

Environmental Risk Assessment Guidance from the EBRD

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What is the EBRD?

- An Investment Bank with Public Shareholders:
 - owned by 62 countries and supranational shareholders (EU; EIB)
 - AAA-rated international financial institution founded in 1991
 - 1000 employees
- Mandate: facilitate the transition to market economies
- Largest single investor in the region
- Capital base of €20 billion and Business Volume of €30.3 billion (end of 2005) - Annual business volume for 2005 = €4.3 billion invested in 151 projects :
 - 34% of business volume devoted to FIs to support local enterprises
 - 22% -infrastructure projects
 - 17% - energy sector
 - 9% - manufacturing
 - 18% agribusiness, property/tourism and telecommunications



32 offices in 28 countries



EBRD's Charter

"... To promote in the full range of its activities, environmentally sound and sustainable development"



EBRD and Environmental Guiding Principles

- Environmental and Sustainable Development Mandate – Responsibility as a public institution
- Core Business Issues – legal, financial and reputation-based- Private sector orientation
- Revised Environmental Policy (2003) and Public Information Policy (2003) and Independent Recourse Mechanism (2004)



Definition of Environment

- Ecological aspects
- Worker health and safety
- Core labour standards
- Community issues (e.g. cultural property)
- Involuntary resettlement
- Impacts on indigenous peoples



Implementation of the EBRD Environmental Mandate

- financing projects in sectors such as environmental infrastructure and energy efficiency
- applying environmental requirements to all of the Bank's operations
- including environmental components in operations to reduce atmospheric emissions and industrial waste-water discharges, to promote energy, resource efficiency, waste recovery, recycling, and clean technologies
- providing technical assistance to promote environmentally proactive measures



Key sustainable development challenges pursued by the EBRD

- Support market transition and provide access to capital
- More efficient use of energy and other resources
- Replacing obsolete with modern technologies and processes
- Introducing best industrial and resource extraction practices
- Improving environmental, health and safety management systems
- Improving public participation in decision making
- Supporting development of economic instruments for reform



Other Challenges for EBRD and its Clients

- Sustainable development perceived as expenditures that do not generate revenue
- sustainability is often seen to slow down progress towards competition goals
- an abundance of legislation but poor enforcement
- legislation changing rapidly



Other Challenges for EBRD and its Clients

- harmonisation with EU standards and Directives
- management continues to remain unengaged in a company's environmental matters (reactive vs proactive)
- environmental liabilities unclear (lack of clean-up standards)



EBRD Approach and Initiatives

- The EBRD commits on average around €3 billion in new projects every year
- Nearly 20 per cent of this commitment is devoted to environmental improvements
- Half of this is accounted for by municipal and energy efficiency projects
- The other half is associated with environmental improvements on industrial and infrastructure projects



EBRD Approach and Initiatives

- Promoting SMEs and fostering entrepreneurship (private sector 70% of €20.2 billion investment portfolio; €199 million of bank lending devoted to SMEs in 2005 through FIs)
- Transfer of Environmentally Sound Technologies and processes
- Investing in Municipal and Environmental Infrastructure (€ 290 million in 2005 supporting 13 municipal infrastructure projects across ten countries)
- Developing Energy Sector Initiatives (energy efficiency, addressing Climate Change, supporting renewable energy)
- Supporting nuclear safety (NSA - pledged more than € 2 bln)
- Improving Transport Infrastructure



EBRD Approach and Initiatives

- The EBRD requires environmental due diligence on all of its projects under preparation (audits, EIA, risk assessment)
- Environmental Action Plans (EAPs) are developed to bring a company's operations into compliance with applicable regulatory requirements (national, EU, WB)
- Heavy industrial modernisation and other projects in environmentally significant sectors undertaken once the Bank is satisfied with clients' environmental management capacities



Environmental Due Diligence (EDD)

- A Tool for Business Decisions-

- Decide if a proposed project should be financed and if so, the way in which environmental issues should be incorporated in the project.
- Identify risks, their magnitude and mitigation measures (e.g. past contamination, liabilities, legal compliance, potential impacts, reputation) and opportunities (e.g. energy efficiency, environmental performance).
- Identify public concerns, disclose information, consult with stakeholders and the public



Criteria to Determine Classification

- Use of Bank funds (project financing, corporate loan, working capital, convertible loan, equity investment, guarantee)
- New facilities or modification to existing ones with associated risks
- Will the use of Bank's funds result in environmental impacts
- Are these impacts significant and can they be readily identified and mitigated
- Is the project high risk from social or labour standards perspective (country, sector, client, resettlement, redundancies)
- Stage of the environmental approval by the host country and the due diligence of other financing institutions (when it comes to the Bank)
- Validity of the host country approval (a gap analysis)
- Environmental record of the Sponsor and the other involved parties



Environmental Standards

- National law (generally in line with international good practice in EBRD COO)
- EU environmental standards as applicable at a project level
- Good international practice including WBG guidelines
- Applicable international conventions
- IFC Policies (indigenous peoples, involuntary resettlement, cultural property)
- FIs – minimum national standards



Environmental Action Plans (EAP, ESAP, EMP, EMAP)

- Key issues and actions, implementation schedule, associated costs, prioritisation of actions,
- Where safety risks or serious non-compliance agreement with regulatory authorities
- Phased approach but generally ahead of EU accession schedule
- Recently emphasis on environmental management systems



Public Disclosure

- Guided by EBRD Public Information Policy and Environmental Policy
- Meaningful consultation
- Diversity of implementation methods and tools

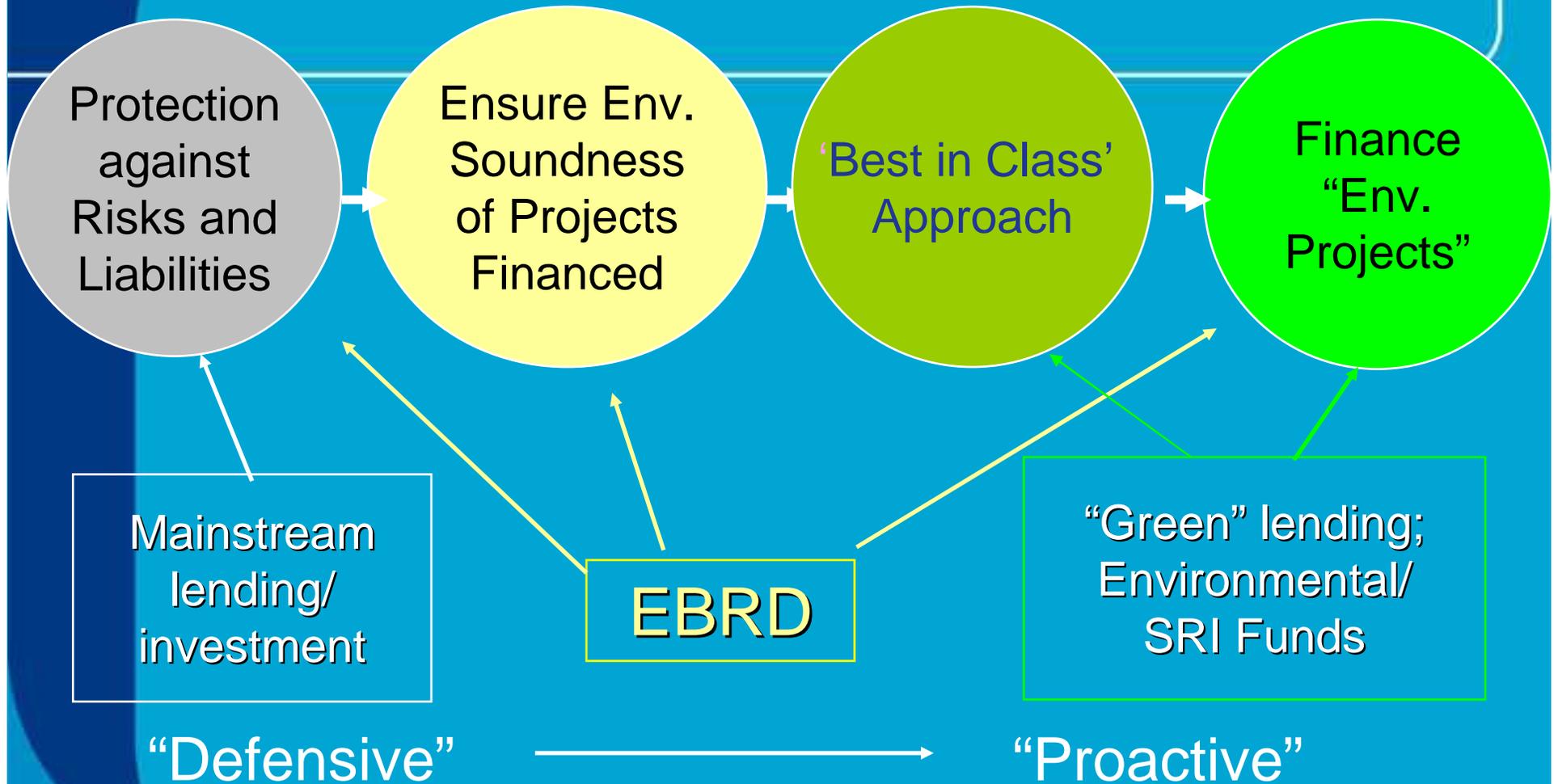


Specific Environmental Requirements for FIs

- Adopt and Implement EDD procedures satisfactory to the EBRD
- Require clients comply at a minimum with local/national standards
- Comply with Environmental Exclusion and Referral Lists
- FIs to monitor environmental performance of sub-projects
- Periodic (usually annual) reporting to EBRD
- FIs encouraged to disclose environmental information



Why FIs consider environmental issues



Factors Affecting Risk Level for Banks

Business activity

Consider overall sector risk, regulatory structure and future market developments

Deal size and term

The size of the deal will define the potential loss, while the term will affect the predictability of risk

Collateral / guarantees

Assess value of collateral and any environmental risk that would be assumed in the event of foreclosure

Management capability

Consider ability to manage current and future environmental risks alongside traditional parameters



Environmental Due Diligence Process

- Screening:
 - this helps determine (1) applicable environmental standards (b) what appraisal action is needed
- Appraisal:
 - level of effort depends on category & case-specifics
 - E.g.: desk-top review of environmental permits; Environmental Audit; Environmental Impact Assessment
- Approval - including environmental risk mitigation if required
- Supervision - continued compliance; implementation of agreed mitigation measures



EBRD examples

- A loan to an electronic goods manufacturer in the Czech Republic. Security package included pledge on land. The client went bankrupt and EBRD became the owner of the land, which turned out to be contaminated. The contamination was not properly assessed at the due diligence stage. The National Property Fund requested that the land should be cleaned up. The cost of the clean up exceeded the value of the land and as a result the Bank made loss.



EBRD examples

- Equity investment in a white goods manufacturing in country X. Due diligence did not identify soil and groundwater contamination. When a strategic investor wanted to buy the company several years later, they brought their own consultants who detected the contamination and the investor asked for a significant reduction of the selling price. As a result the Bank made a loss selling below the level of the original investment.



Banks and Environment – Equator Principles

- Leading Commercial Banks and IFC have signed up to the Equator Principles
- Environmental assessment on all project finance deals over 10 mln USD
- Many commercial lending institutions very sensitive to environmental issues
 - Liability; and
 - Reputation



EBRD's Environmental Capacity Building Programme

- 200+ FIs trained
- Mostly FI-specific
 - Tailored procedures
 - “paper” v CD Rom
- Some product specific group training
- Delivered by:
 - consultants (mainly)
 - Bank Environment Staff
- On-going guidance/hand-holding



EBRD Environmental Risk Management Manual

- Computer based, internet style, “point & click” reference tool
- Key areas:
 - Procedures: 4 step process for environmental appraisal of loans
 - Education: background information on sources of risk & key environmental risk management activities
 - Supporting Tools: reference materials including checklists, contacts, sectoral guidelines, reporting formats

Developed with support from

PRICEWATERHOUSECOOPERS

Version 3

Financing the economic transition in central and eastern Europe and the CIS

Environmental Risk Management for Financial Institutions



European Bank
for Reconstruction and Development



Electronic manual - Overview

Menu navigation

Environmental Procedures

- Lending
- Investment
- Other transactions

Education

Background guidance on sources of risk, key EDD activities and case studies

Supporting tools

Checklists, formats, regulatory overviews, sub sectoral guidelines, etc



Electronic Manual (CD-ROM)

- The manual is downloadable from the EBRD website: <http://www.ebrd.com/enviro/init/erm.htm>
- CD-Rom available in the following languages: English, Russian, Romanian, Latvian, Lithuanian, Polish, Bulgarian and Czech
- To obtain copies contact Anne Maria Cronin, Environment Department (Cronina@ebrd.com)



Conclusion

- Financial Institutions will only invest in the best projects
 - Environmental standing often reflects overall performance
- Environmental Risk is one of the issues more and more institutions look at.
 - Stakeholder issues
- Transparency and public consultation are a major focus of many international institutions and EU
 - Poor consultation can result in major delay to projects.
- Financial sector needs to consider broader European issues.

