**Environmental, social and governance best practice**

**Drafting Guide for equity investments**

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## Introduction

This Drafting Guide is for lawyers acting for funds or fund managers on equity investments. It contains suggested wording to cover environmental, social and governance matters for inclusion in investment documentation. Please refer to the detailed notes for more information on the purpose and use of these clauses.

The clauses in this drafting guide are designed to meet CDC’s requirements for environmental, social and governance (ESG) compliance. Although there is considerable overlap with the requirements of other development finance institutions, the principal source of the underlying standards is CDC’s Code of Responsible Investing.

The clauses should be inserted into the investment documentation for equity investments. Additional options are included for investments into financial institutions, which are generally *in italics*. For financial institutions, the additional requirements are intended to require the institution to screen its clients for ESG risks and apply certain elements of the ESG requirements to the institution’s own clients.

This guide is not intended to be a complete investment or shareholders agreement, nor is it an exhaustive list of what CDC, as a direct investor or limited partner in a fund, would expect to see in such an agreement. The drafting is intended to supplement customary shareholder protections for a minority equity investor (such as board seats, veto rights, tag-alongs etc). As with any precedent, it will require adaptation to the circumstances of the transaction, the definitions used in the underlying investment document and any local legal requirements.

The drafting assumes the requirements should apply to the entire Group (i.e. the portfolio company and any present or future subsidiaries) through the “Group Company” expression. A definition of ‘Group’ is included, but most standard investment agreements should include such a concept.

The ‘Agreed Form’ documents referred to in this guidance are:

* ESG Action Plan (this may be part of a broader diligence action plan or 100-day plan)
* ESG monitoring report
* Anti-bribery and corruption policy (if no such policies exist at the target company, CDC typically makes the adoption of new policies a condition precedent of its investment)
* Whistleblowing policy

The ESG Action Plan is a document prepared following due diligence incorporating the main steps required of the portfolio company to bring it into compliance with the ESG standards.

Your firm should have a template ESG monitoring report. CDC can provide samples if required.

Finally, there is always scope to improve legal drafting. If you have any comments or improvements to suggest, please feed these back to CDC.

## ESG definitions

See [General Definitions](#_General_definitions) in Part Two for definitions of ‘Group’ and ‘Group Company’

"**Business Integrity** **Laws**" means any law, rule or regulation relating to bribery, corruption, financial crime, anti-terrorism, terrorism financing, anti-money laundering, export controls, trade embargoes, travel bans applicable to any Group Company or to the Investors including, without limitation, the economic sanctions and regulations of a Sanctioning Body, any European Union restrictive measure that has been implemented pursuant to any European Council or Commission Regulation or Decision adopted pursuant to a Common Position in furtherance of the European Union's Common Foreign and Security Policy;

Definitions in italics for financial institutions only

*["****Client****" means each customer, depositor or borrower of a Group Company (not being a natural person);*

*“****Client ESG Standards****” means:*

* 1. *in the case of High Risk Clients, the ESG Requirements; and*
  2. *in the case of all other Clients, the ESG Laws and the requirements set out in paragraph 2 of Part A of Schedule [X] (Working conditions and labour rights);]*

"**Environment**" means humans, animals, plants and all other living organisms including the ecological systems of which they form part and the following media:

* 1. air (including, without limitation, air within natural or man-made structures, whether above or below ground);
  2. water (including, without limitation, territorial, coastal and inland waters, water under or within land and water in drains and sewers); and
  3. land (including, without limitation, land under water);

Words in italics for financial institutions deals only

"**Environmental Law**" means any applicable law, rule or regulation (including international treaty obligations) concerning the Environment and natural resource management applicable in each jurisdiction in which a Group Company carries on business [*or in which a Client carries out business activities financed by the Company*];

ESG may be part of a broader Action Plan

"**ESG Action Plan**" means [an environmental, social and governance action plan in the Agreed Form][that part of the Action Plan] defining actions, responsibilities, budgets, deliverables, compliance indicators, and a timeframe for the measures required to remedy any known non-compliances with the ESG Requirements in the business activities of the Company, [including the establishment of an appropriate ESG Management System], as may be amended with the approval of the Investors from time to time;

See note on ESG Breaches below. Cross reference the core ESG Requirements covenant, the ESG Action Plan and the ESG Schedule

“**ESG Breach**” means the breach by any Group Company of any obligation in clauses [3.1] and [3.2] and Schedule [X];

"**ESG Claim**" means any claim, proceeding or investigation by a person in respect of any ESG Laws;

Discuss with your environmental/social team whether an ESG committee is required – it will be appropriate for businesses with greater environmental or social impact. Language should conform to the SHA. If used, changes to terms of reference of the ESG Committee should be a reserved matter and the formation of the committee should be a condition precedent to closing.

["**ESG Committee**" means a committee of the Board comprising [three] directors of which [one] must be [an Investor Director][a appointed by the Investors;]

“**ESG Laws**” means Environmental Laws, Social Laws or Business Integrity Laws and the terms of any permits, licenses, consents, approvals or other authorisations held by a Group Company under Environmental Law or Social Law;

Not financial institutions

["**ESG Management System**" means a management system, appropriate to the size and nature of the business and satisfactory to the Investors which is designed to (1) ensure a systematic approach to compliance with ESG Requirements, (2) monitor progress against the ESG Action Plan, (3) provide a mechanism to assess environmental, social and governance risks and address those risks, (4) monitor and report on progress and (5), to the extent possible, involve stakeholders;]

Financial institutions only

*["****ESG Management System****" means the part of the overall management system of the Group dedicated to the systematic and structured improvement of environmental, social and governance performance, targeted to identify and manage ESG risks and opportunities in both the Group’s activities and in the loan and investment appraisal and management processes, integrated in the Group’s organisational structure, planning activities, responsibilities, practices, procedures, processes and resources, which meets the requirements set out in Part E of Schedule [X] and is satisfactory to the Investors;]*

"**ESG Requirements**"means the requirements set out in Part A of Schedule [X] to the extent applicable to any Group Company;

"**Exclusion List**" means the list of activities in Part B of Schedule [X];

"**Financial Malpractice**" means:

(a) promising, offering or giving, or soliciting or accepting, directly or indirectly, anything of value, to induce any person to act improperly or improperly refrain from acting in connection with any business or public function (or to reward them for improperly acting or refraining from acting) and includes a breach of anti-corruption law in any jurisdiction applicable to an Investor or a Group Company;

(b) any act or omission, including any misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a person to obtain a financial benefit or to avoid an obligation; or

(c) materially impeding an investigation by the Investors, a governmental or regulatory agency or any third party into allegations of the matters referred to in paragraphs (a) or (b) of this definition, including deliberately destroying, falsifying, altering or concealing material evidence, making false statements, limiting access, or threatening, harassing or intimidating any person in order to stop them (i) disclosing their knowledge of matters relevant to such an investigation, or (ii) pursuing the investigation;

Financial institutions only

*[“****High Risk Clients****” means Clients who are or may be active in the industry sectors or otherwise falling within the criteria in Part D of Schedule [X] (Definition of High Risk Client industry sectors);]*

"**IFC** **Performance Standards**" means the International Finance Corporation (IFC) 2012 Performance Standards on Social and Environmental Sustainability (including the technical reference documents known as World Bank Group Environmental, Health, and Safety (EHS) Guidelines) which may be downloaded from the IFC website:

* 1. IFC Performance Standards: <http://www.ifc.org/PerformanceStandards>; and
  2. World Bank Group EHS Guidelines: <http://www.ifc.org/EHSGuidelines>;

"**ILO Convention**" means a convention of the International Labour Organisation (ILO), the tripartite United Nations agency, whose conventions may be downloaded from the ILO website: http://www.ilo.org/global/standards/lang--en/index.htm;

“**Irremediable ESG Breach**” is defined in clause [5.1];

“**KYC Checks**” means obtaining information from a Person to verify the identity and address (and, where applicable, ownership and control) of the Person concerned (to the standard required by any law or regulation to which the Group Company is subject and the UK Financial Conduct Authority regulations) and to ensure that the person concerned is not a Prohibited Person;

“**Prohibited Person**” means:

(a) any person or entity who at the relevant date is, or in the five years preceding such date was, listed on any Sanctions List;

(b) any person who appears, or during such five year period appeared, on the World Bank Listing of Ineligible Firms (see www.worldbank.org/debarr);

(c) any person who has been convicted of or is the subject of a serious allegation of (other than vexatious allegations) a breach of any Business Integrity Law;

(d) any person Controlled (directly or indirectly) by any such person referred to in paragraphs (a) to (c) above or who such person has (directly or indirectly) any interest in;

“**Sanctioning Body**"means any one or combination of the following entities: the Office of Foreign Assets Control of the Department of Treasury of the United States of America, the United Nations Security Council, the European Union and/or Her Majesty’s Treasury of the United Kingdom;

“**Sanctions List**” means a list of designated persons or entities held by a Sanctioning Body (as amended, supplemented or substituted from time to time);

"**Social Law**" means any law, rule or regulation (including international treaty obligations) applicable in the jurisdiction of the Country concerning (i) labour, (ii) social security, (iii) the regulation of industrial relations (between government, employers and employees), (iv) the payment of wages which meet or exceed industry or legal national minima, (v) the protection of occupational as well as public health and safety, (vi) the regulation of public participation, (vii) the protection and regulation of ownership of land rights (both formal and traditional), immovable goods and intellectual and cultural property rights, (viii) the protection and empowerment of indigenous peoples and ethnic groups, (ix) the protection of cultural heritage, and (x) all other laws, rules and regulations providing for the protection of employees and citizens;

References to governmental, supranational, or international bodies or their procedures, protocols or conventions (including IFC Performance Standards and ILO Conventions) or to treaties or to other rules, regulations issued by or deriving from them shall include those bodies, procedures, protocols, conventions, standards, treaties, rules, or regulations as they may be renamed, reorganised, replaced, amended, or superseded from time to time.

Similar language is common in most investment agreements. Delete if repetitious

The expressions “**include**” and “**including**” shall be construed without limitation.

## ESG conditions precedent

Depending on the outcome of due diligence, conditions precedent to create remuneration, audit or ESG committees may be required

* 1. The Company must adopt an anti-bribery and corruption policy and a whistle-blowing policy for the Group (including explanations and procedures) in each case in [the Agreed Form][a form satisfactory to the Investors];

## ESG representations and warranties

Notes on warranties:

(i) It is usually appropriate for warranties to be repeated on subsequent drawdowns, but this is a matter for commercial negotiation. Caps and limitations may be negotiated although the aim is to ensure an incentive for the giver of the warranties to disclose - legal redress is typically less important on minority investing.

(ii) Discuss with your ESG team following DD whether the Investors require warranties on compliance with all ESG requirements or simply compliance with law and the ILO working conditions requirements. This version assumes the latter as generally we do not expect businesses to comply with these standards prior to investment. But for follow-on investments or investments in businesses where the investors or other DFIs already have a stake we may expect full compliance with the ESG Requirements prior to investment.

(iii) The disclosure letter should cross refer to relevant breaches identified in the ESG Action Plan - either specifically or generally.

(iv) The Investors may accept in negotiations that the warranty is limited to compliance [in all material respects] but a ‘reasonable efforts’ or ‘best efforts’ basis for this warranty is generally not acceptable as it does not necessarily cover material issues, merely the efforts made by the giver.

1. ESG compliance and claims
   1. Each Group Company complies with all applicable ESG Laws and with the requirements set out in paragraph 2 of Part A of Schedule [X] (Working conditions and labour rights).

The content of 2.2 is covered under more a general ‘no litigation/no claims’ warranty, in which case duplication would not be necessary

* 1. No ESG Claim has been commenced or (to the best of its knowledge and belief) is threatened against any Group Company.
  2. No written notice or other allegation has been received by, or brought to the attention of, any Group Company to the effect that a Group Company has breached any ESG Laws.

[Financial institutions only - ‘knowledge’ or ‘awareness’ may be defined. ESG Requirements may be appropriate if the financial institution already has DFI investment

* 1. *[To the best of the Company’s knowledge, each Client complies with all applicable ESG Laws and with the requirements set out in paragraph 2 of Part A of Schedule [X] (Working conditions and labour rights) [and each High Risk Client also complies with all other ESG Requirements].]*

1. Corruption and illegal payments
   1. No Group Company has committed any Financial Malpractice.
   2. No Group Company has directed or knowingly permitted any person to commit any Financial Malpractice on its behalf.
   3. The Group has in place procedures designed to prevent Group Companies and those acting on their behalf from committing any Financial Malpractice.
   4. No proceeds of any illegal act or act related to drug trafficking, corruption, bribery, organised crime or terrorism have been received by any Group Company, directly or indirectly (including for the purchase of shares in any Group Company) or as a contribution to or otherwise to support the activities or business of any Group Company or the Group as a whole.

Financial institutions only

* 1. *[To the best of the Company’s knowledge, [after due inquiry,] no Client has committed any Financial Malpractice nor has any Client directed or knowingly permitted any person to commit any Financial Malpractice on its behalf*. ]

1. Exclusion List

Use italicised words in square brackets on financial institutions deals

No Group Company[ *nor any Client*] is carrying on or financing any activity on the Exclusion List.

## ESG information rights

1. Content of annual report

Add this wording to the customary requirement to deliver annual reports to the Investors

* 1. The Company’s annual audited accounts must include:
     1. an analysis of the principal risks that the directors believe the Group faces and the steps taken to mitigate those risks
     2. a review of:
        1. the bribery and financial crime risks faced by the Group,
        2. the systems, policies and procedures for managing such risks, and
        3. the implementation and effectiveness of those systems, policies and procedures
  2. The Company must promptly send the Investors a copy of any management letter addressed to a Group Company by its external auditors.

1. ESG and development impact reporting

Financial Year or Financial Period may be a defined expression

* 1. The Company must, as soon as it is available, but in any event no later than [90] days after the end of each [financial year], deliver to the Investors a monitoring report in the Agreed Form which addresses environmental, social, business integrity and development impact matters.
  2. Without prejudice to clause 6.1, the Company must provide the Investors with such assistance, access and information as the Investors reasonably require in order to monitor and evaluate the development impact of their investment.

Not required if these matters are subject to Investor veto right/reserved matters

* 1. The Company must promptly inform the Investors of any proposed change in the Directors, internal or external auditors or the bankers of any Group Company.

Financial institutions only

* 1. *The Company must deliver to the Investors no later than the date it has to deliver its audited [consolidated] financial statements in accordance with sub-Clause 2.1(a) (Financial Statements), a summary of all Clients and confirmation as to whether or not any of them are or may be High Risk Clients.*

1. Internal audit
   1. The Company must promptly send the Investors any internal audit report prepared for the Company which addresses the Group’s compliance with all or any part of the ESG Requirements.
   2. The Company must ensure that the work plan of any internal audit firm (or internal audit function within the Group) includes a review of:
      1. the assessment of the bribery and financial crime risks faced by the Group,
      2. the systems, policies and procedures for managing such risks, and
      3. the implementation and effectiveness of those policies and procedures.
2. ESG breaches and claims

Use italicised words in square brackets on financial institutions deals

* 1. The Company must inform the Investors in writing immediately upon becoming aware of:
     1. any ESG Claim being commenced or threatened against any Group Company[ *or any Client*] or any facts or circumstances which will or are reasonably likely to result in such an ESG Claim being commenced];
     2. any written notice or other allegation received by, or brought to the attention of, any Group Company to the effect that a Group Company has breached any ESG Requirement;
     3. any actions which may constitute a Financial Malpractice committed by or on behalf of any Group Company [ *or, to the best of its knowledge, by or on behalf of any Client*]; and
     4. any enquires from government enforcement authorities concerning any act that may constitute a Financial Malpractice by or on behalf of any Group Company.
  2. If any Investor notifies the Company that it believes that there may have been a breach of the ESG Requirements, the Company must cooperate in good faith with the Investor in determining whether a breach has occurred. The Company must respond promptly and in reasonable detail to any request for information from the Investors and provide documentary support for the response if requested.

1. Serious incidents

The Company must notify the Investors of Serious Incidents promptly and in any event within 3 days after becoming aware of their occurrence. The Company must supply the Investors within 14 days of the Serious Incident with a report in the form set out in Part C of Schedule [X] incorporating, in each case, details of (1) the nature of the incident and the on-site and off-site effects and (2) any action the Group Company [*or the Client (as the case may be)*] proposes to take in order to remedy the effect of the Serious Incident. The Company must keep the Investors informed about the progress of any remedial action.

A “**Serious Incident**” is one of the following which affects any employee, customer, supplier or other person who has dealings with, or is affected by the activities of, a Group Company [*or a Client*] or which occur on or nearby any site, plant, equipment or facility of any Group Company [*or Client*]:

* + 1. an incident resulting in death or permanent injury to any person;
    2. any other incident which has a material negative impact on the environment or the health, safety and security situation (including without limitation any explosion, spill or workplace accident which results in death, serious or multiple injuries or material environmental contamination); and
    3. any incident of a social nature (including without limitation any violent labour unrest or dispute with local communities), which has or is reasonably likely to have a material negative effect on the social and cultural context.

Note: the following provisions may be merged with more general ‘access’ or ‘costs’ clauses - eg for default in providing financial information. The company will normally push back on giving a ‘blank cheque’ for adviser’s visits – this clause limits reimbursement to one inspection a year plus default

1. Inspection rights
   1. The Company must permit the Investors, their accountants and their other advisers unrestricted access to each Group Company at all reasonable times and on reasonable notice to:
      1. meet with senior management of the Company to discuss any questions or issues in relation to ESG Requirements;
      2. investigate any failure to comply with or implement the ESG Requirements (including the non-implementation of any ESG Action Plan);
      3. inspect and to take copies and extracts from the books, accounts and records of each Group Company; and
      4. view the premises of each Group Company.
   2. The Company must reimburse the Investors on demand for all costs and expenses (including consultancy costs and any travel expenses) incurred in connection with any meetings, investigations or inspections made under clause [2.6] provided that the reimbursement shall only be for:
      1. meetings, investigations or inspections which reveal a material breach of the ESG Requirements; and
      2. one other meeting, investigation or inspection in any financial year of the Company.

All other meetings, investigations or inspections shall be at the Investors’ cost.

## ESG on-going covenants

1. ESG Requirements
   1. The Company must and must ensure that each other Group Company (whether acquired before or after the date of this Agreement) will:
      1. comply with the ESG Requirements, subject to any period permitted to achieve compliance with a ESG Requirement set out in the ESG Action Plan; and
      2. take all reasonable steps in anticipation of known or expected future changes to the ESG Requirements.

Financial institutions only – reasonable endeavours in relation to Clients is acceptable on the basis that the Company adopts all the actions listed in Part E

* 1. *[The Company must use all reasonable endeavours to ensure that each Client complies with the applicable Client ESG Standards].*
  2. *For the purposes of clause 11.2, ‘all reasonable endeavours’ includes (but is not limited to) compliance by the Company with paragraph 5 of Part A of Schedule [X] (ESG Management System) and Part E of Schedule [X] (ESG Management Systems for Financial Institutions)].*
  3. The Company must implement all actions set out in the ESG Action Plan within the time-frames set out in that plan.

## Board process

1. Board qualification

No Prohibited Person shall be appointed as director of the Company and/or any Group Company. The Company shall carry out KYC Checks on the proposed director and send the information received for that purpose to the Investors.

Use the following to the extent not covered in standard SHA wording. ‘Board’ may be defined already. If the Investors have board seats, some of these provisions may be in place already

1. Board schedule and papers

The Company must ensure that:

* + 1. each year it adopts a schedule of meetings of the Company’s board of directors (the “**Board**”) and Board committee meetings, including details of when statutory and regulatory returns are due. A copy of the schedule will be sent to the Investors [on request][when the schedule is adopted];
    2. copies of agendas and papers for Board and Board committee meetings will be sent to the Investors in advance; and
    3. the Investors are supplied on request with minutes of Board and Board committee meetings unless the Company is legally prevented from circulating those minutes.

## Share transfers

1. Restriction on new shareholders

No Prohibited Person shall be registered as a shareholder of the Company. The Company shall carry out KYC Checks on the proposed shareholder and send the information received for that purpose to the Investors.

## ESG Breach

The following drafting is suggested to help define an ESG Breach and those which are capable of remedy

1. Breach of ESG obligations
   1. If the Investors consider that an ESG Breach has (or may have) have occurred, the Investors shall inform the Company of their suspicions and shall have the right to appoint consultants to investigate the possible breach. Thereafter, the Investors and the Company shall meet to discuss possible remedies for the ESG Breach. Provided that [the Investors have reasonable grounds for their suspicions][the appointment has been approved by the ESG Committee], the reasonable cost of appointment of the consultants shall be reimbursed by the Company.

Discuss with the ESG team whether, in the context of the business concerned, other breaches would be automatically irremediable.

* 1. If the ESG Breach is not capable of remedy this shall be an “**Irremediable ESG Breach**”.  The following ESG Breaches shall for the avoidance of doubt be Irremediable ESG Breaches:
     1. Financial Malpractice by a Group Company where (i) the Financial Malpractice or any payment in connection with the Financial Malpractice was authorised by [one or more directors of a Group Company][the Promoters/Managers] or (ii) the Group Company failed to have or to operate adequate procedures to prevent Financial Malpractice; and
     2. a breach of Environmental Law or Social Law which results in death or significant permanent physical injury to natural persons or significant adverse environmental and/or social impacts that are diverse, irreversible or unprecedented.
  2. Other than in relation to Irremediable ESG Breaches, if there is an ESG Breach the Company shall have a defined period (as agreed by the Investors and not to exceed a maximum period of six months) in which to remedy the ESG Breach in the manner agreed between the Investors and the Company.
  3. If the ESG Breach is remedied to the Investors’ satisfaction within the defined time period or the same is waived by the Investors, then the ESG Breach shall lapse.   If the ESG Breach is not so remedied, this shall be an “**Unremedied ESG Breach**”.

See note below on consequences

* 1. If an Irremediable ESG Breach or an Unremedied ESG Breach occurs: …

### Note: Consequences of ESG Breach

**Note:** Practice varies in terms of what happens following an irremediable/unremedied ESG Breach, depending on the commercial bargaining position, the nature of the Investors’ instrument (debt, mezzanine or equity) and the broader deal context. Examples might include:

* a restriction on further drawdowns until the breach is remedied,
* a put option on other parties to buy shares, although these frequently have enforcement challenges – particularly on portfolio company buybacks,
* repayment of loan instruments,
* ability to implement exit rights sooner,
* ability to sell shares without transfer restrictions (and this is included in the drafting in Part Two),
* drag alongs,
* ability to appoint additional directors,
* ability to appoint advisers at the cost of the company (included above) and to require the board to adopt the recommendations

You should discuss options with your legal advisers.

## ESG schedule

**SCHEDULE [X]**

**Environmental, social and governance**

### Part A - ESG Requirements

Discuss with your environmental/social team the relevance of each item to the business in question

1. Compliance with law

Each Group Company must comply with ESG Laws.

1. Working conditions and labour rights

Each Group Company must:

* 1. not employ or make use of forced labour in accordance with ILO Convention No. 29 (Forced Labour) and ILO Convention No. 105 (Abolition of Forced Labour);
  2. not employ or make use of child labour in accordance with ILO Convention No. 138 (Minimum Age) and ILO Convention No. 182 (Worst Forms of Child Labour);
  3. pay wages which meet or exceed industry or legal national minima;
  4. not discriminate in terms of recruitment, progression, terms and conditions of work and representation, on the basis of personal characteristics unrelated to inherent job requirements, including gender, race, colour, caste, disability, political opinion, sexual orientation, age, religion, social or ethnic origin, marital status, membership of workers’ organisations, legal migrants, or HIV status (unless positive discrimination is permitted by law and is intended to address a historical imbalance);
  5. adopt an open attitude towards workers’ organisations and respect the right of all workers to join or form workers’ organisations of their own choosing, to bargain collectively and to carry out their representative functions in the workplace in accordance with ILO Convention No. 87 (Freedom of Association and Right to Organise) and ILO Convention No. 98 (Right to Organise and Collective Bargaining);
  6. provide reasonable working conditions including a safe and healthy work environment, working hours that are not excessive in accordance with ILO Convention No. 1 (Hours of Work (Industry)) and clearly documented terms of employment, respecting any collective bargaining agreements that are in place or (where these do not exist or do not address working conditions) or conditions established, by collective agreement or otherwise, for work in the trade or industry concerned in the area where the work is carried out;
  7. provide an appropriate grievance mechanism that is available to all workers and where appropriate other stakeholders, and which includes grievances brought by those affected by the operation of the Group; and
  8. implement policies and procedures for, and encourage, the reporting of wrongdoing and misconduct by staff, employees and contractors in their dealings with each other or with third parties that includes protection for the reporter and appropriate disciplinary action for anyone found to harass the reporter.

1. Restrictions on activities

Delete ‘[or finance]’ for financial institutions – the provisions in 3.2 to 3.5 are designed to present a reasonable solution for financial institutions in terms of securing compliance by Clients

* 1. The Company must not (and the Company must ensure that no other member of the Group will) carry on [or finance ]any activity on the Exclusion List.

Financial institutions only

* 1. *[No Group Company shall make any loan or other facility to any Client that is engaged in any activity on the Exclusion List.*
  2. *Each Group Company shall have a covenant in any loan or facility document entered into after the date of this Agreement prohibiting any Client from engaging in any activity on the Exclusion List. If a Group Company becomes aware that any Client has breached the covenant, the Group Company shall:*
     1. *promptly notify the Investors of the breach and require the relevant Client to undertake as appropriate, in the Group Company’s reasonable judgement, corrective measures to remedy the breach; and*
     2. *if the relevant Client does not implement the corrective measures, use commercially reasonable efforts to accelerate or dispose of the Client’s loan on commercially reasonable terms, taking into account liquidity, market constraints and fiduciary responsibilities*.]

Financial institutions only.  There may be a defined expression for the investment proceeds

* 1. *No Group Company shall make the [proceeds of the Investors’ investment in the Company] available to any Client to finance (or re-finance) any Coal Power Generation:*
     1. *outside of the Permitted Countries; or*
     2. *inside the Permitted Countries if the aggregate funding of Clients engaged in Coal Power Generation represents (or would, following that financing, represent) more than 10% of the Group’s underlying portfolio volume.*

*For the purpose of this clause:*

*“****Permitted Countries****” means any country eligible for support from the International Development Association (see* [*http://ida.worldbank.org/about/borrowing-countries*](http://ida.worldbank.org/about/borrowing-countries)*); and*

*"****Coal Power Generation****" means the production of electricity (for public energy supply or captive energy production in industrial or commercial activities) using coal as the source of power, including dual-power plants/projects where coal is one of the energy sources.]*

* 1. No Group Company may be formed without the Investors’ prior written consent form in any jurisdiction:
     1. who has not undergone a peer review as part of the OECD’s Global Forum on Transparency and Exchange of Information for Tax Purposes (the “**Global Forum**”) or
     2. following a phase 1 review has not been permitted by the Global Forum to proceed to a phase 2 review; or
     3. has undergone a phase 2 review and has not received an overall rating from the Global Forum of ‘compliant’ or ‘largely compliant’

1. Activities with greater environmental or social impact
   1. If the activities of a Group Company involve or could be reasonably expected to involve:
      1. significant air emissions (including of greenhouse gases), use of water or generation of liquid effluents, generation of hazardous or other solid wastes or resource use inefficiencies;
      2. transactions that generate adverse community health and safety impacts;
      3. the acquisition and/or use of land that will lead to the economic or physical displacement of communities;
      4. significant negative impacts on biodiversity, habitat or ecosystem services, including without limitation (i) provisioning services such as food or timber, (ii) regulating services such as water flow regulation, (iii) cultural services such as sacred sites and (iv) supporting services such as soil formation;
      5. impacts to indigenous peoples (or other marginalised and vulnerable groups);
      6. impacts to cultural heritage; or
      7. other significant negative environmental or social impacts

then (i) the relevant IFC Performance Standards should be implemented, (ii) an appropriate stakeholder engagement plan should be developed in line with the applicable IFC Performance Standard, and (iii) an environmental and social impact assessment and/or issue specific action plan (e.g. a resettlement action plan) should be developed for any such activities.

* 1. If the activities of a Group Company could reasonably be expected to involve:
     1. significant risks to the health and safety of workers or to other stakeholders, including affected communities, the Group Company must assess and mitigate those risks, for example through a Health and Safety audit and action plan, in line with the relevant IFC Performance Standards;
     2. coal-fired power, the Investors must be satisfied that the use of coal is justified by the impact of the proposed activity by the Group Company and that no practicable alternatives exist;
     3. significant emissions of greenhouse gases, ensure that adequate measures to reduce emissions to the extent possible and mitigate adverse climate impacts are implemented and that the Company reports to the Investors on its emissions[.][; and]

Financial institutions only

* + 1. *[microfinance, the Group Company must endorse and apply the SMART Campaign Client Protection Principles (see www.smartcampaign.org).]*

1. ESG Management System
   1. The Company must appoint senior operational officer(s) or other appropriate personnel satisfactory to the Investors to be responsible for the implementation, operation and maintenance of the ESG Management System and must notify the Investors in writing immediately of the removal or replacement (for whatever reason) of that person. Different officers or personnel may be responsible for different aspects of the ESG Management System.
   2. The Company must implement, maintain and continuously improve the ESG Management System, including deploying employees of sufficient expertise and seniority as is necessary for this purpose.
   3. The ESG Management System must be supervised by [the Board][the ESG Committee][a named director satisfactory to the Investors][a director appointed by the Investors]. Supervision of the ESG Management System must include:
      1. overseeing implementation of the ESG Action Plan;
      2. quarterly reports to the Board on any material issue that has arisen as a result of the operation of the ESG Management System since the last meeting and an explanation as to how it is being dealt with;
      3. ensuring that the Group has the systems and resources (including employees of sufficient expertise and seniority) to understand and determine the applicability of the ESG Requirements to the Group and monitor the underlying ESG Laws, IFC Performance Standards and ILO Conventions for applicable changes;
      4. examining policies and procedures relating to the ESG Requirements and their implementation and making recommendations for their improvement to the Board;
      5. considering [quarterly] reports from management on the implementation of the ESG Action Plan;
      6. reviewing and approving the report to the Board and the Investors required under clause [2(a)];
      7. considering ESG assessment reports on new projects or acquisitions [and veto [transaction][project][contract] bids] where [the reports advise that][in the Investors’ reasonable opinion] there is a material risk that the transaction, if consummated, would cause the Group to be in breach of the ESG Requirements]; [and]
      8. appointing consultants to investigate alleged breaches of the ESG Requirements or the related policies and procedures of the Group[.][; and]

Financial institutions only

* + 1. monitoring and seeking to secure the compliance of Clients with the applicable Client ESG Standards in accordance with Part E of this Schedule [X].

1. Opportunities for environmental or social improvement

Each Group Company should consider the potential for positive environmental and social impact from their business activities and how these could also benefit the business, for example through cost savings, reduced staff turnover or improved stakeholder relations. These should include adopting, developing, offering or marketing:

* + 1. products, services, skills or employment opportunities that could benefit community stakeholders;
    2. a living wage that is sufficient to meet workers’ needs; and
    3. resource efficient, greenhouse gas reducing or low carbon technologies or working practices.

1. Business integrity
   1. The Company must not commit (and the Company must ensure that no other Group Company or any agent or delegate commits) any Financial Malpractice or direct or knowingly permit any person to commit any Financial Malpractice on its behalf.
   2. The Company must procure that the Group:
      1. upholds high standards of business integrity and honesty;
      2. adopts and implements policies and practical procedures to prevent extortion, fraud, bribery, corruption and financial crime in accordance with Business Integrity Laws and international best practice, including anti-corruption and anti-money laundering best practice, including:

Adoption of (or amendment of existing) anti-bribery and whistle-blowing policies should be a CP if there are no adequate procedures in place already

* + - 1. the adoption and periodic review of a code of ethics which must incorporate a whistleblower policy, the anti-bribery and corruption policy (including explanations and procedures) in the Agreed Form and other appropriate business integrity and legal compliance policies to ensure compliance with applicable Business Integrity Laws (including prohibiting employees and contractors acting on the Group Company’s behalf from promising, making or receiving gifts of substance in the course of business or making of payments as improper inducement to confer preferential treatment);
      2. employee training programmes; and
      3. appropriate due diligence procedures to evaluate the integrity and business history of persons and entities with whom they wish to transact;
    1. properly records, reports and reviews financial and tax information and adopt internationally recognised accounting standards satisfactory to the Investors;
    2. establishes corporate governance practices appropriate to the size and nature of the business;
    3. deals with regulators in an open and co-operative manner;
    4. uses information received from its business partners only in the best interests of the business relationship and not for personal financial gain by any worker; and
    5. ensures that employees and third parties providing material goods and services to any Group Company are contractually bound not to engage in any Financial Malpractice in the performance of employment or services on its behalf.

Use paragraph 8.1 for financial institutions and for businesses which operate in sectors where trade sanctions may be an issue (e.g. supply of equipment to sensitive countries or sectors, or where equipment could be used for military and non-military purposes). Sanctions laws are also within the ‘Business Integrity Laws’ definition so the general covenant on compliance with ESG Laws will be sufficient for other investments with low sanctions risks.

1. [Sanctions
   1. The Group shall [institute and] maintain internal procedures, consistent with its business and customer profile, to ensure that no member of the Group will enter into any transaction:
      1. with, or for the benefit of, any person or entity listed on any Sanctions List; or
      2. related to any activity prohibited by any Sanctioning Body.

Use for financial institutions

* 1. [*Each Group Company shall ensure that it has a covenant in any loan or facility document entered into after the date of this Agreement prohibiting any Client from being named on any Sanctions List or engaging in any activity prohibited by any Sanctioning Body. If a Group Company becomes aware that any Client has breached the covenant, the Group Company shall:*
     1. *promptly notify the Investors of the breach and require the relevant Client to undertake as appropriate, in the Group Company’s reasonable judgement, corrective measures to remedy the breach; and*
     2. *if the relevant Client does not implement the corrective measures, use commercially reasonable efforts to accelerate or dispose of the Client’s loan on commercially reasonable terms, taking into account liquidity, market constraints and fiduciary responsibilities*.]]

### Part B - Exclusion List

1. The production of, or trade in:
   1. hazardous chemicals, pharmaceuticals, pesticides and wastes, as specified in the 2004 Stockholm Convention on Persistent Organic Pollutants; the 2004 Rotterdam Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade; the 1992 Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal and WHO Recommended Classification of Pesticides by Hazard Class 1a (extremely hazardous); or 1b (highly hazardous);
   2. ozone depleting substances, as specified in the 1999 Montreal Protocol on Substances that Deplete the Ozone Layer;
   3. endangered or protected wildlife or wildlife products, as specified in the 1975 Convention on International Trade in Endangered Species or Wild Flora and Fauna;
   4. any other product or activity deemed illegal under applicable local or national laws or regulations or subject to internationally agreed phase-outs or bans as defined in global conventions and agreements;
   5. arms (i.e. weapons, munitions or nuclear products, primarily designated for military purposes); or
   6. radioactive materials (excluding medical equipment, quality control (measurement) equipment and any equipment in which the radioactive source could reasonably be considered to be trivial or adequately shielded).
2. Production of, use of, or trade in unbonded asbestos fibres.
3. Unsustainable fishing methods such as blast fishing and drift net fishing in the marine environment using nets in excess of 2.5 kilometres in length.
4. Prostitution.

Consider deleting the introductory wording for direct investments in non-financial institutions where the activities are not considered to be likely – in these cases an outright prohibition may be appropriate.

[Any of the following, to the extent that the activities represent more than 10% of the Group’s [consolidated balance sheet or earnings][*underlying portfolio volumes*]:]

1. Gambling, gaming casinos and equivalent enterprises[;][[.]
2. Tobacco or tobacco related products (except where the Group proposes to cease such activities completely within a period agreed with the Investors)[.][; or]
3. Pornography.

### Part C - Serious Incident Report

|  |  |
| --- | --- |
| **REPORT on ESG ISSUES/INCIDENT in [Name of Company]** | |
| **Date of report** |  |
| **Company contact person** |  |
| **Description of issue** | 1. Date and time of incident. 2. Type of incident: environmental issue, fatality, alleged fraud or other. 3. Name of person/s involved/injured/deceased, if applicable 4. Narrative and contextual information. 5. Whether incident was work or non-work related. 6. Causes of incident. 7. Status of investigation. 8. Listing of parties involved in investigation (witnesses and staff, unions, police, other authorities and other parties. 9. Publicity |
| **Follow-up by Company management** | 1. Company view of incident – degree of severity, possible uncertainties or disputed facts to be investigated. 2. Status of investigation. 3. Reports produced (and outstanding, if any). 4. Immediate actions taken by company and other parties. 5. Further actions to prevent re-occurrence of incident. 6. Monitoring/reporting arrangements to follow up on efficacy of actions taken. 7. Results to date of actions taken. |
| **Conclusion** | Next steps: whether to close the case, or proceed investigations, how to do so, and the rationale for it. |

Financial institutions only

### *Part D - High Risk Client industry sectors*

*The following sectors are considered usually to be high risk industry sectors, for both new developments (greenfield) as for existing companies (brownfield). The list is derived from the EDFI Harmonized List of High Risk Sectors (October 2012). Depending on project specifics the environmental and social risks of individual projects may be considered to be medium. In such cases detailed rationales for categorisation must be documented.*

*The sectors as listed below cover the activities as defined under the heading ‘Applicability’ of the corresponding IFC Environmental, Health, and Safety Guidelines in the IFC Performance Standards or directly trigger IFC Performance Standard 5-8.*

***Infrastructure***

* *Railways*
* *Ports, harbours and terminals*
* *Airports*
* *Toll roads*
* *Crude oil and petroleum product terminals*
* *Pipelines*
* *Long distance overhead transmission lines*
* *Large dams (hydro power plants / irrigation/water supply)*
* *River-run-off hydro power plants (> 50 MW)*
* *Waste management / Waste treatment facilities*
* *Thermal power: new plants (> 50 MW)*
* *Thermal power: existing plants (> 50 MW)*
* *Wind parks (> 100 MW installed capacity)*

***Oil & Gas***

* *Offshore oil and gas development*
* *Onshore oil and gas development*
* *Liquefied natural gas (LNG) facilities*

***Large Scale Primary Production (Plants / Animals)***

* *Plantation crop production*
* *Forestry*
* *Aquaculture*
* *Animal production*

***Heavy Industry***

* *Cement and lime manufacturing*
* *Glass manufacturing*
* *Construction materials extraction*
* *Integrated steel mills*
* *Base metal smelting and Refining*
* *Pulp and paper mills*
* *Foundries*
* *Pharmaceuticals and biotechnology manufacturing*
* *Coal processing*
* *Natural gas processing*
* *Oleo chemicals manufacturing*
* *Nitrogenous fertiliser manufacturing*
* *Phosphate fertiliser manufacturing*
* *Pesticides manufacturing and packaging*
* *Petroleum-based polymers manufacturing*
* *Petroleum refining*
* *Large volume petroleum-based organic chemicals manufacturing*
* *Large volume inorganic compounds manufacturing and coal tar distillation*

***Mining***

* *Mining (open pit and underground)*

***Socially Critical Projects***

* *Projects with large groups of low-skilled labour, for instance in free trade zones etc. (e.g. textiles manufacturing projects which may affect indigenous or tribal populations)*
* *Projects which may affect areas of archaeological or cultural significance*
* *Projects which cause or have caused (during last 5 years) physical or economic resettlement*
* *Projects which cause retrenchment of more than 10% of the present work force (or > 50 workers)*

***Environmentally Critical Projects***

* *Projects in or bordering ecological sensitive or protected areas (e.g. agriculture in areas which comprised natural habitat, large scale tourism projects)*
* *Large scale conversion of natural habitats (as a guide anything greater than 10 hectares)*
* *Large scale land reclamation*
* *Projects that have potential to heavily impact ecosystem services (e.g. due to intensive use of ground water)*

Financial institutions only

### *Part E - ESG management system for financial institutions*

*The Group must adopt responsible investment management systems which must include:*

1. Policy and Processes
   1. *ensuring the Group’s own operations comply with the ESG Requirements;*
   2. *identifying the environmental, social and governance risks of all potential Clients and appropriately managing and monitoring those risks (including the identification of climate change risks, and reporting on greenhouse gas emissions from high carbon intensity activities);*
   3. *preventing any investment by the Group in an activity on the Exclusion List;*
   4. *assessing compliance by all Clients with the applicable Client ESG Standards;*
   5. *developing an environmental, social and governance action plan agreed between the relevant Group Company and each Client, defining actions, responsibilities, budgets, deliverables, compliance indicators, and a timeframe for the measures required to remedy any known non-compliance with the applicable Client ESG Standards in the business activities of the Client and for any other measure agreed upon, as amended from time to time (the “****Client ESG Action Plan****”);*
   6. *using all reasonable endeavours to procure, through the inclusion of binding obligations of each Client in favour of a Group Company, that:*
      1. *each Client complies in all material respects with the applicable Client ESG Standards;*
      2. *where applicable, each Client complies with the requirements set out in the relevant Client ESG Action Plan; and*
      3. *each High Risk Client institutes and maintains a management system that ensures compliance with the ESG Requirements; and*
   7. *establishing a public grievance process for the reporting of environmental, social or governance matters and use all reasonable endeavours to ensure that each High Risk Client does so.*
2. Roles and Responsibilities

*assigning environmental, social and governance responsibilities to (i) designated representative(s) of senior management, who are members of appropriate credit and governing bodies and (ii) suitably trained employee(s) or consultant(s).*

1. Performance Management
   1. *working with Clients continually to improve their performance on environmental (including climate change risks), social, corporate governance and business integrity matters;*
   2. *monitoring Clients’ performance and continued compliance with the applicable Client ESG Standards including their timely progress against the relevant Client ESG Action Plans, including periodic meetings and/or site visits (as warranted by the risks of such business) and using technical experts where necessary;*
   3. *identifying and recording any serious incidents involving Clients that result in loss of life, severe permanent injury or severe permanent damage to health, a material adverse environmental or social impact, or material breach of ESG Laws, including financial irregularities, and promote appropriate corrective actions; and*
   4. *ensuring integration of ESG management systems into their business so that they continue after any exit from the investment.*
2. Reporting

*ensuring regular (and no less than annual) reporting of environmental (including climate change), social and governance matters (and immediate reporting of any serious incidents, such as fatalities or breaches of ESG Laws) to the Board and to the Investors.*