

PR 9: Financial Intermediaries

Introduction

1. Financial Intermediaries (FIs) are a key instrument for the EBRD to promote sustainable financial markets and provide a vehicle to channel EBRD funding to the micro, small and medium-sized enterprise (SME) sector. Through its network of partner FIs, the EBRD can support economic development at a scale of enterprise that is smaller than would be possible through direct EBRD investment. The EBRD supports a variety of financial service providers including among others, private equity funds, banks, leasing companies, insurance companies and pension funds. The FIs are engaged in a wide range of activities, such as microfinance, SME lending, trade finance, medium to long-term corporate or project finance, and housing finance.

2. The very nature of intermediated financing means that the EBRD will delegate to the FI responsibility for transaction appraisal and monitoring as well as overall portfolio management. Environmental and social risk management are part of the responsibilities delegated to the FI. Nevertheless, by virtue of its relationship with the FI, the EBRD continues to have an interest in assessing and monitoring whether the environmental and social risks associated with the FI's business activities are adequately addressed by the FI. The exact modalities of delegation and EBRD oversight will depend on a number of factors, including the nature of the FI and its business activities, the type of finance provided and the business environment in the country.

Objectives

3. The objectives of this Performance Requirement (PR) are:

- to establish a practical way in which the Bank's mandate to promote sustainable development can be implemented in its FI investments, in line with best international practice in the commercial financial sector
- to enable FIs to manage environmental and social risks associated with their business activities and to promote good environmental and social business practices amongst their clients
- to promote good environmental and human resource management within FIs.

Scope of application

4. This Performance Requirement applies to all projects classified as "FI" pursuant to paragraph 24 of the Policy.

5. For the purposes of this PR, the word "project" is used in reference to the EBRD transaction with the FI, whereas "subproject" is used to refer to the clients/projects financed by the FIs.

6. Where the EBRD is financing a credit line or other targeted finance facility, the requirements of this PR will apply to all subprojects financed using EBRD funds.

7. Where the EBRD provides equity or quasi-equity financing to an FI, the requirements of this PR will apply to the FI's entire portfolio of commercial subprojects originated from the time of the EBRD becoming a shareholder or investor, subject to paragraph 16.

8. Where an FI project is judged by the EBRD to have minimal or no adverse environmental or social risks, no specific requirements will apply and the FI will not need to adopt any environmental and social risk management procedures.

Requirements

Environmental and social due diligence and monitoring procedures

9. The FI will adopt and implement environmental and social due diligence and monitoring procedures (hereafter “Procedures”) commensurate with the level of environmental and social risks associated with its business activities and type of project with the EBRD. These Procedures will be agreed with the EBRD.

10. Where an FI can demonstrate that it already has in place a set of environmental and social risk management procedures, the EBRD will review the content of these and the FI’s implementation capacity against the requirements of this PR.

11. The FI will design the Procedures so as to ensure that the requirements of paragraphs 13–16 are met. The Procedures will also include risk appraisal and monitoring mechanisms as appropriate, including:

- a risk categorisation of proposed subprojects
- the undertaking of due diligence on clients and subprojects commensurate with the identified risks
- the structuring of subprojects so that they meet national requirements for environment, health, safety, labour and public consultation including, where necessary, requiring clients to implement corrective action plans
- the monitoring of subprojects to ensure compliance with national requirements for environment, health, safety, labour and public consultation, and, where relevant, corrective action plans.

12. To assist FIs with putting the Procedures into practice, the EBRD has developed an environmental and social risk management manual (“eManual”) which includes model Procedures and guidance for various types of FIs and financial services. FIs that do not already have equivalent procedures in place are required to use relevant parts of the eManual in respect of the relevant subprojects.

Requirements for subprojects

13. FIs will screen all subprojects against the Bank’s Environmental and Social Exclusion List included in Annex 1 to this PR. Subprojects involving business activities included on this list are not eligible for FI support and applications involving such activities must be rejected.

14. Annex 2 to this PR includes a number of business activities with particularly high social and environmental risks. Where a subproject involves activities listed in Annex 2 of this PR, the FI will refer that subproject to the Bank, and ensure that the subproject is benchmarked against the applicable EBRD Performance Requirements (PRs). The EBRD strongly encourages FIs to discuss these cases early in their due diligence process. EBRD will assist FIs with the appraisal of these subprojects. EBRD environmental/social specialists will review the due diligence information collected by the FI, determine any additional information needed, assist with determining appropriate mitigation measures and, if necessary, specify conditions under which the subprojects may proceed.

15. FIs will require all clients to comply with national regulations and standards related to (i) the environment, (ii) public consultation, and (iii) employment, including without limitation, occupational health and safety, child labour, forced labour; non-discrimination related to employment, and freedom of association and collective bargaining.

16. When FIs are providing project finance¹ under an EBRD Credit Line with estimated total project capital costs of US\$ 10 million or more for subprojects involving (i) new developments or (ii) expansion or upgrade of an existing facility where changes in scale or scope may create significant additional environmental or social impacts, such subprojects will be required to meet EBRD PRs 1–8 and 10.

17. The EBRD may set additional or alternative environmental and social requirements, depending on the nature of the FI and its portfolio and the country of operation.²

Organisational capacity within the FI

18. The FI will maintain human resources policies, management systems and practices in accordance with EBRD PR 2 – Labour and Working Conditions.

19. The FI will appoint a member of management to have overall responsibility for environmental and social matters, including the implementation of the Procedures.

20. Depending on the size of the FI and its business activities, the FI should also (i) appoint one or more staff responsible for overseeing the day-to-day application of the Procedures, and providing implementation support; and (ii) ensure that adequate technical expertise is available to them to assess transactions with potentially high environmental or social risks, either in-house or as external specialists.

21. The FI will ensure that the Procedures and the requirements set forth in paragraphs 9–20 are clearly communicated to all relevant staff, and provide appropriate training to ensure that staff have the necessary capabilities and support to implement them.

Reporting to the EBRD

22. The FI will submit to the EBRD periodic (typically annual) reports on the implementation of the Procedures and the environmental and social performance of its investment/lending portfolio. Standard reporting formats are included in the eManual.

Stakeholder engagement

23. The FI will put in place a system for dealing with external communication on environmental and social matters, for example a point of contact for dealing with public enquiries and concerns related to environmental and social matters. The FI will respond to such enquiries and concerns in a timely manner.

¹ Project finance is “a method of funding in which the lender looks primarily to the revenues generated by a single project, both as the source of repayment and as security for the exposure. This type of financing is usually for large, complex and expensive installations that might include, for example, power plants, chemical processing plants, mines, transportation infrastructure, environment, and telecommunications infrastructure. Project finance may take the form of financing of the construction of a new capital installation, or re-financing of an existing installation, with or without improvements. In such transactions, the lender is usually paid solely or almost exclusively out of the money generated by the contracts for the facility’s output, such as the electricity sold by a power plant. The borrower is usually an SPE (Special Purpose Entity) that is not permitted to perform any function other than developing, owning, and operating the installation. The consequence is that repayment depends primarily on the project’s cash flow and on the collateral value of the project’s assets.” Source: Basel Committee on Banking Supervision, International Convergence of Capital Measurement and Capital Standards (“Basel II”), November 2005. See www.bis.org/publ/bcbs118.pdf.

² For example, if the country has not ratified all core ILO conventions [ILO conventions 29 and 105 (forced and bonded labour), 87 (freedom of association), 98 (right to collective bargaining), 100 and 111 (discrimination), 138 (minimum age) 182 (worst forms of child labour) and transposed them into national law].

Best practice

24. The EBRD encourages all its FIs to follow best practices in sustainability management in their entire lending and investment operations, irrespective of whether these are financed by the EBRD. In particular, FIs are encouraged to:

- report periodically to their external stakeholders on how they address environmental and social issues in their business and operations. This may, for example, be by including, in the FI's Annual Report, web site or other public document, a section summarising its commitment to the requirements outlined in this PR
- work towards applying best practices in in-house environmental management (including energy and resource efficiency, waste reduction and recycling)
- roll out the application of the Procedures and the eManual to all their business activities, including those to which this PR does not apply
- identify, where appropriate, opportunities for developing financial products with high environmental and/or social benefits (for example, finance for investments in energy efficiency, renewables or pro-biodiversity business, products targeting women entrepreneurs, access to credit for micro entrepreneurs).

Further guidance on best practices is available in EBRD's eManual. FIs should also consider joining appropriate existing international initiatives that promote best practices in the financial sector such as the Equator Principles (EPs), the United Nations Environment Programme Finance Initiative (UNEP FI), and the Principles for Responsible Investment (PRI).³

³ Equator Principles (EPs): www.equator-principles.com; United Nations Environment Programme (UNEP) Finance Initiative (FI): www.unepfi.org; Principles for Responsible Investment (PRI): www.unpri.org.

PR 9 Annex 1: EBRD Environmental and Social Exclusion List

The EBRD will not knowingly finance, directly or indirectly, projects involving the following:

- a) The production of or trade in any product or activity deemed illegal under host country (that is, national) laws or regulations, or international conventions and agreements, or subject to international phase out or bans, such as:
 - (i) Production of, or trade, in products containing polychlorinated biphenyls (PCBs)⁴
 - (ii) Production of, or trade, in pharmaceuticals, pesticides/herbicides and other hazardous substances subject to international phase-outs or bans⁵
 - (iii) Production of, or trade, in ozone depleting substances subject to international phase-out⁶
 - (iv) Trade in wildlife or production of, or trade, in wildlife products regulated under CITES⁷
 - (v) Transboundary movements of waste prohibited under international law;⁸
- b) Production or use of or trade in unbonded asbestos fibres or asbestos-containing products⁹
- c) Activities prohibited by host country legislation or international conventions relating to the protection of biodiversity resources or cultural heritage¹⁰
- d) Driftnet fishing in the marine environment using nets in excess of 2.5 kilometres in length
- e) Shipment of oil or other hazardous substances in tankers which do not comply with International Maritime Organization (IMO) requirements¹¹
- f) Trade in goods without required export or import licenses or other evidence of authorisation of transit from the relevant countries of export, import and, if applicable, transit.

⁴ PCBs: Polychlorinated biphenyls – a group of highly toxic chemicals. PCBs are likely to be found in oil-filled electrical transformers, capacitors and switchgear dating from 1950–85.

⁵ Reference documents are EU Regulation (EEC) No 2455/92 Concerning the Export and Import of Certain Dangerous Chemicals, as amended; UN Consolidated List of Products whose Consumption and/or Sale have been Banned, Withdrawn, Severely Restricted or not Approved by Governments; Convention on the Prior Informed Consent Procedures for Certain Hazardous Chemicals and Pesticides in International Trade (Rotterdam Convention); Stockholm Convention on Persistent Organic Pollutants; WHO Classification of Pesticides by Hazard.

⁶ Ozone Depleting Substances (ODS): Chemical compounds which react with and deplete stratospheric ozone, resulting in the widely publicised 'ozone holes'. The Montreal Protocol lists ODSs and their target reduction and phase-out dates. A list of the chemical compounds regulated by the Montreal Protocol, which includes aerosols, refrigerants, foam blowing agents, solvents, and fire protection agents, together with details of signatory countries and phase out target dates, is available from the EBRD.

⁷ CITES: Convention on International Trade in Endangered Species of Wild Fauna and Flora. The lists of CITES protected species are available at www.cites.org/eng/app/index.shtml.

⁸ Reference documents are: Regulation (EC) No 1013/2006 of 14 June 2006 on shipments of waste; Decision C(2001)107/Final of the OECD Council concerning the revision of Decision C(92)39/Final on the control of transboundary movements of wastes destined for recovery operations; Basel Convention of 22 March 1989 on the control of transboundary movements of hazardous wastes and their disposal.

⁹ This does not apply to the purchase and use of bonded asbestos cement sheeting where the asbestos content is <20%.

¹⁰ Relevant international conventions include, without limitation: Convention on the Conservation of Migratory Species of Wild Animals (Bonn Convention); Convention on Wetlands of International Importance, especially as Waterfowl Habitat (Ramsar Convention); Convention on the Conservation of European Wildlife and Natural Habitats (Bern Convention); World Heritage Convention; Convention on Biological Diversity.

¹¹ This includes: tankers which do not have all required MARPOL SOLAS certificates (including, without limitation, ISM Code compliance); tankers blacklisted by the European Union or banned by the Paris Memorandum of Understanding on Port State Control (Paris MOU); and tankers due for phase out under MARPOL regulation 13G. No single hull tanker over 25 years old should be used.

PR 9 Annex 2: The financing by FIs of the following environmentally or socially sensitive business activities is subject to referral to the EBRD.

The principal Performance Requirement that proposed transactions will be expected to meet is indicated in italics.

a) Activities involving involuntary resettlement – *EBRD Performance Requirement 5.*

b) Activities within, adjacent to, or upstream of designated protected areas under national law or international conventions, sites of scientific interest, habitats of rare/endangered species, fisheries of economic importance, and primary/old growth forests of ecological significance – *EBRD Performance Requirement 6.*

c) Activities within, adjacent to, or upstream of land occupied by Indigenous Peoples and/or vulnerable groups including lands and watercourses used for subsistence activities such as livestock grazing, hunting, or fishing – *EBRD Performance Requirement 7.*

d) Activities which may affect adversely sites of cultural or archaeological significance – *EBRD Performance Requirement 8.*

e) Activities in the nuclear fuel production cycle (uranium mining, production, enrichment, storage or transport of nuclear fuels).¹²

f) Energy generation using nuclear fuels (excluding electricity import/export).¹³

g) Activities involving the release of GMOs into the natural environment – *EBRD Performance Requirement 6.*

h) Construction of mini-hydro cascades – *EBRD Eligibility Criteria for Small Hydro Projects.*

¹² In compliance with the EBRD's Energy Policy, the Bank is permitted to use its funding (directly or indirectly through FIs) in relation to nuclear safety improvements, or for the safe and secure management of radioactive waste and spent nuclear fuel, as well as for decommissioning, without a direct link to the closure of high-risk reactors. Any other activities in the nuclear fuel production cycle are therefore excluded from FI financing.

¹³ In compliance with the EBRD's Energy Policy, the Bank is permitted to use its funding (directly or indirectly through FIs) in relation to nuclear safety improvements, or for the safe and secure management of radioactive waste and spent nuclear fuel, as well as for decommissioning, without a direct link to the closure of high-risk reactors. Any other activities involving energy generation using nuclear fuels are therefore excluded from FI financing.