# Sustainability Guidelines of KfW Development Bank

**April 2014**

KFW

CONTENTS

**April 2014**

**Abbreviations**

| | | |
|---|---|---|
| EHS | - | Environmental Health and Safety Guidelines (World Bank Group) |
| ILO | - | International Labour Organisation |
| FI | - | Financial Intermediary |
| FC | - | Financial Cooperation |
| IFC | - | International Finance Corporation |
| PJF | - | Programme-based joint financing |
| SEA | - | Strategic Environmental Assessment Study |
| ESMP | - | Environmental and Social Management Plan |
| ESIA | - | Environmental and Social Impact Assessment |

## 1 Preamble

For more than two decades, KfW Development Bank has been promoting projects to protect the environment, social development and the climate in numerous areas. Central to its promotional activities are the principles of environmental compatibility and sustainability. Therefore, all promoted projects have long been subject to a comprehensive and systematic assessment by KfW Development Bank to ensure they are compatible with environmental and other crucial development standards. Based on its Statement on Environmental Protection and Sustainable Development, which it submitted to the German parliament, the KfW Group has introduced a set of sustainability guidelines. They set forth the environmental and social policies that govern KfW's operations with a view to contributing to sustainable development within the meaning of the German Federal Government's sustainability strategy. Furthermore KfW Development Bank pursues the objective of actively supporting the implementation of international human rights with the instruments at its disposal to do so. In this regard the KfW Group has issued a Declaration on respect of human rights in its business operations. Starting from these principles, this Guideline provides more specific guiding principles which apply to KfW Development Bank, while also incorporating some important social aspects. Technically speaking, this Guideline expands on the previous Environmental Protection Guidelines of KfW Development Bank, building on many years of experience KfW Development Bank has acquired in assessing the environmental and social impact of German Financial Cooperation (FC) projects.

## 2 Mission of KfW Development Bank

**2.1** KfW Development Bank funds investments and related advisory services in developing and emerging countries on behalf of the German Federal Government. The projects are implemented by local partners on their own responsibility. More specifically, KfW Development Bank uses funds from the federal budget, which are topped up by the bank's own funds, in order to support the construction of economic and social infrastructure, the development of efficient financial sectors, and the implementation of environmental and climate protection measures and programmes to preserve natural resources. The most important objective of KfW Development Bank's promotional activities is to help the Federal Government of Germany and its partner countries achieve their overarching development goals (i.e. to reduce poverty, secure peace, promote democracy, shape globalisation in an equitable manner and engage in environmental and climate protection).

**2.2** The priority areas of KfW's promotional activities in developing countries include social development, environmental and climate protection and the conservation of natural resources. Its work also encompasses projects which make a crucial contribution to implementing international agreements on environmental and climate protection and on the conservation of natural resources such as the United Nations Framework Convention on Climate Change (UNFCC), the Convention on Biological Diversity (UNCBD) and the Convention to Combat Desertification (UNCCD). Whenever the main goal of projects is not geared to environmental, climate or resource protection, KfW Development Bank seeks to incorporate climate and/or environmental objectives into the project scope.

## 3 Objectives and scope of this Guideline

**3.1** This Guideline describes principles and procedures to assess the environmental, social and climate impacts during the preparation and implementation of measures financed by KfW Development Bank. In this context, the Guideline pursues the following objectives, in particular:

- to define a common binding framework to incorporate environmental, social and climate standards into the planning, appraisal, implementation and monitoring of measures financed by KfW Development Bank;
- to promote transparency, predictability and accountability in the decision-making processes of environmental and social impact assessments (ESIA) and climate change assessments;
- to improve the assessment of economic risks associated with projects by taking account of the environmental, climate and social aspects.

**3.2** All funding activities of KfW Development Bank must be subject to an ESIA and a climate change assessment as defined in this Guideline. This applies both to the funding of programmes and projects and to funding activities that are not project-related, such as programme-based joint financings, financial sector programmes and corporate finance operations.. This Guideline covers all forms of financing provided by KfW Development Bank.

# 4 Environmental and social impact assessment and climate change assessment of projects

## 4.1 Objective and core elements

**4.1.1** The objective of environmental and social impact assessments (ESIA) and climate change assessments is to anticipate and appraise any foreseeable impact a project may have on the environment, the climate and/or on social factors (including human rights), and to identify and prevent any negative impact, or limit it to a tolerable level and (provided that the negative impact is inevitable but still tolerable) introduce compensation measures. In addition, the assessments should identify, monitor and manage any residual risks. The objective of the climate change assessment is also to recognise climate change impacts that may impair the achievement of objectives in due time so that, if applicable, required adaptation measures can be taken into consideration in the project conception. Apart from assessing individual projects, ESIAs and climate change assessments are designed to demonstrate to partner countries the need to appraise projects and explore opportunities to make them environmentally, climate and socially compatible; they are also intended to raise awareness of development approaches that are ecologically and socially sustainable. By aligning ESIAs with internationally recognised environmental and social standards (e.g. World Bank Safeguard Policies, IFC Performance Standards, Environmental, Health and Safety Guidelines of the World Bank Group, ILO Core Labour Standards, EU Environmental Legislation), KfW Development Bank aims to improve donor harmonisation in accordance with the Paris Declaration.

**4.1.2** ESIAs and climate change assessments are a core element of the assessment procedure of KfW Development Bank. They are, first and foremost, intended as a management tool to steer and shape projects over their entire life cycle (i.e. from planning to completion). The essential steps of an ESIA and climate change assessment include:

- a preliminary appraisal, called **screening**, to determine the environmental, climate and social relevance of a project;

and, if the project has been found to be environmentally and/or socially relevant:

- the definition of the assessment scope (**scoping**), in close cooperation with the executing agency, in order to identify and assess the project's environmental, climate and social consequences and risks more accurately; and
- the design and implementation of an environmental and social impact study (**ESIS**), climate change adaptation assessment and/or climate change mitigation assessment in order to examine all or individual aspects of the project, including participatory approaches to involve affected local groups and keep the public in the partner country informed.

**4.1.3** The steps mentioned above must cover the entire programme or project; they must not be limited only to those parts of the project which are financed by KfW Development Bank. This also applies to the rehabilitation and/or expansion of existing facilities. Moreover, it is important to consider relevant alternatives to reach the project objective. One possible outcome of an

ESIA or climate change assessment may be that the original project design or the location has to be modified.

### 4.2 Screening and classification of projects

**4.2.1** As part of the screening process, the planned project will be appraised at an early stage in order to determine its relevance in terms of environmental and social aspects and risks, as well as in terms of substantial greenhouse gas reduction potential and substantial need of adaptation to possible climate change. The screening process is designed to identify and appraise the type and scale of any negative consequences or risks that may arise from the planned project (environmental/social impacts), potentials for reducing greenhouse gas emissions and possible climate change impacts on the project that may impair the achievement of objectives. The next step, once the relevance of such consequences or risks has been established, is to define the type and scope of additional studies which need to be conducted as part of project preparations. Appendix 2 includes a checklist to assess the environmental and climate change relevance.

**4.2.2** All projects will be classified into one of the following three **categories A, B or C**, according to the relevance of their potentially negative environmental and social impact.

**4.2.3** **Category A –** Projects will be classified as category A, if they may have a severe negative impact on the environment and/or the social conditions of those concerned. A potentially severe negative impact means that the consequences are manifold, irreversible or unprecedented. Such consequences may affect a larger area beyond the site of the facility under construction, the site of the facility itself or the project area in a narrower sense. As a matter of principle, any projects that are considered sensitive must be classified as category A; this applies to projects which may, for example,

- affect important protected habitats or sites (tropical forests, coral reefs, nature reserves, wetlands, historic cultural sites etc.);
- violate international treaties (such as conventions on international waste management regulations or on marine conservation);
- lead to a high consumption of resources, and of large areas of land or large quantities of water in particular;
- constitute a major hazard to human health (e.g. facilities located in residential areas or handling hazardous substances; noise pollution or harmful emissions); or
- require the resettlement of a large number of people.

An illustrative list of projects that may be classified as category A is attached as appendix 1.

**4.2.4** For **category A** projects, it is mandatory to analyse and appraise any negative ecological and social consequences as part of an independent environmental and social impact study (ESIS) and to draw up an environmental and social management plan (ESMP). The ESMP should describe all measures that need to be taken to avert, mitigate, offset and monitor any negative consequences that have been identified by the ESIS; it should also assign responsibilities for implementing such measures and list the costs involved. For category A projects, KfW Development Bank requires the executing agency to operate an appropriate monitoring system; if the projects are run by private operators, they are required to have their own environmental and social management system. Any such management system must comprise the following elements: (a) adequate organisational capabilities, (b) environmental and social assessment procedures, (c) management programmes, (d) specific environmental and social training measures, (e) well-structured relations with the target group, (f) monitoring and (g) reporting procedures.

**4.2.5 Category B –** Projects will be classified as category B if they may have a potentially negative impact on the environment and on the social conditions of those concerned, which, however, is less severe than that of category A projects and can usually be mitigated through state-of-the-art countermeasures or standard solutions (cf. appendix 1). Typically, the potential consequences of category B projects are limited to the local area, are in most cases reversible and are easier to mitigate through appropriate measures. For category B projects, the need for and the scope, priorities and depth of an ESIS have to be determined on a case-by-case basis.

**4.2.6 Category C –** Projects will be classified as category C if they are expected to have no or only minor negative environmental and social consequences and if the implementation and operation of the project does not require any particular protection, compensation or monitoring measures. Category C projects usually do not require any additional analysis within the meaning of this Guideline or any further ESIA procedures. However, category C projects should be monitored for any relevant changes over their life cycle.

**4.2.7** For the elements of the climate change assessment (adaptation assessment and mitigation assessment), the checklist in appendix 2 is used to determine if the measure may have a substantial climate change relevance or not (also see the definition of the relevance criteria in appendix 2). If relevance is expected, then a detailed climate change assessment is carried out as follows.

- The assessment and consideration of the aspects in terms of **climate change adaptation** (Climate Proofing) should ensure that the desired developmental impacts of the strategy or measure are not endangered despite the forecasted effects of climate change. Furthermore the assessment should analyse whether the partner country's capacity for adaptation can be further increased in the framework of the strategy or measure. In this regard the expected climate changes and their consequences for the strategy or measure will be analysed. This includes both direct effects (e.g. more frequent flooding or drying out of agricultural areas) and indirect effects of climate change (e.g. revenue losses in agriculture). The analysis will also examine the longer targeted period of impacts beyond the formal period of the strategy or measure. On this basis options will be developed and implemented to increase the capacity of the target groups or ecosystems to adapt.
- The assessment and consideration of the potential for **greenhouse gas reduction** (Emission Saving) serves to avoid substantial greenhouse gas emissions and to tap potentials for reducing greenhouse gases. First, the expected development of greenhouse

gases in the project area/sector will be described. This is followed by a presentation of whether the planned strategy or measures contribute to higher or lower greenhouse gas emissions and if there are potentials for reducing greenhouse gas emissions. On this basis options to contribute to greenhouse gas reduction will be developed and if applicable – taking into consideration the developmental impacts and costs – integrated into the strategy or measure.

The climate change assessment only examines the relevance, which if applicable then entails a more in-depth assessment; the result is described in the programme proposal or in internal KfW proposal documents.

### 4.3 In-depth study and appraisal of negative effects and risks

**4.3.1** The outcome of the screening will determine to what extent an in-depth study of potentially negative environmental, climate and social consequences is required. For category A projects, an in-depth environmental and social impact study (ESIS) is mandatory. If according to appendix 2 it is determined that substantial climate change relevance is expected, then an in-depth assessment of the greenhouse gas reduction potential or of the adaptation needs is also obligatory. As a matter of principle, the responsibility for collecting the relevant information to appraise the environmental, climate and social impact rests with the executing agency or the recipient of the funds. If necessary, KfW Development Bank will ask the executing agency to provide the information required to conduct an ESIA and/or climate change assessment, and will manage all additional studies. All ESIS recommendations have to be set forth in an action list as part of an ESMP, which should also specify environmental and social monitoring measures that need to be taken by the executing agency.

**4.3.2** An in-depth study of the potentially negative environmental, climate and social consequences of a project may be conducted either as part of the feasibility study, or as part of an independent study if the negative consequences are severe and of a more complex nature. For planned projects with a potentially severe environmental and social impact (category A), it is mandatory to conduct an independent ESIS, which must involve the communities or groups concerned (public participation, see section 4.6 below). In addition, the ESIS must

- forecast and appraise the negative environmental and social consequences and risks of the planned project;
- identify possible alternatives, including possible amendments to the project and/or protection or compensation measures, and assess the project's residual impact once such measures have been implemented;
- discuss any opportunities afforded by the project to enhance its positive environmental and social effects;
- discuss the management of environmental and social measures;
- discuss the monitoring of environmental and social aspects (development and effectiveness of protection measures) during the implementation and operation of the project.

The analyses in the framework of the climate change assessment are to be implemented with the respective relevant aspects.

**4.3.3** The executing agency, in consultation with KfW Development Bank, is responsible for the design and implementation of such studies, which are part of the project preparations. The study should also involve other relevant bodies and agencies of the partner countries which are responsible for environmental, climate and social issues. If there is a potential need for major protection and/or compensation measures, the costs of such measures have to be taken into account in the economic feasibility study and included in the funding scheme.

**4.3.4** If the ESIS or the climate change assessment provides evidence that the project may have a negative environmental, climate and/or social impacts, which cannot be limited to a tolerable level or offset by modifications or technical devices, the project will not be eligible for funding. Funding will also be denied if the project does not comply with the legal regulations of the partner country or with international agreements.

**4.3.5** A conclusive appraisal of the project's environmental, climate and social impacts will be made in the project appraisal report. Whether an ESIA has been or should be conducted in accordance with generally accepted standards, including disclosure and public hearing, is also relevant for the appraisal. This is mandatory for all category A projects. In addition, it has to be verified whether the ESIS has been duly accepted by the competent public institutions of the project country or if this is part of the national approval procedure. The results of the in-depth climate change assessment are also fed into the final evaluation.

**4.3.6** The conclusive appraisal must be based on the following basic principles:

- The main purpose is to make constructive proposals for improvement which provide solutions to unresolved questions or suggest additional measures to limit negative consequences.
- The project should seek to propose solutions for appropriate protection measures which are commercially viable and socially acceptable.
- Local operators must have adequate technical skills to handle the proposed pollution control measures while ensuring proper operation of their facilities.
- It has to be ensured that funds will be made available to implement the protection measures that have been identified to mitigate or offset adverse social consequences. In that respect, it is necessary to determine the share of expenditure to be borne in the framework of the KfW financing and the contributions of the executing agencies.

**4.3.7** If the project is funded jointly with other donors, (e.g. under PJF schemes, sector programmes, project-related co-funding schemes etc.) that have already conducted an ESIS or an in-depth climate change assessment, a plausibility check will usually suffice. However, this does not rule out that certain aspects may have to be examined in more depth.

### 4.4 Appraisal standards

**4.4.1** In appraising the environmental, social and climate compatibility of its projects, KfW Development Bank takes into account the Sustainability guidelines of KfW Group, the specific development policy concepts and guidelines for development cooperation issued by the German Federal Government, and other international safeguards and standards for the environmental, climate and social sustainability of development projects. With a view to achieving sustainability and preventing negative environmental, climate and social consequences, KfW Development Bank will ensure that all projects funded by the bank comply with the principles of

- preventing, reducing or limiting environmental pollution or degradation, including greenhouse gas emissions and other burdens;
- protecting and preserving biodiversity and tropical forests and managing natural resources in a sustainable manner;
- consideration of probable and foreseeable consequences of climate change;
- avoiding any adverse impact on community life, particularly of indigenous people and other vulnerable communities, and safeguarding the rights, living conditions and values of indigenous communities;
- avoiding or minimising involuntary resettlement and forced eviction of communities and mitigating the negative social and economic consequences arising from changes in the use of land and soil by restoring the original living conditions of the communities concerned;
- promoting health and safety at work and industrial safety for all project staff;
- outlawing forced labour and the worst forms of child labour, banning discrimination in professional life and at the workplace and promoting the freedom of association and the right to collective bargaining;
- protecting and preserving cultural heritage;
- assisting the executing agency in managing and monitoring potentially negative environmental, climate and social consequences arising from the implemented project.

**4.4.2** In any event, the fundamental benchmark for appraising the environmental, climate and social compatibility of projects is their compliance with the environmental and social standards of the partner country and the national licensing or certification requirements. KfW Development Bank evaluates the appropriateness of national environmental and social standards on the basis of internationally recognised appraisal standards, including those of the World Bank Group (Environmental, Health and Safety Guidelines EHS, IBRD/IDA Safeguard Policies and IFC Performance Standards) and other equivalent standards issued by regional development banks or by the EU. KfW Development Bank will disclose the standards it has used for appraisal. When funding major dam and reservoir projects, KfW Development Bank also takes into account the recommendations of the World Commission on Dams (WCD).

**4.4.3** Any permanent or temporary deviation from the applicable appraisal standards must be notified in advance and include an explanation of the reasons for the planned deviation. Whenever temporary deviations occur, the executing agency has to provide substantial evidence that the target standard will be met by the agreed deadline. In doing so, the executing agency is assisted by KfW Development Bank, whose approval of the project will be contingent on whether the reasons for deviations are deemed acceptable.

### 4.5 Protection and compensation measures

**4.5.1** When selecting protection, compensation and monitoring measures, it is important to make sure that they can be enforced and executed in the implementation and operation phase. Whenever protection and compensation measures are set forth in the framework of an ESMP or a climate change assessment and – in the case of involuntary resettlement – in a resettlement management plan, the executing agency will, at the same time, have to agree to monitor the effects of such measures in an appropriate manner and submit a report to KfW Development Bank.

**4.5.2** In some cases, it may not be possible to determine appropriate protection measures with reasonable certainty during the project planning phase. Whenever it is uncertain whether the identified environmental or social risks or risks resulting from climate change will materialise and which countermeasures will be required, such risks have to be tracked on an ongoing basis by an adaptive project monitoring process.

### 4.6 Public participation

**4.6.1** An important element of the ESIA planning and decision-making process is to involve the communities concerned and keep the public in the partner country informed. When the ESIA scope is determined and the ESIS draft is presented, hearings need to be scheduled to consult with the people concerned and/or their community representatives, cooperatives or NGOs. Moreover, it is crucial to use appropriate media channels to provide the affected communities and, as the case may be, the general public of the partner country with comprehensive information in all phases of the project; such information needs to be provided in a timely and culturally suitable manner. Interested parties in a climate change assessment (e.g. those affected, the public) should also be involved in relevant cases.

### 4.7 Monitoring

**4.7.1** In order to guarantee an effective monitoring of any negative environmental, climate and social impacts, the executing agency and/or the recipient of the funds have/has to agree to certain reporting and notification duties and employ appropriate monitoring tools. To track the environmental, climate and social consequences and risks of a project, it is particularly important to supervise the application of the agreed protection measures and monitoring procedures. If an ESMP has been drawn up, it will be used as a basis for monitoring.

KFW

## 5 Environmental and social impact assessment and climate change assessment of general or sector budget support (PBA)

**5.1** Unlike other financing tools, general and sector budget support schemes do not earmark funds for individual measures or projects. Instead, the donors pay their funds directly into the budget of the partner country. The purpose of budget support is to provide assistance for economic, regulatory or institutional reforms across sectors (general support) or to promote sector-specific political and institutional reforms. In that context, the objective of environmental and social impact assessments as well as climate change assessments is to review the environmental regulations and policies of the partner country, to identify and appraise potentially negative environmental, climate and social consequences arising from reform programmes, and to determine at an early stage of the decision-making process (through strategic environmental assessment studies or SEAs) whether they are in line with national development goals for environmental and climate protection. Strategic environmental assessment studies are of particular importance for budget support in environmentally, climate and/or socially sensitive sectors, if there is a foreseeable risk of negative environmental, climate and/or social consequences.

**5.2** Whenever a lead donor (e.g. World Bank, IDB, ADB, AfDB, EU) has already conducted a SEA for a certain budget support programme, the study and its results and recommendations may, subject to this Guideline, be used for assessing the programme's sections that are to be financed by KfW Development Bank, after a plausibility check has been performed and the necessary technical amendments have been made.

**5.3** SEAs are conducted to implement Millennium Development Goal 7, which is 'to integrate the principles of sustainable development into country policies and programmes'. This corresponds to the commitment made in the Paris Declaration on Aid Effectiveness 'to develop and apply common approaches for “strategic environmental assessment” at the sector and national levels'.

## 6 Environmental and social impact assessment and climate change assessment of cooperation with financial intermediaries

**6.1** The objective of ESIAs and climate change assessments for projects involving financial intermediaries (FI) is to anticipate and prevent any negative environmental, climate and social consequences that may arise from loans extended to clients of FIs refinanced by KfW Development Bank. In assessing FIs, ESIAs and climate change assessments should focus – subject to significance and relevance – on environmental, climate and social risks associated with the planned promotional activities on the one hand, and on the FI's procedures and capacity to assess environmental, climate and social concerns and monitor the loans on the other. This includes an assessment of the FI's environmental and social management system in particular. As a rule, no assessment will be made of the environmental and social impact of the individual final loans that have been extended by the FI (exceptions see 6.3). If FIs do not have an appropriate environmental and social management system, they have to agree to introduce a system that complies with the IFC Performance Standards. In addition, partner institutes are required to adhere to the basic principles of 'responsible finance' in dealing with their clients (see position paper attached as appendix 4).

**6.2** FIs have to agree to give adequate consideration to environmental, climate and social aspects in their loan extension process. This includes in any event compliance with national environmental and social legislation and related regulations. As a matter of principle, funds provided by KfW Development Bank must not be used for projects or measures that are registered in the "IFC Exclusion List" (appendix 3); the specifications set forth in the list (e.g. microfinance) apply by analogy.

**6.3** Whenever there is evidence that an FI supports projects or business activities in sectors or subsectors that are associated with grave environmental, social and/or climate risks and for which KfW Development Bank funds are applied for, the assessment of the FI has to determine whether the FI is willing and able to assess the environmental, climate and social relevance of such final loans and will deny funds to all projects or business activities that may have intolerable environmental, climate and social consequences. To satisfy this requirement, the FI must have, or establish, its own ESIA procedure, or commission external assessments (e.g. from local environmental or regulatory bodies or agencies) and enforce appropriate protection measures whenever projects may have a significant negative environmental, climate and social impact. This notwithstanding, KfW Development Bank reserves the right to approve or reject any final loan in critical areas, e.g. category A projects.

**6.4** Microfinance institutions are supported mainly by refinancing loan portfolios rather than loans to individual borrowers. In such cases, the assessment needs to determine whether the introduction of an environmental management system is commensurate with the number of loans and the scale of the negative environmental, social and climate consequences and risks that are to be expected. In any event, it is crucial to examine the microfinance provider's portfolio and its track record in dealing with environmental, climate and social concerns.

## 7 Fast-track procedure in the event of natural disasters, crises and conflicts

**7.1** Fast-track measures which are intended to rapidly repair damage caused by natural disasters, crises and conflicts are subject to a special procedure. The Federal Government will decide on any support provided under a fast-track procedure and may waive individual assessment criteria if such waiver is necessary to speed up the procedure. The criteria that may be waived may relate to the socio-economic, socio-cultural, gender-specific and ecological impact (environmental and social impact assessment and climate change assessment) of the measures (see also the Work Instructions for Fast-Track Procedures).

## 8 Validity and review of this Guideline

This Guideline is effective for all new projects that will be initiated after 1 January 2014. This Guideline will be reviewed for necessary modifications or adjustments in 2015.

# 9 Appendices

## 9.1 Appendix 1 - Illustrative list of projects which may have severe negative environmental, social, and climate change impacts

The following is an illustrative list of project types and measures that have the potential to cause severe negative environmental and/or social impacts and can therefore be assigned to category A or B (where negative impacts are less severe and reversible).

1. Extensive and significant changes to the use of natural resources (e.g. changes in the use of land - as farmland, as forest or pasture land, for rural development, commercial timber production, etc) as well as extensive land reclamation.
2. Extensive and significant changes to management methods in agriculture and fishery (e.g. introduction of new plant species, large-scale mechanisation, introduction of new fish species) and extensive logging.
3. Intensive poultry (more than 40,000 birds) or pig farming operations (more than 2,000 porkers).
4. Use of water resources (e.g. large dams and other impoundments, irrigation and drainage projects, deep wells, water management and management of catchment areas, water supply).
5. Infrastructures (e.g. roads, bridges, airports, seaports, transmission lines, pipelines, railroad networks, tourism).
6. Industrial activities (e.g. metallurgic works, timber processing plants, chemical factories, power plants, cement factories, refineries and petrochemical plants, agro-industries).
7. Use of geological resources, mining etc. (e.g. mines, quarries, peat exploitation, oil and natural gas production).
8. Municipal wastewater treatment plants with a capacity of more than 150,000 population equivalents.
9. Waste management and removal (e.g. sewerage systems, landfills, treatment plants for domestic and hazardous waste).
10. Projects in which a significant number of affected persons have to be resettled involuntarily.

## 9.2 Appendix 2 – Questionnaire for implementation of the preliminary appraisal

The preliminary appraisal (Screening) is performed on the basis of both the checklist below and consideration of existing and additional, easily accessible information.

| | No | Yes |
|---|---|---|
| **Environmental assessment:** | | |
| Does the measure potentially have a substantial negative impact on one or more of the following subjects of protection?<br>• Humans, including human health<br>• Animals, plants and biological diversity<br>• Soil, water, air and landscape<br>• Cultural goods and other assets<br>• nterdependencies between the above-mentioned protected resources | ☐ | ☐ |
| Does the measure have considerable potential to improve environmental quality, resource protection or strengthen ecological sustainability? | ☐ | ☐ |
| Is an environmental assessment required by the national law of the partner country? | ☐ | ☐ |
| **Climate adaptation assessment** (Climate Proofing): | **No** | **Yes** |
| Are the intended developmental impacts of the measure substantially dependent on climatic parameters such as temperature, rainfall, wind, etc? | ☐ | ☐ |
| Does the measure present the possibility of substantially increasing the adaptation capacity of the target groups or ecosystems? | ☐ | ☐ |
| **Climate change reduction assessment (Emission Saving):** | **No** | **Yes** |
| Is the measure expected to make a substantial contribution to greenhouse gas emissions? | ☐ | ☐ |
| Can it be assumed that the measure will have the potential to considerably reduce emissions of greenhouse gases or increase $CO_2$ sequestration in soil? | ☐ | ☐ |

If one or more of the questions are answered with "Yes", then an in-depth environmental and/or climate change impact assessment should certainly be carried out. The in-depth assessment can be limited to the sub-areas or protected resources for which an impact is affirmed.
The following criteria should be used to judge **relevance**:

- extent of the expected impacts (e.g. number of affected persons),
- frequency, duration and expected time of the expected impacts,
- sensitivity of the affected natural spaces, population groups and economic activities as well as their adaptation capacity,
- irreversibility of changes,
- requirements in legal regulations (e.g. threshold values for pollutants).

Considerable negative risks and positive potentials can also result from other aspects than those mentioned in the checklist. Therefore the checklist should not exclude a more extensive analysis.

In accordance with the precautionary principle, an in-depth environmental and/or climate change assessment should also be performed if, due to uncertainties, **no clear decision can be taken in terms of the relevance of the environmental and climate risks or potentials.**

KFW

## 9.3 Appendix 3 – IFC Exclusion List

The IFC Exclusion List defines the types of projects that IFC **does not** finance.

IFC does not finance the following projects:

- Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international bans, such as pharmaceuticals, pesticides/herbicides, ozone depleting substances, PCB's, wildlife or products regulated under CITES.
- Production or trade in weapons and munitions.[1]
- Production or trade in alcoholic beverages (excluding beer and wine).[1]
- Production or trade in tobacco.[1]
- Gambling, casinos and equivalent enterprises.[1]
- Production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where IFC considers the radioactive source to be trivial and/or adequately shielded.
- Production or trade in unbonded asbestos fibers. This does not apply to purchase and use of bonded asbestos cement sheeting where the asbestos content is less than 20%.
- Drift net fishing in the marine environment using nets in excess of 2.5 km. in length.

A reasonableness test will be applied when the activities of the project company would have a significant development impact but circumstances of the country require adjustment to the Exclusion List.

**All financial intermediaries (FIs)**, except those engaged in activities specified below*, must apply the following exclusions, in addition to IFC's Exclusion List:

- Production or activities involving harmful or exploitative forms of forced labor[2]/harmful child labor.[3]
- Commercial logging operations for use in primary tropical moist forest.
- Production or trade in wood or other forestry products other than from sustainably managed forests.

* When investing in **microfinance** activities, FIs will apply the following items in addition to the IFC Exclusion List:

- Production or activities involving harmful or exploitative forms of forced labor[2]/harmful child labor.[3]
- Production, trade, storage, or transport of significant volumes of hazardous chemicals, or commercial scale usage of hazardous chemicals. Hazardous chemicals include gasoline, kerosene, and other petroleum products.
- Production or activities that impinge on the lands owned, or claimed under adjudication, by Indigenous Peoples, without full documented consent of such peoples.

* **Trade finance projects**, given the nature of the transactions, FIs will apply the following items in addition to the IFC Exclusion List:

- Production or activities involving harmful or exploitative forms of forced labor[2]/harmful child labor.[3]

Footnotes

[1] This does not apply to project sponsors who are not substantially involved in these activities. "Not substantially involved" means that the activity concerned is ancillary to a project sponsor's primary operations.

[2] Forced labor means all work or service, not voluntarily performed, that is extracted from an individual under threat of force or penalty.

[3] Harmful child labor means the employment of children that is economically exploitive, or is likely to be hazardous to, or to interfere with, the child's education, or to be harmful to the child's health, or physical, mental, spiritual, moral, or social development.

### 9.4 Appendix 4 – KfW Development Bank position paper on “Responsible Finance”

# "Responsible Finance"
# a Leitmotiv for financial sector promotion at KfW Development Bank

In a globalised world with a high degree of transparency and information flows, socially and morally appropriate behaviour is becoming increasingly important for all market participants. *Responsible Finance* has become a catchword in development finance and, in particular, in financial system development. Along with financial sustainability goals, the “social return” is a factor of growing importance for the decision-making of many finance institutions (double bottom line).

Over the past years the financial and microfinance sectors in developing and transition countries have experienced enormous growth rates. Enterprises and the population in many developing countries now have significantly better access to financial services. This has contributed to economic growth and greater prosperity, including among poorer groups of the population. Yet despite these positive impact, the upward trend has also shown its downside - untransparent and, ultimately, prohibitive lending practices have put many customers at risk of overidebtedness, particularly through the uncontrolled and sometimes aggressive marketing of consumer lending.

Even if there are no internationally acknowledged definitions of *Responsible Finance*, it can be summarized as practices designed to create a fair balance of interests between a financial institution and its customers, employees and business partners on the one hand and their shareholders and financiers, on the other. *Responsible Finance* is a precondition for increasing the well-bedcing of local stakeholders.

## What does Responsible Finance mean for the stakeholders in the financial sector?

*Responsible Finance* is a topic that affects all market players and cannot be reduced merely to the relationship between a finance institution and its customers. The following four dimensions of *Responsible Finance* can be outlined:

- **Customers.** Access to financial services for persons and enterprises should be free from distinctions due to sex, ethnical origin, colour, religion etc. Customers are in a weaker position particularly when their level of education is insufficient for them to overlook the consequences of their borrowing (“financial literacy”). Customers therefore should be capable of understanding the fundamental aspects of financial services, particularly a debt relationship. Giving them certain basic knowledge (“financial education”) is therefore indispensable. Likewise, strengthening clients’ confidence into the whole financial sector is vital, e.g. by promoting deposit insurance schemes.
- **Financial institutions**. Amid growing competition, finance institutions today face the challenge of matching necessary growth with a sound lending practice and, most of all, dispensing with untransparent lending practices. Transparency in a customer relationship includes comprehensible information about the products and conditions, particularly the dis-

closure of all costs associated with the lending operation ("truth-in-lending“), restructuring repayment instalments and periods in line with the customer's repayment capacities and cash flow, credible management of complaints, a clearly defined and communicated corporate philosophy, the setting and monitoring of developmentally relevant objectives such as promoting employment creation, and compliance with adequate environmental and social standards ("social performance").

- **Regulatory authorities**. The protection of consumer interests should include not only responsible banking practices (through voluntary undertakings) but should be based on a legal and regulatory framework that creates proper incentives for banks and their clients. Ultimately, regulatory requirements (proscribing certain collection practices, requiring disclosure of effective annual interest rates, and others) have proven to be more efficient than interest ceilings still being applied in some countries which often impact negatively on the poor sectors of the population (credit rationing).
- **Donors and investors**. Donors and investors can behave responsibly, for example, by engaging in long-term commitments, by not imposing on the finance institutions any donor-specific end-borrower financial conditionalities (which should be market driven), and by deploying their instruments (funding, guarantees, participations, subordinate debt capital) in line with the needs of the finance institutions they support. Moreover, they should help to promote good corporate governance. This would help to achieve a significant impact to strengthen local financial markets so as to respond to the needs of enterprises and private households. In the area of micro-finance this also means, for example, refraining from undermining the potential to mobilise savings.

## What role does KfW Development Bank play in the area of *Responsible Finance*?

*Responsible Finance* is not a new issue for KfW but has been consistent with its own vission before it became a topic of international debate. With its financial sector operations in developing and transitional countries, KfW contributes to disseminating responsible practices in all of the four dimensions described above; and this is definitely not confined to its microcredit operations. KfW thus contributes to the principles established by the German Federal Ministry for Economic Cooperation and Development for a social and ecological market economy, and it contributes above all to achieving broad-based growth for poverty alleviation, promoting gender equality, strengthening the private sector, improving the conditions for a market economy, strengthening social partnerships, making the economy ecologically sustainable and creating equal opportunities for disadvantaged groups of the population.

Various facets show the role of KfW in the area of *Responsible Finance*:

- **Systemic approach**. KfW's activities focus on different levels of intervention (micro, meso and macro level) and pursue a comprehensive and systemic approach to financial system development in transition in developing countries ("building inclusive financial systems"). In this approach we make use of long-standing, close contacts with ministries, central banks, commercial banks and micro-finance institutions in our partner countries which are characterised by a partnership based on mutual trust. The development and application of best practice minimum standards and individual projects helps to develop the financial sector framework conditions. KfW regards itself as a partner who contributes to development at the various levels of intervention with a long-term perspective.

- **Selecting the "right" partners**. We provide funding and equity to financial institutions which, for their part, regard responsible banking as an element of their business model and have appropriate strategies to achieve this. Banks that make their lending terms transparent and customer-friendly are among the preferred partners of KfW Development Bank.
- **Focusing on suitable products**. Financial sector projects centre on successful intermediaries whose business activity is not primarily geared to short-term financial returns (for example by focusing on consumer credit), but to responding to the needs of relevant target groups for development, such as by focusing on MSME loans in the area of micro-finance, housing finance and savings products for small and micro-savers. Through the creation of deposit guarantee funds, for example, micro-savers can be encouraged to place more trust in the financial sector.
- **Long-term commitment as an investor in microfinance funds and MFIs.** KfW plays an import role in setting up and promoting funds which it accompanies over many years as an investor with a seat and vote in the supervisory board, thus contributing to disseminating standards applicable to *Responsible Finance*.
- **“Additionality” for socially motivated investors**. Socially motivated investors (such as private foundations) are developing an increasing interest in investing, for instance in microfinance, and they rely on KfW's country, sector and target-group expertise to ensure that their funds are employed in institutions acting responsibly and that their investment is consistent with their risk preferences. Examples include structured finance operations in the micro-finance sector.
- **Contributing to international discussions**. KfW is acknowledged as one of the leading development finance institutions in the area of financial sector development, particularly microfinance. By hosting and participating in international conferences and in an intensive and continuous dialogue with relevant stakeholders, KfW helps to set the standards for the development and trends in financial sector development. Its main focus is on the promotional and developmental aspect.

Overall, *Responsible Finance* is an important overarching topic for financial systems development at KfW Development Bank. The bank can draw on many years of cooperation with financial intermediaries in developing and transition countries in which it has gathered vast experience with regard to *Responsible Finance*. It feeds this experience into the international debate. By KfW’s way of working, its operations contribute to disseminating good – responsible - practice.