



# **GIZ - SIDBI**

## **Responsible Enterprise Finance Project**



# SIDBI-GIZ Project on Responsible Enterprise Finance

## Objective

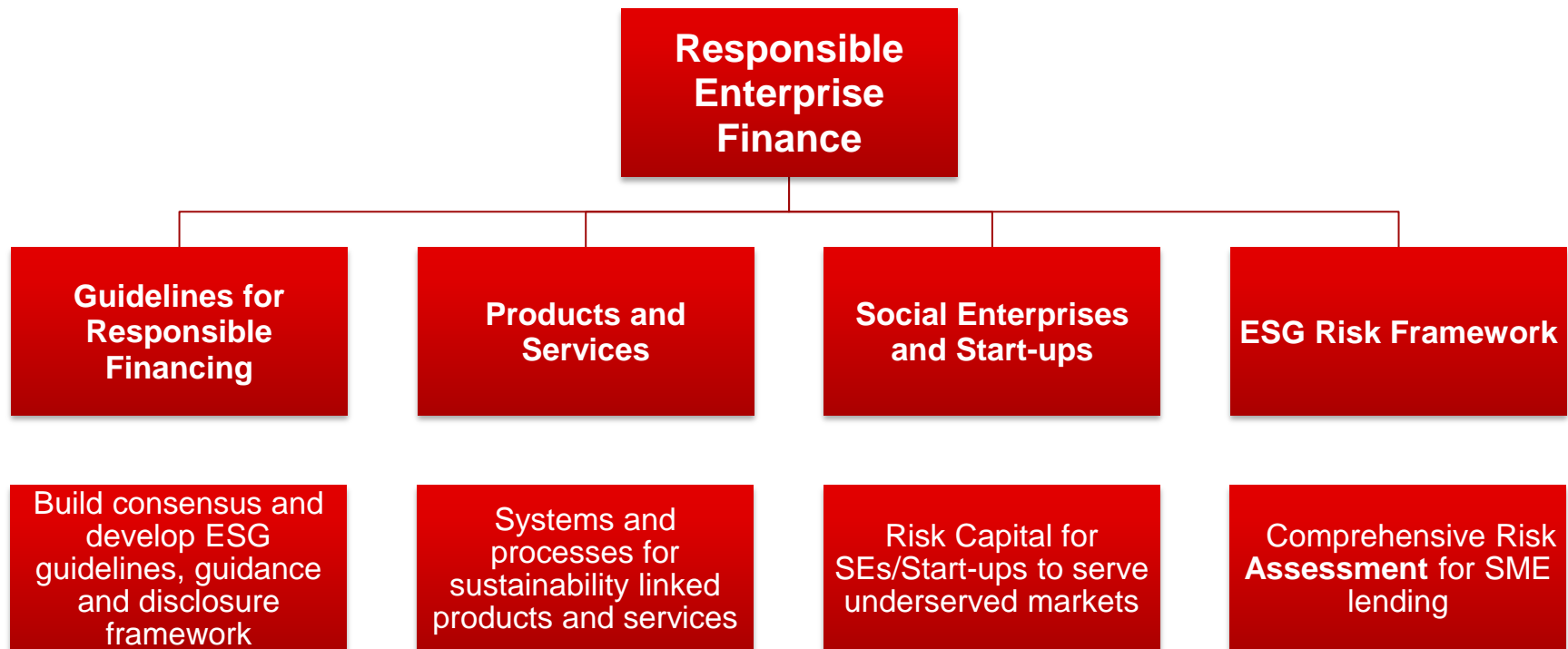
- Improve flow of capital to SMEs for sustainable (environmentally friendly/socially responsible) investments

## Approach

- Voluntary commitment and market based incentives
- Develop Tools and support pilots for adoption



# Design of GIZ-SIDBI Project





# GUIDELINES FOR RESPONSIBLE FINANCING

Supported by: IBA, Mumbai

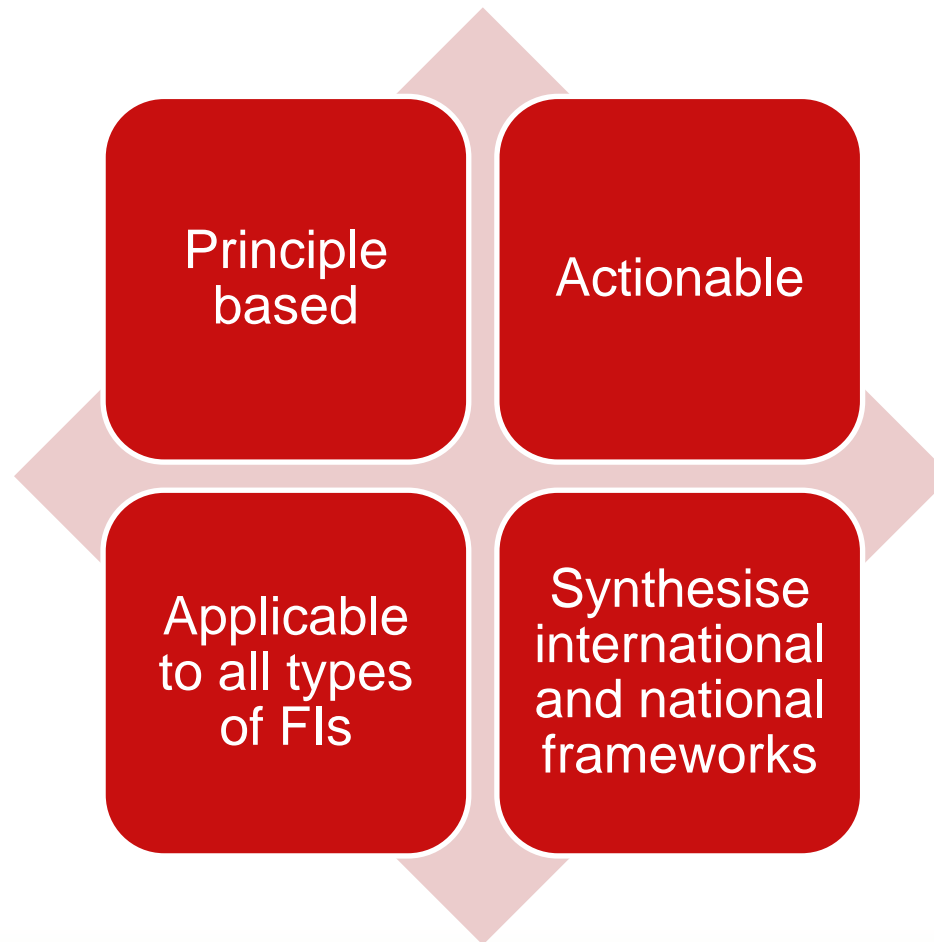


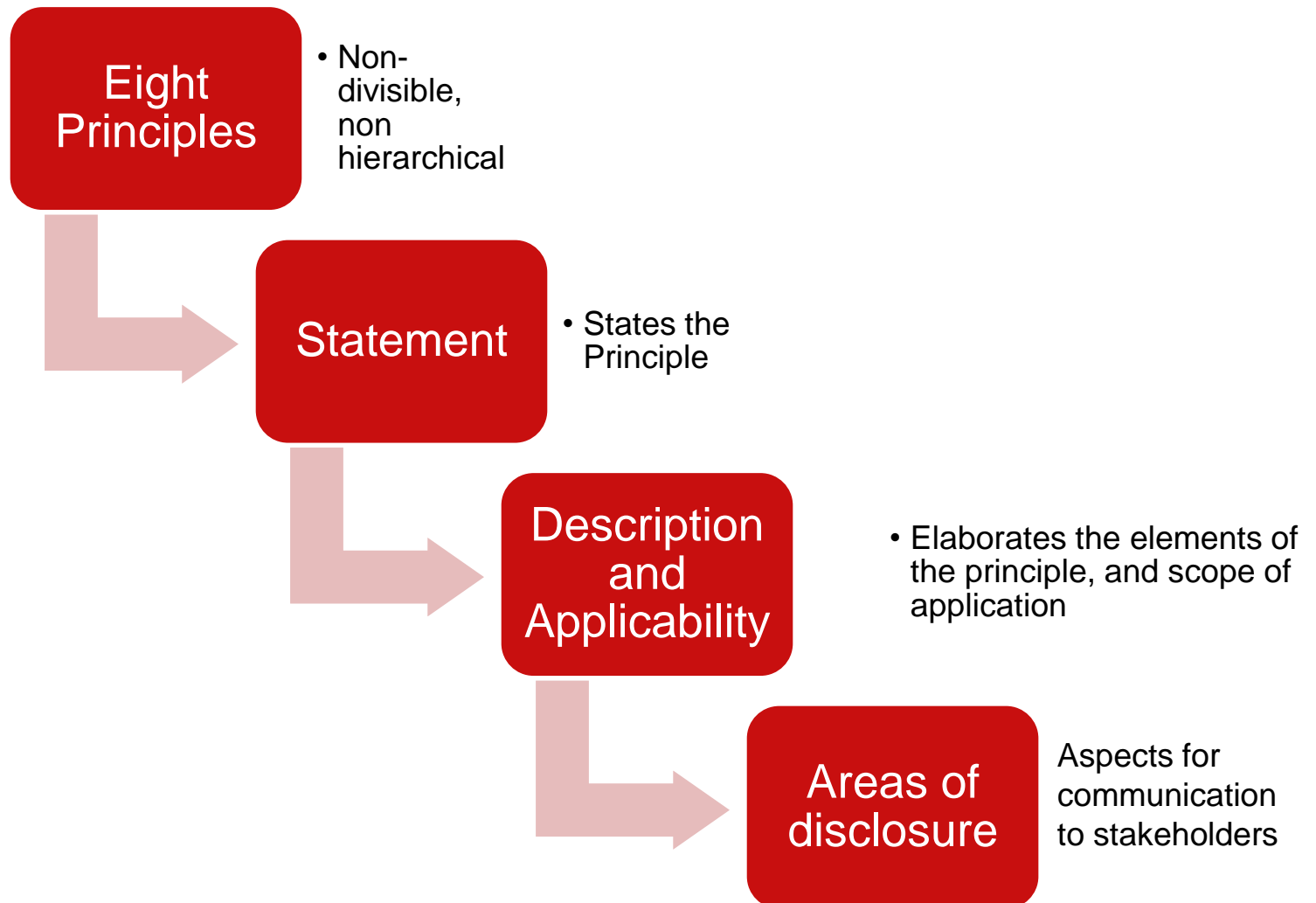
## GDG members

Organisation	Name	Designation
<b>cKinetics</b>	Mr Pawan Mehra	CEO and founder
<b>GIZ</b>	Ms Neha Kumar	Senior Advisor, GIZ and Project Secretariat Lead, Member of the NVGs Drafting Committee
<b>IDFC</b>	Mr Alok Dayal	Senior Director - Credit and Environment Risk
<b>IDFC</b>	Mr Rajnish Kadambar	Director– Environment Risk
<b>IDFC</b>	Mr. Pankaj Verma	Senior Vice President – Environment Risk
<b>IL &amp; FS</b>	Mr Alok Bhargava	CEO – Strategic Support Group
<b>IL&amp;FS</b>	Mr Santhosh Shidhaye	Senior Vice President
<b>SIDBI</b>	Mr Anand Shrivastava	Deputy General Manager
<b>SIDBI</b>	Mr Pradyumna	Deputed by SIDBI
<b>Tata Group</b>	Mr. Shankar Venkateswaran	Group Head- Sustainability, Member of the NVGs Drafting Committee
<b>Yes Bank</b>	Ms Namita Vikas	Head – Responsible Banking
<b>Yes Bank</b>	Ms Neha Kapoor	Senior Vice President- Responsible Banking
<b>SBI</b>	V Murali	Deputy Managing Director
<b>Research and coordination support</b>		
<b>GIZ-SIDBI</b>	Trina Datta	Consultant



## Vision of the Guidelines







## 1. Ethical Conduct and E&S Governance

- Financial institutions should develop sound governance systems to oversee environmental and social performance of their business activities and disclose accordingly.

## 2. Integration of E&S Risk Management in Business Activities

- Financial Institutions should integrate the analysis of environmental and social factors into their investment, lending and risk-management processes across business lines to minimise adverse impact on its own operations and on society.

## 3. Minimising Environmental footprint in internal operations

- Financial institutions should minimise the negative impacts of their business operations on the environment in which they operate and, where possible, promote positive impacts.

## 4. Environmentally friendly products, services and investments

- Financial institutions should invest in environmentally friendly products and businesses that enhance positive environmental impact.





## Principles contd...

### 5. Enabling inclusive human and social development

- Financial institutions should support inclusive and equitable human and social development.

### 6. Stakeholder Engagement

- Financial institutions should develop an understanding of their stakeholders' needs, interests and expectations to inform and guide their strategy and decision-making.

### 7. Commitment to human rights

- Financial institutions should respect and promote human rights.

### 8. Disclosure

- Financial institutions should regularly review and report on their progress in meeting the Principles contained in these Guidelines



# **Introduction to the GIZ-SIDBI Environment Social Governance (ESG) Framework**



## **Contents**

**1**

### **Objective and Methodology**

#### **Development of GIZ-SIDBI ESG Framework**

**2**

- a. Comparative analysis of leading ESG Frameworks**
- b. ESG Policy guidelines for banks**
- c. Development of toolkit**



# Objective and Methodology

## OBJECTIVE

- The GIZ -SIDBI ESG Framework aims at strengthening financial institutions capacities to integrate ESG concerns in their strategic decision- making
- ESG Framework, is broad in scope and can cater to SME lending in different segments and sectors serviced by banks in India.
- It should refer to Indian laws and regulations
- It should be easy to use by non E&S experts

## Methodology for development of the ESG Framework

### 1. Comparative Analysis of leading ESG Frameworks:

As part of this Framework, a comparative analysis of leading ESG Frameworks was carried out to identify key environmental, social and governance concerns

### 2. Draft ESG Risk Assessment Policy:

Development of broad level ESG Policy guidelines for banks defining the business areas to be covered , manner of integration in existing processes and systems and allocation of responsibilities in the Bank

### 3. Development of GIZ -SIDBI ESG Framework:

- Tool 1: Initial screening
- Tool 2: ESG Due Diligence
- Tool 3: ESG Scoring System
- Tool 4: Monitoring and reporting formats



# About GIZ -SIDBI ESG Framework (FW)

## USP /Strengths of FW

## Description

- | USP /Strengths of FW             | Description                                                                                                                                                                                                                                                                    |
|----------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 Excel toolkit                  | <ul style="list-style-type: none"><li>• An excel based toolkit with inbuilt automated tools which will help the bank assessing ESG risks with minimum subjectivity</li></ul>                                                                                                   |
| 2 Initial risk categorization    | <ul style="list-style-type: none"><li>• Tool 1 weights environmental, social and governance factors equally and provides automated results for the Risk based on sector/industry</li></ul>                                                                                     |
| 3 Due diligence                  | <ul style="list-style-type: none"><li>• Appropriate diligence checklists open automatically based on initial risk categorization</li></ul>                                                                                                                                     |
| 4 ESG scoring system             | <ul style="list-style-type: none"><li>• Rating sheet is linked to due diligence checklists, minimizing duplication</li><li>• Based on answers given, a rating ranging from 0 to 3 is automatically generated, indicating the borrowers ESG performance</li></ul>               |
| 5 Monitoring & reporting formats | <ul style="list-style-type: none"><li>• Key ESG risks are highlighted with the mitigation measures in the monitoring sheet.</li><li>• Key opportunities are identified and agreed timelines and responsibilities for achievement are recorded in the loan agreement.</li></ul> |



## Development of GIZ - SIDBI ESG Framework







# ESG Policy Guidelines for Banks

Development of broad level ESG Policy guidelines for banks bringing out the objective, motive, scope, responsibilities for compliance & key ESG considerations

## The Policy guidelines address the following points

### Need for ESG Policy for investments:

- The bank should seek to ensure through its evaluation and assessment processes that the projects it finances are
  - Sustainable
  - Are in compliance with applicable regulatory requirements
- The Bank institutionalizes processes for ESG screening and allocates staff responsibilities



ESG Policy  
guidelines

## The policy should broadly cover the following considerations

### Environmental considerations

- Environmental Management System
- Compliance to regulations
- Pollution prevention (waste water / effluent and emissions)
- Energy - manage and minimize energy usage;
- Waste management;
- Water supply management;
- Protection and conservation of biodiversity; and
- Green House Gas monitoring

### Social considerations

- Compliance to regulations;
- Respect Human Rights;
- Safe working conditions;
- Labour Practice (Prohibition against child and forced labour);
- Land acquisition;
- Resettlement and Rehabilitation;
- Indigenous people;
- Health and safety;
- Collective bargaining;
- Community impact assessment etc.
- Stakeholder consultations; and
- Contract workers;

### Governance considerations

- Ensuring promotion of ethical governance within the organization.
- Ensuring structuring and functioning of Board of Directors and their effectiveness
- Ensuring transparency and disclosure by establishment of governance structures and processes to oversee ESG integration within the organization.
- Control and risks (internal audit and control function, external audit)
- Grievance Redressal mechanism in place.
- Whistle blower mechanism.
- Roadmap for action, and disclosure and reporting on action taken.



# Development of GIZ -SIDBI ESG Framework

- Tool 1: Initial screening
- Tool 2: ESG Due Diligence
- Tool 3: ESG Scoring System
- Tool 4: Monitoring & reporting formats

## Pre - Investment Screening

## Due Diligence

## Investment Decision

## Investment Agreement

## Investment Monitoring

## Exit

**Exclusion List:** Check if the proposed borrower has activities covered in the Exclusion list. If yes, the investment is a 'no-go'.

**Risk based categorization.** If investment clears the exclusion list, the tool automatically categorizes it into high, moderate or low risk based on the sector (See Tool 1)

A thorough check list of the borrowers compliance with all relevant laws, regulations and with international best practices(See Tool 2)

The investment decision is made by the bank / FI after considering and analyzing all the aspects of ESG due diligence.

A scoring system enables the banks / FIs to rate the ESG status of the borrower (See Tool 3). This score will support the decision taken

The investment decision is made by the bank / FI after considering and analyzing all the aspects of ESG due diligence

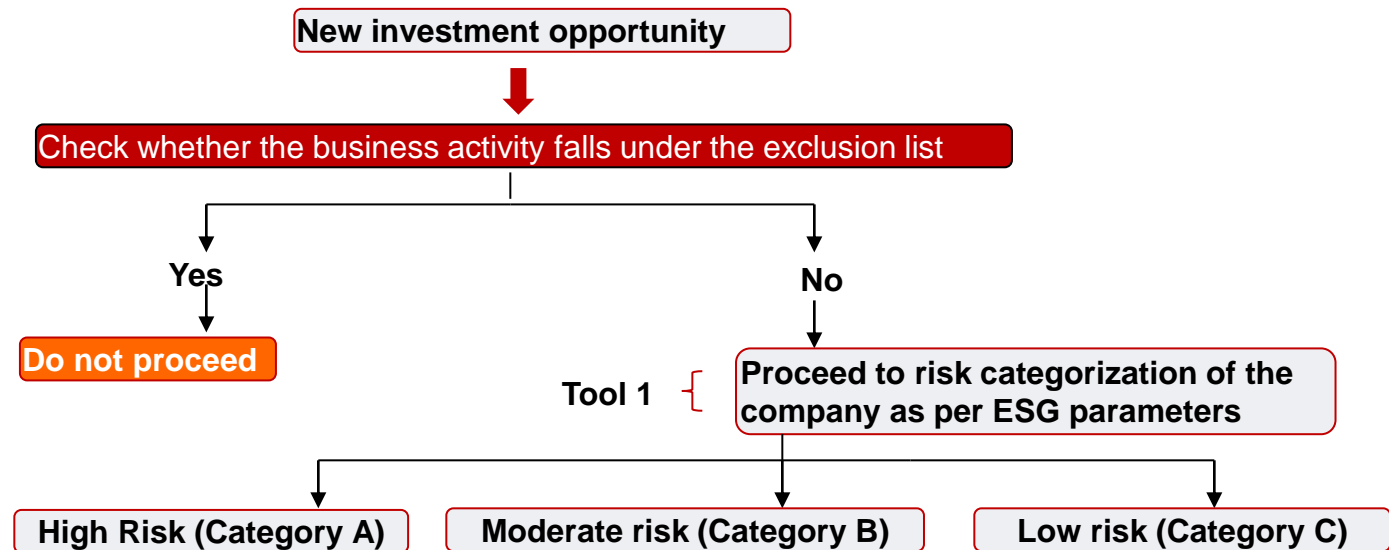
The bank should also monitor its investment throughout the investment period from the ESG perspective and check the company's ESG performance through monitoring and reporting procedures (See Tool 4).





# Development of GIZ -SIDBI ESG Framework

## Procedures to be followed using the ESG Toolkit





# Development of GIZ -SIDBI ESG Framework

## Tool 1: Initial Screening

### Tool 1: Initial Screening

#### Exclusion List

##### A sound exclusion list includes:

- Activities which are regulated or prohibited under international agreements and national laws.
- Activities which may give rise to significant environment / social problems, or that lead to significantly adverse public reaction.

#### Initial risk based categorization

- It is a screening mechanism to determine the level of risk based on social, environmental and governance related impacts linked to that investment and to trigger a series of actions that the company needs to take to manage / mitigate those risks.

1

**Exclusion List : It is an exhaustive list, however Banks / Financial Institutions (FI's) can add and remove industry / activity in this list as per their internal policies and regulations.**

This list was prepared after analyzing various leading international ESG Frameworks such as:

- Department for International Development
- International Finance Corporation
- Asian Development Bank
- FMO



**Tool 1: Initial risk  
categorization**



# Development of GIZ -SIDBI ESG Framework

## Tool 1: Initial Screening

S.No.	Exclusion List	Description
1	Production or trade in any product or activity deemed illegal under Indian laws or regulations or international conventions and agreements.	
2	Production or trade in weapons and munitions (Except Indian Defence approved projects)	The exclusion applies to businesses majorly engaged in the sale of tobacco, alcoholic beverages or gambling and casinos. This does not apply to project sponsors who are not substantially involved in these activities. "Not substantially involved" means that the activity concerned is ancillary to a project sponsor's primary operations.
3	Production or trade in alcoholic beverages (excluding beer and wine)	
4	Production or trade in tobacco	
5	Gambling, casinos and equivalent enterprises	
6	Trade in wildlife or wildlife products regulated under CITES.	CITES (Convention on International Trade in Endangered Species of Wild Fauna and Flora): A list of the species is available from the CITES website at: <a href="http://www.cites.org/sites/default/files/eng/disc/species_02.10.2013.pdf">http://www.cites.org/sites/default/files/eng/disc/species_02.10.2013.pdf</a>
7	Production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where the radioactive source to be trivial and / or adequately shielded.	This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where the radioactive source to be trivial and / or adequately shielded.



# Development of GIZ -SIDBI ESG Framework

## Tool 1: Initial Screening

2

### Initial risk based categorization

#### Qualifying criteria for investments

If the investment is deemed to be a “no-go”, it is not pursued further. If the investment is a “go”, the FIs should then categorize the project into category A, B or C based on the respective risk levels

#### Business Information Request List (BIRL)

BIRL will act as a screening mechanism to determine the level of ESG risk and related impacts linked to an investment. On the basis of the BIRL and the initial risk parameters, each investment will be classified under the ESG categories as High risk, Medium risk and Low risk.

#### Aspects covered as part of BIRL



Understanding of the business

Details of management and Board Members

Location of Company's operations

Understanding of the process or service delivery model

Sectors in which they operate

Finance performance of the company



# Development of GIZ -SIDBI ESG Framework

## Tool 1: Initial Screening

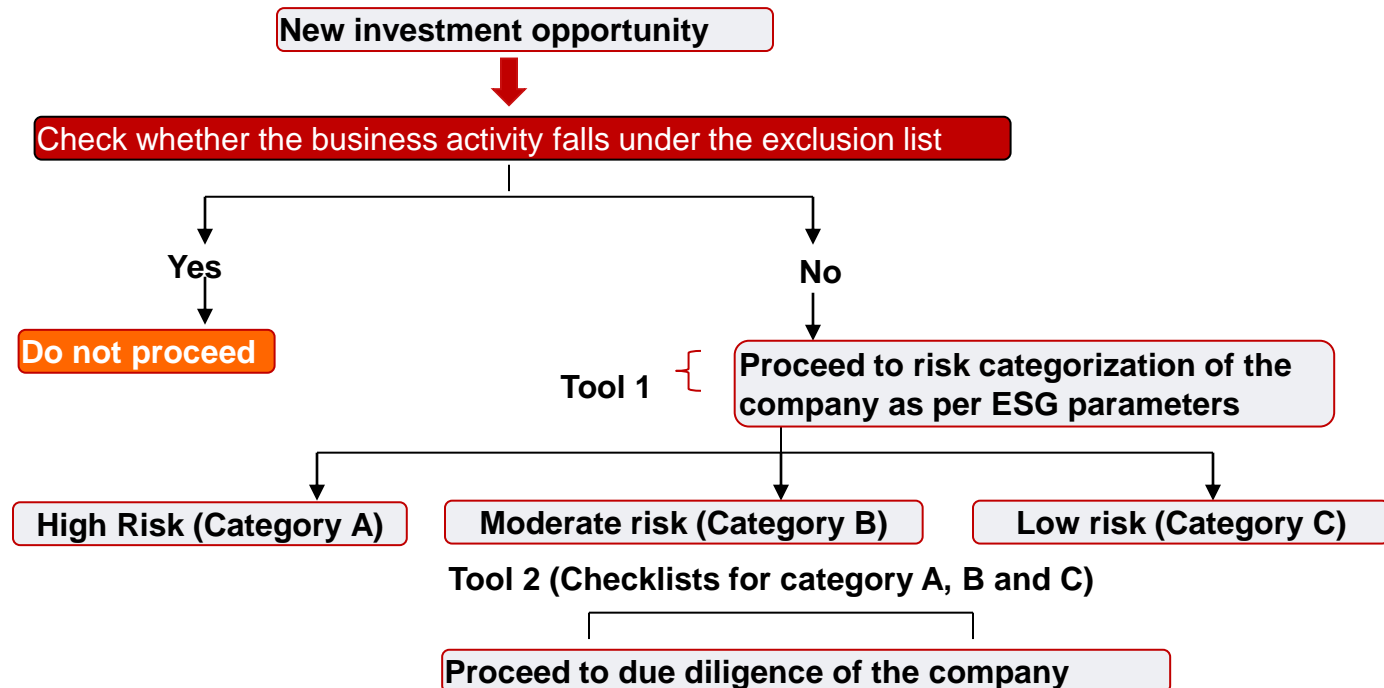
### Classification of investments into high, moderate and low risk

Parameters	Category A	Category B	Category C
<b>Environment</b>	A proposed investment is classified as Category A if it is likely to have significant adverse environmental impacts that are sensitive, diverse or unprecedented.	A proposed investment is classified as Category B if its potential adverse impacts on environmentally important areas are less adverse than those of Category A investments but more adverse than Category C investments.	A proposed investment is classified as Category C if it is likely to have minimal or no adverse environmental impacts. (This list is as per the MoEF classification and is given as Annexure 2)
<b>Social</b>	A proposed investment is classified as Category A if it is likely to have significant adverse impacts on human populations that are sensitive, diverse or unprecedented.	A proposed investment is classified as Category B if its potential adverse impacts on human populations are less adverse than those of Category A investments but more adverse than Category C investments	A proposed investment is classified as Category C if it is likely to have minimal or no adverse impacts on human populations. (This list of industries is given as Annexure 3)
<b>Governance</b>	<p>The proposed investment does not have any elements of good corporate governance</p> <ul style="list-style-type: none"> <li>The CIBIL score of the key promoter lies within the range of 450-539.*</li> <li>There is evidence of company's involvement in controversial or illegal activities (e.g. insider trading, bribery or money laundering and there is evidence that the board is violating its code of ethics) and it has received a litigation notice regarding the same.</li> <li>The experience of the promoter is less than 5 years.</li> </ul>	<p>The proposed investment has only some elements of good corporate governance.</p> <ul style="list-style-type: none"> <li>The CIBIL score of the key promoter lies within the range of 540 and 674*</li> <li>The company has been involved in certain controversial or illegal activities and has taken steps for mitigating any breach in the code of ethics / conduct.</li> <li>The experience of the promoter ranges between 5-10 years.</li> </ul>	<p>The proposed investment has strong elements of good corporate governance.</p> <ul style="list-style-type: none"> <li>CIBIL score of the key promoter is 675 and above *</li> <li>There has been no breach of the code of ethics and no illegal incidents related to bribery or corruption have taken place in the recent past.</li> <li>The experience of the promoter is 10 years and above.</li> </ul>



# Development of GIZ -SIDBI ESG Framework

## Procedures to be followed using the ESG Toolkit





# Development of GIZ -SIDBI ESG Framework

## Tool 2 : ESG Due Diligence Checklist

Due diligence for ESG screening is conducted on the investee company to evaluate their performance on Environmental, Social and Governance parameters. This exercise is done at an early stage to ensure that the investee company complies with the minimum expected international standards and national compliance level.

### Purpose of an Information Request List (IRL)

It would ensure that the investee company complies with the minimum expected standards and identifies areas of improvement in meeting the compliance level and other international ESG criteria during the investment duration.

There are 2 checklists devised:

- a. General Checklist- For Category A, Category B and Category C investments
- b. Sector specific checklists for the 8 identified sectors:
  - Agriculture and food processing
  - Education
  - Healthcare
  - Infrastructure
  - Information Technology
  - Motor vehicles & transport
  - Utilities
  - Telecommunications



ESG Due diligence  
checklist

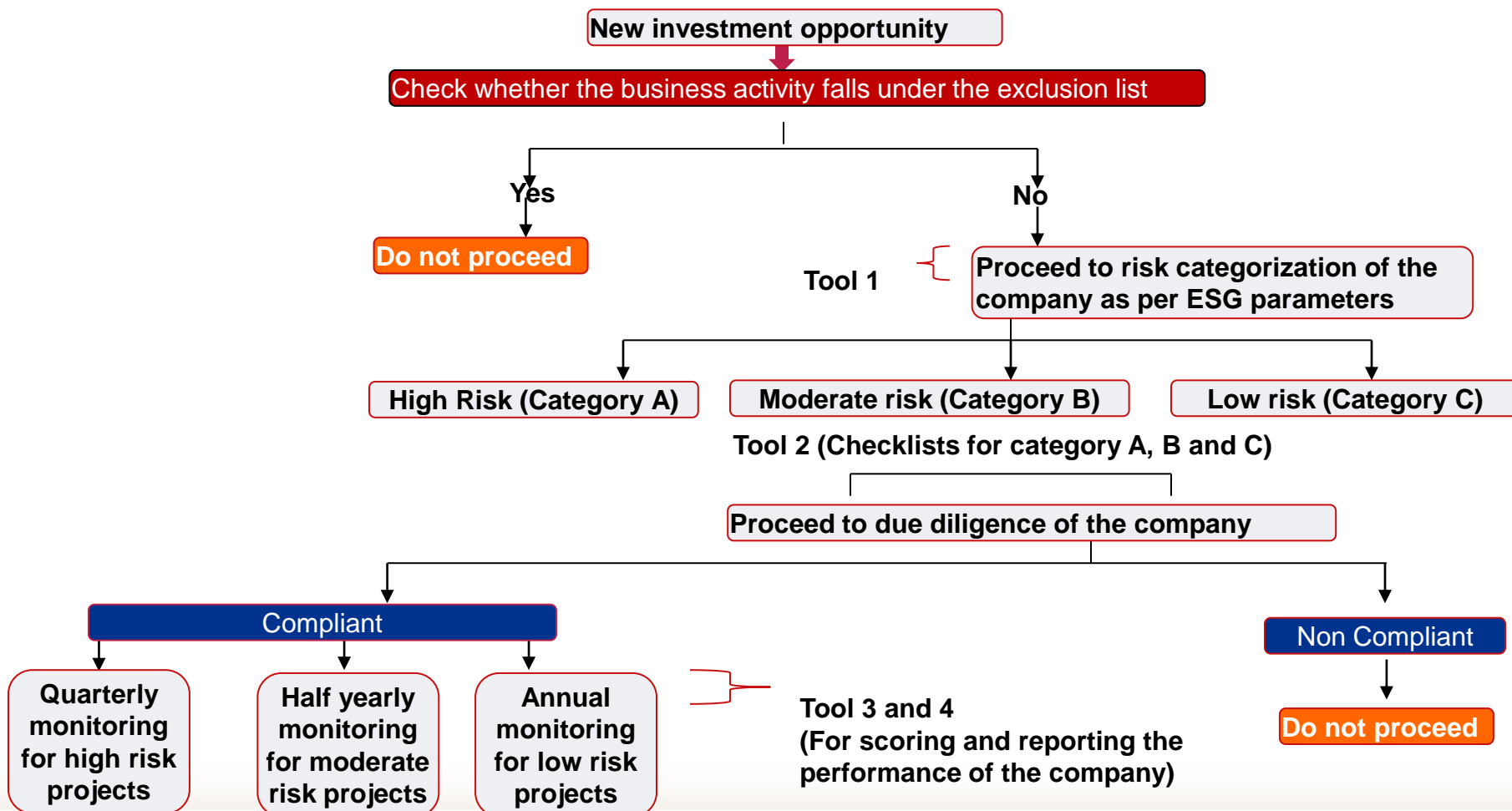


Sector specific  
checklists



# Development of GIZ -SIDBI ESG Framework

## Procedures to be followed using the ESG Toolkit







# Development of GIZ -SIDBI ESG Framework

## Tool 3 : ESG Scoring System

One of the main objectives of the ESG Framework is to enable the Banks / FIs to rate the ESG status of an investee company at the time of investment and through the investment lifecycle. This rating system can be used in the following ways:

- To assess and rate a company at the time of investment;
- To continuously monitor performance and to assess value additions throughout the investment period.

- In the mid-point and final evaluation reports, the company is given an evaluation rating ranging from 0 to 3.
- It is an indicator of ESG performance of the company and facilitates measurement of improvements during performance assessment

### ESG Rating System



Parameters	0	1	2	3
Environment				
Social Development				
Governance				

Note: 0= unsatisfactory; 1= satisfactory;  
2= v. good; 3 = excellent.

### Explanation of rating

Rating 0	Rating 1	Rating 2	Rating 3
The company does not meet minimum requirements, applicable to the company.	Company is taking ESG initiatives, but only to meet regulatory requirements	Company goes beyond the legal requirements and fulfills additional ESG requirements beyond compliance	It represents incorporation of international best practices in the company's procedures



# Development of GIZ -SIDBI ESG Framework

## Tool 3 : ESG Scoring System

### Rating Parameters

#### ENVIRONMENT

- Register of Regulations
- Pollution abatement and testing
- Resource efficiency
- Greenhouse gas emissions reduction
- Environment Policy and organizational structure
- Certification of Management System
- Disclosure and reporting
- Environment Management Plan

#### SOCIAL

- Social Policy
- Grievance redressal mechanism
- Monitoring / audits
- Minimize impacts and provide fair compensation and livelihood restoration
- Emergency plans
- Health and safety policy and training

#### GOVERNANCE

- Promote fair and transparent way of doing business
- Ensure good governance practices at the company
- Ensure adequate internal checks for managing risks

ESG Scoring Tool



ESG Scoring  
System



# Development of GIZ -SIDBI ESG Framework

## Tool 4 : ESG Monitoring and Reporting Formats

**This tool is aimed at depicting the process of monitoring, recording and managing the ESG performance of the investee company through requisite formats and illustrations.**

**Investments are monitored from an ESG perspective to check:**

**Company's on-going compliance with relevant laws, standards and regulations**

**Ensure timely implementation of action plans for ESG improvements**

**Encourage companies to work towards continuous improvement**

**Ensure that any new risks, issues or opportunities for improvement are dealt with in an appropriate manner**

**To monitor and record serious incidents that result in loss of life, serious injury etc.**

**To record and report key performance indicators to the investors**

**There are two reporting structures as part of the monitoring and reporting process:**

- 1. Audit Report**
- 2. Report for potential opportunities**



# Development of GIZ -SIDBI ESG Framework

## Tool 4 : ESG Monitoring and Reporting Formats

1

An Audit Report evaluates if the different aspects of the project are in accordance with the ESG Framework, or any other gaps / issues which need to be managed through the life of the project. The major elements covered as part of Audit Report are:

Key gaps identified

Rating provided (as per  
Tool 3)

Mitigation actions or  
recommendations

Responsibility (of  
investee or Associated  
Party or contractor)

Deadline for completion  
and implementation of the  
corrective actions

Budget or cost for  
corrective actions

2

A report for potential opportunities enlists the scope of opportunities for improvement in terms of the investee Company's ESG performance . The major elements covered as part of report for potential opportunities are:

Potential opportunities

Measures recommended

Review period

Timeframe for  
implementation

Support required from FI

Financial implication

ESG Impact



ESG Monitoring and  
Reporting formats

ESG Monitoring &  
Reporting Format



# Development of GIZ - SIDBI MSME ESG Framework

## Procedures to be followed using the ESG Toolkit

New investment opportunity

Check whether the business activity falls under the exclusion list

Yes

Do not proceed

No

Tool 1

Proceed to risk categorization of the company as per ESG parameters

High Risk (Category A)

Moderate risk (Category B)

Low risk (Category C)

Tool 2 (Checklists for category A, B and C)

Proceed to due diligence of the company

Compliant

Quarterly monitoring for high risk projects

Half yearly monitoring for moderate risk projects

Annual monitoring for low risk projects

Tool 3 and 4  
(For scoring and reporting the performance of the company)

Non Compliant

Do not proceed