

# Title: Nature Finance

**Date:** **13 March 2024**

| **Purpose:** | For information and to receive the Board’s advice and assurance. |
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| **How does this link with our corporate priorities of improving biodiversity or delivering nature-based solutions to climate change:** | The paper provides an overview of our delivery plan which is contributing towards the Corporate Plan objective: **Influence the regulatory, policy, market and institutional infrastructure needed to stimulate private sector investment into nature**. |
| **Summary:** | This paper summarises the roles we are playing, governance proposals and current activity. |
| **Actions:** | The Board is invited to discuss, and provide assurance on, governance, risks, positioning and progress. |
| **Recommendations:** | n/a |
| **Report Author(s):** | John Uttley, Graham Neville |
| **Sponsor:** | Robbie Kernahan |
| **Appendices**: Please note all appendices. | Annex 1 Expanded details on work programme  Annex 2 Audit recommendations and responses |

## Purpose

This paper is a scheduled update to the NatureScot Board on important work to stimulate private sector investment into nature.

**Introduction**

1. Nature Finance is a very fast growing and evolving field arising from the growing recognition that public funding and philanthropic funding is insufficient to pay for the vast investment in nature that is needed to mitigate climate change and loss of biodiversity – the twin crises. The focus is on bringing in new investment from private sources.

**Context**

1. The two primary public sector drivers of Nature Finance in Scotland are:

* The National Strategy for Economic Transformation, which commits to establishing a values-led, high-integrity market for responsible private investment in natural capital to build on Scotland’s international renown for its nature and its environmental policy framework on land and sea, supported by a national project pipeline for nature-based solutions. Scottish Government, with NatureScot and the Scottish Land Commission have established the Private Investment in Natural Capital (PINC) programme.
* The Scottish Biodiversity Strategy, which calls for increased investment in biodiversity and nature restoration including the development of mechanisms for responsible private investment in biodiversity. A key action is to develop a Biodiversity Investment Plan which supports delivery of the Strategy through public, private, third sector and philanthropic investment. It has very close links with the Market Framework.

**Role**

1. NatureScot is playing several different roles in the Nature Finance space.

* Growing the pipeline of investible projects
* Growing the capability of project developers to engage with new Nature Finance
* Co-developing policy on Nature Finance with Scottish Government
* Influencing private investment in nature

1. There is a potential need for a service that identifies priorities and opportunities, especially in terms of landscapes that require restoration and can create significant public benefits. An example of this, from England, is the [West of England Nature Recovery Prospectus.](https://wenp.org.uk/wp-content/uploads/2022/07/NRN-Prospectus_July-2022.pdf)

**NatureScot Activity**

1. In line with the four roles identified above, the majority of NatureScot’s resources are focussed on six big pieces of work, three within the PINC programme, two in partnership with the private sector and another in a cross public sector initiative. [Annex 1](#Annex1) presents further detail on these.

* PINC – Natural Capital Market Framework
* PINC – Facility for Investment Ready Nature in Scotland (FIRNS) – [funded projects](https://www.nature.scot/doc/firns-facility-investment-ready-nature-scotland-successful-round-1-projects)
* PINC & Peatland Programme – Peatland Private Finance workstream – including the Flow Country Green Finance Initiative
* MoU with Hampden & Co, Palladium and Lombard Odier  - the Wild Heart Expansion Project
* CivTech/CreditNature – Developing Nature (Biodiversity) Credits
* Scottish Marine Environment Enhancement Fund

1. The landscape of Nature Finance is complex and full of uncertainty. Much of our effort is on creating more certainty and this requires painstaking collaborative work with government and both supply and demand side actors. At the same time, we are pushing ahead with projects that aim to develop good practice and demonstrate success. This requires a combination of patience, care and urgency as set out in the risk statement below.

**Governance**

1. NatureScot’s activity in the Nature Finance arena was audited in 2022 by Azets, reporting in 2023. The audit made 15 recommendations to help better implement good governance and risk management. Proposals to implement these recommendations were presented to the Audit and Risk Management Committee in February, alongside suggested changes to the risk statement (below). The Committee were supportive of the proposals and requested reporting implementation of these to the Board. [Annex 2](#Annex2) provides an overview of those recommendations including a revised risk statement, taking account of ARC feedback.

**Risk statement**

1. As a result of any or all of poor governance; lack of due diligence; or poor communications, NatureScot’s reputation could be significantly damaged by misjudged or poorly delivered interventions to influence private investment in nature. There is also a risk that, if we do not proceed with the urgency required to stimulate private sector investment into nature, that significant nature restoration will be unachievable. There is therefore a balance of acting with due diligence, versus not acting at all. There are also specific risks attributed to individual projects or partnerships which are dealt with at the project level.
2. These opposing risks suggest a balanced risk appetite is appropriate. It would be helpful if the Board could confirm that within this balance, the risk of some managed and mitigated failures and communications challenges is outweighed by the risk of not acting – this was largely the steer from the Audit and Risk Committee.
3. There are also specific risks attributed to individual projects or partnerships which are dealt with at the project level.

**Recommendations**

1. The ask of the Board is to reflect and advise on:

* The roles that NatureScot is fulfilling, and other roles that could be a priority for us
* The programme of work and progress on the Corporate Plan objective
* The governance arrangements proposed and the appetite for risk.

**Annex 1. Current Nature Finance activity in NatureScot**

1. **Private Investment in Natural Capital (PINC) programme**

NatureScot is represented on the Programme Board (Robbie Kernahan) and Team John Uttley)

1. **PINC - Natural Capital Market Framework**

The proposed aim is to guide market development with clear long-term policy ambition and a coherent policy framework for the development of responsible, high-integrity and values-led natural capital markets in Scotland.

Its draft objectives are to:

* provide guidance to those seeking to enhance Scotland's Natural Capital via private investment
* strengthen Scotland’s interim principles for responsible investment by clarifying expectations, including requirements for community engagement and benefit
* steer Market Governance by setting out expectations for:
* participant eligibility and buyer integrity
* data requirements for all nature-based standards
* accounting requirements for all nature-based standards
* alignment with UK and international frameworks, certification and standards
* set out expectations and actions for alignment with other policy contexts e.g. blended finance, biodiversity, agriculture, land reform, nature recovery
* describe actions to develop a pipeline of investable projects in Scotland
* set out the economic benefits from private investment in natural capital

1. **PINC - Facility for Investment Ready Nature in Scotland (FIRNS)**

FIRNS is delivered by NatureScot on behalf of Scottish Government and jointly with the National Lottery Heritage Fund, with a total value of £6m. It fosters innovation and learning in Nature Finance.

The overall aims and ambitions of the FIRNS programme are to support the development of the pipeline of nature-based projects:

* achieving or enabling the outcomes of Scottish government’s [Interim Principles for Responsible Investment in Natural Capital](https://www.gov.scot/publications/interim-principles-for-responsible-investment-in-natural-capital/)
* enabling swifter, easier and scaled up development of further nature-based investable projects across Scotland,
* valuing and monetising ecosystem services derived from the restoration of natural capital assets, in a model that will attract and repay investment or support an investment model that can be scaled up and duplicated elsewhere.
* helping grow natural capital markets that reach across rural, urban and marine settings, as well as a wide variety of natural assets and ecosystem services,
* creating or supporting the creation of new market infrastructures that would increase the transparency and efficiency of natural capital markets and enables their scope to grow beyond carbon sequestration in woodland and peatland.

Twenty-seven projects are already in progress and a further 14 are under consideration for funding in Round 2 from April 2025. The funding runs until March 2025. FIRNS includes a Community of Practice (CoP), run for NatureScot by Social Investment Scotland. The COP is how FIRNS becomes more than the sum of its parts. It will play a crucial role in building the capacity of FIRNS grantees to deliver their projects and ensuring that lessons learned are shared, both within the cohort of projects and beyond. It will also function as a source of information for Scottish Government and NatureScot to understand challenges, gaps, and policy requirements.

1. **PINC - Peatland Private Finance Workstream**

This a joint workstream with the Peatland Programme. It seeks to increase levels of private finance into peatland restoration through the development of blended finance approaches, which are defined as any combination of public and private funding for the same project.

The policy intent of implementing blended finance approaches for peatland restoration is to maximise the value of public spending and support increased restoration activity by “crowding-in” responsible private investment.

By the end of the financial year 2024-2025, this workstream will have:

* Achieved a better understanding of the existing private finance market for peatland restoration, emerging actors, and their current approaches
* Developed a serious, professional and consistent relationship management approach across the Scottish public sector in its approach to peatland private finance
* Reviewed and determined what proposed blended finance solutions are viable and appropriate options for peatland restoration in Scotland, including undertaking an economic appraisal of these options
* Established a clear strategy for bringing forward blended finance approaches in Scotland
* Assessed whether and how to make any blended finance schemes permanent and developed an understanding of how long each potential scheme would take to develop and reach maturity

The outputs of this workstream will act as a case study in the development of blended finance models to address investment issues in natural capital.

In parallel we are working on the **Flow Country Green Finance Initiative**.

NatureScot, alongside partners in the public, third sector and eNGO sectors, leads the Flow Country Green Finance initiative. This work seeks to use the prospective World Heritage Site listing for the Flow Country as a catalyst to drive an increase in peatland restoration using a blended public/ private finance approach. It is strongly linked to the principles of community benefit and a Just Transition for the region. The project has formalised the Flow Country Partnership into a Scottish Charitable Incorporated Organisation which will lead efforts to aggregate restoration projects at the landscape scale, and from the income received from carbon credit sales, derive community benefit by attracting price premiums from the charismatic carbon approach. The project is also linked to skills development via the project’s academic partner, the Environment Research Institute of UHI. The Flow Country work is in receipt of both Investment Ready Nature Scotland (IRNS) funding to set up the governance structure and FIRNS funding which allows investment into 3 pilot proof of concept projects.

1. **MoU with Hampden & Co, Palladium & Lombard Odier**

NatureScot signed an MoU with Hampden and Co, Lombard Odier and Palladium in March 2023.  The MoU states our intention to work together to find new ways to invest around £2 billion of private capital in nature restoration in Scotland. Our role is to ensure the partnership delivers high integrity investment, delivering the aims of the [Interim Principles for Responsible Investment in Nature Capital](https://www.gov.scot/publications/interim-principles-for-responsible-investment-in-natural-capital/), and to secure public funding to facilitate investment as needed.

* We have completed a scoping study for the first pilot project in the Borders, now called the [Wild Heart](https://bordersforesttrust.org/wild-heart) Expansion Project to restore up to 15,000 hectares of native woodland.  We are working with local partners Tweed Forum, Borders Forest Trust and Southern Uplands Partnership.
* The design phase will commence soon
* We continue to explore a second pilot in the Rainforest and other locations in Scotland.
* An Advisory Board will oversee the project

1. **CreditNature**

NatureScot, with Scottish Government and SEPA, is supporting [CreditNature](https://creditnature.com/), via CivTech, to develop an option for a new voluntary biodiversity market in Scotland that we believe has strong potential to help scale responsible private investment into nature restoration in Scotland. CreditNature’s approach involves issuing nature credits, backed by a robust metric framework that assesses ecosystem integrity and the impact of land management systems. The credits are hosted on blockchain technology, providing, efficiency, transparency, immutability and security amongst other benefits. They are a utility that entitles the owner to various benefits, including rights to report.

1. **Scottish Marine Environmental Enhancement Initiative (SMEEF)**

SMEEF is a marine nature finance tool founded in association with the offshore energy sector and managed by a partnership of NatureScot, Crown Estate Scotland and Marine Directorate. It aims to create a long-term, substantial fund to support Scottish marine enhancement, facilitating donations from business and recirculating these as grants. Since inception SMEEF has allocated more than £3.3m of NRF funding and raised almost £500,000 from private sources. The signing of a contract with SSEN Distribution (due 26.02.24) will see £2.1m donated for the planting of 14ha of seagrass over the next 3-4 years. The team is also negotiating a group agreement with circa 10 companies to fund a £2.5m seabird resilience fund (2024-28). Work continues to ensure flexible finance is brought in to cover the following priority areas:

* Seabed enhancement – to encompass seagrass, native oysters and other seabed species and habitats
* Coastal enhancement – to encompass saltmarsh, sand dunes and other coastal species and habitats
* Marine (ocean) enhancement – all mobile species work and deeper seas
* Seabirds – all work aiming to benefit seabirds
* Research – matching donors with specific research topics

**Annex 2: G****overnance and risk management**

**Azets audit recommendations and implementation proposal**

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| **Audit Recommendation** | **Proposal/ comment** | **Owner** |
| 1. Document initiatives already in place | Refresh, and regularly update the Nature Finance Initiative Tracker with more detail as a single repository of projects/ partnerships and opportunity scoping underway. | Delivery Plan lead |
| 1. Building on initial list, extend to scope and map the work | As above | Nature Finance team |
| 1. Create Communications Plan | A Communications Plan has been created. This will be kept live, and refreshed on acceptance of the risk management controls detailed in this deep dive. | Head of Communications / Delivery Plan lead |
| 1. Create and agree risk appetite statement for work on Nature Finance | Following ARC meeting (8th February) a revised overarching Corporate Risk has been created. This is in the Business Planning system with the risk owner (Objective lead) updating as part of Quarterly reporting. | Programme Board |
| 1. Review risk appetite on annual basis | The Risk Appetite statement to be reviewed as part of updating the Delivery Plan during business planning process in Q4 each year. | Programme Board |
| 1. Create risk register for all agreements/ Projects | In hand, but needs centrally held in the Business Planning system under a project for each Partnership. (e.g. Hampdens one is a document rather than a project risk in Programme Governance documentation or on Business Planning – this is now being transferred to Business Planning). | Delivery Plan lead and individual project leads |
| 1. Provide regular assurance to Board on agreements in place and under development | Through quarterly reporting to Programme Board. | Delivery Plan lead |
| 1. Mechanism in place to oversee governance of Nature Finance partnerships | A Programme Board will have oversight of delivery of the Corporate Plan objective and manage risk. The programme board will meet quarterly, aligned to 90 day BP reporting cycles The board consists of:  SRO: Robbie Kernahan, Director Green Economy  Objective lead/ Programme Manager (delivery plan): Graham Neville  External challenge function: Helen McGeorge (head of Audit) (until external agreed)  Senior Supplier: John Uttley (Principal Advisor)  Senior Users: Ross Lilley/ Kerry Wallace | Programme Board |
| 1. Provide assurances on the management of delivery of projects and risk mitigation | 6 monthly update to ARC on delivery of the programme/ projects to keep ARC sighted on this area of work. | SRO |
| 1. Agree SMART KPIs for the Hampden & Co. Partnership tied back to MOU. | Programme Board to sign off on KPIs as part of a refresh of the documentation around the Hampden & Co. partnership – January | Project lead |
| 1. Consider SMART KPIs for all partnerships/ projects | Framework of project/ partnership documentation to be in place before commencement including Due Diligence/ Responsible investment screening, KPIs, risk register and to be signed off at Programme Board before each project or partnership is initiated. | Individual project leads |
| 1. SMART KPIs to form part of reporting and governance arrangements | KPI performance appraisal to be part of Highlight report to Programme Board | Delivery Plan lead |
| 1. Review Gap Analysis and Resourcing Plan provided by AchieveGood to determine future recruitment need and develop skills matrix | There are several strands to this. In the immediate term, the resource available to provide management of the current workload and priorities has been increased with a reshaping of the delivery plan lead role and Principal Adviser role. Beyond this, a first action is to complete the matrix with the current resource in place. Further development of this would lie with the OD skills work and the POD Business partner for the objective in assessing future skill requirement – and putting in place the strategic workforce plan to achieve them. Strategic Workforce Planning is an action in hand in the People Strategy. | Delivery Plan lead |
| 1. Review recruitment and skills matrix on an ongoing basis | Annual review of the matrix and skill/workforce plan as part of annual business planning cycle. | Delivery Plan lead |
| 1. Identify skills required and capacity available vs required for new partnerships/projects | As part of formal assessment of project opportunities we will assess skills and capacity before making a recommendation whether to take forward a new initiative. | Nature Finance team |