

# CADENT GAS TRANSITION BOND FRAMEWORK

## DNV GL INDEPENDENT ASSESSMENT

### Scope and Objectives

Cadent Gas Limited (henceforth referred to as "Cadent") is a gas distribution company in the UK. Cadent is Britain's largest gas distribution network and maintains 131,000 kilometres of pipes supplying 11 million homes and businesses in the North West, West Midlands, East of England and North London. As a gas distribution network owner - 4 of the 8 regulated gas distribution networks in Great Britain are owned by Cadent Gas - the company does not produce or own the gas that passes through their pipeline networks. Their responsibility stops at the gas shut off valve. Cadent was formerly known as National Grid Gas Distribution Limited and was part of National Grid plc until 31 March 2017.

On the 27<sup>th</sup> June 2019, the UK Government passed legislation to legally commit the UK to net zero green house gas emissions by 2050. Prior to this, the UK Government had legislated for a National Adaption Strategy via the Climate change Act 2008 and is in the second National Adaption Plan covering the 2018-2023 period in England. As a gas distribution company with its assets wholly within England, Cadent does not own or operate fossil fuel based energy generation assets however Cadent will be required to update its network to enable the delivery of low-carbon fuels required for the UK to meet its legal commitments to the transition to a low-carbon economy.

Cadent has identified the following Sustainable Development Goals (SDG's) as the most material to Cadent's business:

- 7 Affordable and Clean Energy;
- 8 Decent Work and Economic Growth;
- 9 Industry, Innovation and Infrastructure;
- 11 Sustainable Cities and Communities;
- 12 Responsible Consumption and Production;
- 13 Climate Action; and
- 17 Partnership for the goals

Cadent has developed a Transition Bond Framework (the "Framework") under which it can raise debt to support the financing and/or refinancing of assets and expenditures which contribute to the transition to a low carbon economy and the SDG's outlined above.

DNV GL Business Assurance Services Limited ("DNV GL") has been commissioned by Cadent to provide a review of the Framework. Our methodology to achieve this is described under 'Work Undertaken' below. We were not commissioned to provide independent assurance or other audit activities.

No assurance is provided regarding the financial performance of Bonds issued via the Cadent Framework, the value of any investments, or the long-term environmental benefits of the transaction. Our objective

has been to provide an assessment that the Framework has met the criteria established on the basis set out below.

## Responsibilities of the Management of Cadent and DNV GL

The management of Cadent has provided the information and data used by DNV GL during the delivery of this review. Our statement represents an independent opinion and is intended to inform Cadent management and other interested stakeholders in the Transition Bond Framework and issuances under the framework as to whether the established criteria have been met, based on the information provided to us. In our work, we have relied on the information and the facts presented to us by Cadent. DNV GL is not responsible for any aspect of the projects or assets referred to in this opinion and cannot be held liable if estimates, findings, opinions, or conclusions are incorrect. Thus, DNV GL shall not be held liable if any of the information or data provided by Cadent management and used as a basis for this assessment were not correct or complete.

## Basis of DNV GL's opinion

We have adapted our green bond eligibility assessment methodology to create a Cadent specific Transition Bond Framework Eligibility Assessment Protocol (henceforth referred to as "Protocol") - see Schedule 2. Our Protocol includes a set of suitable criteria that can be used to underpin DNV GL's opinion.

As per our Protocol, the criteria against which the Framework has been reviewed are grouped under the four Principles below:

- **Principle One: Use of Proceeds.** The Use of Proceeds criteria are guided by the requirement that an issuer of a bond must use the funds raised to finance eligible activities. The eligible activities should produce clear environmental benefits.
- **Principle Two: Process for Project Evaluation and Selection.** The Project Evaluation and Selection criteria are guided by the requirements that an issuer of a Transition Bond should outline the process it follows when determining eligibility of an investment using Transition Bond proceeds, and outline any impact objectives it will consider.
- **Principle Three: Management of Proceeds.** The Management of Proceeds criteria are guided by the requirements that a bond should be tracked within the issuing organisation, that separate portfolios should be created when necessary and that a declaration of how unallocated funds will be handled should be made.
- **Principle Four: Reporting.** The Reporting criteria are guided by the recommendation that at least annual reporting to the bond investors should be made of the use of proceeds and that quantitative and/or qualitative performance indicators should be used, where feasible.

## Work undertaken

Our work constituted a high-level review of the available information, based on the understanding that this information was provided to us by Cadent in good faith. We have not performed an audit or other tests to check the veracity of the information provided to us. The work undertaken to form our opinion included:

- Creation of a Cadent specific Protocol, adapted to the purpose of the Framework, as described above and in Schedule 2;
- Assessment of documentary evidence provided by Cadent on the Framework and supplemented by a high-level desktop research. These checks refer to current assessment best practices and standards methodology;
- Review of Cadent's published material with regards to its environmental activities relating to the company;
- Discussions with Cadent's management, and review of relevant documentation and evidence related to the criteria of the Protocol;
- Documentation of findings against each element of the criteria.

Our opinion as detailed below is a summary of these findings.

## Findings and DNV GL's opinion

DNV GL's findings are listed below:

### 1. Principle One: Use of Proceeds.

Cadent intends to use the proceeds from the issuance of the Bond to finance and refinance Eligible Transition Projects (henceforth referred to as "Eligible Projects"). The Cadent Transition Bond Framework defines Eligible Projects as projects that fall into the following categories (further detail is outlined in Schedule 1 of this opinion):

- Retrofit of gas transmission and distribution networks
- Renewable Energy
- Clean Transportation
- Energy Efficient Buildings

Cadent has also outlined the types of project within each category and associated selection criteria in order to determine eligibility. DNV GL notes that the selection criteria are aligned with the relevant thresholds described in the EU Sustainable Finance Taxonomy.

DNV GL concludes that the above categories fall within the defined categories of climate transition as defined in the UK's National Adaption Plan and are also aligned with the transition to a low carbon economy.

### 2. Principle Two: Process for Project Evaluation and Selection.

DNV GL can confirm that the project evaluation and selection will be undertaken by a working group comprising representatives from Cadent's Treasury and CSR teams as well as a Project team who will evaluate the nominated projects and assets and report the information to this working group. The working group will be responsible to select the Eligible Projects that are compliant with the eligible categories described in Cadent's Transition Bond Framework.

Eligible Projects can be existing or new projects, with refinancing restricted to projects that have been financed within the last 36 months.

DNV GL concludes that Cadent's Transition Bond Framework appropriately describes the process of project evaluation, selection and exclusions.

### 3. Principle Three: Management of Proceeds.

DNV GL can confirm that the net proceeds from Transition Bond issuances will be deposited to a general account and the balance of the tracked proceeds will be periodically adjusted on a quarterly basis, in order to match allocations to Eligible Projects (re)financed during this period. Cadent confirmed it will - pending the allocation of the Transition Bonds proceeds - invest the balance of the net proceeds in cash or cash equivalent, or in other liquid marketable instruments, as per the company's liquidity management policy. DNV GL can also confirm Cadent has committed to allocating the full proceeds within 24 months of issuing a Transition Bond.

### 4. Principle Four: Reporting.

Cadent intends to report on the use of proceeds and environmental impacts within one year from the date of a Transition Bond financing issuance under the Framework and annually thereafter until the proceeds have been fully allocated and as necessary in the event of material changes. The reporting will be done in a stand-alone Transition Bond report which will include all Transition Bonds issued under the Framework.

The allocation Report will detail the list of Eligible Projects (re)financed, aggregated amount of allocation of the net proceeds to the Eligible Projects at category level, the proportion of net proceeds used for financing versus refinancing and the balance of any unallocated proceeds.

Cadent has also committed to measuring where feasible the impact of environmental projects through a wide range of proposed KPIs, which are listed in the Framework.

DNV GL can confirm Cadent has committed to producing appropriate reporting on the environmental impacts of its investments made under the Framework.

On the basis of the information provided by Cadent and the work undertaken, it is DNV GL's opinion that the Framework meets the criteria established in the Protocol and that it is aligned with the UK's climate adaption strategy and the transition to a low-carbon economy.

#### for DNV GL Business Assurance Services UK Limited

London, 3<sup>rd</sup> December 2019



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#### About DNV GL

Driven by our purpose of safeguarding life, property and the environment, DNV GL enables organisations to advance the safety and sustainability of their business. Combining leading technical and operational expertise, risk methodology and in-depth industry knowledge, we empower our customers' decisions and actions with trust and

confidence. We continuously invest in research and collaborative innovation to provide customers and society with operational and technological foresight.

With our origins stretching back to 1864, our reach today is global. Operating in more than 100 countries, our 16,000 professionals are dedicated to helping customers make the world safer, smarter and greener.

## SCHEDULE 1: DESCRIPTION OF CATEGORIES TO BE FINANCED THROUGH THE FRAMEWORK

Eligible Category	Scope and definition for Eligible Projects	SDGs
<p><b>Retrofit of gas transmission and distribution networks</b></p>	<ul style="list-style-type: none"> <li>• Replacement of pipeline to facilitate the integration of hydrogen and other low-carbon gases</li> <li>• Repair and replacement of existing gas pipeline that is already hydrogen-ready in order to reduce methane leakage</li> </ul> <p><b>For avoidance of doubt, gas network expansion is excluded</b></p>	<p>11,12</p>
<p><b>Renewable Energy</b></p>	<p>Projects aimed at developing the production and use of low carbon energy, such as:</p> <ul style="list-style-type: none"> <li>• Development of biomethane and bio-Substitute Natural Gas (BioSNG) plants, which convert household waste into gas, with an emissions threshold of 100g CO2e/KWh</li> </ul>	<p>7,9,13</p>
<p><b>Clean Transportation</b></p>	<p>Projects aimed at developing new sustainable transport infrastructure, including but not limited to:</p> <ul style="list-style-type: none"> <li>• Hydrogen fueling station</li> <li>• High pressure CNG refueling station</li> <li>• CNG Iveco vans which incorporate a split-drive power take off system that enables the vehicle to generate electrical power and pneumatic air</li> <li>• Investments in alternatively fueled low/zero tail pipe emission vehicles such as electric and electric-hybrid vehicles operational fleet</li> </ul>	<p>11,13</p>

	(vehicles with tailpipe emission intensity of max. 50g CO2/km)	
<p><b>Energy Efficient Buildings</b></p>	<ul style="list-style-type: none"> <li>• Projects aimed at reducing the energy consumption of buildings, offices and depots, including but not limited to:               <ul style="list-style-type: none"> <li>○ replacement of traditional lamps with LED lamps;</li> <li>○ walls, roof, ground floor insulation</li> <li>○ any other energy efficient solutions leading to energy savings of at least 30% compared to a baseline performance before the renovation</li> </ul> </li> <li>• On-site renewable energy installations (solar, wind)</li> <li>• Construction of new buildings which are expected to receive a certification of at least LEED "Gold" or at least BREEAM "Excellent"</li> </ul>	<p>11</p>

## SCHEDULE 2: CADENT SPECIFIC SUSTAINABILITY FINANCING FRAMEWORK ELIGIBILITY ASSESSMENT PROTOCOL

### 1. Use of proceeds

Ref.	Criteria	Requirements	Work Undertaken	DNV GL Findings
1a	Types of Financing Framework	The bond must fall in one of the following categories, : <ul style="list-style-type: none"> <li>• Use of Proceeds Bond</li> <li>• Use of Proceeds Revenue Bond</li> <li>• Project Bond</li> <li>• Securitized Bond</li> </ul>	In addition to reviewing the evidence below, we had several detailed discussions with Cadent Gas.  Evidence reviewed: <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul>	The Framework outlines that Cadent will issue Transition labelled bonds, these will be Use of Proceeds bonds.
1b	Project Categories	The cornerstone of a transition bond is the utilisation of the proceeds which should be appropriately described in the legal documentation for the security.	Evidence reviewed: <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul>	We conclude that the Framework appropriately describes the proposed utilisation of proceeds. The specific utilisation of proceeds of each issuance will need to be further assessed on an individual basis
1c	Environmental benefits	All designated Eligible Project categories should provide clear environmentally sustainable or social benefits, which, where feasible, will be quantified or assessed by the issuer.	Evidence reviewed: <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul>	The Framework outlines the expected environmental benefits that will be realised by any Bonds issued under the Framework. Specific quantifiable benefits of each issuance will be agreed on a case by case basis and subject to further assessment.

## 2. Process for Project Selection and Evaluation

Ref.	Criteria	Requirements	Work Undertaken	DNV GL Findings
2a	Investment-decision process	The issuer of a Transition Bond should outline the decision-making process it follows to determine the eligibility of projects using Transition Bond proceeds	<p>Evidence reviewed:</p> <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul>	We conclude that the Framework appropriately describes the process of project selection. The specific issuances will need to be further assessed on a case by case basis.
2b	Issuer’s environmental and governance framework	In addition to information disclosed by an issuer on its Transition Bond process, criteria and assurances, investors may also take into consideration the quality of the issuer’s overall framework and performance regarding environmental sustainability.	<p>In addition to reviewing the evidence below, we had several detailed discussions with Cadent. Evidence reviewed:</p> <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul> <p>We also performed reviewed environmental and social governance documentation:</p> <ul style="list-style-type: none"> <li>• Cadent Gas Environmental Policy</li> <li>• Cadent Gas ISO 14001 Certificate</li> <li>• Cadent Gas Safety and Sustainability Report 18/19</li> <li>• Cadent Gas Always Doing the Right Thing Code of Conduct</li> </ul>	We conclude that from the information provided, the Framework is in line with Cadent Gas’s wider approach to managing environmental sustainability.

### 3. Management of proceeds

Ref.	Criteria	Requirements	Work Undertaken	DNV GL Findings
3a	Tracking procedure	The net proceeds of a Bond should be credited to a sub-account, moved to a sub- portfolio or otherwise tracked by the issuer in an appropriate manner and attested to by a formal internal process that will be linked to the issuer’s lending and investment operations for Eligible Projects.	In addition to reviewing the evidence below, we had several detailed discussions with Cadent.  Evidence reviewed: <ul style="list-style-type: none"><li>• Cadent Framework 2019</li></ul>	We conclude that the Framework commits Cadent Gas tracking use of proceeds in an appropriate manner and attested to by a formal internal process.
3b	Tracking procedure	So long as the Bonds are outstanding, the balance of the tracked proceeds should be periodically reduced by amounts matching eligible investments or disbursements made during that period.	Evidence reviewed: <ul style="list-style-type: none"><li>• Cadent Framework 2019</li></ul>	We conclude that there is a clear process in place for the tracking of the balance taking into account disbursements.
3c	Temporary holdings	Pending such investments or disbursements to Eligible Projects, the issuer should make known to investors the intended types of temporary investment instruments for the balance of unallocated proceeds.	Evidence reviewed: <ul style="list-style-type: none"><li>• Cadent Framework 2019</li></ul>	We conclude that Cadent Gas has appropriately disclosed how it will manage any unallocated proceeds within its liquidity portfolio.

4. Reporting

Ref.	Criteria	Requirements	Work Undertaken	DNV GL Findings
4a	Periodical reporting	In addition to reporting on the use of proceeds and the temporary investment of unallocated proceeds, issuers should provide at least annually a list of projects to which Bond proceeds have been allocated including - when possible with regards to confidentiality and/or competitive considerations - a brief description of the projects and the amounts disbursed, as well as the expected environmentally sustainable impact.	<p>In addition to reviewing the evidence below, we had several detailed discussions with Cadent.</p> <p>Evidence reviewed:</p> <ul style="list-style-type: none"> <li>• Cadent Framework 2019</li> </ul>	We confirm Cadent Gas has committed to annual transition bond reporting which will be made available through as a stand-alone report which will provide investors with information on the selected projects and, where possible, include quantification of the environmental benefits of the selected projects.