

DRAFT FOR PUBLIC COMMENT**Guidance Note for ESS9****Financial Intermediaries**

The Guidance Notes provide guidance for the Borrower on the application of the Environmental and Social Standards (ESSs), which form part of the World Bank’s 2016 Environmental and Social Framework. The Guidance Notes help to explain the requirements of the ESSs; they are not Bank policy, nor are they mandatory. The Guidance Notes do not substitute for the need to exercise sound judgment in making project decisions. In case of any inconsistency or conflict between the Guidance Notes and the ESSs, the provisions of the ESSs prevail. Each paragraph of the Standard is highlighted in a box, followed by the corresponding guidance.

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Introduction

1. *ESS9 recognizes that strong domestic capital and financial markets and access to finance are important for economic development, growth and poverty reduction. The Bank is committed to supporting sustainable financial sector development and enhancing the role of domestic capital and financial markets.*

2. *FIs are required to monitor and manage the environmental and social risks and impacts of their portfolio and FI subprojects, and monitor portfolio risk, as appropriate to the nature of intermediated financing. The way in which the FI will manage its portfolio will take various forms, depending on a number of considerations, including the capacity of the FI and the nature and scope of the funding to be provided by the FI.*

3. *FIs are required to develop and maintain, in the form of an Environmental and Social Management System (ESMS), effective environmental and social systems, procedures and capacity for assessing, managing, and monitoring risks and impacts of subprojects, as well as managing overall portfolio risk in a responsible manner.*

Objectives

- *To set out how the FI will assess and manage environmental and social risks and impacts associated with the subprojects it finances.*
- *To promote good environmental and social management practices in the subprojects the FI finances.*
- *To promote good environmental and sound human resources management within the FI.*

Scope of Application

4. *This ESS applies to Financial Intermediaries (FIs) that receive financial support from the Bank. FIs include public and private financial services providers, including national and regional development banks, which channel financial resources to a range of economic activities across industry sectors.¹ Financial intermediation also includes provision of financing or guarantees by FIs to other FIs. For the purposes of this ESS, the term "FI subproject" refers to projects financed by FIs with support from the Bank.² Where the project involves on-lending by the FI to another FI, the term "FI subproject" will include the subprojects of each subsequent FI.*

Footnote 1. Such FIs use various financial products such as project finance, corporate finance, medium and small enterprise finance, microfinance, housing finance, leasing, and trade finance. This ESS covers all types of financing and financial products provided by FIs that are targeted to productive business activities.

Footnote 2. "FI subprojects" are defined as projects or activities financed by an FI. Where an FI provides financing, or guarantees to other FIs, "FI subprojects" are defined as projects or activities financed by the latter FI with support from the former FI.

GN4.1. World Bank IPF support to FIs can take different forms, and may include:

- (a) loans, credits or grants to FIs to be used by them for loans or equity for specific sub-projects, or channeled to other FIs to be used by them for loans or equity for specific sub-projects; and
- (b) Guarantees to FIs to enable them to mobilize debt financing for loans, guarantees, or equity for specific sub-projects; and

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The scope of application of ESS9 depends on the project activities or commitments covered by Bank investment project financing. Technical assistance may be provided to IPF loans, credits and grants.

GN4.2. Project structures supporting financial intermediation may include the following types of entities:

- (a) Ministries of Finance;
- (b) central banks;
- (c) state financial institutions that may be a state agency, authority or board not established under corporate law;
- (d) independent financial institutions established under corporate law (including banks, financial companies, whether state or privately owned); or
- (e) funds managed by a fund manager, which may include a formally established fund or funds in the form of a government bank account for a purpose defined by the project (without staff or operating resources). This category does not include funds that are not part of financial intermediation, for example, matching grant schemes.

GN4.3. FIs may provide a variety of financial products and services including credit products, which can be funded (loans) or unfunded (guarantees); other financial products such as dealing room products (for example, hedging, swaps) and investment banking products (for example, bond underwriting, arranging of equity issuances); equity investments; or fund management.

GN4.4. Projects may involve one or more FIs, different terms may be used to describe the different entities involved in financial intermediation projects. For example, the World Bank may provide investment project financing to a Ministry of Finance (borrowing entity), which delegates the administration of a line of credit to an apex FI (wholesaling entity), which on-lends to participating FIs (retail entities), which lend to small and medium enterprises for projects or activities (FI subproject).

GN4.5. An “FI subproject” is the ultimate project or activities supported by the FI. As Footnote 2 states, if an FI provides financial support to another FI (for example, through a loan or guarantee) the FI subproject is the project or activities supported by the participating FI. For example, where the FI provides a loan to a rural finance institution, which then lends (via a sub-loan) to a farmer (sub-borrower) who uses the loan to expand farming operations, the FI subproject is the expanded farming operation.

GN4.6. Where a World Bank project includes technical assistance to an FI, the FI follows the requirements set out in ESS1 as relevant and appropriate to the nature and risks of the technical assistance.

5. *The requirements of this ESS apply to all FIs that receive support from the Bank, either directly from the Bank or the Borrower, or through the Borrower or other FIs, as follows:*

- (a) *Where Bank support is provided to the FI to fund clearly-defined FI subprojects the requirements of this ESS will apply to each of the FI subprojects;*

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(b) Where Bank support is provided to the FI for a general purpose,³ the requirements of this ESS will apply to the entire portfolio of the FI's future subprojects from the date on which the legal agreement becomes effective.

Footnote 3. Support for a 'general purpose' means that the support cannot be traced to a specific FI subproject or specific types of financing.

6. Where an FI receiving support from the Bank provides financing or guarantees to other FIs, the FI will apply the requirements of this ESS and will cause each subsequent FI to apply the requirements of this ESS, as specified in paragraph 5 of this ESS.

GN6.1. The way in which each FI will apply the requirements of ESS9 will depend on the FI's relationship to the FI subprojects. As noted in GN7.1, the ESMS will be established and maintained by the Responsible FI. Where funding is provided through a number of FIs, the requirements relating to ESS9 are incorporated into each of the contractual agreements between an FI and the subsequent FIs, to which loans, equity, financing or guarantees are provided.

Requirements

7. FIs will put in place and maintain an ESMS to identify, assess, manage, and monitor the environmental and social risks and impacts of FI subprojects on an ongoing basis. The ESMS will be commensurate with the nature and magnitude of environmental and social risks and impacts of FI subprojects, the types of financing, and the overall risk aggregated at the portfolio level.⁴ Where the FI can demonstrate that it already has an ESMS in place, it will provide adequate documented evidence of such an ESMS, indicating which elements (if any) will be enhanced or modified to meet the requirements of this ESS.⁵

Footnote 4. For the purpose of assessing the adequacy of the ESMS, the FI portfolio means the portfolio of current and/or proposed subprojects to which this ESS applies, as described in paragraph 5.

Footnote 5. Where the Bank is providing support to a project involving Financial Intermediaries (FIs), and other multilateral or bilateral funding agencies, including IFC and MIGA, will or have already provided financing to the same FIs, the Bank may agree to rely on the requirements of such other agencies for the assessment and management of environmental and social risks and impacts of the project, including the institutional arrangements already established by the participating FIs, provided that such requirements will enable the project to achieve objectives materially consistent with this ESS and other ESSs, as applicable. Following review by the Bank, an FI may be required to enhance its ESMS, as deemed necessary by the Bank.

GN7.1. The FI that is required to develop and maintain the ESMS is the FI that has direct responsibility for selecting and funding the FI subprojects (the Responsible FI). The Responsible FI develops and maintains the ESMS, so that the environmental and social risks and impacts of the FI subprojects financed or guaranteed by the Responsible FI can be identified, assessed, managed and monitored appropriately.

GN7.2. The ESMS includes processes for screening and categorizing proposed subprojects based on their potential environmental and social risks and impacts, conducting environmental and social assessments and monitoring subproject environmental and social performance. An existing ESMS may need to be strengthened to meet the requirements of ESS9, in which case it is recommended that a time-bound action plan be used by the FI for this purpose.

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GN7.3. An effective ESMS is commensurate with the highest level of environment and social risk that is anticipated in FI subprojects and/or portfolio. The ESMS is reviewed and enhanced by the responsible FI as needed prior to supporting a new FI subproject with higher levels of environmental and social risks and impacts.

GN7.4 Where the Borrower on-lends Bank funds, the contractual arrangements between on-lending parties should set out the requirements of ESS9 including establishment of ESMS and the application of ESS2 to the Responsible FI.

8. *The FI's ESMS will include the following elements: (i) environmental and social policy; (ii) clearly defined procedures for the identification, assessment and management of the environmental and social risks and impacts of subprojects; (iii) organizational capacity and competency; (iv) monitoring and review of environmental and social risks of subprojects and the portfolio; and (v) external communications mechanism.*

9. *Where FI subprojects are likely to have minimal or no adverse environmental or social risks or impacts, the FI will apply national law.⁶*

Footnote 6. This will rely on an assessment of the risks of the potential FI subprojects that the FI is proposing to finance, and the capacity of the FI. This may apply to certain retail financial products, such as consumer loans or credit cards.

10. *The FI will review and adjust, in a manner acceptable to the Bank, its ESMS from time to time, including when the environmental and social risk profile of its portfolio changes significantly.*

GN10.1. The ESMS is updated or supplemented by the responsible FI if the environment and social risk profile of the FI's general purpose or subproject portfolio changes significantly. Changes to the ESMS may include updating procedures, conducting staff training on specific issues or adding additional staff with relevant skills. Any significant changes proposed to the ESMS are agreed with the Bank prior to their adoption. A summary of changes to the ESMS can be included in the reports submitted to the Bank, in accordance with Paragraph 23 of ESS9.

11. *The FI will comply with any exclusions in the legal agreement and apply relevant national law for all FI subprojects. In addition, the FI will apply the relevant requirements of the ESSs to any FI subproject that involves resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on Indigenous Peoples or significant risks or impacts on the environment, community health and safety, labor and working conditions, biodiversity or cultural heritage.*

12. *An FI may be required to adopt and implement additional or alternative environmental and social requirements, depending on the nature of the FI, its activities, the sector or countries of operation, and the environmental and social risks and impacts of the potential FI subprojects.⁷*

Footnote 7. These will be incorporated into the ESMS, the environmental and social procedures and/or set out in the legal agreement.

GN11.1. Paragraph 11 applies to the Responsible FI, and the requirements of Paragraph 11 are incorporated in the ESMS. Examples of exclusions include the ineligibility of subprojects or general purpose activities that are high risk or have significant adverse environmental or social impacts, or

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ineligibility of business activities that involve land expropriation, involuntary resettlement or loss or damage to assets.

GN11.2. Where Bank support is provided for a general purpose, as set out in Paragraph 5(b) of ESS9, the exclusions in the legal agreement apply to the entire portfolio of the FI. Where the World Bank support is for clearly defined subprojects, the exclusions apply only to those subprojects.

GN11.3. When the risks and impacts referred to in Paragraph 11 are identified, the Responsible FI ensures that (i) the ESMS contains procedures to address such risks and impacts, and (ii) the contractual arrangements between the Responsible FI and the FI subprojects provide for application of such procedures.

13. *The FI will provide a safe and healthy working environment. Accordingly, relevant aspects of ESS2 will apply to the FI itself. The FI will have in place and maintain appropriate labor management procedures, including procedures relating to working conditions and terms of employment, non-discrimination and equal opportunity, grievance mechanisms and occupational health and safety. The FI will provide adequate documented evidence of such procedures.*

GN13.1. This requirement applies to the Responsible FI.

A. Environmental and Social Management System

Environmental and Social Policy

14. *The environmental and social policy of the FI will be endorsed by the FI's senior management and will include organizational commitments, objectives, and metrics with regard to the FI's environmental and social risk management. The policy will clearly state applicable requirements for FI subprojects, and will include the following:*

- (a) *All FI subprojects will be prepared and implemented in accordance with relevant environmental and social national and local laws and regulations;*
- (b) *All FI subprojects will be screened against exclusions in the legal agreement;⁸*
- (c) *All FI subprojects will be screened for environmental and social risks and impacts;*
- (d) *All FI subprojects which involve resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on Indigenous Peoples or significant risks or impacts on the environment, community health and safety, labor and working conditions, biodiversity or cultural heritage will apply relevant requirements of ESSs.⁹*

Footnote 8. These will be set out in the legal agreement between the FI and the entity providing financing to the FI, and will reflect the exclusions in the legal agreement pursuant to which the Bank provides its support.

Footnote 9. The relevant requirements of the ESSs will be applied to such projects regardless of how such projects are categorized under the FI's own risk categorization system as referred to in paragraph 17.

GN14.1. The ESMS contains the elements that allow the FI to manage the environmental and social risk of its operations and the subprojects it supports. These elements include:

- an environmental and social policy;

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- procedures for the assessment and monitoring of sub-projects;
- organizational capacity and competency of the FI;
- stakeholder engagement; and
- monitoring and reporting.

Environmental and Social Procedure

15. *The FI will put in place and maintain clearly defined environmental and social procedures which reflect and implement the FI's Environmental and Social Policy. The procedures will be proportionate to the nature of the FI and the level of potential environmental and social risks and impacts associated with the FI subprojects.¹⁰*

Footnote 10. Where the FI already has appropriate environmental and social procedures in place, it will provide adequate documented evidence of such procedures to the Bank and, following review by the Bank, will enhance them, as deemed necessary by the Bank.

16. *The FI's environmental and social procedures will include measures to:*

- (a) Screen all FI subprojects against any exclusions in the legal agreement;*
- (b) Screen, review and categorize the FI subprojects according to their potential environmental and social risks and impacts;*
- (c) Require that all FI subprojects are assessed, prepared and implemented to meet national law and, in addition, where an FI subproject involves resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on Indigenous Peoples or significant risks or impacts on the environment, community health and safety, labor and working conditions, biodiversity or cultural heritage, the relevant requirements of the ESSs are applied;¹¹*
- (d) Ensure that the measures needed to satisfy the requirements of (c) above are set out in the legal agreement between the FI and the sub-borrower;*
- (e) Monitor and keep and regularly update environmental and social information on FI subprojects;*
- (f) If the risk profile of an FI subproject increases significantly, apply relevant requirements of the ESSs¹² and document these appropriately; and*
- (g) Monitor the environmental and social risk of the FI portfolio.*

Footnote 11. The environmental and social procedures will require such FI subprojects to conduct stakeholder engagement pursuant to ESS10 in a manner proportionate to the risks and impacts of the FI subprojects.

Footnote 12. The 'relevant requirements of the ESSs' will relate to the reasons for which the risk profile of the FI subproject has increased.

GN16.1. If the risk profile of an FI subproject increases significantly, and the FI's existing environmental and social procedures are not adequate to address this increased risk, the FI modifies such procedures as necessary.

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17. As part of the environmental and social procedures, the FI will develop and adopt a categorization system for subprojects with clearly defined risk categories.¹³ The categorization system will take into account (i) the nature and magnitude of environmental and social risks and impacts of subprojects; (ii) sectoral and geographical context; (iii) type of financing. The risk categorization will inform the scope and nature of the FI's environmental and social due diligence and risk management of its subprojects. Such categorization system will allow for a systematic aggregation and analysis of risk at the portfolio level.

Footnote 13. A typical categorization system used by FIs may consist of three or four risk categories, which correspond to high, substantial, moderate, or low risk. Good international practice in some instances suggests that four risk categories allow for more comprehensive assessment and management of environmental and social risk by FIs.

18. As part of its environmental and social risk categorization system, the FIs will categorize any subproject which involves resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on Indigenous Peoples or significant risks or impacts on the environment, community health and safety, labor and working conditions, biodiversity or cultural heritage, as high or substantial risk.

Organizational Capacity and Competency

19. The FI will develop and maintain organizational capacity and competency for implementing the ESMS with clearly defined roles and responsibilities. The FI will designate a representative of the FI's senior management to have overall accountability for environmental and social performance of the FI subprojects, including the implementation of this ESS and ESS2 and resources necessary to support such implementation. The representative will: (a) designate a staff member to be responsible for day-to-day implementation of the ESMS, including the environmental and social procedures; (b) ensure that adequate resources are available for management of and training in environmental and social issues; and (c) ensure that adequate technical expertise, either in-house or external expert support, is available to carry out due diligence and manage the environmental and social risks of the FI subprojects, including providing implementation support as required.

20. The FI will ensure that the requirements of this ESS and ESS2 are clearly communicated to all relevant FI personnel,¹⁴ and to ensure that relevant personnel have the necessary knowledge and capabilities¹⁵ for managing environmental and social risks in accordance with the FI's ESMS.

Footnote 14. Such personnel may include investment, legal, and credit officers, security personnel etc.

Footnote 15. Including by providing appropriate training.

Monitoring and Reporting

21. The FI will monitor the environmental and social performance of the FI subprojects in a manner proportionate to the risks and impacts of the FI subprojects, and provide regular progress reports to the FI's senior management. This will include periodic review of the effectiveness of the FI's ESMS.

GN21.1. As part of its ESMS, the Responsible FI develops a written procedure detailing how performance monitoring is conducted. This monitoring is proportionate to the environmental and social risks and impacts of the FI subprojects. Monitoring and reporting is conducted on a regular basis.

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GN21.2. The frequency and method of monitoring of FI subprojects depends upon the risk levels and performance of the FI subprojects. Monitoring outcomes and identified corrective actions should be documented. The Responsible FI works with the FI subproject to ensure corrective actions are implemented.

GN21.3. The ESMS is reviewed periodically by the Responsible FI to assess the effectiveness, and determine whether changes are needed. The review of the ESMS is expected to evaluate the FI's implementation of its own environmental and social policy as referenced in Paragraph 14, and how environmental and social procedures have been implemented with respect to FI subprojects

22. The FI will promptly notify the Bank of any significant accidents or incidents associated with FI subprojects. If the risk profile of an FI subproject increases significantly, the FI will notify the Bank and will apply relevant requirements of the ESSs in a manner agreed with the Bank, as set out in the ESMS. The FI will monitor the measures and actions agreed, and report to the Bank as appropriate.

GN22.1. The notification of any significant accidents or incidents to the World Bank may be provided directly by the Responsible FI to the World Bank or through the Borrower.

23. The FI will submit to the Bank Annual Environmental and Social Reports on the implementation of its ESMS, including its environmental and social procedures, this ESS and ESS2, as well as the environmental and social performance of its portfolio of FI subprojects. The annual report will include details of how the requirements of this ESS are being met, the nature of the FI subprojects financed through the project, and the overall portfolio risk, profiled by sector.

GN23.1. Depending on the level of risk of a subproject, reporting may be required more frequently than annually.

B. Stakeholder Engagement

24. The FI will require the FI subproject to conduct stakeholder engagement in a manner proportionate to the risks and impacts of the FI subproject, and which reflects the type of FI subprojects it will finance. The relevant provisions of ESS10 will be included in the FI's environmental and social procedures. In certain circumstances, depending on the risks and impacts of the project and the type of FI subprojects it will finance, the Bank may require the FI to be engaged in stakeholder engagement.

GN24.1. ESS10 sets out requirements relating to the disclosure of information to allow stakeholders to understand the potential risks and impacts of FI subprojects. This information is disclosed in the relevant local languages and in a manner, that is accessible and culturally appropriate, and prior to approval of the FI subproject. Further details on stakeholder engagement are set out in ESS10.

25. The FI will put in place procedures for external communications on environmental and social matters proportionate to the risks and impacts of the FI subprojects, and the risk profile of the FI's portfolio. The FI will respond to public enquiries and concerns in a timely manner.

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GN25.1. Procedures for external communications on environmental and social issues are designed to receive, respond to, and document requests for information or concerns to allow a timely response. This includes making contact information publicly available and easily accessible (for example, a phone number, website, e-mail address). If a concern is deemed not to be relevant, the Responsible FI records the reasons for this determination.

26. *The FI will disclose through the FI's website, if a website exists, and permit, in writing, the Bank to disclose on the Bank's website, a summary of each of the elements of the FI's ESMS.*

27. *The FI will require its sub-borrowers to disclose, in relation to FI subprojects, any project-related documents¹⁶ required (a) by the application of the ESSs; (b) for any FI subprojects categorized as high risk in accordance with the FI's own categorization system; and (c) any environmental and social monitoring reports relating to (a) or (b).*

Footnote 16. For example, environmental and social assessment reports, resettlement action plans and Indigenous Peoples plans.

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