

FINANCIAL INCLUSION AND ENTREPRENEURSHIP SCALING PROJECT

Ministry of Finance, Economic Planning and Development



Reserve Bank of Malawi

**ENVIRONMENTAL AND SOCIAL POLICY AND PROCEDURES FOR
FINANCIAL INCLUSION AND ENTREPRENEURSHIP SCALING PROJECT**

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1. INTRODUCTION

The Project Development Objective (PDO) of the Financial Inclusion and Entrepreneurship Scaling Project (FINES) is to increase access to financial services, and entrepreneurship and skills support for Micro, Small and Medium Enterprises (MSME's)¹ access to financial services and entrepreneurship and skills support. The project shall also allow for the existence of a more suitable environment within which MSMEs can thrive.

Activities under this project will be structured under four mutually reinforcing components, namely: 1) Increasing financing to MSMEs; 2) Scaling Entrepreneurship and Building Firm Capabilities; 3) Enhancing the Enabling Environment for Supporting Financial Inclusion of Entrepreneurs; and 4) Project Implementation Support.

A Project Implementation Unit (PIU) will be established at the RBM to manage the project. Under the first component of the project, the RBM will implement the Line of Credit (LOC) and a private entity will manage the partial credit guarantee (PCG) through a subsidiary agreement with the RBM (although details of the PCG are not yet finalized and that it will only be completed during project implementation if it will be considered feasible and in line with the PDO). The PCG will aim at lowering credit risk by absorbing a portion of the lender's losses on the loans made to MSMEs in the case of default. MoITT will be the implementing agency for component two and will manage contract and technical implementation. RBM will be implementing agency for components 3 and 4.

RBM recognizes that sustainable development is now widely accepted and adopted as the preferred development model and that the financial sector has an important role to play by promoting green financing by ensuring that financing resources are invested in a way that supports preservation of clean environment and Earth's natural resources, as well as ensuring that such financing does no harm to workers and communities and that they are treated fairly and equitably. It is thus imperative that both the RBM and the PFIs put in place robust environmental and social risk management systems to not only avoid direct financial losses but to also protect the integrity and reputation of the RBM and the PFIs.

Currently the RBM's focus and experience is on managing financial risks² and the E&S Policy and Procedures strengthen management of risks that are environmental and social in nature. It is therefore important that the project provides capacity building of RBM staff working on this project and where applicable, the PFIs to systematically identify and manage the risks that will arise from the implementation of the project.

The World Bank Environmental and Social Standards (ESS) provide a benchmark for measuring to what extent project outcomes are a result of an integration of environmental and social risk management procedures in the project cycle.

¹ MSMEs are enterprises with 100 employees or less: enterprises with 1 to 4 employees are defined as micro while those with 5-20 employees and 21 to 100 employees are defined as small and medium enterprises, respectively

² Through the RBM's Risk Management Guidelines for Banking Institutions (2007)

2. PURPOSE AND COMPONENTS OF RBM ENVIRONMENTAL AND SOCIAL POLICY AND PROCEDURES

The RBM Environmental and Social Policy and Procedures provides a framework for the implementation of appropriate Environmental and Social Risk Management (ESRM) procedures with the aim to identify, avoid and reduce E&S risks and impacts for itself and the financial institutions to which it is going to on-lend under this project. It is in this context that RBM is committed to developing and operationalizing its own E&S Policy and Procedures and promoting the development, operationalization ESMS for the financial institutions in order to assess the nature, extent and the magnitude of the E&S risks and impacts associated with such lending activities and devise mitigation measures for the identified risks and negative impacts.

The Core components of the RBM E&S Policy and Procedures for FINES are:

- a) The Environmental and Social Risk Management (ESRM) Policy which is aligned to Malawi laws and regulations and the World Bank Environmental and Social Standards (ESS) requirements;
- b) ESRM procedures for screening, identification, assessment, mitigation, monitoring and reporting of E&S risks; these procedures include record keeping, disclosure, and reporting to internal and external stakeholders on implementation;
- c) An outline of roles and responsibilities of the structures charged with the implementation and managing and monitoring E&S risks;
- d) Reporting
- e) Budget and training.

3. ENVIRONMENTAL AND SOCIAL RISK MANAGEMENT POLICY

The RBM's Environmental and Social Risk Management (ESRM) Policy provides guidance on the approach for the integration of environmental and social issues in the assessment of eligibility of PFIs to access credit under the FINES Project. The policy seeks to introduce a systematic approach to the identification, rating and management of social and environmental issues relevant to all on-lending by RBM to PFIs under the FINES project. The policy further ensures that all the implementing institutions are equipped with adequate skills and resources needed to effectively implement this Policy.

3.1 Policy Approach

This policy is a demonstration of RBM's commitment to integrate environmental and social considerations in the PFI activities to be funded under this project to minimize, avoid or eliminate the potential negative impacts arising from such activities. In addition, the policy encourages MSMEs to put in place measures that enhance the positive impacts of the projects. The project will thus fund activities with positive environmental and social outcomes through lines of credit to eligible PFIs for on lending to MSMEs. The project will in addition provide partial credit guarantee fund through a private entity to encourage MSMEs to invest in businesses and to participate in value chains. The PCG fund will be developed by the on-going Malawi Agricultural Commercialization Project (AGCOM) to facilitate access to financial services for the project-supported producer organizations.

The RBM recognises that in the course of implementing the project, it will be exposed to environmental and social risks through the PFIs - to the E&S risks associated with the business activities of the sub-

borrowers and sub-projects they finance. It is envisaged due to the small-scale nature of the MSMEs involved and the modest levels of funds being made available to each, the risks and impacts will largely be of low magnitude, not extensive and reversible. However, the potential for sub-projects to develop high or substantial level risks and impacts remains and RBM's ESRM will seek to mitigate any impacts to acceptable levels. It is however noted that management of E&S risks is behavioural in nature and as such, the MSMEs that embrace E&S risk management are likely to continue to do so as they graduate into large scale enterprises. The policy calls upon the MSMEs to integrate E&S management in their core business strategies. In addition, it is globally recognised that the initial cost of integrating sustainability into the core business strategy, and reporting on it, can (at least in the long term) be more than offset by cost savings, reduced risk, positive brand association, and the ability to meet consumer, investor, and supplier demand for environmentally conscientious products and services.

The policy supports the capacity development of PFIs to develop and maintain adequate system procedures and a capacity for identifying, managing and monitoring risks and impacts of sub-borrowers and sub-projects commensurate with the amount of funds on-lent, the size of the MSME and the nature of the activities to be implemented. This will be achieved primarily by through development, by each PFI, of an Environmental and Social Management System (ESMS), as defined in this Policy.

3.2 Policy Objectives

The main objectives of the policy are to:

- a) Integrate ESRM policy considerations into the RBM on-lending and partial credit guarantee decision making processes;
- b) Set out requirements for the PFI for environmental and social screening associated with the activities implemented with funding they on-lend to MSMEs;
- c) Ensure compliance with national regulation pertaining to E&S governance and the applicable World Bank environmental and social standards (ESS);
- d) Promote greater transparency and accountability on E&S issues among all RBM stakeholders through disclosure and reporting; and
- e) Ensure that the RBM ESRM policy considerations are ingrained in the PFI's core business strategies and thus increase the likelihood that these lending practices will be sustained beyond the life span of the project.

4. SCOPE OF APPLICATION

The requirements of this Policy apply to the LoC and PCG facility established by RBM, to PFIs (in the MSME financing sector) and the ultimate borrowers, the MSMEs.

4.1 Applicable Environmental and Social Requirements

Under FINES, RBM will only finance business activities that are expected to meet applicable E&S Requirements within a reasonable period of time. Persistent delays and gaps in meeting these requirements shall lead to loss of financial support from RBM.

4.2. Requirements for Participating Financial Institutions

As a condition of eligibility to receive financing from RBM, the PFI will put in place and maintain an Environmental and Social Management System (ESMS) to identify, assess, manage, and monitor E&S risks

and impacts associated with business activities they finance under FINES, as commensurate with the nature and magnitude of such risks and impacts.³ Where the PFI can demonstrate that it already has an ESMS at the time of RBM's due diligence, it will provide adequate documented evidence to that effect.⁴

The PFI's ESMS should include the following elements: (i) environmental and social policy, (ii) clearly defined E&S risk identification, assessment, and management procedures, (iii) organizational capacity and competency, (iv) monitoring and review of E&S risks of individual transactions and the portfolio, (v) reporting mechanism of the E&S risks, (vi) external communications mechanism, (vii) grievance handling mechanism.

As part of the above elements, the PFI's ESMS must include:

- (i) An E&S risk categorization system with clearly defined risk categories⁵
- (ii) As part of the PFI's E&S policy, PFIs will state the applicable E&S Requirements as follows:
 - All sub-borrowers and sub-projects follow relevant E&S national and local laws and regulations (overview provided in Annex 1).
 - No financing will be provided to activities on the List of Excluded Activities⁶ (Annex 2).
- (iii) Appropriate E&S screening process, taking into consideration provisions of section 5 of this Policy, to ensure that sub-borrowers and sub-projects financed are environmentally and socially sound.
- (iv) That all sub-projects which involve resettlement (unless the risks of such resettlement are minor) or significant risks or impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural heritage will apply relevant requirements of World Bank ESSs.

RBM will require PFI's maintain labour management procedures in line with national laws and WB Performance Standard 2 on Labour and Working Conditions.⁷

³ The PFI's ESMS will be tailored and scaled to the nature of their lending activities (size of the transactions, sectors of operation, size of the micro-enterprises supported etc.) and be commensurate with the magnitude of anticipated risks and impacts of their portfolio, which are generally low/moderate for MSMEs at the individual transaction level.

⁴ Where RBM is providing support to a PFI, RBM may use an ESMS already established by the PFI, provided that such requirements will enable the PFI to achieve objectives materially consistent with this Policy. A PFI may be required to enhance or supplement its ESMS, as deemed necessary by RBM.

⁵ A typical categorization system used by PFIs may consist of three risk categories, which correspond to high, medium, or low risk. It should, therefore, be noted that the main purpose of a categorization system is to help PFIs prioritize their due diligence and supervision activities with a focus on higher risk and larger transactions (as compared to other transactions of the PFI) within a PFI's portfolio. In case of a microfinance institution, the categorization system is designed to be relative to the nature of the transactions in the portfolio. Such categorization system can include internal thresholds that help classify transactions based on such parameters as amount of loan, tenor of loan, size of enterprise/ borrower and sectors of operation etc.

⁶ List of Excluded Activities may be amended from time to time.

⁷ RBM will analyse and leverage the synergies that may exist between World Bank Performance Standard 2 and relevant national labour laws and regulations.

The PFI will prepare and submit to the RBM an Annual E&S Report on the implementation of its ESMS that will include information on E&S risk profile of its portfolio financed through FINES. The PFI will promptly notify RBM of any significant accidents or incidents associated with sub-borrowers and sub-projects to be financed which may have any material impact on the compliance of the applicable Environmental and Social Requirements.

5. ENVIRONMENTAL AND SOCIAL CATEGORIZATION

5.1 E&S Risk Rating for Participating Financial Institutions

Each PFI considered for RBM investments for the purpose of financing FINES-eligible business activities will be assigned an E&S risk rating by RBM according to the PFIs' risk profile that can change over time.

E&S risk rating assigned to each PFI will be based on the outcomes of the E&S screening and due diligence of the PFIs, including portfolio of proposed business activities to be financed by FINES funds and PFI's E&S competency and capacity (see Annex 3). PFIs' risk rating will determine the level of RBM E&S due diligence and supervision. The risk ratings are as follows:

- **RR-1 (High Risk):** When a PFI's proposed portfolio includes, or is expected to include, substantial financial exposure to business activities with potential significant adverse E&S risks or impacts.
- **RR-2 (Moderate Risk):** When a PFI's proposed portfolio is comprised of, or is expected to be comprised of, business activities that have potential limited adverse E&S risks or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures.
- **RR-3 (Low Risk):** When a PFI's proposed portfolio includes financial exposure to business activities that predominantly have minimal or no adverse E&S impacts.

RBM recognizes that the investment activities it considers for financing through PFIs have different levels of information available at the time of RBM's PFI-level due diligence. For FINES, the use of proceeds from RBM's investment and the associated E&S risks and impacts are largely understood across the eligible sectors, even though they are often not directed at specific assets or projects in the case of working capital finance.

Therefore, given that funds provided to PFIs through FINES are fully traceable and intended for a specified end use, RBM will determine the E&S risk rating of its PFI investment in relation to risks associated with the specified end use of FINES funds. RBM will consider size, and type of investments as well as the sectoral exposure of investments in the PFI's relevant portfolio.

As a result of RBM's regular supervision of PFIs with regard to their E&S performance as described in section 6.2, RBM may change a PFI's risk rating based on the outcomes of PFI's portfolio risks profile and E&S capacity assessment. Such re-assessment may take place on an annual basis or in connection with the PFI's new request for FINES funds, whichever is sooner.

6. ENVIRONMENTAL AND SOCIAL DUE DILIGENCE

Environmental and social due diligence applies to all RBM FINES investment activities. E&S due diligence is integrated into RBM's overall due diligence of the investment under consideration, including the review of financial and reputational risks. RBM weighs the costs and benefits of proposed business activities and

articulates its rationale and specific conditions for the proposed activity. These are provided to appropriate RBM Approval Teams when the investment is presented for approval.

Legal agreements pertaining to the financing of business activities between RBM and PFIs for financing under FINES, shall incorporate specific E&S provisions. These include complying with the applicable E&S requirements as detailed in section 4 of this Policy and Procedures and specific conditions included in Corrective Action Plans⁸ if applicable, as well as relevant provisions for E&S reporting, as appropriate. If the MSMEs financed through PFIs fail to comply with their E&S commitments as expressed in the legal agreements and associated documents, PFIs will work with them to bring them into compliance. If they fail to establish compliance, PFIs will exercise their rights and remedies, as appropriate.

6.1 Participating Financial Institutions

In order to appropriately identify the E&S risks associated with providing support to PFIs during the appraisal process, RBM will review the existing and proposed business activities of the PFIs to identify risk and impacts associated with sub-borrowers and sub-projects. Based on this assessment, RBM defines requirements and standards the PFIs will apply to manage these risks. RBM will also review the capacity of the PFIs to manage E&S risks and impacts.

During the PFI assessment, RBM will take into consideration (a) the types of products and services provided by the PFI with RBM's support; (b) size of financing; (c) the nature of the PFIs portfolio, including sectors and locations; (d) adequacy of PFI's ESMS including organizational capacity to identify, assess and manage environmental and social risks and impacts of its RBM-supported portfolio; (f) any contextual risks, to the extent possible.

Where necessary, RBM will require the PFIs to strengthen their ESMS as well as organizational capacity, responsibilities, and accountability for implementing the ESMS to be commensurate with RBM's assessment of the PFI's E&S risk profile.

6.2 SUPERVISION

RBM will develop and maintain a regular program and procedures for supervision of its PFI investments, based on a clearly defined set of E&S performance criteria included in RBM's E&S Procedures for investments through PFIs. RBM will periodically review adequacy and implementation effectiveness of the PFIs' ESMS, including the processes and the results of the E&S due diligence conducted by the PFIs on its MSME sub-borrowers, PFIs organizational competency and capacity, on-going and consistent compliance with Applicable E&S Requirements, E&S records maintenance and availability of supporting documentation etc. In addition, RBM will periodically review a sample of PFIs' MSME sub-borrowers, especially for business activities with significant E&S risks.

⁸ A Corrective Action Plan is a short / itemized list of key risk mitigation measures that a client/ lessee will need to undertake within a reasonable period of time to comply with the E&S requirements. A Corrective Action Plan is based on the outcomes of E&S screening (and further E&S due diligence, if required). Corrective Action Plans range from a simple list of mitigation measures (for lower risk transactions) to the potential legal requirement to prepare Environmental and Social Assessments (ESIAs) and follow detailed E&S Management Plans (ESMPs) with actions that can be measured quantitatively or qualitatively (for high risk transactions).

7. DISCLOSURE

This E&S Policy shall be endorsed and approved by RBM Senior Management. The approved E&S Policy and Procedures for FINES will be publicly disclosed on RBM's website.

PFI's are required to disclose the following key elements of their ESMS:

- The PFI's policy statement which describes specific objectives, implementation matrix, and aspirations that the PFI has set with regard to its environmental and social performance;
- The PFI's procedures for screening and assessing risks and impacts of sub-projects or individual transactions.

MSME sub-borrowers will be required by PFI's, as appropriate, to disclose full or partial ESIA's, if applicable, and any corresponding risk management instruments prepared for investments categorized as High Risk.⁹ Such disclosure will be done as part of the overall process of stakeholder engagement in a manner consistent with the World Bank Environmental and Social Framework and the Environmental and Social Standards, as applicable.

In addition, in case of an investment categorized as High Risk in accordance with this E&S Policy and requires a full ESIA, RBM will disclose a summary of the ESIA on its website.

8. ACCOUNTABILITY AND GRIEVANCE MECHANISM

RBM recognizes the importance of accountability and that stakeholder concerns should be addressed in a manner that is fair, objective, and constructive. The purpose of a grievance mechanism is to establish a way for affected individuals, groups or communities to communicate their enquiries, concerns or formal complaints. The grievance mechanism will address affected persons' concerns and complaints promptly, using an understandable and transparent process that is gender responsive, culturally appropriate, and readily accessible to all segments of the affected parties. The GM should not impede access to the already established judicial and administrative remedies. In addition, it should be made known to the project-affected parties that they may submit complaints regarding the project to the World Bank Corporate Grievance Redress Service (GRS).

8.1 RBM Grievance Mechanism

The Financial Services Act 2010, in Part VIII, establishes the Financial Services Appeals Committee (FSAC) with the mandate to review regulatory decisions of the Registrar of the financial institutions and hear appeals from financial institutions. The Act provides for the Committee to consist of three members, one of whom shall be designated as Chairperson and others as ordinary members. The members are appointed by the Minister of Finance. The Rules prescribe the procedure for the conduct of proceedings brought before the FSAC. Under the Rules, a person affected by the decision of the Registrar may appeal against the decision by filling a Notice of Appeal with the Secretary within 21 days of date of the decision.¹⁰

⁹ For *High Risk* direct investments by RBM, this disclosure will be done in accordance with the relevant laws and regulations of Malawi and relevant requirements of the World Bank Performance Standards. For all other investments, this disclosure will be done in accordance with the relevant laws and regulations of Malawi.

¹⁰ See Financial Services (Financial Services Appeal Committee Procedures (Rules)

The notice of appeal must among other information contain a copy of disputed decisions, grounds for appeal relief sought by the applicant, grounds and urgency of the appeal. At the conclusion of the appeal FSAC delivers its decision in writing to the parties. A copy of the decision and the reasons for the decision are published on the FSAC website.

The right to appeal the decision of the Registrar is well known by the Banks and Financial Institutions and the PFIs will be reminded of this remedy during stakeholder engagement meetings.

8.2 Grievance Mechanisms of PFIs

The Registrar in 2016 issued a directive to all financial institutions on the requirement of an internal complaint handling system by all the financial institutions to assist in resolving complaints by customers of financial institutions in relation to financial services and products. It is in this context that the Registrar of Financial Institutions issued a Complaints Handling Directive. The Objectives of Complaints Handling Directive are to:

- (a) Ensure that a financial institution has in place avenues for resolving complaints lodged by financial consumers;
- (b) Promote transparency in the process of handling financial consumer complaints to improve service delivery; and
- (c) Ensure that financial institutions timely report data on complaint to the Registrar.

The Registrar outlined procedures for complaints handling as follows:

1. A consumer reports complaint to financial service providers (FSPs) through designated officers and once received, officers must record complaints and strive to timely resolve the complaint;
2. Provide feedback on complainants;
3. Complaints handling should be guided by internal process approved by the Board and reviewed by the Registrar;
 - Complaint resolution rule - 0/10/30 rule - should apply where simple complaints be dealt with immediately; complaints that require investigation should be dealt within 10 working days and complex complaints be resolved within 30 days;
 - Longer periods should be approved by management and specifically flagged in complaints register;
 - Response should be in line with how the complaint was lodged;
 - Institutions must inform complainants about the right to appeal to an internal appeals committee, if available, the Registrar of Financial Institution and contacts, or to a civil court - file a lawsuit.

The FIs are under the directive obliged to submit complaints reports to Registrar on quarterly basis highlighting the number of complaints received, nature of complaints and the resolutions.

All the FIs consulted indicated that they have internal grievance redress mechanism although not all reported to be submitting report to the Registrar on quarterly basis as required. Some reported to submit reports to the Registrar upon request. Most grievances received by FIs and the Reserve Bank relate to financial services such as poor customer care services, technology failure, lack of transparency and full disclosure of all financial risks as well as reward of their products, unfair contract terms and

misrepresentation of financial services and deceptive advertising. However, the potential grievances of much interest to this project are those related to the negative environmental and social impacts arising from the implementation of the subprojects. There are various acts of parliament and regulations that provide remedies to grievances related to land disputes as well as negative environmental and social impacts.

The EMA 2017, created a Tribunal to address issues of environmental and social impacts to the extent that “any person who has reason to believe that his right to a clean or healthy environment has been violated by any person may, file a written complaint to the Tribunal outlining the nature of his complaint and particulars. The Tribunal shall, within thirty (30) days from the date of the filing of the complaint, institute an investigation into the activity or matter complained about and shall give a written response to the complainant indicating what action the Tribunal has taken or shall take to restore the claimant's right to a clean and healthy environment, including instructing the Authority to take such legal action on the matter as the Authority may deem appropriate”. Similarly, the Customary Land Act has put in place alternative land dispute settlement mechanism. It has created customary land committees (CLCs) at group village headman (GVH) level to manage land within a Traditional Land management Area (TLMA). Land dispute resolution under the Act are through Land Tribunals. These are Customary Land Tribunals at Traditional Authority and district level. At the Central the Act established the Central Land Board to be presided over by a Resident Magistrate. If the complainant is not satisfied with a decision of a land tribunal, he or she can appeal to the next level or the high court. The grievance mechanisms outlined above are not directly linked and it is the duty of the relevant GRC to ensure that project affected persons are given the option of using the grievance redress mechanisms that are led by local authorities where project led negotiations have not been able to provide a satisfactory solution to the complaint. The project is duty bound to forward to the relevant local authority the complaints they receive that are, in their view, can be better resolved by the local government led dispute resolution systems.

The PFIs will be duty bound to use in-house intelligence mechanisms and routine supervisory visits to register grievances affecting the disadvantage and vulnerable groups.

9. SECTOR-SPECIFIC GUIDELINES

As part of its E&S management system for FINES, if necessary RBM may develop sector-specific guidelines which would be applicable to lending activities within the specific sectors eligible for FINES financing.

10. INSTITUTIONAL ARRANGEMENTS AND ROLES AND RESPONSIBILITIES

This section describes the roles and responsibilities of PIU staff in charge of implementing and maintaining oversight of the various parts of the E&S Policy and Procedures. Key departments/individuals with accountability for implementation are listed below:

Responsible Entity	Roles and Responsibilities
Project Steering Committee	<ul style="list-style-type: none"> a) Provide overall policy guidance on E&S risk management; b) Provide oversight to PIU on E&S risk issues; c) Receive and review quarterly and annual E&S risk management reports and provide guidance on the on the way

Technical Committee	a) Provide technical oversight on issues of E&S risk management
RBM Senior Management	<ul style="list-style-type: none"> a) Review and approval of E&S Policy and Procedures; b) Allocation and approval of the PIU budget including resources for E&S implementations; c) Provide Management oversight of the PIU and specifically for E&S risk management; and d) Mutual accountability to and from external stakeholders including the World Bank, Malawi Government, Partial Credit Guarantee facility and PFIs.
RBM Human Resources Department	<ul style="list-style-type: none"> a) Support the PIU in organizing orientations and training for staff with E&S risk management responsibilities at RBM and within PFIs b) Ensure that E&S risk management roles and responsibilities are added to job descriptions for relevant staff.
RBM Internal Audit Department	<ul style="list-style-type: none"> a) Periodic Independent review and verification of internal compliance with RBM E&S Policy and Procedures b) Preparing and monitoring time-bound plans for improvement
PIU	<ul style="list-style-type: none"> a) Documenting initial E&S screening, as per the E&S Procedures; b) Requesting, obtaining, and conducting initial analysis E&S reporting from PFIs; c) Provide secretarial services to PSC on issues of E&S risk management; d) Responsibility for E&S risk management component of the Project; e) Day-to-day management and oversight of E&S risk management, in line with ESRM Policies and Procedures, including E&S screening, review and appraisal, and supervision; f) Developing and improving tools to support implementation of E&S risk management measures such as checklists and TORs for Consultants; g) Development of training materials for PIU and PFI staff h) Development and implementation of Capacity Building and Training Plan for RBM, PFI staff; i) Liaising with PFIs on compliance with E&S requirements j) Liaising with the RBM on E&S risk management issues; k) Ensuring quality, completeness, and timeliness of capturing information in the E&S Performance System (ESPS); l) Reporting to RBM Senior Management and preparation of reports on behalf of RBM for external stakeholders (Government of Malawi and the World Bank); m) Preparing revisions to the RBM ESRM Policy and Procedures, and presenting them for approval by Senior Management; n) Undertake targeted visits to subprojects and report findings to the PSC Monitoring progress of the E&S Action Plan, as included in the legal agreement with PFIs; o) Maintaining records in the E&S Performance System (ESPS), as per E&S Procedures; and p) Monitoring potential E&S issues associated with the PFIs, such as incidents and accidents. q) Ensuring that E&S covenants are included in credit agreements with PFIs

Partial Credit Guarantee entity	a) Incorporate the RBM E&S Policy and Procedures in its own processes and procedures
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11. BUDGET AND TRAINING

The project budget will be activity based and RBM has experience using this approach from its experience in the implementation of FSTAP. The project budget cycle will follow that of RBM running from January to December. The budget will also be incorporated in the accounting software and used to monitor and control project expenditure. The E&S risk management budget will be managed by the PIU. The project will allocate adequate resources for the implementation of the E&S Policy and Procedures for FINES and capacity building for the PIU and PFIS on E&S Policy and Procedures procedures including dedicating staff time to perform E&S responsibilities to ensure effective implementation across RBM and effective ESMS implementation by the PFIs. Items to be budgeted for include:

- a) Development and maintenance of E&S Policies and Procedures - policy, procedures and tools;
- b) Training of PIU and PFI Staff;
- c) E&S risks orientations for MSMEs;
- d) Targeted E&S risks management field visits by PIU staff; and
- e) E&S risk management orientation of Steering and Technical Committees and other relevant implementing partners.

The E&S Risk Coordinator will be responsible for:

- a) Undertake E&S capacity development needs assessment internally and for implementing partners including PFIs;
- b) Based on the outcome of the capacity development assessment, develop and implement and training planning; and
- c) Continuously assess the E&S risk management performance of PFIs through regular monitoring and supervision and reporting;

The Capacity Building and Training Plan for E&S risk management, including budget, will be reviewed and approved by RBM Senior Management.

12. AMENDMENT

This Policy shall be amended by RBM's own initiative and based on feedback obtained from PFIs, lenders/investors, MSMEs and other stakeholders and concerned government organs as deemed necessary. The amendment of the ESMS should not lower the minimum provisions stated in it.

ANNEX 1. RELEVANT LEGAL FRAMEWORK

The Malawi National Land Policy (2002)

The Malawi National Land Policy is relevant to the project in so far as it provides the policy framework for land administration in Malawi. The subproject with a spatial dimension will be subject to controls as stipulated in the Land Policy and provided for in the relevant Statutes.

National Environmental Policy (NEP) - 2004

The Policy is meant to promote sustainable socio-economic development through sound management of the environment in the country. The Policy provides the objectives, the guiding principles and strategies for addressing environmental concerns in human settlements planning and design.

The National Industry Policy (2014)

The policy vision is the creation of a competitive, structurally transformed industrial sector, generating livelihoods that are environmentally and socially sustainable. The sector will be inclusive of MSMEs and contribute to reducing the trade deficit. The Policy goal is an altered GDP growth path resulting from ensuring the industrialization and structural transformation of the Malawian economy by coordinated policy efforts to address key constraints and increase the productive capacity of industry. The policy focuses on manufacturing. The policy specifically calls upon stakeholders to address the environmental and social sustainability of industrialization.

The National HIV/AIDS Workplace Policy (2010)

The policy is instrumental in helping to prevent the spread of the pandemic, mitigate its impact on workers and their families and provide social protection to help cope with the disease. The policy covers key principles, such as the recognition of HIV and AIDS as a workplace issue, non-discrimination in employment, gender equality, screening and confidentiality, social dialogue, prevention and care and support, as the basis for addressing the pandemic in the workplace. The Policy applies to the public and private sectors, NGOs, including employers and managers, jobseekers and job applicants, apprentices, casual workers, volunteers, part- and full-time employees and to all types of employment contract. It applies to the workplace in the broad sense with specific provisions concerning the informal sector. All employers and employees and their respective organizations are encouraged to use this policy to develop, implement and refine their HIV and AIDS policies and programmes to suit the needs of their workplace.

National Gender Policy (2011)

Overall Policy goal is to mainstream gender in the national development process in order to enhance participation of women and men, girls and boys for attainment of sustainable and equitable development. One of the objectives of the policy is to reduce poverty among women through economic empowerment. It is thus important that beneficiaries of this project create a favourable and safe environment for both men and women at the workplace and exercise a zero-tolerance policy on sexual harassment.

The Malawi Growth and Development Strategy III (MGDS III) – 2017 – 2022

The third Malawi Growth and Development Strategy (MGDS III) is the medium-term strategy for Malawi designed to contribute to Malawi's long-term development aspirations. The strategy covers a period of five years, from 2017 to 2022 and it is a successor to the MGDS II that was implemented between 2011

and 2016. The overall objective of the strategy is to move Malawi to a productive, competitive and resilient nation through sustainable economic growth, energy, industrial and infrastructure development while addressing water, climate change and environmental management and population challenges.

The Constitution of the Republic of Malawi (1995)

Section 13d of the Constitution of the Republic of Malawi (1995) stipulates mechanisms for management of the environment for the benefit of the current and future generations. The Constitution further provides for the integration of international environmental legislation into Malawi's own legal system. The Section places on the State the responsibility to actively promote the welfare and development of the people of Malawi by progressively adopting and implementing policies and legislation aimed at achieving the following goals:

- Prevent the degradation of the environment
- Provide a healthy living and working environment for the people of Malawi
- Accord full recognition to the rights of future generations by means of environmental protection and the sustainable development of natural resources
- Conserve and enhance the biodiversity of Malawi.

It prohibits arbitrarily deprivation of property and stipulates that expropriation of property shall be permissible only when done for public utility and only when there has been adequate notification and appropriate compensation provided and there shall always be a right to appeal to a court of law.

Statutory provisions

The Environment Management Act, 2017

The Environment Management Act provides the legal basis for the protection and management of the environment and the conservation and sustainable utilization of the natural resources. The Act outlines the ESIA processes to be followed and requires that all project developers in both the public and private sectors comply with the process. The *"Prescribed List for which ESIA is Mandatory"* that is gazetted under the Act, sets out which activities must have an ESIA before they can be implemented. If a developer is proposing a "prescribed project", ESIA applies, and the developer needs to submit a project brief. Furthermore, projects that have the potential to affect national parks, water resources, cemeteries and historical sites (among other screening criteria) also require ESIA. The Act further requires that no licensing authority issues any license for a project for which an ESIA is required unless the Director of Environmental Affairs (DEA) has given consent to proceed due to completion and approval of a satisfactory ESIA report or due to non-requirement of an ESIA. Prescribed activities for which ESIA is mandatory are outlined in the Guidelines for ESIA. The act provides for public participation and enforcement of duties created under the Act. In order to promote the right of every person, the Act provides for (a) access to environmental information and lead agencies, private sector and non-governmental organizations are duty bound to provide such information in a timely manner; (b) public participation in environmental decision-making processes directly or through representative bodies and mechanisms for effective, direct and indirect public participation shall be created by lead agencies; and (c) the public to be afforded an adequate and effective administrative or judicial remedy for any harmful or adverse effects resulting from acts or omissions affecting the environment. The Authority is mandated to establish guidelines and, where

necessary, recommend promulgation of regulations for ensuring the realization and implementation of the provisions noted above

The Physical Planning Act (2016)

The Physical Planning Act (2016) and several associated legal texts, form the basis for guiding physical development planning and development control in Malawi. The Act contains provisions for most of the basic environmental concerns under this project. Section 50 (1) of Act provides for matters planning authorities should consider in granting planning permission. The considerations most relevant to this project are in connection with noise and air, water and groundwater pollution. The beneficiaries of this project will, where applicable, be required to take the necessary steps to comply with this legislation.

Water Resources Act (2013)

One of the objectives of the Act is the control of pollution and the promotion the safe storage, treatment, discharge and disposal of waste and effluents which may pollute water or otherwise harm the environment and human health. In this regard, the screening of subprojects, where, applicable will endeavour to identify the activities with potential to pollute surface and ground water resources and will implement appropriate measures to reduce or eliminate those adverse impacts.

Local Government Act (1998)

The Act mandates local governments to regulate planning and development within their area of jurisdiction and empowers them to have by-laws that specify how specific development projects should minimize or avoid environmental degradation. The subprojects supported under this project will have to comply with the applicable by-laws.

Public Health Act (1996)

The Act requires the developer to provide adequate sanitary and health facilities to avoid harmful effects of waste.

Safety, Health and Welfare at work Act (2005)

The Act regulates the requirement for adequate environmental health and safety measures within industrial estates. Under the Act, no person shall occupy or use a workplace unless he is a holder of (a) a registration certificate issued in respect of such premises (b) a current provisional registration permit issues in respect of such workplace. Under the Act the employer's duties and responsibilities include

- Provision and maintenance of plant and systems of work that are safe and without risks to health;
- Arrangements for ensuring safety, absence of risks to health about the use, handling, storage and transportation of articles and substances; and
- Provision of information, instructions, training and supervision to ensure safety at work of his employees.

Land Act (2016)

The title to land in Malawi is recognized by the Land Act, 2016. The Act recognizes two categories of land, namely: public and private land. Public land is classified as either Government Land or unallocated

customary land while private land is identified as freehold, leasehold or customary estate. The provisions under private land that are most relevant to this project are:

- The right of the Government to collect rent; and
- Power of re-entry by the Minister where a lease is in breach or does not observe any of the covenants or conditions contained or implied in the lease

The beneficiaries of this project will be, where applicable, be required to comply with the provision of the Act.

Public Roads (Amendment) Act (Act 8 of 2017)

According to the Public Roads (Amendment) Act (Act 8 of 2017), the amount of compensation in respect of private land shall be based on the loss or damage suffered by the claimant arising from the damage or destruction of his interest in surface rights on such land valued at the valuation date. In case of customary estate, the Act stipulates that the occupier shall be entitled to reasonable compensation in respect of the disturbance and the amount of such compensation shall be based on the open market value on the loss suffered by the claimant arising from damage to or destruction of his interest in the land and surface rights on such land. The Act provides for compensation for other disturbances where the claimant must move his place of residence or business

Registered Land (Amendment) Act, 2017

The Act incorporates provisions to provide for title registration throughout the country for all Categories of land including customary estates. The Act also considers the move to decentralize land administration and management. Thus, all land shall be subjected to registration for purposes of determination of ownership. Registration districts have been decentralised and reliance is no longer placed on the Minister to declare registration districts. The Act stipulates that the consent of local lands committees be obtained in the dealings with customary land in place of the Local Land Boards.

Customary Land Act, 2016

The Customary Land Act, 2016 is the main act in customary land administration and management in Malawi. The Act establishes “customary estates”, which is customary land owned, held or occupied as private land within a traditional land management area and which is registered as private land under the Registered Land Act. As such, customary land is given equal value as any privately-owned land such as leasehold or freehold. In terms of operation, the Act creates customary land committees (CLCs) at group village headman (GVH level) to manage land within a Traditional Land management Area (TLMA). Land dispute resolution under the Act will be through Land Tribunals. These will be Customary Land Tribunal at traditional Authority level (to be chaired by the TA for TLMA), District Land Tribunal (to be chaired by the District Commissioner) and Central Land Board (to be presided a Resident Magistrate). If the complainant is not satisfied with a decision of a land tribunal, he or she can appeal to the next level or the high court.

The Reserve Bank of Malawi Act, 1989

The Reserve Bank of Malawi Act (the Act) Chapter 44:02 of the Laws of Malawi was enacted in 1989 with the purpose of establishing the Reserve Bank of Malawi (the Bank), regulating the issue of currency, providing for central banking powers and duties, including general powers for provision of supervision of banks and financial institutions, among others. However, since its enactment, the operations of central banks have evolved both regionally in the Southern Africa Development Community (SADC) region and internationally. At the time of compiling this report, the Act is being repealed and replaced with a new one for the Bank to operate in accordance with best practices obtaining internationally for a central bank and for the efficient and sound economic management of the country. The new law, basically, harmonizes all the piecemeal amendments made to the Act and also introduces new provisions aimed at incorporating best practices for the efficient discharge of the mandate of the Reserve Bank of Malawi and address the shortfalls currently in the Act, as well as enhance penalties for some offences.

Financial Services Act, 2010

The Reserve Bank of Malawi is appointed as the Registrar of Financial Institutions under this Act with regulatory and supervisory authority for the financial institutions. The Registrar shall perform his supervisory function with a view to achieving the:

- Safety and soundness of prudentially regulated financial institutions;
- Highest standards of conduct of business by financial institutions;
- Fairness, efficiency and orderliness of the financial sector;
- Stability of the financial system; and
- Reduction and deterrence of financial crime in financial institutions.

Guidelines

The Malawi Guidelines for Public Consultation during ESIA Preparation

The EIA process typically involves consultations with members of the public—individuals, community and business leaders, elected officials, and non-governmental organizations. These people are consulted because they are usually "stakeholders" in that, in several ways, they can have a "stake" in a project.

There are several methods for consulting the public, however, no one method is usually enough by itself: An effective public consultation programme typically incorporates two, three or more methods which complement each other in ensuring adequate input to the EIA process.

- **Press conferences, information notices & brochures/ fliers:** Typical methods used to disseminate public information about a project. The sole objective of these methods is to inform the public so, strictly speaking, they are not genuine consultation. They are one-way communication "with" no attempt made to solicit people's views about the project. Genuine public consultation goes beyond issuing information to using two-way communication methods which allow the public both to be informed and to express their views about a project.
- **Overviews, questionnaires and polls:** Useful for soliciting information about an environmental and socio-economic setting for use in an EIA. They assist in gathering the views of the public about the project proposal, its desirability, and how it might best fit into the local community.

- **Interviews:** Generally conducted individually with a selected group of people, hopefully representative of the range of "stakeholders" in a project. They tend to be unstructured Conversations' guided by some general questions, in which the interviewer seeks key information about a project and responses to it.
- **Questionnaires and polls:** The methods seek more specific information from a broader sample of people. They are not simple "instruments" to design and implement. The questions must be carefully crafted to avoid ambiguity and "leadings the respondent to a particular reply. Both "closed" and "open" questions can be asked, the first presenting a set range of replies for the respondent to choose from, and the second allowing the respondent to say anything. The two types are often used together to cover the same topic and provide the opportunity for unexpected answers.
- **Community meetings:** More structured gatherings where the developer, stakeholders and, perhaps, government representatives exchange information, views, concerns and suggestions.
- **Public hearing:** Formal meetings are usually held to consider the official of an EIA or of an entire project. They are structured proceedings, presided over by an administrative authority, in which testimony is given and examined, arguments for and against approval are heard, and a decision is made concerning approval or not.

Public consultations should be started as early as possible in the project cycle. This will ensure that information is given and received in a timely fashion to expedite the EIA and to dispel unfounded rumours and suspicions which may make project planning and implementation more difficult. The process should be continued at some level throughout the project cycle. A sustained programme will contribute to better project planning, to enhanced public confidence in a project, and to timely notice should difficulties with public acceptance of a project begin to develop. It should have its major elements timed to coincide with significant planning and decision-making activities in the project cycle. It is important to ensure that it reaches important stakeholders in the project area and both informs them about the project and gathers their views on the costs and benefits and how these can best be managed.

The objectives, methods and results of consulting the public during an EIA must be documented in the ESIA report. Lists of individuals, groups and organizations which were consulted should be included as an appendix to the study report

ANNEX 2. RBM FINES LIST OF EXCLUDED ACTIVITIES

RBM FINES will not provide financing to any projects involving the following activities.

1. Production or trade in any product or activity deemed illegal under Malawian laws or regulations or international conventions and agreements.
2. Production or trade in weapons or ammunitions.¹
3. Gambling, casinos and equivalent enterprises.¹
4. Production or trade in alcoholic beverages (excluding beer and wine).¹
5. Activities targeting tobacco manufacturing, processing, or specialist tobacco distribution, and activities facilitating the use of tobacco.¹
6. Trade in wildlife or wildlife products regulated under Convention on International Trade in Endangered Species (CITES).
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 RBM considers the radioactive source to be trivial and/or adequately shielded.
8. Production or trade in or use of unbounded asbestos fibres.
9. Any activities involving significant degradation or conversion of natural² and/or critical habitats³ and/or any activities in legally protected areas.
10. Activities damaging to national monuments and other cultural heritage.⁴
11. Unsustainable fishing practices such as drift net fishing in the marine environment using nets in excess of 2.5 km in length, electric shocks, or explosive materials.
12. Production or trade in wood or other forestry products other than from sustainably managed forests.⁵
13. Production or trade in pharmaceuticals, pesticides/herbicides, ozone depleting substances, polychlorinated biphenyls (PCBs) subject to international phase outs or bans.
14. Production or activities involving harmful or exploitative forms of forced labour⁶ or hazardous child work⁷.
15. Production, trade, storage, or transport of significant volumes of hazardous chemicals, or commercial scale usage of hazardous chemicals (gasoline, kerosene, other petroleum products, textile dyes etc.).
16. Production or activities that have adverse impacts, including relocation, on the lands, natural resources, or critical cultural heritage subject to traditional ownership or under customary use by historically underserved traditional local communities.
17. Activities involving land acquisition and/or restrictions on land use resulting in involuntary resettlement or economic displacement.⁸
18. Military or police equipment or infrastructures, and equipment or infrastructure which result in limiting people's individual rights and freedom (i.e. prisons, detention centres of any form) or in violation of human rights.
19. Activities involving live animals for experimental and scientific purposes.

Footnotes

1. This does not apply to enterprises that are not substantially involved in these activities. "Not substantially involved" means that the activity concerned is ancillary to an enterprise's primary operations.
2. Natural habitats are areas composed of viable assemblages of plant and/or animal species of largely native origin, and/or where human activity has not essentially modified an area's primary ecological functions and species composition.
3. Critical habitat is defined as areas with high biodiversity importance or value, including:(a) habitat of significant importance to Critically Endangered or Endangered species, as listed in the IUCN Red List of threatened species or

equivalent national approaches; (b) habitat of significant importance to endemic or restricted-range species; (c) habitat supporting globally or nationally significant concentrations of migratory or congregatory species; (d) highly threatened or unique ecosystems; (e) ecological functions or characteristics that are needed to maintain the viability of the biodiversity values described above in (a) to (d).

4. The term 'cultural heritage' encompasses tangible and intangible heritage, which may be recognized and valued at a local, regional, national or global level, as follows: Tangible cultural heritage, which includes movable or immovable objects, sites, structures, groups of structures, and natural features and landscapes that have archaeological, paleontological, historical, architectural, religious, aesthetic, or other cultural significance. Tangible cultural heritage may be located in urban or rural settings, and may be above or below land or under the water; Intangible cultural heritage, which includes practices, representations, expressions, knowledge, skills—as well as the instruments, objects, artifacts and cultural spaces associated therewith— that communities and groups recognize as part of their cultural heritage, as transmitted from generation to generation and constantly recreated by them in response to their environment, their interaction with nature and their history.

5. Sustainable forest management may be demonstrated by the application of industry-specific good practices and available technologies. In some cases, it may be demonstrated by certification/ verification or progress towards certification /verification under a credible standards system.

6. Forced labor, which consists of any work or service not voluntarily performed that is exacted from an individual under threat of force or penalty

7. Work considered hazardous for children is work that, by its nature or the circumstances in which it is carried out, is likely to jeopardize the health, safety, or morals of children.

8. Land acquisition and/or restrictions on land use may result in the physical displacement of people (involuntary resettlement) as well as their economic displacement (as loss of assets and/or means of livelihood, regardless of whether or not the affected people are physically displaced). Land must be acquired on willing-seller willing-buyer basis.

ANNEX 3: ENVIRONMENTAL AND SOCIAL RISK MANAGEMENT PROCEDURES FOR RBM INVESTMENTS

1. PURPOSE

These E&S Procedures set out RBM FINES arrangements and processes that aim to support the implementation of RBM Environmental and Social Risk Management Policy. These Procedures describe how RBM conducts its due diligence with regard to the finance components of the project to PFIs for on-lending of working capital finance to SMEs.

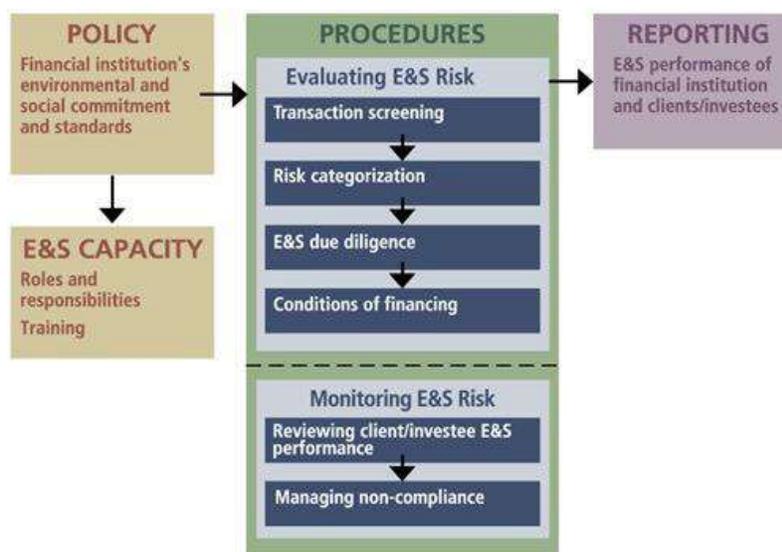
The core objective of these Procedures is to facilitate and promote proper implementation and institutionalization of the Environmental and Social management System (ESMS) at the level of participating Financial Institutions (PFIs). Such ESMS will articulate processes, roles, and activities for ensuring that have in place adequate systems and capacity for identification and mitigation of E&S risks involved in RBM’s finance under FINES (see Box 1). These Procedures are an integral part of RBM’s risk management framework, are embedded in the overall investment screening and appraisal process under FINES.

Box 1. What is an ESMS for a financial institution?

In general, Environmental and Social Management System for the financial sector is defined as is a systematic process to assess the environmental and social risks and impacts arising from their investees’ business activities, manage the financial institutions’ exposure to them, and improve operating efficiency and effectiveness. This system ensures that environmental and social risk management plays a role in all of the investment decision-making processes. It enables financial institutions to consider environmental and socioeconomic issues comprehensively, and by so doing, move beyond simply complying with regulations to taking advantage of increased sustainability of their operations.

An ESMS for financial institutions is normally anchored in the E&S policy and corresponding procedures, supplemented by the internal capacity to identify, manage, and monitor E&S risks in the activities financed. The effectiveness of the system is determined by the implementation performance factors such as consistent compliance with the E&S risk management requirements and maintenance of adequate documentation to that effect by the financial institution.

Figure 1. Core components of an ESMS for a financial institution



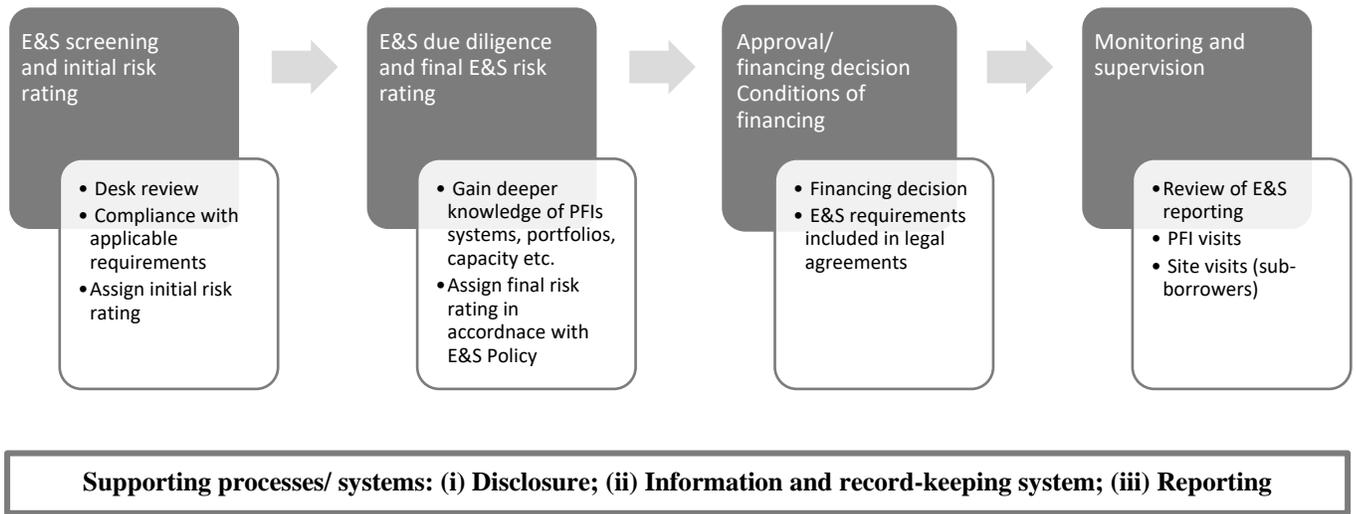
2. SCOPE OF APPLICATION

The implementation of these E&S Procedures will apply to all finance provided by RBM under FINES to PFIs.

3. STRUCTURE OF E&S PROCEDURES FOR RBM INVESTMENTS

The ESRM Procedures are comprised of four distinct components (Figure 1). Visual flow for transaction-level decision-making process is provided in Appendix 1.

Figure 1. Structure of E&S Procedures for RBM FINES Financing



4. E&S SCREENING AND DUE DILIGENCE

4.1. E&S Screening and Initial Risk Rating

This procedure outlines steps required for initial transaction screening for E&S risks when a new PFI is identified for a financing opportunity. RBM's Environmental and Social Development Specialist completes the following steps:

- Reviews the relevant information collected from the PFI (current portfolio, any existing E&S screening and due diligence processes and capacity etc.). The review will include assessment of the PFI's current portfolio and lending activities against the FINES List of Excluded Activities, the financing product types offered to the sub-borrowers, the expected portfolio to be supported, and the overall E&S systems and capacity (per criteria in Appendix 4), including PFI's commitment to comply with national and local laws and regulations and RBM's requirements.
- Completes PFI E&S Screening Questionnaire (Appendix 2).
- Participates in all relevant credit / investment review meetings at the early stages of decision-making and provides inputs and recommendations with regard to E&S issues.
- Assigns an initial E&S risk rating to the PFI taking into account the general provisions of the RBM E&S Policy and documents the summary of the initial risk screening and risk rating in the E&S Risk Rating Memorandum (Appendix 3). This memorandum may be adjusted following E&S due diligence procedure outlined in section 6 of the E&S Policy and Procedures.

Based on the results of E&S screening, a PFI will not be eligible for financing by RBM under FINES where (i) PFI has high exposure to activities on the List of Excluded Activities; (ii) PFI does not meet minimum eligibility criteria for its E&S systems and capacity¹¹, or (iii) E&S risks associated with a PFI's portfolio are deemed to be unacceptable to RBM.

4.2. E&S Due Diligence and Final Risk Rating

This procedure outlines steps required for PFI transactions found eligible following the initial E&S screening. E&S due diligence for PFIs is the responsibility of the Environmental and Social Risk Officer.

- Transactions identified as RR-3 (Low Risk) during E&S screening do not require additional E&S due diligence and are processed through the regular investment procedures following confirmation of the final PFI's E&S risk rating by Environmental and Social Development Specialist.
- Transactions identified as RR-1 (High Risk) or RR-2 (Moderate Risk) may require further E&S due diligence, commensurate with the risks and impacts identified during the screening stage, which may involve PFI engagement where appropriate and necessary to determine whether the PFI is committed to improving its Environmental and Social Management System (i.e. E&S management policies, procedures, capacity), as well as E&S performance in relevant business activities financed.

The Environmental and Social Development Specialist:

- Requests and reviews detailed PFI's existing and proposed portfolio information to determine the level and nature of E&S risks associated with the relevant activities financed by the PFI's.

¹¹ In accordance with the PFI eligibility criteria specified in the FINES Project Implementation Manual.

The portfolio review will include an assessment of the types of financing, transaction sizes, enterprise sizes, and industrial sectors of the portfolio to be supported particularly in connection with the Environmental Management Act (1996) and the Environmental Assessment Guidelines, or any other directives by local authorities; and the PFI's business plan and strategy.

- Requests and obtains evidence of the PFI's ESMS and capacity for its implementation. The review will include the following aspects of the PFI's system and capacity commensurate with the nature of the activities supported as detailed in Appendix 5.
- Requests and obtains information about the PFI's compliance with national Labour laws and evaluates compliance with the World Bank Performance Standard 2.¹²
- Provides final E&S risk rating based on the detailed information and due diligence actions, such as PFI or project/ borrower site visits if deemed necessary, taking into account considerations detailed in Appendix 4. These considerations should be used together and will require exercising reasonable judgment.
- Updates the E&S Risk Rating Memorandum (Appendix 3) with the results of E&S due diligence, including E&S Action Plan, as necessary.
- Files all relevant documentation in a systematic manner.

4.3. E&S Action Plan for PFIs

Based on the results of the E&S due diligence, RBM will require the PFI to develop and /or maintain an ESMS in accordance with RBM E&S Policy. The PFIs ESMS will enable application of FINES applicable E&S requirements. Where the PFI's ESMS must be strengthened in order to be acceptable to RBM, the PFI will put in place a time-bound action plan as a condition of its eligibility¹³.

Environmental and Social Development Specialist:

- Identifies key gaps in the PFI's ESMS and institutional capacity (per Appendix 5) and documents proposed measures and actions to address the gaps in the PFI E&S Action Plan as included in the E&S Risk Rating Memorandum (Appendix 3).
- Discusses and agrees on the Action Plan with the PFI.
- Ensures it is included in the investment decision-making and subsequently in the legal agreement with the PFI.

At a minimum, a PFI shall have:

- (a) Written E&S policy and screening procedures in place;
- (b) PFI designates staff with clearly defined responsibilities for E&S risk management;
- (c) Commitment to taking part in E&S training and capacity building activities.

The process and timelines for achieving compliance with actions identified in the E&S Action Plan are as follows:

¹² RBM will analyse and leverage the synergies that may exist between World Bank Performance Standard 2 and relevant national labour laws and regulations. It should be noted that Malawi has adopted the majority of core ILO conventions.

¹³ In accordance with the PFI eligibility criteria specified in the FINES Project Implementation Manual.

- Gaps in the ESMS of a PFI rated as RR-1 (High Risk) or otherwise engaged in sub-projects with potentially significant E&S risks must be closed to ensure compliance with the applicable E&S requirements before first disbursement of funds by RBM;
- Gaps in the ESMS (per the performance criteria in Appendix 5) – e.g. inadequate E&S procedures, no staff assigned to manage E&S issues, gaps in practical implementation of E&S screening measures by PFIs’ credit staff, no documentation maintained for lending transactions etc. – of a PFI rated RR-2 (Moderate Risk) with either relatively low E&S risks or no immediate financing activities in risky areas must be closed according to agreed timelines in the E&S Action Plan as specified in the legal agreements;
- PFIs rated as RR-3 (Low Risk) are assumed to have no substantial gaps in their ESMS;
- Significant gaps in the E&S performance (including outstanding E&S Action Plan items) of existing clients / PFIs must be closed through the process of commitment as conditions of commitment or as conditions of subsequent disbursements.
- If a PFI is consistently not able to meet the requirements set out in the E&S Action Plan, and any subsequent remedial actions, RBM may decide to terminate its financing to the PFI.

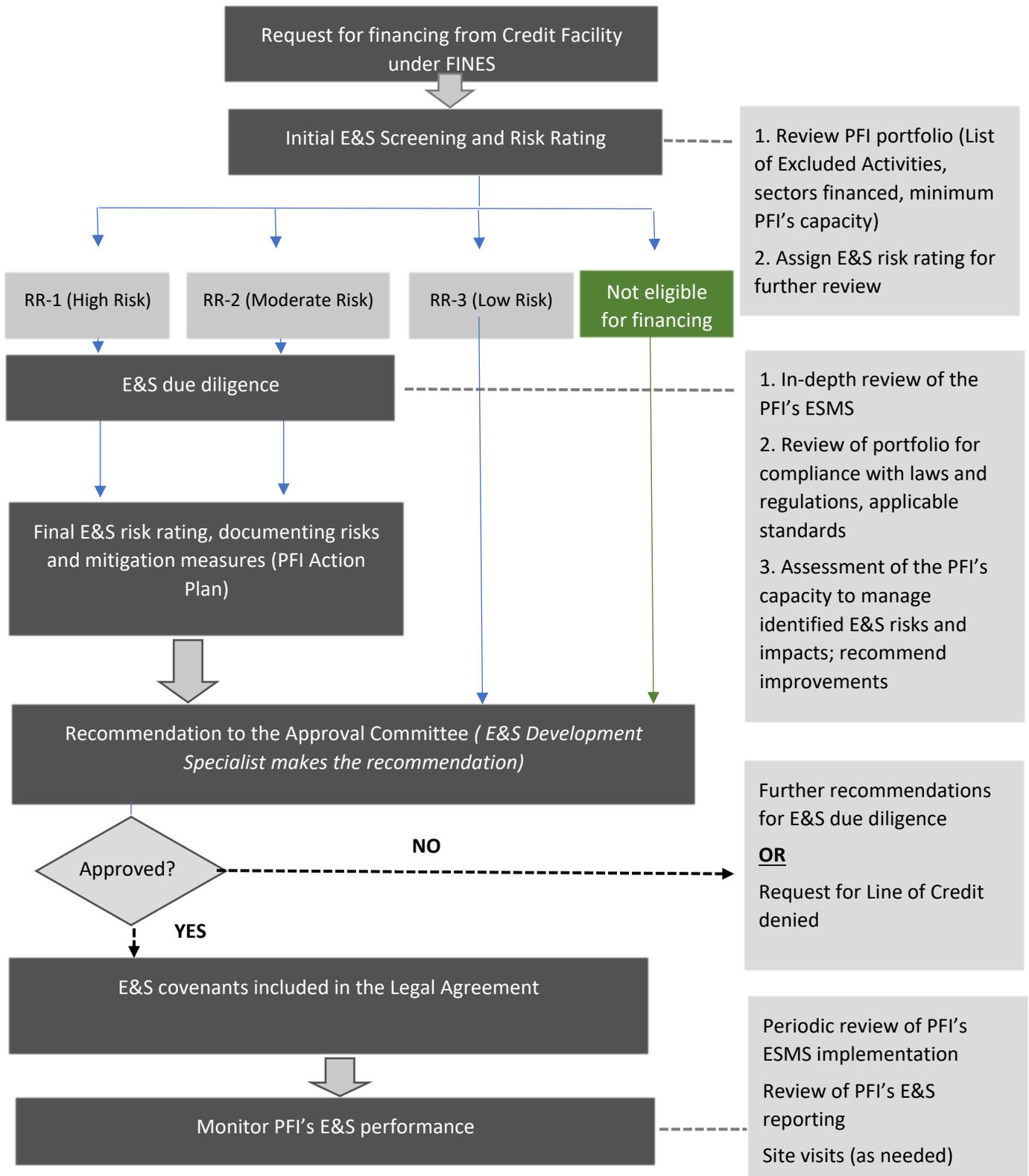
5. APPROVAL AND CONDITIONS OF FINANCING

This procedure outlines applicable requirements and performance commitments formalized in loan covenants as part of the approval process by the Approval Committee. E&S loan covenants should cover the following:

Environmental and Social Management System:

- PFIs shall have an ESMS comprising written policy and procedures, acceptable to RBM, and will delegate a person responsible for its implementation and reporting
- PFIs will provide an annual environmental and social performance report to RBM within 90 days after the end of each calendar year (Appendix 6).

APPENDIX 1. E&S PROCEDURE FLOWCHART (INVESTMENTS THROUGH PFIS)





RESERVE BANK OF MALAWI

FINANCIAL INCLUSION AND ENTREPRENEURSHIP SCALING PROJECT

Environmental and Social Screening Questionnaire (Participating Financial Intermediaries)

[date]

Section A. Financial Institution's Details

Financial Institution Name:

Financial Institution Type (*Commercial Bank; Microfinance Institution*)

Financial Institution Address:

Website:

Contact person for E&S issues:

Name and title of the person filling the Questionnaire:

Section B. Financial Institution's SME Portfolio

Total number of transactions approved over the last year:

Total value of transactions:

Number of transactions screened / assessed for E&S risks

Value of transactions screened / assessed for E&S risks

Number of transactions not approved for E&S reasons

Number of transactions exited poor E&S performance, non-compliance with agreed E&S Action Plans, or breach of loan documentation covenants/conditions

(Please attach a summary of transactions by E&S risk category, where available, sector, size, financial product type)

Section D. Exposure to Activities on the List of Excluded Activities

Does the financial institutions have investments / sub-borrowers that fall under SME category with exposure to activities on fines Exclusion List? **(Yes/ No)**

(If yes, please attach a summary of transactions with exposure to such activities)

Section E. Environmental and Social Management System

Does the financial institution have an Environmental and Social Management System (ESMS)? **(Yes/No)**

If yes, please attach any documents that can serve as evidence of an ESMS, including E&S policy and procedures, and its approval by the FI's Senior Management.

Does the financial institution have an E&S categorization system? **(Yes/No)**

If yes, please briefly describe the system below:

Does the financial institution require E&S risk mitigation measures from sub-borrowers? **(Yes/ No)**

If yes, number of corrective action plans developed for high and medium risk transactions/sub-borrowers over the past year:

Does the financial institution require regular reporting from sub-borrowers on E&S issues? **(Yes/ No)**

If yes, percentage of transactions with regular reporting from sub-borrowers over the past year:

Does the financial institution have staff with clearly designated roles and responsibilities for E&S risk management? **(Yes/ No)**

Does the financial institution conduct regular E&S monitoring visits? **(Yes/ No)**

Does the financial institution maintain an E&S records system? **(Yes/ No)**

Section F. Other Relevant Information

Please provide any other relevant information below

Date _____

Signature _____

APPENDIX 4. KEY CONSIDERATIONS FOR E&S RISK RATING

Risk Rating	Sector-based risks	Main types and nature of financing proposed / performed ¹⁴ under FINES	List of Excluded Activities	PFI's Systems and Capacity for E&S Risk Management
RR-1 (High Risk)	Substantial lending in sectors subject to full EIA per Environmental Management Act (1996) and the Environmental Assessment Guidelines Appendix B	Loans with tenors over 36 months Loan sizes from 10 to 20 million Kwacha MSME size: medium	PFI's portfolio includes <u>some exposure</u> to such activities that can be eliminated over a reasonable period of time	Overall weak E&S systems and capacity based on criteria in Appendix 5.
RR-2 (Moderate Risk)	Some lending in sectors subject to full EIA per Environmental Management Act (1996) and the Environmental Assessment Guidelines Appendix B	Loan sizes from 5 to 10 million Kwacha MSME size: small	PFI's portfolio includes <u>no exposure</u> to such activities	Overall moderate to strong E&S systems and capacity based on criteria in Appendix 5.
RR-3 (Low Risk)	Most lending in sectors not subject to EIA per Environmental Management Act (1996) and the Environmental Assessment Guidelines.	Loan sizes below 5 million Kwacha MSME size: micro	PFI's portfolio includes <u>no exposure</u> to such activities	E&S systems and capacity are well in excess of minimum capacity as above.

¹⁴ When re-assessing PFIs based on E&S portfolio financed under FINES (on an annual basis or in connection with request for repeat transaction).

APPENDIX 5: PFI'S E&S PERFORMANCE CRITERIA

Area	Description
1. Systems and capacity	
E&S Staffing and Capacity	<p>Staff with clearly designated roles, responsibilities and capacity to manage E&S issues</p> <p>Internal training developed and implemented to sensitize relevant investment staff on the required E&S screening process, criteria, and documentation</p>
E&S screening process	<p>A systematic E&S screening process, including an E&S categorization system, is supported by written documents (e.g. a policy statement, a standardized E&S questionnaire) and adequately internalized within the PFI</p>
Management Commitment	<p>Level of management commitment to incorporate E&S aspects into the PFI's risk management practices. Management commitment can be indicated by formal endorsement of the E&S policies and procedures by the PFI's management and willingness to provide adequate resources (staff and budget) for implementation.</p>
2. Implementation	
Compliance with applicable requirements	<p>Adequate implementation of the E&S screening process, including evidence of application of RBM E&S requirements</p> <p>Corrective action plans for sub-borrowers are developed</p>
Documentation	<p>Adequate documentation is maintained by the PFIs and available upon request from RBM</p> <p>Appropriate language is incorporated in financing agreements and other relevant documentation with end borrowers</p> <p>Annual E&S reports are prepared and submitted in a timely manner to RBM</p>

APPENDIX 6: E&S REPORTING TEMPLATE FOR PFIs



Reserve Bank of Malawi
E&S Performance Report for Participating Financial Institutions (PFIs)

Please provide responses to the questions below. Please include additional sheets or attachments as required to provide details on questions that have been answered Yes.

NAME OF FINANCIAL INSTITUTION			
COMPLETED BY:			
OFFICIAL POSITION		DATE	
REPORTING PERIOD	FROM:	TO:	

REPORT COVERING PERIOD	
FROM:	TO:

For the reporting period indicated above, please provide the following information about your portfolio where applicable:

Term	Product Line	Description	Total exposure outstanding for most recent year end in MK	Average loan or transaction
Long Term: Transactions with Tenor Greater Than 12 Months	MSME	Any lending or other financial assistance to any corporate or legal entity other than an individual, with 100 employees or less:		
Short term (ST): transactions with tenor less than 12 months	MSE			
Other if applicable	Other if applicable	Please describe		

PFI's Environmental & Social Management System (ESMS)

Policies and processes	Y/N	
Has your organization developed and implemented an ESMS?		If yes, please attach a copy of the ESMS to this report.
If there is an ESMS already in place, have there been any updates to the ESMS, or policy and procedures adopted by your organization during the reporting period?		If yes, please provide a copy of the updates including dates and reasons for the same
Has senior management signed off on the updated policy/procedure		If yes, please provide the date and internal communication indicating the same
Please give details of any transactions rejected on environmental, health, safety or social grounds		

Please state any difficulties and/or constraints related to the implementation of the environmental and social procedures.		
Please describe how you ensure that your clients and their sub-projects are operated in compliance with the National laws and regulations		
Please give details of any material environmental and social issues associated with sub-borrowers during the reporting period.		
Capacity	Y/N	
Please provide the name and contact information of the Environmental Officer or Coordinator who has the overall responsibility for the implementation of ESMS		Please describe the training or learning activities the Environmental Officer or Coordinator attended during the year
Please provide current staffing of other core ESMS persons in the organization involved with ESMS implementation.		Please describe the training provided to the ESMS persons and other team members during year.
What was the budget allocated to the ESMS and its implementation during the year		Please provide budget details including staff costs and training as well as any actual costs
Monitoring	Y/N	
Do you receive any non-financial reporting from industrial sub-projects that you finance?		If yes, please describe and provide supporting documents including any E&S considerations if applicable
Do you check for ongoing compliance of your subprojects with national regulation and any other requirements?		Please describe how you monitor the client and project
Please describe how you monitor the client and project environmental and social performance		Please describe and provide supporting documents and please provide information on the number of sub-projects where a field visit was conducted by staff to review aspects including E&S issues
Please provide details of any accidents/ litigation/ complaints/regulatory notices and fines: - Any significant accidents - Any incidents of non-compliance with the E&S Requirements - Any existing or potential complaint, order, directive, claim, citation or notice from any Authority under applicable law and local requirements - Covenants/ conditionalities imposed by the Bank as a result of any non-compliance		
Reporting	Y/N	
Is there an internal process to report on E&S issues to Senior Management?		If yes, please explain the process, reporting format and frequency and actions taken if any.
Do you prepare any environmental and social reports: - Other stakeholders - E&S reporting in the Annual Report - Sustainability reports		If yes, please provide copies of these reports.