



Meeting the Social Performance Standards of International Project Finance Institutions: *Guidance for Energy Companies*

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The Social Performance Management Unit of Shell International in London and the programme on Business and Development Performance of the Overseas Development Institute, have collaborated in the preparation of a number of social performance guidance notes. This report draws substantially on a Shell Guidance Note: 'Meeting International Social Performance Requirements for Project Financing'.

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The views in the report are those of the author alone.



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Glossary

DFI	Development Finance Institution
EBRD	European Bank of Reconstruction and Development
EIA	Environmental Impact Assessment
HSE	Health, Safety and Environment
HIPC	Highly Indebted Poor Countries
HSEC	Health, Safety, Environment and Community
IFC	International Finance Corporation
IFI	International Finance Institution
JV	Joint Venture
MIGA	Multilateral Investment Guarantee Agency
NOC	National Oil Company
ODI	Overseas Development Institute
OECD	Organisation for Economic Cooperation and Development
PSC	Production Sharing Contract
SIA	Social Impact Assessment
STD	Sexually Transmitted Diseases

Executive Summary

Why Companies Seek International Project Finance

For the most part, upstream and integrated oil and gas companies are able to finance their share of development costs from internal financial resources, ie from the balance sheet. However, when working with partners in low and low-middle income countries characterised by high political and social risks, there are a number of reasons why companies might seek to secure international project finance. These include:

- ➔ to spread the elevated project risks beyond the internal resources of the company or joint venture;
- ➔ to retain influence over certain joint venture partners, such as national companies and junior partners, who might have less experience in controlling project risks;
- ➔ as a 'comfort factor' for commercial banks in providing finance;
- ➔ as a form of implicit risk guarantee (principally associated with approaching development finance institutions whose shareholders – ie governments – may have national interests related to the investment);
- ➔ to provide credibility and transparency for a potentially controversial project through association with internationally recognised environmental and social standards.

Social Risks

For international financing institutions (IFIs), sound social risk management and social performance are becoming key components of due diligence studies and project finance agreements for investments in developing countries. Social risks affecting upstream oil and gas developments include:

- ➔ the operational and reputational risks arising from the effects of construction and operations on local and indigenous communities (eg from on and off-site accidents, loss of natural resources, proximity of worker camps to communities, degradation of local water supplies and other local infrastructure);
- ➔ compliance-specific issues, such as involuntary resettlement, workers' rights, child labour in local supply chains, corruption etc.;
- ➔ inadvertent fuelling of community grievances and politically motivated violence; and
- ➔ local economic grievances from 'boomtown effects', failure of government to re-distribute tax revenues, and unfulfilled local and national employment and supplier expectations.

If left unmanaged, such risk and impacts can lead to commercial consequences for the business in both the short term (eg in relation to construction schedules and costs, production output and timely facilities maintenance) and the long term (eg reduced access to in-country growth opportunities and damage to global reputation).

Growing Importance of Social Performance within Finance Institutions

Securing international project finance – be that in the form of equity, loans (debt), export credit or other risk guarantees or insurance – requires a project to meet increasingly stringent health, safety, environmental, economic and social performance standards. Of these, **social and local economic standards are the least evolved**. The social requirements of international finance institutions often rely on either an interpretation of environmental standards and procedures, such as the Environmental Policy of the European Bank for Reconstruction and Development, or on good practice guidelines that lie outside an institution's minimum requirements, such as the good practice guidance note on social

impact assessment recently published by the International Finance Corporation. Furthermore, the SP standards of many IFIs are designed to avoid or mitigate the negative social and socio-economic consequences of a project. They are less clear on how to enhance social or local economic benefits.

As demonstrated by the current review of environmental and social standards within the World Bank Group, the evolution of social performance standards within international finance institutions is piece-meal at best. By implication, the social performance practices of companies invariably overlap not only with the stated minimum social standards of the finance institutions, but also with aspects of their environmental standards, and with the broader economic and international development aims that inform investment decisions and define aspects of project performance. At least four types of standards and guidance are thus relevant to oil, gas and mining companies as they seek to meet the social performance requirements of international project finance institutions:

- ➔ **social policy standards** – policy statements, core principles and implementing rules for managing issues such as resettlement, cultural property, indigenous peoples, child labour and worker camps;
- ➔ **economic standards and guidance** – institutional policy statements, qualitative benchmarks and assessment procedures which assist institutions and project sponsors to ensure that the investment delivers a positive economic or ‘development’ impact;
- ➔ **procedural social standards and guidance** – minimum required procedures and good practices for preparing environmental and social impact assessment studies and for social performance reporting; and
- ➔ **numerical social and environmental standards** – quantifiable social performance requirements, such as rates of staff succession and compensation levels (as well as environmental performance requirements with a social aspect, eg effluent discharges to surface water bodies).

Influence of the World Bank Group

The World Bank Group (in particular the International Finance Corporation) impacts on the way in which international finance institutions around the world manage social performance within their lending portfolio. The Group is influential not only with other multilateral and bilateral financial institutions (Asian Development Bank, UK Commonwealth Development Corporation, US and UK export credit agencies etc.), but also within commercial banks. 27 major banks are now signatories to the ‘Equator Principles’. These principles are essentially the World Bank Group’s environmental and social ‘safeguard policies’. This is important, since commercial banks, and not development finance institutions, are generally the first port of call for companies seeking international project finance.

Road Map for Compliance

The main report provides a ‘road map’ to allow companies to meet the social performance standards of international finance institutions, during both financing negotiations and project implementation. First and foremost, all negotiators need to understand that meeting the social (and environmental) performance requirements of IFIs is an incremental and iterative, process. Secondly, more so for social issues than

environmental, meeting IFI requirements rests on a joint lender-borrower interpretation of the social risks and issues affecting a project. Beyond understanding these basic concepts of iteration and joint design, certain steps need to be followed to meet the social performance requirements of IFIs:

- ➔ Identifying the dominant IFIs for social standards within the consortium of project finance institutions.
- ➔ Bringing social specialists into project finance negotiations early.
- ➔ Documenting a common understanding of the relevance to the project of the IFIs' different social performance standards. Which ones apply?
- ➔ Assessing the need for alignment of the financing institutions' social performance standards with those agreed during other project negotiations, eg joint venture partners, host country governments or environmental regulators.
- ➔ Undertaking a Gap Analysis of the company's (or joint venture's) internal social performance standards and guidance, against those of the lead project financing institutions.
- ➔ Agreeing actions to manage unforeseen social issues that fall outside of the covenants of financing agreements.
- ➔ Building the capacity of local staff and consultants to ensure social performance requirements are met and sustained over time.

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1. Introduction

1.1 Background

This report provides guidance to upstream and integrated oil and gas companies on meeting the social performance standards and good practice guidance issued by international (project) financing institutions (IFIs). It may also be of interest to smaller energy companies and joint venture partners who are considering approaching IFIs.

The report presents the findings of a six-month study undertaken by the Overseas Development Institute between May 2004 and January 2005. The contents draw substantially upon recent work commissioned by Shell International. This work generated a 'road map' for Shell businesses to assist their project partners in meeting the social performance compliance requirements of international finance institutions, in particular the World Bank Group and European Bank for Reconstruction and Development.¹

The following report broadens the commissioned work undertaken with Shell. It provides an extended and published version of the guidance aimed at companies in the hydro-carbon business who might be involved in negotiating or delivering social performance commitments to project financing institutions. A perspective on social and political risk is included. In addition, inventories of social performance requirements are given for the World Bank Group and European Bank for Reconstruction and Development, as well as standards relevant to those commercial banks who are signatories to the 'Equator Principles'.

Section 2 discusses why multi-national oil and gas companies might approach project finance institutions, highlighting the commercial importance of managing social and political risks for operations in low and low-middle income countries. *Section 3* looks at the practices of social performance within companies, with reference to the Shell Group as a case example. Categories of social performance standards within IFIs are disaggregated in *Section 4*. *Section 5* is a Road Map for companies to avoid the pitfalls in trying to meet the social performance requirements of IFIs. The Road Map includes key questions to ask at junctures in the negotiation process, and a illustrative 'gap analysis' comparing Shell Group and World Bank Group social standards. *Section 6* provides a checklist of 'dos and don'ts' for companies approaching IFIs.

The views in this paper reflect those of the author alone. The report falls under the programme on Business and Development Performance at the Overseas Development Institute. This programme works to design and align business management tools and public policy instruments to optimise the development performance of corporate investment.² Funding for this report has been kindly granted by Shell International.

1.2 Study Objectives

The objectives of the study were sevenfold:

¹ Shell International (2005 forthcoming) Meeting International Social Performance Requirements for Project Financing (internal publication) *Social Performance Guidance Note Series, No. E3*, London: Shell International, Social Performance.

² For details of the programme, see: www.odi.org.uk/PPPG/activities/country_level/odpci

- ➔ to understand better why multi-national oil and gas companies become involved in negotiations over project finance with international finance institutions (IFIs);
- ➔ to explore how the treatment of social performance standards and good practice guidance within IFIs differs from that for environmental performance;
- ➔ to understand how IFIs and companies reach agreement on which social performance issues are those that likely to form commitments in a financing agreement;
- ➔ to identify where there might be inconsistencies between the social standards agreed in project financing arrangements and those agreed with host country governments and joint venture partners, and identify management strategies;
- ➔ in relation to investments in oil and gas development, to investigate the social performance standards of two influential IFIs: the World Bank Group and the European Bank for Reconstruction and Development (EBRD);
- ➔ to undertake a Gap Analysis of the World Bank's social standards against those of Shell International; and
- ➔ to provide guidance to project managers within country businesses and joint ventures on how to participate in the negotiation and/or delivery of commitments on social performance management covenanted under project financing agreements.

1.3 Approach to Research

The conclusions reached in this report have been informed by a detailed review of the current and evolving social performance standards and good practice guidance issued by Shell International, the World Bank Group, the European Bank for Reconstruction and Development, and banks who are signatories to the Equator Principles. More limited analysis has been undertaken of the social performance standards of other oil and gas companies and IFIs. Interviews were held with staff within Shell International (the Social Performance Unit and Shell Finance Services), with the International Finance Corporation (principally the Environment and Social Development Department), and with the environmental review team of the European Bank for Reconstruction and Development.

2. Why Multi-National Companies Solicit International Project Finance

Generally upstream and integrated oil and gas companies are able to finance their share of development costs from internal resources, ie from their own Balance Sheet. However, companies are increasingly driven to look for crude oil and gas in high-risk locations, which introduces different perspectives into financing and risk management.

2.1 Reasons for Approaching IFIs

When working with partners in higher political and social risk countries (usually low or low-middle income countries³) there are a number of reasons why oil and gas development companies might participate in negotiations to secure international project finance. These include:

- ➔ to fulfil a prerequisite in the license, or other home country agreement;
- ➔ to support junior partners in gaining access to investment capital;
- ➔ to buy into an existing agreement that is already seeking external finance;
- ➔ to spread the financial risk of large development projects beyond the internal resources of the immediate business and other joint venture partners;
- ➔ to maintain influence over certain joint venture (JV) partners, such as National Oil Companies (NOCs) and junior partners, who might take on project finance but then in doing so present a risk to the project from weak compliance of financing terms;
- ➔ as a 'comfort factor' for commercial banks to loan directly, or to participate in syndicated (shared) debt;
- ➔ as a form of implicit risk guarantee, whereby additional political and regulatory project risk security is derived from developed country governments having a financial stake in the success of an overseas projects;
- ➔ to provide credibility and transparency for the project from association with internationally recognised social performance standards, especially relevant for controversial projects; and
- ➔ to invoke verification by the IFI of the project's social performance, which may help counter potential reputational dangers to the company in cases where its project partners pose a social risk, such as in the areas of business integrity, resettlement, labour standards, health and safety and conflict awareness.

Of the nine reasons cited above, the last six are all underpinned by the elevated commercial risks of doing business in countries characterised by some combination of the following: low per capita income, unstable political regimes, violent conflict, weak economies, low education levels and skills capacity, underdeveloped private sector, poor local infrastructure, chronic poverty, weak institutions and regulatory enforcement, and environmental degradation. As noted by Insight Investment – the institutional investment arm of the Halifax and Bank of Scotland Group:

³ World Bank Development Indicators Database - <http://www.worldbank.org/data/countryclass/classgroups.htm>

We suggest that the greatest challenge of corporate responsibility today lies with company activities in developing countries, for three reasons: globalisation means that more Western companies have operations or supply chains in developing countries than previously; companies operating in developing countries often face acute problems associated with poverty, disease, corruption, conflict and the abuse of human rights...; governments of developing countries are often unable or unwilling to provide the strong regulatory supervision that guides and constrains company activity in rich countries.⁴

2.2 Social Risks Defined

In contrast with oil and gas production in more industrialised countries, these socio-economic-political realities present business with a broader range of risks. *Table 1* lists some of the social risks common to oil and gas development projects in low and low-middle income countries. In the table, risks are divided into: (i) short-term risks – risks to construction schedules and direct costs, and periodic risks to production output and facilities maintenance; and (ii) long-term risks – risks of reduced access to in-country growth opportunities, ie as a foreign company exploiting a non-renewable sovereign resource, and global reputation risks.

In addition, an indication is given of the commercial consequences for the company (or joint venture) if these risks are not controlled. Note that the list of social risks in *Table 1* is by no means comprehensive. Project-specific social impact assessment (SIA) studies,⁵ combined with modified processes of project risk analysis,⁶ are methods for undertaking more detailed social risk identification and assessment.

2.3 Social Risks and Material Country Operations

For integrated, trans-national, oil and gas companies, the commercial importance of these risks is compounded by the relatively recent concentration of overall profits and capital expenditure in low and low-middle income countries.⁷

To illustrate, *Table 2* provides an analysis of the global geography of BP's operations,⁸ identifying the coincidence of material country operations (> 10% of total profit, capital or revenue, now or in the near future), with countries characterised by high social risk. In the table, 'good governance' is used as a proxy for the level of social risk, based on a composite index of six indicators of good governance: voice and accountability; political stability; government effectiveness; regulatory quality; rule of law; and control of corruption.⁹

⁴ Insight Investment (2003) *Defining Global Business Principles*, London, Insight Investment, p4.

⁵ Examples of relevant guidance on social impact assessment include:

- International Finance Corporation (2004): *Addressing the Social Dimensions of Business: A Good Practice Note*, Washington DC, International Finance Corporation – [http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/\\$FILE/SocialGPN.pdf](http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/$FILE/SocialGPN.pdf)
- IPEICA/OGP (2002) *Key Questions in Managing Social Issues in Oil and Gas Projects*, Report No. 2.85/332, London: International Association of Oil and Gas Producers/International Petroleum Industry Conservation Association

⁶ See for example: ODI/EAP/Balfour Beatty (2004) *Enhancing Social Performance in the Engineering Services Sector through the Process of Risk and Opportunities Analysis*, London: ODI.

⁷ ODI, 2004.

⁸ Countries hosting business entities within the wider Group which have a discrete management structure, and are centres of revenue generation, and/or capital and/or profit.

⁹ Kaufmann, D, et al (2003) *Governance Matters III*, Washington DC: World Bank

Table 1 Short and Long-term Social Risks, with Commercial Consequences

Social Risks and Impacts	Short-term		Long-term		Commercial Consequence ¹⁰
	Risks to construction schedule and costs	Risks to production and facilities maintenance	Risk of reduced access to in-country growth opportunities	Global reputation risks	
Resettlement – Separation of families and communities, loss of livelihood security etc., arising from relocation, resettlement or displacement owing to pipeline routing, or plant or facilities siting	✓			✓	High
Livelihoods resources – Loss, degradation or impediment to livelihood-important natural resources		✓			Low
Indigenous peoples and cultural property – Undermining of cultural values and indigenous rights; damage to non-replicable cultural property, sites having archeological, paleontological, historical, religious or unique natural values.		✓		✓	Moderate
Water resources – Degradation or pollution of surface waters and ground water	✓	✓			Low
Local infrastructure – Infrastructure requirements (eg for construction activities or migrant workers) deplete capacity of local district/community infrastructure to the detriment of local users	✓				Low
Waste – Human health impacts from transportation accidents, or poor treatment or disposal of hazardous and non-hazardous wastes	✓	✓			Moderate
Disturbance – Adverse disturbance and human health effects from noise, dust, air emissions, traffic accidents and pollution, excessive lighting etc	✓	✓			Low
Worker camps – Unacceptable behaviour towards local communities from labour camp workers; fuelling of alcohol, prostitution and drugs in local communities and disrespect for cultural norms; transmission of infectious (STD/HIV) and endemic (malaria, TB etc.) diseases	✓				Moderate
Workers rights and child and forced labour – Failure to satisfy basic workers' rights (collective bargaining, retrenchment, treatment of contract labour, working conditions etc.); inadvertent use of suppliers who use child, forced or bonded labour	✓	✓		✓	High
Local-level economic risks – Unfulfilled expectations of local communities to realise employment opportunities; 'boomtown' effects; local community jealousy of migrant workers, and intra and inter-community jealousies and rivalry, with potential for violence; construction wage levels in excess of market norms (eg in agriculture) leading to 'labour drain'; adverse effects of employee/sub-contractor retrenchment post construction	✓	✓			High
National-level economic risks – Lack of transparency and accountability in payment of revenues to central and provincial government; production revenues fail to return to region of operations in a way that provides visible economic benefits to local population; national and provincial suppliers unable to access opportunities on project owing to economic barriers to market entry				✓	High

¹⁰ If not avoided, mitigated or compensated.

Table 2 Indicative Social Risk Analysis for BP's Global Business Operations¹¹

Country Operations	Material Country Operations (MCOs)			Dominant Business			Composite Governance Index	Initial Risk Grading			
	>10% revenues	>10% profits	>10% capital	Up-stream	Mid-stream	Down-stream		MCO and very poor governance	MCO and poor governance	MCO and fair to good governance	Country presence but not MCO, and very poor governance
Angola			Y	Y			-1.63	A			
Azerbaijan	Y	Y	Y	Y			-1.15	A			
Georgia			Y	Y			-1.20	A			
Indonesia	Y						-1.01				B
Kazakhstan	Y		Y	Y			-0.81		B		
Pakistan	Y						-1.01				B
Russia	Y		Y	Y			-0.66		B		
Turkey	Y		Y	Y			-0.31		B		
Zimbabwe	Y						-1.60				B
Algeria	Y	Y	Y	Y			-0.97		B		
China	Y		Y	Y			-0.40		B		
Colombia	Y	Y	Y	Y			-0.80		B		
Germany	Y	Y				Y	1.90			C	
United Kingdom	Y	Y			Y	Y	1.97			C	
Trinidad & Tobago	Y	Y	Y	Y			0.40			C	
United states of America	Y	y		Y	Y	Y	1.67			C	

Social Risk Country Grading		
Governance Index	MCO	
	Y	N
<-1.0	A	B
0.0 to -1.0	B	
>0.0	C	

2.4 Social Risks and the Configuration of Joint Ventures

Social risks, or more precisely the 'likelihood' or commercial 'consequence' of a social risk event, can be further heightened depending on the configuration of a particular joint venture. For example, there seems some weight to the argument that the 'likelihood' of adverse social impacts¹² would be increased where the project operator – who generally establishes the environmental and social risk management regime for the investment – is a 'junior' company or a national oil company (NOC) with little experience in social performance. This likelihood is arguably even greater where the experienced multinational company within the venture has only minority voting rights and thus lacks management influence.

Likewise, the 'consequence' of a social risk event can be accentuated by the same configuration. For example, an inexperienced operator might fail to react to insensitive community relations, allowing local intra-community political violence to become

¹¹I Internal, web-based, research by ODI (unpublished); and Kaufmann et al (2003).

¹²Such as STD infections within local communities from worker camps, or existing local political violence being fuelled by insensitive community relations.

redirected towards the company, with a consequential loss of production through sabotage etc.

Table 3 captures the way in which the configuration of a joint venture might influence the likelihood and commercial consequence of social risks to a project. The higher the likelihood and consequence, the greater the benefit of approaching development finance institutions with strong social performance requirements.

Table 3 How Social Risks might be Heightened by the Configuration of a Joint Venture: from the perspective of Company X

Company X	Joint Venture with Company X as Operator	Joint Venture where Company X is not the Operator	
		NOC or New 'Junior' Partner as Operator	Other Experienced Company as Operator
Majority (equity) partner	L = low; C = low As the operator and majority partner, Company X is able to establish effect social risk mitigation and response systems. The need for project to strengthen its social performance is unlikely to be a consideration for approaching an IFI.	L = high; C = mod Inexperience of operator in social risk management raises likelihood of social risks. However, as majority partner, Company X may be in a position to reduce consequence of risk events, for example by sanctioning additional social investment or by bringing in its own expertise. As majority partner, Company X is also in a strong position to encourage other partners to view engagement with IFIs (particularly DFIs) as an opportunity to enhance a projects overall social performance.	L = low; C = low Company X able to relay on operator to establish effect social risk mitigation and response systems. Need for enhanced social performance unlikely to be a consideration for approaching an IFI.
Minority (equity) partner	E – low; C = mod As above, but owing to minority voting rights on the board, may be constrained in ability to respond to social risk events, eg unable to increase social investment to respond to community tensions.	L = high; C = high Inexperience of operator in social risk management raises likelihood of social risks. As minority partner, Company X is in a weak position to reduce the commercial consequences of risk events. Also in weak position to encourage other partners to view approaching IFIs (particularly DFIs) as an opportunity to enhance the project's social performance.	L = low; C = low As above.

Key:
 ➔ Likelihood of a social risk event taking place = L;
 ➔ Commercial consequence = C;
 Higher intensity colour indicators higher overall severity of risk

Approaching DFIs to protect against political risk has two possible motives. First, the protection sought may be 'explicit', taking the form of credit or financial risk guarantees. For example, the Natural Resources Operations Policy of the European Bank for Reconstruction and Development notes that: '[project] sponsors still desire the Bank's involvement due to its capability in arranging co-financing, mitigating political risk...This was the case in the recently closed Chirag project in Azerbaijan and Sakhalin in Russia.'¹³

¹³ EBRD (undated) Natural Resources Operations Policy: <http://www.ebrd.com/about/policies/sector/natural/natural.pdf>

Alternatively, it can also be about ‘implicit’ risk control, where the choice of DFI is made in part because of the additional political, regulatory and exchange rate risk security derived from the political or trade-related national interests of the shareholders in the financing institution, namely governments. *Table 4* lists the main government-backed DFIs.

Beyond the consideration of risk management, companies may approach IFIs to fulfil other needs: as a prerequisite in a license or other home country agreement; to help junior partners gain access to investment capital; to buy into an existing agreement that is already seeking external finance; or to facilitate the engagement of (provide ‘comfort’ to) other financial institutions. Even where risk is not a reason for approaching a particular IFI, the institution will, to varying degrees, have their own internal due diligence requirements for identifying and managing risks, including sometimes aspects of social risks. Thus, it is likely that social risk management and social performance will become, *de facto*, aspects of engagement with IFIs, regardless of whether or not enhanced social performance was a primary consideration in approaching the IFI in the first place.

Table 4 Development Finance Institutions¹⁴

Multilateral Development Banks and Agencies	Official Export Credit Agencies
African Development Bank (ADB)	Compagnie Française d'Assurance pour le Commerce Extérieur (COFACE, France)
Asian Development Bank (ADB)	Export Credits Guarantee Department (ECGD, UK)
European Bank for Reconstruction and Development (EBRD)	Credit Guarantee Insurance Corporation of Africa Limited (CGIC, South Africa)
European Investment Bank (EIB)	Export Development Canada (EDC, Canada)
Inter-American Development Bank (IDB)	Export Finance and Insurance Corporation (EFIC, Australia)
Inter-American Investment Corporation (IIC)	Export-Import Bank of the United States (EXIM, US)
International Finance Corporation (IFC)	Export Risk Guarantee Agency (ERG, Switzerland)
International Monetary Fund (IMF)	Exportkreditnämnden (EKN, Sweden)
Islamic Development Bank (IDB)	Finnvera plc (Finnvera, Finland)
Multilateral Investment Guarantee Agency (MIGA)	Guarantee Institute for Export Credits (GIEK, Norway)
Nordic Investment Bank (NIB)	Hermes Kreditversicherungs-AG (Hermes, Germany)
United Nations Development Program (UNDP)	Istituto per i Servizi Assicurativi e il Credito all'Esportazione (SACE, Italy)
World Bank Group	Japan Bank for International Cooperation (formerly JExIm)
	KfW IPEX Bank (part of the KfW BankenGruppe, Germany)
	Nederlandsche Credietverzekering Maatschappij NV (NCM, Netherlands)
	Norwegian Guarantee Institute for Export Credits (Giek, Norway)
	Office National du Ducreire (OND, Belgium)
	Overseas Private Investment Corporation (OPIC, United States)
	Svensk Exportkredit (SEK, Sweden)
Bilateral Development Banks and Agencies	
Agence Française de Développement (AFD, France)	
Commonwealth Development Corporation (CDC, UK)	
Finnish Fund for Industrial Cooperation (FINNFUND, Finland)	
Industrial Development Corporation (IDC, South Africa)	
Industrialization Fund for Developing Countries (IFU, Denmark)	
Japan Bank for International Cooperation (OECE, Japan)	
Kreditanstalt für Wiederaufbau (KfW, Germany)	
Overseas Private Investment Corporation (OPIC, US)	
Swedfund International AB (Swedfund, Sweden)	

¹⁴ Project Finance Portal: <http://www.people.hbs.edu/besty/projfinportal/ecas.htm>

3. Social Performance and Energy Companies

Along with the elevation of social risks in relation to oil and gas developments in low and low-middle income countries comes the need for improved social management performance by the project owners.

3.1 Company Practices

In contrast with the management of most environmental risks, social risk management combines the mitigation of potential negative impacts with the enhancement of positive social and local economic benefits. This emphasis on benefits, or project 'additionality', is both a form of mitigation against the financial risks arising from social exclusion and local economic disenfranchisement caused by some projects, and a means to enhance company reputations and foster long-term access to new business opportunities and finance.

To illustrate these different perspectives, the definition of social performance used by the Shell Group in its recent Guidance Notes series on the subject¹⁵ includes three pillars:

- ➔ to minimise the negative socio-economic impacts of local presence;
- ➔ to optimise the socio-economic benefits of local presence; and
- ➔ to undertake broader contributions to society in the region of operations.

Table 5 below summarises some of the practices of companies in delivering social performance in oil and gas development projects.

Table 5 Practices of Companies in Delivering Social Performance on Oil and Gas Development Projects

Category of Social Risk	Social Performance Practices
Resettlement management	<ul style="list-style-type: none"> ➔ Modifications to front-end engineering design to avoid involuntary resettlement wherever possible ➔ Participation of affected parties in resettlement planning, both those resettled and the host communities ➔ Full compensation and rehabilitation of income earning potential and livelihood security
Livelihood resource management	<ul style="list-style-type: none"> ➔ Investigate local livelihood systems and resources critical to livelihood security, and put in place alternative resource base with equivalent ownership and/or usufruct entitlements ➔ Special emphasis on most vulnerable community groups, women-headed households, old, handicapped
Indigenous peoples and cultural properties management	<ul style="list-style-type: none"> ➔ Survey of cultural sites and practices ➔ Ensure participation of formal and informal indigenous leaders in ongoing consultation ➔ Grievance and compensation procedures to incorporate customary values
Water resource management	<ul style="list-style-type: none"> ➔ Prohibit surface water dredging of aggregates ➔ Control stormwater runoff and revegetate disturbed areas ➔ Bury drilling muds and cuttings ➔ Good housekeeping practices at construction sites to minimise leaks and spills
Infrastructure capacity management	<ul style="list-style-type: none"> ➔ Survey all community, local and regional infrastructure capacity ➔ Apply the NEWT rule ('not environmentally worse than') with respect to decision-making on whether to invest in local infrastructure capacity and utilities to meet construction requirements ➔ Share the costs of infrastructure upgrades with local and regional authorities ➔ Reuse non-potable water, eg for dust suppression, concrete mixing, pilling etc.

¹⁵ First defined in Guidance Note A2 titled: 'Partnerships' (unpublished).

Category of Social Risk	Social Performance Practices
Waste management	<ul style="list-style-type: none"> ➔ Ensure safe transportation, treatment and disposal of hazardous and non-hazardous wastes ➔ Best practice occupational health and safety measures to be applied, and available to treat off-site parties if affected by project
Disturbance impacts management	<ul style="list-style-type: none"> ➔ Meet or surpass minimum national environmental quality standards for noise, dust and air emissions ➔ Introduce traffic calming measures, eg night time bans, driver training ➔ Minimise excessive lighting close to communities, eg in night hours
Workers camp management	<ul style="list-style-type: none"> ➔ Locate worker camps away from local communities and transport 'hubs' ➔ Alcohol in camp limited by hours and volume ➔ Possession of illegal substances forbidden ➔ Drug and alcohol testing allowed if under suspicion of not being able to undertake tasks ➔ No social visitors permitted in camp ➔ Camp access to communities allowed if follow specific Code of Conduct ➔ Security implications for neighbouring communities assessed as part of security plan ➔ No firearms or other weapons permitted
Workers rights and child and forced labour	<ul style="list-style-type: none"> ➔ Adoption of relevant International Labour Standards(ILO) conventions
Mitigating adverse local economic impacts	<ul style="list-style-type: none"> ➔ Maintain wage levels for manual and semi-skilled employees at market rates ➔ Locate all temporary manual and semi-skilled procurement at a single urban location away from the construction site ➔ Ensure 'rules' for procurement preferencing to affected communities and local businesses are clear and perceived as justified and fair ➔ Maximise number of local people able to benefit from temporary employment, eg introducing shorter-term contracts, rotating positions and suppliers for non-business-critical tasks
Enhancing positive national and local economic impacts	<p><i>Sourcing</i></p> <ul style="list-style-type: none"> ➔ Source accommodation and provisions for construction workers/labour camps from project-affected communities ➔ Sub-contractors required to source raw materials from land owners or micro-enterprises within the communities affected by construction or, if sourcing outside project area, from regional suppliers who have a proportion of staff/workers from affected communities <p><i>Training, provide a combination of the following:</i></p> <ul style="list-style-type: none"> ➔ On-the-job training programmes, with trainees utilised on immediate construction project ➔ On-the-job training programmes, with preference given to trainees for later in the construction period and/or on subsequent projects managed by the main contractors ➔ Off-the-job training programmes open to a wider range of participants, involving training staff from the main contractors alongside other regional training agencies, with the aim of developing local skills for future markets <p><i>Local infrastructure</i></p> <ul style="list-style-type: none"> ➔ Support to local enterprise development through the provision of business-critical infrastructure (electricity, road upgrading, telecoms) ➔ Partnering with the Shell Operator and relevant public sector public works departments to extend the benefits of temporary construction activities and/or permanent infrastructure to local communities (eg road and bridge rehabilitation, water, power suppliers, wastes management, telecoms) ➔ Employment and training for community members in the construction and long-term maintenance of above infrastructure

3.2 Company Standards and Guidance

In general, social performance standards and guidance within oil and gas development companies are less well developed compared with those for health, safety and environment. Where they do exist, they are likely to combine both minimum requirements, ie true 'standards', and voluntary good practice or guidance.

In the case of the Shell Group, these include standards such as the Shell Business Principles, Sustainable Development Principles and HSE Commitment and Policy; and good practice guidance such as the suite of Shell EP 95-000 Manuals (covering Social Impact Assessment, Stakeholder Consultation, Guidance on Integrated Impact Assessment etc.), and the more recent series of Social Performance Guidance Notes (covering, *inter alia*, stakeholder engagement, resettlement, vulnerable groups, community health, and biodiversity and communities).

4. Social Performance Requirements of IFIs

Securing international project finance – be that in the form of equity, loans/debt, export credit or other risk guarantees or insurance – requires a project to meet increasingly stringent health, safety, environmental, social and economic performance standards. Of these, social standards are the least evolved.

4.1 Types of Social Performance Standards

The social standards of IFIs often rely on either an interpretation of environmental standards and procedures, such as following the Environmental Policy of the EBRD, or on good practice guidelines that may lie outside the institution's minimum standards, such as the recent good practice guidance note on social impact assessment published by the International Finance Corporation (IFC).

The current slow and rather piece-meal evolution of social performance standards within many IFIs means that the social performance practices of companies – particularly those associated with providing social and economic 'benefits' – is likely to overlap with not only the stated social and environmental standards of the IFIs, but also with the broader economic and international development aspirations that inform investment decisions and define project performance. This is clearly more the case for government-backed multilateral and bilateral investment institutions. It is perhaps less relevant to export credit agencies and commercial banks, where the 'economic' objectives of the project are generally defined in terms of the promotion of home-country exports and maximisation of 'return on investment', respectively.

At least four types of standard are relevant to companies seeking to meet the social performance requirements of IFIs:

- ➔ **Social policy standards** – policy statements, core principles and implementing rules for managing issues such as resettlement, cultural property, indigenous peoples, child labour and worker camps.
- ➔ **Economic standards and guidance** – policy statements, qualitative benchmarks and assessment procedures that assist project sponsors to ensure that the investment delivers a positive economic impact;
- ➔ **Procedural social standards and guidance** – minimum required procedures and good practices for preparing environmental and social impact assessment studies and for social performance reporting.
- ➔ **Numerical social and environmental standards** – quantifiable social performance requirements, such as rates of staff succession and compensation levels (as well as environmental performance requirements with a social aspect, eg ambient air quality, ambient noise levels, effluent discharges to surface water bodies, fisheries quality).

4.2 Social Performance Standards in the World Bank Group and EBRD

The World Bank Group is influential in the ways in which IFIs around the world manage social performance within their lending. The Group includes the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA), offering various project financing services and products to the private sector.

Box 1 Future Trends for Social Performance Standards within the World Bank Group

At the time of writing, the World Bank Group is in the process of revising its social and environmental standards. These changes will affect the requirements placed on companies seeking project finance, and may, to varying degrees, influence other government-backed or commercial international financing institutions. The likely changes include:

- ➔ new procedures for preparing a 'combined' social and environmental impact assessment (SEIA) report and management (action) plan (as opposed to social issues being covered as a single chapter in the EIA report or as a separate Social Impact Assessment);
- ➔ a stronger emphasis on using the SEIA process to identify and enhance the social and economic benefits of investments, such as employment, training, supplier enhancement, local infrastructure and institutional strengthening (in line with the conclusions of the World Bank's recent Extractive Industries Review);
- ➔ requirements for public consultation and information disclosure to be made ongoing throughout the life of the investment project, rather than more narrowly focused on the EIA studies alone;
- ➔ greater emphasis on transforming social and environmental action plans into fully-fledged management and monitoring systems;
- ➔ strengthening of the existing minimum ('safeguard policy') standards to include new provisions on:
 - ⇒ workers' rights, eg collective bargaining, retrenchment, treatment of contract labour, working conditions
 - ⇒ community health and safety
 - ⇒ vulnerable non-indigenous peoples dependent on renewable natural resources
- ➔ clear distinction between (i) minimum performance standards; (ii) implementing guidance for these minimum standards; and (iii) voluntary good practice guidance that goes beyond minimum standards.

The main social performance standards and guidance of the World Bank Group are given in *Annex A*, those of the EBRD in *Annex B*. Some recent trends in the evolution of the social standards within the World Bank Group are summarised in *Box 1* above.

4.3 The Equator Principles

World Bank Group social standards are influential not only with other multilateral and bilateral IFI's around the world, such as the Asian Development Bank or the US and UK export credit agencies, but also within commercial banks.¹⁶ 27 major banks are now signatories to the Equator Principles. These are essentially the World Bank Group's environmental and social 'safeguard policies'. *Box 2* summarises the Equator Principles. *Box 3* lists the current institutional signatories.

Commercial banks and non-government-backed IFIs are generally the first port of call for those seeking international project finance in the upstream oil and gas sector. It is therefore important for companies to understand how the Equator Principles are being interpreted by these banks. For example, some banks are employing social specialists and require projects to deliver high levels of indirect, positive, social and economic benefits. Others employ no dedicated staff and limit themselves to financing terms that require

¹⁶ See specific policies and standards at: <http://www.equator-principles.com/exhibit2.shtml>

only the mitigation of direct, negative, social impacts. Further, whilst signatories have made no commitment to date to adopt the revised World Bank environmental and social standards when these are finalised, some commercial banks may be likely to do precisely this owing to shareholder and public pressure. There is therefore every prospect of the emerging social standards of the World Bank Group (*Box 1*) becoming requirements of international 'equator banks'.

Box 2 The 'Equator Principles' : An Industry Approach for Financial Institutions in Determining, Assessing and Managing Environmental & Social Risk in Project Financing (*social risks highlighted*)¹⁷

'These principles are intended to serve as a common baseline and framework for the implementation of our individual, internal environmental and social procedures and standards for our project financing activities across all industry sectors globally. In adopting these principles, we undertake to review carefully all proposals for which our customers request project financing. We will not provide loans directly to projects where the borrower will not or is unable to comply with our environmental and social policies and processes.

STATEMENT OF PRINCIPLES – *We will only provide loans directly to projects in the following circumstances:*

1. We have categorised the risk of a project in accordance with internal guidelines based upon the environmental and social screening criteria of the IFC as described in the attachment to these Principles (Exhibit 1: <http://www.equator-principles.com/exhibit1.shtml>).
2. For all Category A and Category B projects, the borrower has completed an Environmental Assessment (EA), the preparation of which is consistent with the outcome of our categorisation process and addresses to our satisfaction key environmental and social issues identified during the categorisation process.
3. In the context of the business of the project, as applicable, the EA report has addressed:
 - a) assessment of the baseline environmental and social conditions; b) requirements under host country laws and regulations, applicable international treaties and agreements; c) sustainable development and use of renewable natural resources; d) protection of human health, cultural properties, and biodiversity, including endangered species and sensitive ecosystems; e) use of dangerous substances; f) major hazards; **g) occupational health and safety**; h) fire prevention and life safety; **i) socio-economic impacts**; j) land acquisition and land use; **k) involuntary resettlement**; **l) impacts on indigenous peoples and communities**; m) cumulative impacts of existing projects, the proposed project, and anticipated future projects; **n) participation of affected parties in the design, review and implementation of the project**; **o) consideration of feasible environmentally and socially preferable alternatives**; p) efficient production, delivery and use of energy; q) pollution prevention and waste minimization, pollution controls (liquid and air emissions) and solid and chemical waste management.
- Note: In each case, the EA will have addressed compliance with applicable host country laws, regulations and permits required by the project. Also, reference will have been made to the minimum standards applicable under the World Bank and IFC Pollution Prevention and Abatement Guidelines...and, for projects located in [low](#) and [middle income](#) countries as defined by the [World Bank Development Indicators Database](#), the EA will have further taken into account the then applicable IFC Safeguard Policies (Exhibit II - <http://www.equator-principles.com/exhibit2.shtml>). In each case, the EA will have addressed, to our satisfaction, the project's overall compliance with (or justified deviations from) the respective above-referenced Guidelines and Safeguard Policies.
4. For all [Category A](#) projects, and as considered appropriate for [Category B](#) projects, the borrower or third party expert has prepared an Environmental Management Plan (EMP) which draws on the conclusions of the EA. The EMP has addressed mitigation, action plans, monitoring, management of risk and schedules.
5. For all [Category A](#) projects and, as considered appropriate for [Category B](#) projects, we are satisfied that the borrower or third party expert has consulted, in a structured and culturally appropriate way, with project affected groups, including indigenous peoples and local NGOs. The EA, or a summary thereof, has been made available to the public for a reasonable minimum period in local language and in a culturally appropriate manner. The EA and the EMP will take account of such consultations, and for [Category A](#) Projects, will be subject to independent expert review.
6. The borrower has covenanted to: a) comply with the EMP in the construction and operation of the project; b) provide

¹⁷ Statement of Principles: <http://www.equator-principles.com/principles.shtml>

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regular reports, prepared by in-house staff or third party experts, on compliance with the EMP and c) where applicable, decommission the facilities in accordance with an agreed Decommissioning Plan.

7. As necessary, lenders have appointed an independent environmental expert to provide monitoring and reporting services.

8. In circumstances where a borrower is not in compliance with its environmental and social covenants, such that any debt financing would be in default, we will engage the borrower in its efforts to seek solutions to bring it back into compliance.

9. These principles apply to projects with a total capital cost of \$50 million or more.

Box 3 Signatories to the Equator Principles

[ABN AMRO Bank, NV](#)

[Banco Bradesco](#)

[Banco Itaú](#)

[Banco Itaú BBA](#)

[Bank of America](#)

[Barclays plc](#)

[BBVA](#)

[Calyon](#)

[CIBC](#)

[Citigroup Inc.](#)

[Credit Suisse Group](#)

[Dexia Group](#)

[Dresdner Bank](#)

[EKF](#)

[HSBC Group](#)

[HVB Group](#)

[ING Group](#)

[KBC](#)

[MCC](#)

[Mizuho Corporate Bank](#)

[Rabobank Group](#)

[Royal Bank of Canada](#)

[Standard Chartered Bank](#)

[The Royal Bank of Scotland](#)

[Unibanco](#)

[WestLB AG](#)

[Westpac Banking Corporation](#)

5. A Road Map for Meeting the Social Performance Requirements of IFIs

The consequences of failing to comprehend fully the social performance requirements of IFIs are summarised below. This is followed by a road map for companies to avoid the pitfalls of trying to meet the social performance requirements of IFIs.

5.1 Consequences of Failing to Understand the Social Performance Requirements

Failure to adhere closely to the way in which IFIs approach issues of social performance can result in a number of difficulties for the borrowers, both in terms of the process of financial negotiation and in long-term project implementation.

First, failure to anticipate the full range of social performance ‘condition precedents’ within project financing agreements, or to navigate the full complexity of social performance policies, procedures and quality standards within the IFI, can lead to delays in negotiations.

Secondly, additional development costs (mostly unrecoverable) can be incurred from being compelled by the IFI to make modifications to front-end project design as a result of the borrowers underestimating the level of social risk likely to be perceived by the IFI.

Thirdly, the ‘moving goal-posts’ of social performance standards evolution and interpretation within IFIs can pose a problem for borrowers. Revision to social performance standards within IFIs can result from internal institutional reviews (such as the World Bank Extractive Industries Review¹⁸) and from external pressure, such as new HSEC practices, new government policy on international development (eg promotion of the Millennium Development Goals), or new interests of civil society and the media, eg on local content, revenue transparency and distribution, child labour in supply chains. Keeping pace with these changes is hard enough for the institution’s staff themselves. Prospective borrowers need to do the same, *and* keep pace with how the changes are being interpreted by an institution’s staff.

Fourthly, and related to this, there is unpredictability over which social performance issues will likely emerge within the lending IFI after the financial agreement and related covenants for social performance have been reached.

Fifthly, misunderstanding between the lending IFI and project owner sometimes occurs over what constitutes a breach in the covenants on social impact management and monitoring during project implementation, and what should be the procedures for prevention or rectification.

Lastly, in the case of government-backed DFIs, companies sometimes underestimate the opportunity to leverage concessional financial assistance to enhance the social and economic benefits of the project. Recent examples include World Bank support for revenue management in relation to the Chad-Cameroon Petroleum Development and

¹⁸ See: Extractive Industries Review – Final World Bank Group Management Response – <http://www.worldbank.org/ogmc/>

Pipeline project; the IFC-supported enterprise development initiative in Azerbaijan,¹⁹ and the resources available from the new Corporate Citizenship Facility of the IFC.²⁰

5.2 Road Map

Responding to these weaknesses requires better guidance for companies on how they can meet the social performance requirements of IFIs. The road map below provides advice on seven steps that companies can take.

First and foremost, all negotiators need to understand that meeting the social (and environmental) performance requirements of IFIs is an incremental, iterative, process. For example, what may seem to be the most important social issues at the beginning of negotiations, may recede as the project design is modified. Likewise, new issues may arise during the course of financial negotiations, triggering the need for additional public consultation and further design modifications. For example, EBRD policy for public consultation states that 'requirements may increase during due diligence if the environmental [or social] investigations demonstrate a need for increased disclosure or communication.'²¹

More so for social issues than environmental, in meeting IFI requirements much rests on a joint lender-borrower interpretation of the social risks and issues affecting a project. For the potential borrower, it is therefore less a question of asking the IFI, 'what do we have to do?', and more one of working together to evolve a social (and environmental) management plan for the project that satisfies both the IFI and the project.

Beyond understanding these basic concepts of iteration and joint design, certain steps need to be followed to meet the social performance requirements of IFIs:

- ➔ Identifying the dominant IFI for social performance standards within the consortium of project finance institutions;
- ➔ Bringing social specialists into project finance negotiations early;
- ➔ Documenting a common understanding of social performance expectations upfront in the negotiations;
- ➔ Assessing the potential for misalignment of the financing institutions' social performance standards with those agreed during other project negotiations, eg with joint venture partners, in host country agreements or with environmental regulators;
- ➔ Undertaking a Gap Analysis of the company's (or joint venture's) internal social performance standards and guidance, against those of the lead project financing institutions;
- ➔ Agreeing actions to manage unforeseen social issues that fall outside of the covenants of financing agreements; and

¹⁹ See: BP/IFC Enterprise Centre: <http://www.ecbaku.com/>

²⁰ See: IFC Corporate Citizenship Facility:

<http://ifcln1.ifc.org/ifcext/enviro.nsf/e11ffa331b366c54ca2569210006982f/11a491f7398c599585256ead006d0d2b?OpenDocument>

²¹ EBRD (2002) *Environmental Policy, Annex 2: Consultation with the Public*, London: European Bank for Reconstruction and Development.

- ➔ Building the capacity of local staff and consultants to ensure social performance requirements are met and sustained over time.

Each of these steps is discussed below.

5.2.1 *Identifying the dominant IFI for social performance standards within the consortium of project finance institutions*

In setting social performance financing terms, some lenders defer to the financial institution leading negotiations over the financing package (as is the case for syndicated B-loans). Others make explicit reference to the application of 'international recognised' standards, such as those of the World Bank Group or European Bank for Reconstruction and Development. In addition, many of the major commercial banks now apply the 'Equator Principles' (see *Section 4.3*).

Questions to assist in identifying the financing institution whose social performance standards will dominate the terms of any financing agreement include the following:

- ➔ Q1 – *Is the host country, region of production or immediate area of operation characterised by high levels of political and social risk, for example as indicated by lack of public participation in decision-making, political instability and corruption?* There are various options here. Companies can use a commercial risk rating firm specialising in environmental and political risk within the oil and gas sector.²² Alternatively, an indication of the likelihood of social risks in a country can be obtained using publicly available data. For example, the World Bank's public sector 'good governance' indices offer a proxy for social risk (as used in *Table 2*). Either way, the higher the social (and political) country risk rating, the more likely it is that social performance requirements will figure strongly in the project negotiations and financing agreements of one or more lenders.
- ➔ Q2 – *What is the most likely project financing package to manage the political risks?* Project finance packages can include risk guarantees, loans, export credit, insurance, equity, commercial loans, as well as balance sheet contributions by project partners. On the assumption that political risk (eg risk of contract modification, regulatory change and revenue or ownership appropriation) rather than social risk is the dominant threat to project sustainability in developing countries, it is likely that one or more of the institutions providing the main political risk insurances or guarantees will also lead on overall project risk assessment. Given that this institution will likely assume that social risk is a subset of, or contributing element to, political risk, it may not place as high a value on social performance as perhaps a more social-development-driven finance institution. Thus, knowing who is leading on political risk is important, although it is not the whole story.
- ➔ Q3 – *Which institutions are likely to lead the project finance negotiations regarding each of the main elements of the financing package?* Beyond the lead risk guarantee institutions, it is therefore important to identify which other financing institutions are likely to lead on different aspects of project finance, and thus be influential with respect to applying social performance standards. For example, if a development finance institution is

²² For example, the Mineral Risk Extraction Assessment formula used by BERI (Business Environment Risk Intelligence), see: <http://www.beri.com/mera.asp>

involved in providing debt, the institution may well require the mitigation of certain adverse social risks, such as child or forced labour in supply chains, and explicit consideration, such as of indigenous peoples, as well as some assurance that the transaction will deliver a positive economic or 'development' impact. This is the current situation with the International Finance Corporation. Similarly, the UK Export Credit Guarantee Department (ECGD) requires all of its transactions in HIPC countries not only to adhere to the World Bank 'safeguard' policies, but also to pass a 'Productive Expenditure' test.²³ This test, undertaken for ECGD by the Department for International Development, looks for alignment between the transaction and the economic and social development priorities of the country.

- Q4 – of the lead project financing institutions, which institution/s is considered by the others as having the most stringent or comprehensive social performance standards or requirements, and what are these standards? Since both development finance institutions and the 'Equator' banks make reference to the World Bank Group social (and environmental) 'safeguard' policies (see *Annex A2*); and given that these safeguard policies are generally recognised as the most stringent among IFIs at present, so the question can rapidly become less about 'which standards apply', and more about 'whose interpretation matters'.

However, beyond the World Bank 'safeguard' policies, the question of whose standards apply gets more complicated. For example, standards and requirements around 'local content' may be relevant to negotiations with commercial banks, in that some banks may view elevated investment risks arising from technically questionable 'local content' requirements within host government agreements. Further, standards around ensuring economic 'additionality' from investments or transactions may fall to a lone development finance institution, even if this institution is providing only a very small portion of the overall risk finance. This is sometimes the case with bilateral DFIs.

Table 6 provides an illustration of the application of these questions to the part-IFC financed Karachaganak oil and gas development project in Kazakhstan.

5.2.2 Bringing social specialists into project finance negotiations early

An apparent error on the part of many of those negotiating project financing arrangements with IFIs is a failure to demonstrate full comprehension of the lenders' priorities for social and environmental performance, and to relate this to the control of operational risks and assurance of long-term financial sustainability. This can be a particular problem for national oil companies and junior partners who may have less experience with environmental and social management. To overcome this omission, borrowers should be encouraged to include within their negotiating team individuals familiar with social (and relevant environmental) performance and risk management.

²³ ECDG (2003) *ECGD Business Principles*, London: Export Credit Guarantee Department.

Table 6 Steps to Identifying the Dominant IFIs for Social Performance Standards within a Consortium of Project Finance Institutions: Karachaganak oil and gas development project, Kazakhstan²⁴

1. What is the level of social risk for the proposed investment?	2. What is the most likely project financing package to manage the political risks?	3. Which institutions are likely to lead the project finance negotiators for each of the elements of the 'financing package'?	4. Which institutions have the most stringent or comprehensive social performance standards, and what are these?
<p>Country social risk rating – Moderate</p> <p>Composite country governance index (World Bank) Kazakhstan: -0.81 (moderate)</p>	<p>Multi/bilateral development finance</p> <ul style="list-style-type: none"> • <i>Lender:</i> International Finance Corporation (World Bank Group) • <i>Recipient:</i> Lukoil B.V (Russian NOC) • <i>Financing package:</i> <ul style="list-style-type: none"> • A Loan – \$50m • B (syndicated) Loan – \$75m • C (subordinated) Loan – \$25 	<p>International Finance Corporation</p>	<p>International Finance Corporation</p> <ul style="list-style-type: none"> • World Bank Country Strategy • IFC Safeguard Policies • IFC/WB Sector Specific Guidelines • Various other IFC social management guidelines
	<p>Balance sheet</p> <ul style="list-style-type: none"> • Lukoil B.V. – 15% (IFI loan) • BG – 32.5% • ENI-Agip – 32.5 • ChevronTexaco – 20% 	<p>BG and ENI Agip joint operators</p>	<p>BG</p> <p><i>Statement of Business Principles:</i></p> <ul style="list-style-type: none"> • Communications • Corporate conduct governance • Human resources • HSE, human rights
	<p>Commercial loans</p> <ul style="list-style-type: none"> • ABN-AMRO Bank NV • Bayerische • Hypo- und Vereinsbank Aktiengesellschaft • Crédit Lyonnais • ING Bank NV • Natexis Banques Populaires • RZB-Austria • SG Investment Banking WestLB AG 	<p>'Equator Principle' signatories:</p> <ul style="list-style-type: none"> • ABN-AMRO Bank NV • ING • WestLB AG 	<p>No one party dominant</p> <p>Equator Principles include:</p> <ul style="list-style-type: none"> • IFC Safeguard Policies • IFC Sector Specific Guidelines

5.2.3 Documenting a common understanding of the relevance of particular social performance standards to the project

A number of social performance questions need to be put before the IFIs early in negotiations. These are listed below:

- ➔ Which social and economic management issues does the IFI consider relevant to this particular investment, and what level of analysis of the issue is considered acceptable?
- ➔ Which social performance standards (policies, procedures, numerical standards, good practices) need to be followed to secure financial agreement, and how are these being interpreted within the IFI?
- ➔ Which social performance issues are likely to be covenanted within financial agreements, and which not?

²⁴ IFC press release 2004:

<http://www.ifc.org/ifcext/eca.nsf/Content/SelectedPRKazakhstan?OpenDocument&UNID=FADE0A517EC92B5A85256CBF00773031>

- ➔ For government-based IFIs: what are the key international aid policies that frame the activities of the institution in the country hosting the investment, ie those that ultimately drive the expected economic returns, eg poverty alleviation, institutional capacity building, infrastructure provision?
- ➔ What is the IFI's expectation of how breaches in social and environmental performance covenants will be managed, eg withholding loan disbursements, joint problem-solving?
- ➔ How are project partners expected to handle unforeseen social issues that arise over the life of the investment?
- ➔ What resources are available within the IFI, or contacts does the IFI have, that might be available to enhance the positive social and economic benefits of the project?

Companies need to be prepared to explore these questions widely within the IFI. It is not sufficient to rely only on talking with those who comprise the IFI's core investment team. Some socially progressive IFIs – the International Finance Corporation for instance – will ensure that a dedicated social specialist is party to these early negotiations, and will be able to provide many of the answers. However, within most IFIs, this position is still uncommon, and the answers to many of the initial enquiries on social performance standards will lie with a range of different departments, for example, units responsible for due diligence, evaluating investments for their economic impact, or for legal oversight.

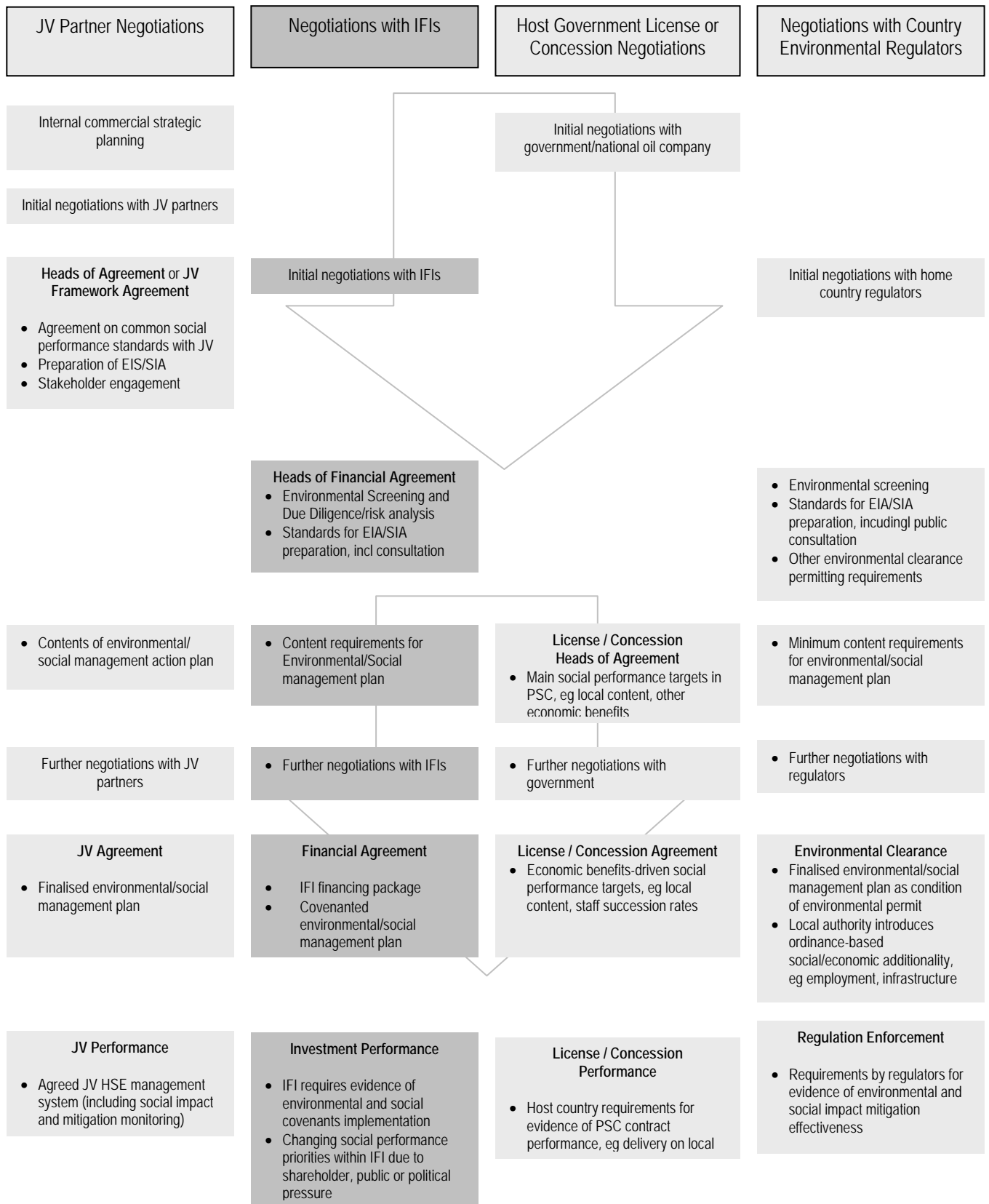
As noted earlier, four avenues of inquiry are needed to clarify the range of applicable social performance standards and guidance: social policy standards; economic standards and guidance; procedural social standards and guidance; and numerical social standards. It is recommended that answers to the above questions be documented in a Memorandum of Understanding, or equivalent.

5.2.4 Assessing the potential for misalignment of the IFI's social performance standards with those agreed during other project negotiations

It is not uncommon for an IFI to have social (and environmental) performance standards and practices that are higher than those already negotiated by a customer as part of their (the customer's) agreements with joint venture partners, within host country license or concession agreements, or as a condition of local project permits with in-country environmental regulators. Past experience has demonstrated that these differences may give rise to financing negotiations becoming protracted, and/or the terms of financing covenants being overly complicated. It is good practice for the main social performance standards and good practice guidance governing the different project negotiation processes to be anticipated as early as possible, and areas of potential non-alignment identified and managed.

Figure 1 shows the key stages of four sets of project negotiations. As far as practicable, convergence of social performance standards and expectations (as with other aspects of HSE and security standards) should be an aim of the negotiations. As a rule, where this is not possible, companies should work to the highest social performance standards required by whichever negotiation process, be this the widest scope of social issues, most comprehensive social assessment report, or most stringent numerical quality standards.

Figure 1 Potential for Misalignment of Social and Environmental Performance Standards Across Different Project Negotiations



5.2.5 Undertaking a Gap Analysis

Most operators of established multi-national oil and gas companies must adhere not only to local regulations but also to minimum environmental and social performance standards established at headquarters. These company-wide standards, in conjunction with relevant good practice guidance, may thus become ‘project standards’ to which all joint venture partners abide.

It is *not* safe, however, to assume that application of company-wide or project-specific standards and guidance will necessarily deliver the social performance requirements of participating IFIs. Where one particular company’s standards are likely to dominate within a project or JV, it is recommended that an analysis be conducted to identify any gaps between these and the standards and guidance of the relevant IFIs. To illustrate, *Table 7* provides a brief Gap Analysis of the Shell Group social performance standards and guidance against those of the World Bank Group. Further detail on World Bank Group and EBRD standards are provided in *Annex A* and *B*, respectively. It is important to share the results of any Gap Analysis with the IFI’s internal investment team, as well as agreeing and recording how any differences or shortfall in standards will be overcome.

Table 7 Summary Gap Analysis of Shell Group Social Standards and Guidance with those of the World Bank Group (minimum standards in *italics*)

Type of Standard	World Bank Social Performance Standards and Selected Guidance	Shell Group Standards and Guidance Relevant to SP ²⁵	Risk of Significant Gap in Standards	Commentary
Social and economic core standards	<ul style="list-style-type: none"> • <i>involuntary resettlement</i> • <i>indigenous peoples</i> • <i>cultural property</i> • <i>child labour</i> • <i>forestry</i> <p>(forthcoming policies on <i>workers’ rights, community health, renewable natural resource dependents</i>)</p>	<ul style="list-style-type: none"> • <i>Shell Business Principles</i> • Shell Sustainable Development Principles • <i>HSE Commitment and Policy</i> • <i>Environmental Minimum Standards (produced water)</i> • <i>Minimum Health Management Standards</i> • <i>Reputation Management standard</i> 	High	It cannot be assumed that application of Shell minimum social and environmental policies, commitments and principles will necessarily meet the core safeguard policies (performance standards) of the World Bank Group. Each World Bank safeguard policy comprises a set of principles that needs to be ‘seen’ to be considered explicitly in EIA/SIA studies and, where applicable, operationalised in project implementation.
		<ul style="list-style-type: none"> • Social performance good practice guidance notes, including: resettlement; vulnerable groups, child labour (primer), community health, biodiversity and communities 	Low	If followed, the new suite of Shell social performance Guidance Notes more closely follow many of the current and proposed safeguard policies/performance standards of the World Bank Group, though attention to detail will still be required.

²⁵ Shell International (2005) Commitments, Policies and Standards – <http://www.ifc.org/ifcext/policyreview.nsf>

Type of Standard	World Bank Social Performance Standards and Selected Guidance	Shell Group Standards and Guidance Relevant to SP ²⁵	Risk of Significant Gap in Standards	Commentary
Social impact assessment procedures	<p><i>OP 4.01 Environmental Assessment and related implementing procedures</i></p> <p>(forthcoming social and environmental assessment and management system standards)</p> <p>Good practice guidance note on SIA: 'Addressing the Social Dimensions of Business'</p>	<p>Environmental, Social and Health Impact Assessment</p> <p>HSE Commitment and Policy</p> <p>Group Procedure for an HSE Management System</p> <p>Shell Group level 'Yellow Guides' – Technical Guidance on Environmental Assessment; Health Risk Assessment; Management System</p>	Moderate	<p>If the suite of EP 95-0000 Manuals are followed closely, SIA reports and management plans prepared by the borrower will likely be World Bank compliant.</p> <p>However, a common problem is the quality of consultants contracted to prepare SIA reports. Problems include failing to:</p> <ul style="list-style-type: none"> • prepare public consultation plans to inform the terms of reference of the SIA studies • quantify impact predictions and mitigation measures • optimise socio-economic project benefits • integrate SIA studies with ongoing stakeholder engagement by the operator • integrate Social Management Plans with HSE management system
		<p>Exploration & Production EP 95-000 Manuals: Social Impact Assessment; Stakeholder Consultation; Guidance on Integrated Impact Assessment</p>	Low	
Numerical standards	<p>IFC Off-shore Oil & Gas Guidelines</p> <p>WB On-shore Oil & Gas Guidelines</p> <p>IFC Pollution Prevention and Abatement Handbook</p> <p>WB General Environmental Guidelines</p>	<p>Shell 'Yellow Guides'</p> <p>WHO standards</p>	Low	<p>Most important for social compliance will be to ensure that mitigation of pollution risks satisfies the 'ambient' numerical environmental quality standards of the World Bank/IFC, in particular:</p> <p>Noise: Shell (follows British Standards in 'Yellow Guide'); World Bank: day time residential 55 dB(A); night time 45 dB(A)</p> <p>Air quality: Shell (follows WHO guidelines): NO_x= annual 40 ug/m³; So₂= annual 50ug/m³; World Bank: NO_x= annual 100 ug/m³; So₂= annual 80ug/m³</p> <p>Produced water: Shell has commitment (in EMS) to 'discharge produced waters to a receiving environment with which it is compatible'; World Bank: see On-shore Off-Shore Oil & Gas Guidelines, and WB General Environmental Guidelines.</p>

5.2.6 *Agreeing actions to manage unforeseen social issues*

Securing finance from government-backed DFIs and some high-profile commercial banks can act as a 'lightening rod' for public scrutiny of a project. This is especially so if the company consultation procedures have not been broad enough to recognise and address stakeholder concerns. As such, the social mitigation and benefits measures covenanted in a financing agreement should be recognised for what they are: a prioritised set of measures identified at a specific moment and which are vulnerable to change over time.

Compounded by the reality that, within many IFIs, social performance standards themselves are evolving, it is possible that unforeseen or underestimated social issues will arise once a project begins, and that management of these will fall outside the scope of existing covenants. Developing a systematic approach to the identification and control of unforeseen social issues is welcomed by IFIs, not only to protect their immediate investment, but also to assure the institution's reputation.

One option is to work within the operator's health, safety, environment and security management systems. Here, as well as incorporating the tracking of social management measures covenanted in the project's financing agreement within the main HSE management system, design modifications should be made to scan for, and respond to, unforeseen social issues. As an alternative, the risk severity tables used in periodic project risk evaluation, and which fall under most companies' risks and hazards management systems, could be broadened to include ratings for social risks and opportunities. Whichever approach is taken to manage unforeseen social issues, it is important to acknowledge this approach explicitly within the financing agreement.

5.2.7 *Building human resource capacities*

Deploying social (and environmental) specialists sufficiently early can ensure that initial negotiations on project financing are informed of the principal socio-economic risks and opportunities posed by the investment. It is noticeable that, unlike the principal international development finance institutions, neither the Shell Group nor BP Group seems to have a system of investment screening that automatically draws in additional, central, specialist resources in social performance management if a project proposal registers a particularly high level of social risk. This said, the Shell Group has a dedicated in-house consultancy unit – Global Solutions – as well as various business advisors and the Shell Social Performance Management Unit, SPMU, all of which can provide expert advice on social performance management to assist negotiations if invited.

At the project level, local staff and consultants may be involved in carrying out social impact assessment (SIA) studies and finalising social mitigation and management plans as required by an IFI. Though these parties may have a good understanding of the national regulatory standards for social (and environmental) impact assessment, and even of the operator's own social standards and guidance, they may not be fully aware of the sometimes complex and ambiguous social performance standards of the participating IFIs.

Prior capacity building of local staff and consultants, on-the-job training, or adding the necessary international skills, may be critical in reducing delays to financing negotiations, for example. This is particularly the case when, owing to the omission of required information, borrowers are required to revisit their social studies and management plans after submission to the IFI.

6. Key Success Factors

Interviews with company staff and social specialists within IFIs were conducted for this study. These suggest a number of key success factors for companies in meeting the international social performance standards of project financing institutions (see *Box 4*). *Box 4* is designed to be used as a checklist.

Box 4 Key Success Factors when Negotiating with IFIs on Issues of Social Performance

presented as a checklist of Dos and Don'ts

Do

- when determining the scope of a social impact assessment, give close consideration to: (i) the 'checklists' on potential social impacts offered by IFIs, and (ii) the results of early public consultation – both will be considered important by the IFI;
- closely follow and document all the procedural social performance requirements of the IFI – timing of SIAs, submission of monitoring reports etc. Government-backed IFIs and brand-sensitive commercial banks are acutely aware that they are most vulnerable to external criticism for not following their own procedures.
- ensure that host country regulatory requirements on environmental and social issues are complied with. It is important not to lose site of home country social requirements, some of which, particularly on the community and economic benefits side, may be more stringent than those required by the internal standards of the IFI.
- recognise that the issue of 'international conventions' (on environment, labour etc.) needs to be discussed with the IFI before signing covenants. For example, knowing whether the host country has ratified a convention or not, or whether the borrower is incorporated in a third country, may have implications for what is covenanted;
- based on a prior agreed format, track and report regularly to participating IFIs on the project's compliance with covenanted social impact mitigation and management measures, as well as on unforeseen social issues.

Don't

- think that applying Group level social performance standards as the benchmark in a joint venture agreement will necessarily prepare the project for complying with an IFI's social standards. It may. It may not;
- assume that various voluntary 'guidance notes' and 'good practice manuals' on social performance published by an IFI are irrelevant. It is not uncommon for IFIs to encourage consideration of voluntary guidance (eg on resettlement, indigenous peoples, public consultation, community development) within social assessment studies. Thus what starts out as a voluntary standard can rapidly become a requirement, covenanted within a financing agreement;
- underestimate the effect of securing finance from government-backed IFIs, or banks that have signed up to the Equator Principles. This may increase scrutiny of the project from the media and NGOs, with the consequence that unintentional breaches of covenants on social and environmental issues carry greater reputational risks for both the project owners and the IFI;
- agree to a blanket covenant to implement all social and environmental policies and standards of the IFI. Secure an interpretation of these policies and standards first. Then record this joint understanding in an MoU;
- agree to covenant specific social impact mitigation measures that you have not clearly understood or costed, or may not be able to deliver in practice; and
- when no direct financing is involved, make statements that the project will be designed to World Bank Group, EBRD (or other IFI) social performance standards without fully comprehending the commitment being made.

Annex A

Key Social Performance Standards and Good Practice Guidance
within the **World Bank Group** (*Minimum Standards highlighted*)

Hypertext links:

World Bank Group

[A1 - Economic Policy Standards](#)

[A2 - Social Policy Standards](#)

[A3 - Social Performance Procedural Standards](#)

[A4 - Social Performance Numerical Quality Standards](#)

A1 – Economic Policy Standards

Economic Policy Standards (WBG)		
Type	Source	Standards
Mission Statement	http://www.ifc.org/about	'The International Finance Corporation (IFC) promotes sustainable private sector investment in developing countries as a way to reduce poverty and improve people's lives.'
Economic policies that frame investment decisions, ie that become investment objectives	World Bank Country Assistance Strategy (see country website)	Eg Kazakhstan: <ul style="list-style-type: none"> • Attract foreign investment • Increase export revenues • Develop domestic private sector

A2 – Social Policy Standards

Social Policy Standards (WBG)		
Type	Source	Standards
Policy on integration of social issues	Environmental and Social Project Review Procedures	'The general requirement to address social issues during the EA process is contained in OP 4.01, Environmental Assessment. Specific policy requirements are contained in [other Operational Policies (OPs) and Directive (ODs)].' 'In some situations...the magnitude and complexity of social issues go beyond the scope or responsibility of the private sector and fall within the domain of government. IFC recognizes the importance and sensitivity of the project sponsor-government relationship in addressing such issues.'
Safeguard policies	OP 4.01 – Environmental Assessment OD 4.20 – Indigenous Peoples OD 4.30 – Involuntary resettlement OPN 11.03 – Safeguarding Cultural Property Child and Forced Labor Policy Statement	see Procedure Standards 'For an investment project that affects indigenous peoples, the borrower should prepare an Indigenous Peoples Development Plan'.... 'Indigenous peoples [defined as] social groups with a social and cultural identity distinct from the dominant society that makes them vulnerable to being disadvantaged in the development process.' 'Where population displacement is unavoidable, Resettlement Plans should be developed'...based on principles of (i) compensation for losses; (ii) support during transition; (iii) restore or improve living standards. 'Category B projects where there are small-scale resettlement...management issues...prepare a detailed Public Consultation and Disclosure Plan (PCDP).'
		'...normally declines to finance projects that will significantly damage non-replicable cultural property...sites having archeological (prehistoric), paleontological, historical, religious, and unique natural values...Deviations from this policy may be justified only where expected project benefits are great, and the loss of or damage to cultural property is judged by competent authorities to be unavoidable, minor, or otherwise acceptable...This policy pertains to any project in which the Bank is involved, irrespective of whether the Bank is itself financing the part of the project that may affect cultural.'
		'...not support projects that use Forced or Harmful Child Labor [as defined in Policy Statement]. Projects should [also] comply with the national laws of the host countries, including those that protect core labor standards and related treaties ratified by the host countries.'

Social Policy Standards (WBG)		
Type	Source	Standards
Disclosure policy	IFC Disclosure Policy, 1998	<p>'IFC recognises and endorses the fundamental importance of accountability and transparency in the development process...the Corporation's policy is to be open about its activities, to welcome input from affected communities, interested members of the public and business partners.'</p> <p>'As an organization owned by governments, IFC is accountable for its stewardship of public moneys and has an obligation to be responsive to its shareholders... As a borrower, IFC has established that disclosure of information concerning its financial condition and policies, in addition to information it is required to publish, helps to attract purchasers of its securities.'</p>
Position Paper	Revenue Distribution	<p>In high-impact, high governance-risk projects, 'IFC will systematically assess the risks that government would misuse the large payments or that intended benefits may not reach local communities'.</p> <p>'IFC encourages sponsors to follow good practice as appropriate in [revenue] transparency, disclosure, capacity building and tracking.'</p>
Position Papers	SME Linkages	'The World Bank Group is promoting SME linkage programs as an effective tool for fostering sustainable poverty reduction, both through strengthened [project] financial viability, and through enhanced development impact.'
Good Practice Manuals	Environmental Assessment Source Book	<p>Various guidance notes used by social review specialists including, inter alia:</p> <p>Ch 3 – Social and Cultural Issues Ch 5 – Strengthening Local Capacities and Institutions Ch 7 – community involvement Update 5 – Public Involvement Update 8 – Cultural heritage Update 14 – Environmental Performance Monitoring Update 18 – Health Aspects Update 19 – Urban Development Update 26 – Strategic Public Consultation</p>
	Doing Better Business through Public Consultation and Disclosure	'All project sponsors should consult IFC's Doing Better Business Through Effective Public Consultation and Disclosure: A Good Practice Manual' – see Manual.
	Community Development Manual	<p>'This guide aims to provide IFC clients...with practical advice to guide them through the process of establishing corporate community development programmes.'</p> <p>Key Principles for Community Development programmes:</p> <ul style="list-style-type: none"> ● engage in effective community consultation ● build trust ● manage expectations by defining roles ● develop appropriate capacity ● mobilise core competencies ● set measurable goals and report on progress ● forge strategic partnerships ● plan for sustainability
	Handbook for preparing a Resettlement Action Plan	See Handbook.

Social Policy Standards (WBG)		
Type	Source	Standards
Good Practice Notes	Addressing the Social Dimensions of Business	<p>'This [guidance] Note will provide the roadmap necessary to undertake the social impact assessment [SIA] process at the project level and prepare the appropriate documentation... needed to fulfill the social assessment requirements for IFC-financed projects.'</p> <p>http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/\$FILE/SocialGPN.pdf</p> <p>'..clients are requested to undertake an integrated Environmental and Social Impact Assessment (ESIA). This includes the Environmental and Social Action Plan [ESAP] ...The social component of the ESAP might comprise a combination of general social mitigation plans (to respond to non-safeguard related impacts) and more specific, policy-driven mitigation plans such as Resettlement Action Plans or Cultural Property Management Plans...and Community Development Plans.'</p> <p>'Whereas traditional social impact assessment tends to focus primarily on the identification and mitigation of adverse impacts. IFC broadens the definition in the context of its ESIA to ...include identification and assessment of positive impacts and opportunities for enhancing socio-economic well being of the people who live and work in the project's area of influence.'</p>
	Addressing Child Labour in the Workplace and Supply Chain	See: http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_childlabor/\$FILE/ChildLabor.pdf
	HIV/AIDS in the workplace	See: http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_hiveng/\$FILE/HIWAIDSEng.pdf
Environmental and Social Facilities	SME Unit (World Bank)	Funds available for: supply chain support; SME development; community development; local economic development.
	Corporate Citizenship Facility	Funds focused on manufacturing and extractive industries, and available for: supply chain support; SME development; community development; local economic development; HIV/AIDS.
	Environmental Opportunities Facility	Funds available for: community development projects that bring specific environmental benefits, eg drinking water, waste water treatment, solid waste disposal/recycling, pollution reduction.
	Sustainable Financial Markets Facility	Funds available for integration of environmental and social considerations into (i) financial institutions and core business activities and corporate strategy.
	Project Development Facility	Technical assistance to private sector, funds available for: strengthening the regulatory environment; building the capacity of business service providers; strengthening business and financial institutions.

A3 – Social Performance Procedural Standards

Social Performance Procedural Standards (WBG)		
Type	Source	Standards
EIA Screening	OP 4.01 EA Procedures for Environmental and Social Review	<p>Category A – ‘significant adverse environmental affects that are sensitive, diverse or unprecedented’. Sensitive defined as ‘irreversible (eg loss of a major natural habitat), affect vulnerable groups or ethnic minorities [ie raise issues in OD 4.20], involve involuntary displacement and resettlement [OD 4.30], or affect significant cultural heritage sites [OPN 11.03]’. EAs for Category A projects must: (i) follow a pre-agreed Public Consultation and Disclosure Plan (PCDP); (ii) compare project design with feasible alternatives, including the ‘without project’ scenario; (iii) examine the projects potential ‘positive and negative impacts’; (iv) include an Environmental Action Plan (EAP). Decisions on categorisation are made on a case-by-case basis, but examples of Category A (given in Annex B) include: major oil and gas developments, including pipelines; industrial plants (large scale); large port and harbour developments, projects with large resettlement components and all projects with potentially major impacts on human populations, projects which pose serious socio-economic concerns.</p> <p>Category B – ‘impacts are site-specific impacts; few of them are irreversible’. EAs for Category B projects ‘examines the project’s potential negative and positive environmental impacts’. Category C – minimal or no adverse environmental impacts. No EA required.</p>
Content of an EA report (Category A projects):	<p>Procedures for Environmental and Social Review: Guidance Note B</p> <p>Guidance Note A</p>	<ul style="list-style-type: none"> • Executive Summary • Policy, legal, and administrative framework • Project description • Baseline data • Environmental and social impacts • Analysis of alternatives • Environmental Action Plan • Appendix – record of interagency and consultation <p>Checklist of potential social issues for assessment:</p> <ul style="list-style-type: none"> • Cultural Properties • Indigenous peoples • Induced development and other socio-cultural aspects (eg boomtown effects etc.) • Involuntary resettlement • Land settlement • Hazards • Occupational health • Exploitation of livelihood-relevant natural resources: forests, watersheds, wetlands, wildlands
Preparation of Public Consultation and Disclosure Plan (PCDP)	Guidance Note F	<p>‘for Category A projects, the project sponsor is required to conduct meaningful consultation with relevant stakeholders including affected groups, nongovernmental organizations (NGOs) and local authorities about the project’s environmental and social aspects...The project sponsor initiates such consultations as early as possible. For meaningful consultations, the project sponsor provides relevant information in a timely manner and in a form and language that are understandable and accessible to the groups being consulted... these actions, and future consultations to be undertaken during the construction and operation of the project, are incorporated into a public consultation and disclosure plan (PCDP).’</p>

A4 – Social Performance (Numerical) Quality Standards

Social Performance (Numerical) Quality Standards (WBG) relevant to Social Performance – <i>not exhaustive</i>		
Type	Source	Details
Air conditions at property boundary	World Bank General Environmental Guidelines	Particulates: annual 50 ug/m ³ NOx: 150 ug/m ³ (max 24hr av) SO ₂ : 50 annual 50 ug/m ³
Liquid Effluent Discharged to Surface Waters (max values)	On-shore Oil & Gas Guidelines (World Bank)	Ph 6-9 BOD 50 mg/l TSS 50 mg/l Oil and grease 20mg/l Phenol 1 mg/l Sulfide 1 mg/l Total toxic metals 5 mg/l Temperature increase <3°C
Noise Levels – residential and educational	On-shore Oil & Gas Guidelines (World Bank)	Day 07:00 - 22:00 55 dB(A) Night 22:00 – 07:00 45 dB(A)

Annex B

Key Social Performance Standards and Good Practice Guidance
within the **European Bank for Reconstruction and Development**
(*Minimum Standards highlighted*)

Hypertext links:

European Bank for Reconstruction and Development

[B1 - Economic Policy Standards](#)

[B2 - Social Policy Standards](#)

[B3 - Social Performance Procedural Standards](#)

[B4 - Social Performance Numerical Quality Standards](#)

B1 – Economic Policy Standards

Economic Policy Standards (EBRD)		
Type	Source	Standards
General policy	Environmental Policy	<p>'An important aspect of the EBRD's additonality is promoting environmental improvements...environmental measures that improve its project sponsor's environmental, operational and economic performance.'</p> <p>The measures suggested in the policy focus on energy and resource efficiency and bio-diversity.</p> <p>'...the EBRD will support investments to assist municipalities...[their] credit-worthiness, decentralisation of public services, involvement of the private sector in provision of public services'..</p>
Country strategies	Various	See specific strategies
Sectoral economic strategies	Natural Resources Operations Policy (new Energy Policy to be adopted in 2005)	<p>'...the natural resource sector could act as a catalyst for foreign investment and greater integration into the global economy. The Bank's project conditionality can represent a certain leverage in tackling these issues, and the economic benefits of natural resource exploitation might therefore be increased.'</p> <p>'the exploitation of natural resources should aim to build up a country's physical and human assets by at least the same amount as its natural wealth is decreased'.</p>
Economic additonality	Annex I (Natural Resources Operations Policy)	<p>'Maximise domestic added value...focus on projects with maximum forward and backwards linkages; promote upstream service ad material supply projects that facilitate local sourcing.'</p> <p>'Maximise return of domestic parties ...concentrate on projects with substantial local involvement; projects with limited foreign involvement or without foreign sponsors.'</p>

B2 – Social Policy Standards

Social Policy Standards (EBRD)		
Type	Source	Standards
General Environmental Policy	Environmental Policy, July 2003	<p>Article 2.1vii – ‘promote in the full range of its activities environmentally sound and sustainable development...’Sustainable development must rank among the highest priorities of the EBRD’s activities...meeting the needs of the present without compromising those of the future.’</p> <p>‘the term ‘environment’...is used in a broad sense to incorporate not only ecological aspects but also worker protection issues (occupational health and safety, harmful child labour, forced labour, discriminatory practices..) and community issues, such as cultural property, involuntary resettlement and impacts on indigenous peoples.’</p> <p>‘The EBRD also clearly establishes the principle that a proposed project can be rejected on environmental grounds.’</p> <p>‘Project will be structured to structured to meet IFC Safeguard Policies on indigenous peoples [OD 4.20, 1991]; involuntary resettlement [OD 4.30, 1990] and cultural property [OPN 11.03, 1986]... The reference to these three Safeguard Policies does not extend to other IFC or World Bank Group policies, operational procedures or any OD, OMS, OPN, Circular, OPNSV or guidelines which may be referenced therein.’</p> <p>‘The EBRD will actively seek, through Bank-financed projects, to contribute to the implementation of relevant principles and rules of international environmental law. These principles and rules are set forth in instruments such as treaties, conventions and multilateral, regional or bilateral agreements, as well as in relevant non-binding instruments.’ (Section 8)</p>
Disclosure and Consultation Policy	Environmental Policy, July 2003, Annex 2	<p>‘The Bank is committed to providing information, within the requirements of the Public Information Policy and the Environmental Policy.’</p> <p>‘Whenever possible, information concerning the Bank’s operational activities will be made available to the public in the absence of a compelling reason for confidentiality.’</p> <p>‘Public consultation and information disclosure is the responsibility of the project sponsor.’</p> <p>‘In particular, for significant ‘greenfield’ projects and projects involving a major expansion or transformation-conversion, the Bank is committed to meaningful consultation.’</p> <p>‘At a minimum, project sponsors must ensure that all such national requirements for public consultation, and that the EBRD requirements, are met.’</p> <p>‘The EBRD does not have specific requirements for public hearings, but encourages development of appropriate methods of meaningful consultation, depending on the objectives of the consultation, cultural norms of the project location, and good international practice.’</p>

B3 – Social Performance Procedural Standards

Social Performance Procedural Standards (EBRD)		
Type	Source	Standards
EIA Screening Procedures	EBRD Environmental Procedures	<p>'Any project being considered for Bank funding that is listed in [Annex 1 of the Environmental Policy] is automatically subject to an EIA and must...be classified as a Category A project.'</p> <p>Annex I: Environmental screening categories: 'Greenfield or major extension projects: Extraction of petroleum and natural gas for commercial purposes... Crude oil refineries (excluding undertakings manufacturing only lubricants from crude oil) and installations for the gasification and liquefaction of 500 tonnes or more of coal or bituminous shale per day...Integrated chemical installations...Pipelines, terminals and associated facilities for the large-scale transportation of gas, oil and chemicals.'</p>
Environmental Audit Screening Procedures	Environmental Policy	<p>'The screening process also determines whether an Environmental Audit is required (Category 1) or not (Category 0). Environmental Audits are carried out to assess the impact of past and current operations of existing project and/or company facilities'</p>
EIA procedures	EBRD Environmental Procedures	<p>Environmental Summary form [Annex 1] requires information on screening category; (environmental) risk rating and environmental opportunities rating.</p> <p>For oil and gas projects, Initial Environmental Examination not needed because EEI only used where category is uncertain. Since all oil and gas projects are Cat A, no EEI is needed.</p> <p>Likewise, Environmental Analysis (a lesser version of EIA), is not needed, since all Category projects require a full EIA.</p> <p>Annex 2 – Generic guidance on Table of Contents for EIA, including: landscape and visual impacts; air quality; noise; social and socio-economic issues – community, vulnerable groups, cultural, archaeological/heritage, public health – occupational health and safety.</p> <p>Analysis of project 'feasible alternatives' including 'no project option' is required.</p>
Information Disclosure and Public consultation	Environmental Policy – Annex 2 EBRD Environmental Procedures	<p>'...For all category A projects, public consultation requirements should be built into each stage of the EIA':</p> <p>'notification...to affected people...[defined as: potentially affected public and interested non-governmental organisations]...about the nature of the project'</p> <p>'scoping.. identification of all key issues...by consulting the affected public...as part of the scoping process the project sponsor is required to prepare a draft Public Consultation and Disclosure Plan (PCDP) describing the public who may be affected by the project, how communication will work throughout the EIA process, and what information will be disclosed in relevant languages and by what means. The public should be able to provide to provide comments and recommendations on the PCDP as well</p>

Social Performance Procedural Standards (EBRD)		
Type	Source	Standards
		<p>as other scoping documents.'</p> <p>EIA disclosure ..project sponsors must make the EIA publicly available for comment, see details in Environmental Policy Annex 2 http://www.ebrd.com/about/strategy/index.htm</p> <p>EBRD disclosure – ...'EIA will be provided to the Bank's Business Information Centre. and in the EBRD resident office. Public comments – project sponsor will need to provide information to those commenting [on the EIA] and the effected o how comments were taken into account.'</p> <p>'As part of the scoping process, the project sponsor is required to prepare a draft Public Consultation and Disclosure Plan (draft PCDP), describing the public who may be affected by the project, how communication will work throughout the EIA process, and what information will be disclosed in relevant language and by what means.'</p> <p>'For projects involving transboundary impacts, the notification and consultation guidelines in the working papers to the UNECE Convention on EIA in a Transboundary Context must be taken into account in the planning process and followed in principle. Bank staff will summarise how these guidelines have been followed to management, the Board, and in the Project Summary Document. The EBRD may, according to circumstances, provide guidance to, and assist, the project sponsors at this and other stages of the public consultation process, recognising the Convention obligations are between governments with the aim of finding practical solutions to implementation of the principles, particularly for those projects in countries which are not party to the Convention.'</p> <p>'For all projects involving Environmental Impact Assessment according to the Bank's requirements, the Bank will take guidance from the principles of the UNECE Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matters, as committed in the EBRD Public Information Policy.'</p> <p>'On 'B' level projects, the country's public consultation requirements will need to be followed at a minimum.'</p> <p>In addition, the project sponsor must notify the affected public about the relevant environmental issues associated with the project and summarise the mitigation measures, action plans and other initiatives agreed, in an appropriate language. This summary must be released locally by the time of the final management review of the project, prior to Board consideration.</p> <p>'Requirements for information disclosure on 'C' level projects are set on a case-by-case basis.'</p>

Social Performance Procedural Standards (EBRD)		
Type	Source	Standards
Public Reporting	Environmental Policy	<p>'For all categories of projects where significant environmental issues have been raised, or where the affected public is particularly interested, the EBRD will encourage or require project sponsors to commit to ongoing information and communication programmes. For example, the Bank may require the results of ongoing environmental monitoring to be made available to the public.</p> <p>For all projects, environmental issues will be summarised in the Bank's Project Summary Document, which is posted on the Bank's website and is available from the Bank in hard copy prior to Board, in accordance with the EBRD Public Information Policy.</p> <p>As part of the annual environmental reporting requirements to the Bank, project sponsors will be asked to provide a summary on the environmental status and implementation of project environmental requirements for publication on the Bank's website, attached to the Project Summary Document for the project.</p> <p>For A-level projects, the Bank will require project sponsors to provide an annual environmental report to the affected public locally and will encourage release of this information on the project sponsor's website.'</p>
Conditionality	Environmental Policy EBRD Environmental Procedures	<p>'Legal documents for the EBRD's investment in a project will include specific provisions reflecting EBRD's environmental requirements resulting from the environmental appraisal process, such as compliance with the Environmental Action Plan (EAP), provisions for environmental reporting, periodic environmental audits by independent experts, the inclusion of environmental performance criteria in the definition of 'Project Completion', exit audits and/or monitoring visits.'</p> <p>'The main instrument for negotiating between the Operation Team [overall responsible for environmental aspects of the project, informed by Environment Department] is the Term Sheet...Environmental requirements and conditionalities should be incorporated early into the draft Term Sheet, to avoid delays in the project cycle, including the need to renegotiate the Term Sheet.'</p>
Delays	EBRD Environmental Procedures	'If the project remains unsigned after twelve months, ...ED specialists may request an update from the Company on the environmental status of the project and in implementing the EAP.'
EAP implementation	Environmental Policy	<p>'the EBRD requires that the project sponsors submit periodic reports on the implementation of EAPs and any other environmental requirements. As a rule annual reports will be expected.'</p> <p>'During implementation, results of reports, audits or monitoring trips may indicate that change are necessary to the EAP. In this case the EAP may be updated or revised, to the satisfaction of the Bank.'</p>

B4 – Social Performance Numerical Quality Standards

Social Performance (Numerical) Quality Standards (EBRD)		
Type	Source	Details
Quality standards	Environmental Policy	<p>‘The EBRD will require that projects be structured so as to meet: (i) applicable national environmental law; (ii) EU environmental standards, insofar as these can be applied to a specific project.. Where such standards do not exist or are inapplicable, the EBRD shall identify other sources of good international practice, including relevant World Bank Group guidelines, the approach to other IFIS and donors, and good industry practice.’</p> <p>‘EBRD will not finance projects that would contravene country obligations under relevant international environmental treaties and agreements, as identified during environmental appraisal.’</p> <p>For labour issues the above, in connection with Section 8, are implemented by the Bank to the effect that projects must meet national employment laws, as well as the ILO conventions related to child labour (138,182) , forced labour (29, 105), and unlawful discrimination (100, 111).</p> <p>Each EBRD Country Strategy reflects the EBRD environmental mandate, and will draw on National Environmental Action Plans and EU accession strategies, the latter which may refer to applicability of EU standards.</p>

Key References

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- ➔ EBRD (2002) *Environmental Policy, Annex 2: Consultation with the Public*, London: European Bank for Reconstruction and Development.
- ➔ EBRD (undated) Natural Resources Operations Policy - <http://www.ebrd.com/about/policies/sector/natural/natural.pdf>
- ➔ ECDG (2003) *ECDG Business Principles*, London: Export Credit Guarantee Department.
- ➔ Extractive Industries Review - Final World Bank Group Management Response - <http://www.worldbank.org/ogmc/>
- ➔ IFC Corporate Citizenship Facility: <http://ifcln1.ifc.org/ifcext/enviro.nsf/e11ffa331b366c54ca2569210006982f/11a491f7398c599585256ead006d0d2b?OpenDocument>
- ➔ Insight Investment (2003) *Defining Global Business Principles*, London, Insight Investment.
- ➔ International Finance Corporation (2004): Addressing the Social Dimensions of Business: A Good Practice Note - [http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/\\$FILE/SocialGPN.pdf](http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/$FILE/SocialGPN.pdf)
- ➔ IPEICA/OGP (2002) 'Key Questions in Managing Social Issues in Oil and Gas Projects', *Report No. 2.85/332*, London: International Association of Oil and Gas Producers/International Petroleum Industry Conservation Association.
- ➔ Kaufmann, D, et al (2003) *Governance Matters III*, Washington DC: World Bank.
- ➔ Mineral Risk Extraction Assessment formula used by BERI (Business Environment Risk Intelligence) - <http://www.beri.com/mera.asp>
- ➔ ODI/EAP/Balfour Beatty (2004) *Enhancing Social Performance in the Engineering Services Sector through the Process of Risk and Opportunities Analysis*, London: Overseas Development Institute.
- ➔ Shell International (2005 forthcoming) 'Meeting International Social Performance Requirements for Project Financing' (internal publication) *Social Performance Guidance Note Series, No. E3*, London: Shell International, Social Performance.
- ➔ Shell International (2005) *Commitments, Policies and Standards* - <http://www.ifc.org/ifcext/policyreview.nsf>
- ➔ World Bank Development Indicators Database - <http://www.worldbank.org/data/countryclass/classgroups.htm>

Further Information

- ➔ Equator Principles (social and environmental standards for commercial lenders) – <http://www.equator-principles.com/>
- ➔ International Finance Corporation: Addressing the Social Dimensions of Business: A Good Practice Note – [http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/\\$FILE/SocialGPN.pdf](http://ifcln1.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/p_socialGPN/$FILE/SocialGPN.pdf)
- ➔ International Finance Corporation – latest on review of social and environmental performance standards: <http://www.ifc.org/ifcext/policyreview.nsf>
- ➔ Mineral Risk Extraction Assessment formula used by BERI (Business Environment Risk Intelligence) – <http://www.beri.com/mera.asp>
- ➔ Project Finance Portal – <http://www.people.hbs.edu/besty/projfinportal/ecas.htm>
- ➔ World Bank/IFC social and environmental review procedures (safe guard policies, SIA/EIA procedures; guidance notes etc.) – <http://ifcln1.ifc.org/ifcext/enviro.nsf/Content/ESRP#policies>