

SUSTAINABILITY POLICY OF THE CFC

I. PURPOSE OF THE POLICY

The purpose of this Sustainability Policy is to convey CFC's commitment to sustainable development and Sustainable Development Goals as an integral part of its development mandate and impact management. CFC's mission in sustainable development is *"to contribute to poverty alleviation by strengthening the income-generating capacity of commodity producers and mitigating vulnerability to their economic well-being"*. The environmental and social sustainability of the activities supported by the CFC is central to fulfilling CFC's mission.

By following this Policy, the CFC seeks to enhance the sustainability of the commodity value chains and related markets. The CFC is committed to ensure that the projects supported by the Fund properly manage their environmental and social impact, so the costs of economic development do not fall disproportionately on those who are poor or vulnerable, the environment is not degraded in the process, and that renewable natural resources are managed sustainably.

In terms of economic and financial sustainability, avoidance and management of environmental, social and health and safety risks and impacts reflects sound practice of development impact finance. Sustainability policy serves to address specific challenges such as reduce waste, improve profitability and generate goodwill and positive benefits in the communities where a project operates.

This Sustainability Policy works by increasing the predictability, transparency, and accountability of CFC's operations and helps projects to better manage their environmental and social risks and impacts, improve their performance, and achieve sustained positive development outcomes in CFC's Member States.

This Policy guides the work of the CFC in achieving sustainable development impact from its operations supporting the Member Countries in the achievement of the SDGs. This Policy further provides the foundation of CFC's Social and Environmental Management System (SEMS) and provides guidance to CFC's internal processes in managing economic, social and environmental risks. The policy covers all activities and operations the CFC undertakes and supports, including, among others, direct and indirect financing of projects.

II. PRINCIPLES

The projects receiving CFC support shall produce the outcomes which are economically, financially, socially and environmentally sustainable. The CFC requires that the activities supported by the Fund maximize resource efficiency and consider social and environmental impact of the project in accordance with this Policy.

The CFC assesses the sustainability in its entirety, including potential risks and impacts of its proposed projects, for compliance with existing regulations of the CFC and consistency with SDGs in the context of:

- host country laws, rules and regulations as may be applicable to the operations envisioned in a specific project, and;
- subject the rules and regulations of the CFC, the primary standards prevailing in development finance, i.e. the International Finance Corporation (IFC) Environmental and Social Performance Standards and the associated World Bank Group Environmental Health and Safety Guidelines.

II.1 Economic and financial sustainability

Economic and financial sustainability provides the basis for sustainable socioeconomic impact of projects receiving CFC support to deliver their intended contribution to the core SDGs adopted by the CFC. Projects seeking support from the CFC should be able to demonstrate a clear path to economic and financial sustainability, demonstrating its capacity to maintain and expand its operations on completion of the project without continuing support by the CFC. This is based on the financing policy of the CFC aiming to maximize its development impact while preserving the capital of the Member Countries.

Adherence to IFC Performance Standards may also provide a solid base for the projects to find new opportunities to improve their financial performance. The implementation of good social and environmental practices is increasingly associated with a wide range of business benefits including access to markets, reduced staff turnover, cost efficiencies in production and enhanced stakeholder relations. By following these standards, the projects will be able to better identify opportunities to be more profitable on the long run, increasing the overall sustainability of their operations.

II.2 Social and Environmental sustainability and risk management

IFC Performance Standards evaluate environmental and social performance through risk and outcomes based approach. They offer full guidance on identifying social and environmental issues, helping projects to assess and decide on the actions needed to be taken based on the nature and scale of the activity of the project and commensurate with the potential level of risks and impacts. Central to these requirements is the application of mitigation measures to anticipate and avoid adverse impacts on workers, communities, and the environment.

While managing environmental and social risks and impacts in a manner consistent with the Performance Standards is the responsibility of the projects, the CFC seeks to ensure, through its due diligence, monitoring, and supervision efforts, that the activities it supports are consistent with positive social and environmental impact in Member Countries as evidenced in the framework of the Performance Standards. The CFC conducts environmental and social due diligence analysis as an important factor in the assessment of each project, and will determine the scope of the environmental and social conditions of CFC support.

III. OPERATIONAL IMPLEMENTATION

CFC implements this Policy by establishing internal environmental and social appraisal procedures assuring that all projects supported by the CFC duly contribute to the SDGs. This is an integral part of the CFC investment process, with the environmental and social appraisal aiming to identify all relevant risks and opportunities of the projects.

III.1 Minimum requirements.

The CFC does not finance operations that are not expected to reach economic and financial sustainability and meet its environmental and social requirements within a reasonable time frame. In certain cases, a project may not be in full compliance at the time of signing the legal agreement with the CFC, in which case approval of financing will be linked with the contractual obligation of achieving compliance within a designated timeframe. Persistent delays in meeting these requirements can lead to loss of financial support from the CFC.

The CFC establishes clear procedures to assure the projects supported by the Fund are complying with sustainability standards, including social and environmental sustainability. The CFC maintains and periodically reviews the Exclusion List, which defines the type of activities which shall not receive financial support from the CFC. The Exclusion List representing existing rules and regulations of the CFC is contained in Annex I.

III.2 Risk assessment

Projects meeting the essential requirements of the CFC undergo an assessment of the main potential social and environmental risks, and the main findings of the assessment are presented to the Consultative Committee (CC) as part of the Note by the Secretariat. The CC discusses the social and environmental risks of the project and indicates the main issues that should be addressed during the full due diligence analysis.

The CFC's environmental and social due diligence is commensurate with the level of environmental and social risk and impacts of each project. This analysis includes, when applicable:

- assessment of the specific set up of each project, identifying the main stakeholders involved and how they could be impacted by the project;
- full review of available documents, records, and information related to the environmental and social risks and impacts of the project. If gaps are identified, additional information is requested, when necessary;
- the use of several external resources, which help to identify the potential risks of the project;
- a site visit and interviews with the staff involved on the project and other relevant stakeholders;
- evaluation of the project's environmental and social management plans and its environmental and social performance in relation to the requirements of the CFC standards and guidelines as defined in this Policy;
- identification of gaps and any areas of non-compliance with the requirements of the CFC's Sustainability Policy.

The assessment of the project's social and environmental risks includes a categorization system using risk-based approach. CFC categorizes operations based on type, sector, scale and likely magnitude and significance of potential environmental and social risks and impacts of the projects. The categorization of risk scores as recommended by the International Labour Organization is contained in Annex II to this Policy.

III.3 Advising projects on the issues to be addressed

On the basis of social and environmental risk assessment, the CFC prepares a list of issues that a project should address, if applicable. These issues are categorized according by priority:

- Condition precedent: The project should address the issue before disbursement of CFC's funds. This condition is indicated in the project agreement. This type of covenant is used in cases where the project is breaching the law and could pose a considerable risk on society or on the environment.
- Undertaking in the loan agreement: The project shall address the issue during the loan agreement and is bound by a timeline. It needs to be monitored and reported on. This covenant is used if the risk is not immediate, but still should be addressed as it may result in negative impacts on people, the environment and consequently leading to fines and reputational risks for the project.
- Recommendation: The project is not bound through the loan agreement to address the issue. The recommendation, which is not a covenant, could help improve sustainability practices within the company. It does not pose an imminent risk on people or the environment.

IV. MONITORING

CFC maintains frequent and intensive contact regarding social and environmental aspects with its projects and, when applicable, requires annual social and environmental performance reports to assess the project's performance and progress on the action plans. Depending on the project's risk and impact profile, CFC determines the required intensity of the engagement and monitoring and may also

conduct monitoring visits and/or ask for independent external monitoring. CFC sees monitoring as an important opportunity to support projects in achieving their sustainability goals.

V. WORKING WITH PARTNER INSTITUTIONS

CFC is committed to work constructively with other development financial institution and with a variety of private and public sector entities. This could include exchanging information, collaborating in developing a mutual understanding of social and environmental risks, impacts and mitigation strategies, co-financing and engaging with the projects. CFC may partially or fully rely on trusted Partner institutions to operationalize the intentions of CFC's Sustainability Policy during due diligence, contracting and monitoring.

Annex I: CFC's Exclusion list

The CFC Exclusion List reflects the types of projects that CFC does not finance. The list is presented in the format consistent with the IFC Exclusion list.

The CFC does not finance projects which match one or more of the following exclusion rules:

- production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international bans, such as pharmaceuticals, pesticides/herbicides, ozone depleting substances, PCB's, wildlife or products regulated under CITES;
- production or trade in weapons and munitions;
- gambling, casinos and equivalent enterprises;
- production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where CFC considers the radioactive source to be trivial and/or adequately shielded;
- pose an international recognized public health hazard, such as production or trade in unbonded asbestos fibers. This does not apply to purchase and use of bonded asbestos cement sheeting where the asbestos content is less than 20%;
- exploit natural resources in a way that contravenes national or international law, such as drift net fishing in the marine environment using nets in excess of 2.5 km. in length.

A reasonableness test will be applied when the activities of the project company would have a significant development impact but circumstances of the country require adjustment to the Exclusion List.

All financial intermediaries supported by the CFC, must apply the following exclusions, in addition to CFC's Exclusion List:

- production or activities involving harmful or exploitative forms of forced labor¹/harmful child labor²;
- commercial logging operations in primary tropical moist forest;
- production or trade in wood or other forestry products other than from sustainably managed forests;
- production, trade, storage, or transport of significant volumes of hazardous chemicals, or commercial scale usage of hazardous chemicals. Hazardous chemicals include gasoline, kerosene, and other petroleum products;
- production or activities that impinge on the lands owned, or claimed under adjudication, by Indigenous Peoples, without following the applicable legislation including full documented consent of such peoples.

¹ Forced labor means all work or service, not voluntarily performed, that is extracted from an individual under threat of force or penalty.

² Harmful child labor means the employment of children that is economically exploitive, or is likely to be hazardous to, or to interfere with, the child's education, or to be harmful to the child's health, or physical, mental, spiritual, moral, or social development.

Annex II: Risk assessment categorization

The following categorization has been recommended by the ILO as best practice in the evaluation of environmental and social risks. The recommendation indicates the appropriate extent of environmental and social impact assessment, information disclosure and stakeholder engagement required.

Score	Risk
<25%	<p><u>High and insufficiently mitigated risk:</u></p> <ul style="list-style-type: none"> Due to the nature of its activities, scale and location, the project can have diverse and significant risks on people and environment. There is little awareness on risks and limited measures to manage them. There is limited or no involvement of relevant stakeholders.
25-50%	<p><u>High but sufficiently mitigated or medium but insufficiently mitigated risk:</u></p> <ul style="list-style-type: none"> Due to the nature of its activities, scale and location, the project can have diverse and significant risks on people and environment, however, the project is aware of the risks and impacts linked to its operations and scale, and is implementing measures to manage those risks, and monitors its performance and engages relevant stakeholders. The project 's impacts on people and environment are limited, site-specific and mitigation measures can be put in place, but the project is not aware and/or not managing these impacts, which could lead, in certain situations, to significant adverse effects on people and environment.
50-75%	<p><u>Medium risk:</u></p> <ul style="list-style-type: none"> Project's impacts are site-specific, limited and mitigation measures can be put in place. There is some awareness and some measures in place, but these might not consider all risks, are mainly reactive, there is no consistent monitoring, and little engagement of relevant stakeholders.
>75%	<p><u>Low risk:</u></p> <ul style="list-style-type: none"> Project's impacts are site-specific, limited and mitigation measures can be put in place. There are clear objectives and targets on social and environmental aspects and performance is periodically monitored. There are clear responsibilities for management and workers on social and environmental risks and impacts and adequate engagement of stakeholders.

For the projects with a risk score inferior to 25%, the CFC expects an independent Environmental and Social Impact Assessment (ESIA) study including an Environmental and Social Management Plan (ESMP). The ESMP normally describes all measures that need to be taken to avoid, mitigate, offset and monitor any adverse impacts and risks that have been identified by the ESIA. Furthermore, the project needs to have an appropriate monitoring system in place, which will enforce that the gaps identified will be addressed.