

## Task Force on Climate-related Financial Disclosures (“TCFD”)

31 March 2022

The challenge posed by climate change necessitates a complete transformation of the way the world produces and consumes energy. In August 2021, the United Nations’ Intergovernmental Panel on Climate Change (“IPCC”) published their Sixth Assessment Report, which stated “global warming of 1.5°C and 2°C (before pre-industrial levels) will be exceeded during the 21st century, unless deep reductions in CO<sub>2</sub> and other greenhouse gas emissions occur in the coming decades”. The transition to a low-carbon economy is imperative to make meaningful reductions in global greenhouse gas concentrations, minimise long-term climate change impacts, and enable a development trajectory that is sustainable on a global scale.

The Company sees renewable energy as having a crucial role to play in the low-carbon transition and in providing economic opportunities that support governmental mandates such as the UK net-zero target by 2050.

To be a leader in ESG and responsible investment space, accountability is paramount. The Investment Manager has delivered on increased transparency reporting as this constitutes a valuable addition to existing disclosures, including a broad set of policies and position statements, a set of Sustainable Development Goals (“SDGs”) to report on our impact and contribution to the SDGs and an ESG disclosures document to confirm compliance with EU SDFR particularly Article 8 and Article 9, as well as fund-level Green Impact Reports, which discloses our contribution to climate mitigation.

The Company endeavours to communicate progress as we expand our low-carbon businesses capabilities, develop our policy engagements, build on our climate risk management strategies, expand our core ESG metrics, and pursue engagements with investors, stakeholders and the wider solar industry in order to collectively address the climate challenge and promote the transition to a low-carbon economy.

### Introduction

The Company recognises that climate impacts should no longer be considered non-financial and has been an official supporter of the goals of the TCFD since September 2019. TCFD was established in 2015, with the aim of developing a comprehensive and uniform framework for climate reporting, enabling investors and other stakeholders to assess the companies’ climate-related financial risk. These risks may be categorised as follows:

- **Physical Risk:** These are risks related to the changes to the physical environment from the impacts of climate change in terms of intensity/frequency of extreme events (acute risks) and longer-term changes in climate (chronic risks)
- **Transition Risk:** Moving towards a low carbon economy will entail political, technological, legal, market and social changes

that can create risks and opportunities to existing businesses and their underlying revenue streams

The Company has been a leader within its sector for integrating considerations on climate throughout its organisation and within its decision-making processes. For the year ended 31 March 2022, the Company responded to the 11 recommendations set out by TCFD, with the ambition of continually expanding and evolving its implementation and reporting in line with TCFD recommendations into future reports.

### Governance

1. The Board oversees climate related risks and opportunities
2. The Investment Manager assesses and manages climate related risks and opportunities

### Board

Overall responsibility for NESF’s performance and management falls on the NESF board. Understanding climate risk management processes is critical to the Board. ESG matters are more important than ever to investors, stakeholders, and society. Tracking progress and reporting impact change throughout the NESF value chain is a crucial step in tackling climate change, driving accountability, and ultimately delivering a sustainable future for generations to come. Climate considerations and progress updates are discussed during ESG Committee meetings and quarterly meetings with the Investment Manager. During such meetings risks related to climate change are discussed.

### Investment Manager/Adviser

The Investment Manager and Investment Adviser realise that the integration of a climate and ESG strategy into NESF’s governance structures is imperative to effectively identify and manage potential risks. Under the leadership of NextEnergy Capital’s CEO, climate-related matters have been integrated into their corporate Sustainability Framework, which is based on three pillars - Climate Change, Biodiversity and Human Rights. Continuing this emphasis within business principles, the ESG team has developed a Climate Change Position Statement, which was

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first published in March 2021<sup>1</sup>. The Statement set the ambitions, the reference standards, and the practice that the Manager adopts when dealing with climate-related risks and opportunities. The Manager’s commitment to minimising both physical and transitional climatic risks is evident not only in the nature of the business as a leading solar investment manager, but also in the activities undertaken by the individual departments of the business. The CEO and senior management are the driving force behind the conception of NESF’s climate ambitions, while the Head of ESG is responsible for the strategy execution and for updating the Board and Investment Committee members on recent climate-related activities and progress. The Head of ESG is a member of the Group Risk Committee which meets quarterly. The risk register includes climate related risks and other ESG risks. The implementation of ESG and climate strategy is facilitated by a Sustainability Framework, which draws on SDGs as the structure by which risks are identified, managed, and reported across on a broad range of ESG issues that encompasses climate change and beyond.

NEC coordinates stewardship practices amongst senior management with an external collaborator. This partnership enables the Manager to have political influence over the climate-related policies, mandates and consultations that are most material to us. These include engaging with the UK Department for Business, Energy and Industrial Strategy (“BEIS”) on consultations such as UK carbon pricing. In addition, NEC has participated in panel sessions on the natural capital value of solar farms and has contributed to the Department for Environment, Food and Rural Affairs (“DEFRA”) consultation on biodiversity net gain. NEC are also a member of the Institutional Investor Group on Climate Change (“IIGCC”) and are currently participating in the Working Groups for the Paris Alignment Investment Initiative. The Head of ESG also sits on the board of Solar Energy UK (“SEUK”) and was recently appointed chair of the SEUK Supply Chain Working Group that is tasked with setting auditable ESG standards and a traceability programme for improving transparency and business ethics in the global solar supply

### Asset Manager

Climate risks are assessed during each pre-acquisition and development phase through a screening questionnaire. When potential risks are identified, the ESG team, together with the investment team and, where relevant, external advisers, undertake a further risk assessment and agree upon the necessary mitigation measures to manage and minimise the impacts. Usually, an action plan that includes these mitigation measures is put forward and presented to the Investment Committee for approval. The action plan is then negotiated with contractors, including Engineering, Procurement and Construction (“EPC”) and operations and maintenance (“O&M”), and then handed over to the asset manager of NESF, WiseEnergy. The asset manager oversees the implementation of these measures, including biodiversity management, land management, community engagement, and health and safety, amongst others. WiseEnergy report on any progress towards these plans on a regular basis and, in addition, will measure and manage several selected KPIs based on the SDGs and the EU SFDR and Taxonomy Regulatory Technical Standards which have been identified as material to NESF’s business and operations.

### Strategy

1. Describe the climate related risks and opportunities the organisation has identified over the short, medium and long term
2. Describe the impact of climate-related risks and opportunities on the organisation’s businesses, strategy and financial planning
3. Describe the resilience of the organisation’s strategy, taking into consideration different future climate scenarios, including a 2°C or lower scenario

The Company understands that climate change poses risks and opportunities across all stakeholders. Through its commitment to providing clean energy, the Company is well placed to help curb global carbon emissions. Conversely, there are risks associated with such a transition and the potential physical consequences associated with rising temperatures

The table below covers some of the key risks and opportunities faced over the short, medium and long term.

<sup>1</sup>[https://cdn.next1.nextenergycapital.com/next/2021/04/NEC\\_ClimateChange\\_Statement.pdf](https://cdn.next1.nextenergycapital.com/next/2021/04/NEC_ClimateChange_Statement.pdf)

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	Risks	Opportunities
Short-Term	<ul style="list-style-type: none"> <li>• Lower power prices due to over-deployment of renewables and cannibalisation</li> <li>• Saturated market and increased competition for investments leading to a reduction in financial returns of new projects</li> <li>• Increased temperatures reducing energy demand and driving down power prices</li> </ul>	<ul style="list-style-type: none"> <li>• Increased governmental support for renewables as nations aim to curb climate emissions in line with commitments made</li> <li>• Increased public support for decarbonisation increases the volume of ESG investing in public markets</li> <li>• Increased deployment of renewables drives the benefits and importance of battery storage assets</li> </ul>
Medium-Term	<ul style="list-style-type: none"> <li>• Extreme weather events (storms and flooding) causing physical damage to assets within portfolio</li> <li>• Increased temperatures reducing the efficiency and productivity of assets due to heat losses</li> <li>• Implementation of carbon pricing and taxation could impact companies within the supply chain, leading to price increases and reduced profitability</li> </ul>	<ul style="list-style-type: none"> <li>• Technological advancements driving down levelised cost of energy (LCOE)</li> <li>• Implementation of carbon pricing and taxation could help direct capital towards renewable technologies, such as solar and battery storage, and away from carbon-intensive sources</li> </ul>
Long-Term	<ul style="list-style-type: none"> <li>• Adverse changes in yearly irradiation averages and variances impacting the commercial viability of solar</li> <li>• New technologies leading to early obsolescence of solar assets</li> </ul>	<ul style="list-style-type: none"> <li>• As transport, industry and heating move away from fossil fuels and rely on electricity, demand increases could increase power prices</li> </ul>

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### Climate-Related Risks and Opportunities

#### Portfolio Investments

Productivity of a solar asset is a balance between maximising irradiation and minimising heat losses. As temperature increases, the efficiency of solar assets falls because heat stress impacts critical equipment, such as inverters and transformers. The consistent and relatively cool climate makes the UK a uniquely strong location for efficiency of solar assets. However, increased temperatures could lead to increased heat losses and inefficiency of the portfolio’s assets. Likewise, the Company’s portfolio of eight Italian assets and its co-investment in Spain could face similar challenges.

The Company’s asset manager, WiseEnergy, closely monitors the portfolio’s assets throughout the year, measuring metrics such as irradiation, generation, and availability. This enables the Company to identify assets at risk and implement mitigation strategies to limit heat loss in the future.

Increased greenhouse gas emissions are not simply associated with increased temperatures, but also with other extreme weather conditions, such as storms, flooding, and fires. All of NESF’s assets have been constructed with a 1 in a 100 year assessment of likely wind conditions for the specific location of construction. One of the key benefits of the portfolio of distributed energy assets that NESF has its resilience to any localised issues. As a result of recent UK weather events (storms Arwen, Dudley and Eunice), the ESG team aims to engage with an external expert to carry out a high-level climate risk screening for the entire portfolio of UK assets to be better prepared against any future physical climate risks.

#### Strategy

The political and social climate is currently very supportive of climate change action, of which the deployment of solar and other renewable assets is an essential part. Subsequently, there are significant capital flows being directed towards sustainable investments and the deployment of green infrastructure. There is strong evidence to suggest this trend is likely to continue. Indeed, at the UN Climate Change Conference (COP26) in October 2021, the Glasgow Financial Alliance for Net Zero (“GFANZ”) stated that the financial sector commitments to net zero over the next three decades will exceed \$130 trillion.

Alongside the opportunities this brings, there are also some risks. High levels of investment lead to increased competition and, subsequently, acquisition costs of assets can be driven up and lead to a reduction in returns. The Company has seen this within the UK market over recent years. The Company has been able to draw upon the expertise of the investment manager to diversify its portfolio

into new jurisdictions as well as assets classes (such as construction and development assets), in line with the Company’s investment limits.

#### Financial Planning

There are some key challenges to the Company in relation to finances and cash flows because of climate change. The wholesale market price of electricity is affected by several factors, including demand, subsidies, fuel commodity prices and foreign exchange. As renewables become a greater proportion of the energy mix, the volatility in the availability of these renewable resources is expected to drive volatility in power prices and, subsequently, distributions to the fund and its shareholders. Increased concentration of solar assets also leads to cannibalisation, and the price captured on the market by solar is eroded over time.

The Company’s hedging strategy aims to eliminate these risks associated with power price volatility. Some of the Company’s investments benefit from subsidies and short-term PPA hedges that fix prices, with the remaining revenue streams subject to wholesale electricity prices. The Company has agreed fixed UK pricing (hedged) covering 85% of budgeted generation for the 2022/23 financial year and 74% of budgeted generation for the 2023/24 financial year.

By contrast, this volatility could provide a significant opportunity to battery storage assets, which generate returns through such volatility. Optimising through its arbitrage involves charging the battery when energy prices are low and discharging during more expensive peak hours. The Company’s investment objective allows investment in standalone energy storage systems (not ancillary to or co-located with solar PV assets owned by the Company) up to an aggregate limit of 10% of the Gross Asset Value. In September 2021, NESF entered the standalone battery storage space by agreeing a £100m Joint Venture Partnership (“JVP”) with Eelpower Limited, a leading battery storage specialist in the UK. The JVP includes a framework for acquisitions up to 250MW, providing ample opportunities to offer complimentary revenue streams to our existing portfolio of solar assets.

The Intergovernmental Panel on Climate Change (“IPCC”) use Representative Concentration Pathways (“RCPs”) as a basis for modelling future consequences of anthropogenic greenhouse gas emissions and reflect a wide range of possible outcomes. There are 4 key scenarios: RCP2.6, RCP 4.5, RCP6 and RCP8.5. The four scenarios are outlined in the table below.

Scenarios RCP2.6 and RCP4.5 refer to pathways whereby significant efforts are made to reduce anthropogenic climate change. These scenarios assume greater deployment of

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renewable energy and subsequently pose greater transition risks to businesses. As previously mentioned, this is associated with greater power price volatility and cannibalisation as solar (and other renewable technologies) becomes a greater proportion of the energy mix. However, as industries (such as transport) move away from fossil fuels and towards electrification, the subsequent demand increase is expected to offset such changes to the supply.

The Company’s Net Asset Value (“NAV”) sensitivity analysis shows that a 10% decrease in power prices lead to a 6.6% decrease in the NAV and a 10% increase in power prices lead to a 6.3% increase in the NAV.

Alongside increased support for green investment, another key part of the RCP2.6 and RCP4.5 scenarios likely involve increased regulations aimed at actively mitigating CO2 emissions. These include carbon pricing that will impact organisations in countries that take part in emissions trading schemes or are subject to emissions taxes. The purpose of such strategies is to charge the hidden cost of carbon emissions to the source. It is expected that in low emissions scenarios, prices in existing emissions trading schemes are likely to increase. Whilst this could improve the commercial viability of renewable technologies, it may simultaneously drive-up costs within the supply chain of solar infrastructure assets.

By contrast, under scenarios where limited efforts are made to reduce emissions (RCP6 and RCP8.5), global temperature increases are significantly higher than 2°C. This leads to several physical risk factors, such as extreme weather conditions, floods and heat stress. Storms may put solar assets at risk of physical damage that could drive up operational costs and lead to losses in generation due to periods of repair. The existing portfolio of assets has a weighted average expected life of 27.3 and are designed to be extremely resilient to different weather conditions. There is also insurance in place to cover physical damage to plants that may lead to large financial and environmental losses.

Furthermore, higher emissions scenarios are expected to both increase average temperatures and the variance in irradiation. As previously mentioned, increased temperatures reduce the efficiency and productivity of assets due to heat losses and higher volatility in irradiation directly impacts the volatility of the company’s revenues. Our NAV sensitivity analysis shows that a 5% decrease in irradiation leads to an 6.3% decrease in the NAV and a 5% increase in irradiation lead to a 6% increase in the NAV.

Radiative Forcing	Atmospheric CO2 equivalent (parts per million)	Description
8.5	>1,370	Worst-case emissions scenario, whereby no effort is made to curb climate change and emissions continue to rise throughout the 21st century
6	850	Emissions peak around 2080, then decline
4.5	650	Emissions in RCP 4.5 peak around 2040, then decline
2.6	490	Ambitious pathway, whereby emissions go to zero by 2100

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### Risk Management

1. Describe the organisation’s processes for identifying and assessing climate-related risk
2. Describe the organisation’s processes for managing climate-related risks
3. Describe how processes for identifying, assessing, and managing climate related risks are integrated into the organisation’s overall risk management

The core business of the investment manager of NESF is focused on generating positive climate-related impacts through the reduction of carbon emissions associated with the clean energy generated by the renewable energy assets. Despite no direct exposure to carbon-intensive sectors, the investment manager has identified certain physical climate risks as material to the business. NEC has reviewed the Company’s risk appetite to reflect its climate ambitions that has been expressed to stakeholders and have aligned it with NEC’s group-wide Risk Management framework. The Company will continue to refine its climate risk assessment approach in order to reflect the constantly evolving nature of climate factors and impacts.

Potential physical climatic risks associated with the asset acquired or developed after 2020, are screened by the ESG team, and where there is evidence of potential risks, an external climate risk advisor is appointed for further assessment during the pre-acquisition stage. The advisor will provide a climate change risk assessment report, which will inform final investment decision. As a member of both the NEC Group Risk Committee and the NESF Investment Committee, during Committee meetings the Head of ESG is responsible for advising on the ESG risks and

opportunities associated with each acquisition and or development, including those related to climate.

### Risk Factors and Risk Assessment

The level of risk assigned to an investment is determined by investigating and engaging with involved parties over a wide range of factors throughout the due diligence process. While the risk level varies depending on the asset being acquired, certain risk factors can be more easily mitigated than others and as such are classified with a lower risk rating due to their ability to be more readily managed.

The Investment Manager’s ESG team have worked with an external consultant to develop an internal climate risk rating system that is aligned with the TCFD guidelines. It is expected that this will be implemented by Q4 2022. Carrying out this procedure enables the ESG team to highlight the severity of any climate-related risks associated with the portfolio during the acquisition process, and to determine which assets will require a third-party assessment to be carried out post-acquisition. Based on the findings of the assessment, it is expected that mitigation measures will be presented by the advisor and passed onto the asset manager, ensuring the risk is monitored and reported on for as long as required and where relevant, for the entire lifetime of the Project

General classification	Physical risks	Possible consequences	Risk rating
Acute	Increased severity and frequency of extreme weather events (hurricanes, storm surge, heat waves)	Damage to property and infrastructure resulting in environmental damage, increased capital costs (e.g. repairs, cleaning, write-offs and possible early retirement of assets), decreased power generation, worker incidents (e.g. unable to access site).	Medium (Likely + Moderate)
	Fires		Low (Unlikely + Minimal)
	Flooding		Low (Likely + Minimal)
Chronic	Changes in precipitation patterns, solar irradiation and cloudiness	Reduction of anticipated power generation, increased losses in transmission lines, increased costs associated with more frequent or intense cleaning requirements and an increase in health and safety incidents as a result of increased changed weather conditions (e.g. heat stress associated with hot days)	Low (Likely + Minimal)
	Changes in dirt, dust, snow, atmospheric particles and others		Low (Likely + Minimal)
	Changes in mean temperatures		Low (Likely + Minimal)
	Water stress and drought		Low (Unlikely + Minimal)

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### Metrics and Targets

1. Disclose the metrics used by the organisation to assess climate related risks and opportunities
2. Disclose Scope 1, Scope 2, and if appropriate, Scope 3 greenhouse gas emissions, and the related risks
3. Describe the targets used by the organisation to manage climate related risks and opportunities and performance against targets

We recognise the value in considering ESG metrics when identifying potential investment risk or opportunities. In terms of NESF’s asset emissions, the Greenhouse Gas (GHG) Protocol has outlined the most effective framework for reporting on carbon emissions. The framework separates emissions into the following categories:

- Scope 1: Direct emissions from the activities of a company under its control, includes fuel company-owned vehicles and air-conditioning leaks.
- Scope 2: Indirect emissions from purchase of electricity, steam heating and cooling by the company.
- Scope 3: All other indirect emissions that are embedded within the Company’s value chain.

NESF and its fund manager aim to obtain the GHG emission data directly from suppliers, although it is anticipated that this process will take time. Until then, NESF has commissioned the Green Investment Group to estimate the Scope 1 and 2 GHG emissions associated with the Company’s solar assets.

The Company estimated GHG emissions are 37.6CO<sub>2</sub>e/yr for the year ended 31 March 2022 and aims to incorporate measured scope 3 emissions into its reporting in due course.

### Targets

The Science Based Targets initiative (“SBTi”) was established in 2015, with the goal of helping companies to set emission reduction targets in line with climate science and Paris Agreement goals. The Company is in the process of evaluating its targets commitments.

### Outlook

The Company is aware of the potential for the effective management of climate risks and opportunities to impact returns and has therefore identified a few areas to expand on its current TCFD disclosures in the future. The Company is aiming to introduce a comprehensive scenario analysis that will help quantify climate risks faced over time. This analysis will involve projections of irradiation levels and power prices under two different emissions pathways, one with high physical risk (e.g. RCP 8.5) and another with high transition risk (e.g. RCP 2.6). This deeper analysis would provide greater clarity on the potential revenue impacts across different outcomes.

The Green Investment Group has been instrumental in providing metrics for the Companies reports and disclosures, including as scope 1 and 2 emissions as well as the number of homes powered through the Company’s electricity generated. The Company therefore intends to expand its metrics to include scope 3 emissions, which will give clarity on upstream and downstream emissions within its value chain. Once identified, the Investment Manager can begin engaging with its suppliers in order to take action to reduce such emissions from its suppliers. The emissions calculated may then be used as a baseline for future performance and will be used to inform its SBTi-aligned targets. The Company is continuously striving to improve on its disclosures and processes to ensure risks are effectively identified and, where possible, mitigated