

## Our Approach to Sustainability

Sustainability is at the heart of IFC's business model. As a development bank, we are charged by our shareholders with a mission to reduce poverty and improve people's lives. The projects we choose to finance and the various products and services we offer must have a long-term outlook and fulfill development goals that go beyond financing.

Our definition of sustainability encompasses four dimensions of good business performance:

- the financial sustainability of IFC and our clients so that we can continue to make a long-term contribution to development
- the economic sustainability of the projects and companies IFC finances through their contribution to host economies
- environmental sustainability through the preservation of natural resources
- social sustainability through improved living standards, poverty reduction, concern for the welfare of communities, and respect for key human rights concerns

The challenges of sustainable development are very real and far from simple. Together with our clients, we nevertheless face significant risks to our business – reputational, legal, operational, and financial – if we don't take into account the full range of factors that influence our investments, including the environmental and social impacts of our projects.

Our role as a broker between companies and governments, our ability to access global funds, and our specialized knowledge and expertise help build a stronger and more sustainable private sector while promoting social and environmental concerns. It also means that we are uniquely placed to leverage the resources needed to help countries meet the Millennium Development Goals.

Our commitment to specific dimensions of sustainability results directly from our experiences in the field. We have seen not only how our business prospects and those of our clients can be improved, but also how society as a whole can be strengthened through the growth of smaller businesses, better governance, less corruption, access to clean drinking water, a cleaner and more richly diverse environment, and effective private sector responses to social problems such as HIV/AIDS.

As a natural outgrowth of our development mandate, IFC was one of the first multilateral finance institutions to adopt high social and environmental standards of due diligence tailored specifically to private sector investment activities. Having for many years used the World Bank's environmental and social safeguards, we adapted them in 1998 to make them more applicable to the private sector. This commitment reflected our belief in sustainability as a guiding business principle.

These early safeguards have since become a recognized model of good practice among other financial institutions, and, in 2003, were adopted as the basis for the Equator Principles, a framework for commercial financial institutions to use when investing in development projects with a capital cost of \$50 million or more. As of February 2006, 41 banks had adopted the Principles, and it is estimated that they now cover approximately 80 percent of global project lending.

As more banks join the ranks, the impact of our standards is being more widely felt. In order to continue to meet the needs of the marketplace and to ensure that our standards kept pace with emerging best practice in sustainability, we launched a comprehensive revision of our safeguards in 2004. The process has invigorated the debate on the role of financial institutions in development and pushed

us to dramatically increase the added value that we can bring to our clients through sustainability.

## **A NEW POLICY AND PERFORMANCE FRAMEWORK**

In February 2006, IFC completed a rigorous process of updating the environmental and social safeguard policies used to ensure minimum standards of performance in all our investments. Part of the process was renaming and expanding them to become IFC's Policy and Performance Standards on Social and Environmental Sustainability.

Updating our standards gave us an opportunity to advance our own practices as well as provide greater clarity for an increasing number of practitioners and concerned stakeholders. It also enabled us to respond to significant external changes in expectations and knowledge related to sustainability and the private sector's role over the last decade. The result is a revised framework consisting of three parts, each of which has been updated to reflect changing stakeholder needs and expectations.

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**A Sustainability Policy**, which defines IFC's responsibility for supporting project performance in partnership with clients.

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**Environmental and Social Performance Standards**, which define clients' roles and responsibilities for managing their projects and the requirements for receiving and retaining IFC support. The standards include requirements to disclose information as an integral part of engaging in early and ongoing discussion with communities that are affected by projects.

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**A Disclosure Policy**, which defines IFC's obligations to disclose information about itself as an institution and its activities.

In addition, three sets of supporting documents serve as advisory or reference material to give direction to IFC staff and clients in implementing the proposed sustainability policy and performance standards.

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**Guidance Notes**, which are companion documents to the Performance Standards and provide additional



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guidance to clients and IFC staff in fulfilling their roles and responsibilities under the standards.

**An Environmental and Social Review Procedure**, which gives direction to IFC staff in implementing the Sustainability Policy and reviewing compliance and implementation by private sector projects.

**Environment, Health, and Safety (EHS) Guidelines**, which provide technical guidance informing those parts of the new policy structure which relate to environmental, health, and safety issues.

**What has changed?**

The new policies and Performance Standards will be among the strongest environmental and social standards globally. They clearly state IFC's requirements, which are applicable to all our investments. They also add new requirements relating to integrated social and environmental assessments, core labor standards, greenhouse gas emissions, and community health and safety.

**NEW AND EXPANDED STANDARDS**

<b>Labor Rights</b>	A broader policy requires a comprehensive approach to labor and working conditions on the part of the client and addresses all four core ILO labor standards: forced labor, harmful child labor, non-discrimination, freedom of association and collective bargaining.
<b>Human Rights</b>	IFC now incorporates key human rights concerns into the Performance Standards, such as adequate housing, security of tenure, and voluntary principles on security
<b>Community Health and Safety</b>	A new standard requires firms to consider a project's effects on health and safety in the surrounding community beyond the project itself.
<b>Community Engagement</b>	IFC will require early and ongoing community engagement in developing a project and throughout a project's lifecycle. Related new requirements are that IFC must be satisfied that broad community support is present for projects with significant impacts, and a grievance mechanism must be established by the client to address any community concerns.
<b>Indigenous Peoples</b>	The standards aim to protect the dignity, human rights, aspirations, cultures and customary livelihoods of Indigenous Peoples. On the commercial use of Indigenous Peoples' cultural resources, the standards require good faith negotiation between the client and Indigenous Peoples.
<b>Pollution Prevention and Abatement</b>	A new standard requires clients to avoid, minimize, or mitigate pollution and its impact on the environment, and quantify a project's greenhouse gas emissions.
<b>Biodiversity</b>	IFC is expanding its focus beyond preservation of natural habitats to a broader view of protection and conservation of biodiversity. Habitat destruction and invasive alien species are recognized as the major threats to biodiversity, and the standard specifies how to address them in natural and modified habitats. Sustainable management of all renewable natural resources is required, and must be demonstrated by independent certification in sectors such as forestry.

The new framework reflects IFC's extensive experience of what works in developing countries as well as emerging good practice. Addressing gaps in the previous IFC Safeguard Policies, the Performance Standards emphasize private sector considerations while ensuring compatibility with IFC's policies.

More importantly, the update reflects a new approach to managing social and environmental risks and a focus on achieving improved outcomes. Because strong outcomes are most likely when companies can incorporate standards into their own internal management systems and understand the business case for doing so, the new standards encourage firms to establish and maintain effective management systems as part of their basic operations.

The new standards also define clear requirements to help clients assess and manage social and environmental risks comprehensively. The requirements for achieving specific outcomes go into an Action Plan, which is disclosed to the affected communities by the client and posted on IFC's Web site. The Action Plan becomes part of the client's legal agreement with IFC.

An emphasis on integrated social assessment means that the Performance Standards now encompass all vulnerable groups and related social issues, while continuing to put special attention on the complexity of involuntary resettlement, Indigenous Peoples, and cultural heritage.

The new approach also lets companies consider diverse means and seize new opportunities for achieving required outcomes. This enables the private sector to do what it does best: manage projects efficiently, innovate, and improve performance over time for the long-term benefit of local people and the environment.

## INCREASING IFC'S DISCLOSURE

The new disclosure policy clarifies and expands the responsibilities of IFC to disclose corporate information to the public. It determines the appropriate level of disclosure for IFC as a publicly owned institution working in the private sector and respecting the business confidentiality of its client companies. The policy improves IFC's process for disclosing information as well as expanding the types of information disclosed.

A disclosure policy advisor will be appointed to serve as an internal review mechanism and respond to complaints from stakeholders who believe their request for information has been unreasonably denied or that the policy has been incorrectly applied. The disclosure policy advisor will report directly to the Executive Vice President.

The Board also approved a new disclosure policy for IFC's Independent Evaluation Group, to take effect at the end of April 2006. For the first time, all IEG evaluation and budget documents that are distributed to the Board will be disclosed. With the change, IEG's disclosure practices will be aligned with other multilateral development banks that carry out private sector investment operations.

## OUR COMMITMENT

### New items that IFC is now committed to disclose include

- IFC's budget and business plan
- Minutes from IFC board meetings
- Annual reporting on the aggregate development impact of IFC's activities starting in 2006 (Results to be reported in 2007)
- A summary of IFC's environmental and social review of an investment
- A Summary of Proposed Investment for each investment project, featuring information on expected development impacts

## A FOCUS ON IMPLEMENTATION

IFC’s environmental and social specialists are responsible for the review, clearance, and supervision of all IFC investments in a manner consistent with IFC’s policy and performance standards.

As controversial cases show, putting policies and procedures into practice can often involve enormous complexity. Who is a stakeholder? What is legitimate environmental and social impact? When is flexibility justified in order to achieve a greater development impact over the long term? At what point do we withdraw from projects that have too negative an impact? These are all questions that our investment officers and environmental and social specialists struggle to address on a daily basis.

### FY05 COMMITMENTS BY ENVIRONMENTAL AND SOCIAL CATEGORY

Category*	Commitments in millions	No. of investments
A	\$169.09	3
B	\$2,515.26	101
C	\$1,078.54	61
FI	\$1,378.02	68

### ALL COMMITMENTS AS OF JUNE 2005 BY ENVIRONMENTAL AND SOCIAL CATEGORY

Category*	Commitments in billions	No. of investments
A	\$3.86	120
B	\$21.00	1444
C	\$5.33	637
FI	\$9.54	625
N	\$7.59	1194
U	\$2.01	289

\*See category descriptions on pg. 27.

\*\*N and U refer to projects committed before IFC began implementing environmental policies and guidelines in 1993

### STAFF DEVOTED TO ENVIRONMENTAL, SOCIAL AND INSURANCE-RELATED SUPERVISION

	FY03	FY04	FY05
Number of environmental and social (E&S) specialists	27	27	36
Number of insurance specialists	6	8	7
	FY03	FY04	FY05
Number of E&S specialists in regional offices	5	7	10
Number of E&S specialists in industry departments	7	7	11

### STAFF HOURS SPENT ON ENVIRONMENTAL AND SOCIAL APPRAISAL AND SUPERVISION

	FY03	FY04	FY05
Appraisal of new projects	20,576	21,099	21,689
Supervision of portfolio projects	12,865	9,768	10,314
Insurance-related appraisal	2,099	2,004	2,400
Insurance-related supervision and added value	3,071	3,056	4,337



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## THE SUPERVISION CHALLENGE

By William Bulmer,  
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The ability to mobilize first-class environmental and social development expertise in support of its business activities is essential for IFC to successfully meet its strategic objectives and have a leadership role in sustainability. Since the recruitment of the first environmental specialist in 1988 and the first social development specialist in 1996, the team has grown to a total of 36 specialists who provide IFC with an unparalleled resource both to assist clients and to improve its own portfolio performance.

This is a challenging time for the team. In addition to the ongoing work with the update of our environment and social policies, sector guidelines, and review procedure, we are dealing with a large volume of new business and project supervision needs.

So demands on staff are high, but the opportunities are enormous. The extensive consultations that have taken place in relation to the policy update have strengthened our belief that we are moving in the right direction and that the new policy and performance standards will provide an excellent tool to help IFC and its clients both manage risk and improve their performance. But if we are to achieve this we must be able to ensure that quality assurance procedures keep pace and that we have good performance metrics to determine our effectiveness.

The exercise of professional judgment in the context of a consistent approach to decision-making is fundamental to the services provided by IFC's

investment staff. Consistency can be achieved only through a combination of good training and a robust quality management system. The heart of such a system will be the revised environment and social review procedure that will accompany IFC's new sustainability policy and performance standards.

The procedure will capture the important decisions that are made by environmental and social specialists during the project lifecycle. It will also provide a mechanism for the peer review of complex projects, a clearance mechanism for such decision-making and a guarantee that follow-up actions are documented and acted upon.

The procedure will of course also apply to supervision activities, and an important new document will track key performance indicators during the life of an investment. These indicators will be available for use in helping assess IFC performance at the department and corporate level.

Like all enterprises, we have to deal with resource constraints. The key challenge is the limited number of staff to deal with \$6 billion in new investments per year and a portfolio of \$19 billion – both growing quite fast.

Although some new recruitment will take place, we need to work more efficiently and mobilize external resources more effectively. The new procedure should help allocate staff more efficiently on the basis of the risk of material adverse environmental or social impact.

We are increasing our field presence to react more quickly and meet client needs. We will also be looking at ways to better integrate environment and social risk management into the

programs of the investment department portfolio managers. Finally, we will continue to depend upon some external consulting help, and so it will be necessary to provide clear guidance and support to these professionals as we introduce our new policies.

The bottom line is that we rely heavily on a highly trained pool of staff. The professional judgment of those staff will be an important determinant of IFC's credibility as a sustainability leader and, more importantly, how we achieve our goals of protecting the environment and ensuring that the poor and most vulnerable are beneficiaries rather than victims of development. IFC is placing high demands on its clients to implement effective management systems to ensure quality control and good performance. We must demand the same of ourselves.

The exercise of professional judgment in the context of a consistent approach to decision making is fundamental to the services provided by IFC's investment staff.

### OUR COMMITMENT

**In our next Sustainability Report, we commit to report on**

- **Progress with implementation of the new IFC Policy and Performance Standards on Social and Environmental Sustainability**
- **The volume of business to which individual Performance Standards are being applied**
- **The environmental and social performance of our portfolio according to sector and region, and lessons from experience**