



SEEDS OF CHANGE CLIMATE FINANCE POLICY BRIEF

STRATEGIES, POLICY OPTIONS, AND SCALABLE
INTERVENTIONS FOR ADVANCING CLIMATE FINANCE

CLIMATE SAFE LENDING NETWORK OUTCOME REPORT OF
THE FINANCE INNOVATION ROUNDTABLE 2020 HOSTED
BY THE FEDERAL RESERVE BANK OF SAN FRANCISCO

MARCH 2021

REPORT AUTHOR: SARAH BOEGE, UNIVERSITY OF NEW HAMPSHIRE



CONTENTS

INTRODUCTION 2

SEED#1: A CLIMATE VERSION OF THE COMMUNITY REINVESTMENT ACT (CRA) 3

SEED#2: SIMULTANEOUS SOCIAL INVESTMENTS ALONGSIDE CLIMATE INVESTMENTS 4

SEED#3: REGULATORY ACTION WITHIN CURRENT MANDATES 5

SEED#4: INTEGRATION OF EQUITY IN CLIMATE FINANCE 6

SEED#5: SCALING SUCCESSFUL, STANDARDIZED CLIMATE PRODUCTS
– ESPECIALLY THOSE DESIGNED FOR LOW-INCOME COMMUNITIES 7

INTRODUCTION

The Financial Innovations Roundtable (FIR) is an annual event that works to address problems related to access to capital for low- and moderate-income consumers and communities. The FIR convenes a range of financial institutions, government agencies, foundations, and trade associations to access their expertise for problem-solving discussions.

The 2020 FIR focused on the expanding field of climate finance and was co-hosted by the Carsey School of Public Policy at the University of New Hampshire, the Federal Reserve Bank of San Francisco, and The Climate Safe Lending Network. This policy brief will explore some seed ideas and emblematic initiatives that arose from FIR discussions on policy and industry pathways to climate safe lending both in the United States and internationally.

Currently, much of climate finance is still in an early phase (i.e., “climate finance 1.0”) focusing only on risks to institutions. rather than systemic risks and consequences

for harmful lending practices as well as increased investment in positive innovations. One of the major challenges in climate finance is that climate risk time frames are significantly longer than the time intervals financial institutions and policy makers routinely consider such as business plans, CEO and board tenure, and loan and investment terms. This mismatch, described as the Tragedy of the Horizon¹, means that addressing systemic climate risk will require industry and policy responses to be stronger than what might seem warranted in the present context. Here we present strategies , policy options, and scalable interventions for advancing climate finance now.

¹ As famously referenced by Mark Carney, governor of the Bank of England, in this speech: www.bis.org/review/r151009a.pdf



SEED#1

A CLIMATE VERSION OF THE COMMUNITY REINVESTMENT ACT (CRA)

“ Low-income and other underserved communities must actively work to equitably mitigate the risks of climate change. A CRA-type regulation for the climate would encourage lenders to invest so as to address immediate climate issues and increase resilience to future climate risks in underserved and local low- and moderate-income communities. ”

Michael Swack, Director of the Center for Impact Finance at the University of New Hampshire Carsey School of Public Policy

The transition to a low-carbon economy will likely take trillions of private dollars each year to compliment public funding. In the United States, the Community Reinvestment Act (CRA) has unlocked trillions of dollars of capital for disadvantaged communities and could be similarly used to deliver capital for community-related climate investments. In 2016 alone, \$419 billion dollars of CRA-related loans were made to small businesses and farms, community development investments, and single-family and multifamily lending.²

The U.S. Community Reinvestment Act (CRA) of 1977 was established to encourage financial institutions to serve low- and moderate-income communities – and often communities of color – that had been traditionally excluded through discriminatory lending policies such as redlining.³ Banks now must earn CRA credit through providing lending, investment, and banking services in low- and moderate-income communities and a reevaluated on their CRA performance.⁴ A key to successful CRA efforts has been lending through or in partnership with Community Development Financial Institutions (CDFIs)⁵, which are

community-based lenders with significant local knowledge and relationships. While CDFIs are specific to the U.S., other countries may have analogous networks of community lenders that can be leveraged or created.

Stemming from this example are two policy options: the first – specific to the U.S. context – is to expand the current CRA law to allow banks to receive CRA credit for climate adaptation activities. This would leverage existing CRA infrastructure and could include resilience-building pursuits such as loans to control flooding or support energy-efficient upgrades.⁶ Additionally, any investments that are harmful could be deemed ineligible for CRA credit. However, there is concern that adding climate to the existing CRA might take attention and investment away from pressing challenges like financing affordable housing. The other policy option – applicable in and beyond the U.S. context – is to develop new legislation establishing a ‘climate version’ of the CRA. The same way that the CRA has encouraged banks to lend in underserved areas through minimal compliance requirements, a climate CRA could provide incentives and obligations for lenders to support climate investments.

2 www.urban.org/urban-wire/small-business-and-community-development-lending-are-key-cra-compliance-most-banks

3 Schwartz, Alex F. Housing Policy in the United States [Third Edition]. New York: Routledge, 2015.

4 Banks are evaluated on their CRA performance in CRA exams conducted by U.S. regulatory agencies such as the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC), and the U.S. Treasury’s Office of the Comptroller of Currency (OCC).

5 Community Development Financial Institutions (CDFIs) are U.S. lenders dedicated to expanding economic opportunity in low-income, low-wealth, and other disadvantaged communities by providing access to financial products and services. For more, see: www.cdfifund.gov/sites/cdfi/files/documents/cdfi_infographic_v08a.pdf

6 For additional discussion of ways climate adaptation could be incorporated into the CRA, see www.frbsf.org/community-development/files/climate-adaptation-investment-and-the-community-reinvestment-act.pdf



SEED#2

SIMULTANEOUS SOCIAL INVESTMENTS ALONGSIDE CLIMATE INVESTMENTS

“As investment in climate investments continues to grow, we must be intentional about identifying necessary social investments that help bolster the long-term and comprehensive benefits for people and communities. Climate investments represent capital events that can catalyze other needed investments, such as in quality and affordable child care, which is critical to the current and future workforce who will drive a climate-positive economy.”

Keith Bisson, President of Coastal Enterprises, Inc. (CEI)

There are often many co-benefits that come with climate-positive investments that may be highly valued by communities. For example, investing in climate-resilient infrastructure also provides stability and security for families and communities. In this way, climate investments themselves may unlock co-benefits – such as a public green space that supports biodiversity and provides natural capital benefiting local residents. Similarly, investment in climate-positive aquaculture and agriculture helps support quality jobs, associated economic activity, and builds resilience in rural places where most of these businesses are located.

However, it is also important to consider separate, complementing social investments that can be made alongside climate investments to further enhance community resilience and wellbeing. An example is investing in public health efforts to reduce the prevalence of asthma at the same time as investing in sustainable forestry to manage wildfires and reduce smoke emissions. Likewise, as we grow climate positive investments that generate new jobs, it

is critical to invest in child care to ensure that quality care is accessible and affordable to this workforce. Simultaneous social investments are especially pertinent given that many low-income communities and communities of color have been left more vulnerable to climate-related disasters as a result of decades of divestment and disenfranchisement.⁷

In the United States, CDFIs and credit unions are well-positioned to play a significant role in coordinating appropriate social and climate investments, especially in disadvantaged communities (as they have in supporting CRA efforts). CDFIs and local credit unions have meaningful, direct connections to the real economy through loans and relationships and can highlight these opportunities to larger financial institutions and policymakers. Furthermore, some of the techniques that have helped finance social investments can also be used to make climate investments. An example could be a climate parallel to structured funds – which combine capital from various public, private, or philanthropic sources into one loan fund – that are used in affordable housing projects.

⁷ Méndez, M. (2020). *Climate Change from the Streets: How Conflict and Collaboration Strengthen the Environmental Justice Movement*. Yale University Press. <https://yalebooks.yale.edu/book/9780300232158/climate-change-streets>



SEED#3

REGULATORY ACTION WITHIN CURRENT MANDATES

“ Systemic climate risk of the finance system must be minimized through coordinated, structural change. Central banks and supervisors, along with other policymakers, have a responsibility to proactively build the resilience of the system as a whole, rather than hope that individual agents will adapt and that the market will solve the problem. ”

Fran Boait, Executive Director, Positive Money/Climate Safe Lending

Both in the United States and internationally, there is far more that regulators could do to address climate risks within their current mandates. For example, in the United States the Federal Reserve Bank is charged with ensuring the safety and soundness of the banking system as well as promoting the overall stability of the financial system – and climate risk poses a catastrophic threat to all of these elements.

What could such regulatory action look like? In addition to requiring emissions disclosures by individual financial institutions, regulators also need to participate in larger international coordination to mitigate systemic climate risk. Regulators, including central banks, have an important

role to play in leading by example in this system-wide collaboration to incorporate climate risk management in their own balance sheet and also build resilience into the entire financial system. It is crucial that regulators acknowledge the Tragedy of the Horizon problem and base their actions on the understanding that the policies of today determine the climate risks of tomorrow. It is also not enough to have one department or position dedicated to climate; rather, climate risk should be an integrated piece considered by all. Although updating regulatory mandates to specifically and thoroughly address climate risk should be a priority, expanding regulatory action within current mandates is a good first step that can be taken immediately.



SEED#4

INTEGRATION OF EQUITY IN CLIMATE FINANCE

“ The integration of inclusivity and equity in climate finance is crucial. Systemic risk, including systemic climate risk, does not treat everyone equally since injustice is baked into systemic failures. ”

James Vaccaro, Executive Director Climate Safe Lending Network

Many of the neighborhoods most energy-burdened and most vulnerable to climate events are the same areas with historical divestment and structural inequality. Both negative climate-related impacts (such as pollution) and the positive benefits from climate adaptations (such as climate-resilient infrastructure, new jobs with permanent and fair wages) must be equitably distributed. As acknowledged in President Biden’s inaugural address, “growing inequity,” “the sting of systemic racism,” and “a climate in crisis” are three of the six simultaneous crises facing the United States.⁸ Certainly, there is new momentum in the United States to address these challenges systematically and simultaneously.

Further, the clean energy transition offers an opportunity to dismantle current systems of inequity in favor of new systems led by people of color and low-income communities. As Shalanda H. Baker—the Deputy Director for Energy Justice & Secretary’s Advisor on Equity at the U.S. Department of Energy—outlines in her recent book *Revolutionary Power*:

“[P]eople of color, poor people, and Indigenous people must serve as the architects of the new system. They must actively engage in the creation of the new energy system so as to upend the embedded and unequal power dynamics that are a direct outgrowth of the current energy system... the revolution must be fought on the unfamiliar terrain of energy law and policy.” (Baker, 2021, p. 10)⁹

Embedding equity from the outset is a critical piece of all strategies aiming to advance climate finance. In policy design, policymakers must consider historical injustices, identify populations they aim to protect, define clear outcomes, and determine how those outcomes will be measured. Low-income communities and communities of color should be actively and substantively involved in policy creation and implementation processes. Similarly, banks and other financial institutions also need to embed equity in their processes, leadership, and measured outcomes.

Currently, a key way that capital markets can advance equity is through investments that enhance access for underserved communities—access to capital, education, affordable housing, clean water, clean air, healthy foods, economic opportunity, and healthcare, to name a few. For example, access to capital can be supported through a range of investment strategies, including supporting small businesses in underserved communities via CDFIs, community investment notes, and/or private equity funds; venture capital investments in correcting market failures such as gentrification; and excluding financial institutions that engage in predatory lending practices.¹⁰ In general, Green Bonds and Municipal Bonds are two especially promising instruments that could be used in financing projects such as climate-resilient infrastructure, water and wastewater management, renewable energy projects, land preservation, and other relevant endeavors that improve access for underserved communities.

8 www.whitehouse.gov/briefing-room/speeches-remarks/2021/01/20/inaugural-address-by-president-joseph-r-biden-jr/

9 Baker, S. H. (2021). *Revolutionary Power: An Activist’s Guide to the Energy Transition*. Island Press. <https://islandpress.org/books/revolutionary-power>

10 Many more capital market investment options across asset classes are outlined on page 5 of: Bush, H., Leonard, J., Metrick, C., & Pease, K. (2020). *Investing to Advance Racial Equity: Second Edition Practical ways to tackle economic inequality*. Cornerstone Capital Group. https://cornerstonecapinc.com/wp-content/uploads/Investing-to-Advance-Racial-Equity_Second-Edition.pdf



SEED #5

SCALING SUCCESSFUL, STANDARDIZED CLIMATE PRODUCTS – ESPECIALLY THOSE DESIGNED FOR LOW-INCOME COMMUNITIES

“ Providing mission-driven, community-based investors with access to a shared operating platform and a standardized climate finance product could help to both drive scale and improve access for communities that might otherwise be left behind.”

**Eric Hangen, Senior Research Fellow, Center for Impact Finance at
the University of New Hampshire Carsey School of Public Policy**

Scaling existing, standardized climate products with proven track records can help expand climate finance more rapidly—particularly in communities that may otherwise not have access. For example, in the United States the Smart-E platform is a tool that leverages local networks to connect low- to moderate-income and mainstream homeowners with over 40 eligible green energy home improvement projects including rooftop solar, efficient heating and cooling, efficiency upgrades, and resilience.¹¹ The program is deployed through local lenders—credit unions, CDFIs, and community banks—with the support of local contractors who are identified through a vetted network

This standardized unsecured loan product has been tested across three U.S. states (Michigan, Connecticut, and Colorado), currently has 16 active lenders, over 1,000 participating contractors, and thus far over \$250 million of loans have been originated helping 22,000 homeowners. Early program adopters include mission-driven actors with a climate focus, such as Connecticut Green Bank, as well as lenders that are new to climate products, like Nutmeg State Financial Credit Union (a CDFI credit union). Participants have

found the program easy to implement with low transaction costs due to a standardized loan product, program protocols, and an enabling fintech workflow platform. While it is an unsecured program, participating lenders have reported that these high-performing, high-quality loans function more like a secured program. An important piece of continuing to expand this program is training¹² and building the capacity of community lenders. Smart-Eplatform creators are now looking towards developing the infrastructure and systems to deliver this lending to a broader marketplace.

The Smart-E program shows how standardized loan products with tailored programmatic supports facilitate easy adoption of climate products, especially among community lenders with limited time and capacity to develop new products on their own. Smart-E focuses on green energy home improvement, but the strategy of developing standardized loan products could be used to create climate products for other green investments such as deep retrofitting of non-residential buildings and expanding electric vehicle charging stations and infrastructure and EV car loans.

¹¹ <https://www.inclusiveprosperitycapital.org/smart-e-loan/>

¹² <https://carsey.unh.edu/center-for-impact-finance/solar-lending-training-series>

An aerial photograph of a city skyline at sunset. The sky is filled with vibrant orange, pink, and purple clouds. The city buildings are illuminated with warm lights, and the overall scene is a mix of natural beauty and urban architecture. A large teal rectangular box is overlaid on the upper half of the image, containing white text.

ABOUT THE CLIMATE SAFE LENDING NETWORK

The Climate Safe Lending Network (CSL) is a multi-stakeholder collaborative working to align bank lending with climate safe scenarios. A climate safe scenario is defined as: By 2025 the trajectory of banks' lending portfolios are aligned with the Paris Climate Agreement by achieving science-based targets for net-zero scope 1-3 climate impact, reaching a net-zero emissions goal well before 2050, and incorporating strategies for a socially equitable and just transition.

Aligning financial flows with the transition to a net-zero carbon economy, on a timeline that helps us avoid the most severe destruction from climate change, requires rapid progress across the financial sector. CSL catalyses this shift by supporting lending institutions to collaborate with each other and wider parts of the financial system – including investors, clients, regulators, policy makers, academics, and NGOs – to accelerate the global shift to a climate-safe world.

For more information see: www.climatesafelending.org