

KfW Development Bank

# »»» Sustainability Guideline

## Assessment and management of Environmental, Social, and Climate Aspects: Principles and Procedures

30 June 2023

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## Abbreviations

BMZ	Federal Ministry for Economic Co-operation and Development (Bundesministerium für Wirtschaftliche Zusammenarbeit und Entwicklung)
EHS	Environmental Health and Safety
ESAP	Environmental and Social Action Plan
ESDD	Environmental and Social Due Diligence
ESIA	Environmental and Social Impact Assessment
ESMF	Environmental and Social Management Framework
ESMP	Environmental and Social Management Plan
ESMS	Environmental and Social Management System
ESS	Environmental and Social Standards (of the World Bank)
EU	European Union
FC	Financial Cooperation
FI	Financial Intermediary
FPIC	Free, Prior, Informed Consent
FSC	Forest Stewardship Council
GHG	Green House Gas
GPN	Good Practice Note
HRIA	Human Rights Impact Assessment
IATI	International Aid Transparency Initiative
IFC	International Finance Corporation
ILO	International Labour Organization
IPCC	Intergovernmental Panel on Climate Change, IPCC
KfW	Kreditanstalt für Wiederaufbau
LRP	Livelihood Restoration Plan
NAP	National Adaptation Plan
NDC	Nationally Determined Contributions
NGO	Non-Governmental Organisation
PBA	Programme-Based Approaches
PBF	Policy Based Financing
PS	Performance Standards (of IFC)
RAP	Resettlement Action Plan
RBF	Results Based Financing
RPF	Resettlement Policy Framework
SDG	Sustainable Development Goals
UNCBD	United Nation Convention on Biological Biodiversity
UNCCD	United Nation Convention to Combat Desertification
UNFCCC	United Nation Framework Convention on Climate Change
VGGT	Voluntary guidelines on the responsible governance of tenure of land, fisheries and forests in the context of national food security
WB	World Bank
WCD	World Commission on Dams

# 1. Preamble

**1.1.** For more than five decades, the business area KfW Development Bank of the KfW Group (referred to hereinafter as KfW Development Bank) has financed measures in numerous areas to protect the environment and the climate and support social development. The principles of sustainable development are central to KfW Development Bank's funding activities, along with associated environmental and social sustainability and climate protection.

**1.2.** KfW Development Bank adheres to the KfW Group Sustainability Mission Statement<sup>1</sup> and to the Paris-compatible sector guidelines<sup>2</sup> to contribute to

- The sustainability strategy of the Federal Republic of Germany;
- The achievement of the 2030 Agenda together with the objectives of Sustainable Development Goals (SDGs); and
- The fulfilment of the Paris Climate Agreement.

This Guideline defines KfW Development Bank's implementation approach in line with this Mission Statement.

**1.3.** All the Financial Cooperation measures (referred to hereinafter as "FC-measures") financed by KfW Development Bank are therefore subject to a comprehensive and systematic assessment of environmental and social aspects as well as other relevant development aspects. Furthermore, KfW Development Bank aims to actively support the implementation of international human rights in its business operations through the existing instruments at its disposal and in line with KfW's human rights declaration<sup>3</sup>.

**1.4.** This Guideline applies to all forms of financing of KfW Development Bank.

## 2. Mission of KfW Development Bank

**2.1.** KfW Development Bank finances investments and related advisory services in developing and emerging countries on behalf of the German Federal Government, which are implemented by local partners as the executing agency. More specifically, KfW Development Bank uses funds from the federal budget, which are topped up by the bank's own funds, in order to support the construction of economically and socially beneficial infrastructure, the development of efficient financial sectors, and the implementation of environmental and climate protection measures as well as adaptation on climate change and programmes to preserve natural resources. The most important objective of KfW Development Bank's promotional activities is to help the Federal Government of Germany and its partner countries to achieve their overarching development goals.

**2.2.** The priority areas of KfW's activities in developing countries include social development, environmental and climate protection, adaptation to climate change, and the conservation of natural resources. Its work also encompasses FC-measures which make a crucial

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<sup>1</sup> [KfW Group Sustainability Mission Statement \(German version\)](#)

<sup>2</sup> [Paris-compatible sector guidelines](#)

<sup>3</sup> [Policy statement of KfW and its subsidiaries' on human rights and on its human rights strategy](#)

contribution to implementing international agreements on environmental and climate protection, and on the conservation of natural resources such as the United Nations Framework Convention on Climate Change (UNFCCC), the Convention on Biological Diversity (UNCBD) and the Convention to Combat Desertification (UNCCD). For FC-measures where the primary objective is not environmental, climate or resource protection, KfW Development Bank seeks to nevertheless incorporate climate and/or environmental outcomes or adaptation to climate change into the scope of the FC-measure.

### 3. Objectives of this Guideline

**3.1.** This Guideline describes principles and procedures to assess the environmental, social and climate aspects during the preparation and implementation of FC-measures financed by KfW Development Bank. In this context, this Guideline has the following objectives, in particular:

- to define a common binding framework to incorporate environmental, social and climate standards into the planning, appraisal, implementation, and monitoring of FC-measures; and
- to enhance transparency, predictability and accountability in the decision-making processes of the internal environmental and social due diligence (ESDD) and climate mainstreaming.

**3.2.** In line with the overall objective of promoting sustainability and avoiding adverse environmental, social and climate impacts and risks, KfW Development Bank aligns its FC-measures the following principles:

- to avoid, reduce or limit environmental pollution and environmental damage including climate-damaging emissions and pollution;
- to preserve and protect biodiversity and tropical rainforests and to sustainably manage natural resources;
- to consider probable and foreseeable impacts of climate change including utilising the potential to adapt to climate change. In this context climate change is understood as climate variability and long-term climate change;
- to avoid adverse impacts on the living conditions of communities, in particular indigenous peoples and other vulnerable groups, as well as to ensure the rights, living conditions and values of indigenous peoples;
- to avoid and minimise involuntary resettlement and forced eviction of people and their living space as well as to mitigate adverse social and economic impacts through changes in land use by reinstating the previous living conditions of the affected population;
- to ensure and support occupational health and safety as well as health protection in the workplace;
- to condemn forced labour and child labour, ban discrimination in respect of employment and occupation, and support the freedom of association and the right to collective bargaining;

- to avoid all forms of discrimination;
- to avoid negatively influencing existing conflict dynamics;
- to protect and preserve cultural heritage; and/or
- to support the executing agency in the management and monitoring of possible adverse environmental, social and climate impacts and risks associated with the implementation of the FC-measure.

**3.3.** KfW Development Bank only supports new projects that are in line with the “Exclusion List of KfW Group”<sup>4</sup>. Further, for FC-measures with financial intermediaries (FI) the IFC Exclusion List<sup>5</sup> applies complementary (see 4.8).

## 4. Environmental and Social Due Diligence of FC-measures

### 4.1. Objective and Core Elements

**4.1.1.** All funding activities of KfW Development Bank must be subject to an internal ESDD as defined in this Guideline.

**4.1.2.** The objective of the ESDD is to anticipate and appraise any foreseeable impacts and risks a FC-measure may have on environment and social factors (including human rights), and to identify, avoid and/ or minimise adverse impacts and risks to an acceptable level, or if unavoidable, to offset and compensate for these impacts and risks. In addition, the assessments should identify, monitor and manage any residual risks. Apart from assessing individual FC-measures, ESDDs are designed to demonstrate to partner countries the need to appraise the FC-measures, demonstrate the possibilities for environmentally and socially responsible FC-measures and raise awareness of ecologically and socially sustainable development approaches.

**4.1.3.** The ESDD is a core element of the appraisal procedure of KfW Development Bank. It is, first and foremost, intended as a management tool to steer and shape FC-measures over their entire life cycle (i.e., from preparation to completion). The ESDD and categorization of the FC-measures are performed under involvement of the environmental and social experts of KfW Development Bank.

**4.1.4.** The essential steps of the ESDD include:

- a preliminary appraisal (**screening/categorisation**) to evaluate the environmental and social risks of a FC-measure to determine if an in-depth ESDD is required;

and, if this is affirmed:

- the definition of the scope (**scoping**) to identify and assess the FC-measure's environmental and social impacts and risks more accurately in close cooperation with the executing agency; and

<sup>4</sup> [Exclusion List of KfW Group](#)

<sup>5</sup> [IFC Exclusion List – Version 2007](#) (for Financial Intermediaries of KfW Development Bank)

- the design and implementation of an **ESDD** in order to examine all or individual aspects of the FC-measure, including participatory approaches to involve project affected peoples and public disclosure in the partner country.

**4.1.5.** The steps mentioned above do not only apply to the project components financed directly by KfW Development Bank but consider the entire project. This applies also to the rehabilitation and/or expansion of existing facilities. Moreover, the ESDD considers relevant project alternatives that are available to reach the FC-measure objective. One possible outcome of an ESDD may be that the original FC-measure design or the location has to be modified.

## 4.2. Appraisal Standards

**4.2.1.** When assessing the environmental and social impacts of FC-measures, KfW Development Bank adheres to the KfW Group Sustainability Mission Statement and the specific developmental concepts and guidelines of the German federal government for development cooperation.

**4.2.2.** The foundation of the assessment of environmental and social impacts of a FC-measure is its compliance with relevant national law and legal requirements as well as the assessment requirements of KfW Development Bank. The KfW Development Bank assessment standards are the Environmental and Social Standards of the World Bank Group (i.e., for public agencies the Environmental and Social Standards (ESS) as well as relevant Operational Policies of the World Bank and the IFC Performance Standards (PS) for cooperation with the private sector, General and sector-specific Environmental, Health and Safety (EHS) Guidelines<sup>6</sup> as well as the Core Labour Standards of the International Labour Organization (ILO). Within the framework of donor harmonisation (Paris Declaration), KfW Development Bank can also use comparable standards of other development banks. This can be done through assessment of individual cases or in accordance with rules that have been agreed upon as part of the cooperation agreement. If the FC-measure involves funds related to the European Union (EU) or is financed in countries with EU membership prospects, the environmental and social standards of the EU apply, as far as they go beyond the above-mentioned standards and guidelines. The underlying evaluation standards in each case are disclosed to the executing agency.

**4.2.3.** Furthermore, the assessment takes into account the requirements of the human rights guidelines of the BMZ. This includes the acknowledged principle of free, prior, informed consent (FPIC) if an FC-measures affects the rights of indigenous peoples, the Voluntary guidelines on the responsible governance of tenure of land (VGGT)<sup>7</sup>, and the UN Basic Principles and Guidelines on Development-based Evictions and Displacements. When financing large dam projects, KfW Development Bank refers to the recommendations of the World Commission on Dams (WCD).

**4.2.4.** Deviations from individual sub-standards are only permitted in justified exceptional cases and must be documented accordingly. If the standards cannot be applied immediately by individual executing agencies, a concrete action plan<sup>8</sup> must be agreed or deviations avoided through exclusion of individual investment measures.

## 4.3. Screening and Categorisation of FC-measures

**4.3.1.** As part of the screening process, the planned FC-measure is appraised at an early stage in order to determine its relevance in terms of environmental and social impacts and risks. The screening process is designed to identify and appraise the type and scale of any adverse environmental and social impacts or risks that may arise from the planned FC-measure.

<sup>6</sup> For sectors without sector-specific EHS Guidelines, the respective Good Practice Notes (GPN) of the World Bank Group are applied.

<sup>7</sup> Voluntary guidelines on the responsible governance of tenure of land, fisheries and forests in the context of national food security

<sup>8</sup> E.g., an Environmental and Social Action Plan (ESAP)

The appraisal of the environmental and social impacts considers the whole project, even if KfW Development Bank is financing only a component of the project. The next step, once the relevance of such consequences or risks has been established, is to define the type and scope of additional studies which need to be conducted as part of FC-measure preparations.

**4.3.2.** All FC-measures are classified into one of the following four **categories “A”** (high risk), **“B+”** (substantial risk), **“B”** (moderate risk) or **“C”** (low risk), according to the relevance of their potentially adverse environmental and social impacts and risks.<sup>9</sup>

**4.3.3.** FC-measures are classified as **Category A** if it risks having diverse significant adverse impacts and risks on the environment or the social conditions of the affected population. Such impacts and risks may derive from the complex nature of the FC-measure, its scale (large to very large), the sensitivity of the location(s) of the FC-measure or from the potential impacts and risks being irreversible or unprecedented. Such impacts and risks may affect a larger area that is beyond the site of the facility under construction, the facility itself as well as any associated facilities or just the FC-measure area in a narrower sense. Therefore, a FC-measure will be classified as Category A if for example:

- adversely impacts important sites such as tropical forests, coral reefs, nature reserves, wetlands, natural/near-natural forests, and important cultural heritage sites;
- has significant transboundary impacts or is of relevance with respect to international treaties (such as conventions on international waste management regulations or on marine conservation, or agreements on the protection of biodiversity);
- leads to a high consumption of resources, in particular soil, land or water;
- is associated with high risks to human health or safety (e.g., industry or traffic facilities located adjacent to residential areas with considerable noise pollution and harmful emissions during construction and/or operation or handling hazardous substances);
- requires large scale resettlement or lead to a significant loss of livelihood; and/or
- is anticipated to have an adverse impact upon indigenous peoples.

An illustrative list of FC-measures that may be classified as Category A is attached as [Annex](#).

**4.3.4.** For **Category A** FC-measures, it is mandatory to analyse and appraise any adverse environmental and social effects as part of an independent Environmental and Social Impact Assessment (ESIA) study including an Environmental and Social Management Plan (ESMP). The ESMP should describe 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. It should also assign responsibilities for implementing such measures and list the costs involved. For Category A FC-measures, KfW Development Bank requires the executing agency to operate an appropriate monitoring system. If the FC-measures are run by private operators, they are required to have their own Environmental and Social Management System (ESMS) in place. Any such management system must comprise the following elements: (a) adequate organisational capacity and competency, (b) environmental and social assessment procedures, (c) management programmes, (d) specific environmental and social training measures, (e) well-structured relations with the target group, (f) monitoring, and (g) reporting procedures.

**4.3.5.** A FC-measure is classified as **Category B** if it potentially risks having adverse impacts and risks on the environment or the social conditions of those concerned, However, the impacts and risks tend to be less significant than those of Category A FC-measures and can usually be mitigated through standard, best available mitigation approaches (cf. [Annex](#)). Typically, the potential impacts and risks of Category B FC-measures are limited to a local area, are in most cases reversible and easier to mitigate through appropriate measures. For Category B FC-

<sup>9</sup> For FC-measures with financial intermediaries „FI/“ is added as a prefix. See section 4.8.



measures, the need for and the scope, the priorities and depth of an ESIA are determined through a case by case evaluation.

**4.3.6.** If it is expected that a Category B FC-measure has single significantly adverse environmental and social impacts or risks (**Category B+**), an ESIA and an ESMP as well as an ESMS adapted to these impacts and risks are required, as described under Category A.

**4.3.7.** FC-measures will be classified as **Category C** if they are expected to have no or only minor adverse environmental and social impacts or risks, and if the implementation and operation of the FC-measure does not require any particular protection, compensation or monitoring measures. Category C FC-measures usually do not require any additional analysis within the scope of this Guideline or any further ESDD procedures. Category C FC-measures should, however, be monitored for any relevant changes over their life cycle.

**4.3.8.** If a FC-measure is to be implemented in an area in which a critical human rights situation is known or expected, or if the project has effects that may result in conflicts that could significantly harm human rights (e.g., resource use conflicts), KfW Development Bank may require a detailed Human Rights Impact Assessment (HRIA) and additional measures aimed at ensuring that human rights are upheld.

#### **4.4. In-depth Environmental and Social Due Diligence (ESDD)**

**4.4.1.** Depending on the results of the screening, a decision is made regarding the extent of the in-depth assessments of possible adverse environmental and social impacts. An in-depth ESDD of adverse environmental and social impacts and risks is obligatory for FC-measures categorised as Category A, B+ and B. The executing agency or the funding recipient is responsible for providing the relevant information for the assessment of environmental and social impacts. If required, KfW Development Bank will request the information that is needed for the ESDD from the executing agency, and manages the execution of any further investigations. The recommendations of the ESIA are to be written in an action-oriented manner in an ESMP that also includes the required environmental and social monitoring by the executing agency.

**4.4.2.** An in-depth investigation of the possible adverse environmental and social impacts and risks of a FC-measure can, depending on the circumstances, take place as part of a feasibility study. In the event of significant adverse impacts and risks, further stand-alone studies and respective management plans are required. For FC-measures with significant adverse environmental and social impacts the studies should include the following information:

- identification and assessment of the adverse environmental and social impacts and risks of the FC-measure;
- avoidance or mitigation as well as sufficient protection and offset measures for the remaining impacts and risks;
- opportunities for the FC-measure to enhance positive environmentally and socially-relevant impacts (enhancement measures);
- management of environmental protection measures and social measures as well as occupational health and safety;
- monitoring of environmental and social aspects (development, effectiveness of mitigation measures) during implementation and operation of the FC-measure; and
- stakeholder engagement (see section. 4.9).

**4.4.3.** If there is a considerable loss of livelihood due to land taking or if project affected persons are impacted by involuntarily resettlement, a stand-alone Livelihood Restoration Plan

(LRP), a Resettlement Action Plan (RAP) or Resettlement Policy Framework (RPF) must be developed. This plan must be available at the time of the assessment of the FC-measure.

**4.4.4.** The assessment of a FC-measure also considers all necessary associated facilities required to establish and operate the FC-measure, or without which the FC-measure would not be viable (e.g., access roads, power lines for transmitting energy from a power station). If the FC-measure financed by KfW Development Bank is used as associated facility for another investment (e.g., power lines for transmitting energy from a wind farm), KfW Development Bank also assesses whether the other investment aligns with the requirements of KfW Development Bank and if subsequent improvements are possible. The impacts and risks as a result of the cumulative effects with other projects within the region (e.g., hydropower in one catchment and the downstream area) are also to be included in the assessment.

**4.4.5.** The executing agency, in consultation with KfW Development Bank, is responsible for the design and implementation of the required studies which are part of the preparation phase of the FC-measure. During the preparation, relevant bodies and agencies of the partner countries responsible for environmental and social issues are to be consulted. Where major mitigation and/or compensation measures are to be expected, the costs of such measures have to be taken into account in the economic feasibility study and included in the funding scheme.

**4.4.6.** If the ESDD reveals that the FC-measure may have adverse environmental and social impacts or risks which cannot be mitigated or modified through technical changes to an acceptable level and no adequate offset can be envisaged, the FC-measure will not be eligible for funding. Funding will also be denied if the FC-measure does not comply with the legal regulations of the partner country or with international agreements.

**4.4.7.** A conclusive appraisal of the FC-measure's environmental and social impacts will be made in the FC-measure appraisal report.

**4.4.8.** The conclusive appraisal must be based on the following basic principles:

- The main results are the identification of appropriate measures to adequately address the weaknesses identified during the appraisal in order to avoid, minimise or, where appropriate, offset adverse impacts.
- The FC-measure proposes solutions for appropriate protection measures which are commercially viable and socially acceptable.
- Local operators must have adequate technical skills to handle the proposed pollution control measures while ensuring proper operation of their facilities.
- Capacities, management systems and available funds for the implementation the protection measures identified to mitigate or offset adverse social consequences are to be confirmed. In that respect, it is necessary to determine the share of expenditure within in the framework of the KfW financing and the contribution of the executing agencies.

**4.4.9.** The implementation of the mitigation measures identified as a result of the ESDD to avoid or mitigate adverse impacts and risks, as well as – where required – offset measures, will be stipulated as binding for the executing agency in the financing agreements. KfW Development Bank requires regular reports on the implementation, and on corrective actions taken if measures have not been adequately implemented or if the objectives of these measures have not been achieved.

## **4.5. Specifics for FC-Measures with Programmatic Character**

**4.5.1.** If a FC-measure consists of separate smaller or larger sub-projects that will be identified, defined and prepared in more detail only after appraisal stage, categorisation at the

screening stage is based on considering the potential environmental and social risks associated with the project types or sector(s) in which these activities are planned. It is required to develop an Environmental and Social Management Framework (ESMF) for this type of FC-measures, which sets out the principles, rules, guidelines, and procedures to assess the environmental and social risks and impacts as well as the measures and plans to reduce, mitigate and/or offset adverse risks and impacts. If it is conceivable that physical resettlement and/or loss of livelihood will be caused as a result of one or several sub-projects of the FC-measure, a Resettlement Policy Framework (RPF) is usually prepared. No physical resettlement of people shall take place until a project-specific RAP has been developed and agreed by KfW Development Bank. The ESMF and/or the RPF are subject of the ESDD by KfW Development Bank. Their subsequent implementation of the sub-projects is defined within the financing agreement and monitored through reporting and site visits.

**4.5.2.** KfW Development Bank reserves the right to undertake an appraisal or approval of sub-projects in critical areas, on a case-by-case basis, such as for Category A projects.

#### **4.6. Specifics for Programme-Based Approaches (PBA): Results-Based-Finance (RBF) und Policy-Based-Finance (PBF)**

**4.6.1.** The financing of result- and programme-based approaches is characterised by the fact that funding is linked to the achievement of pre-agreed results, relevant for development or the development and implementation of (sector) policy reforms. Unlike to traditional investment projects, costs are not reimbursed but achievements of agreed outcomes are rewarded. In contrast to FC-measures with project or programme characteristics, PBF/RBF are broadly defined and may cover a wide range of measures, from specific project investments to general or sectoral policy reforms or basket financing. Therefore, depending on the structure of the measure, very different types of assessment studies may be needed. The categorisation is based on the potential environmental and social risks that could arise from the planned reforms or outcomes.

**4.6.2.** The analysis and assessment of the potential environmental and social impacts and risks are carried out in the context of the given country system and legislative framework of the sector. This may range from a specific ESIA for an infrastructure measure to a general ESDD of the current legal and institutional context, identifying potential risks and developing approaches to mitigate these risks.

#### **4.7. Specifics for Fast-Track Emergency Procedure (e.g., in the event of natural disasters, crises and conflicts)**

**4.7.1.** Fast-track emergency procedures cover generally emergency aid and/or removal of damages caused by natural disasters, crisis and/or conflict situations, which require immediate response and timely implementation. Hence, a procedure adapted to the specifics of the context is applied for the ESDD. In a shortened screening phase, the FC-measure is categorised as for all FC-measures (see 4.3). The screening determines also if an in-depth ESDD is required, and if so, what scope the ESDD shall have. If impacts and risks are considered moderate, the relevant E&S activities such as preparation of studies and management plans can be carried out in parallel with implementation – meeting both the urgency for fast-tracked procedures as well as the appraisal requirements.

#### **4.8. Specifics for the Financing with Financial Intermediaries (FI)**

**4.8.1.** The objective of the ESDD (as part of the due diligence) for FC-measures with FIs is to anticipate risks and prevent any potential adverse environmental and social impacts and risks that may arise from sub-loans granted by the FI and are refinanced by KfW Development Bank (in accordance with to WB ESS 9). The categorisation is carried out in accordance with section

4.3 with the pre-fix “FI”<sup>10</sup>, whereby in addition to the potential environmental and social impacts and risks of the sub-loans, the organisational capacity of the FIs to manage these impacts and risk also determines the categorisation.

**4.8.2.** The scope of the ESDD of the FI depends on:

- the significance and relevance of environmental and social risks associated with the planned funding area, and
- the FI's procedures and capacity to assess environmental and social concerns and to monitor loans in its existing portfolio.

The ESDD includes an appraisal of the FI's environmental and social management system (ESMS) in particular. As a rule, KfW Development Bank will not carry out an appraisal of the environmental and social impacts and risks of each individual sub-loans, but instead relies on this on the FI's ESMS and screening procedures (for exceptions see 4.8.5).

**4.8.3.** If KfW Development Bank holds shares in an FI e.g., in a fund, a bank or similar, everything under 4.8 applies to the entire FI-portfolio, and is not limited to the financing and the associated sub-loans.

**4.8.4.** The following is to be agreed with the FI:

- a) The development and implementation of an appropriate ESMS, commensurate with the envisaged financing. The ESMS shall meet the requirements of IFC PS 1/WB ESS 1 and include human resources management approaches in accordance with IFC PS 2/WB ESS 2. In addition, KfW Development Bank works with the partner institution towards the basic principles of “responsible finance”<sup>11</sup> in dealing with their clients;
- b) appropriate monitoring of the environmental and social risks in the FI's portfolio;
- c) implementation of a grievance mechanism; and
- d) regular reporting on the implementation and/or modifications of the ESMS as well as the environmental and social aspects of the FC-measure (line of credit) as appropriate.

With respect to the particular sub-loans:

- e) screening of all sub-loans against the Exclusion Lists for FIs of KfW Development Bank;<sup>12</sup>
- f) appraisal and categorisation of the sub-loans by the FI based on their environmental and social risks;
- g) all sub-loans must meet the national requirements and be assessed appropriately in accordance with the national environmental and social laws and regulations;
- h) all sub-loans must be in accordance with IFC PS/WB ESS 1 and 2 as well as WB ESS 10 and the ILO Core Labour Standards;
- i) all sub-loans with one or more of the following environmental and social risks: resettlement, adverse risks or impacts on Indigenous Peoples, significantly adverse impacts on the environment, community health and safety, labour and working conditions, biodiversity or cultural heritage must meet the requirements of the relevant IFC PS/WB ESS 3–8; and

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<sup>10</sup> When sub-loans of a FC-measures are likely to fall into different categories, the highest risks determine the category for the FC-measure as part of the precautionary principle

<sup>11</sup> [Responsible Finance – Guiding principle of KfW when developing financial systems \(2019\)](#)

<sup>12</sup> [Exclusion List of KfW Group](#) and [IFC Exclusion List – Version 2007](#) (for Financial Intermediaries of KfW Development Bank)

- j) the borrower of the sub-loan must be required to adequately inform the project affected persons about the impacts and risks of the measures that is financed through the sub-loan.

**4.8.5.** KfW Development Bank reserves the right to approve or reject any sub-loan in critical areas, e.g., sub-loans with potentially high environmental and social risks (Category A) .

**4.8.6.** If the support of a Microfinance institution is focused on a large number of very small sub-loans (e.g., refinancing complete loan portfolios), the assessment needs to determine whether the introduction of an ESMS is commensurate with the number of loans and the scale of the adverse environmental and social impacts and risks that are to be expected. In any event, it is crucial to examine the FI portfolio and its previous track record in dealing with environmental and social concerns.

**4.8.7.** Deviations from the agreements stipulated in section 4.8 are only permitted in justified exceptional cases and must be documented accordingly. If the agreements of individual FIs cannot be implemented immediately, a concrete action plan must be agreed or individual final loans be excluded.

## **4.9. Stakeholder Engagement and Grievance Management in FC-measures**

**4.9.1.** An important element of the ESDD planning and decision-making process is to involve the affected communities and keep the public in the partner country informed. Stakeholder Engagement e.g., in form of public hearings, are to be scheduled for the scoping phase of the ESIA process and for the presentation of the draft ESIA report, in order to consult with the affected persons and/or their community representatives, stakeholders, cooperatives or non-governmental organisations (NGOs). The executing agency is required to conduct a meaningful participation and consultation process that allows affected people and interested stakeholders to express their views and concerns on project risks, impacts and the proposed mitigation measures. At the same time, the process shall also enable the executing agency to take these views into account and react. For the sake of transparency, the executing agency is required to disclose relevant information and a non-technical summary on the environmental and social assessment of the FC-measure via appropriate media channels at an accessible location and in a timely, culturally appropriate manner. The whole process shall be comprehensive and be implemented throughout all phases of the FC-measure.

**4.9.2.** The executing agency is to establish a grievance process for the FC-measure for receiving and dealing with concerns and complaints of employees and members of the affected public. The procedure should be culturally appropriate and proportional to the FC-measure. Grievances and their processing and resolution are to be documented and form part of the reporting to KfW Development Bank.

# **5. Climate Mainstreaming of FC-measures**

## **5.1. Objectives and Core Elements**

**5.1.1.** All funding activities of KfW Development Bank must be subject to climate mainstreaming as defined in this Guideline.

**5.1.2.** The objective of climate mainstreaming is to consistently consider climate change from the early start of all FC-measures and therewith align KfW Development Bank's portfolio with

the challenges posed by climate change wherever it is reasonable and needed. These challenges relate to climate change mitigation (reducing green-house gas (GHG) emissions) and adapting to climate change (increasing the resilience of people, countries and economic systems, infrastructure and ecosystems to the negative impacts of climate change). The aim is to achieve positive climate-related effects, leverage potentials associated with climate change and reduce climate-related risks to the sustainability of FC-measures, whenever possible. Therefore, for each FC-measure, possible opportunities for climate mitigation and adaptation aspects are evaluated in the early project planning phase in order to identify all climate-related aspects at an early stage and consider them in the feasibility studies. Since feasibility studies, as well as the subsequent implementation are carried out by the project-executing agencies, it is also possible to support the planning and implementation capacity of the executing agency and partner countries so that they may further benefit from KfW Development Bank's experience in climate-related matters.

**5.1.3.** Climate mainstreaming does not only refer to the FC-measure financed by KfW Development Bank but considers the entire project and ideally also the overall activities of the executing agency. That means that if climate-related potentials or risks are identified, in particular the FC-measures and related project components are taken into account and suitable measures to leverage potentials and address risks are agreed with the executing agency.

**5.1.4.** When implementing climate mainstreaming of FC-measures, KfW Development Bank adheres to the KfW Group Sustainability Mission Statement and the specific developmental concepts and guidelines of the German federal government for development cooperation.

## **5.2. Climate Change Mitigation**

**5.2.1.** For climate Change Mitigation, the focus of the approach is on reducing GHG emissions and avoiding excessive GHG emissions. In order to slow down global climate change and to limit the increase of the average temperature in accordance with the Paris Agreement to well below 2°C – if possible 1.5°C – the emission of greenhouse gases needs to be reduced continuously until a net-zero greenhouse gas neutrality has been achieved. Therefore, climate protection focuses on the reduction, avoidance and sequestration of greenhouse gas emissions.

**5.2.2.** As a first step, an initial screening process is conducted as part of project preparation to evaluate

- if the Exclusion List<sup>13</sup> and Paris-compatible Sector Guidelines<sup>14</sup> of KfW Group are met. and
- which potentials might exist to reduce GHG emissions or further increase the reduction of GHG emissions (in case of FC-measures that specifically focus on mitigation). This may also relate to the potential to sequester carbon in soils and in vegetation.

**5.2.3.** Based on these early findings, the aspects that are relevant to climate change mitigation are incorporated into the feasibility study for the FC-measure. The feasibility study then describes and lays out how GHG emissions are expected to evolve in the project area/sector, whether the FC-measure will contribute to higher or lower GHG emissions, whether it is compatible with the country's climate strategy, e.g., the Nationally Determined Contributions (NDC) under the UN Framework Convention on Climate Change, and whether there are any potentials to reduce GHG even further. On this basis, options are developed for ways to reduce GHG and where applicable – considering the effectiveness in terms of development policy, and cost – these are integrated into the FC-measure. The calculation of the FC-measure related reduction of GHG, and, respectively, the calculation of the carbon footprint, is based on internationally recognized standards that are applied to the relevant sectors.

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<sup>13</sup> [Exclusion List of KfW Group](#)

<sup>14</sup> [Paris-compatible sector guidelines](#)

**5.2.4.** A risk assessment is conducted to examine whether the emissions caused by the FC-measure are proportionate or whether, from a mitigation perspective, implementation should not be carried out.

### **5.3. Adaptation to Climate Change**

**5.3.1.** Here, climate mainstreaming focuses on increasing the population's resilience to the effects of climate change as well as preventing risks generated by climate change.

**5.3.2.** An initial screening process as part of project preparation examines whether the area of implementation of the FC-measure is exposed to climate-related risks that would have an impact on the project concept, or whether such risks could emerge in the future. If the FC-measures involve the construction of long-term infrastructure or if there is a foreseeable risk that the FC-measure could exacerbate the effects of climate-related risks, particular attention is paid to this in the screening process.

**5.3.3.** This initial screening provides the basis for the development of the feasibility study for the FC-measure that contains the aspects relevant for adaptation. The analysis carried out during this process is based on the methodology for analysing climate risks described in the fifth expert report from the United Nations Intergovernmental Panel on Climate Change (IPCC). Based on this method, the first step is to examine what effects could be achieved through the FC-measure that would increase resilience to the impacts of climate change. This could be, for example, to reuse treated wastewater in case of drought or cultivate hardy crops. The next step is to analyse the climate-related risks to the success of the project. The risk assessment covers two key aspects:

- a) It is assessed whether the effects of climate change (such as an increase in extreme weather events) could endanger the sustainability of the FC-measure. In order to mitigate this risk, adequate measures are identified and implemented. These might include adapting the construction methods of the infrastructure, choosing an alternative location or providing accompanying financial support, e.g., by offering access to special insurance products. If no suitable adaptation measures can be identified, consideration must be given to not pursuing the FC-measure further.
- b) It will be ensured that the FC-measure does not exacerbate the effects of climate change on populations or ecosystems outside of the system that the FC-measure is targeting (e.g., building flood protection could increase the flood risk downstream). Again, appropriate countermeasures must be implemented as part of the FC-measure.

**5.3.4.** When designing the FC-measure, attention must be paid that the intended measures are compatible with the country's climate strategy, e.g., with the National Adaptation Plan (NAP) under the UN Framework Convention on Climate Change.

### **5.4. Specifics for FC-Measure with Programmatic Character**

**5.4.1.** If a FC-measure consists of separate smaller or larger individual projects that will be identified, defined and prepared in more detail after the appraisal stage, climate mainstreaming is mandatory for each individual project. The analysis of climate-related potentials, effects and risks is carried out for the individual projects of the FC-measure to the extent possible at appraisal stage. Otherwise, an agreement should be reached with the executing agency that individual appraisals will be carried out in line with the stipulations on climate mainstreaming. KfW Development Bank reserves the right to undertake an appraisal or approval of individual projects in critical areas on a case-by-case basis.

## 5.5. Specifics for Programme-Based Approaches (PBA): Results-Based-Finance (RBF) und Policy-Based-Finance (PBF)

**5.5.1.** The financing of results- and programme-based approaches is characterized by the fact that funding is linked to the achievement of pre-agreed results, relevant for development or the development and implementation of (sector) policy reforms. Analysis and evaluation of potential effects of the reforms on climate-related effects and risks is also part of climate mainstreaming.

## 5.6. Specifics for the Financing with Financial Intermediaries (FI)

**5.6.1.** The objective of climate mainstreaming for FC-measures with FIs is to assess climate related potentials, effects and risks and to prevent potential negative impacts from risks that may arise from sub-loans granted by the FI and are refinanced by KfW Development Bank. The analysis of climate-related aspects is conducted similarly to sections 5.2 and 5.3, but climate mainstreaming also examines the FI's capacity to deal with the effects of climate change. Depending on the FI's institutional capacity to adequately address adaptation and mitigation-related climate risks, additional accompanying measures to ensure the sustainable development of climate-related processes within the FI may be incorporated into the concept of the FC-measure.

**5.6.2.** KfW Development Bank reserves the right to approve or reject sub-loans in areas with a high level of climate risk. The FI has to apply the Exclusion List<sup>15</sup> and Paris-compatible Sector Guidelines<sup>16</sup> of KfW Group to all sub-loans refinanced by KfW Development Bank.

# 6. Sustainable Implementation of FC-measures

## 6.1. Monitoring and Reporting

**6.1.1.** In order to implement an effective monitoring of any adverse environmental, social and climate impacts and risks, the executing agency and/or the recipient of the funds have/has to agree to certain reporting and notification requirements and implement appropriate monitoring tools. Attention should be paid to the enforceability and practicability of the monitoring tools during construction, commissioning and operation and, if relevant, also during decommissioning. In order to monitor the environmental, social and climate impacts and risks of a FC-measure, it is particularly important to track the implementation of the agreed mitigation measures and monitoring procedures. If an ESMP has been developed, it will be used as a basis for monitoring. The same applies to an ESAP. If deemed necessary due to the complexity of the circumstances, KfW Development Bank may require – in consultation with the executing agency – an independent third-party monitoring.

**6.1.2.** The results of the implementation of resettlement and livelihood restoration activities are to be assessed as part of a separate completion audit.

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<sup>15</sup> [Exclusion List of KfW Group](#)

<sup>16</sup> [Paris-compatible sector guidelines](#)



## 6.2. Sustainable Procurement at KfW Development Bank

**6.2.1.** For the implementation of the individual components of a FC-measure, external consultants are usually commissioned with the planning and tendering process, and one or more contractors (e.g., supplier, construction firm, plant manufacturer) are commissioned to implement the measures. In order to take environmental and social aspects appropriately into account for the implementation of the FC-measures – in particular for FC-measures of Category “A” and “B+” – the selection of the commissioned companies and the solutions they propose are extremely important. The procurement process offers the following possibilities to influence E&S mainstreaming in the process:

- planning the tendering process – e.g., reducing environmental impacts through the specification of certain minimum and maximum values or focusing upon the environmental quality label (e.g., FSC - Forest Stewardship Council®);
- bidder pre-qualification – integration of project references and how the companies manage environmental and social as well as occupational health and safety aspects including relevant certifications (e.g., ISO 14001, ISO 45001);
- evaluation of the proposals – e.g., bonus system for eco-friendly systems / products;
- contractual arrangements – contractual embedding of relevant parameters, ILO core labour standards and occupational health and safety measures on the construction site including the definition of penalties in the event of non-compliance.

**6.2.2.** To support the executing agency with the implementation of sustainable procurement, KfW Development Bank provides, besides a toolbox for sustainable procurement,<sup>17</sup> also mandatory Standard Bidding Documents.<sup>18</sup> The toolbox includes explanations of methods and offers procedures that can be used in the individual procurement phases. The Standard Bidding Documents provided by KfW Development Bank include respective requirements and regulations for the tendering of consulting services, construction services and building contracts. If an executing agency may not be able to use these standard bidding documents due to regulatory restrictions, the executing agency must include respective requirements in the bidding documents that are used.<sup>19</sup>

## 6.3. Complaint Management at KfW Development Bank

**6.3.1.** The procedure for managing complaints at KfW Development Bank enables the public to express negative perceptions and criticism about FC-measures, i.e., also related to environmental and social sustainability aspects. Complaints can be filed to KfW Development Bank via a dedicated page on the KfW Development Bank website, where an online complaint form<sup>20</sup> in both German and English is available. Besides transparency, this procedure enables KfW Development Bank to treat complaints in a structured and categorised way, track them systematically and respond quickly. Further, it enables KfW Development Bank to make systematic use of project-related and process-related improvement potentials. Since 2020, KfW Development Bank has been publishing a complaint report<sup>21</sup> with an evaluation of the number of complaints by topic and country, as well as an overview of all admissible complaints received in the reporting year and the status of their processing.

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<sup>17</sup> [Toolbox Sustainable Procurement](#)

<sup>18</sup> [Standard Bidding Documents under guidelines and contracts](#)

<sup>19</sup> This requirement arises from the new procurement guideline of KfW Development Bank, valid since January 1<sup>st</sup>, 2019 for all FC-measures appraised thereafter.

<sup>20</sup> [Online Complaint Form](#)

<sup>21</sup> [Complaint Report KfW Development Bank](#)

## 7. Transparency at KfW Development Bank

**7.1.** KfW Development Bank uses the Project Database<sup>22</sup> in its Transparency Portal (only available in German) to disclose information of FC-measures with funding agreements signed from 1 January 2013. The database is updated monthly and contains information on FC-measure level. Since mid-2019, the environmental and social risk Category has been included, and from 2020 on, a short summary of the ESDD results will also be added.

**7.2.** Detailed information on all FC-measures that are implemented on behalf of BMZ is published monthly via BMZ in accordance with the standards of the International Aid Transparency Initiative (IATI). The machine-readable data can be accessed via the BMZ Transparency Portal<sup>23</sup>, the IATI registry<sup>24</sup>, the d-portal<sup>25</sup> and via GovData<sup>26</sup>.

## 8. Validity and review of this Guideline

**8.1.** This Guideline is binding for all FC-measures from 30 June 2023. It will be reviewed in 2024 if modifications or adjustments are required.

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<sup>22</sup> [Project database](#) (German only)

<sup>23</sup> [BMZ Transparency Portal](#)

<sup>24</sup> [IATI registry](#)

<sup>25</sup> [d-portal](#)

<sup>26</sup> [GovData](#)

# Annex

## **Illustrative list of FC-measures which may have potential significant adverse environmental and social impacts**

The following is an illustrative list of FC-measure types and measures that have the potential to cause significant adverse environmental and/or social impacts and can therefore be assigned to Category A and B+ or B (where adverse impacts are less significant and reversible).

1. Extensive and significant changes to the use of natural resources (e.g., changes in the use of soils as farmland, as forest or pasture land, for rural development, commercial timber production, etc.) as well as extensive land reclamation.
2. Extensive and significant changes to management methods in agriculture and fishery (e.g., introduction of new plant species, large-scale mechanisation, introduction of new fish species) and extensive logging.
3. Use of water resources (e.g., large dams and other impoundments, pumped-storage systems/power stations, irrigation and drainage projects, deep wells, water resource management and management of catchment areas, water supply, sea water desalination plants).
4. Infrastructure (e.g., roads, bridges, airports, ports, transmission lines, pipelines, railroad networks, other rail transport, tourism).
5. Energy generation (e.g., large wind farms, extensive solar parks, biomass plants, geothermal plants, thermal power stations).
6. Industrial activities (e.g., metallurgic works, timber processing plants, chemical factories, cement factories, refineries and petrochemical plants, agro-industries).
7. Use of geological resources, mining, etc. (e.g., mines, quarries, peat exploitation, oil and natural gas production).
8. Waste and wastewater management and removal (e.g., sewerage systems, wastewater treatment plants, landfills, treatment plants for domestic and hazardous waste).

Further classification criteria can be found in section 4.3.3 of the main text.

*NOTE: This is a translation of the German version. In case of divergence, the German version shall prevail.*

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**Editing**

Non-Financial Risk Management and Sustainability &  
Competence Centre Environmental and Social Sustainability &  
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Subject to change without notice  
Frankfurt am Main, as at: June 2023