



The Environmental and Social Norms of the Islamic Development Bank

Environmental and Social Norm 9 (ESN9): Financial Intermediaries



Acronyms and Abbreviations

AESR	Annual Environmental and Social Report
ACHPR	African Commission on Human and Peoples Rights
AMR	Anti-microbial Resistance
BC	Black Carbon
BMP	Biodiversity Management Plan
CBD	Convention on Biological Diversity
CBO	Community Based Organization
CDD	Community-Driven Development
CHMP	Cultural Heritage Management Plan
CO ₂	Carbon Dioxide
CITES	Convention on the International Trade in Endangered Species
CSO	Civil Society Organization
DLI	Disbursement Linked Indicator
DUC	Dam Under Construction
EHSGs	World Bank Group Environmental, Health and Safety Guidelines
ESDD	Environmental and Social Due Diligence
ESIA	Environmental and Social Impact Assessment
EITI	Extractive Industries Transparency Initiative
EPRP	Emergency Preparedness and Response Plan
ES	Environmental and Social
ESA	Environmental and Social Assessment
ESP	Environmental and Social Plan
ESMP	Environmental and Social Management Plan
ESMS	Environmental and Social Management System
ESNs	Environmental and Social Norms
FAO	Food and Agriculture Organization (of the UN)
FI	Financial Intermediary
FPIC	Free, Prior and Informed Consent
GBV	Gender-Based Violence
GCF	Green Climate Fund
GHG	Greenhouse Gas
GM	Grievance Mechanism
GMO	Genetically Modified Organism
GIIP	Good International Industry Practice
HIA	Health Impact Assessment
HSMP	Health and Safety Management Plan
HVRMs	Highly Vulnerable Rural Minorities
IDEV	Independent Development Evaluation Department
IFC	International Finance Corporation
IFI	International Financial Institution
ILO	International Labour Organization
IPP	Indigenous Peoples Plan
IPM	Integrated Pest Management
IRM	Independent Recourse Mechanism
ISS	Integrated Safeguards System
IUCN	International Union for the Conservation of Nature
IVM	Integrated Vector Management
LIMP	Labour Influx Management Plan
LMPs	Labour Management Procedures
MFI	Multilateral Financial Institution
NGO	Nongovernmental Organization
NSO	Non-Sovereign Operation
O&M	Operation and Maintenance
OHS	Occupational Health and Safety
OP	Operational Policy

OS	Environmental and Social Operational Safeguard
POPs	Persistent Organic Pollutants
PMP	Pest Management Plan
PPP	Public-Private Partnership
RAP	Resettlement Action Plan
RBF	Results-Based Financing
RCIP	Riparian Communities Involvement Plan
RHA	Risk Hazard Assessment
RMC	Regional Member Country
SDGs	Sustainable Development Goals
SEAH	Sexual Exploitation and Harassment
SEP	Stakeholder Engagement Plan
SESA	Strategic Environmental and Social Assessment
SO	Sovereign Operation
SPV	Special Purpose Vehicle
TA	Technical Assistance
UNDRIP	United Nations Declaration on the Rights of Indigenous Peoples

Introduction

1. ESN9 recognizes that strong domestic capital and financial markets and access to finance are important for economic development, growth and poverty reduction. The Bank is committed to supporting sustainable financial sector development and enhancing the role of domestic capital and financial markets. This ESN addresses the environmental and social requirements associated with intermediated financing through financial and non-financial institutions.
2. Intermediated financing partners (FIs) of the Bank are required to identify, assess, monitor and manage the environmental and social risks and impacts associated with their overall portfolios and individual subprojects, as appropriate to the nature of the intermediated financing they provide. The way in which the FI will manage its portfolio will take various forms, depending on several considerations, including the capacity of the FI and the nature and scope of the funding to be provided by the FI including the ultimate use of proceeds.
3. FIs are required to develop and maintain, in the form of an Environmental and Social Management System (ESMS), effective environmental and social systems, procedures and capacity for assessing, managing, and monitoring risks and impacts of subprojects, as well as managing overall portfolio risk in a responsible manner.

Objectives

4. The objectives of ESN9 are as follows:
 - To set out how the FI will assess and manage environmental and social risks and impacts associated with the subprojects it finances.
 - To promote good environmental and social management practices in the subprojects the FI finances.
 - To promote good environmental and sound human resources management within the FI.
 - To support the adoption of best practice standards in corporate governance, business management and corporate responsibility by enterprises supported by the Bank based upon the requirements of ESNs 1 through 10, as appropriate.
 - To encourage the consideration of environmental and social governance issues in capital market institutions such as development finance entities and stock exchanges.

Scope of Application

5. This ESN applies to Financial Intermediaries (FIs) such as financial institutions and other entities¹ that receive financial support from the Bank. The range of FIs includes (but is not limited to) public and private financial services providers such as national and regional development banks, microfinance institutions, leasing and factoring companies, bridge finance companies, private sector banks and investment funds that channel and invest financial resources in a range of economic activities across industry sectors². Financial intermediation also includes provision of financing or guarantees by FIs to other FIs. For the purposes of this ESN, the term 'subproject' refers to projects financed by FIs with support from the Bank³ and investments supported by the Bank. Where the project involves on-lending by one FI (tier one) to another FI (tier two), the term "FI subproject" will include the subprojects of each subsequent tier two FI.

6. The requirements of this ESN apply to all FIs that receive support from the Bank, either directly from the Bank or through the Client to other FIs, as follows:

- Where Bank support is provided to the FI to fund clearly defined subprojects the requirements of this ESN will apply to each of the subprojects.
- Where Bank support is provided to the FI for a general purpose⁴, the requirements of this ESN will apply to the entire portfolio of the FI's future subprojects from the date on which the Financing Agreement becomes effective.

7. Where an FI receiving support from the Bank provides financing or guarantees to other FIs, the FI will apply the requirements of this ESN and will cause each subsequent FI to also apply the requirements of this ESN.

¹ For example, passive equity funds, insurance corporations, commodity exchange entities, capital markets and capital market support institutions.

² Such FIs use various financial products such as equity investment, subordinated debt, guarantees, project finance, corporate finance, medium and small enterprise finance, microfinance, housing finance, leasing, and trade finance. This ESN covers all types of financing and financial products provided to and by FIs that are targeted to productive business activities..

³ "FI subprojects" are defined as projects or activities financed by an FI. Where an FI provides financing or guarantees to other FIs, "FI subprojects" are defined as projects or activities financed by the latter FI with support from the former FI..

⁴ Support for a 'general purpose' means that the support cannot be traced to a specific FI subproject or specific types of financing.

Requirements

A. General Requirements

8. FIs will put in place and maintain an ESMS to identify, assess, manage, and monitor the environmental and social risks and impacts of FI subprojects on an ongoing basis. The ESMS will be commensurate with the nature and magnitude of environmental and social risks and impacts of FI subprojects, the types of financing, and the overall risk aggregated at the portfolio level⁵. Where the FI can demonstrate that it already has an ESMS in place, it will provide adequate documented evidence of such an ESMS, indicating which elements (if any) will be enhanced or modified to meet the requirements of this ESN⁶.

9. The FI's ESMS will include the following elements: (i) environmental and social policy; (ii) clearly defined procedures for the identification, assessment and management of the environmental and social risks and impacts of subprojects; (iii) provisions for the necessary organizational capacity and competency, including the budget; (iv) monitoring and reporting of environmental and social risks of subprojects and the portfolio; and (v) an external communications mechanism and provisions for information disclosure and grievance mechanism, including on subprojects⁷ as appropriate.

10. Where FI subprojects are considered by the FI to have minimal or no adverse environmental or social risks or impacts, they will still be expected to comply with any and all national laws and regulations⁸.

11. The FI will review and adjust, in a manner acceptable to the Bank, its ESMS from time to time, including when the environmental and social risk profile of its portfolio changes significantly

⁵ For the purpose of assessing the adequacy of the ESMS, the FI portfolio means the portfolio of current and/or proposed subprojects to which this ESN applies, as described in paragraph 5.

⁶ Where the Bank is providing support to a project involving Financial Intermediaries (FIs), and other multilateral or bilateral funding agencies will provide or have already provided financing to the same FIs, the Bank may agree to rely on the requirements of such other agencies for the assessment and management of environmental and social risks and impacts of the project, including the institutional arrangements already established by the participating FIs, provided that such requirements will enable the project to achieve objectives materially consistent with those of this ESN and other ESNs, as applicable. Following review by the Bank, an FI may be required to enhance its ESMS, as deemed necessary by the Bank.

⁷ Disclosure at the project site of IsDB's involvement in sub-projects, of the existence of the project-level Grievance Redress Mechanism (GRM), the Bank's Independent Recourse Mechanism (IRM) and ensuring that this information is clearly visible, accessible and understandable to affected communities.

⁸ This will rely on an assessment of the risks of the potential FI subprojects that the FI is proposing to finance, and the capacity of the FI. This may apply to certain retail financial products, such as consumer loans or credit cards.

12. For FI subprojects to be funded (directly or indirectly, in all or in part) or participated or guaranteed by the Bank or for all FI subprojects, as the case may be pursuant to paragraph 6 above, the FI will comply with any restrictions or exclusions in accordance with ESN1 and/or in the Financing agreement(s) and apply relevant national law. In addition, the FI will apply the relevant requirements of the ESNs to any FI subproject that involves resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on vulnerable groups and highly vulnerable rural minorities such as Indigenous Peoples or significant risks or adverse impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural heritage.

13. An FI may be required to adopt and implement additional or alternative environmental and social requirements, depending on the nature of the FI, its activities, the sector or countries of operation, and the environmental and social risks and impacts of the potential FI subprojects⁹.

14. The FI will provide a safe and healthy working environment. Accordingly, relevant aspects of ESN2 will apply to the FI itself. The FI will have in place and maintain appropriate labour management procedures, including procedures relating to working conditions and terms of employment, non-discrimination and equal opportunity, grievance mechanisms and occupational health and safety. The FI will provide adequate documented evidence of such procedures.

B. Environmental and Social Management System

Environmental and Social Policy

15. The environmental and social policy of the FI will be endorsed by the FI's senior management and will include organizational commitments, objectives, and performance benchmarks with regard to the FI's environmental and social risk management. The policy will clearly state applicable requirements for FI subprojects, and will include the following:

- All FI subprojects will be prepared and implemented in accordance with the relevant national environmental and social laws and regulations.
- All FI subprojects will be screened against exclusions in the Financing agreement¹⁰, including the Bank Group's Negative List.
- All FI subprojects will be screened for environmental and social risks and impacts.
- All FI subprojects which involve resettlement (unless the risks or impacts of such resettlement are minor), significant risks or adverse impacts on HVRM or significant risks or adverse impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural

⁹ These will be incorporated into the ESMS, the environmental and social procedures and/or set out in the Financing agreement(s).

¹⁰ These will be set out in the Financing agreement(s) between the FI and the entity providing financing to the FI, and will reflect the exclusions in the Financing agreement pursuant to which the Bank provides its support.

heritage, will apply relevant requirements of ESNs¹¹.

Environmental and Social Procedures

16. The FI will put in place and maintain clearly defined environmental and social procedures that reflect and implement the FI's Environmental and Social Policy. The procedures will be proportionate to the nature of the FI and the level of potential environmental and social risks and impacts associated with the FI subprojects¹². The procedures will address internal reporting and approval pathways.

17. The FI's environmental and social procedures will include measures to:

- Screen all FI subprojects to be funded (directly or indirectly, in all or in part) or participated or guaranteed by the Bank against any exclusions in the Financing agreement, including the Bank Group Negative List.
- Screen, review and risk rate¹³ the subprojects according to their potential environmental and social risks and impacts.
- Require that all the aforementioned FI subprojects are assessed, prepared and implemented to meet relevant national law and regulations. In addition, where an FI subproject involves resettlement (unless the risks or impacts of such resettlement are minor), significant risks or adverse impacts on HVRM or significant risks or adverse impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural heritage, the relevant requirements of the ESNs are applied¹⁴.
- Ensure that the measures needed to satisfy the requirements of (c) above are set out in the Financing agreement between the FI and the sub-Client or investee company.
- Monitor and regularly update environmental and social information on FI portfolios and subprojects, including by site visits and by requiring subprojects report regularly to the FI on their environmental and social performance in a manner satisfactory to the FI.
- If the risk profile of an FI subproject increases significantly, apply all relevant requirements of the ESNs¹⁵ and document these appropriately; and
- Monitor the environmental and social risk of the FI portfolio and prepare and submit to the Bank regular progress reports in line with the requirements in the ESMS. Quarterly reports are required as a minimum though the Bank may require additional reporting (including monthly) depending on the risks and impacts associated with the project and subprojects.

¹¹ The relevant requirements of the ESNs will be applied to such projects regardless of how such projects are categorized under the FI's own risk categorization system as referred to in paragraph 18. The environmental and social procedures will require such FI subprojects to conduct stakeholder engagement pursuant to ESN10 in a manner proportionate to the risks and impacts of the FI subprojects.

¹² Where the FI already has appropriate environmental and social procedures in place, it will provide adequate documented evidence of such procedures to the Bank and, following review, will enhance them, as deemed necessary.

¹³ A three-tier risk rating is sufficient (High, Medium, Low).

¹⁴ The environmental and social procedures will require such FI subprojects to conduct stakeholder engagement pursuant to ESN10 in a manner proportionate to the risks and impacts of the FI subprojects.

¹⁵ The 'relevant requirements of the ESNs' will relate to the reasons for which the risk profile of the FI subproject has increased.

Risk Rating of Subprojects

18. As part of the environmental and social procedures, the FI will develop and adopt a risk rating/categorization system for subprojects with clearly defined risk categories. The categorization system will take into account (i) the nature and magnitude of environmental and social risks and impacts of subprojects; (ii) sectoral and geographical context; (iii) type of financing. The risk categorization will inform the scope and nature of the FI's environmental and social due diligence and risk management of its subprojects. Such a categorization system will allow for a systematic aggregation and analysis of risk at the portfolio level.

19. As part of its environmental and social risk categorization system, the FIs will categorize any subproject which involves resettlement (unless the risks or impacts of such resettlement are minor), adverse risks or impacts on vulnerable groups or significant risks or impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural heritage, as high risk.

Organizational Capacity and Competency

20. The FI will develop and maintain organizational capacity and competency for implementing the ESMS with clearly defined roles and responsibilities¹⁶. The FI will designate a representative of the FI's senior management to have overall accountability for environmental and social performance of the FI subprojects, including the implementation of this ESN and ESN 10 and resources necessary to support such implementation. The representative will: (a) designate staff to be responsible for day-to-day implementation of the ESMS, including the environmental and social procedures (some responsibilities should be assigned to credit/loan officers); (b) ensure that adequate resources are available for management of and training in environmental and social issues; and (c) ensure that adequate technical expertise, either in-house or external expert support, is available to carry out due diligence and manage the environmental and social risks of the FI subprojects, including providing implementation support as required.

21. The FI will ensure that the requirements of this ESN and ESN2 are clearly communicated to all relevant FI personnel¹⁷, and ensure that relevant personnel have the necessary knowledge and capabilities¹⁸ for managing environmental and social risks in accordance with the FI's ESMS.

Monitoring and Reporting

22. The FI will monitor the environmental and social performance of the FI subprojects in a

¹⁶ The ESMS must be in place and adequately resourced before lending or investing can take place using Bank support.

¹⁷ Such personnel may include human resources, investment, legal, and credit officers and security personnel.

¹⁸ Including by providing appropriate training.

manner proportionate to the risks and impacts of the FI subprojects and provide regular progress reports to the FI's senior management. This will include periodic review of the effectiveness of the FI's ESMS.

23. The FI will promptly notify the Bank of any significant accidents or incidents associated with FI subprojects. If the risk profile of an FI subproject increases significantly, the FI will notify the Bank and will apply relevant requirements of the ESNs in a manner agreed with the Bank, as set out in the ESMS. The FI will monitor the measures and actions agreed, and report to the Bank as appropriate.

24. The FI will submit to the Bank:

- Quarterly Reports on the environmental and social aspects of subprojects and on the overall portfolio, in a form and substance satisfactory to the Bank.
- Annual Environmental and Social Reports on the implementation of its ESMS, including its environmental and social procedures, this ESN and ESN2, as well as the environmental and social performance of its portfolio of FI subprojects. The annual report will include details of how the requirements of this ESN are being met, the nature of the FI subprojects financed through the project, and the overall portfolio risk, profiled by sector.

C. Stakeholder Engagement

25. The FI will require FI subprojects to conduct stakeholder engagement in a manner proportionate to the risks and impacts of the FI subproject, and which reflects the type of FI subprojects it will finance. The relevant provisions of ESN10 will be included in the FI's environmental and social procedures. In certain circumstances, depending on the risks and impacts of the project and the type of FI subprojects it will finance, the Bank may require the FI to be engaged in stakeholder engagement.

26. The FI will put in place procedures for external communications on environmental and social matters proportionate to the risks and impacts of the FI subprojects, and the risk profile of the FI's portfolio. The FI will respond to public enquiries and concerns in a timely manner.

27. The FI will disclose its ESMS through the FI's website, if a website exists, and permit, in writing, the Bank to disclose it on the Bank's website, in accordance with paragraph 59 of the ESSP.

28. The FI will require its sub-Clients to comply with national requirements for disclosure of information. In addition, the FI will require subprojects to disclose any project-related documents¹⁹

¹⁹ For example, environmental and social assessment reports, resettlement plans and vulnerable group plans.

required (a) by the application of the ESNs; (b) for any FI subprojects categorized as high risk in accordance with the FI's its own categorization system; and (c) any environmental and social monitoring reports relating to (a) or (b). The FI will require the subprojects to disclose IsDB's support to them, the existence of the project-level Grievance Redress Mechanism (GRM), the Bank's Independent Recourse Mechanism (IRM) and ensure that this information is clearly visible, accessible and understandable to affected communities.