MEMORANDUM FOR FACING THE CHALLENGE OF CLIMATE CHANGE

SUBJECT: GREEN TRANSITION LINKED BONDS

1. **Issue:** Man-made greenhouse gas emissions have contributed to increased global temperatures and induced other forms of climate change, detrimental to global society and economy as well as the national interest of the United States. The following policy is one of many to address a complex problem that requires a multi-pronged solution.

2. **Strategic Analysis:** Past international approaches to address the climate emergency such as the Kyoto Protocol and Paris Agreement have failed because of a lack of enforcement mechanisms, transparency, and financing options. Green Transition-Linked Bonds (GTLBs) are innovative debt instruments that countries can issue to tie their green transition commitment to their actual performance to eliminate these pitfalls. Implementing GTLBs as a policy is a strategic imperative for the United States to reestablish credible commitment to achieve emissions targets and capitalize on first-mover advantage. Such an intervention advances the United States’ ability to catalyze global action, foster technological innovation, and demonstrate leadership in international climate finance, while opening new markets for innovation in American green technology. This strategy aligns with the United States’ objectives of promoting global stability, economic growth, and diplomatic influence by addressing the issue of greenhouse gas emission, which, if unchecked, may lead to greater economic disruptions and geopolitical instability.

3. **Relevant National Interests:** The United States has a national security interest in combating the climate crisis. As stated by senior United States military leaders, climate change is a “threat multiplier” due to its impact on “global stability, military readiness, humanitarian crises, and the risk of war.” Climate disruption has led to the melting of the Arctic, opening strategic transportation routes and exposing North America to new seafaring vulnerabilities. Furthermore, rising sea levels, flooding, and drought caused by climate change create food shortages, public unrest, and regional insecurity.

4. **Strategic Options:** Budgetary reallocation is a viable option to fund green transition projects. However, this strategy would not increase the transparency and accountability of the United States’ green transition. To improve clarity, more green bonds could be issued, but they still lack enforcement mechanisms. Sustainability-Linked Bonds (SLBs) have shown promise but are broad and do not fully address the green transition. GTLBs, as a way of financing climate initiatives, feature robust structure and penalty mechanisms to discourage greenwashing. Indeed, these bonds require a prior identification of a specific target and their repayment structure is linked to the relative performance. Failure to hit the targets results in
the issuance of additional penalty coupons to be paid to the investor. GTLBs must have Key Performance Indicators (KPIs) associated with them in order to ensure that quantitative impacts are made regarding climate change. This is to eliminate the shortcomings with SLBs faced by the private sector. Successful investment outcomes require material incentives to impose penalties for under-achieving Sustainability Performance Targets (SPTs). Data transparency and integrity generates trust and motivates investment.

5. **Recommendation:** By 01 January 2024, The United States Treasury will issue a specific percentage of the nation's annual bond debt in GTLBs with the sole purpose of appropriating funds towards projects that have a measurable impact on negating the world's carbon footprint. The Congress of the United States will enact legislation that sets these targets and act as an enforcer of the proper distribution of funds generated by GTLBs. If the money is misused or unsuccessful, penalty coupons will be issued to investors.

6. **Implementation:** Our policy will rely on cooperation between Congress and the United States Treasury and will be implemented throughout a procedural process as follows:

   1. Congress will determine the United States’ priorities for combating climate change.
   2. Priorities will be attainable, measurable, and externally verifiable by KPIs with the assistance of an external research agency.
   3. The project characteristics, such as duration, coupon value, penalties, interest, and amount of bonds to be issued, will be defined in collaboration with the Treasury.
   4. A pilot project will be identified to test the effectiveness of GTLBs.
   5. The United States Treasury will issue the bonds.
   6. The pilot project will be evaluated by its KPIs at various stages.
   7. Once proven effective, GTLBs will be implemented globally.

7. The United States must promote innovative environmental policies to address the wicked problem of climate change. Successfully implementing GTLBs will mitigate the effects of climate change, ensuring domestic safety and tranquility. To maintain its role on the economic world stage, the United States must provide innovative solutions in capping greenhouse gas emissions. Early adoption will lead other global superpowers to issue bonds that have a direct positive impact on the environment and alleviate the worst impacts of climate change as we accelerate our efforts in a transition to a green-linked society.

8. The point of contact for this memorandum is Maxwell Rutledge at maxwell.rutledge@westpoint.edu or 567-525-2967.