

Energy Sector Policy

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Introduction

The energy sector provides the fuel, power and heat on which people, organisations and businesses across the world depend. It has played a key role in the improvement of living standards globally and is expected to continue its strong growth over the next 20 years, particularly in developing countries. This increasing demand for energy presents some significant challenges.

The generation and supply of energy can have negative impacts on people and on the environment when not managed responsibly. These impacts tend to increase where accessible energy resources have already been exploited and companies seek unconventional resources in sensitive or undeveloped locations. There is a growing trend towards exploiting unconventional resources, partly driven by the governments which are concerned about energy security and wish to exploit new energy resources within their own countries.

The sector also needs to respond to climate change. Its greenhouse gas emissions (GHGs), mainly carbon dioxide (CO₂) from the burning of fossil fuels, are a significant contributor to global warming. If serious impacts from climate change are to be avoided, energy demand needs to be reduced and energy supply made more efficient.

HSBC's Approach

HSBC has a long-standing commitment to sustainable development and, when supporting customers in the energy sector, we seek to balance the complex economic, environmental and social issues. Our internal Energy Sector Policy sets out the sustainability standards which guide our involvement with the sector and this document is a public summary of that policy. Our standards are based on international good practice, where available, and have been drawn up after extensive consultation with the sector and with other key stakeholders. The standards set benchmarks that we expect our customers to meet and also reflect HSBC's commitment to engage with and support our customers as they deal with complex challenges.

With many potential impacts of the sector addressed by our other policies, such as the Equator Principles, a particular area of focus in this policy is climate change. The basis of our approach is to support the transition to a low carbon economy. This transition will take time and, if living standards are to be maintained or improved, we recognise that carbon-intensive fossil fuels will remain part of the energy mix for the foreseeable future. However, this situation presents a dilemma. Activities that create high GHGs will, if unchecked, undermine international efforts to limit climate change. One of the most notable international efforts is the broad consensus that countries - led by developed countries under the principle of "common but differentiated responsibilities" - should cut global GHG emissions by 50% in the period of 1990-2050 if dangerous climate change is to be avoided. That target may yet prove to be ambitious but, nevertheless, HSBC recognises its own responsibility to incorporate the implications of climate change progressively into its business.

HSBC, therefore, adopts a cautious approach to activities which contribute significantly to climate change and which have a long asset life inconsistent with the transition to a low carbon economy. We analyse such situations by focusing on carbon intensity (the amount of GHGs per unit of energy), leaving customers and regulators to determine appropriate technologies. This approach allows HSBC to engage with and influence our customers, although we acknowledge that, ultimately, absolute reductions in GHGs will be needed if a 50% cut in global emissions is to be achieved by 2050.

Scope

The financial services covered by the policy include all lending and other forms of financial assistance, debt and equity capital markets activities, project finance and advisory work.

The activities within the scope of the policy are: oil and gas exploration and production; power generation from coal, oil, gas, nuclear or renewable sources; and electricity or gas transmission and distribution.

HSBC's other sector policies may also apply, such as *Forest Land and Forest Products* regarding biodiversity or the *Equator Principles* regarding the financing of projects such as oil production or refineries.

General Prohibitions and Restrictions

HSBC will not provide financial services which directly support specific operations or projects either in UNESCO World Heritage Sites or in wetlands on the Ramsar List.

Policy restrictions, requiring analysis and case-by-case approval, apply where customers are known to have operations or projects in, immediately adjacent to, or significantly impacting on the above sites, or where customers are known to be in breach of GHG regulations.

Coal-Fired Power Plants (CFPPs)

Within the energy sector, CFPPs are the most significant contributor to climate change. HSBC will increasingly support only new CFPPs which have lower carbon intensities. We will require more robust standards for developed countries¹.

We will not provide financial services which directly support new CFPPs, including expansions, with individual units of 500MW or more² and a carbon intensity³ exceeding:

- 850g CO₂/kWh in developing countries;
- 550g CO₂/kWh in developed countries. With existing technologies, this may require acceptable CCS (carbon capture and storage) plans⁴ or material benefits from combined heat and power or biomass.

In addition, there are policy restrictions requiring an analysis of carbon intensity where:

- Any other new CFPP exceeds 300MW. Particular emphasis is placed on whether the plant could be constructed with a lower carbon intensity and whether flue gas desulphurisation equipment is to be fitted.
- Plants of 300MW or more extend their previously agreed lifetime.
- Customers have a portfolio of CFPPs exceeding 3000MW in aggregate generating capacity.

Oil Sands

Oil sands are areas, mainly in Canada, where bitumen (semi-solid oil) is found in a mixture of sand and clay. The oil sands have economic benefits which include revenue generation, employment and energy security. They also have the potential for negative impacts relating to local communities, water usage, land affected by surface mining, contamination from tailings ponds and biodiversity. The way in which the oil is extracted and upgraded (partially refined) also means that oil from the oil sands may generate more GHGs per barrel than oil from more conventional sources, although the oil production process itself is responsible for only a small proportion of the related GHGs – most comes from combustion (such as use in vehicles).

HSBC has policy restrictions where customers are involved in the principal processes of mining, extraction and upgrading. We undertake a balanced analysis of positive and negative impacts to understand whether customers operate in accordance with good practice, focusing on factual data and trends where available. Specifically, we analyse: GHG intensity; water usage; land and tailings pond reclamation; the grievance process in place for local communities; and the extent to which a customer discloses standards and performance.

Nuclear Power Plants

Nuclear power prompts a wide variety of views in the countries where HSBC operates. Some stakeholders are concerned about the safety of dealing with radioactive materials. These concerns extend through the life cycle of a nuclear power plant to long-term waste disposal and decommissioning. There is also a risk that nuclear power plants could provide material for weapons. Other stakeholders contend that nuclear power generally has a good safety record, its technology and processes are continually improving, it offers energy security and it may be part of the solution to climate change because of its low GHG emissions.

1 Developed countries: High-Income Economies as defined by the World Bank Group.

2 CFPPs and individual units: The policy prohibition focuses on unit capacity rather than overall plant capacity. Cleaner technologies which allow lower carbon intensity are typically available for units with a gross capacity of 500MW or more, but some countries - especially developing ones - are limited to lower unit sizes by factors such as their local electricity grid.

3 Carbon intensity: Average annual CO₂ emissions divided by the annual average gross electricity production. Offsets are permitted for emissions where CO₂ is captured by CCS (subject to acceptable CCS plans), produced by biomass or offset by carbon credits meeting international standards. Offsets are permitted for electricity production where excess energy is used by a combined heat and power plant (eg to heat homes). Otherwise offsets are considered on a case-by-case basis.

4 Acceptable CCS plans: Firm and achievable plans are in place to capture, transport and permanently store CO₂ from the plant from the start of operations, typically reducing carbon intensity to less than 150g CO₂/kWh.

HSBC takes a balanced approach to the nuclear power sector, recognising the various types of potential impact. A policy restriction applies to customers in this sector and case-by-case approval of any business is required. Approvals are based on our analysis of a number of factors, such as: plants not being linked to weapons production; the principal safety and regulatory standards of the International Atomic Energy Agency (IAEA) being implemented; the operators having a proven track record; and plans being in place for waste storage and decommissioning. We make use of external performance data, such as IAEA reviews of regulators and safety, operating statistics from the World Association of Nuclear Operators and incidents recorded under the International Nuclear and Radiological Event Scale.

Best Practice

HSBC supports good international practice by its customers and encourages them to move towards best practice on the management of sustainability impacts. Our policy makes specific reference to:

- **Disclosure of GHG emissions** – which is often a first step towards reducing emissions and may be done independently or via frameworks such as the Carbon Disclosure Project.
- **Extractive Industries Transparency Initiative** - which encourages the sharing of economic and social benefits with local communities by publishing revenue figures.
- **International Petroleum Industry Environmental Conservation Association** - whose members commit to operate in an environmentally and socially responsible manner.
- **UNESCO World Heritage Sites** - which encourages companies to commit to a “no go pledge” to avoid operations in World Heritage Sites.
- **World Association of Nuclear Operators** - which supports safety in the nuclear power sector, including the use of a peer review system.

Summary

The energy sector will remain a key sector in the world economy. HSBC will support customers in the sector, subject to their meeting the standards of good environmental and social practice contained in this policy. We will exit relationships, or not enter into new relationships, where our standards are not met. We will review the policy from time to time in response to changes in technology, scientific opinion or governmental policies.

HSBC will proactively support the transition towards a low carbon economy, recognising that this will take time. Hence, we will continue to work with fossil fuel-based customers while supporting and encouraging them to move towards cleaner technologies. This engagement reinforces HSBC’s commitment to sustainable development and the attainment of a balance between economic, environmental and social demands.