAC is an expert committee tasked with advising the Secretary of State for International Trade and Minister of State for Trade Export Promotion on the ethical policies applied by UKEF when doing business. The Secretary of State will consider EGAC's remit to provide advice on UKEF's climate-related policies and how it applies them to the businesses that it supports. The Committee's inquiry was discussed by EGAC when it met the Minister for Trade and Export Promotion in March, shortly after her oral evidence to the Committee.

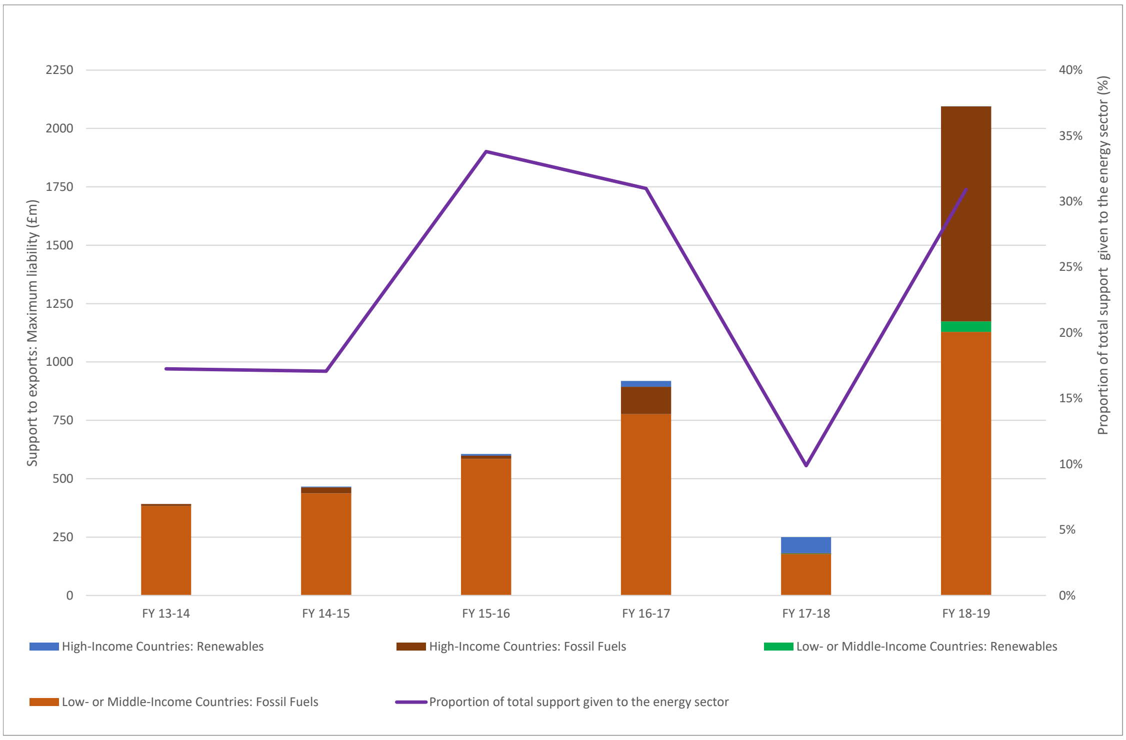
EGAC will review its current reporting to the Secretary of State for International Trade to consider the climate-related impacts of UKEF's support.

In line with the TCFD's recommendations, UKEF will describe EGAC's governance role on climate-related risks and opportunities in further detail when it issues its first climate related disclosures statement. EGAC will also play an active role in advising UKEF as it develops its strategy on climate-related risks and opportunities. In order to support EGAC in this role, UKEF will seek to add further climate change expertise to EGAC through additional recruitment of a climate change expert to join EGAC.

# Appendix: UK Export Finance 2018–19 energy support - updated figures

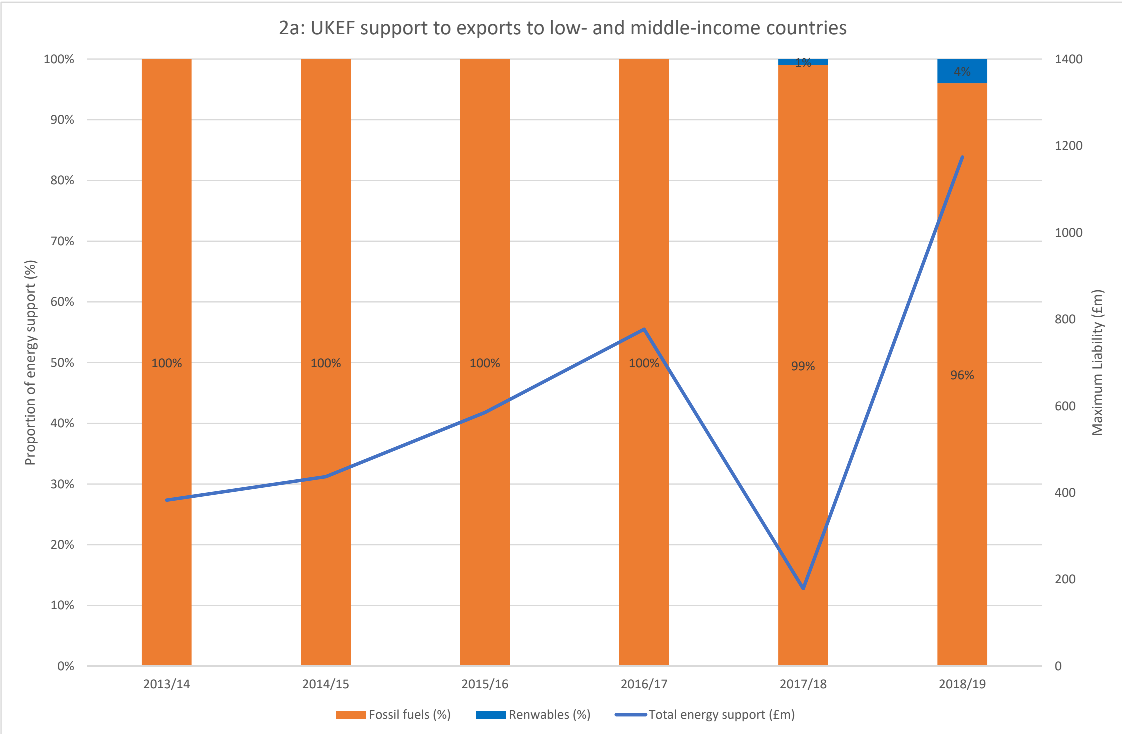
1. Since the publication of out report, we have received UK Export Finance's (UKEF) 2018–19 figures for their energy support. We have updated Figures 1, 2a and 2b with these support figures accordingly.

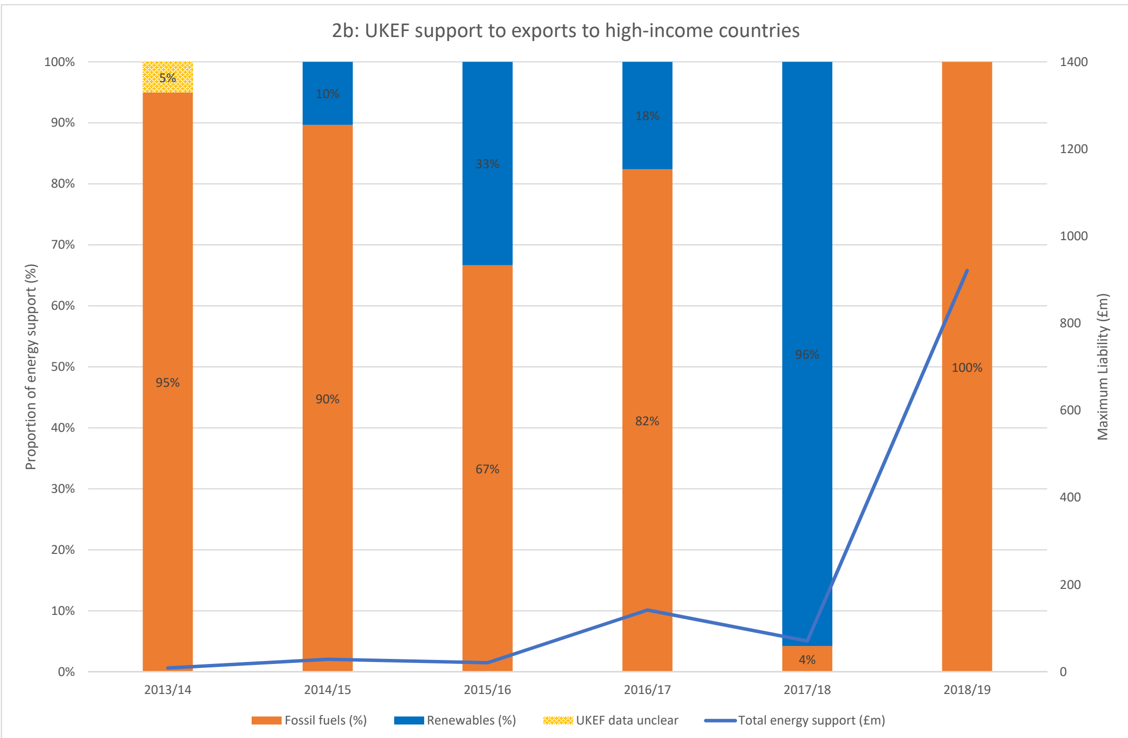
**Figure 1: UKEF's energy support by recipient country classification and energy type**




Source: Based on breakdown of UKEF support by Financial Year in written and supplementary evidence by UKEF

**Figure 2a: UKEF's support to energy exports in low- and middle-income countries, 2b UKEF's support to energy exports in high-income countries**




Source: Based on breakdown of UKEF support by Financial Year in written and supplementary evidence by UKEF. All data is rounded to the nearest whole number.