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ASSESSMENT
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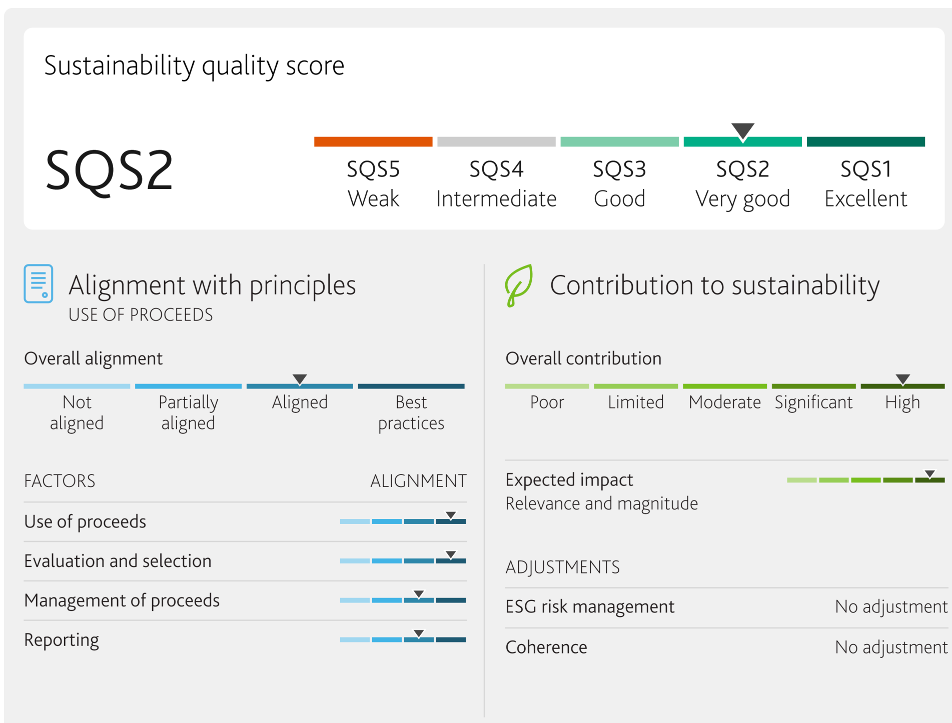
# Lugos Renewables LLC

## Second Party Opinion – Green Finance Framework Assigned SQS2 Sustainability Quality Score

## Summary

We have assigned an SQS2 Sustainability Quality Score (very Good) to Lugos Renewables LLC's green finance framework dated 5 June 2023. The holding company has established its use-of-proceeds framework to finance projects across one eligible green category, renewable energy. Lugos Renewables has described the main characteristics of the green finance instruments within a formalized framework that is aligned with the four core components of the International Capital Market Association's (ICMA) Green Bond Principles (GBP) 2021 (including the June 2022 Appendix 1), and the Loan Market Association, the Asia Pacific Loan Market Association and the Loan Syndications & Trading Association's (LMA/APLMA/LSTA) Green Loan Principles (GLP) 2023. Furthermore, the framework demonstrates a high contribution to sustainability.



## Scope

We have provided a Second Party Opinion (SPO) on the green credentials of Lugos Renewables' green finance framework, including the framework's alignment with the ICMA's GBP 2021 (including the June 2022 Appendix 1) and the LMA/APLMA/LSTA's GLP 2023. Under its framework, the holding company plans to finance projects comprising one green category, as outlined in Appendix 2 of this report. The framework is applicable to Lugos Renewables and all subsidiaries of the holding where Lugos Renewables has ownership and influence.

Our assessment is based on the last updated version of Lugos Renewables' framework dated 5 June 2023, and our opinion reflects our point-in-time assessment of the details contained in this version of the framework, as well as other public and non-public information provided by the company.

We produced this SPO based on our Framework to Provide Second Party Opinions on Sustainable Debt, published in October 2022.

## Issuer profile

Founded in 2014 and headquartered in Budapest, Lugos Renewables LLC is a developer of solar projects. It operates in Hungary and the Balkans, and assists its clients in planning, licensing, implementation and operation of the assets. Furthermore, Lugos Renewables undertakes the preparation of development plans for the existing energy portfolio, the sale of project rights and the provision of services in connection with the power plants to be constructed. As of June 2023, Lugos Renewables had more than 7 gigawatts (GW) of solar power capacity under development in six countries.

Lugos Renewables' sustainability considerations cover environmental, social and governance (ESG) topics. As regards environmental measures, Lugos Renewables focuses on decreasing waste and emissions along its operations by increasing recycling, using electric vehicles and investing in sustainable energy sources. As a project development company, Lugos Renewables conducts ESG assessments of its subcontractors, based on its procurement policy.

## Strengths

» The eligible category is clearly defined and has the option to follow the European Union (EU) taxonomy criteria.

» Eligible projects address environmental challenges that are highly relevant for the issuer and its sector.

» The environmental benefits are relevant and measurable.

» The process for project evaluation and selection is structured and transparent, and incorporates an assessment of ESG risks and benefits for each selected project.

» Continued compliance of selected projects is monitored throughout the life of any instrument issued under the framework.

## Challenges

» The allocation period goes beyond 24 months.

» There is no independent verification of the allocation and impact reporting on environmental benefits or externalities associated with the financed projects.

## Alignment with principles

Lugos Renewables' green finance framework is aligned with the four core components of the ICMA's GBP 2021 (including the June 2022 Appendix 1) and the LMA/APLMA/LSTA's GLP 2023 for all four components:

- [x] Green Bond Principles (GBP)
- [ ] Social Bond Principles (SBP)
- [x] Green Loan Principles (GLP)
- [ ] Social Loan Principles (SLP)
- [ ] Sustainability-Linked Bond Principles (SLBP)
- [ ] Sustainability Linked Loan Principles (SLLP)

### Use of proceeds

| Not aligned | Partially aligned | Aligned | Best practices ▼ |
|---|---|---|---|

**Clarity of the eligible category – BEST PRACTICES**

Lugos Renewables has clearly communicated the nature of the expenditures and detailed the eligibility as well as the exclusion criteria for the single category, renewable energy, including solar photovoltaic (PV) and electricity storage projects. As optional eligibility criteria, the framework includes the EU taxonomy criteria for economic activities 4.1 and 4.10, which constitute stringent and internationally recognized technical thresholds. We have not assessed the adherence of the framework to the EU taxonomy criteria. Possible locations of the projects include, but are not limited to, Hungary and the Balkans (North Macedonia, Bulgaria, Serbia, Croatia, Albania, Montenegro, Romania, Bosnia and Kosovo). In the event that additional countries are added to the portfolio, the issuer has undertaken to inform investors of the new locations.

**Clarity of the environmental objectives – BEST PRACTICES**

Lugos Renewables has clearly outlined a relevant environmental objective for the eligible category, namely climate change mitigation. The environmental objective is coherent with the EU taxonomy objectives, and the issuer has linked the eligible category to several United Nations' Sustainable Development Goals (UN SDGs).

**Clarity of expected benefits – BEST PRACTICES**

Lugos Renewables has clearly identified environmental benefits for the eligible category. These benefits are relevant, measurable and will be quantified in the reporting. In case of refinancing, the company commits to disclosing the share of refinancing before issuance and to keeping the lookback period limited to four calendar years from the issuance of the instruments.

**Best practices identified**

- » Eligibility criteria are clearly defined for all project categories
- » Objectives set are defined, relevant and coherent for all project categories
- » Relevant benefits are identified for all project categories
- » Benefits are measurable and quantified for most projects, either ex-ante with clear baselines or with a commitment to do so in future reporting
- » Commitment to transparently disclose the share of proceeds used for refinancing where feasible
- » Commitment to transparently communicate the associated lookback period(s) where feasible

## Process for project evaluation and selection

| Not aligned | Partially aligned | Aligned | Best practices ▼ |
|---|---|---|---|

**Transparency and quality of the process for defining eligible projects – BEST PRACTICES**
Lugos Renewables has established a clear and structured process for the evaluation and selection of eligible projects, including detailed decision-making criteria, as well as roles and responsibilities formalized in its publicly available framework. The process relies on relevant internal expertise and more precisely on the existence of a Green Finance Committee, consisting of a managing director (chairman), a head of design and a business development expert. If advice is required in specific cases, experts may be called in (including professionals with legal, technical, financial or risk management expertise). Occasionally, representatives of the relevant subsidiaries and holding companies can be invited as well. The Green Finance Committee is responsible for reviewing expenditures in terms of their alignment with the eligibility criteria defined in the use of proceeds, and monitoring the compliance of the existing allocation of proceeds on a biannual basis throughout the lifetime of the respective financial instrument. Projects that become ineligible can be left out from funding. This process is traceable and documented.

**Environmental and social risk mitigation process – BEST PRACTICES**
The environmental and social (E&S) risk mitigation process is disclosed in Lugos Renewables' framework, and is embedded in its process for project evaluation and selection, as well as its environmental policy, to be disclosed to investors on demand. Environmental impact assessment is carried out before the construction of each project. The process implemented includes a combination of identification, management, mitigation, monitoring and control measures. As part of preliminary ESG assessments, which include assessments to minimize pollution, waste production, protection of biodiversity and natural resources, the company also evaluates its subcontractors to assess their level of exposure to ESG risks.

The process for managing potential E&S controversies for financed projects and the associated reallocation of proceeds are part of the responsibilities of the Green Finance Committee, and the framework specifies that projects facing E&S controversies can be withdrawn from the funding. The Green Finance Committee is responsible for monitoring E&S controversies on a biannual basis throughout the lifetime of the respective financial instrument, and to mitigate and take corrective actions in cooperation with relevant stakeholders (for example, local authorities, the community and with NGOs).

### Best practices identified

» The roles and responsibilities for project evaluation and selection are clearly defined and include relevant expertise

» There is evidence of continuity in the selection and evaluation process through the life of the financial instrument(s), including compliance verification and procedures to undertake mitigating actions when needed

» The process for project evaluation and selection is traceable

» Material environmental and social risks for most project categories are identified

» Presence of corrective measures to address environmental and social risks across projects

» ESG controversies are monitored

## Management of proceeds

| Not aligned | Partially aligned | Aligned | Best practices |
|---|---|---|---|

**Allocation and tracking of proceeds – ALIGNED**

The company has defined a clear process for the management and allocation of bond proceeds in its publicly available framework. Net proceeds raised will be managed by the Green Finance Committee and segregated on a separate account or subaccount, using a bond-by-bond approach. There will be periodic tracking of how funds are matched to eligible projects, and this will be adjusted at least annually to match allocations made during that period. The allocation period will be within 36 months from the time of the issuance.

**Management of unallocated proceeds – BEST PRACTICES**

Unallocated proceeds will be invested in cash, cash equivalents or other liquid instruments. The framework has explicitly excluded temporary placements of unallocated proceeds into nuclear energy generation, weapons and defense, gambling or tobacco, and potentially environmentally harmful resource extraction and green house gas (GHG)-intensive activities. In the event that a project is postponed, canceled or otherwise becomes ineligible, the company has committed to replace that project with a new eligible project.

### Best practices identified

» Broad disclosure of a clearly articulated and comprehensive management of proceeds policy to external stakeholders; bondholders or lenders at a minimum

» Disclosure on temporary placement and presence of exclusion criteria toward environmentally or socially harmful activities

» Commitment to reallocate proceeds to projects that are compliant with the framework

## Reporting

| Not aligned | Partially aligned | Aligned | Best practices |
|---|---|---|---|

**Transparency of reporting – ALIGNED**

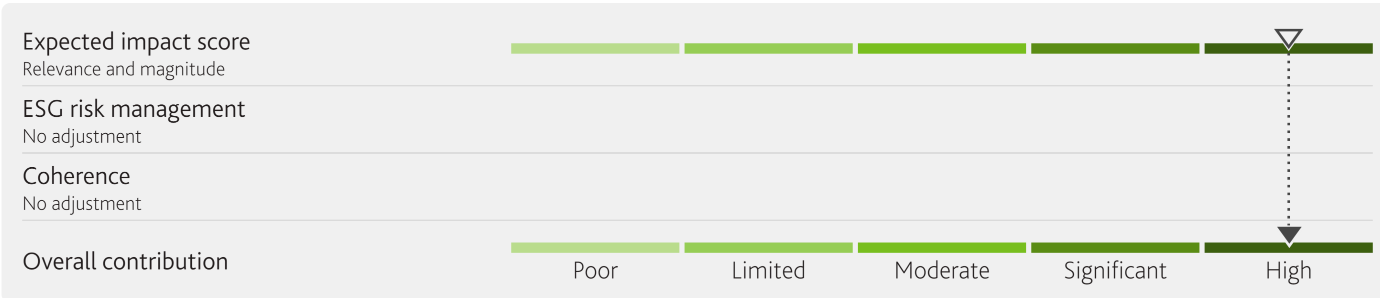
Lugos Renewables will report annually on the use of proceeds of bonds issued under its framework. This reporting will be publicly available and will disclose data from all subsidiaries within the holding. Allocation and impact reporting will be conducted until full allocation of proceeds and on a timely basis in case of significant developments. The reporting is exhaustive, including the amount of proceeds allocated, a brief description of the projects, the number of eligible loans, balance of unallocated funds and share of refinancing, significant changes or controversies that may impact the investment of bondholders and the expected environmental benefits of the projects. The company has identified relevant environmental reporting indicators, and has clearly disclosed these indicators in its framework. The methodology and assumptions used to report on environmental impacts will be publicly available in the impact reporting. Lugos Renewables is considering the possibility of obtaining a post-issuance verification by a third party in the future.

### Best practices identified

- Reporting covers material developments and issues related to the projects or assets
- Reporting on allocation of proceeds and benefits done at least at eligible category level
- Exhaustive allocation reporting – balance or % of unallocated funds, types of temporary investments (e.g. cash or cash equivalent) and share of financing vs re-financing
- Clear and relevant indicators to report on the expected environmental impact of all the projects, where feasible, or eligible categories
- Disclosure of reporting methodology and calculation assumptions to bondholders or lenders at a minimum

## Contribution to sustainability

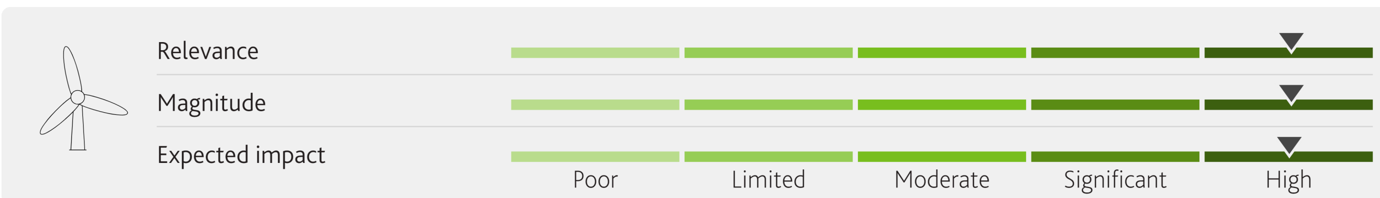
The framework demonstrates a high overall contribution to sustainability.




### Expected impact

The expected impact of the eligible project category on the environmental objectives is high. A detailed assessment of the single eligible category is provided below.

**Renewable energy**




Financing energy transition is considered a key issue and of high relevance to the decarbonization challenges of the Hungarian and the Balkan economies, as the energy mix in these countries, where the projects will be implemented, is highly dependent on fossil fuels for the overall energy supply[1]. In Hungary, for example, only 21.4% of electricity was generated from renewable energies in 2022[2]

In terms of magnitude, the eligible category is likely to contribute to a highly positive long-term impact. Neither the electricity generation nor the storage projects are expected to have lock-in effects or significant negative externalities, as the issuer has committed to exclusively use solar PV panels and batteries for storage. Both technologies are in line with the most stringent internationally recognized standards for green projects that contribute to climate change mitigation. As the projects are not limited to rooftop, we assessed the company's management of land use and biodiversity, and it appears to have solid risk management measures in place. For example, the issuer has informed that ground installations are most likely to be carried out only in areas with no constraints or lack of space or on low-quality soil. Lugos Renewables has informed that the vast majority of the proceeds will be allocated to PV technologies, with just a small amount financing electric battery storage.

### ESG risk management

We have not applied a negative adjustment for ESG risk management to the expected impact score. Hungary is a Designated Country under the Equator Principles (EP)[3], which requires the issuer to sufficiently address the management of most of the E&S risks. The issuer states that the expansion of its activities to the Balkans — all of which are Non-Designated Countries as defined by the EP — should be accompanied by the introduction of new policies reflecting Lugos Renewables' commitment regarding ESG requirements. In any case, Lugos Renewables has confirmed that in all those countries an environmental impact assessment will be carried out before the construction of any new asset. The holding company monitors ESG compliance of its subcontractors in the projects executed under its supervision.

### Coherence

We have not applied a negative adjustment for coherence to the expected impact score. The solar projects to be financed under the framework correspond to the core activity of the company, which includes increasing the share of renewable energies in the global energy mix in cooperation with its subcontractors. Those are also aligned with the sustainability priorities of Lugos Renewables, as stated in its environmental policy, which entails the reduction of GHG emissions and other air pollutants.

## Appendix 1 - Mapping eligible categories to the United Nations' Sustainable Development Goals

The single eligible category included in Lugos Renewables' framework is likely to contribute to two of the UN SDGs, namely:

| UN SDG 17 Goals | Eligible Project | SDG Targets |
|---|---|---|
| GOAL 7: Affordable and Clean Energy | Renewable energy | 7.2: Increase substantially the share of renewable energy in the global energy mix |
| GOAL 13: Climate Action | Renewable energy | 13.1: Strengthen resilience and adaptive capacity to climate-related hazards and natural disasters in all countries |

The UN SDGs mapping in this SPO takes into consideration the eligible project category and the associated sustainability objectives/ benefits documented in the issuer's financing framework, as well as resources and guidelines from public institutions, such as the ICMA's SDG Mapping Guidance, and the UN SDG targets and indicators.

## Appendix 2 - Summary of eligible categories in Lugos Renewables' framework

| Eligible Project Category | Description | Sustainability Objectives | Impact Reporting Metrics |
|---|---|---|---|
| Renewable energy | New or existing investments in or expenditures on the development, construction and/or installation of Solar PVs (including rooftop solar projects), including electrical storage infrastructure related to renewable energy production,<br><br>or<br><br>Alignment with the EU Taxonomy Regulation and its Minimum Social Safeguards (MSS), Technical Screening Criteria (TSC) and Do No Significant Harm Criteria (DNSH) related to eligible project category 4.1 and/or 4.10 with substantial contribution to the Climate Change Mitigation objective. | Climate Change Mitigation | - Installed renewables capacity in MW<br>- Annual renewable energy generation in MWh<br>- Annual avoided GHG emissions (t $CO_2e$) |

## Moody's related publications

### Second Party Opinion analytical framework:

» Framework to Provide Second Party Opinions on Sustainable Debt, October 2022

### Topic page:

» ESG Credit and Sustainable Finance

## Endnotes

1 IEA - International Energy Agency, Countries, retrieved in June 2023

2 Our World in Data, Hungary, retrieved in June 2023.

3 About the Equator Principles, Equator Principles, retrieved in June 2023.

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