



International Finance Corporation's Policy on Social & Environmental Sustainability

April 30, 2006

Section 1: Purpose of this Policy

1. International Finance Corporation (IFC) strives for positive development outcomes in the private sector projects it finances in emerging markets. An important component of positive development outcomes is the social and environmental sustainability of projects, which IFC expects to achieve by applying a comprehensive set of social and environmental performance standards.

2. Through its *Policy on Social and Environmental Sustainability* (the Sustainability Policy), IFC puts into practice its commitment to social and environmental sustainability. This commitment is based on IFC's mission and mandate, as explained in Section 2 of this Policy. Translating this commitment into successful outcomes depends on the efforts of IFC and its clients. Consistent with this commitment, IFC carries out the actions described in Section 3 of this Policy, including its responsibility to review projects proposed for direct financing against the Performance Standards.

3. The Performance Standards consist of the following:

Performance Standard 1: Social and Environmental Assessment and Management System

Performance Standard 2: Labor and Working Conditions

Performance Standard 3: Pollution Prevention and Abatement

Performance Standard 4: Community Health, Safety and Security

Performance Standard 5: Land Acquisition and Involuntary Resettlement

Performance Standard 6: Biodiversity Conservation and Sustainable Natural Resource Management

Performance Standard 7: Indigenous Peoples

Performance Standard 8: Cultural Heritage

4. These Performance Standards are essential documents to help IFC and its clients manage and improve their social and environment performance through an outcomes-based approach. The desired outcomes are described in the objectives of each Performance Standard, followed by specific requirements to help clients achieve these outcomes through means that are appropriate to the nature and scale of the project and commensurate with the level of social and environmental risks (likelihood of harm) and impacts. Central to these requirements is a consistent approach to avoid adverse impacts on workers, communities, and the environment, or if avoidance is not possible, to reduce, mitigate, or compensate for the impacts, as appropriate. The Performance Standards also provide a solid base from which clients may increase the sustainability of their business operations.

5. While managing social and environmental risks and impacts in a manner consistent with the Performance Standards is the responsibility of the client, IFC seeks to ensure that the projects it finances are operated in a manner consistent with the requirements of the Performance Standards. As a result, IFC's social and environmental review of a proposed project is an important factor in its decision to finance the project or not, and will determine the scope of the social and environmental conditions of IFC financing. By adhering to this Policy, IFC enhances the predictability, transparency, and accountability of its actions and decision-making, helps clients manage social and environmental risks and improve performance, and enhances positive development outcomes on the ground.

Section 2: IFC's Commitment

6. IFC's mission is to promote sustainable private sector development in developing countries, helping to reduce poverty and improve people's lives. IFC believes that sound economic growth, grounded in sustainable private investment, is crucial to poverty reduction.

Policy on Social and Environmental Sustainability

April 30, 2006

7. In order to accomplish its mission, IFC seeks to base partnerships with clients on the understanding that the pursuit of social and environmental opportunities is an integral part of good business. Socially and environmentally responsible businesses can enhance clients' competitive advantage and create value for all parties involved. IFC believes that this approach also helps to promote the long-term profitability of investments in emerging markets and to enable IFC to fulfill its development mandate and strengthen the public's trust in IFC.

8. Central to IFC's development mission are its efforts to carry out its investment operations and advisory services in a manner that "do no harm" to people or the environment. Negative impacts should be avoided where possible, and if these impacts are unavoidable, they should be reduced, mitigated or compensated for appropriately. In particular, IFC is committed to ensuring that the costs of economic development do not fall disproportionately on those who are poor or vulnerable, that the environment is not degraded in the process, and that natural resources are managed efficiently and sustainably. IFC believes the client's regular engagement with local communities about matters that directly affect them plays an important role in avoiding or reducing harm to people and the environment. IFC also recognizes that the roles and responsibilities of the private sector in respecting human rights are emerging as an important aspect of corporate social responsibility. The Performance Standards, developed by IFC to help private sector clients address environmental and social risks and opportunities, are consistent with these emerging roles and responsibilities.

9. Accordingly, IFC endeavors to invest in sustainable projects that identify and address economic, social and environmental risks with a view to continually improving their sustainability performance within their resources and consistent with their strategies. IFC seeks business partners who share its vision and commitment to sustainable development, who wish to raise their capacity to manage their social and environmental risks, and who seek to improve their performance in this area.

Section 3: IFC Roles and Responsibilities

10. In its operations, IFC expects clients to manage the social and environmental risks and impacts of their projects. This entails the client's assessment of these risks and impacts, and implementation of measures to meet the requirements of the Performance Standards. An important component of the client's management of its social and environmental performance is the client's engagement with the affected communities through disclosure of relevant project information, consultation, and informed participation, as stated in Performance Standard 1.

11. IFC's role is to review the client's assessment; to assist the client in developing measures to avoid, minimize, mitigate or compensate for social and environmental impacts consistent with the Performance Standards; to categorize the project in order to specify IFC's institutional requirements to disclose to the public project-specific information; to help identify opportunities to improve social and environmental outcomes; and to monitor the client's social and environmental performance throughout the life of IFC's investment. IFC also discloses information relating to its own institutional and investment activities in accordance with its Policy on Disclosure of Information. IFC implements these process requirements through its Environmental and Social Review Procedure.

12. The foregoing general approach applies to IFC's direct investments at both the corporate and project levels, including equity investments. Investments through financial intermediaries and advisory work have separate procedures for applying the Performance Standards (see paragraphs 27 through 30 below). IFC's internal procedure for the application of these Performance Standards through its different types of investments and operations are set out in the Environmental and Social Review Procedure.

Social and Environmental Review

Overall Approach

13. When a project is proposed for financing, IFC conducts a social and environmental review of the project as part of its overall due diligence. This review is appropriate to the nature and scale of the project, and commensurate with the level of social and environmental risks and impacts. IFC reviews any new business activity that is being considered for IFC financing, whether in the pre-construction, construction, or operational stage. The scope of the review may be expanded to other business activities of the client as part of IFC's risk management considerations. Where there are significant historical social or environmental impacts associated with the project, including those caused by others, IFC works with its client to determine possible remediation measures.

14. The effectiveness and efficiency of the social and environmental review depend partly on the timing of IFC's involvement. When this involvement occurs in the early stages of project design, IFC is able to support the client more effectively in anticipating and addressing specific risks, impacts and opportunities, and help build its capacity to manage these throughout the life of the project.

15. The social and environmental review includes three key components: (i) the social and environmental risks and impacts of the project as assessed by the client; (ii) the commitment and capacity of the client to manage these expected impacts, including the client's social and environmental management system; and (iii) the role of third parties in the project's compliance with the Performance Standards. Each of these components helps IFC to ascertain whether the project can be expected to meet the Performance Standards. In the case of projects with significant adverse impacts on affected communities, IFC also assures itself that there is broad community support for the project within the affected communities (see paragraphs 19 and 20 below). IFC bases its review on the client's Social and Environmental Assessment. In cases where such Assessment does not meet the requirements of Performance Standard 1, IFC requires the client to undertake additional Assessment or, where appropriate, to commission Assessment by external experts.

16. IFC's social and environmental review is integrated into IFC's overall assessment of the project, including the assessment of financial and reputational risks. IFC also considers whether its investment can be expected to contribute to the development of the host country and to broadly benefit its relevant constituencies in economic, social, or environmental terms. Through weighing these costs and benefits, IFC articulates its rationale and project-specific conditions for the proposed investment. These are provided to IFC's Board of Directors when the project is presented for approval.

17. IFC does not finance new business activity that cannot be expected to meet the Performance Standards over a reasonable period of time. In addition, there are several types of activities that IFC does not finance. A list of these activities can be found in the Exclusion List in the Environmental and Social Review Procedure.

Categorization of Projects

18. As part of its review of a project's expected social and environmental impacts, IFC uses a system of social and environmental categorization to: (i) reflect the magnitude of impacts understood as a result of the client's Social and Environmental Assessment; and (ii) specify IFC's institutional requirements to disclose to the public project specific information prior to presenting projects to its Board of Directors for approval in accordance with Section 12 of the Disclosure Policy. These categories are:

Policy on Social and Environmental Sustainability

April 30, 2006

- **Category A Projects:** Projects with potential significant adverse social or environmental impacts that are diverse, irreversible or unprecedented
- **Category B Projects:** Projects with potential limited adverse social or environmental impacts that are few in number, generally site-specific, largely reversible and readily addressed through mitigation measures
- **Category C Projects:** Projects with minimal or no adverse social or environmental impacts, including certain financial intermediary (FI) projects with minimal or no adverse risks
- **Category FI Projects:** All FI projects excluding those that are Category C projects (see paragraphs 27 through 29 below)

Community Engagement and Broad Community Support

19. Effective community engagement is central to the successful management of risks and impacts to the affected communities. Through the Performance Standards, IFC requires clients to engage with affected communities through disclosure of information, consultation, and informed participation, in a manner commensurate with the risks to and impacts on the affected communities.

20. IFC is committed to working with the private sector to put into practice processes of community engagement that ensure the free, prior, and informed consultation of the affected communities. Building on this commitment, when clients are required to engage in a process of free, prior, and informed consultation, IFC reviews the client's documentation of the engagement process. In addition, through its own investigation, IFC assures itself that the client's community engagement is one that involves free, prior, and informed consultation and enables the informed participation of the affected communities, leading to broad community support for the project within the affected communities, before presenting the project for approval by IFC's Board of Directors. Broad community support is a collection of expressions by the affected communities, through individuals or their recognized representatives, in support of the project. There may be broad community support even if some individuals or groups object to the project. After the Board approval of the project, IFC continues to monitor the client's community engagement process as part of its portfolio supervision.

Sector-Specific Initiatives on Governance and Disclosure

21. In the extractive industries and infrastructure sectors in particular, where a project can have potentially broader implications for the public at large, IFC recognizes the importance of assessment of governance risks and disclosure of information as a means to manage governance risks. Accordingly, subject to applicable legal restrictions, IFC has the following sector-specific initiatives on disclosure of project-related information, in addition to the disclosure requirements specified in Performance Standard 1.

Extractive Industry Projects

22. When IFC invests in extractive industry projects (oil, gas and mining projects), IFC assesses the governance risks to expected benefits from these projects. In the case of significant projects (those expected to account for ten percent or more of government revenues), risks are appropriately mitigated, and for smaller projects, the expected net benefits of projects and the risks to these from weak governance are reviewed. Where the balance of benefits and risks is not acceptable, IFC does not support such projects. IFC also promotes transparency of revenue payments from extractive industry projects to host governments. Accordingly, IFC requires that: (i) for significant new extractive industries projects, clients publicly disclose their material project payments to the host government (such as royalties, taxes, and profit sharing), and the relevant terms of key agreements that are of public concern, such as host government agreements (HGAs) and intergovernmental agreements (IGAs); and (ii) in addition, from January 1, 2007, clients of all IFC-financed extractive

industry projects publicly disclose their material payments from those projects to the host government(s).

Infrastructure Projects

23. When IFC invests in projects involving the final delivery of essential services, such as the retail distribution of water, electricity, piped gas, and telecommunications, to the general public under monopoly conditions, IFC encourages the public disclosure of information relating to household tariffs and tariff adjustment mechanisms, service standards, investment obligations, and the form and extent of any ongoing government support. If IFC is financing the privatization of such distribution services, IFC also encourages the public disclosure of concession fees or privatization proceeds. Such disclosures may be made by the responsible government entity (such as the relevant regulatory authority) or by the client.

Managing Third Party Performance

24. At times, the client's ability to achieve social or environmental outcomes consistent with the Performance Standards will be dependent on third party activities. A third party may be a government agency as a regulator or contract party, a principal contractor or supplier with whom the project has a substantial involvement, or an operator of an associated facility (as defined in Performance Standard 1).

25. IFC seeks to ensure that the projects it finances achieve outcomes consistent with the Performance Standards, even if the outcomes are dependent upon the performance of third parties. When the third party risk is high, and when the client has control or influence over the actions and behavior of the third party, IFC requires the client to collaborate with the third party to achieve the outcomes consistent with the Performance Standards. Specific requirements and options will vary from case to case.

Project Monitoring

26. After IFC financing is committed in legal documents and disbursed, IFC carries out the following actions to monitor its investments as part of its portfolio supervision:

- Require the project to submit periodic Monitoring Reports on its social and environmental performance as agreed with IFC
- Conduct site visits of certain projects with social and environmental risks and impacts
- Review project performance on the basis of the client's commitments in the Action Plan, as reported by the client's Monitoring Reports, and, where relevant, review with the client any performance improvement opportunities
- If changed project circumstances would result in adverse social or environmental impacts, work with the client to address them
- If the client fails to comply with its social and environmental commitments, as expressed in the Action Plan or legal agreement with IFC, work with the client to bring it back into compliance to the extent feasible, and if the client fails to reestablish compliance, exercise remedies when appropriate
- Encourage the client to report publicly on its social, environmental and other non-financial aspects of performance, in addition to reporting on the Action Plan as required by Performance Standard 1
- Encourage the client to continue to meet the Performance Standards after IFC's exit from the project

Investments through Financial Intermediaries

27. IFC is committed to supporting sustainable capital market development and has a significant program of investment that is implemented through financial intermediaries (FIs). Through this program, IFC helps strengthen domestic capital markets that support economic development at a scale of enterprise that is smaller than would be possible through direct IFC investments. IFC's FI clients are engaged in a diverse range of activities, including project finance, lending to large, medium and small businesses, microfinance, trade finance, housing finance, and private equity, each with its own social and environmental risk profile.

28. Through its Environmental and Social Review Procedure, IFC reviews the business of its FI clients to identify activities where the FI could be exposed to social and environmental risk as a result of its investments. IFC's requirements for the FI client will be proportional to the level of potential risk:

- FIs with business activities that have minimal or no adverse social or environmental risks will be considered Category C projects and need not apply any specific requirements
- All other FIs will apply the Exclusion List
- In addition to the Exclusion List, FIs providing long-term corporate finance or project finance will require the recipient of such finance to:
 - (i) follow national laws where the activity financed presents limited social or environmental risks; and
 - (ii) apply the Performance Standards where the activity financed presents significant social or environmental risks

29. The FI will be required to establish and maintain a Social and Environmental Management System to ensure that its investments meet IFC's requirements, and IFC will monitor the FI's performance on the basis of the Management System.

Advisory Services

30. IFC provides advisory services that range from advice in connection with large-scale industry privatizations to grass-roots support for small enterprises. IFC funds some of these services directly, and in other cases leverages funds from donor-funded facilities. These donor-funded facilities have their own operating procedures, including how they manage social and environmental issues. When IFC is providing advice for large-scale investment projects, the Performance Standards are used as a reference in addition to national laws. IFC does not provide advice to support activities that are described in IFC's Exclusion List, and encourages recipients of IFC's advisory services to enhance opportunities to promote good social and environmental practices.

Section 4: Compliance Advisor/Ombudsman

31. IFC supports its clients in addressing social and environmental issues arising from their projects by requiring clients to set up and administer appropriate mechanisms or procedures to address project-related grievances or complaints from people in the affected communities. In addition to these project-level mechanisms and procedures, the role of administrative or legal procedures available in the host country should be considered. Nonetheless, there may be cases where grievances and complaints from those affected by an IFC-financed project are not fully resolved at the project level or through other established mechanisms.

Policy on Social and Environmental Sustainability

April 30, 2006

32. Recognizing the importance of accountability and that the concerns and complaints of project-affected people should be addressed in a manner that is fair, objective, and constructive, a mechanism has been established through the Compliance Advisor/Ombudsman (CAO) to enable individuals and communities affected by IFC projects to raise their concerns to an independent oversight authority.

33. The CAO is independent of IFC management and reports directly to the President of the World Bank Group. The CAO responds to complaints from those affected by IFC-financed projects and attempts to resolve them through a flexible problem-solving approach, and to enhance the social and environmental outcomes of projects. In addition, the CAO oversees audits of IFC's social and environmental performance, particularly in relation to sensitive projects, to ascertain compliance with policies, guidelines, procedures, and systems.

34. Complaints may relate to any aspect of an IFC-financed project that is within the mandate of the CAO. They can be made by any individual, group, community, entity, or other party affected or likely to be affected by the social or environmental impacts of an IFC-financed project. Complaints should be submitted to the CAO in writing to the address below:

Compliance Advisor/Ombudsman
International Finance Corporation
2121 Pennsylvania Avenue NW
Room F11K-232
Washington, DC 20433 USA

Tel: 1 202 458 1973

Fax: 1 202 522 7400

E-mail: cao-compliance@ifc.org

35. The CAO receives and addresses complaints in line with the criteria set out in the Operational Guidelines for the CAO. The CAO's Operational Guidelines are available at the CAO's web site:

www.cao-ombudsman.org

Section 5: Resources for Policy Implementation

IFC Client Support and Funding Programs for Social and Environmental Sustainability

36. In conjunction with its financing of projects, IFC can mobilize in-house capacity to provide hands-on support to clients that seek to improve their social and environmental performance, particularly those with limited capacity and resources, including small and medium enterprises. Where needed, IFC is also prepared to work closely with international financial institutions and the private sector on project and policy issues related to sustainability. In addition, IFC may make funding available to support its clients' social and environmental initiatives and programs.

Client Support Services

37. IFC provides client support, capacity building, and value-adding services in the social and environmental area, subject to its assessment of the client's capacity and available resources. These services include assistance with Social and Environmental Assessment for small and medium-size clients; assistance with identifying opportunities to enhance social and environmental outcomes;

Policy on Social and Environmental Sustainability

April 30, 2006

discussion with national environmental protection agencies or other relevant regional, national or local agencies on project -specific issues at the request of the client; mobilization of IFC's network of external consultants and experts; and advice on good practice to improve project performance.

38. IFC provides support for training of FI clients to facilitate the adoption and consistent application of a Social and Environmental Management System, and to enhance their social and environmental performance. The training includes programs to: (i) raise awareness of social and environment risks that the client may face; (ii) establish a Social and Environmental Management System appropriate to the client's business; and (iii) help clients identify business opportunities, for example, through market identification and new financial products.

Funding for Social and Environmental Initiatives

39. IFC may make financial assistance available to support its clients' social and environmental initiatives and programs. This may include helping clients improve their social and environmental performance beyond the requirements of the Performance Standard; financing innovative projects that promote local environmental benefits; supporting innovative projects with global environmental benefits, including conservation of biodiversity; and purchasing carbon credits from projects in emerging markets that reduce greenhouse gas emissions.

Liaison with Public and Private Sector Institutions

40. IFC's position as an arm of the World Bank Group focusing on the private sector, together with its extensive network among private sector and international financial institutions, enables IFC to liaise with public and private sector stakeholders to promote a broader dialogue on sustainable private sector financing in emerging markets. The following are examples of IFC's liaison role:

- Identification and dissemination of private sector best practices in the social and environmental area
- Promotion of sustainable financial markets in developing countries through the Equator Principles, and through engaging private equity managers and financial analysts, and using other financial market mechanisms
- Playing the role of the lead bank on social and environmental matters in syndicated loans and joint projects with other international financial institutions, promoting close coordination and harmonization among the participating institutions
- Liaison and coordination with the World Bank on country systems, or the social or environmental aspects of national policy or enforcement or monitoring issues
- Liaison with relevant international financial institutions or national agencies on strategic, regional, or sectoral environmental assessment where appropriate for private sector projects with significant social or environmental issues
- Liaison and coordination with external partners and initiatives, such as the UN Global Compact, to enhance the social and environmental sustainability of private sector projects
- Formal notification to countries potentially affected by the transboundary effects of proposed project activities, to help those countries determine whether the proposed project has the potential for causing adverse effects through air pollution or deprivation of water from or pollution of international waterways

Additional Supporting Documents for Policy Implementation

41. In addition to the Performance Standards, IFC uses other policy, procedure, guidelines, and guidance materials to assist its staff and clients in achieving social and environmental sustainability

Policy on Social and Environmental Sustainability

April 30, 2006

in projects in emerging markets. For example:

- IFC's institutional disclosure of information will be carried out pursuant to IFC's Policy on Disclosure of Information
- IFC's internal procedure to address social and environmental issues through different types of investment and advisory services can be found in the Environmental and Social Review Procedure
- The Guidance Notes, corresponding to the Performance Standards, offer helpful guidance on the requirements contained in the Performance Standards, including reference materials, and on good sustainability practices to improve project performance
- The guidelines on sector and industry practices and performance levels consistent with Performance Standard 3 can be found in IFC's Environmental, Health and Safety Guidelines
- Good practice notes and handbooks disseminate examples of good practice and reference information about these practices

These documents are available at:

www.ifc.org/enviro

Resources on IFC's approach to sustainability are available at:

www.ifc.org/sustainability