Introductory Training Workshop (ITW) on

Identification and Evaluation of Environmental and Social Risk in Credit Processes

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Istanbul, 26th March, 2013
Introduction

- Part of UNEP FI’s support to build capacity within the FI sector to facilitate sustainable development
  - [www.unepfi.org](http://www.unepfi.org)
- Taste of the UNEP FI ESRA course
- Share experience
“What are the E&S risks?”

- Project Finance: Gold mining, Turkey; Hydropower project, Turkey
- Trade finance: Commodity trader, Singapore
- Corporate Finance: Thermal power plant operator, Turkey
- Property Finance: Apartments in Sao Paolo, Brazil
- SME lending: Russian confectionary
Turkish dam threatens town that dates back to the bronze age
Hasankeyf has survived drought, war and empire, but it could be flooded out of existence within a few years

Constanze Letsch in Hasankeyf
The Guardian, Friday 20 May 2011 17.48 BST

Hasankeyf has 'housed all the civilisations of Mesopotamia', but now faces being submerged by a dam project. Photograph: Bülent Kilic/AFP/Getty Images

It is one of the oldest continuously inhabited settlements on Earth, a town on the banks of the Tigris that dates back to the bronze age.

Over the years it has survived the rise and fall of empires, drought, war and the harsh vicissitudes of nature.

Turkey’s Great Leap Forward risks cultural and environmental bankruptcy
Turkish government's rush to build dams, hydro and nuclear power plants angers villagers and environmental campaigners

Flachra Gibbons and Lucas Moore in Ankara
The Guardian, Sunday 29 May 2011 18.56 BST

Work was halted on a massive dam project in Hasankeyf three years ago after the ancient city was flooded. Campaigners fear the government will go ahead with the dam regardless. Photograph: Alamy

Every springtime Pervin Çoban Savran takes her camels and sheep up into the Taurus mountains of southern Turkey, following the same routes along the Goksu river that Yoruk people like her have taken for more than 1,000 years. To many Turks these last nomadic tribes are symbols of the soul of their nation.
Lessons learnt?

- Risk does not always come from obvious sources
- Risk can arise in different types of financing
- Environmental and social risks can be a financial risk and not just a reputational risk
- Reputation is hard to price - until you have lost it.
E&S Risk Management

1. Identification of E&S risks
2. Categorisation
3. Assessment of environmental and social risks
4. Managing client compliance
**Process Integration**

**Marketing**
- S&E position in marketing material
- Information available on S&E risk analysis

**Origination**
- Initial project & client screening & appraisal
- Exclusion lists
- Presentation of financing proposal to Client, including S&E appraisal

**Know Your Client**
- Filter for anti-money laundering, terrorism

**Technical/Due Diligence**
- Categorisation
- S&E Assessment
- Independent reviews
- Process findings & establish deal conditions

**Term Sheets/investment documentation**
- S&E requirements included in loan documentation

**Credit Approval & Review of Legals**
- Deal review against internal S&E standards

**Deal Conclusion Forum**
- Presentation to Client
- Agree to final terms
- Closure
- Disbursement

**Monitoring & Annual Reviews**
- Client submits monitoring reports
- Engagement over non-performance
E&S Risk Management

Technical/Due Diligence

- Categorisation
- S&E Assessment
- Independent reviews
- Process findings & establish deal Conditions

Loan documentation Approvals & Disbursement

- S&E requirements included in loan documentation
- Credit review & approval
- Presentation to client
- Agree to final terms
- Closure
- Disbursement

Monitoring & Annual Reviews

- Client submits monitoring reports
- Independent verification
- Engagement over nonperformance
E&S Risk Management

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Analysing the Context:
The Changing Nature of Risk Assessment
Risks to the client

- Market loss
- Disinvestment
- Loss of operating license
- Strike, sabotage
- Shutdown, delay
- Campaigns
- Negative publicity
- Increased cost
- Loss of
- Contract loss, boycott

- Shareholders
- Employees
- Government
- NGOS
- Media
- Clients
- Insurers
- Financiers
- Export market Regulators
- Community
- Company

- Resources for sustainability
- Innovative financing for sustainability
Risks to the FI

• **Credit Risk**
  – defaults
  – payment rescheduling

• **Market Risk**
  – sector-wide practices
  – market devaluation

• **Guarantee Risk**
  – defunct / devalued collateral

• **Legal Risk**
  – potential transfer of liability from borrower to lender

• **Funding Risk**
  – access to capital
  – cost of funds

• **Reputational Risk**
  – national
  – international
Risks to the Client

- Shareholders
- Export market regulators
- Clients
- Community
- Employees
- NGOs
- Government
- Media
- Financiers
- Insurers
- Long-term investors
- Open markets
- Reduced cost
- Better cover/Reduced cost
- Stable markets, premium pricing
- Operating license
- Retention
- Renewal, expansion
- Cooperation
- Reputational benefits

Company
Purpose of analysing the context:

- To detect and assess possible environmental and social risk that the project/company activities might generate
- To establish the company’s E&S performance against appropriate standards
- It is a general enquiry to establish the need for further follow up and research.
Aspects to Analyse

• Type & scope of the project – associated & related facilities
• Sector Risk
• Market
• Location
• Third party risk
• Client commitment and capacity
Challenges

• Access to information
• Client willingness, resistance
• Reliability of information
• Benchmarks for performance
  – National standards
  – EU directives and standards
  – IFC Performance Standards and EHS guidelines
E&S Risk Management

1. Identification of S&E risks
2. Categorisation
3. Assessment of social and environmental risks
4. Managing client compliance
Project Categorisation

• A screening process to categorise a project based on the nature and magnitude of its potential impacts

• For the purpose of determining level of social and environmental risk assessment and management required
## Definitions

<table>
<thead>
<tr>
<th>Category</th>
<th>Characteristics</th>
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<tbody>
<tr>
<td>A</td>
<td>Potential significant adverse social or environmental impacts that are <strong>diverse, irreversible or unprecedented</strong>. No standard mitigation measures.</td>
</tr>
<tr>
<td>B</td>
<td>Potential limited adverse social or environmental impacts that are few in number, generally site-specific, largely reversible and readily addressed through standard mitigation measures.</td>
</tr>
<tr>
<td>C</td>
<td>Minimal or no adverse social and environmental impacts.</td>
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</tbody>
</table>
Categorising Projects

The category of a project would depend on:

- Type and sector
- Location
- Sensitivity
- Scale
- Nature and magnitude of potential impacts
- Related and associated activities
- Supply chain
- Client profile
Tools

- ER002 form: an environmental screening and categorisation form
- ER003: economic activities according to risk criteria
- ER003A: project selection according to risk criteria
- National social and environmental impact assessment regulations
E&S Risk Management

1. Identification of E&S risks
2. Categorisation
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4. Managing client compliance
E&E Assessment

- The duration, depth and type of E&S assessment required depends on the nature, scale and potential impact of the project, company activities.
- Area of influence
- Alternatives
- Avoid, minimise, mitigate and compensate
- Increase positive impact
## S&E Assessment

<table>
<thead>
<tr>
<th>Category</th>
<th>Assessment</th>
<th>ESRA form</th>
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<tbody>
<tr>
<td>A</td>
<td>SEIA and/or audit, Action Plans, Public Consultation &amp; Disclosure</td>
<td>ER006, ER007, ER008A, ER010A</td>
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<tr>
<td></td>
<td>Independent Review</td>
<td></td>
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<tr>
<td>B</td>
<td>Environmental Audit or internal Environmental Management Analysis, Evaluation of Risks, Corrective Action Plan</td>
<td>ER008, ER009</td>
</tr>
</tbody>
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E&S Risk Management

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2. Categorisation
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Managing Client Compliance

- Action plans
- Identify conditions for financing
  - approvals, disbursements
- Inclusions into loan documentation & provisions
- Monitoring
  - all category A and B should be monitored
  - independent verification of compliance
Next English based ESRA online courses

1 - 19 April
6 - 24 May
22 July - 9 August
28 October - 15 November

See: http://www.unepfi.org/training/risk_training/index.html
Thank you!

Aneta Wisniewska  Tutor: UNEP FI