

ENVIRONMENTAL AND SOCIAL RISK MANAGEMENT POLICY

Introduction

The Environmental and Social Risk Management (ESRM) Policy outlines DBN's overall approach and parameters for the provision of responsible financing.

The policy seeks to introduce a systematic approach to the management of relevant social and environmental issues, and the risks inherent in DBN's business processes and operations. DBN will ensure that adequate financial and human resources needed to implement this Policy are made available within the institution.

Policy Approach

1. Through this Policy, DBN puts in practice its commitment to integrating environmental and social considerations into decision-making processes relating to its business activities to avoid, minimize or reduce, or compensate for/offset risks and negative impacts.
2. DBN strives for positive development outcomes in the activities it supports. These activities include:
 - (a) Lines of credit to eligible PFIs for on-lending to eligible MSMEs and small corporates, including both investment and working capital loans;
 - (b) Providing credit guarantees, through a Credit Guarantee Facility on PFIs' loans made to MSMEs. This model is intended to overcome limitations in MSME access to finance, reduce volatility, and increase the contribution of the Nigerian financial sector to economic development.
3. DBN believes that an important component of achieving positive development outcomes is the environmental and social sustainability of these activities, which DBN expects to achieve through the application of this Policy.
4. DBN recognizes that in the delivery of its lending and investment, it may be exposed – through the PFIs – to the E&S risks associated with the business activities of the sub-borrowers and sub-projects they finance. Managing such risks means that DBN and the PFIs must develop and maintain adequate systems, procedures, and capacity for identifying, managing, and monitoring risks and impacts of sub-borrowers, and sub-projects commensurate with the types, scope, and nature of financing provided.
5. DBN, therefore, supports the capacity development of the PFIs to manage environmental and social risks. This is achieved primarily through the development and implementation of an Environmental and Social Management System (ESMS).

Objectives of the Environmental and Social Management System (ESMS) Policy

6. Specific objectives of the ESRM Policy are to:

- (a) Integrate ESRM considerations into the DBN's credit and investment decision-making processes.
- (b) Fully implement and comply with national requirements for E&S risk management in Nigeria, as well as DBN's bilateral and multilateral lenders and/or shareholders requirements.
- (c) Set out requirements for the PFIs for assessment and management of environmental and social risks and impacts associated with sub-borrowers and subprojects they finance.
- (d) Promote greater transparency and accountability on E&S issues internally and externally through disclosure and reporting.

Scope of Application

7. The requirements of this Policy apply to all financial products and services, as defined in paragraph 2 of this Policy, offered by DBN through PFIs Environmental and Social Risk Management System.

Summary for Public Disclosure

Introduction

8. The objective of the Development Bank of Nigeria (DBN) is to alleviate financing constraints faced by micro, small and medium enterprises (MSMEs) in Nigeria through the provision of wholesale financing and partial credit guarantees to eligible financial intermediaries for on-lending to an underserved MSME sector.

DBN aspires to be Nigeria's primary development finance institution; promoting growth and sustainability to this sector.

DBN recognizes that sustainable development is now widely accepted as the preferred development paradigm and that the financial sector has an important role to play by ensuring that financing resources are invested in a way that supports preservation of clean environment and the Earth's natural resources, as well as ensuring people, workers, and communities are not harmed but treated fairly and equitably.

DBN, therefore, considers environmental and social risk management (ESRM) to be an important part of its mandate for providing sustainable access to finance. As part of this mandate, DBN is committed to incorporating environmental and social (E&S) risk considerations into its decision making and lending processes in a manner that is aligned with the Nigerian legal requirements and international best practices.

DBN has adopted the Central Bank of Nigeria's Sustainable Banking Principles (Annex 1) that underscores the financial sector's responsibility to deliver positive developmental impact whilst protecting the communities and environment. The Principles are mandatory for implementation by the country's financial institutions and, among other inter-related commitments, require full integration of environmental and social considerations into decision-making processes relating to business activities financed to avoid, minimize, or offset negative impacts.

PURPOSE

9. This document outlines DBN's approach to the implementation of appropriate ESRM that aims to reduce E&S risks and impact in its portfolio. In particular, it is designed to support DBN's implementation of Principle 1 under the Central Bank of Nigeria Sustainable Banking Principles: "Our business activities: Environmental and Social Risk Management".

DBN is, therefore, committed to operationalizing and promoting an appropriate Environmental and Social Management System (ESMS) for itself, as well as for the financial institutions it on-lends to – in order to effectively assess and manage the E&S risk exposure associated with DBN's lending activities. The ESMS is a framework that integrates ESRM into PFIs overall procedures for lending and investment operations supported by DBN. Core components of the ESMS are as follows:

ESRM policy with clearly specified applicable E&S requirements and standards;

ESRM procedures for screening, identification, assessment, mitigation, monitoring and reporting of E&S risks; these procedures include record keeping, disclosure, and reporting;

Reporting to internal and external stakeholders on implementation;

Roles and responsibilities within the organizational structure for managing and monitoring E&S risks;

Resources for implementation such as organizational capacity, budget, training;

Guidance and tools: Practical resource materials for implementing ESRM provisions internally by DBN and among PFIs; these tools are developed and improved on an on-going basis.

The provisions in this document are applicable across DBN, and specifically to the departments directly involved in lending activities.

Environmental and Social Due Diligence and Supervision

INTRODUCTION:

Summary for Public Disclosure

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

11. DBN will categorize all its lending to PFIs into one of three categories (High, Medium, Low) based on exposure to risk and in accordance with the requirements of the NSBPs (Annex 3). DBN will take into consideration:

(a) Types of products and services provided by the PFI with DBN's support;

(b) Size and tenor of financing;

(c) The nature of the PFIs portfolio, including sectors and locations;

- (d) Organizational capacity and commitment of the PFIs to identify, assess and manage environmental and social risks and impacts of its DBN supported portfolio;
- (e) Any contextual risks, to the extent possible.

In particular, DBN will categorize PFIs that have substantial exposure to the activities on DBN's List of E&S Sensitive Activities, where supported by DBN financing, as High Risk. DBN will develop and maintain a regular program and procedures for supervision of its investments.

DBN will periodically review the adequacy and implementation effectiveness of the PFIs' ESMS, including the processes and the results of the E&S due diligence conducted by the PFIs on its sub-borrowers/sub-projects.

In addition, DBN will periodically review a sample of PFI' sub-borrowers/sub-projects, especially for business activities with significant E&S risks.

Applicable Requirements

12. As a condition of eligibility to receive financing from DBN, the PFIs will put in place and maintain an Environmental and Social Management System (ESMS) to identify, assess, manage, and monitor environmental and social risks and impacts associated with activities they finance, as commensurate with the nature and magnitude of such risks and impacts of the individual transaction and portfolio level. Such ESMS will be in compliance with the NSBPs. Where the PFI can demonstrate that it already has an ESMS at the time of DBN's due diligence, it will provide adequate documented evidence to that effect.

13. The PFI's ESMS should include the following elements:

- (a) Environmental and social policy
- (b) Clearly defined environmental and social risk identification, assessment, and management procedures
- (c) Organizational capacity and competency
- (d) Monitoring and review of E&S risks of individual transactions and the portfolio
- (e) External communications mechanism

The ESMS will be endorsed by the PFI's senior management and have adequate resources dedicated to its implementation.

14. The PFI's ESMS must include an E&S risk categorization system. The PFI's categorization procedures will incorporate the requirements of the NSBPs (Annex 3), and will consider the type, size, and tenor of financing; the nature of activities, including sectors and locations; and borrower's capacity to manage E&S risks. As part of this procedure, the PFI will be required to categorize activities on DBN's List of E&S Sensitive Activities (Annex 5), if any, as High Risks, or provide DBN with a justification for not doing so.

15. The PFI's ESMS, as part of the PFI's E&S policy, will clearly outline the following applicable requirements, depending on the level of risk associated with sub-borrowers and subprojects supported by DBN:

For the purposes of this Policy, portfolio means the portfolio of current and/ or proposed sub-projects financed by DBN to which this Policy applies, as set out in paragraph 7.

In particular, DBN will limit PFI review to Principle 1 under the Central Bank of Nigeria Sustainable Banking Principles: "Our business activities: Environmental and Social Risk Management". Where DBN is providing support to a PFI, and other multilateral or bilateral funding agencies/or shareholders will or have already provided financing to the same PFIs, DBN may agree on a common approach or to rely on the requirements of such other agencies project, including any ESMS already established by the PFI, provided that such requirements will enable the PFI to achieve objectives materially consistent with this Policy. A PFI may be required to enhance or supplement its ESMS, as deemed necessary by DBN. High-Risk categorization by PFIs may not be limited to activities on DBN's List of E&S Sensitive Activities.

- (a) The PFI will require that all sub-borrowers and sub-projects follow relevant environmental and social national and local laws and regulations.
- (b) The PFIs will comply with the requirements of the NSBPs on E&S risk management (Annex 1).
- (b) The PFI will not finance activities on the DBN Exclusion List (Annex 4).
- (d) Where DBN, as a result of its E&S due diligence process, is not satisfied that adequate capacity exists in a PFI for identifying, assessing, and managing risks and impacts, DBN may also exclude some or all of the activities on the DBN's List of E&S Sensitive Activities from its support to the PFI, until DBN is able to confirm that the PFI developed adequate capacity over time.
- (e) All sub-borrowers and sub-projects categorized by the PFI as High Risk, in accordance with the PFI's E&S categorization system as outlined in paragraph 15 of this Policy, will apply relevant requirements of the NSBPs and the World Bank Performance Standards. For these projects categorized both as High Risk and where there are affected communities, this will include a grievance mechanism prepared and implemented in accordance with the provisions of the Performance Standards.

16. Where necessary, DBN will require the PFIs to strengthen their ESMS as well as organizational capacity, responsibilities, and accountability for implementing the ESMS.

17. DBN will require PFI's maintain labour management procedures in line with national laws.

18. The PFI will prepare and submit to DBN an Annual E&S Report on the implementation of its ESMS (Annex that will include information on the environmental and social risk profile of its portfolio financed through DBN). The PFI will promptly notify DBN of any significant accidents or incidents associated with sub-borrowers or sub-projects.

Communications and Disclosure

19. DBN will communicate the provisions of this Policy internally at all levels of the institution. DBN will also maintain a process for external communications to deal with public inquiries and concerns related to E&S matters.

20. DBN is committed to reporting on its ESRM activities in accordance with the NSBPs obligations and the requirements of other investors. DBN will put in place a system for internal reporting to senior management on implementation of its ESMS. In addition, DBN will also seek to incorporate such reporting into its annual external publications.

World Bank Performance Standards can be found at

<http://go.worldbank.org/BZ9RCBSRBO>

21. DBN will require PFIs to publicly disclose summaries of E&S assessment reports for any sub-projects supported by DBN classified as High Risk according to PFIs' E&S risk categorization system unless prohibited by relevant national laws and regulations.

Changes to the ESRM Policy and New Policy Development

22. DBN's ESRM policies and procedures are reviewed and approved by senior management.

23. DBN will review the ESRM Policy on an annual basis to ensure its adequacy in line with any changes in DBN's operations, compliance with relevant national laws and alignment with funding bilateral or multilateral lender and investor requirements, as relevant. The review will also ensure that the overall approach to assessing and managing E&S risk remains relevant and aligns with ESRM national and international best practices and standards.

24. DBN may, as necessary, also develop complementary E&S policies, procedures and tools to address specific risks more comprehensively. Examples include detailed measures to address sector-specific (e.g. agriculture) or issue-specific (e.g. child and forced labour) risks.

25. Environmental and Social Risk Coordinator has the responsibility for proposing changes as needed to the ESRM policies and procedures or creating new policies and presenting these to DBN's senior management for approval.

ENVIRONMENTAL AND SOCIAL RISK MANAGEMENT PROCEDURES

Purpose

ESRM Procedures set out DBN's institutional arrangements and processes that aim to support the implementation of DBN's Environmental and Social Risk Management Policy. These procedures describe how DBN conducts its due diligence on investment activities under consideration, as well as its supervision on activities to which financing has been provided. The procedures identify the relevant functions and individuals involved in implementation.

These procedures are an integral part of DBN's risk management framework, are embedded in the overall investment screening and appraisal process, and form part of DBN's investment decision-making. DBN's ESRM Procedures are based on the principle of continuous improvement. These procedures allow for engagement with Participating Financial Institutions (PFIs) on the identified risks and impacts to improve their policies, systems, and processes for better E&S outcomes in their portfolios.

Applicability

ESRM procedures apply to all DBN's investment activities.

Revisions and Approval

DBN's ESRM procedures are approved by DBN's Senior Management. DBN reviews these procedures on an annual basis to ensure they reflect the scope and nature of DBN's lending activities, as well as requirements of bilateral and multilateral lenders and/or shareholders.

Structure of the ESRM Procedures

The ESRM Procedures are comprised of five distinct components, with each component representing a critical step of DBN's integrated ESRM approach (Figure 1). The structure of the procedures follows the typical chronology of events in the investment project cycle.

Visual flow for transaction-level decision-making process is provided in Annex 6.

DBN exclusion list

DBN Exclusion List outlines activities DBN will not support through the provision of financial products and services. The Exclusion List is compliant with Nigerian law and is aligned to the exclusion requirements of multilateral and bilateral lenders and/or shareholders that provide financing to DBN. The Exclusion List is reviewed annually to ensure compliance with national regulations in Nigeria and alignment to IFIs' lists of prohibited activities.

DBN will not finance any activity involving:

- Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements.
- Production or trade in pharmaceuticals, pesticides/herbicides, ozone-depleting substances, polychlorinated biphenyls (PCBs) subject to international phase-outs or bans.
- Trade in wildlife or wildlife products regulated under Convention on International Trade in Endangered Species (CITES).

- Production or trade in weapons and ammunition.
- Production or trade in alcoholic beverages (excluding beer and wine).
- Production or trade in tobacco.
- Pornography and/or prostitution.
- Gambling, casinos and equivalent enterprises.
- Racist and/or undemocratic and or neo-nazi media.
- Production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where DBN considers the radioactive source to be trivial and/or adequately shielded.
- Cross-border trade in waste and waste products, unless compliant with the Basel Convention and the underlying regulations.
- Production or trade in or use of unbonded asbestos fibres.
- Driftnet fishing in the marine environment using nets in excess of 2.5 km in length, electric shocks, or explosive materials.
- Production or trade in wood or other forestry products other than from sustainably managed forests.
- Production or activities involving forced labour or child labour
- Any activities involving significant degradation or conversion of natural and/or critical habitats and/or any activities in legally protected areas.
- Activities involving live animals for scientific and experimental purposes, including the breeding of these animals.
- Military or police equipment or infrastructure.

Footnotes

1 This does not apply to project sponsors who are not substantially involved in these activities. "Not substantially involved" means that the activity concerned is ancillary to a project sponsor's primary operations.

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

3 Employees may only be taken if they are at least 15 years old, as defined in the ILO Minimum Age Convention (C138, Art. 2), and ratified by Nigeria in 2002. Children under the age of 18 will not be employed in hazardous work. Children will not be employed in any manner 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.

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

5. Natural habitats are areas composed of viable assemblages of plant and/or animal species of largely native origin, and / or where human activity has not essentially modified an area's primary ecological functions and species composition.

6. Critical habitat is a subset of both natural and modified habitat that deserves particular attention. Critical habitat includes areas with high biodiversity value that meet the criteria of the World Conservation Union (IUCN) classification, including habitats of significant importance for required for critically endangered or endangered species as defined by the IUCN Red List of Threatened Species; habitats of significant importance for endemic or

restricted range species; habitats supporting globally significant concentrations of migratory species and /or congregatory species; areas with unique assemblages of species or which are associated with key evolutionary processes. Primary Forests or forests of High Conservation Value shall be considered Critical Habitats.

7. This includes High Conservation Value (HCV) forests. HCV areas do not directly correspond with definitions for modified, natural and critical habitat. The HCV Resource Network, an internationally-recognized group, provides information and support on the evolving usage of HCV to ensure a consistent approach. <https://www.hcvnetwork.org>

DBN list of E&S sensitive activities

The following environmentally and socially sensitive activities are subject to restrictions in PFI transactions financed by DBN, where DBN is not satisfied that adequate systems and capacity exists within the PFI to screen, assess, and manage the associated risks.

DBN will revise this list on a regular basis to ensure it meets the requirements of relevant Nigerian laws and regulations and those of bilateral and multilateral lenders and/or shareholders

Activities involving the risk of work performed by children;

Activities involving land acquisition and/or restrictions on land use resulting in involuntary resettlement or economic displacement.¹

Industrial-scale activities in or near critical habitats.²

Industrial-scale activities involving production,³ harvesting,⁴ or trade in wood or other forestry products from plantation and natural forests or wild fish and other aquatic species;

Industrial-scale production trade, storage, or transport of significant volumes of hazardous chemicals or commercial scale usage of hazardous chemicals. Hazardous chemicals include gasoline, kerosene, other petroleum products, textile dyes etc.

Production or activities that have adverse impacts, including relocation, on the lands, natural resources, or critical cultural heritage that are used as livelihoods by vulnerable and/or historically underserved traditional local communities.⁵

Activities involving significant adverse impacts on critical cultural heritage.⁶

Footnotes

1. Land acquisition and/or restrictions on land use may result in the physical displacement of people (involuntary resettlement) as well as their economic displacement (as loss of assets and/or means of livelihood, regardless of whether or not the affected people are physically displaced).

2. Critical habitat is a subset of both natural and modified habitat that deserves particular attention. Critical habitat includes areas with high biodiversity value that meet the criteria of the World Conservation Union (IUCN) classification, including habitats of significant importance for required for critically endangered or endangered species as defined by the IUCN Red List of Threatened Species; habitats of significant importance for endemic or restricted range species; habitats supporting globally significant concentrations of migratory species and/or congregatory species; areas with unique assemblages of species or which are associated with key evolutionary processes. Primary Forests or forests of High Conservation Value shall be considered Critical Habitats.

3. Production means cultivation or rearing of plants or animals, including annual and perennial crop farming, animal husbandry (including livestock), aquaculture, plantation forestry, etc.

4. Harvesting refers to productive activities that include extraction of these resources from natural ecosystems and habitats.

5. Vulnerable and/or historically underserved traditional local communities refers to those communities that may be most marginalized in the country context and lack access to resources and public services.

6. Critical cultural heritage consists of (i) the internationally recognized heritage of communities who use, or have used within living memory the cultural heritage for long-standing cultural purposes; and (ii) legally protected cultural heritage areas, including those proposed by host governments for such designation.