

Sustainable Criteria for Residential Projects and the Role of Government

Introduction

Current challenges

CMHC has the aspirational goal of ensuring every household in Canada has a home that they can afford and that meets their needs. To achieve this goal, CMHC works with other participants such as housing proponents (e.g. provincial/municipal governments, housing associations), developers and investors to meet two main challenges facing the housing industry in Canada.

- **A funding gap for affordable housing.** Some studies estimate a gap ranging from \$77 billion to \$120 billion,¹ representing more than three million units per year starting in 2016 for the following decade. This gap is strongly influenced by the need for resources to: replace or renovate the existing social housing stock; assist Canadians in core housing need; minimize waiting lists for subsidized housing; and increase the supply of social and affordable housing. Furthermore, COVID-19 has made housing even more challenging, particularly for those most vulnerable and households with the lowest level of income.

- **The environmental impact of the housing sector on climate change.** Among all sectors in Canada, the residential housing sector consumes the most energy (23.8%) and contributes significantly to greenhouse gas (GHG) emissions (18.8%).² This includes building, retrofitting and renovating, as well as consumption by dwellers. As the effects of climate change become more disruptive, the effect of the housing sector on the environment will inevitably become more relevant.

CMHC research project

To address these challenges, CMHC undertook a study of sustainable mortgage bonds (SMBs) and their potential implications for the housing industry in Canada. Our objectives were as follows: explain the opportunities presented by SMBs; raise awareness of their positive environmental, social and economic impacts; and explore the potential role of government in bringing about these positive outcomes.

CMHC conducted internal research and commissioned the services of a global professional services firm. The firm conducted literature reviews, econometric analysis and a series of consultations with key industry players.

¹ HPC Housing Investment Corporation. "HPC Housing Investment Corporation: Background." <https://www.housinginvestment.ca/background>

² Statistics Canada, "Canadian System of Environmental-Economic Accounts", September 2019.

About CMHC Research Insights

Research insights are summaries of our research reports.

These insights:

- identify a housing research issue, gap or need
- provide an overview of the research project undertaken to address it
- present major findings of the research

The research presented in this series explore the areas of Housing Need, Housing Finance, Housing Supply and Outcomes of the National Housing Strategy.

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Reporting on this project

Our objectives in this last research insight on SMBs are to:

- summarize the high-level ESG (environmental, social and governance) eligibility criteria that could be considered by developers and housing proponents;
- identify the potential outcomes that could be expected in Canada's housing industry; and
- underline the role that the Government of Canada could play in directly or indirectly supporting the ESG bond market and materializing sustainable goals.

Articles in this series:

- Sustainable Mortgage Bonds – Why are they so relevant to the housing industry in Canada?
- Sustainable Mortgage Bonds – Expected performance, investors' motivations and econometric analysis.
- **Sustainable criteria for residential projects and role of government.**

ESG measures used by global leading frameworks in the housing sector

In our previous article, we selected Fannie Mae and NWB Bank frameworks for a deeper analysis to learn about potential solutions to address the funding gap and environmental issues related to the housing market in Canada (see *Sustainable Mortgage Bonds—Why are they so relevant to the housing industry in Canada?*). The analysis of these two frameworks showed that aligning criteria with desired social and environmental outcomes has been observed to have positive impacts on greenhouse gas (GHG) emissions, energy/water savings, the supply of affordable housing, and people who are vulnerable, as well as economic benefits (e.g., economic activity, employment creation).

Table 1: Fannie Mae and NWB Bank green and social bonds key measures and outcomes

Framework	Description/Volumes	Green/Social Measures & Outcomes
Fannie Mae Multifamily Green Bond Framework	Fannie Mae is the world's largest issuer of green bonds. Total issuances of US\$69.1 billion through its green bond program between 2012 and 2019.	<ul style="list-style-type: none"> • GHG emissions: 2018 annual savings of over 280,000 metric tons of CO₂ emissions (social cost savings of about \$15 million per year). • Energy savings: 4.3 billion kBtu in 2018 (amount of energy used by over 34,000 American homes in one year). • Water reductions: 22.3 billion litres (amount of water used by nearly 54,000 American families in one year). • Employment: Creation of 170,000 jobs, addition of US\$14.6 billion to GDP economic output, representing US\$105 million in annual savings for owners and tenants.
NWB Bank Housing Bond Framework	NWB Bank is one of the world's largest issuers of social/sustainable bonds. Total issuances of EUR 6.7 billion from 2017 to 2019.	<ul style="list-style-type: none"> • Affordable housing units: In 2019, housing associations managed approximately 2.4 million residential units, delivered 15,000 new affordable homes and provided shelter for roughly 60% of the Netherlands' population. • Evictions: 19% y/y decrease in 2018 and showing a steady decline. • Populations experiencing vulnerabilities: 98% of total annual social housing allocations went to the target groups. • Rent levels: Monthly affordable rents performing well below the EUR 710 rent cap.

Source: CMHC, Deloitte LLP (Canada)

Alignment with the National Housing Strategy

To assist with closing the affordable housing gap and with the climate change challenge, issuers can consider aligning their ESG eligibility criteria with those policy objectives laid out under Canada's National Housing Strategy (NHS). The NHS³ promotes sustainable outcomes in the housing market by developing or improving affordable and community housing and supporting environmental objectives through water and energy savings:

Table 2: High-level summary of key NHS green and social policy objectives

NHS Green Policy Objectives	NHS Social Policy Objectives
To support energy- and water-efficiency retrofits to existing community housing.	To create new units of affordable and community housing and shelter spaces, particularly for people who are vulnerable, such as victims of family violence, seniors, people with disabilities, Indigenous peoples, veterans, recent immigrants, etc.
To renovate and repair buildings or housing developments to reduce energy consumption and GHG emissions.	To protect, maintain, and repair existing affordable housing, community housing and shelter spaces to support groups that are vulnerable, particularly those in core housing need.

Source: NHS, Deloitte LLP (Canada)

³ Canada Mortgage and Housing Corporation, National Housing Strategy: <https://www.cmhc-schl.gc.ca/en/nhs/guidepage-strategy>



ESG suggested eligibility criteria for residential properties in Canada

Green criteria for residential properties

The green criteria could be adapted to new developments and to the retrofit of existing units, including both residential multi-unit projects and homeowner properties. The criteria can consider a gradual improvement in outcomes and can consider measurements targeting the construction phase (through building certifications) and the operation phase (through energy and water consumption savings), such as:

Green Building Certifications	Energy/Water Consumption Savings
<ul style="list-style-type: none"> • Use of reliable green building certifications in Canada to identify those potential housing projects that could be eligible under a SMB framework. • Leading green ESG frameworks, such as Fannie Mae’s Multifamily Green Bond Program have actively used green building certifications in eligibility criteria. • In Canada, there are clear examples of such certifications:⁴ the EnerGuide label, Energy Star, LEED certification, Green Globes certification etc. • The green eligibility criteria could be structured to allow a combination of certifications that could be selected by developers or housing proponents based on location, activities and overall suitability to investors, particularly to facilitate reporting. 	<ul style="list-style-type: none"> • Based on the NHS strategy: <ul style="list-style-type: none"> – New units: can aim at a 25% reduction in energy consumption and GHG emissions over national building and energy codes. – Renewed/repaired units: can follow a similar target of a 25% reduction in energy consumption and GHG emissions (relative to previous performance). • Setting reasonable energy/water targets in close communication with lenders and housing proponents would be relevant for issuers to achieve a balance between volumes and eligibility criteria. Targets could be gradually escalated to achieve higher energy improvements in the long term. • While there is not a specific NHS target for water reduction, housing projects pursuing water savings would be of interest to investors, since these are aligned with United Nations Sustainable Development Goal 6 (refer to <i>Sustainable Mortgage Bonds—Why are they so relevant to the housing industry in Canada?</i>).

Source: CMHC, Deloitte LLP (Canada)

⁴ Green certifications have been sourced from: (i) NRCAN, *EnerGuide in Canada*, Accessed Nov.9, 2020: <https://www.nrcan.gc.ca/energy-efficiency/energuide/12523>; (ii) NRCAN, *Guide to ENERGY STAR Certified Homes*, Accessed July 16, 2020: <https://www.nrcan.gc.ca/energy-efficiency/energy-star-canada/energy-star-new-homes/guide-energy-star-certified-homes/12348>; (iii) USGBC, *LEED Certification for Residential*, Accessed July 15, 2020: <https://www.usgbc.org/leed/rating-systems/residential>; (iv) Green Globes, *What is Green Globes?*, Accessed July 15, 2020: <http://www.greenglobes.com/v3/interiors/about.asp>

Social criteria for residential properties

To more effectively impact the supply of affordable housing, social criteria could target groups and individuals experiencing vulnerability who are living in multi-unit (new or existing) properties. This relatively new area represents an opportunity to promote equity and diversity in meeting housing needs in Canada.

Affordability	Populations Experiencing Vulnerability
<ul style="list-style-type: none"> • Affordability could be defined differently depending on location, project type, household characteristics and population subgroup. The definition of affordability could also vary based on segmented income levels for target populations. • As such, the eligibility criteria should be adaptable to ensure a common understanding among different stakeholders (i.e. investors, developers, housing proponents) about plausible variations in definitions and overlapping targets. • The criteria could initially be based on existing affordable housing programs, to be further developed as more experience is gained in this field: <ul style="list-style-type: none"> – For example, CMHC’s Mortgage Loan Insurance Program (Affordable Flex product) has criteria for both new and existing units based on a minimum number of affordable rental units and rent caps. – There are other affordability definitions approved or aligned under existing federal, provincial or municipal programs that could be considered.⁵ • The criteria need to be supported by a standardized methodology to facilitate monitoring, analysis and reporting. This has been highlighted in our research. 	<ul style="list-style-type: none"> • Multi-unit projects could include a portion of units targeted to those most in need. • Those most in need, defined locally at the provincial and municipal levels, could be targeted based on a combination of low income and the NHS’s target populations, such as Indigenous people, people with disabilities, single mothers, seniors, refugees, etc. • The criteria should continuously evolve to align the supply of housing with the changing needs of the housing sector due to economic or social changes or unexpected events. For example, criteria could be added to help those low-income populations most impacted by COVID-19 and other types of health, climate, and financial disasters. • To align with the social inclusion objectives identified in the NHS, eligible multi-unit buildings can mix shelter types (affordable and market units), targeting both the broader market and populations experiencing vulnerability. • Targets could be set based on the number of people experiencing vulnerabilities associated with housing. This approach has been used by the City of Toronto Social Bond Framework. The target groups under ESG frameworks could be defined together with other local-level authorities to adjust to local market conditions and needs.⁶

Source: CMHC

⁵ Accessed May 20, 2021, <https://www.toronto.ca/legdocs/mmis/2020/ph/bgrd/backgroundfile-156420.pdf>

⁶ This approach has been successful, in some projects financed under CMHC’s Affordable Housing Innovation Fund, in reducing stigma and facilitating the provision of support services to those most in need.

Role of the Government of Canada in the SMB market

Our research has helped us identify some areas where the Government of Canada (GoC), through its departments and agencies, such as CMHC, could play a more active role in supporting the growth of the ESG bond market and in the realization of expected social and environmental outcomes related to the housing market:

Defining and standardizing ESG criteria used by investors, developers and housing proponents participating in the issuance of SMBs.

- During our consultations, investors emphasized the importance of adequate and standardized ESG definitions, criteria, and measurements to:
 - efficiently carry out green and affordable housing projects;
 - facilitate the development of ESG frameworks;
 - clarify differences in opinions related to labelling; and
 - support clear and transparent reporting.
- By standardizing the criteria framing ESG issuances, the GoC can ensure that investors, developers and housing proponents have a similar understanding of various terms in the context of SMBs (e.g., sustainable housing, green housing, social housing, affordable housing, housing hardship). This clarity could reduce information asymmetry and, potentially, risk premiums related to ESG bonds.

Setting best practices for monitoring, analysis and reporting.

- The GoC can encourage the adoption of principles and guidelines aligned with the NHS and its priorities, particularly those related to the supply of affordable housing.
- The GoC can also promote transparent reporting and encourage regular, clear, high-quality monitoring on the outcomes associated with SMBs. This could promote more socially responsible investment decisions and confidence in the ESG bond market.

Filling in ESG data gaps.

- Increase data sharing and availability by developing ESG data exchange programs, open data platforms and analytical tools to facilitate the assessment of social and green affordable housing projects. The GoC could also consider identifying or narrowing ESG data gaps as an alternative to support the market.

- ESG data and tools could be made available to investors, municipalities, developers and not-for-profit organizations to ensure a common alignment of goals and expectations.

Raising awareness and knowledge of the benefits of SMBs to the housing industry.

- The GoC can provide information and educational resources to ensure SMBs are well understood by all types of stakeholders, such as developers and not-for-profit organizations, in addition to those close to the financial markets, in order to:
 - ensure those who participate in SMB issuances understand the potential benefits and risks of SMBs; and
 - ensure developers and housing proponents understand the importance of meeting and reporting the social and green criteria required by lenders, issuers, and investors.

Consider providing government backing to SMBs to support public policy objectives.

- A public guarantee could reduce risk premiums and increase investors' adoption more rapidly, but could potentially expose taxpayers to financial losses. However, government guarantees may be considered if they can support the development of housing stock that is more affordable and climate-change-resilient, potentially resulting in long-term economic savings and positive environmental impacts for all Canadians.
- Government backing could be used to target public policy objectives not specifically or fully addressed by the private sector (i.e. affordable housing gap).
- According to our research, ESG bonds have shown a tendency to outperform non-ESG comparables during economic downturns (see *Sustainable Mortgage Bonds—Expected performance, investors' motivations and econometric analysis*). It is unclear whether this tendency could have an impact on public guarantees in the long term.

Establish a sizeable public ESG framework program and issue green, social, sustainable bonds to achieve social and environmental goals.

- The GoC, through its agencies, can issue ESG bonds or SMBs to reduce the funding gap in affordable housing and help fight climate change.
- A GoC issuance of an ESG bond could be used as a reference for other issuers to help standardize definitions and set best practices and benchmarks for reporting, oversight and measurement.

Summary

Our series of research insights has demonstrated that SMBs can be a catalyst to address the affordable housing gap and assist with the climate change challenge in Canada.

- ESG bonds, and by extension SMBs, can bring positive green, social and economic outcomes to the housing sector as they continue to grow and become mainstream.
- The appetite for ESG bonds in Canada is expected to continue growing as investors, developers and housing proponents become more familiar with the ESG bond market, and as the Canadian ESG bond market matures.
- Expected outcomes of SMBs can result in an increased supply of affordable housing, more affordable rents, and energy consumption savings in the medium to long term. The higher the volume of ESG bonds, the larger the impact that can be expected on the housing sector.
- The GoC can explore various options to support the growth of the ESG bond market. Some of these include raising awareness, developing guidelines, setting best principles/practices and potentially taking a more active role by issuing ESG bonds or providing government guarantees.

Assessing these various options is a potential step towards a bright future for the environment and the housing sector in Canada, particularly for those populations experiencing vulnerabilities that cannot afford a home that meets their needs.

Further reading

[Sustainable Mortgage Bonds—Why are they so relevant to the housing industry in Canada?](#)

[Sustainable Mortgage Bonds—Expected performance, investors' motivations and econometric analysis](#)

[Full report—Review of Sustainable Mortgage Bonds and Securities](#)

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