Deborah Low, Jacob Pearlman in Real Estate Finance Journal on New LSTA Loan Principles

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The Loan Syndications and Trading Association developed guidelines to ensure the legitimacy and credibility of the Sustainability Linked Loan financial product as a means of facilitating and supporting environmental, social, and governance compliant economic activity and growth. These Sustainability Linked Loan Principles and guidance were recently amended. The authors of this article discuss the revised principles.

As interest in environmental, social, and governance ("ESG") financing has increased, lenders are increasingly looking to offer financial products for projects or companies that are environmentally friendly, socially conscious or focused improving a company's relationship with, or impact on, its community. One such financial product that has grown in popularity is the Sustainability Linked Loan ("SLL"), which includes a key pricing mechanism tied to the sustainability operations of the borrower.

Based on the borrower's sustainability policies and objectives, the borrower and the lender will identify key performance indicators ("KPIs") to measure the borrower's progress towards sustainability goals and then set a sustainability performance target ("SPT"). By way of example, the borrower and lender might determine that the KPI is the reduction of greenhouse gas emissions in the borrower's operations, while the SPT would be the specific percentage (such as 10 percent) by which emissions need to be reduced on a year over year basis. If the borrower meets the SPT and reduces its greenhouse gas emissions by 10 percent each year, it would be eligible to receive a reduction in pricing under the SLL, which might be reflected as a decrease in the margin or interest rate that kicks in once the SPT is met.

Given the increasing popularity of SLLs, the Loan Syndications and Trading Association ("LSTA") developed guidelines to ensure the legitimacy and credibility of the SLL financial product as a means of facilitating and supporting ESG compliant economic activity and growth. Known as the Sustainability Linked Loan Principles (the "SLLP"), these voluntary guidelines were first published in May 2019 and together with the accompanying Guidance on Sustainability Linked Loan Principles (the "Guidance") identify five key components of SLLs and provide a framework to better define the recommended or required elements of an SLL.

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