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## Second Party Opinion

# Neste Oyj's Green Finance Framework

Feb. 14, 2024

**Location:** Finland

**Sector:** Oil and gas refining and marketing

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## Alignment With Principles

Aligned = ✓ Conceptually aligned = ○ Not aligned = ✗

- ✓ Green Bond Principles, ICMA, 2021 (with June 2022 Appendix 1)
- ✓ Green Loan Principles, LMA/LSTA/APLMA, 2023

See [Alignment Assessment](#) for more detail.

**Medium green**

Activities that represent significant steps towards a low-carbon climate resilient future but will require further improvements to be long-term low-carbon climate resilient solutions.

Our [Shades of Green Analytical Approach](#) >

## Strengths

**Neste has developed a clear decarbonization roadmap with quantitative reduction targets.** Climate commitments are embedded into the long-term incentives of the company's key personnel and an internal carbon price is used to guide investments.

**The framework's eligible projects bring clear benefits for climate change mitigation and enable a circular economy.** Neste is supporting decarbonization in other sectors through its products. By refining waste, residue, and other raw materials, Neste produces renewable fuels and sustainable feedstocks for polymers and chemicals production. The inclusion of thresholds for the production of renewable fuels and feedstocks is positive.

## Weaknesses

No weakness to report.

## Areas to watch

**Neste's efforts to reduce deforestation risk have strengthened since its last framework, but it remains difficult to ensure no deforestation in its supply chain.** Neste has phased out palm oil, but risks remain for palm by-products and wastes, animal/fish waste and other vegetable oils.

**Fossil fuel-based oil products represent a large portion of Neste's business.** Nevertheless, Neste aims to make its Porvoo refinery a renewable and circular solutions site and end crude oil refining in the 2030s.

**The framework provides for debt instruments to which the Principles do not specifically apply.** This may require additional care in the selection of projects.

**The framework includes the possibility for investments in jointly controlled companies.** Neste will ensure its sustainability principles and guidance apply to joint ventures, for instance.

## Eligible Green Projects Assessment Summary

Eligible projects under issuer's green finance framework are assessed based on their environmental benefits and risks, using Shades of Green methodology.


**Eco-efficient and circular economy adapted products, production technologies, and processes**

  **Dark to Medium green**

Investment in assets and projects related to refining waste, residues, and innovative raw materials into renewable fuels such as sustainable aviation fuels (SAFs) and renewable diesel.

Investment in assets and projects related to refining waste, residue, and innovative raw materials into renewable feedstocks for polymers and chemicals production.

**Renewable energy**

 **Medium green**

Investment in assets and projects related to renewable energy production, including supporting infrastructure, technologies, and solutions such as green hydrogen and power-to-x.

See [Analysis Of Eligible Projects](#) for more detail.

## Issuer Sustainability Context

This section provides an analysis of the issuer's sustainability management and the embeddedness of the financing framework within its overall strategy.

### Company Description

Founded in 1948, Neste is an oil and gas refining and marketing company based in Espoo, Finland. The company is listed on the Nasdaq Helsinki, and the Finnish Prime Minister's Office is the largest shareholder, with 44.2% of share as of Dec. 31, 2023. Neste operates in four segments namely renewable products, oil products, marketing & services, and others. In 2023, renewable products and oil products represent 35.8% and 41.7% of its total revenue, respectively, amounting to €22.9 billion. Transforming from a traditional oil refiner, Neste has become the world's largest producer of renewable diesel and sustainable aviation fuel. Its renewable products include SAF, renewable diesel and renewable feedstock solutions for various polymers and chemicals industry uses, produced at its Porvoo, Rotterdam, and Singapore refineries.

### Material Sustainability Factors

#### Climate transition risk

Climate transition is the most material exposure for the oil & gas sector. Stakeholders are increasingly pushing to reduce greenhouse gas (GHG) emissions to fight climate change, shaping the strategic directions of a growing number of oil and gas companies toward less carbon-intensive operations, while reducing emissions throughout their value chains. More sector participants are detailing strategies, including changes to capital allocation, to reduce emissions or reach "net zero." This transition away from new oil and gas production activities, while still early, will likely be strongly influenced by government policies favoring low-carbon transportation and renewable energy. Due to the immense social and economic risks climate change poses, sovereign and local governments globally have been enacting stricter policies and regulations, while also providing subsidies aimed at reducing both GHG emissions from burning fossil fuels and spurring investment in more nascent technologies like carbon capture and storage and green hydrogen. Finland aims to achieve carbon neutrality by 2035 and then become carbon negative; the Netherlands and Singapore aim to reach net zero by 2050.

#### Pollution

Pollution associated with both upstream and downstream oil and gas operations can dramatically affect the environment and society, often leading to important biodiversity, health, and economic consequences for sector participants and the communities in which they operate. This includes air pollution, to which the refining industry is particularly exposed through nitrogen and sulfur oxide emissions, although asset modernization investments have helped reduce emissions intensity. Large-scale pollution catastrophes like Macondo are very rare but have severe consequences. Most pollution events, including pipeline spills, are small in scale and financially and operationally manageable by the industry, but still carry a risk of reputational damage, especially if not managed effectively. For example, the Finnish Oil Pollution Compensation Fund is managed by the Ministry of the Environment and compensates for the costs of oil spills.

#### Physical climate risk

Climate-related physical events such as hurricanes, rising sea levels, or flooding, can be disruptive to oil and gas operations, and, if severe enough, can directly affect large communities (notably by impeding the ability to work) and businesses around the globe by destroying homes and vital infrastructure. Heat waves are currently the biggest health hazard related to climate change in Finland, while Singapore and The Netherlands, where the company also operates refineries, are exposed to rising sea levels for instance.

#### Sustainable products and services

There is a growing need to provide sustainable products to gradually replace fossil-based fuels and chemicals in response to increasingly stringent government-led regulations and public awareness of the externalities linked to the extraction and combustion of hydrocarbons. This may mean greater demand for biofuels or other environmentally friendly substitutes and less for crude oil and refined products in the long run. Renewable road fuels and SAFs have lower emissions compared to traditional fuels, and benefit from regulatory credits, including low carbon fuel standards, biodiesel tax credits, and renewable identification numbers, which encourages fossil fuel conversion investments. Still, some of these products are not yet mature technologically.

### Biodiversity and resource use

Both upstream and downstream oil and gas operations can dramatically affect the environment. The downstream refining industry can have adverse impact on biodiversity, through the promotion of large-scale monoculture to be used as renewable feedstock or the location of industrial complexes in sensitive ecological areas. Policymakers' thinking on the assessment and preservation of natural capital is accelerating stringent regulatory action, which may require changes to materials sourcing. Refined products and chemical products can also impact biodiversity through air pollution, particularly from the impact of nitrogen and sulfur oxide emissions on soil and water. Other environment-related events include spills and leakages in pipelines that are generally on a small scale and manageable by the industry. In addition, even waste-based feedstocks can come from unsustainable initial production and have biodiversity impacts such as direct or indirect land use change.

## Issuer And Context Analysis

**Project categories aim to address climate transition risk, which is a material sustainability factor for Neste.** The company has set clear GHG emission reduction targets, including reducing scope 1 and 2 absolute emissions by 50% by 2030 and scope 3 intensity-based emissions by 50% by 2040, achieving carbon neutral production by 2035 and 100% renewable electricity by 2023. Neste has achieved 93.8% share of renewable electricity as of the end of 2022, and its refinery at Porvoo achieved 100% in 2020. Extending beyond its footprint, Neste targets a carbon-neutral value chain by 2040 and to reduce its carbon handprint by helping its customers to reduce their emissions by avoiding 20 million tons of carbon dioxide equivalent (MtCO<sub>2</sub>e) annually by 2030 with its renewable products. In 2023, Neste enabled its customers to reduce GHG emissions by 11.0 million tons of CO<sub>2</sub>e. While fossil fuel-based oil products still represent a large portion of Neste's current business, it aims to convert its Porvoo refinery into a renewable and circular solutions site and end crude oil refining in the mid-2030s. Climate commitments are embedded into the long-term incentives of the company's key personnel and an internal carbon price is used to guide investments.

**Neste's renewable and circular solutions help combat plastic waste pollution.** The company recycles plastic waste into feedstocks for polymers and chemicals production, enabling a circular economy and reducing the need for virgin fossil resources. It aims to process over 1 million tons of plastic waste annually from 2030. However, recycling plastic waste implies plastic will not be phased out soon.

**Physical risks are important considerations for Neste's operations.** The company relies on its company-level physical climate risk management procedures aligned with Task Force on Climate-related Financial Disclosures (TCFD) recommendations, including conducting scenario analysis to assess the resilience and adaptability of its strategy to climate change. Neste acknowledges that both acute (e.g. extreme weather events) and chronic physical risks (e.g. changes in precipitation patterns or rises in sea level), may cause disruptions in its supply chain and the availability of different raw materials, as well as operating issues or damages to its industrial sites. In addition, Neste has evaluated the water stress status, showing that all of its sites fall into low to moderate physical risks regarding indicators such as flooding, water quality, ecosystem services and biodiversity importance. Yet, mitigation measures are not clearly articulated in the project selection process.

**The framework's eligible projects support Neste's sustainable product offerings.** Neste expects to expand its renewable and circular solutions by increasing its production capacity of renewable products. For example, it intends to expand its Singapore and Rotterdam refineries. The company has strong research and development (R&D) investment (€85 million in 2022) in developing innovative business platforms for new sustainable and scalable feedstock pools. Its renewable feedstock products, for example, can be used as a sustainable drop-in solution for the polymers and chemical industry.

**Biodiversity considerations could gain in prominence as the company diversifies its current portfolio to include new raw materials.** As part of its biodiversity vision launched in 2021, Neste has set targets of achieving net positive impact from new activities from 2025 and no net loss from all ongoing activities by 2035. Although we note past allegations around deforestation and unfavorable working conditions from Neste's palm oil suppliers, the company's transparent supplier traceability dashboard (an online platform disclosing information on its palm oil and palm fatty acid distillate (PFAD) supply chain), and publicly accessible monthly grievance logs partly mitigate these risks. Neste also reduced its refinery inputs of conventional palm oil to zero at the end of 2023. However, the use of PFAD may still link to environmental risks such as land use change. Nevertheless, Neste is committed to having all renewable crop based raw materials traceable to their cultivation sites and waste based raw materials to their production sites.

# Alignment Assessment

This section provides an analysis of the framework's alignment to the Green Bond and Loan principles.

## Alignment With Principles

Aligned = ✓ Conceptually aligned = ○ Not aligned = ✗

- ✓ Green Bond Principles, ICMA, 2021 (with June 2022 Appendix 1)
- ✓ Green Loan Principles, LMA/LSTA/APLMA, 2023

### ✓ Use of proceeds

All of the framework's green project categories are shaded in green, and Neste commits to allocate the net proceeds raised under the framework exclusively to eligible projects. Eligible investments cover assets or operations of both controlled or jointly-controlled entities. Under the framework, Neste can issue a variety of green debt instruments including green bonds, green loans, and green commercial paper to finance or refinance eligible green projects that contribute to climate change mitigation. The maximum lookback period for refinancing is 36 months, in line with standard market practice.

The framework includes two green project categories, namely eco-efficient and circular economy adapted products, production technologies and processes, and renewable energy. Please refer to Analysis of Eligible Projects section for more information on our analysis of the environmental benefits of the expected use of proceeds.

### ✓ Process for project evaluation and selection

Neste has established a green finance committee (GFC) to oversee the allocation of proceeds. The committee includes members from management, treasury and sustainability. The sustainability representative holds a veto right, adding credibility to the screening process. Neste's investment committee will first submit a list of projects to the GFC. The GFC will then verify the eligibility of assets and approve shortlisted projects. Neste will identify and manage associated environmental and social risks of financed projects, adhering to its sustainability policy, which is publicly accessible. The framework also excludes funding activities that relate to fossil fuel refining, fossil fuel co-processing activities, and fossil-based feedstocks.

### ✓ Management of proceeds

Neste will use a green debt register to track and monitor the net proceeds raised from instruments issued under the framework. The register will include the allocation of proceeds from instruments to eligible assets and projects. Neste commits, on a best effort basis, to fully allocate all the proceeds within two years of issuance, in line with market practice. If an asset no longer meets the framework's eligibility criteria, the GFC will adjust the eligible green asset portfolio accordingly. Pending allocation, proceeds will be held in accordance with Neste's liquidity management policy and in cash or placed in liquid instruments such as interest-bearing securities.

### ✓ Reporting

Neste commits to reporting annually on the allocation and impacts of proceeds until full allocation of the green debt instruments. Reporting will include the amounts allocated and unallocated, description of activities financed, breakdown of financing versus refinancing, among others. Neste will also report on the actual or expected impact of financed projects. These impact indicators include the amount of GHG emissions avoided through the use of renewable products, amount of renewable energy generated, capacity of renewable energy constructed, among others. Same as Neste's previous green finance reports, the company commits to engage an independent third party to review and verify the allocation reporting, adding transparency.

# Analysis Of Eligible Projects

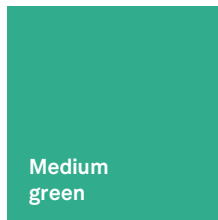
This section provides details of our analysis of eligible projects, based on their environmental benefits and risks, using the Shades of Green methodology.

The net proceeds issued under the framework will be exclusively used to finance and refinance eligible eco-efficient and circular economy adapted products, production technologies and processes, and renewable energy projects, while Neste does not have an estimate share between the two categories.

Neste expects the majority of proceeds to be allocated to financing activities, while a minority of proceeds will be directed to refinancing.

## Overall Shades of Green assessment

Based on the project category shades of green detailed below, and consideration of environmental ambitions reflected in Neste's green finance framework, we assess the framework medium green.



**Medium green**

Activities that represent significant steps towards a low-carbon climate resilient future but will require further improvements to be long-term low-carbon climate resilient solutions.

Our [Shades of Green Analytical Approach](#) >

## Green project categories

### Eco-efficient and circular economy adapted products, production technologies and processes

#### Assessment

**Dark to Medium green**

#### Description

Investment in assets and projects related to refining waste, residues, and innovative raw materials into:

(a) renewable fuels such as SAFs and renewable diesel; and

(b) renewable feedstocks (such as isoalkane oil, naphtha, and propane) for polymers and chemical production.

Renewable fuels:

Refining waste, residues and innovative raw materials into renewable sustainable aviation fuels reduces GHG emissions up to 80% over the fuel's life cycle compared to fossil jet fuel (CORSA method). For renewable diesel, the GHG emission reduction is 75% or 95% compared to fossil diesel over the fuel's life cycle (the GHG emission reduction varies depending on the region-specific legislation that provides the methodology for the calculations (e.g. EU RED II 2018/2001/EU for Europe and US California LCFS for the US), and the raw material mix used to manufacture the product for each market).

Renewable polymers and chemicals:

Refining waste, residues and innovative raw materials into drop-in solutions that are produced from 100% renewable raw materials provide more than 85% smaller carbon footprint over the life cycle compared with conventional fossil raw materials for polymer and chemicals production (Life cycle assessment of environmental impacts of Neste RE, June 2021).

All Neste's renewable production refineries are International Sustainability & Carbon Certification (ISCC) certified or approved by the U.S. Environmental Protection Agency (EPA).

#### Analytical considerations

- Renewable fuels and feedstocks for polymers and chemical production support climate change mitigation. According to Neste, its SAFs has up to an 80% smaller carbon footprint compared to kerosene; renewable diesel has 75% or 95% lesser lifecycle emissions compared to conventional diesel; and recyclable feedstocks have more than 85% carbon reduction compared with

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traditional fossil raw materials for polymer and chemicals production. Neste's renewable products help the EU and its customers such as the aviation and polymers/ chemicals industry to meet their GHG reduction targets. These products and technologies also help enable a circular economy, which is a dark green element. They contribute to reducing the use of resources and emissions associated with raw materials by reusing waste and residue. We note from Neste's Green Finance Report 2022 that the use of its renewable and circular solution products is estimated to avoid an average of 3 MtCO<sub>2</sub>e of GHG emissions at the time of completion per annum.

- The raw materials of Neste's renewable products are primarily waste and residue (e.g. animal fat from the food industry, used cooking oil, and wastes and residues from vegetable oils processing), accounting for 92% of its total inputs. While Neste has reduced its refinery inputs of conventional palm oil to zero at the end of 2023, which is likely to reduce deforestation risks, the use of PFAD (i.e. palm oil refining residues) may still link to land use change, contributing to the range of shades. Neste follows its Supplier Code of Conduct and Responsible Sourcing Principle, such that it buys only raw materials that are traceable to the point of origin. Being certified by ISCC or approved by EPA adds an additional layer of safeguards.
- The transportation of raw materials is another source of GHG emissions. Neste is working to optimize its logistics by engaging its logistics partners to scale up the use of lower-emission solutions and increasing fuel efficiency. On product distribution, Neste has renewed its fleet to more energy-efficient vessels and used renewable diesel in Finland since 2021.
- Neste shared that some of the heating needs at its refineries are still covered by fossil fuels, but that they are working to replace this by renewable energy, as part of their climate roadmap. While Neste endeavors to achieve 100% of its purchased electricity to be renewable by 2023, its refinery in Singapore is connected to a fossil fuel heavy power grid. Measures include purchasing renewable electricity certificates from neighboring countries.
- Physical climate risks and biodiversity are important for both Neste's operations and its supply chain. Neste will rely on scenario analysis to evaluate potential impacts of physical climate risks. For example, as per Neste's water stress study, all Neste locations fall into low or moderate level of physical risks, covering indicators such as flooding, water quality, ecosystem services, and biodiversity importance. In addition, Neste will conduct a biodiversity assessment on potential sites and create a biodiversity baseline at the beginning of the project cycle. The company has also set a target to create net positive impacts from new activities from 2025.

### Renewable energy

#### Assessment

 **Medium green**

#### Description

Investment in assets and projects related to renewable energy production including supporting infrastructure, technologies, and solutions such as green hydrogen, and power-to-x.

### Analytical considerations

- Only green hydrogen (i.e. produced from water and renewable electricity) and not blue or grey hydrogen is eligible under the framework. Green hydrogen is part of a 2050 solution due to applications in industrial processes, transportation, and energy storage, as well as being a lower emissions energy source. Under this framework, renewable energy produced will be used for Neste's renewable product production, but not fossil fuel refining or fossil-based feedstocks, as per the exclusion.
- Leakage of stored hydrogen is difficult to avoid due to the gas' small molecule size and low density. Impacts from leakage of stored hydrogen to the atmosphere are not yet well-understood, but emerging research indicates it could increase the atmospheric lifetime of methane and its climate impacts, partially offsetting its emissions reduction benefits, and may contribute to Antarctic ozone depletion. Nevertheless, Neste has measures in place to prevent hydrogen leakage and to manage potential safety issues, such as conducting safety studies, selecting suitable materials for high pressure hydrogen use, and ensuing adequate preventive barriers and safeguards.
- The use of power-to-x technology is still in evaluation phase. As communicated with Neste, while the end-products are not yet clearly decided, the company is considering options such as drop-in renewable fuels of non-biological origin (RFNBO), e-fuels, green ammonia, e-methanol, e-naphtha. Primary inputs will be green hydrogen and carbon dioxide (CO<sub>2</sub>). Such CO<sub>2</sub> should be non-fossil (i.e. either biogenic or from direct air capture) in order to avoid transition risks. Biogenic CO<sub>2</sub> may be associated with direct and indirect land use change if sourced from biomass/ biofuel combustion, depending on feedstock, as well as substitution effects and valorization of potentially unsustainable economic activities if derived from waste and by-products.















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Neste does not currently have visibility on potential CO2 input sources. Nevertheless, Neste commits to only financing activities where the input is considered as green under this framework and complying with regulatory criteria.

- We are mindful of the significant amounts of renewable energy required for green hydrogen production and associated lifecycle emissions and environmental risks. The project category receives a Medium Green shading because Neste has yet to set a lifecycle emission threshold for green hydrogen and power-to-x but is following the regulation development in this area.
- Similarly, Neste will rely on scenario analysis and water stress study to evaluate potential impacts of physical climate risks. Biodiversity assessment will be conducted similarly at the beginning of the project cycle.

S&P Global Ratings' Shades of Green

Assessments					
 Dark green	 Medium green	 Light green	 Yellow	 Orange	 Red
Description					
Activities that correspond to the long-term vision of an LCCR future.	Activities that represent significant steps toward an LCCR future but will require further improvements to be long-term LCCR solutions.	Activities representing transition steps in the near-term that avoid emissions lock-in but do not represent long-term LCCR solutions.	Activities that do not have a material impact on the transition to an LCCR future, or, Activities that have some potential inconsistency with the transition to an LCCR future, albeit tempered by existing transition measures.	Activities that are not currently consistent with the transition to an LCCR future. These include activities with moderate potential for emissions lock-in and risk of stranded assets.	Activities that are inconsistent with, and likely to impede, the transition required to achieve the long-term LCCR future. These activities have the highest emissions intensity, with the most potential for emissions lock-in and risk of stranded assets.
Example projects					
 Solar power plants	 Energy efficient buildings	 Hybrid road vehicles	 Health care services	 Conventional steel production	 New oil exploration

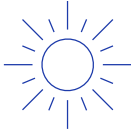



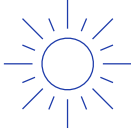
Note: For us to consider use of proceeds aligned with ICMA Principles for a green project, we require project categories directly funded by the financing to be assigned one of the three green Shades.

LCCR--Low-carbon climate resilient. An LCCR future is a future aligned with the Paris Agreement; where the global average temperature increase is held below 2 degrees Celsius (2 C), with efforts to limit it to 1.5 C, above pre-industrial levels, while building resilience to the adverse impact of climate change and achieving sustainable outcomes across both climate and non-climate environmental objectives. Long term and near term--For the purpose of this analysis, we consider the long term to be beyond the middle of the 21st century and the near term to be within the next decade. Emissions lock-in--Where an activity delays or prevents the transition to low-carbon alternatives by perpetuating assets or processes (often fossil fuel use and its corresponding greenhouse gas emissions) that are not aligned with, or cannot adapt to, an LCCR future. Stranded assets--Assets that have suffered from unanticipated or premature write-downs, devaluations, or conversion to liabilities (as defined by the University of Oxford).

# Mapping To The U.N.'s Sustainable Development Goals

Where the Financing documentation references the Sustainable Development Goals (SDGs), we consider which SDGs it contributes to. We compare the activities funded by the Financing to the International Capital Markets Association (ICMA) SDG mapping and outline the intended linkages within our SPO analysis. Our assessment of SDG mapping does not impact our alignment opinion.

This framework intends to contribute to the following SDGs:

Use of proceeds	SDGs			
Eco-efficient and circular economy adapted products, production technologies and processes	 <b>7. Affordable and clean energy</b>	 <b>9. Industry, innovation and infrastructure</b>	 <b>*12. Responsible consumption and production</b>	 <b>13. Climate action</b>
Renewable energy	 <b>*7. Affordable and clean energy</b>			

\*The eligible project categories link to these SDGs in the ICMA mapping.

## Related Research

- [Analytical Approach: Second Party Opinions: Use of Proceeds](#), July 27, 2023
- [Analytical Approach: Shades of Green Assessments](#), July 27, 2023
- [FAQ: Applying Our Integrated Analytical Approach for Use-of-Proceeds Second Party Opinions](#), July 27, 2023
- [ESG Materiality Map: Oil and Gas](#), May 18, 2022

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