This presentation was prepared for purposes of public consultation. Feedback from this consultation will inform the formalization of the approach.
IFC is developing an Approach to Responsible Exit as part of its ongoing efforts to further and more systematically integrate how it analyzes and addresses environmental and social (E&S) issues throughout its investment project cycle, and as a result of its adoption of the Operating Principles for Impact Management and its specific commitments in a Management Response to a Compliance Advisor Ombudsman case, as detailed below.

A focus on responsible exit takes forward the Operating Principles for Impact Management, of which IFC led the development in 2019 and to which it is a signatory.

- “Principle 7: Conduct exits considering the effect on sustained impact: When conducting an exit, the Manager shall, in good faith and consistent with its fiduciary concerns, consider the effect which the timing, structure, and process of its exit will have on the sustainability of the impact.”

- “Principle 8: Review, document, and improve decisions and processes based on the achievement of impact and lessons learned: The Manager shall review and document the impact performance of each investment, compare the expected and actual impact, and other positive and negative impacts, and use these findings to improve operational and strategic investment decisions, as well as management processes.”

Work on responsible exit is also rooted in IFC’s Management Response to the Compliance Advisor Ombudsman (CAO) Compliance Investigation Report for Corporación Interamericana para el Financiamiento de Infraestructura (CIFI) (2020), in which IFC committed to “review IFC’s investment operations, policies and procedures as they relate to aspects of exit and define IFC’s approach to ‘responsible exit.’”

Key Considerations in Developing Approach (1/2)

In developing an approach, IFC took into account a number of key considerations, as follows:

- **IFC’s existing policies and practices**, including:
  - The specific commitment under IFC’s Policy on Environmental and Social Sustainability that IFC “will only finance investment activities that are expected to meet the requirements of the Performance Standards within a reasonable period. Persistent delays in meeting these requirements can lead to loss of financial support from IFC,” which means that E&S issues that the investee company or sponsor is unwilling or unable to rectify may trigger an exit by IFC.
  - IFC’s Articles of Agreement, which provide, in general terms, that IFC may take actions that protect its interests, and that IFC has an obligation to revolve its funds by selling its investments to private investors whenever it can appropriately do so on satisfactory terms.
  - IFC’s board-approved equity sale policy, which expressly requires IFC to take into account developmental impact concerns by mandating that, unless exceptional cases apply, IFC will not sell its equity investments unless IFC’s role has been completed or cannot be completed.
  - Relevant practices, such as that IFC’s specialists, including E&S specialists, are consulted on particular risks that may arise in connection with an exit being contemplated, but how exactly E&S issues are taken into account in exit decision-making is not formalized.


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3 IFC, Articles of Agreement, Article III, Section 3(vi).
Key Considerations in Developing Approach (2/2)

- **Policies and practices of peer institutions**, specifically, commitments related to exit made in the context of specific projects.

- **Analysis of potential consequences of exiting or of not exiting for different relevant stakeholders**, including for project-affected communities and or clients. These include potential financial impacts, reputational and legal impacts, and E&S impacts due to the potential loss of IFC’s leverage, potential changes in the client’s capacity and commitment to address E&S issues, and the potential signaling effect of IFC’s exit more generally. Potential consequences are highly dependent on the unique circumstances of each project.

- **Additional constraints**: IFC also considered additional constraints on exit decision-making, including the following:
  - **Limits on screening purchasers**: It may be difficult to determine the ultimate beneficiary of the sale, e.g., if equity or debt is sold to distressed funds or for listed equity.
  - **Post-exit contractual limitations**: After IFC exits an investment, meaningful monitoring and enforcement of ongoing covenants may not be available due to the nature of legal remedies for contracts.
  - **Co-investors**: In syndicate or club deals, IFC may need to take into account the views of co-investors.
  - **Misplaced incentives**: There is a risk that guidelines related to responsible exit could have unintended consequences, such as if an approach included conditions to be satisfied pre-exit, leading clients to not address issues in order to prevent exit.
  - **Illiquidity**: Creating exit opportunities for any investment depends on critical commercial and market factors to match a willing seller with a willing buyer. IFC’s exits often include the sale of instruments that are illiquid, meaning they are not easily sold or exchanged. Accordingly, when considering the timing, structure, and process of any exit, there may only be a limited window of time to make the sale and a relatively small number of interested purchasers.
Proposed Approach: Key Elements

Preparing for Exit:

• IFC would take actions taken early in the project cycle to reduce the likelihood of E&S issues being present at exit and to strengthen the ability of IFC and its clients, respectively, to act to address them if they are. Actions under consideration include strengthened assessments – specifically of IFC’s leverage or influence and of client preparedness for implementing E&S Action Plans (ESAPs) and for remedial action – costing ESAPs and exploring options for contingency financing; and additional contractual provisions.

Responsible Exit Principles:

• Overview: IFC would apply the “responsible exit principles” to inform decision-making on whether and how to exit. Project teams would apply each of the principles in turn, considering whether the proposed exit is aligned with the principle and exploring any additional actions that can be taken to strengthen alignment. The principles are designed to be applicable to a broad range of factual circumstances.

• Process: The responsible exit principles would be considered when exit is being contemplated, whether it is being contemplated due to financial considerations, E&S considerations (e.g., non-compliance with E&S requirements), reputational considerations, or otherwise. The principles would be taken into account throughout the process of exit decision-making. The thought process would be documented including analysis of the principles, including additional actions taken.

• Scope: IFC is currently considering applying the principles when contemplating an active exit from all projects in which (i) there is an associated open CAO case past eligibility and/or (ii) the project’s environmental and social performance is unsatisfactory. An active exit is one in which IFC proactively decides to exit from an investment or agrees to amend the terms of the transaction documents to enable the client to exit in circumstances where such exit, at that time, would not have otherwise occurred without action by IFC. IFC could take action due to financial considerations, E&S considerations (e.g., non-compliance with E&S requirements), reputational considerations, or otherwise. The majority of equity sales, as well as debt accelerations or situations in which IFC has the right to consent to loan prepayment, are active exits. IFC would also apply the principles in projects not meeting either of these criteria, with such additional projects to be identified on an ad hoc basis by project teams or management.
Proposed Approach: Principles 1 and 2

**PRINCIPLE 1. SUPPORT THE ACHIEVEMENT AND SUSTAINABILITY OF TARGETED DEVELOPMENT IMPACT.** IFC’s exit should support the achievement and sustainability of the contemplated development impact of the project. IFC should consider the project outcomes that have been achieved and whether remaining invested would or would not enhance the likelihood of achieving or sustaining that impact or mitigating significant adverse results, within a timeframe that is substantially consistent with the contemplated timeline for such investment.

**Guiding Questions:**
- Can IFC protect the impact and outcomes that have been achieved?
- Has the targeted development impact (including specific project outcomes) been achieved? Can the development impact still be achieved?
- Are the purchasers of IFC’s equity or debt (if known or knowable) mission-aligned and capable (i.e., positive E&S track record, experience in the industry, supportive of the impact objectives, and with a rationale for the investment that is consistent with the achievement and sustainability of the development impact)?
- For equity investments in which IFC has taken nominee director rights, consider the potential impacts achieved (e.g., enhancing a company’s E&S capacity) through exercising such rights.

**PRINCIPLE 2. ADDRESS E&S ISSUES.** IFC’s exit should, to the extent practicable:

a. be consistent with the ESAP and other action plans or structured in a way that enables the issues identified in such plans to be addressed prior to exit;

b. not increase or exacerbate existing E&S issues;

c. consider whether, and if so, how to address and/or mitigate any other E&S risks identified during the life of the investment (i) that could materialize post exit and cause imminent and serious harm to public health, safety or security, and/or imminent and significant adverse impacts on the environment and (ii) which IFC has the means to address and/or mitigate, including through support to its client.

**Guiding Questions:**
- If significant E&S issues exist that IFC’s E&S guidance is positively impacting or is reasonably likely to positively impact, consider whether the exit can be delayed or conditions precedent added to the sale to support addressing E&S issues.
- Take into account the risk of reprisals against civil society organizations (CSOs) and project-affected communities following exit.
Proposed Approach: Principles 3, 4, and 5

**PRINCIPLE 3. USE LEVERAGE PRE-EXIT.** IFC should use the practicable leverage at its disposal to implement the ESAP and other action plans and to address and/or mitigate any other adverse E&S risks and impacts that are both likely and severe, including considering any remedial actions.

**Guiding Question:**
- Consider whether IFC has remaining leverage it can deploy through remaining invested versus any leverage it may have in association with exit.

**PRINCIPLE 4. CONSIDER INSTITUTIONAL CONSTRAINTS.** IFC’s exit should be consistent with IFC’s private sector development mandate (Article I); operational principles (Article III, Section 3), and risk considerations (including significant reputational damage and legal liability).

**PRINCIPLE 5. CONSIDER PRECEDENTIAL IMPLICATIONS.** IFC’s exit should not be counter to the appropriate standard for IFC to follow in similar cases.

**Additional Guidance:** Applying the principles would also entail the following:
- The project team will take into account the risk of reprisals against civil society organizations (CSOs) and project-affected communities following exit.
- The project team will analyze possibilities for, and, where feasible given the circumstances of the exit, define a stakeholder engagement approach with, individuals and communities that may be impacted by the proposed exit and any related actions. This will allow IFC to identify and pursue opportunities for meaningful stakeholder engagement.
Next Steps

• **Compliance Advisor Ombudsman (CAO):** We appreciate the insights shared by the CAO during our discussions with them and look forward to reviewing their advisory note on Responsible Exit, which we understand will present the findings of a landscape study on how responsible exit is being framed and approached by a range of actors, including IFC.

• **Pilot:** The responsible exit principles are currently being piloted in exits from certain projects to draw lessons learned for the further development of the approach.

• **Feedback:** Feedback from this consultation, our continuing discussions with CAO, as well as lessons learned from piloting, will inform the formalization of IFC’s approach to responsible exit.

• **Finalizing Approach:** IFC anticipates finalizing the draft responsible exit principles and submitting a proposed revised approach for the consideration of the Committee on Development Effectiveness (CODE) in 2023.