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IFC's Policy and Performance Standards on Social and Environmental Sustainability and Policy on Disclosure of Information:

Report on the First Three Years of Application

International Finance Corporation

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IFC'S POLICY AND PERFORMANCE STANDARDS ON SOCIAL AND ENVIRONMENTAL SUSTAINABILITY AND POLICY ON DISCLOSURE OF INFORMATION: REPORT ON THE FIRST THREE YEARS OF APPLICATION

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ACRONYMS

AMC	Asset Management Company
BCS	broad community support
CAO	Compliance Advisor Ombudsman
CES	IFC's Environment and Social Development Department
CESES	CES Policy & Quality Assurance Division
CESI	CES Investment Support Divisions
CGF-FMS	Global Financial Markets-Financial Markets Sustainability team
CODE	Committee on Development Effectiveness
DOTS	Development Outcomes Tracking System
DP	Disclosure Policy
E&S	environmental and social
EBRD	European Bank for Reconstruction and Development
EDFIs	European Development Financial Institutions
EHS Guidelines	Environmental, Health and Safety Guidelines
EP	Equator Principles
EPFIs	Equator Principles Financial Institutions
ESRD	Environmental and Social Review Document
ESRP	Environmental and Social Review Procedure
ESRS	Environmental and Social Reviews and Mitigation Measures
ESRR	Environmental and Social Risk Rating
FI	financial intermediaries
FPIC	free, prior and informed consultations
IDA	International Development Association
IEDR	Independent Evaluation of Development Results
IEG	Independent Evaluation Group
MIGA	Multilateral Investment Guarantee Agency
OECD	Organization for Economic Co-operation and Development
PS	Performance Standards
QA	quality assurance
QC	quality control
SEMS	Social and Environmental Management System
STEP	Sustainability Training and E-Learning Program
WB	World Bank
WBG	World Bank Group
XPSR	Expanded Project Supervision Report

IFC's Policy and Performance Standards on Social and Environmental Sustainability and Policy on Disclosure of Information: Report on the First Three Years of Application

EXECUTIVE SUMMARY

This report updates the Board's Committee on Development Effectiveness (CODE) on the International Finance Corporation's (IFC) implementation of the Policy and Performance Standards on Social and Environmental Sustainability (the Sustainability Policy and Performance Standards) and the Policy on Disclosure of Information (the Disclosure Policy). This new policy framework was approved by the Board on February 21, 2006 and came into effect on April 30, 2006. This report responds to the Board's request, at time of approval, for a review after three years of implementation.

The report considers three years of experience with the new policy framework and assesses the effectiveness of implementation through analysis of the impacts on IFC and its clients, on projects that IFC finances, and on market practices. The report also proposes an approach and timeline for reviewing and updating the Performance Standards and Disclosure Policy.

For the period covered in this report, approximately 560 projects have been presented to the Board for approval, amounting to more than $25 billion in investments. Performance Standards projects now represent 25% of IFC's portfolio in terms of number of projects.

IFC has developed good insights into how the framework applies and how it performs at the project appraisal and approval phases. Based on the report findings:

- IFC considers the framework to be sound and effective. It does not hinder IFC's business and helps with risk management.
- The Performance Standards framework is adaptable even in the face of the financial and economic crisis and to different financial instruments.
- Recent annual client survey results show continued satisfaction with IFC on environmental and social matters. Clients did not find implementation to be excessively costly. These conclusions are based on client survey results from over 140 existing clients that apply the Performance Standards.
- Implementation of the disclosure requirements has begun to improve transparency, and increased awareness among stakeholders, regarding IFC's investments and advisory services projects.

The report also identifies a number of implementation lessons and challenges from policy and operational perspectives. IFC's own experience, independent views from IEG and CAO, and ongoing feedback from external stakeholders, such as the financial institutions that apply the Performance Standards, and civil society organizations, have identified challenges, including:

- Managing cross-sectoral global environmental issues such as climate change and biodiversity protection.
- Social development issues such as consultation with affected communities, broad community support, project level disclosure, resettlement, labor issues and retrenchment policies, and human rights.
- Process challenges such as managing financial intermediary risks and differing stakeholder views on how IFC categorizes projects.
- Managing supply chain issues, especially in the agribusiness sector where E&S risks continue to grow in complexity.
- Project categorization, especially for new financial products.

In terms of the impacts on market practices, the Performance Standards have made a positive contribution to the global convergence of E&S risk management practices. There are now 68 financial institutions that have adopted the Equator Principles. Public development financial institutions such as the OECD Export Credit Agencies and European Development Finance Institutions have also publicly referenced the use of the Performance Standards.

Regarding disclosure, the report finds that IFC is generally effective in meeting its institutional requirements, as defined in the Disclosure Policy. However, disclosure of information regarding IFC's activities throughout the life cycle of the project remains inconsistent. Implementation experience also suggests that the degree of disclosure, documented evidence of community engagement, and quality of information disclosed varies across IFC's clients. The result is that stakeholders must often look both to IFC and to clients to piece together a picture of the project, whom it affects, the expected development outcomes, how the project is being implemented, and whether IFC achieved the development goals and outcomes for the project. In particular, there is significant interest in more measurement and reporting of project-level development impact results.

The findings from the report suggest that, on balance, the updates to the policy framework should focus on clarifications to further strengthen the risk management aspects of the framework, and adjustments to address evolving internal and external context, not wholesale revision or addition.

IFC seeks CODE's approval to disclose this report to the public and to initiate the review-and-update process as outlined in the report. The immediate next step would be to begin a process of consultation and communication through an approach paper.

PART I. BACKGROUND, CONTEXT, AND OBJECTIVES

1. **On February 21, 2006, IFC's Board of Directors approved management's proposal to adopt a new policy framework governing the social, environmental, and disclosure of information aspects of IFC's operations.** This new framework consists of:

- Policy on Social and Environmental Sustainability
- Performance Standards on Social and Environmental Sustainability
- Policy on Disclosure of Information

2. **This new policy framework, which became effective on April 30, 2006, is part of IFC's longstanding commitment to sound environmental management and social development,** going back almost 20 years (see Box 1). It reflects IFC's commitment to the sustainability of the projects IFC finances and to its strategic pillar on climate change and environmental and social sustainability. The framework also represents a renewed statement of IFC's commitment to transparency and accountability in the way it conducts its business.

3. **This *Three-Year Report* covers implementation, thus far, of IFC's Policy and Performance Standards on Social and Environmental Sustainability (Performance Standards, or PS) and the Policy on Disclosure of Information (Disclosure Policy, or DP)**. It updates the Board's Committee on Development Effectiveness on the experience and lessons learned in applying this new policy framework, and it responds to the Board's request for a report after three years of implementation.

4. **At an informal meeting on December 13, 2007, the Board reviewed the 18-month progress report on the application of the PS and DP** (IFC/SecM2007-0052). The positive and constructive discussion confirmed the Board's continued support for the new policy framework. Management responded to a number of questions largely related to: the potential cost and impacts of the new framework on IFC's business and its clients; implementation challenges involving new areas introduced by the PS, notably labor issues; areas of historical challenge, such as biodiversity; and the role of

Box 1: Milestones in the Development of IFC's Policy Framework on Social and Environmental Sustainability

- Prior to 1989, the Environment Department of the World Bank reviewed proposed IFC investments in accordance with its policies.
- In 1989, IFC developed its first formal procedure for environmental review of projects. IFC used the 1988 World Bank Guidelines for evaluating project-specific pollution-prevention and -control measures.
- This procedure, effective from March 1990 to December 1992, placed responsibility for review in the hands of IFC's Environmental Advisor, a newly created position.
- In response to the growing portfolio of investments in financial institutions and funds, the environmental category "FI" was introduced in December 1992 as part of the environmental review procedure.
- This procedure was subsequently revised, and a new one was put in place and was effective from September 1993 to September 1998, at which time IFC approved a new version of the Environmental and Social Review Procedure (ESRP).
- In 1998, IFC's Board of Directors also approved the IFC Safeguard Policies (based on World Bank Safeguard Policies). These policies were accompanied by the Pollution Prevention and Abatement Handbook. Additional sector-specific guidelines were developed by IFC on an as-needed basis.
- The IFC Safeguard Policies were replaced by the Policy and Performance Standards on Social and Environmental Sustainability on April 30, 2006. Guidance Notes for interpreting the Performance Standards and an updated ESRP were issued in the same time frame.
- Lessons learned post-April 2006 were incorporated in updated Guidance Notes and ESRP in July 2007, and a third version of the ESRP was issued in February 2009.
- In 2007, the World Bank Group Environment Health and Safety Guidelines were introduced and effectively replaced Part III of the 1998 Pollution Prevention and Abatement Handbook.

IFC regarding the Equator Principles (EP) and the continued expansion of this set of voluntary principles across emerging-market financial institutions and the financial sector more generally. The 18-month progress report noted that the new policy framework appeared to have created positive impacts on IFC's business without creating significant incremental implementation costs (see Box 2).

5. **In August 2008, IFC presented a paper (IFC/R2008-0276) to the Board, proposing a way forward to review and update the policy framework.** The paper proposed that the *Three-Year Report* consider whether the implementation of the PS and the DP is meeting the objectives set out in the new policy framework. The 18-month progress report also noted that the impacts on IFC clients and the projects financed by IFC were only beginning to emerge, and that the *Three-Year Report* would be based on more substantive implementation data. With this in mind, this report sets out to:

- Assess the efficiency and effectiveness with which this new policy framework is being implemented
- Assess the impacts of this policy framework on IFC, the projects IFC finances, IFC clients, as well as impacts on market practice
- Describe the proposed process for reviewing and updating the PS and DP, and lay out in broad terms the emerging agenda that is likely to form the core of the review-and-update process.

Box 2: Key Messages from the 18-Month Progress Report

- Early implementation experience suggests that IFC's implementation of the new policy framework is largely sound, and that the new approach is working to strengthen projects.
- Costs of project processing did not increase significantly for IFC. Seventy-two percent of clients who responded to a survey said that the cost of meeting the Performance Standards would not affect their decision to return to IFC for financing.
- The Performance Standards' tailored approach to risk management, which allows clients and IFC to specify appropriate and relevant requirements in accordance with the level of risk, is resulting in the appropriate level of due diligence.
- In financial markets worldwide, the Performance Standards have catalyzed the swift convergence of practice and standards for cross-border project finance, and this has contributed to a more level playing field.

6. **This report is based on a review of a growing body of work that IFC has carried out under the Performance Standards and Disclosure Policy**. The review is anchored in an internal stocktaking, a review and analysis of implementation data captured through IFC's information management systems, and in an internal consultation process with industry, regional, and corporate departments. The review also captures feedback and firsthand experience from staff that dealt directly with stakeholders and affected communities, as well as feedback received from external practitioners, commentators, and critics through ongoing outreach efforts. A client survey was conducted to assess implications of client costs. IFC has also organized an external advisory group to advise it throughout the PS review-and-update process. This report also highlights opportunities to further strengthen implementation of the policy and operational framework for the additional enhancement of development impacts and outcomes (see Box 3).

7. **The report is structured around four key themes.** Part II of the report provides a brief overview of the strategic, organizational, and operational framework in which the Performance Standards and Disclosure Policy were implemented. Part III presents a summary of three years of implementation experience with the Performance Standards and Disclosure Policy.

Box 3: Key Aspects of IFC's Sustainability Framework

The framework puts into practice IFC's commitment to social and environmental sustainability and clients' environmental and social responsibilities.

Key features of the Sustainability Framework:

- New standards, such as integrated Social and Environmental Assessment and Management System; community-engagement and grievance mechanisms; labor and working conditions; greenhouse gases; and community health, safety, and security
- Expanded standards in areas such as pollution prevention and abatement; land acquisition and involuntary resettlement; protection and conservation of biodiversity; indigenous peoples; and cultural heritage
- Articulation of IFC's roles and responsibilities as a publicly owned development institution
- Articulation of reasonable responsibilities of private sector clients in emerging markets
- Focus on good project outcomes through:
  - the client's social and environmental management system, which incorporates social and environmental standards in its business process
  - a set of broad objectives as outcomes and rationale for the specific requirements of the Performance Standards
  - measures and actions that are proportional to the potential project risks and impacts, and adapted to the particular business of the client

Part IV discusses the impacts and effectiveness of implementation**,** and part V lays out the prospects and strategic outlook that must be considered as IFC enters a process of review and update of the Performance Standards and Disclosure Policy.

8. **This report will also contribute to the growing body of knowledge concerning the implementation of the World Bank Group's commitment to environmental and social sustainability.** It joins other significant review activity on this front: 1) The Independent Evaluation Group (IEG) is reviewing the World Bank Group's experience with the use and implementation of safeguards and performance standards (in IFC and in the Multilateral Investment Guarantee Agency, or MIGA); 2) International Bank for Reconstruction and Development (IBRD) is reviewing its disclosure policy; and 3) IFC's Compliance Advisor and Ombudsman (CAO) has issued an approach paper for its own review of three years of PS and DP implementation. The analysis presented in this report should also benefit the work on the World Bank Group's environment strategy, which has just been initiated.

PART II. STRATEGIC, ORGANIZATIONAL, AND OPERATIONAL FRAMEWORK

A. Strategic and Business Environment

9. **Environmental and social sustainability has been one of IFC's strategic pillars since 2004.** IFC's approach to environmental and social sustainability is grounded in a commitment to sound and sustainable economic growth through private sector development. IFC promotes sustainability through E&S risk-management policies; standards, guidelines and industry good practice; advisory services that bring business solutions to sustainability challenges faced by companies and markets; and a growing volume of investments that are responsive to the opportunities provided by the sustainability agenda. The new policy framework fits into this strategic environment, where sustainability is part of IFC's core commitment to private sector development and an important market differentiator. Since 2006, IFC annual reports have highlighted developments associated with the implementation of the new policy framework. The 2007 Annual Report brought together, for the first time, reporting on financial performance, environmental and social performance, and development impact—the triple bottom line.

10. **IFC believes that transparency and public dissemination of information regarding its activities can strengthen public trust in IFC and its clients, and enhance the development impact of its initiatives.** IFC updated its Disclosure Policy in 2006 to reflect its commitment to enhancing transparency of its activities and promoting good governance. The guiding principle in the new policy is a presumption in favor of disclosure. The updated DP clarified IFC's responsibility and the client's responsibility for local disclosure, as described in Performance Standard 1 (Social and Environmental Assessment and Management Systems).

11. **The business environment in which the Performance Standards and Disclosure Policy have been implemented over the three-year period under review has been dynamic.** The first two and a half years were characterized by rapid growth in IFC's business across most industry sectors and regions. During this period, industry sector growth was most rapid in infrastructure and financial markets and funds, while regional growth has been more broad-based, although most pronounced in Africa, Latin America, and South Asia regions. Furthermore, the nature of IFC's products, and the balance between them, has continued to evolve, with traditional project-finance activities representing a smaller share of new business. The role of equity and corporate finance in IFC's product mix has become more significant over time. IFC continues to respond to market demand for new financial products and financing structures that are aligned with its private sector development mission and strategic objectives.

B. Organizational and Operational Context

i. Organization

12. **IFC's institutional performance in social and environmental sustainability is a shared responsibility within IFC, and accountability is placed in various functions across the organization, with the ultimate accountability resting with the relevant vice presidents**. Regional and industry directors are responsible for overall performance of IFC's investments, including environmental and social performance. IFC's Environment and Social Development Department (CES) supports investment departments with the environmental and social review of projects, and is accountable to its vice president. Recently, CES's accountability was strengthened

through its quarterly reports on environmental and social performance and risks associated with IFC operations to the Corporate Risk Committee (a recently established committee of IFC's Management Group). Three independent units oversee IFC's overall accountability, namely Compliance Advisor and Ombudsman, Independent Evaluation Group and Internal Auditing Department. Recommendations from these units pertaining to E&S aspects are tracked by CES and corrective actions and improvements are reported to IFC management.

13. **CES continues to anchor implementation of the Performance Standards, and the Corporate Relations Department oversees implementation of the institutional responsibilities associated with the Disclosure Policy**. To better respond to business needs, larger body of staff, and decentralization, CES's original investment support group (known as CESIG) was divided into two divisions, CESI1 and CESI2 (referred to jointly as CESI), for more focused management attention to E&S risks and issues along industry and regional lines. This reconfiguration, combined with a clearer and stronger mandate for CESI industry and regional team leaders, has strengthened CES's management capacity.

14. **The Policy and Standards Unit, which has coordinated IFC's work on the Performance Standards, was reconfigured as the Policy and Quality Assurance Division.** The shift to full division status recognizes the growing role of policy development and policy-related matters (internal and external to IFC) and the importance of even more effective engagement with stakeholders regarding emerging issues and trends. It also aims to consolidate the quality assurance functions and to expand them beyond process compliance to issue-based, thematic, and regional reviews, effectively broadening the mandate for quality assurance.

ii. Staffing and Capacity

15. **The CESI team supporting the application of the Performance Standards continued to grow (through end-FY08) and to decentralize, in response to IFC's strategic directions and operational priorities**. CESI now consists of a global team of close to 60 specialists and 2 managers. Decentralization has further accelerated since the 18-month progress report and will carry into FY10, when it is expected that nearly 50 percent of specialists will be in country offices.

16. **Training and capacity building—for internal and external audiences—continues to be a key element of the implementation strategy**. In the first three years of implementation, CES delivered PS training to a total of 1,616 IFC and WB staff in 58 face-to-face training sessions. Over 50 percent of training sessions took place in IFC country offices. Of the total participants, 51 percent were investment staff. In addition, 192 staff completed the "Managing Environmental and Social Performance" online course, 56 percent of them in country offices. Staff also received training on the new disclosure requirements. In total, over 1,500 IFC staff members were trained on the basics of the DP, and 40 individuals were nominated and selected to be the disclosure champions of their departments. Training and capacity building of IFC staff continues to be an important area of activity related to PS implementation. CES recently launched a second-generation PS training program.

17. **One of the most notable developments in the last 18 months is the rapid growth in staff support for the appraisal, supervision, and portfolio management of the financial intermediaries (FI) business.** With a global presence, this team of E&S specialists focusing on the

FI business has grown from two staff in FY07 and now consists of five staff and six full time consultants. This growth is due in part to catching up on staffing in response to business needs, and in part to a more formal recognition of the need for FI portfolio supervision and more regular and sustained interaction with clients. The additional resources dedicated to the FI business has been recognized as long overdue in recent IEG reports.

18. **CES developed an FI knowledge-management strategy to address FI capacity needs on E&S risk management**. CES, in close cooperation with IFC's Global Financial Markets Department Sustainability team (CGF-FMS), leveraged IFC's many years of experience in delivering the Competitive Business Advantage sustainability training program for FIs to develop a new client capacity-development strategy and began implementation in FY09. In addition to addressing the main shortcomings of the previous programs, the new strategy includes working with local partners in emerging markets to deliver training programs customized to reflect local market conditions, and deliver them with more regular frequency. An example of one such successful partnership is IFC's memorandum of understanding with the National Institute of Banking Management, the training body for the Indian banking regulator (the Reserve Bank of India). Another core component of the strategy is the recently launched Sustainability Training and E-Learning Program (STEP).

19. **Capacity development will have global reach through the creation of a Web-based toolkit to provide FIs with access to IFC's entire suite of E&S risk-management offerings**, including STEP and guidelines and tools for the financial sector. The toolkit will be designed for use by FIs as well as regional training organizations and consulting firms offering E&S risk-management services to the financial sector. IFC will promote the toolkit to training partners and consultants to develop locally available capacity to support FIs.

a. Environmental and Social Review Procedure

20. **The Environmental and Social Review Procedure (ESRP) outlines management-approved steps for processing proposed investments, thereby operationalizing the policy framework**. These procedures complement the IFC Operational Procedures and are aligned with the investment cycle. The ESRP applies to the full range of IFC's investment activities and provides parameters to guide consideration and documentation of key issues and decisions made during the investment cycle. Guidance in the ESRP is structured according to the sequence of events in the investment project cycle. The ESRP also describes the application methodology to implement IFC's institutional disclosure requirements in accordance with the Disclosure Policy. The procedure describes actions necessary to identify and bridge gaps with the requirements of the Performance Standards. It also describes steps to be taken in case of noncompliance with the PS during the implementation phase. The ESRP has been updated twice since April 30, 2006, to reflect lessons of implementation, a more robust approach to managing environmental and social risk in Advisory Services, delegated authority to regions, and IFC's changing product mix, among others. The requirements for supervision were also updated in accordance with the revised portfolio risk management framework for E&S risk.

b. Environmental and Social Review Document

21. **CES's quality-assurance process incorporates the Environmental and Social Review Document (ESRD), an information-analysis and decision-recording system**. The ESRD facilitates creation of a permanent record of each project, denoting findings and structuring of ameliorative measures throughout the project life cycle, and has a built-in clearance mechanism as outlined in the ESRP. It requires E&S specialists to consider each requirement and theme of each Performance Standard and to score it on a five-point system, as the project stands pre-IFC intervention, thus establishing the baseline Environmental and Social Risk Rating (ESRR) score. Any item that scores "unsatisfactory" must be addressed either prior to investing or through a time-bound action plan. The specialist creates a record for each supervision year to record findings and analysis based on an annual monitoring report, communication with the client (for some low-risk FI clients), or a supervision visit. Outstanding action plans are automatically displayed in the ESRD as a reminder to follow up with clients. Implementation of the ESRD has involved a significant change in practice for E&S specialists with regard to project documentation generation and management, and has been one of the more challenging aspects of the management system. With the experience gained so far, opportunities for streamlining the ESRD have been identified and are under consideration.

22. **The ESRD system was further developed in the last 18 months to accommodate the special needs of the FI business.** The ESRD-FI, launched in January 2009, serves as a workflow-management system that follows requirements of the ESRP for FI operations. The system enables capture of all analysis and decisions related to a project during the entire project cycle. It also enables reports that can show project-level and portfolio-level performance on E&S issues. For FI investments, a management score is derived from supervision analysis and used as a proxy for the Development Outcome Tracking System (DOTS) E&S effects score.

c. Quality Assurance (QA) and Quality Control (QC)

23. **CES's Quality Assurance team performs independent reviews of the quality and completeness of the ESRD, looks for trends in the data, develops support tools for specialists, and produces reports for management**. This information, along with pipeline and portfolio data gathered from various IFC systems, is used as the basis for quarterly reporting by CES to IFC's Management Group (through the Corporate Risk Committee). It includes analysis of the portfolio with regard to E&S performance shifts; identification of trends in sectors, regions, or specific issues; and highlighting of the poorest performing projects. The risk-based supervision program is also developed by the QA team, based on project risk profile and status of available information. The resulting preliminary supervision program is then vetted through discussions with CESI industry and regional team leaders and regional investment officers and portfolio managers. The QA team tracks and reports on implementation of the program on a monthly basis throughout the fiscal year.

24. **The QA and QC functions have been strengthened over the last 18 months.** In addition to the QA functions described above, project-level technical QC is performed at the team-leader level. The CESI team leaders are organized on a regional basis and by industry sectors, and each has terms of reference outlining roles, responsibilities, and authority. This mix allows CESI to be involved at the earliest stages of project consideration.

25. **CES manages a process of peer reviews through which it considers special or difficult project situations, and policy-interpretation issues**. These meetings are an important part of the deliberative process and the quality-assurance framework through which all E&S specialists are invited to participate in a discussion on specific issues raised by a project team. The issues considered in peer review meetings are either linked to risks associated with new or difficult project situations, or are of an interpretational nature or content aspect of the review procedures or the PS or DP.

d. Portfolio Management and Supervision Program

26. **As part of its portfolio-management system, IFC monitors environmental and social performance of its investments and manages associated risk**. Portfolio-management activities include, among others, maintaining current information on regional and industry portfolios and risk profiles (including a high-risk list), onsite visits with clients, desk review of annual monitoring reports, phone interviews, and discussions with clients. The portfolio-management functions were further strengthened in FY09 through the designation of regional team leaders, who assumed responsibility for supervision-program coordination. In 2001, IFC began calculating a project-specific Environmental and Social Risk Rating (ESRR), which is assigned and updated as supervision information on a client's performance is obtained. The ESRR summarizes IFC's current assessment of a company's project-management capacity, inherent riskiness of the industry sector and performance with its legal requirements (such as reporting), and action-plan compliance.

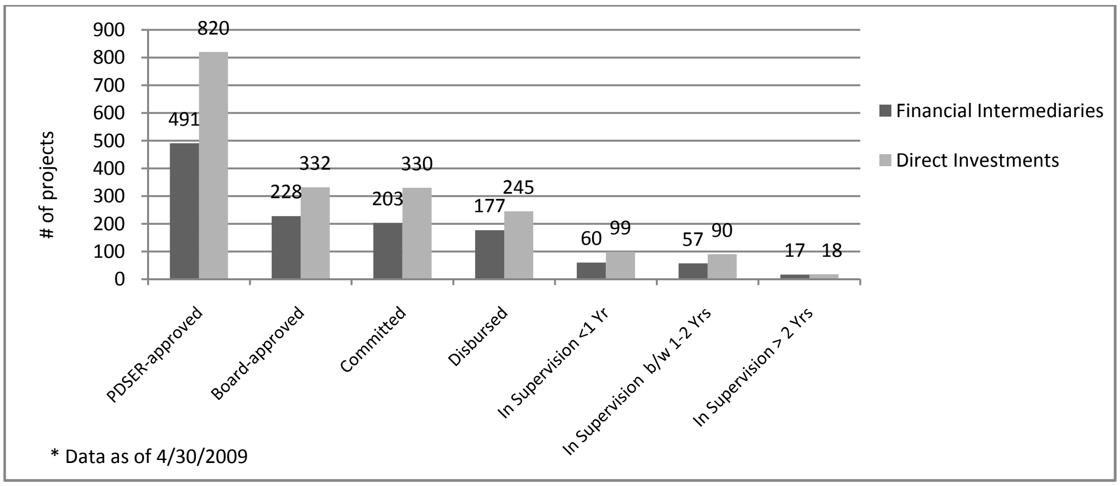
27. **In 2006, IFC management endorsed a revised approach to supervision, which included a dedicated supervision budget and a risk-based supervision program that targeted high-risk projects, poorly performing projects, and projects with limited or missing information**. CES, supporting regional and industry departments, developed a three-year rolling supervision strategy using the ESRR as a relative indicator of project risk and performance, so that high-risk companies and poorly performing companies are visited more frequently. CES conducted over 720 supervisions in the last three fiscal years and reviewed Annual Monitoring Reports which significantly reduced the number of companies with no or limited E&S performance information. The E&S information indicator, referred to as the E&S knowledge gap, is one of the indicators that CES tracks and reports on to the Corporate Risk Committee.

PART III. IMPLEMENTATION EXPERIENCE

A. The Performance Standards Project Portfolio

28. **Over 1,300 projects have been screened so far against the Performance Standards**, as denoted by the PDS-ER[1] volume in Figure 1 between May 1, 2006 and April 30, 2009. Out of these projects, 560 projects were approved by the Board, of which 422 had reached first disbursement stage. The PS project portfolio nonetheless remains young, with only 35 Board-approved PS projects having completed more than two years of implementation (post-disbursement). About 30 percent of Board-approved PS projects have been in implementation for over a year (post-disbursement).

Figure 1: Progression of Projects Through Project-Cycle Stages



29. **IFC has accumulated valuable operational experience with the Performance Standards at the screening, preparation, and Board-approval stages.** The experience post-disbursement remains nonetheless limited. It will be another three years before the first PS projects reach operational maturity and begin to be captured in IFC's program of Expanded Project Supervision Reports (XPSRs).[2] However, IFC's environmental and social project-supervision program is capturing operational experience more effectively, earlier, and more comprehensively than in the past. An important part of the supervision program is early and sustained supervision of higher-risk projects, a further contributor to portfolio knowledge and PS experience.

30. **Despite rapid growth in IFC's business during the period under review, the portfolio (post-disbursement) is still dominated by projects that were approved prior to the introduction of the PS and new DP**. The PS project portfolio of disbursed projects represents about 25 percent of IFC's current portfolio on a number-of-projects basis. Projects processed under the safeguards framework continue to form the bulk of the portfolio. This is likely to be the case for another three years. This transition period highlights the importance of developing

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[1] PDS-ER (project document system–early review) is part of IFC's project documentation cycle and effectively indicates entry into IFC's project pipeline.

[2] XPSRs assess the appraisal and supervision quality and the private sector impact of IFC portfolio projects that have reached operational maturity, typically five years of implementation after Board approval.

tools, instruments, and systems that can be deployed for the benefit of the entire portfolio. Although the first 18 months of PS implementation saw a number of project approvals grandfathered under the safeguards framework, the transition to the PS had been completed by the beginning of the second 18-month period.

B. Overview of Implementation

i. Business Development

31. **Distribution of Board-approved projects by E&S category remains consistent with previous years.** The breakdown of project approval by E&S risk category is presented in Table 1. Category FI projects, representing about 40 percent of approvals by the number of projects, is slightly higher than the 35 percent at the end the first 18-month period. At first glance, the number of category A projects appears to be low, but historically (FY98–08) they have represented 1–4 percent of IFC projects. Since 2005, the number has remained toward the lower end of this range, largely due to the growth of FI investments, which reduced non-FI projects proportionally. However, the number of category A projects doubled in the second 18-month period, from 5 to 14, consistent with the lead time required for preparation of these typically more complex projects. The shift from a process-driven to impact-based system of social and environmental categorization has been operationally successful but some challenges still remain, for instance, with projects whose parameters are largely unknown at the outset. IFC's system of categorization is dependent on defined project activities, boundaries and timelines, as well as expected types and levels of impacts, and the identity of those who receive the impacts, including the affected communities. The challenge is most pronounced in cases of exploration equity and investment facilities, where little is known about the eventual physical attributes of the projects at the time of the initial IFC due diligence, and where neither category A nor B conveys an adequate measure of the future potential impacts. In addition, categorization has also been a source of questions from some stakeholders. This indicates that the current system of categorization should be examined, keeping in mind that any change to the system might create disruption not only within the WBG but also among the financial community that uses the system. The following sections examine selective aspects of IFC's implementation experience for direct investment (or real sector projects) and for FI operations.

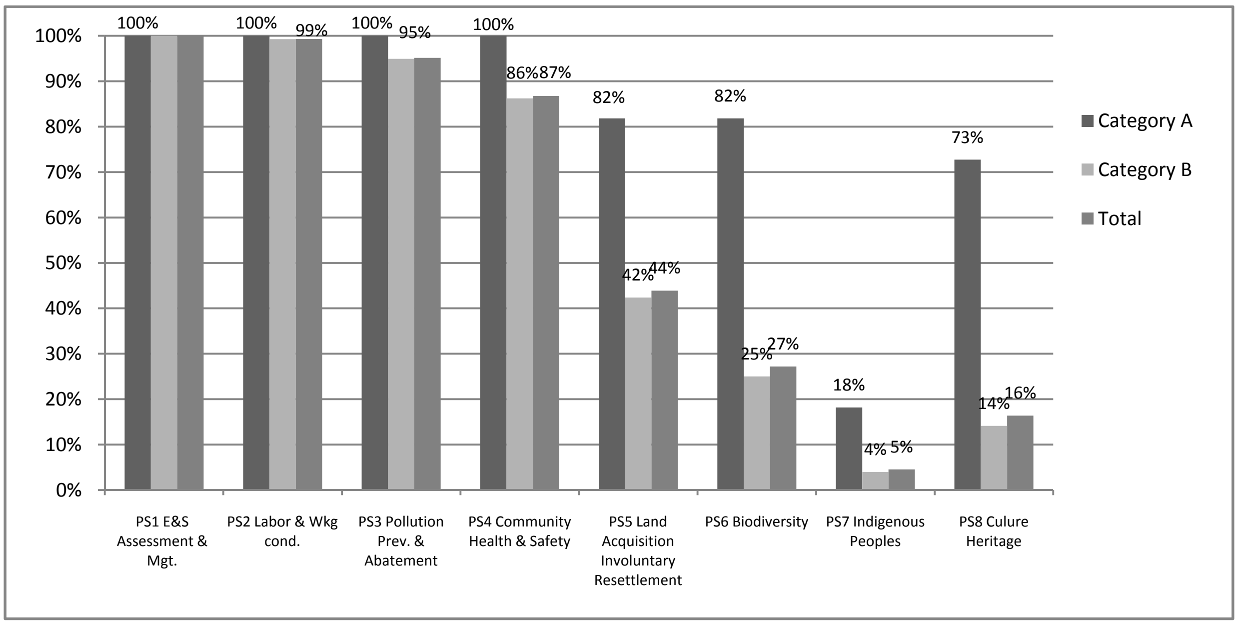
Table 1: Board-Approved Projects Applying the Performance Standards—by Environmental and Social Category

E&S Category	PS projects that have received Board Approval	
	No. of Projects	%
Category A	14	2.5%
Category B	276	49.3%
Category C	47	8.4%
Category FI	223	39.8%
Total	**560**	**100%**

a. Direct Investments

32. **Performance Standards 1–4 represent the core standards that are applied most frequently across all sectors, regions, and types of projects.** Figure 2 shows the frequency of application of each of the Performance Standards for direct investment projects (non-FI projects), representing 290 category A and B projects approved in the three-year period. These results are consistent with findings from the 18-month progress report. Performance Standards 5–8 are more specialized, and their application depends on specific project circumstances. PS1 (Social and Environmental Assessment and Management Systems) and PS2 (Labor and Working Conditions) are triggered in practically every project. The numbers drop slightly for PS3 (Pollution Prevention and Abatement) and PS4 (Community Health, Safety and Security) for category B projects. PS7 (Indigenous Peoples) is the least triggered of the Performance Standards. The following paragraphs highlight the most notable aspects of the implementation experience to date and areas of challenge for IFC and/or its clients.

Figure 2: Triggering of the Performance Standards



33. **Overall, implementation experience confirms that a management-system-based approach is an effective way to structure and manage E&S issues at the enterprise level, and clients see significant value in this approach** (discussed in Part IV). However, experience gained during the first three years of implementation suggests that some clarifications to Performance Standard 1 (Social and Environmental Assessment and Management Systems) are warranted, including clearer definitions of the E&S management plan, program, and system. These three concepts are sometimes misunderstood by clients. Experience also suggests that the requirement of an emergency preparedness plan would be better understood as part of the E&S management system rather than as a separate requirement under PS3 and PS4.

34. **During the February 2006 Board discussion of the Performance Standards, several Executive Directors expressed a special interest in the application of free, prior and informed consultations (FPIC) and broad community support (BCS)**. PS 1 requires that

sponsors of projects with potentially adverse impacts on communities conduct FPIC, but IFC must determine, prior to Board approval, whether BCS exists for such projects. The FPIC and BCS requirements are most easily understood and implemented in relation to greenfield projects, where the demarcation of the project's environmental footprint is clear and where impacts on the communities are direct. Implementation experience indicates that it is more complex to determine BCS in expansion and retrofit cases where companies have been in operation for some time, especially if E&S performance has varied over time. To date, 21 projects (14 category A and 7 category B) have applied the FPIC/BCS requirement. BCS is a snapshot that documents IFC's judgment on the community's support for the project at a particular time—right before project presentation to the Board. It should not be assumed that BCS is granted indefinitely, and depending on the project's performance over time, the community's perception of the project may change. Experience with the BCS timeline and the post-approval aspects requires closer examination as well as more explicit definition of BCS requirements for the different investment products. To support effective application of this requirement by IFC clients, IFC produced a *Handbook on Stakeholder Engagement* and a *Good Practice Note on Grievance Mechanisms* (forthcoming).

35. **Performance Standard 2 (Labor and Working Conditions) has been broadly applied across regions and sectors, though the requirements have been challenging for some clients, particularly in countries where enforcement of national laws is weak or where such laws do not exist.** Requirements on collective bargaining and workers' organizations, as well as supply chain issues have proved to be challenging. The issue of migrant workers, often hired indirectly through contractors, is another area of challenge for clients. Clarifications on working and living conditions of "nonemployee" workers might be needed. Moreover, in a time of economic crisis and shrinking labor market, the role of PS2 in the context of large-scale retrenchment should be considered.

36. **Ongoing training and capacity building have supported the strengthening of PS2 implementation.** IFC has been hiring new staff with PS2 skill sets, in addition to improving the skills of E&S specialists through custom-designed training courses. As awareness increases, comprehensive labor audits of more complex projects are being required on a more frequent basis. To date, 17 projects have undergone labor audits, and an additional 4 are in the planning or execution stage. IFC has published a number of knowledge products to promote good practice under PS2, including a *Labor Toolkit*, a practical screening and due diligence tool for project review by financial institutions; two *Good Practice Notes* (on retrenchment and on discrimination); and *Guidelines on Working Accommodation*, jointly with the European Bank for Reconstruction and Development (EBRD). In addition, CES established a labor advisory group, consisting of practitioners from leading institutions, enterprises, and labor unions. Members of this group had advised IFC on labor issues in general and on PS2-related matters, and met three times.

37. **Regarding Performance Standard 3 (Pollution Prevention and Abatement), IFC lead a WBG-wide effort to review and update the WBG *Environment, Health and Safety Guidelines*.** Since the 18-month progress report, seven new guidelines were added as part of the updated series. This brings to 63 the number of guidelines published since the Performance Standards were introduced. The guidelines are intended to provide a technical reference for IFC

staff and clients, and to promote the use of good international industry practice in pollution prevention and abatement. The *EHS Guidelines* are also widely used and referenced by governments, financial institutions, and industry the world over.

38. **PS3 establishes a reporting requirement on greenhouse gas (GHG) emissions in excess of 100,000 tons per annum CO_2 equivalent**. PS3 also requires that alternatives be considered if emissions are above that threshold, and that energy efficiency measures be explored. This reporting requirement has been triggered by 37 projects (3 category A and 34 category B). Sixteen of these projects were in general manufacturing and services sector (cement, paper, and glass production), ten in chemicals, oil, gas and mining, eight in infrastructure (thermal power and air transportation), and three in agribusiness (sugar production). Twelve of these projects were located in East Asia, eight in Latin America, five in Eastern Europe and Central Asia, five in South Asia, three in Middle East, two in South Eastern Europe, and two in Africa. The IFC Carbon Emissions Estimation Tool (IFC-CEET) has been developed to assist industry departments and clients with calculating project emissions. This calculator is based on the GHG Protocol, established by the World Business Council for Sustainable Development and the World Resources Institute.

39. **Performance Standard 4 (Community Health, Safety and Security) places a wide range of requirements on IFC's clients to ensure safety of communities.** Several of these requirements were not explicitly covered under the previous safeguards framework. Some examples of issues that have triggered PS4 include projects that could potentially introduce communicable diseases into project areas due to influx of migrant workers; projects where community participation was essential to prepare and respond to emergency situations, such as those related to the transport of dangerous goods through community roads, or related to major hazards from certain industrial facilities (mines, chemical plants, cement plants, etc.); and projects that required use of security forces.

40. **Implementation of PS4 has required internal capacity building on issues related to the management of security forces by IFC clients, and the use of health impact assessment as part of the E&S public or private due diligence process**. CES developed and delivered internal training programs and carried out a significant update of the *Guidance Note* to reflect the importance of health issues in communities, and of issues related to security forces. In addition, a handbook *Introduction to Health Impact Assessment* was published to provide guidance to IFC staff and clients.

41. **Meeting the full requirements of Performance Standard 5 (Land Acquisition and Involuntary Resettlement) on resettlement due to land acquisition continued to be challenging for many clients**, particularly in countries that have legally specified compensation levels that are below market reference point, and in countries where the resettlement process is exclusively the domain of government. Furthermore, meeting the requirement related to displaced people who have no recognizable legal right or claim to the land remains a difficult area of implementation for private sector clients. Nonetheless, implementation data shows that private sector companies do get involved in various forms of resettlement to ensure good outcomes at the project level, often working closely with governments, as encouraged by PS5. The total number of projects that triggered PS5 appears high at 126, because only 23 of the 126

projects involved any kind of resettlement. A review is under way to access whether the PS was regularly triggered on precautionary basis. Implementation experience has also highlighted the issue of influx and the pressure this creates on land and potential issues to be managed under PS5. To strengthen capacity of consultants working with IFC and its clients, CES designed a "Land Acquisition and Resettlement" training course, piloted in Latin America and the Caribbean in FY09. Similar sessions for other regions are scheduled for FY10.

42. **A challenge in implementing Performance Standard 6 (Biodiversity Conservation and Sustainable Natural Resource Management) has been the collection of, or access to, biodiversity baseline information.** In some cases, baseline data must cover several seasons or even years over an appropriate geographic to be meaningful. For projects triggering the PS6 critical-habitat requirement, CES has required additional data collection to make an adequate judgment, a process that is often very difficult and time consuming and has sometimes led to project processing delays. IFC has also begun to examine the critical habitat definition to see if it reflects the most current scientific approach. To address the operational challenges, CES is developing a guidance note and new tools for identifying critical habitats and related client requirements more effectively. The *Integrated Biodiversity Assessment Tool*—developed originally by a consortium of United Nations Environment Programme-World Conservation Monitoring Centre, Birdlife International, Conservation International, and International Union for the Conservation of Nature—will be adapted to help address PS6 requirements.

43. **Performance Standard 7 (Indigenous Peoples) is the least triggered standard**. It applied in two category A and eleven category B projects, many of which invoked the standard as a precautionary measure in case the project, as it develops, might impact indigenous peoples in the future. The standard's toughest requirement is for documentation of good faith negotiation with indigenous peoples if their traditional land or cultural resources are threatened by the project. To date, only three projects have had to meet this requirement.

44. **Performance Standard 8 (Cultural Heritage) was triggered by about 45 projects, largely in anticipation of potential impacts on cultural heritage**. Five projects created risks for critical cultural heritage, but mitigation measures introduced at the project design level allowed the projects to avoid the negative impact. Three projects used cultural heritage for commercial purposes, mainly tourism. So far, IFC investments have not triggered the requirement of good faith negotiations with affected communities and indigenous peoples on cultural heritage.

45. **Issues discussed in peer review meetings are useful indicators of challenges faced in implementation**. As noted earlier, one of the approaches used for quality assurance is the process of peer review, where all E&S specialists are invited to participate in a discussion of specific issues raised by a project team. In the 37 such meetings held since the introduction of the Performance Standards and Disclosure Policy, the issues most frequently raised are related to the following aspects of the policy framework: resettlement and land acquisition; habitat and biodiversity; project categorization; FPIC, BCS, and community engagement; and disclosure of information.

b. Financial Intermediaries and Funds

46. **The new policy framework and associated Environmental and Social Review Procedure created the basis for IFC to apply a risk-based approach to addressing E&S issues related to its investments through financial intermediaries**. In 2006, at the time the Performance Standards were approved, IFC's operational focus was on developing core business processes supporting project appraisal and portfolio management, and standardizing legal language. In FY08, CES introduced its first FI annual work plan, a roadmap for operations, systems, and capacity development. The focus for FY08 and FY09 was on consolidating and enhancing business processes. Scaling-up E&S support to IFC's growing FI business has been challenging and much back-filling and catching-up has occurred during the period under review. The experience to date also highlights the need for the Performance Standards to more specifically address FI requirements where appropriate.

Box 4: The Performance Standards Support IFC in Responding to the Financial Crisis

The IFC Asset Management Company will serve as a fund manager of third-party capital mobilized to invest in a wide variety of emerging-market companies and financial institutions. As an IFC subsidiary, AMC will apply the Performance Standards to all investments in its portfolio, thereby extending the reach of IFC's environmental and social risk-management policies and practice.

AMC will manage the $3 billion IFC Capitalization Fund, which is designed to support systemically important emerging-market banks as they deal with the effects of the global financial crisis. The IFC Capitalization Fund aims to provide additional capital for banks in developing countries, to ensure that they can support economic recovery and job creation throughout the crisis.

By requiring that the Performance Standards be applied to investments made by the IFC Capitalization Fund, IFC and AMC will ensure that sound E&S risk-management principles are applied by these market-influencing banks, thereby potentially creating a demonstration effect for other FIs in these markets.

The structure of the PS, anchored in the simple concept of a management-system, allows for their deployment in different operational settings and corporate structures.

47. **Requirements for managing environmental and social risk in FI operations are based on a three-tiered risk-based approach: exclusion list, national law, and the Performance Standards**. FIs with low-risk portfolios (such as student loans or housing finance) apply the FI exclusion list; FIs with medium-risk portfolios (such as small corporate loans) apply national law in addition to the exclusion list; and those with higher-risk portfolios (such as project financing or large corporate loans) apply the Performance Standards as well as the other two tiers. IFC actively engages with the FI—upfront and during the appraisal stage—to agree on an action plan for the FI to create or enhance an E&S management system that will enable the FI to comply with IFC requirements. Of the 223 category FI projects approved in the first three years, 13 percent were low-risk and 56 percent were medium-risk. The remainder, representing about 65 projects, applied the Performance Standards, based on an expectation of a higher-risk profile of the subproject portfolio.

48. **During FY09, CES supported IFC's financial-crisis response efforts by ensuring the integration of the Performance Standards into newly established facilities.** An example is the structuring of the IFC Asset Management Company (AMC) and the private equity funds under its management (see Box 4).

49. **IFC's implementation experience to date confirms a number of implementation challenges and opportunities for further strengthening the policy framework.** Several aspects of the policy framework challenged IFC and its clients with respect to policy content or application.

This review has identified an initial set of themes and topics that require further analysis and consultation to determine whether clarification and/or changes are warranted in the Sustainability Policy, the Performance Standards, and/or the accompanying Guidance Notes (see Table 2).

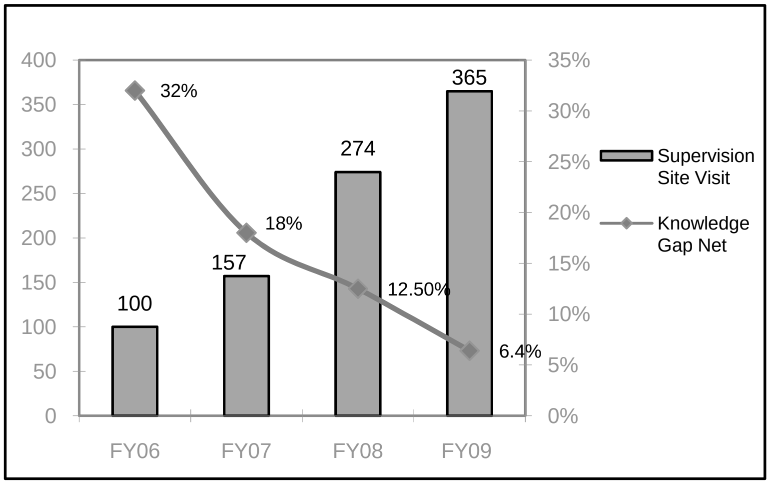
Table 2: Themes and Topics Emerging from Implementation Experience

Policy	• Further clarify the approach to project categorization • Better document the E&S review process of FIs • Clarify BCS requirements and explore the BCS timeline
PS1	• Provide further clarity of the E&S management plan, program, and system • Include guidance on Emergency Preparedness Plan in the management system • Clarify further when and to what extent to examine supply chains • Expand scope of community engagement to include engagement on issues such as water • Elaborate on Social and Environmental Management System requirements for FIs
PS2	• Provide additional reference on working conditions, such as application to nonemployees and living-condition requirements • Consider expanding retrenchment requirements to cover labor brokers, and extend the client's grievance mechanism to nonemployee workers • Require that employers disclose safety and other information to their workers
PS3	• Review requirements on GHG emission, climate-change-related matters, and energy efficiency • Clarify the role of the *EHS Guidelines* • Highlight importance of water-conservation measures
PS4	• Clarify when a Health Impact Assessment might be most appropriate
PS5	• Examine security of tenure requirement
PS6	• Clarify supply chain requirements • Clarify the actions required when dealing with natural habitats • Clarify the definition of critical habitat
PS7	• Provide guidance on the technical judgment needed to prepare an IP plan
PS8	• Clarify the definition of internationally recognized heritage

ii. Portfolio Management

50. **Portfolio knowledge on E&S performance and risks has improved significantly.** Projects formally enter IFC's portfolio after the first disbursement, at which time reporting and supervision requirements formally begin. Since mid-FY06, IFC has been monitoring and reporting on the E&S knowledge gap of its portfolio. The E&S knowledge gap represents active portfolio companies for which E&S performance information is dated or lacking, and represents a broad indicator of portfolio knowledge on E&S issues. The knowledge gap has steadily decreased over the last three fiscal years, from 32 percent to less than 7 percent, as a result of aggressive risk-based supervision. (See Figure 3.) Improvements in this area are also beginning to make their way into the ongoing review work by IEG. In its 2009 Independent Evaluation of IFC's Development Results, IEG reported that IFC's work quality (three-year moving average) for E&S supervision for non-FI projects had reached a historical high of 89 percent, and for FI projects, had improved from a low of 47 percent in 2006 to 62 percent for 2008 XPSRs. In FY09, CES completed a total of about 365 supervision visits, more than 100 of them with FI clients. The

Figure 3: Project Supervision and E&S Knowledge Gap



increased supervision has yet to translate into better performance by FIs and this remains the ultimate objective. The FI supervision program and related support programs have been enhanced to address IEG recommendations in this regard.

C. Institutional, and Project-Level Disclosure

51. **Implementation of the disclosure requirements in the Performance Standards and Disclosure Policy has resulted in the beginning of greater transparency and increased awareness of IFC investments among stakeholders.** IFC updated its Policy on Disclosure of Information in 2006 to reflect its commitment to enhance transparency about its activities and promote good governance. The updated policy is meant to establish disclosure of information to IFC's stakeholders as a fluid and ongoing process throughout the project life-cycle. It places some responsibilities on IFC, but focuses more on the client (as defined in the Performance Standards) as the actual executor of the project. IFC's Corporate Relations Department was charged with implementing IFC's institutional responsibilities.

i. Institutional Disclosure

52. **Implementation of the new DP led to the development and implementation of an innovative Web-based disclosure portal to serve as a central location for corporate information, policies and standards, proposed investments, and stakeholder feedback.** The Web site, launched in September 2006, offers the Disclosure Policy in six languages and links to IFC's Performance Standards. The site also links to a project database containing client information, a summary of proposed investment, ESRS, and anticipated development impacts, among other information. Through the IFC Disclosure Portal, IFC discloses the Environmental and Social Reviews and Mitigation Measures (an analysis of the project) and the client's Environmental and Social Action Plan, which sets out time-bound tasks that the client must accomplish to achieve compliance with the PS. Consistent with the DP, the timing of project information disclosure is linked to the project's environmental and social category—30 days prior to consideration of the proposed investment by IFC's Board of Directors for category B, C, and FI projects and 60 days for category A projects. In May 2009, IFC began disclosing Advisory Services project information.

53. **IFC's disclosure portal is the most advanced Web-based tool among the international financial institutions**, all of whom have similar policies on disclosure of information. It allows users to ask questions or provide comments regarding specific projects. Since the portal was launched, IFC has disclosed information related to 1,014 projects, and has received 162 inquiries (see Box 5). More than 57 percent were related to category A and B

projects. The disclosure portal was profiled in the 2008 Global Accountability Report by the British nongovernmental organization OneWorld Trust. The report—which measures transparency and accountability across a group of major multinational corporations, nongovernmental organizations, and international intergovernmental organizations annually—profiled IFC's disclosure portal as good practice in corporate transparency.

Box 5: Sources of Information Requests

Nongovernmental organizations were the top source of information requests, accounting for 29 percent of inquiries. Individuals accounted for 28 percent of such requests; private sector companies, 25 percent; academics, 13 percent; and governments, 5 percent. Most inquiries came from the United States (52), the United Kingdom (29), and India (15), with the rest coming from a variety of countries in Europe (18), South and East Asia (18), Middle East and North Africa (9), Sub-Saharan Africa (8), South America (7), Canada (5), and Australia (1).

54. **For members of the public who feel that an initial request for information has been unreasonably denied or that our policy has been incorrectly applied, IFC has established a complaints mechanism.** Complaints are reviewed by the Disclosure Policy Advisor, who reports directly to IFC's Executive Vice President. To date, only one request has been appealed to the Disclosure Policy Advisor.[3]

55. **The Disclosure Policy requires IFC to report aggregated development effectiveness results on an annual basis**. IFC's Development Outcomes Tracking System (DOTS) measures development results for all active projects in IFC's portfolio, for both investment and advisory services. IFC began disclosing DOTS results in the 2007 annual report, which integrated sustainability and development impact results reporting for the first time. The annual report now includes DOTS results for IFC investment and advisory projects by region and industry.

56. **Since January 2007, IFC has required all extractive industries projects it supports to disclose public payments to government from their operations.** In 2008, IFC worked with clients to review their practices and, as a result, developed a Web site to facilitate access to the information made public by companies. To date, nine extractive industries clients are using the Web site to disclose their payments to host governments. Beginning in 2009, IFC clarified its reporting requirements for clients and will require disclosure in a more consistent form for all companies. Other institutions have also instituted this requirement. In the Sustainability Policy, IFC also committed to encourage public disclosure of information related to household tariffs and tariff adjustment mechanisms, service standards, investment obligations, and the form or extent of any ongoing government support when IFC invests in projects involving the final delivery of essential services to the public under monopoly conditions, such as the retail distribution of water, electricity, piped gas, or telecommunications. Where IFC finances the privatization of such distribution, IFC encourages the public disclosure of concession fees or privatization proceeds.

[3] The request related to the language in which an environmental and social impact assessment document was published. The Disclosure Policy Advisor determined that IFC had a reasonable basis for non-disclosure of the requested information.

ii. *Project-level Disclosure*

57. **Responsibilities for disclosure of Social and Environmental Impact Assessments results and other information throughout the project life cycle rest primarily with the client.** IFC's experience shows that the degree of disclosure, documented evidence of community engagement, and quality of information disclosed varies across clients. Clients with projects that have greater social or environmental impact (such as infrastructure, oil and gas, and manufacturing) tend to report more information regarding their activities.

58. **Performance Standard 1 requires clients to disclose information to affected communities as part of the community-engagement process.** Since the implementation of the PS and DP, it is estimated that 67 percent of projects where E&S impacts had been identified disclosed their associated action plans and mitigation measures as part of their community engagement. The remainder did not, either because no local community existed around the project, or because the details of the actual project to be implemented were still under development or had not been identified yet (such as working-capital finance). IFC encourages disclosure regarding progress on implementation of the action plan, but many clients find it difficult to do so on a sustained basis.

59. **There is growing interest, both internal and external to IFC, in project-level disclosure of development impacts of IFC-financed projects.** External interest in project-level disclosure is driven by a number of factors—including, among others, a desire to better understand project-sponsor performance against development-outcome targets. MIGA is currently processing several new projects where local impact tracking and reporting may apply, but they have not yet been signed and it is too early to draw any lessons.

60. **IFC started work on developing pilot approaches to enhanced project-level measurement and reporting of development results in November 2008**. It began with a stocktaking exercise to assess the extent to which its clients are already publicly reporting, with the aim of informing IFC's approach. IFC industry departments have also begun to identify projects at early stages of the project cycle to pilot enhanced measurement of local development impact and reporting, beginning in FY10. IFC is also looking into project-level disclosure for projects in this portfolio, for which results are already being tracked, with the first external reporting expected in FY10.

iii. The Emerging Agenda

61. **IFC is generally effective in meeting its institutional requirements, as defined in the DP.** However, disclosure of information regarding IFC's activities throughout the life cycle of the project remains inconsistent. Responsibilities for disclosure of information throughout the project lifecycle rest primarily with the client, which is appropriate given that the client should be the main interface with the affected community. However, the degree of disclosure, evidence of community engagement, and quality of information disclosed varies widely across IFC's clients. IFC begins to disclose information once it has assured itself that the client can be expected to undertake the project in a manner consistent with the Performance Standards. At that point, IFC discloses the Summary of Proposed Investment (SPI) and the Environmental and Social Reviews and Mitigation Measures (ESRS). After the project is approved by the Board, or

relevant internal authority, it becomes the client's sole responsibility to report on the project's ongoing social and environmental performance and the implementation of the action plan. As a result, stakeholders must look to both IFC and the client to piece together a picture of what the project is, whom it affects, the expected development outcomes, how the project is being implemented, and whether IFC achieved the development goals it hoped for with the project. In reviewing and determining possible updates to the Disclosure Policy, the overarching goal will be to add clarity to the disclosure requirements in terms of what is expected of our clients and what our stakeholders can expect to know.

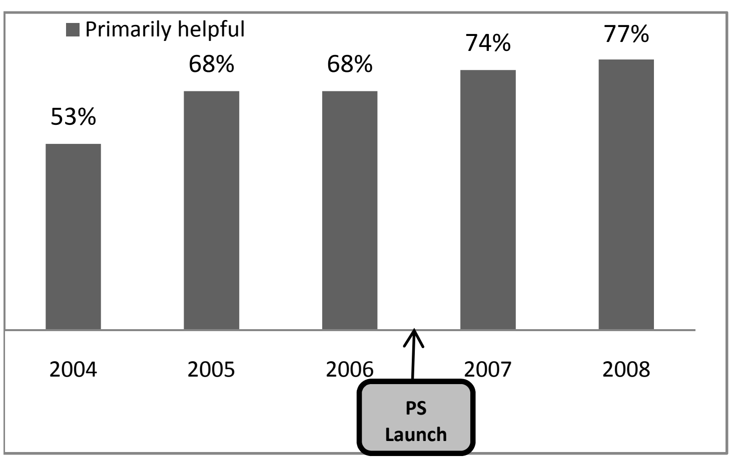
PART IV. IMPACTS AND EFFECTIVENESS

A. Impacts on IFC's Business and Clients

62. **IFC is implementing measures to assess the impacts of the new policy framework on its business and clients.** During the first two and a half years of implementation IFC experienced considerable business growth. Even in the midst of the current global economic slowdown, FY09 commitments appear to be strong. At the end of FY08, IFC's market share among multilateral and bilateral financial institutions supporting the private sector in emerging markets remained steady at about 30 percent. In addition to IFC's annual external survey of client satisfaction, CES conducted a special survey for this report to assess the cost implications to clients of PS implementation—an expanded version of the survey conducted for the 18-month progress report. IFC's interest in potential impacts on clients is two-fold: 1) level of client satisfaction; and 2) maintaining or developing client interest (new and repeat clients) in working with IFC.

63. **The annual IFC external client survey shows continued satisfaction with IFC's E&S policy framework.** The number of clients who view IFC's E&S expertise and inputs as "primarily helpful" has continued to grow since the launch of the PS in 2006. (See Figure 4.) Both surveys suggest that the new policy framework has not negatively impacted IFC's business or put IFC at a competitive disadvantage. In fact, IFC's E&S risk management framework appears to have been of interest to a growing number of clients who have looked to strengthen their project risk management capacity and to enhance their reputation. Combined with the *EHS Guidelines*, the PS and the DP provide private sector clients with a clear and comprehensive view of requirements early in their engagement with IFC. This is of critical importance for private sector clients that need a high level of certainty on roles, responsibilities, and performance expectations before entering into a financial transaction.

Figure 4: Percentage of IFC Investment Clients Who See E&S Requirements as "Primarily Helpful"



i. Impacts on Costs

64. **CES has not observed any significant additional increases in costs of PS implementation beyond that reported in the 18-month progress report**. The total costs have been commensurate with the growth of IFC's business, reflecting additional staff and resources needed to process and supervise projects. As noted in the 18-month progress report, processing costs of category B projects were on average higher than under the safeguards framework. The increase is due not only to requirements under the PS, but also to additional time spent by specialists to conform to the demands of a more robust QA process and more rigorous documentation requirements. Furthermore, projects that involve new or more complex financial

structures have required more time for assessing the approach to E&S due diligence. CES has pursued a number of cost-control and productivity-improvement measures, including the leveraging of staff through the use of consultants in Washington, D.C., and country offices.

65. **Results of the CES client survey suggest that costs associated with meeting PS requirements are broadly acceptable to clients.** Nonetheless, over 60 percent of respondents said the cost is higher than the *average* cost of meeting social and environmental requirements for their sector. About 20 percent of returning clients indicated that the costs are higher today than when they first sought financing from IFC under the safeguards framework. Half of IFC's clients indicated that the cost factor related to PS implementation would not impact their decision to consider pursuing IFC financing in the future, whereas 21 percent said the cost of PS implementation might negatively influence future decisions to work with IFC.

66. **Over 80 percent of survey respondents from among the FI subset think that a Social and Environmental Management System (SEMS) in their institutions help them better understand risks in their portfolios**. About 85 percent of respondents consider an SEMS useful for gaining better access to international finance, and almost 60 percent see it as having a positive impact on their brand name and value. On the basis of financial intermediaries' general experience with the development and implementation of such management systems, 48 percent indicated that the related cost factor would not affect their decision to consider pursuing IFC's financial support in the future. About 15 percent think that costs related to the requirement to implement an SEMS might negatively influence their decision to pursue IFC financing in the future.

67. **The survey therefore suggests that clients are not usually deterred by the cost associated with implementing the Performance Standards but that they remain conscious of costs.** IFC must continue to help existing clients and prospective project sponsors find value and opportunity in the more substantive management of E&S risk that is required under the new policy framework. Despite some concern with costs and the overall process for meeting PS requirements, it has not been possible to document cases where clients turned away from IFC solely because of E&S requirements as reasons tend to be numerous and complex.

Box 6: Performance Standard 2 at Work

IFC was asked to support a project comprising the construction of a greenfield state-of-the-art cement plant in Eastern Europe. The project sponsor, a leading European cement producer, planned to hire a foreign subcontractor to build the cement plant on a turnkey basis. The subcontractor's corporate policy was to hire all of its workers in Asia to work on its overseas projects, which meant that about 700 foreign workers would be involved during the construction phase.

Given the timing of the investment, IFC was not able to assess the subcontractor's practices in the field before commencement of construction, although IFC was familiar with this company through its involvement in another project in the region. Labor practices at this existing project were not consistent with PS2 requirements, particularly with regard to living conditions, occupational health and safety, working hours and overtime, and employee leave.

To address PS2 aspects, IFC assessed the subcontractor's labor policies and procedures at a corporate level. IFC also ensured that the contract between the sponsor and subcontractor had the appropriate covenants to ensure compliance with Performance Standards 2 and 4, including aspects relating to the management of impacts of the influx of migrant workers. Specifically, in consultation with IFC, the sponsor prepared a "code of conduct," with provisions pertaining to labor and working conditions, to be included in the contract with the subcontractor. IFC also incorporated into the loan agreement a provision requiring the sponsor to undertake a third-party labor audit three months after the beginning of construction work.

ii. Impacts on Projects

68. **While the Sustainability Policy addresses IFC's responsibilities, the Performance Standards spell out the requirements placed on clients to manage E&S risks of their projects.** The clear division of responsibilities enables clients to focus on identification, and avoidance or mitigation of E&S risks and impacts, and managing these over the life of the project through their management system. IFC believes that this approach, advocated in Performance Standard 1, is the main factor that promotes mainstreaming of E&S issues at the project level, and is one of the more tangible impacts of the Performance Standards. The emphasis on management systems under PS 1 also promotes companies to develop actions and programs that go beyond specific PS requirements. The case of a leading hotel chain in the Middle East (Box 7) illustrates how a PS requirement driven through a management system creates opportunities on energy conservation in a sector that is not traditionally considered energy intensive, but where energy costs are a significant part of the overall operational expenditures. Improved project outcomes are a stated objective of PS 1.

69. **While IFC does not yet have consistent data on the PS's impacts to the natural environment and affected people, tangible results and benefits on the ground should be attainable through the most consistently triggered Performance Standards - PS1 through 4.** The balance of environmental and social issues addressed in these four standards, including the new requirements (e.g., labor, climate change and greenhouse gases, community health, safety, and security, in addition to management system approach referred to above), presents an opportunity for projects to manage risks and create benefits.

70. **IFC was the first multilateral financial institution to address all four ILO core labor standards in its financing requirements through PS 2**. Implementation of PS 2 has provided a useful framework for IFC to pursue objectives related to worker-management relationships, fair treatment of workers, and the promotion of safe and healthy working conditions (see Box 6).

71. **Performance Standard 3 (Pollution Prevention and Abatement) raised to the policy level what previously had been covered only through technical guidance.** PS3 clearly defines the expected level of performance as good international industry practice, ensuring that companies' efforts toward the prevention and control of pollutants in all forms (solid, liquid, and gaseous) are conducted in a way that

Box 7: Performance Standard 3 Promotes Efficient Use of Energy and Water: The Case of a Hotel Chain in the Middle East

For one of the largest hotel operators in the Middle East, IFC's 2007 environmental and social appraisal of a corporate loan considered, among other things, the energy and water consumption of the existing hotels, as well as design aspects of one of the company's proposed new properties.

The appraisal compared the company's energy and water use with benchmarks adopted in IFC's 2007 *Environmental, Health, and Safety Guidelines for Tourism and Hospitality Development*. This benchmarking showed that water consumption varied significantly among facilities. Electricity use was generally high. Annual cost of energy and water was about $4.8 million.

Given the benchmarking outcome, IFC included in the E&S Action Plan requirements to undertake energy- and water-use audits at the existing properties. It turned out that overall annual cost savings were estimated by auditors at $1.3 million with simple payback in seven months. Recommendations were substantially energy-related, and associated CO_2 emissions savings were estimated at about 5,000 tons per year.

The company has leveraged its experience with IFC and is seeking to develop additional measures to reduce its cost of operations and its environmental footprint. The company has since approached IFC seeking additional funding to implement the audit recommendations, and to install solar water-heating facilities at two of its properties.

Box 8: How PS4 on Community Health, Safety, and Security Contributes to Positive Project Impacts

The sponsor is a major mining entity that has managed diverse mining interests across Africa. In its review of a proposed project, IFC found that one of the most complex challenges facing the company stemmed from the potential impact on local communities.

The sponsor established a number of processes to address issues required under PS4, including surveys conducted around open-cast operations to discover whether houses and other structures have been affected by vibration from blasting activities. Communities have recently requested and been allowed to participate in the selection of independent consultants for water- and air-quality monitoring.

Special efforts have been directed toward planting vegetation on all dormant tailings dams to address community concerns about airborne dust during the dry winter months. On the operating slimes dams, the company has installed a system of sprinklers that automatically turn on when threshold wind speeds are exceeded. The company's medical department has extended its program to surrounding communities, in collaboration with the Department of Health, to raise community awareness of health risks such as HIV-AIDS, diabetes, and high blood pressure. A health-and-environment focus group, formed as a result of the stakeholder-engagement process, meets regularly and has various ongoing projects, including construction of a new community clinic.

The company works closely with communities and the police force, including on traffic-control issues. Key security issues for the client include access control and asset protection, with a focus on the smelters and prevention of cable theft. The company has used contract security firms to control access at its facilities. It also has reaction units to deal with organized crime, especially with regard to theft of concentrate and underground equipment. To avoid any misuse of force, the company has established operational procedures governing the conduct of security personnel, and has adopted the applicable UN protocols.

effectively protects human health, safety, and the environment. This PS outlines a project approach to the prevention and control of pollution, taking into account the local, regional, and global consequences of pollution, and promoting the private sector's ability to integrate internationally recognized technologies and practices.

72. **Performance Standard 4 was developed to address, in an integrated manner, issues related to community health, safety, and security.** PS4 addresses the client's responsibility to avoid or minimize the risks and impacts to community health, safety, and security that may arise from project activities. Such risks and impacts can arise from project-related activities potentially occurring outside what is traditionally considered the project's physical boundary. As implementation experience has shown so far, PS4 ensures that some of the most significant issues directly affecting the health and safety of potentially affected communities are now incorporated by the client in its assessment and management of E&S impacts (see Box 8).

73. **Indicators of project compliance discussed in the 18-month progress report remain a useful proxy for assessing PS impacts on projects**. A sample of such indicators is presented in Table 3. These indicators can potentially be used as indicators of PS impacts on projects, and, to some extent, development outcomes. However, they do not allow us to draw conclusions about impacts on the ground, whether on the natural environment or communities. Audits and evaluations undertaken by the CAO and the IEG are also indicators of PS impacts on projects.

B. Effectiveness and Developmental Outcomes

74. **Timing of IFC's involvement and the type of investment it finances impacts the extent to which IFC can influence project design.** In the case of greenfield projects, IFC is usually well positioned to influence project design, at both the construction and operational phases, and to make the project consistent with PS requirements from the earliest stage of project development. The situation is more complex in corporate loans, where the use of proceeds is often not necessarily dedicated to new construction activity. Such a situation requires a screening

Table 3: Select Key Indicators for Non-FI Projects (Approved April 30, 2006, to April 30, 2009)

Projects disclosing action plans to local communities:	**67%** of all category A and B projects
Projects following FPIC requirement:	**21 (**14 category A and 7 category B)
Labor audits and inspections:	**17** (all of them were category B)
Projects with GHG emission above 100,000 tons per annum:	**37** (3 category A and 34 category B)
Projects with Health Impact Assessment:	**5** (1 category A and 4 category B)
Projects with resettlement action plans:	**23** (3 category A and 20 category B)
Projects with Good Faith Negotiations with IPs:	**3** (2 category A and 1 category B)

of the full range of clients' activities, operations of significant subsidiaries, and companies for which the client has management control. The situation can be even more complex in listed equity investments, where IFC's leverage can be limited. Notwithstanding the above, IFC engages with clients to develop action plans that capture opportunities for improving E&S performance, leading to more substantive and sustainable development outcomes. Successful implementation of the action plan is therefore an important proxy for effectiveness and for development outcomes.

75. **IFC's measurement of E&S-related outcomes is based on the performance of environmental and social management systems at the company level**. As noted previously, it is too early to assess the full scale of developmental impact associated with the PS project portfolio. A more effective assessment of PS-implementation impacts in the field will take another two to three years. However, initial data from 149 projects that have already reached the supervision stage, and for which an Environmental and Social Risk Rating is available, suggests that the PS portfolio is performing at a high level. The ESRR is a four-point rating system that summarizes IFC's current assessment of a company's project-management capacity, inherent riskiness and performance with its legal requirements (such as reporting), and action-plan compliance on E&S issues. Currently in the PS project portfolio, 80 percent of projects have an ESRR score of 1 or 2, meaning satisfactory and above, indicative of close adherence, so far, to action-plan requirements designed to improve their E&S performance. This compares favorably to an average of about 65 percent for IFC's portfolio as a whole.

76. **IFC established its Development Outcome Tracking System (DOTS) to facilitate more effective tracking of and reporting on the Corporation's development outcomes.** DOTS came into effect in October 2005. IFC was the first multilateral financial institution to report on current development results for its entire portfolio beginning with its 2007 Annual Report. Environmental and social performance is one of the performance areas covered by this system. DOTS requires the selection and monitoring of environmental and social indicators, the assignment of an E&S effects score (on a five-point scale), and assessment of development impact of each project from an environmental and social standpoint. E&S reporting is based on 10 core and 9 supporting development-outcome indicators. DOTS is currently reporting on investment projects approved between 2000 and 2005 that are mature enough to be rated. Projects approved under the new policy framework will begin entering the DOTS reporting stream in about two years and be part of a corporate-wide development outcomes monitoring system that is also subject to an external assurance process. Work relating to E&S reporting through DOTS has received more attention in the last 18 months, and a significant amount of

backfill has been completed across the portfolio. Going forward, IFC expects to capture a larger number of E&S outcome indicators in its reporting as the most relevant indicators are identified at appraisal and incorporated into the overall reporting framework.

i. Recent Experience with the CAO

77. **To date the CAO has received complaints on five projects appraised under the Performance Standards.** The CAO has engaged with all companies through its ombudsman function, and the ongoing cases are in various stages of resolution. Two complaints concerned allegations of anti-union activities. The CAO moved quickly to help find common ground between management and labor in these cases, and the mediation is largely completed. Other complaints are related to IFC investments with a client active in the palm oil sector. The CAO recently completed an audit of these investments and made several recommendations with implications on supply chain management, which IFC will consider as part of the review process. The CAO has also initiated an additional audit of a company that experienced issues related to poor working conditions. The audit is ongoing. No apparent trends have otherwise emerged from complaints received during the first three years of PS implementation.

78. **Through its advisory role, the CAO advises IFC on broader social and environmental issues related to policies, standards, procedures, guidelines, resources, and systems.** The CAO's advice, derived from lessons learned from ombudsman and compliance roles, aims to improve performance and provide guidance on emerging trends and strategic issues. Since 2006, the CAO has published several advisory notes. During the review-and-update process, IFC will carefully reexamine suggestions and recommendations made in these notes. In another advisory note, *Commentary on IFC's Progress Report on the First 18 Months of Application*, the CAO welcomed IFC's report on its application of the new policy framework and acknowledged that it was a first step in institutional accountability and reporting on the new policy framework. While acknowledging that the framework could not be expected to have generated stable outcomes at that point, it observed that IFC had enhanced its ability to manage portfolio performance, and that more efforts will be needed to improve the quality of the new management systems and to increase the independence of the quality-assurance function from line management. The note also included a recommendation to publicly disclose local development impacts and each project's development outcome. Part II of this report highlights several IFC actions that have addressed in full or in part many of these recommendations.

79. **The CAO has issued an approach paper for a CAO advisory note it intends to produce as its contribution toward the PS and DP review-and-update process.** The approach paper recognizes that few projects processed under the PS have yet generated significant outcomes, given the early stage of implementation, particularly for the more complex projects that may involve significant action plan items linked to communities, a key area of interest for the CAO. The CAO will therefore be focusing on IFC's implementation of the PS, particularly on interactions with local communities and the sponsor-community relationship. The CAO's review will include a study of local stakeholder perceptions, covering five projects processed under the Performance Standards, in addition to a sample-based portfolio review. The advisory note is to be completed by December 2009, in time for it to be considered by IFC in the review-and-update process.

ii. Recent Experience with IEG

80. **IEG has published over the last three years a number of reports that are of interest from a sustainability perspective,** including *Supporting Environmental Sustainability: An Evaluation of World Bank Group Experience (1990–2007)*. IEG findings and recommendations on development outcomes from this recent body of work have been based entirely on the review of projects approved under the safeguards framework. The nature of these recommendations is nonetheless of interest for the entire portfolio, since the lessons of implementation must be captured for the benefit of ongoing pre-PS as well as the growing portfolio of PS projects. A forthcoming report, for which an approach paper has been issued—*Evaluation of the World Bank Group's Experience with Safeguard and Sustainability Policies (1999–2008)*—will examine more closely the WBG's experience with environmental and social safeguards and Performance Standards.

81. **IFC has been responding substantively to IEG recommendations on environmental and social issues**. Part II of this report highlights the comprehensive program of actions taken to improve implementation performance in areas identified by IEG through its various reviews, including FIs. In response to the 2008 Independent Evaluation of Development Results (IEDR), IFC committed to continue to strengthen the E&S supervision and to build capacity in country offices, including in the Africa region, where performance issues have been most acute. IFC has also strengthened its team that supports the FI business, closed the knowledge gap of the FI portfolio, and intensified supervision requirements needed to bring about change in implementation performance. An increase in field-based staff is providing improved supervision coverage, particularly for smaller enterprises in frontier regions and countries.

82. **IEG indicators for E&S work quality have improved over the last three years.** As part of the annual IEDR process, IEG tracks and reports on IFC's quality of work on three separate dimensions: screening, appraisal, and structuring; supervision and administration; and IFC role and contribution. For the first two indicators, the results for environmental and social work quality

Box 9: Strengthening Grievance Mechanisms in Support of Development Outcomes

The project consists of the construction of crude-oil processing facilities and development of a crude-oil pipeline and trans-shipment terminal. The sponsor is a well-established company in South Asia.

Since the project start, the sponsor has worked to establish ongoing community engagement through its Consultation and Disclosure Plan Framework, which governs its communications programs and ongoing stakeholder engagement and includes a process for handling grievances. With the expansion of the company infrastructure in 2006, the Framework has been expanded to accommodate more complex engagement with communities, including complex land-acquisition issues along the pipeline route.

The company engaged with the local government early in its stakeholder-engagement planning, particularly on the grievance mechanism and its focus on land-acquisition issues. The local authorities serve as one of the channels to receive project-related grievances as well as part of the Grievance Redressal Committee. The GRC includes representatives from the district magistrate, the company, the community, and a special Land Acquisition Officer nominated by the local government as officer-in-charge of all matters related to land for the project.

The company's grievance procedure consists of six steps: Receipt of grievances, preliminary assessment, acknowledgement of grievances, investigation and resolution, closeout, and follow-up. The first three steps are primarily the responsibility of the company, and most of the matters related to a specific department or operation are resolved at this level, with the decision communicated to the complainant. If complainants are not satisfied, the matter is taken up in the GRC, which then investigates the underlying cause of the grievance and may introduce changes required to internal systems to prevent recurrence of a similar grievance. In parallel and where necessary, the GRC holds meetings or other appropriate communication with the complainant, with the aim of reducing any tensions and preventing them from escalating. During closeout, the GRC seeks to confirm that its actions have satisfied the complainant. During follow-up, the GRC, with the assistance of the company's manager of community development, investigates the root causes of major or symptomatic grievances, where necessary, to ensure that the grievance does not recur.

have improved over the last three years and reached their highest level. The results for the role-and-contribution indicator remain in a tight band.

iii. Recent Experience within the World Bank Group

83. **Closer collaboration within the WBG can enhance the effectiveness of project implementation even where there might be some differences in approach, although these appear to be minor and some alignment has occurred recently**. MIGA adopted its Performance Standards, modeled on IFC's, in 2007. Since the 18-month progress report, the International Development Association (IDA) IDA-IFC Secretariat examined in detail the opportunities available for projects to be co-financed by IDA and IFC to optimize collaboration and client requirements when applying two different sets of requirements of the two institutions. The analysis suggested that the challenges involved with an IDA and IFC co-financing arrangement were more related to the institutions' different project cycles, staff collaboration and timing of involvement, than to requirements of the social and environmental impact assessment process. In areas where differences in approach were confirmed, for example, on the subject of international waterways and disputed territories (for which the World Bank has safeguard policies but IFC has mostly procedural requirements), IFC now plans to explore establishing a more formal process for addressing these topics. During the Performance Standards review and update process, IFC will consult Bank colleagues on areas in which further policy coherence and process efficiencies can be achieved, with a view to strengthening Bank Group collaboration.

C. Impact on Market Practices

84. **IFC's Performance Standards have been catalyzing the convergence of standards in global financial markets.** The Performance Standards have become a global benchmark for managing environmental and social risk by financial institutions. Previous IFC safeguards were adopted as the basis for the Equator Principles in 2003. Since 2006, the Performance Standards have formed the basis of a revised set of the Equator Principles for financing projects with capital cost above $10 million. As of June 2009, 68 financial institutions have adopted the EP, including 16 from emerging markets. It is estimated that over 70 percent of project finance activity in emerging markets is now carried out in accordance with the EP. Recent developments are outlined in Box 10. Emerging market financial institutions display a growing interest in learning about the potential benefits of applying the Performance Standards to their business. To respond to these requests for information and engagement, IFC has expanded its PS outreach program in emerging

Box 10: The Performance Standards as a Global Benchmark—Recent Developments

In June 2007, 32 export credit agencies from the OECD announced their intent to benchmark projects against the Performance Standards in private sector limited-recourse projects.

In August 2007, MIGA's Board of Directors approved the adoption of the Performance Standards.

In October 2007, European Development Financial Institutions (EDFIs) signed the Rome Consensus, which refers to IFC's Performance Standards. In May 2009, this same group signed a declaration on Principles for Sustainable Investing. EDFIs agreed to use the Performance Standards as a benchmark for the environmental and social review process in all co-financed projects. Some of them, such as DEG (Deutsche Investitions Entwicklungsgesellschaft mbH), also use the Standards for projects financed unilaterally.

In the summer of 2008, EBRD adopted its new Environmental Policy and Performance Requirements, largely modeled on IFC's Performance Standards.

In June 2009, the Bank of Israel requested all Israeli banks to apply the Equator Principles. This represents an example of a country-wide initiative to elevate the practice of E&S risk management.

markets, collaborating with Equator Principles Financial Institutions (EPFIs). Box 11 provides a summary of IFC's engagement with China on the Performance Standards and EHS Guidelines.

85. **IFC has been the key technical resource for financial institutions using Performance Standards, and for those interested in adopting them, in both developed and emerging markets.** As IFC has expanded its PS outreach activities in emerging markets, it has continued to observe, analyze, and disseminate the distinctive sustainability initiatives of private banks and public sector institutions. Innovation in E&S sustainability is no longer an exclusive domain of banks in developed countries. New, dynamic, and creative approaches to sustainability are emerging from banks in middle-income countries and other places where there are skilled and insightful professionals who discern both the risks and opportunities in their business and create systems, products, and services to address them.

86. **To support better consistency in Performance Standards implementation among external practitioners, IFC established and manages a network known as the PS Community of Learning** (see Box 12). In the past three years, IFC has convened three meetings of the Community of Learning, with over 240 participants, representing international financial institutions, multilateral and bilateral institutions, and export credit agencies. The first two events were accompanied by additional training on PS and a course on labor and working conditions.

87. **IFC will continue to strengthen its external outreach programs and activities during the review-and-update period.** In the next two years, IFC's Performance Standards outreach program will focus on countries and regions with banks and other financial institutions with significant project finance portfolios. IFC also recognizes that the success of further outreach activities in emerging markets also depends on the prevailing regulatory framework and the political environment. Going forward, outreach activities will also involve governmental agencies such as central banks, banking regulators and environmental ministries where appropriate.

Box 11: Support to Green Credit Policy in China

Driven by its pollution-prevention agenda, the government of China increasingly scrutinizes the environmental and social performance of Chinese enterprises. In July 2007, the Chinese government announced a Green Credit Policy—jointly formulated by the Ministry of Environmental Protection, the China Banking Regulatory Commission, and the People's Bank of China—calling on banks not to finance environmentally damaging projects on the one hand, and to direct credit toward environmentally favorable projects and enterprises on the other.

To fully flesh out the policy, the Chinese government and banks have been searching for internationally recognized good practices in environmental policies, and guidance on their implementation. Of particular interest to the government were the Equator Principles, the IFC Performance Standards, and the EHS Guidelines. In this context, IFC initiated a policy dialogue and technical collaboration with the Chinese government that also included a comprehensive program to support implementation of China's Green Credit Policy. The program focuses on two specific areas: 1) a partnership with the Chinese government on policy formulation and capacity building for the Chinese financial sector in the area of E&S risk management; and 2) provision of advisory services to individual Chinese banks interested in adopting the Equator Principles.

Box 12: Highlights of IFC's Performance Standards Outreach Program for Financial Institutions

In the last three years, IFC has:

- Organized annual PS Community of Learning events attended by over 240 participants from EPFIs, export credit agencies, EDFIs, and MFIs
- Organized awareness-raising seminars for financial institutions in Brazil, Chile, China, India, Russia, and Vietnam
- Initiated discussion with over 40 banks from all regions (of which 12, so far, have announced their decision to adopt the Equator Principles)
- Signed two memoranda of understanding with the Chinese government, to support its Green Credit Policy
- Trained over 100 consultants from all regions on PS
- Developed an online training course on the Performance Standards for FIs
- Developed good practice notes, handbooks, and case studies, to enhance consistency in the use of PS

PART V. STRATEGIC OUTLOOK

A. The Emerging Agenda

88. **Three years of implementation experience and ongoing interaction with stakeholders is helping shape an agenda for the Performance Standards and Disclosure Policy review-and-update process.** IFC has initiated a process of internal stocktaking with E&S specialists that work with the PS on a daily basis, and with investment and regional departments, which constitute an important internal stakeholder. This initial stocktaking is further informed by ongoing interaction with external PS practitioners. A number of these institutions were consulted informally during the May 2009 Community of Learning event hosted by IFC. Drawing upon these early interactions and ongoing exchanges with stakeholders, IFC has identified an initial set of questions, themes, and topics that require further analysis to determine whether clarification or changes may be warranted in the policy framework. This list, by no means complete, indicates an emerging agenda, which IFC expects to refine through consultation on an approach paper. The scope of the update of the policy framework will be finalized in accordance with consultation outcomes. IFC will also propose its approach to consultation on the review-and-update process in the approach paper.

89. **IFC's outreach and networking efforts provide a constant stream of views on opportunities to further strengthen the policy content of the Performance Standards and Disclosure Policy as well as the operational framework for its implementation**. With a growing number of financial institutions using the PS as a basis or benchmark for their own policies, IFC can review and consider what these institutions have done to supplement the Performance Standards and assess the relevance and desirability of these enhancements for IFC's own policy framework. For example, IFC will look at the process of development and early implementation experiences of EBRD's new Environmental and Social Policy and Performance Requirements and specific policies developed by some EPFIs. IFC has also maintained an engagement with civil society on issues related to the PS and DP since their adoption in 2006. In addition, IFC's network of contacts includes the Multilateral Financial Institutions Working Group on Environment, the Organization for Economic Co-operation and Development (OECD), International Labor Organization, World Health Organization, and several other UN agencies as well as industry groups covering key sectors, among others. WBG Spring Meetings and Annual Meetings have been important venues for discussion on topics such as project-level disclosure, FPIC/BCS, human rights, and project-related impacts on communities. IFC also maintains an online platform for stakeholders, which creates an opportunity for them to share their comments and raise specific concerns on PS and DP implementation.

90. **The external context in which the Performance Standards are applied has evolved rapidly in certain thematic areas**. The most striking example of rapid development may be the issue of climate change. WBG involvement with the climate agenda has progressed significantly in the last three years, culminating in the report, *Development and Climate Change: Strategic Framework for the World Bank Group*. In this context, it is appropriate to ask whether the Performance Standards need to support clients' more effective management of climate-related risks—a question to be addressed during the review-and-update process. This particular issue is explored in Box 13, and represents an example of the questions that the review-and-update process will consider.

Box 13: Is the Current Coverage of Climate Change in the Performance Standards Sufficient?

With climate change a strategic priority for IFC and the WBG, the review of the Performance Standards provides a timely opportunity to explore possible approaches to more effectively integrate climate-change considerations into the Performance Standards. Prudent risk management requires a better understanding of climate risk on project activities into the future, and clients should be encouraged to undertake climate risk assessments to gauge climate resilience. Integrating such analysis at the project design stage could allow for some level of climate risk management from the very start.

One question already being debated relates to the threshold for GHG emissions under PS3. Some multilateral development banks and export credit agencies use the threshold of 100,000 tons per annum of CO_2 equivalent, while others use thresholds as low as 20,000 tons per annum. Experience under PS3 has shown that GHG-emissions measurements are useful in highlighting candidate projects for potential energy-saving opportunities—perhaps the most compelling argument for setting a lower threshold. On the other hand, experience to date also suggests that 90 percent of GHG emissions are likely to be attributable to only about 10 percent of projects, and the higher threshold is already capturing these large sources. Would a broader scope for GHG-emissions calculation, monitoring and reporting thus impose an additional burden on IFC and its clients if a lower threshold was adopted?

Notwithstanding the measurement discussion, experience has shown that energy-efficiency opportunities exist even if the industry has a relatively low emissions profile. This is particularly acute in the hotels and buildings sector, where energy consumption is often the highest cost of operation, due in part to poor design but mainly due to poor operational practice. If projects, regardless of their emissions profiles, were to estimate their GHG emissions during both the construction and operational phases, would there be a more systematic opportunity for energy-efficiency discussions with the client? These questions illustrate the nature of the dialogue that is likely to occur regarding climate change, a key area to be examined during the review-and-update process.

91. **Interest from external stakeholders has also evolved in certain thematic areas in the last three years.** For example, ongoing submissions from NGOs indicate that they will urge IFC to mainstream human rights in the PS. Although the Performance Standards extensively cover topics that support various human rights in the context of private sector operations, IFC anticipates that, in the context of updating the standards, it will analyze, within the parameters of IFC's Articles, the relationship between the Performance Standards and specific human rights. In addition, with the adoption by the UN General Assembly in 2007 of the Declaration on the Rights of Indigenous Peoples, advocacy groups expect multilateral development institutions to adopt a "consent" standard for projects dealing with indigenous peoples. However, IFC's experience with indigenous peoples issues has been limited so far, and IFC will need to understand better whether and how the "consent" standard can be put into operation in the field, and whether the "consent" is materially different from the current provisions in PS7, before it can take a position on the matter. Another area of emerging interest (and also of operational challenge for IFC) is that of supply chain management, particularly in agribusiness. IFC recognizes the importance of further clarifying the reach of the supply chain requirement. Questions and challenges linked to this issue are explored in Box 14.

92. **The evolving nature of IFC's business must also be considered in the review-and-update process**. This report highlights developments in IFC operations and business—important internal factors—that must be considered during the review-and-update process. These include the increased number of equity and corporate finance projects in IFC's portfolio mix, the continued growth of business with FIs, funds, and facilities, and the establishment of the IFC Asset Management Company, among others.

93. **While the emerging agenda appears to include diverse and challenging topics, on balance, IFC experience with the PS application over the last three years indicates that the**

Box 14: Can Supply Chain Responsibility and Accountability Be Further Delineated?

Performance Standard 1 currently states, "The impacts associated with supply chains will be considered where the resource utilized by the project is ecologically sensitive, or in cases where low labor cost is a factor in the competitiveness of the item supplied."

The "ecologically sensitive" case (beef, oil palm, cocoa, and so on) is a rapidly evolving area that is not always easy to control. If an IFC client has control or influence over the supply chain, such as sourcing from its own plantations, IFC requires the client to apply the PS to its facilities. If the client is a majority buyer from a supply chain supplier, IFC requires it to use its leverage to effect positive results.

The difficulty arises when clients do not have control or influence over the supply chain and do not sit in an advantageous place in the value chain. Sometimes ecologically sensitive products are commingled and it is not possible to even identify suppliers, or for the client to exert influence.

Another complication is the type of financial instrument IFC may be using. The Sustainability Policy recognizes this situation in Paragraph 25, but the question remains: Can IFC go further, and, if so, how?

current complement of standards appears to be appropriate. IFC believes that the basic structure of the Policy and Performance Standards is sound and that the list of topics covered is material and relevant to its functions. This suggests that the review and update will focus on clarifications, adjustments, balance, and strengthening of the PS, not wholesale revision or additions. Additional clarity will also be provided through the review of the supporting Guidance Notes, which are the main interpretation tools developed by IFC for those who use the Performance Standards.

94. **The overarching goal of the review and update of the Disclosure Policy will be to clarify what is expected of IFC clients and what stakeholders can expect to know**. For example, IFC could add more transparency to the process by providing access to information that the client is already disclosing, such as evidence of community engagement. IFC will also consider what it might disclose during the supervision and evaluation stages of a project, and how to better measure and report IFC's additionality and development impact to affected communities and interested stakeholders. The result should be an updated policy with greater predictability regarding availability of information for IFC stakeholders and clients.

95. **The review and update of the Disclosure Policy will also consider the growing interest, both internal and external to IFC, in project-level disclosure of development impacts of IFC-financed projects**. External interest in project-level disclosure is driven by a number of factors—including, a desire to better understand project-sponsor performance against development outcome targets, particularly for more controversial projects.

96. **IFC will seek to identify improvements to the current disclosure processes, and determine whether they require changes to the existing policy or enhancing its practices under the existing policy**. In some cases, disclosure across the project life cycle may not be appropriate, or may be too cumbersome for some clients or for IFC. Options should be considered for different disclosure requirements, depending on the size or impact of the project. For example, appropriate disclosure for real sector projects may not be appropriate for FI projects. In all cases, IFC must be mindful of the need to protect clients' confidential or market-sensitive information. Throughout the review, IFC will be guided by experience gained from the project-level disclosure pilot projects, recommendations from the recent CAO advisory note, feedback from internal and external stakeholders, and the disclosure practices of other international development institutions, including other parts of the WBG.

B. Timeline for the Review-and-Update Process

97. **The review-and-update process is expected to take 15 months to complete**. The proposed timeline and key milestones are presented in Box 15. The timeline is driven in part by three consultation periods, the first two for 60 days and the third for 30 days. The proposed approach to consultations is similar to that adopted when the PS and DP were first introduced, and therefore conforms with established international good practice.

98. **IFC expects to return to CODE and the Board on two occasions during the review period**. In February 2010, IFC will seek CODE's clearance before it discloses the draft changes to the PS and DP for the initial 60-day consultation period. In June 2010, IFC will submit to CODE (for information) the revised draft final text, which will then be made public for a 30-day consultation period. IFC will then seek final Board approval of the revised PS and DP. Subject to final approval, IFC proposes that the revised policy framework become effective in October, 2010. Any significant deviations from the proposed timeline will be communicated.

99. **IFC is ready to meet the challenges going forward as the Performance Standards and Disclosure Policy review-and-update process is launched**. The sustainability agenda and its policy framework have become important differentiators for IFC in the marketplace and a pillar of its corporate strategy. The DP represents an unequivocal statement of IFC's commitment to transparency and accountability in the way it conducts its business. Continued successful implementation of this framework is therefore a corporate priority. IFC expects significant interest in this review from external stakeholders and proposes to engage in a constructive and collaborative dialogue to fully explore the opportunities offered by this exercise. The necessary human and financial resources to deliver the review and update have been mobilized.

Box 15: Proposed Review-and-Update Timeline and Milestones

- ***By July 31, 2009:*** Presentation of the *Three-Year Report* to CODE, and formal launch of the review-and-update process
- ***August 2009:*** Issuing of the approach paper for the review-and-update process (including an initial list of themes and topics, a proposed consultation process, and a timeline) for a 60-day consultation period
- ***November 2009*:** Public issuing of a summary of the consultation outcomes on the approach paper, and an adjusted timeline if needed
- ***December 2009 to January 2010*:** Review of findings from the CAO report on three years of PS and DP implementation and the IEG's report on WBG implementation of safeguards and standards
- ***February 2010:*** Presentation of the initial set of changes to PS and DP to CODE for review and authorization to initiate consultation on proposed language
- ***March to April 2010:*** First formal (60-day) consultation period open to all stakeholders to comment on draft text changes
- ***May 2010:*** Preparation of a revised draft reflecting stakeholders' comments
- ***June 2010***: Draft final text changes to CODE for information
- ***July 2010:*** Second formal (30-day) consultation period open to all stakeholders to comment on the draft final text changes
- ***September 2010:*** Presentation of the complete final draft text to the Board
- ***October 2010:*** Revised PS and DP in effect

100. **IFC is seeking approval to initiate the review and update of the Performance Standards and Disclosure Policy as proposed in this report, beginning with consultations on an approach paper to the review-and-update process itself. IFC also seeks CODE's approval to disclose this report to the public.**

Annex A: Publications Related to the Performance Standards

PS 1:

- Stakeholder Engagement: A Good Practice Handbook for Companies Doing Business in Emerging Markets
- Guide to Human Rights Impact Assessment and Management Road-Testing Draft, June 2007
- Good Practice Note: Addressing Concerns and Grievances from Project-Affected Communities (Draft)

PS 2:

- Labor Toolkit: A Practical Screening and Due Diligence Tool for Project Review
- Workers' Accommodation: Processes and Standards
- Good Practice Note on Retrenchment
- Good Practice Note on Discrimination

PS 4:

- Introduction to Health Impact Assessment
- Project-Induced In-Migration: Risk Assessment and Management Strategies

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PS7:

- ILO 169 and the Private Sector: Questions & Answers for IFC Clients

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New Environmental, Health and Safety Guidelines:

- 63 EHS Guidelines translated into Arabic, Chinese, French, Russian, and Spanish

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Updates of E&S Procedure and Guidance Notes:

- Updated Guidance Notes (July 2007)
- Updated Environmental and Social Review Procedure, v3.0 (February 2009)

Others:

- Good Practice Note on Animal Welfare
- BTC Lessons of Experience
- External Monitoring of the Chad-Cameroon Pipeline
- Banking on Sustainability

Annex B: List of Institutions That Have Adopted the Equator Principles

Equator Principles Financial Institutions

1. ABN AMRO Bank (*Netherlands*)
2. Access Bank Plc *(Nigeria)*
3. ANZ (*Australia*)
4. Arab African International Bank *(Egypt)*
5. Banco Bradesco (*Brazil*)
6. Banco de la Republica (Uruguay)
7. Banco do Brasil (*Brazil*)
8. Banco Galacia (*Argentina*)
9. Banco Itaú (*Brazil*)
10. Bancolombia S.A. *(Colombia)*
11. Banco Santander *(Spain)*
12. BankMuscat (*Oman*)
13. Bank of America (*US*)
14. BT MU (*Japan*)
15. Barclays plc (*UK*)
16. BBVA (*Spain*)
17. BES Group (*Portugal*)
18. BMO Financial Group (*Canada*)
19. BNP Paribas *(France)*
20. Caja Navarra (*Spain*)
21. Calyon (*France*)
22. CIBC (*Canada*)
23. CIFI (*Costa Rica*)
24. Citigroup Inc. (*US*)
25. CORPBANCA (*Chile*)
26. Credit Suisse Group (*Switzerland*)
27. Dexia Group (*France, Belgium*)
28. DnB Nor *(Norway)*
29. Dresdner Bank (*Germany*)
30. E+Co (*US*)
31. EFIC *(Australia)*
32. EKF (*Denmark*)
33. Export Development Canada (*Canada*)
34. Financial Bank (*Togo*)
35. FMO (*Netherlands*)
36. Fortis (*Belgium*)
37. HBOS (*UK*)
38. HSBC Group (*UK*)
39. HypoVereinsbank (*Germany*)
40. ING Group (*Netherlands*)
41. Intesa Sanpaolo (*Italy*)
42. Industrial Bank Co. Ltd *(China)*
43. JPMorgan Chase (*US*)
44. KBC (*Belgium*)
45. KfW IPEX-Bank *(Germany)*
46. la Caixa (*Spain*)
47. Lloyds TSB *(UK)*
48. Manulife (*Canada*)
49. Millennium bcp *(Portugal)*
50. Mizuho Corporate Bank (*Japan*)
51. National Australia Bank (*Australia*)
52. Nedbank Group (*South Africa*)
53. Nordea (*Denmark, Finland, Norway & Sweden*)
54. Rabobank Group (*Netherlands*)
55. Royal Bank of Canada (*Canada*)
56. Scotiabank (*Canada*)
57. SEB (*Sweden*)
58. SMBC (*Japan*)
59. Société General (*France*)
60. Standard Chartered Bank (*UK*)
61. Standard Bank Group (*South Africa*)
62. TD Bank Financial Group (*Canada*)
63. The Royal Bank of Scotland *(UK)*
64. Unibanco (*Brazil*)
65. Wachovia (*US*)
66. Wells Fargo (*US*)
67. WestLB AG (*Germany*)
68. Westpac Banking Corporation (*Australia*)

European Development Financial Institutions

AWS	• Austria Wirtschaftsservice Gesellschaft mbH	NORFUND	• Norwegian Investment Fund for Developing Countries
BIO	• Belgian Investment Company for Developing Countries	OeEB	• Oesterreichische Entwicklungbank
CDC	• CDC Group	PROPARCO	• Societe de Promotion et de Participation pour la Cooperation Economique
COFIDES	• Compania Espanola de Financiacion del Desarollo	SBI-BMI	• Belgian Corporation for International Investment
DEG	• Deutsche Investitions-und Entwicklungsgesellschaft mbH	Sifem	• Swiss Investment Fund for Emerging Markets
FINNFUND	• Finnish Fund for Industrial Cooperation Ltd.	SIMEST	• Societa Italiana per le Imprese all'Estero
FMO	• Netherlands Development Finance Company	SOFID	• Sociedade Para o Financialmento do Desenvolvimento
IFU, IØ, FV	• Danish International Investment Funds	SWEDFUND	• Swedfund International AB

Export Credit Agencies

Australia	Export Finance and Insurance Corporation (EFIC)
Austria	Oesterreichische Kontrollbank AG (OeKB)
Belgium	Office National du Ducroire/National Delcrederedienst (ONDD)
Canada	Export Development Canada (EDC)
Czech Republic	Export Guarantee and Insurance Corporation (EGAP) Czech Export Bank
Denmark	Eksport Kredit Fonden (EKF)
Finland	Finnvera Oyj Finnish Export Credit Ltd (FEC)
France	Compagnie francaise d'Assurance pour le commerce exterieur (COFACE) Direction des Relations Economiques Exterieures (Ministere de l'Economie) (DREE)
Germany	AuslandsGeschaftsAbsicherung der Bundesrepublik Deutschland Euler Hermes
Greece	Export Credit Insurance Organisation (ECIO)
Hungary	Hungarian Export Credit Insurance Ltd (MEHIB) Hungarian Export-Import Bank
Italy	Sezione Speciale per l'Assicurazione del Credito all'Esportazione (SACE)
Japan	Nippon Export and Investment Insurance (NEXI) Japan Bank for International Cooperation (JBIC)
Korea	Korea Export Insurance Coporation (KEIC) The Export-Import Bank of Korea (KEXIM)
Luxembourg	Office du Ducriore (ODD)
Mexico	Banco National de Comercio Exterior
Netherlands	Atradius
New Zealand	Export Credit Office (ECO)
Norway	The Norwegian Guarantee Institute for Export Credits (GIEK)
Poland	Korporacja Ubezpieczen Kredytow Eksportowych (KUKE)
Portugal	Companhia de Seguro de Creditos
Slovak Republic	Export-Import Bank of the Slovak Republic (Eximbank SR)
Spain	Compania Espanola de Seguros de Credito a la Exportacion Secretaria de Estado de Comercio (Ministerio de Economia)
Sweden	Exportkreditnamnden (EKN)
Switzerland	Swiss Export Risk Insurance (SERV)
Turkey	Export Credit Bank of Turkey (Turk Eximbank)
United Kingdom	Export Credits Guarantee Department (ECGD)
United States	Export-Import Bank of the United States (Ex-Im Bank)