Aviva Investors Real Assets - Real Estate Debt Sustainable Transition Loan Framework

December 2023

Aviva Investors Real Assets (AIRA) is an active asset manager with £39.5bn assets under management.[1] We manage strategies that make direct investments in real estate debt and equity, infrastructure debt and equity, private corporate debt and structured finance. As an asset manager, AIRA's fiduciary duty is to protect and maintain the value of assets. Aviva Investors recognises its duty to act as responsible stewards of its clients' assets.

AIRA is committed to reducing the carbon footprint of our portfolio and future proofing our assets against physical and transition climate risks. It is for this reason that AIRA has developed a leading Sustainable Transition Loan framework for our Real Estate Debt (RED) business, accredited by an external second-party opinion provider, to demonstrate our commitment to the transition towards a low-carbon economy.

Tackling Climate Change in Real Estate

Real assets may be critical for society, but the unconstrained delivery of buildings and infrastructure has been a major contributor to the climate crisis. While our built environment is central to the way we live, its contribution to the climate emergency cannot be underestimated. It is one of the worst contributors, estimated to consume 40% of global energy annually and account for more than 20% of international carbon emissions, in addition to waste production, pollution, water use and consumption of other limited natural resources. In Europe, an estimated 90% of European real estate is built before 1990 and is therefore likely to have poorer quality insulation and heating systems.[2]

Buildings must therefore form the focal point of urgent efforts to reduce greenhouse gas emissions and create an environmentally sustainable future. Moreover, the sheer volume of existing stock means that any climate solution must not only consider the environmental credentials of new developments but prioritise the reform of existing buildings.

We recognise the scale of the challenge that climate change presents and understand the urgency with which actions to combat it must yield results. A significant opportunity exists to enhance ESG credentials of existing buildings we lend against, whilst generating investment returns and reducing the buildings' impact on the environment and wider society.

1. Source: Aviva Investors as of 30 September 2023
2. Source: European Commission April 2019

Sustainable Transition Loan Framework

Sustainable Transition Loan Goals

The objective of our Sustainable Transition Loan Framework is to further support AIRA's long term objective to lower carbon emissions across our portfolio. Furthermore, we seek to strengthen our efforts to engage borrower clients on ESG factors, and to support a transition to a low-carbon economy.

There are three overarching goals that AIRA Real Estate Debt (RED) aims to achieve through our framework:

1. **Set a target of originating at least £1bn of Sustainable Transition Loans accredited to this Framework by 2025**
2. **Creating loan term incentives to ensure measurable improvements on buildings we lend against**
3. **Delivering tangible impact for our clients through their investments with external verification through Second Party Opinions**

The Sustainable Transition Loan Framework will provide a structure for loans to property companies with terms linked to improvements in the environmental performance of the buildings we lend against. The origination framework will determine key environmental targets (e.g. energy efficiency improvements), as well as green initiatives (e.g. installation of solar) required on the underlying secured assets, which will also guide the type of financial incentive mechanisms (e.g. margin ratchets) on each loan.

When considering climate transition, we recognise that different building types require different levels of environmental improvements. There are a range of weak to strong performing environmental buildings, and as an active lender, we need to identify and tailor the required actions for improvements. As such, these Sustainable Transition Loans will actively support borrowers in transforming their sustainability and ESG credentials.

Framework Objectives

To meet these goals, we are increasing the volume of transactions focused on climate transition that meet the eligibility criteria set out our framework below. Our focus areas align to the UN's Sustainable Development Goals (SDGs), which include:

- SDG 7 - Affordable and Clean Energy
- SDG 9 - Industry Innovation and Infrastructure
- SDG 11 - Sustainable Cities and Communities
- SDG 13 - Climate Action

This framework is also developed in alignment with the Loan Market Association's (LMA) Sustainability Linked Loan Principles (SLLP). It also draws from the Climate Bond Initiative (CBI) Standards, the EU Sustainable Finance Taxonomy and other relevant industry standards in determining appropriate eligibility criteria for RED. These standards and principles are voluntary guidelines that promote greater transparency and disclosure in the sustainable financing market. In alignment with LMA guidance, we present our Framework through the following pillars:

1. ESG Strategy
2. Target Setting
3. Process for project evaluation and selection
4. Reporting
5. Review

1. ESG Strategy

Real Assets Responsible Investment Policy

We have developed a clear policy framework with a consistent set of responsible investment policies to ensure our approach to ESG at an institutional, asset class and product level is clearly understood. The responsible investment policies sit within a tiered policy framework, ensuring that all policies maintain consistent principles and any positions agreed at an institutional level cascade down and are implemented across each asset class in an efficient manner.

AIRA has put in place a Real Assets Responsible Investment Policy with supporting RED Operating Procedures with the intention of promoting responsible investment, mitigating ESG risks and improving the performance of its clients' investments over time. Implementation of responsible investment practices occurs throughout the investment process. We seek to invest in assets and make improvements as required, rather than screen out underperforming assets. This is how we increase the overall ESG improvement and is a fundamental part of what we consider to be responsible investment.

An in-house proprietary ESG Risk Assessment Questionnaire has been developed for RED to enable the investment team to assess, at the outset of a lending opportunity, the associated ESG risks and impact. This covers a direct lend, acquisition of an existing loan or the event of existing borrowers substituting a new property into our charge. The ESG Risk Assessment Questionnaire helps guide both the Investment Committee and investment team in the appropriateness of any proposed loan, drawing in the wider expertise of the ESG Team where the assessment flags risk(s).

We prioritise investment selection decisions which have a positive contribution to society, and we aim to validate the sustainable value through the selection process. We do this by 1) selecting projects or investments where we believe the asset can make a positive impact on society; and 2) where we are able to contribute as a responsible investment manager by selecting and working with partners which have a proven track record in delivering projects in a sustainable manner.

2. Target Setting – Aligning to UN SDGs

For the purpose of this Framework, Sustainable Transition Loans are classified under one of the eligible criteria. We aim to have 2-3 eligible KPIs embedded in each loan, with a minimum requirement of 1 KPI selected from 'Group A'. Each loan will be assessed on an individual basis with example eligibility criteria below.

Group A

UN SDG Theme	Example Eligibility Criteria	Example initiatives and indicators
7 AFFORDABLE AND CLEAN ENERGY	**1. Energy efficiency** Targets that improve, or aim to improve, energy efficiency of buildings resulting in a reduction in energy consumption: - Reduce energy demand of at least 30% in comparison to the energy performance of the building before the renovation, in line with EU Taxonomy's 'Building renovation' (8.2) for 'Construction and real estate activities'; or - Improvement in energy efficiency through transition to EPC rating B or higher; or - Achieving green building certification through BREEAM excellent or outstanding accreditation	Example initiatives and projects can include, but are not limited to: • Improving building management systems (BMS) and installing smart meters • Improve energy efficiency of HVAC systems • Installation of onsite renewable energy • Installing LED lighting • Installation of energy storage technology • Installation of renewable heat technology
	2. Renewable energy Targets that improve, or aim to improve, the level of onsite low carbon energy resulting in an increase in renewable electricity generation: - Increase on-site renewable electricity generation proportion by at least 15%, or an equivalent amount per annum, through the lifetime of the loan. For example, certified by REGO backed sources (or equivalent); or - Commitment to procure 100% renewable power by 2050, For example, in line with the RE100's technical criteria (with interim target of 60% by 2030)	Example indicators: • Annual energy savings (e.g. kWh/m2.yr) • Annual energy supply from renewable sources (kWh.yr) • Green certification (e.g. EPC or BREEAM) • Renewable certification (e.g. RE100 Membership or REGO backed sources)

Group A (cont)

UN SDG Theme	Example Eligibility Criteria	Example initiatives and indicators
13 CLIMATE ACTION	**3. Green buildings** Targets that reduce, or aim to reduce, the level of carbon emissions of the borrower's buildings: - Setting carbon emissions reductions targets on buildings in line with limiting warming to 1.5°C, in line with Climate Bonds Standard (or equivalent); or - Commitment to develop a net-zero carbon pathway. For example, in line with the Science Based Targets initiative (SBTi) methodology	Example initiatives and projects can include, but are not limited to: • LEED Gold/Platinum • Increase in electrified heating • Increase level of occupier green energy tariffs Example indicators: • Green certification (e.g. Climate Bonds Standard certified) • Annual carbon intensity (kg CO2/m sq)

Group B

UN SDG Theme	Example Eligibility Criteria	Example initiatives and indicators
11 SUSTAINABLE CITIES AND COMMUNITIES 9 INDUSTRY, INNOVATION AND INFRASTRUCTURE	**4. Circular Economy** Targets that contribute to sustainable management of living natural resources and land use: - Onsite (or nearby) biodiversity net gain by at least 15% through measured improvements using the Natural England Biodiversity Metric (2019); or - Increase on-site biodiversity projects and recycling initiatives contributing to the conservation and recovery of natural habitats by at least 15%	Example initiatives and projects can include, but are not limited to: • EU Taxonomy's 'Individual measures and professional services' (8.3) for 'Construction and real estate activities', a list of eligible activities which are compliant with minimum requirements in the applicable national regulations • Tenant fit out guides to deliver SKA rated refurbishment • Refurbishment that contributes to the local community (e.g. investments into open space) • Clean infrastructure improvements (e.g. EV charging) and air quality improvements
	5. Clean Transportation Targets that increase the level of investments that promote use of low carbon transport: - Increase on-site low carbon transport infrastructure (e.g. electric vehicle charging, bike parking infrastructure) by at least 15%, or an equivalent amount per annum, through the lifetime of the loan	
	6. Wellbeing Targets that make buildings inclusive, safer, resilient and sustainable: - Increase on-site refurbishment initiatives that improve employee/occupier/ wellbeing by at least 15%; or - Improve occupier and staff wellbeing through certification towards the WELL Building standard, a performance-based certification scheme developed to put occupant health in building design	Example indicators: • % of material by total weight/volume/value • % of material certified for their sustainable qualities • % of reused or recycled material • % of dedicated parking spaces for electrical and hybrid vehicles • Certified WELL Building Standard

3. Process for project evaluation and selection:

Independent ESG Governance

In order to approve sustainable loans that meet the eligibility criteria of our Framework, we have established a robust governance process in our investment decision making process. This ensures that these loans are meaningful, impactful and consistent with our existing ESG standards.

Any RED Sustainable Transition Loan must:

1. Meet our rigorous existing ESG origination assessment process (as per our ESG Real Assets policy); and

2. Meet our Eligibility Criteria (as per section 2 of Framework); and

3. Be externally verified through an independent Second Party Opinion (SPO) provider

AIRA decision-making process for progressing sustainable loans are outlined below:

Steps	Description
Assess Loan Eligibility	At the outset we assess the borrower and opportunity through our existing ESG Real Asset policy process. We will use our in-house ESG scorecard, which assesses the asset, activity or counterparty involved in the transaction for exposure to ESG risk. Where ESG risk is deemed high, we may choose to decline the transaction, or impose further ESG covenants. We will engage with borrowers on identifying and setting appropriate KPIs linked to the eligibility criteria set in our Framework (see section 2).
Identify Financial Mechanisms	Financial incentives to incentivise the delivery of environmental performance will be modelled. These will generally be in the form of margin ratchets which reduce the cost of debt to the sponsor and allow our clients to become more competitive in winning lending opportunities with organisations which are keen to invest in becoming sustainable.
Initial Sustainability-Linked Loan Assessment	Assessment will be conducted on the coherence between the borrower's selected sustainable targets and our Framework. This will follow the main SLLP standard set by the LMA. These principles include: - Materiality, which is concerned with a view on a KPI being appropriate to the activities of the corporate and/or the project. - Ambition, which is a qualitative assessment of the pre-determined sustainability performance targets within the arrangement If the issuance satisfies the terms of the Framework's parameters, then the remaining SPO checks on ambition will be conducted by an external Second Party Opinion provider following investment committee approval.
External Second Party Opinion Analysis	Post investment committee due-diligence will cover the remaining aspects of borrower KPI alignment to our Framework to gain full SLL loan classification in-line with LMA principles. This will be externally verified by an independent SPO Provider

4. Reporting

Reporting will be conducted in two parts:

Sponsor/Borrower obligations

The sponsor/borrower will be primarily responsible for reporting against the KPIs agreed from this Framework. These will be recorded in the loan documentation, including providing the underlying data and assumptions used to calculate the KPI. The reports must satisfy the following requirements:

- The reports must demonstrate compliance with the KPI's along with the External Reviewer assessment of the loan and related procedures.

- The Sponsor's reporting will form part of the wider loan quarterly compliance reports.

- Where necessary, post-issuance verification and/or auditing of the data may be obtained to clearly demonstrate compliance.

Aviva Investors Reporting

We will report annually through:

- **Allocation Reporting.** For sustainable loans originated in-line with our Framework, we will report proceeds used for eligible loans. This will include the aggregated amount of allocation of the net proceeds to eligible assets aligned to the criteria. We will report this through our Aviva Investors Annual Responsible Investment review.

- **Impact Reporting.** Subject to borrower confidentiality agreements, we will endeavour to report on the KPI impact of eligible loans in our Framework. Owing to the large number of underlying assets and the limited available information, we will only present any KPIs on an aggregated basis.

5. Review

Second Party Opinion

The second party opinion (SPO) provider, VE, has reviewed this RED Sustainable Transition Loan framework and certified its alignment with LMA's Sustainability-Linked Loan Principles 2020. The SPO of the framework will be made available on our website.

Review & Rating Committee

The relevant Sponsors' reports will be reviewed and commented on in the loan annual review paper which is submitted to the Review & Rating Committee.

Sustainable Impact Lending Group

The Sustainable Impact Lending Group will oversee the lifetime of the loans to ensure proceeds are used for financing and/or refinancing of eligible criteria as defined in Section 2. The Group will also monitor the latest developments in the green, social and sustainability loan and bond markets, and update the Framework accordingly. The Group will be initially formed by members of the private debt origination, relationship management and credit teams, and will be chaired by the ESG Real Assets specialist.