

Environmental and Social Management System Arrangement

November 2017

Sri Lanka: Additional Financing of Small and Medium-Sized Enterprises Line of Credit Project

ENVIRONMENTAL MANAGEMENT SYSTEM FRAMEWORK

A. INTRODUCTION

1. The proposed project is a line of credit to small and medium-sized enterprises (SMEs) in Sri Lanka via participating financial institutions (PFIs). The project also includes an attached technical assistance (TA) for export-oriented cluster development to develop Sri Lanka's next generation of SMEs, promoting business development skills, administering the auction, and developing a proposal for a national credit guarantee scheme.

2. The proposed project is built on previous donor-supported SME projects including Asian Development Bank's (ADB) Small and Medium Enterprise Regional Development Project (2008–2012), the World Bank's ongoing Small and Medium Enterprise Development Facility Project (effective 2011), and European Investment Bank's ongoing SME and Green Energy Global Loan (effective 2014). Common limitations of previous credit lines are that the targeted SMEs do not receive credit or that strict onlending requirements make the credit lines difficult for banks to disburse. To address these limitations, the proposed line of credit will include an innovative auction mechanism to (i) encourage efficient allocation of funds to those financial institutions with competitive advantages in lending to the targeted SMEs and (ii) allow PFIs to account for the higher costs of lending to targeted SMEs and to adjust their bids accordingly.

3. The growth and promotion of SMEs will not only yield increasing social and economic returns domestically, but also empower private sector integration to the global economy. According to the estimates of the Industry Survey of 2009 conducted by the Department of Census and Statistics, there are over 17,000 industries operating in Sri Lanka ranging from micro to small and medium to large scale industries.¹ The SME sector in Sri Lanka is a highly diversified sector which ranges from manufacturing to services with value addition in various degrees. The sector contributes significantly to the gross domestic product of the country with its strong influence on economic and social matters. On the environmental aspect, SMEs have their considerable impacts as well. For example, although waste from individual SMEs could be small, the cumulative environmental and health impacts on the society from the sector can be quite high—not only in terms of volume but the overall mix/diversity. Taking this into account, the National Environmental Act (NEA) tried to address the issues and impacts of industrial pollution. The Act contains standards and regulations involved in obtaining Environmental Protection Licenses (EPLs) for majority of industries to operate in Sri Lanka. Periodically, the national regulation is reviewed and revised.

4. In Sri Lanka, pollution mitigation is regulated by the regulations gazette under the National Environmental Act No. 47 of 1980 as amended by Act No. 56 of 1988 and 53 of 2000 for the industrial sector—be it small, medium, or large scale. The regulations are gazetted under Gazette Extraordinary No. 1533/16 dated 25 January 2008, for a variety of sectors involving manufacturing, construction, or services which need to obtain EPLs. The license is issued to an industry stipulating the standards and criteria under which it is allowed to discharge waste and other emission levels. The EPL issued to an industry is legally binding and violation of conditions in the license is a punishable offense under the NEA. EPLs are issued by the Central Environmental Authority or a designated body which can be local authorities for low polluting industries, Board of Investment (BOI) for BOI industries. In the northwestern province, where a

¹ Environmental guidelines for SMEs in Sri Lanka.

separate provincial environmental authority exists, the EPLs are issued by the North Western Environmental Authority (NWPEA).²

5. For financial intermediary loans, ADB requires financial intermediaries that onlend funds under ADB's financial intermediary loans to have, among other criteria, adequate policies, systems, and procedures to assess and monitor the economic, social, and environmental impacts of subprojects in accordance with parameters established by ADB for this purpose. In this regard, an environment and social management system (ESMS) is being required to guide both PFIs and ADB on project impacts and mitigation measures associated with it. The ESMS aims to (i) avoid, and when avoidance is not possible, minimize and mitigate adverse impacts of subprojects on the environment and affected people and (ii) maximize opportunities for environmental and social benefits. The ESMS provides a list of mitigation and compliance measures that the PFIs have to abide by. For ADB, the ESMS serves as a compliance checklist of environmental mitigation and social commitments that PFIs have to fulfill.

B. IMPLEMENTATION ARRANGEMENT OF THE PROJECT

6. The Ministry of Finance and Mass Media (MOF) will be the executing and implementing agency. MOF will establish a project management unit for implementation. A steering committee, which will include the Central Bank of Sri Lanka will provide senior guidance to the project. ADB will provide guidance, review, and monitoring on the progress of the subprojects through reports provided by the PFIs. The PFIs are the ten (10) local banks who have expressed their interest to participate in the auction. The same PFIs will ensure that potential environmental impacts from subborrowers' projects will be assessed and mitigated to ensure environmental integrity in the implementation of SME projects.

7. The PFI must ensure and enhance effective environmental management practices in all its activities, products, and services. In the selection of subprojects, PFIs will ensure that: (i) all subprojects are screened against the Prohibited Investment Activities List (PIAL) of the ADB Safeguard Policy Statement (SPS) (2009); (ii) all subprojects using ADB funds with significant environment and/or social impacts are reviewed and evaluated against safeguard requirements 1–3 of the ADB SPS (2009); (iii) all subprojects are reviewed and evaluated against the national laws, regulations, and standards on environment, health, safety, involuntary resettlement and land acquisition, indigenous peoples, and physical cultural resources; and (iv) all subprojects will undergo screening and categorization using a checklist as approved by ADB. To ensure that subprojects are properly screened, assessed, and monitored, PFIs should appoint a dedicated and qualified personnel for environmental and social assessments in their respective institutions.

C. PROCEDURES

8. The procedures below provide guidance to ADB in the selection of PFIs eligible to participate. They also provide a basis for the PFIs to develop their own set of procedures and requirements to avoid, minimize, mitigate, manage, and monitor subproject impacts, as appropriate, to the types and scales of subprojects in line with the type, sensitivity, and magnitude of the subprojects' impacts.

² Environmental guidelines for SMEs in Sri Lanka.

1. Screening and Categorization

a. PFI Screening and Classification

9. PFIs will be classified into two: class C and class B/C. ADB will determine which class the PFIs belong to through the process of due diligence with the use of (i) a categorization information sheet and a screening questionnaire and (ii) a review of their existing environmental management system (EMS) for its capacity to minimize, mitigate, manage, and monitor project impacts on the environment and the community. ADB also checks if the PFI's EMS has been previously used in a similar multilateral development bank financing and if the institutions have dedicated and qualified personnel to conduct environmental and social assessments.

10. Class C PFIs have incomplete safeguard systems and so must covenant to restrict their financing to a pre-agreed list of subprojects with minimal or no adverse impacts on the environment and social components (Appendix 1).

11. Class B/C PFIs have an EMS that ADB has approved. They may finance projects with site-specific environment impacts, but which can be mitigated.

12. All PFIs may refer to the indigenous peoples and involuntary resettlement checklists (Appendix 2) to ensure that subprojects exclude social safeguard impacts.

13. ADB's assessment of the PFIs is summarized in Appendix 3.

14. During implementation, class C PFIs can prepare and strengthen their EMS. Upon ADB's review of the EMS, ADB's South Asia Department, in consultation with Sustainable Development and Climate Change Department, may upgrade PFIs to class B/C. During fact finding, some class C PFIs indicated that this possibility to upgrade to class B/C may encourage them to invest in their EMS, which would be an ancillary benefit of the credit line.

b. Subproject Screening and Categorization

15. After each auction, the winning PFI will proceed with subproject loan applications. At an initial stage of identifying a subproject, the environmental safeguard manager (or other designated staff) will screen the subprojects in accordance with, among others, the following criteria:

- (i) The SMEs should comply with the government and ADB's environmental and social safeguard policies and not involve activities in ADB's PIAL; and
- (ii) The SMEs will not entail any activities that may have adverse environmental impact, which could be classified as category A pursuant to ADB SPS 2009.

16. At the subproject identification stage, the environmental and social safeguard manager (or other designated officer) will work with the subproject company to make a rapid assessment of the likely environmental and involuntary resettlement impacts and effects on indigenous peoples. Each category B/C bank has environmental assessment and social safeguard screening checklists designed to guide the team in the rapid assessment of impacts. The checklists are used to determine the significance of potential environmental and/or social impacts associated with the subproject.

17. Once the checklists and the verification work are completed by the PFI, the PFI will classify the subproject as one of the following categories:

- (i) **Category B.** A proposed project is classified as category B if its potential adverse environmental impacts are less adverse than those of category A projects. These impacts are site-specific, few if any of them are irreversible, and in most cases mitigation measures can be designed more readily than for category A projects. An initial environmental examination (IEE) is required. The PFI will check and monitor implementation of the environmental management plan enclosed in the IEEs, which contains the subprojects' potential impacts and accompanying mitigation measures.
- (ii) **Category C.** A proposed project is category C if it is likely to have minimal or no adverse environmental impacts. No environmental assessment is required although environmental implications need to be reviewed.

18. The subprojects' progress will be monitored and reported by PFIs in their annual periodic safeguards audit reports.

19. The following categories will be **outright rejected** in the list of eligible projects for financing: (i) category A for environment and (ii) category A or B for involuntary resettlement and indigenous peoples.

2. Due Diligence

20. The environmental and social safeguard manager of the PFI will undertake environmental and social due diligence. Due diligence will be done in the form of desk reviews and site visits. The subproject companies provide all requested information to the PFI through their regional offices and should be able to demonstrate responsiveness with regard to the applicable environmental and social safeguard requirements. A due diligence report will be prepared and the results of the due diligence will be reflected in the report to the subproject committee of the PFI, which will take into account these issues in approving the subproject.

21. All subproject investment agreements will contain appropriate environmental covenants requiring subprojects to be in compliance in all material respects with the applicable environmental safeguard requirements.

3. Monitoring and Reporting

22. After a subproject is approved, the designated PFI safeguards/compliance officer (i) communicates with the subproject and confirms periodically that the subproject company is undertaking the obligations of compliance with all applicable environmental safeguard requirements and (ii) the PFI will promptly report to ADB any actual or potential breach of the compliance requirements after becoming aware of it. The PFI, through its regional branches, will supervise and coordinate with the subproject company for the latter to address corrective actions, if any. These will be reflected in the monitoring reports that class B/C PFIs will submit annually to ADB.

23. Category B subprojects will be evaluated on an annual basis. The benchmark for performance will be the ongoing compliance against the applicable environmental safeguard requirements. The PFI will ensure that category B subproject companies prepare and submit an annual monitoring report (Appendix 4), an incident report following any environmental or safeguard occurrence (Appendix 5), and review and assess the subproject companies' performance on environmental safeguard issues.

24. Based on monitoring report submissions from the category B subproject companies, the PFI safeguards staff of class B/C PFIs will prepare an annual performance and monitoring report and submit it to the management of the PFI and ADB (Appendix 6).

D. CAPACITY

25. The PFIs are encouraged to achieve high standards of ESMS practice by recruiting staff or consultants with environmental management skills and through in-house or external training programs.³

26. In addition, ADB recommends that a separate function of the EMS compliance officer be established to assist the credit function in evaluating, monitoring, and managing all matters involving EMS risk.

27. By providing additional training, the participating FIs will ensure that their safeguard officers are qualified to play their roles and discharge their responsibilities.

³ The PFIs are encouraged to send representatives to participate in relevant training programs sponsored by ADB.

PERMITTED SUBPROJECTS FOR CLASS C PARTICIPATING FINANCIAL INSTITUTIONS
(Prohibited Investment Activities List still applies)

Fishing and aquaculture	<p>(i) Fishing: freshwater fishing (ii) Aquaculture</p> <p>No dynamite fishing allowed Marine and coastal fishing practices, such as large-scale pelagic drift net fishing and fine mesh net fishing, harmful to vulnerable and protected species in large numbers and damaging to marine biodiversity and habitats (ADB SPS [2009], PIAL).</p>
Manufacturing	<p>(i) Manufacture of beverages (wines cider and other fruit wines, beer malt, mineral waters and soft drinks) (ii) Manufacture of wearing apparel: Manufacture of knitted and crocheted apparel (knitted and crocheted hosiery, other knitted and crocheted apparel) (iii) Printing and reproduction of recorded media (a) Printing and service activities related to printing (not Pb-based) (b) Reproduction of recorded media (iv) Manufacture of computer, electronic and optical products (a) Assembly of computers and peripheral equipment (b) Assembly of communication equipment (c) Assembly of consumer electronics (v) Assembly of furniture (vi) Other Manufacturing (a) Manufacturing of jewelry, bijouteries and related articles (b) Manufacture of musical instruments (c) Manufacture of sports goods</p> <p>For other manufacturing:</p> <ul style="list-style-type: none"> Under item 33 of Prescribed Activities B, "Any industry which discharges 3 or more or less than 10 cubic meters of industrial processing wastewater per day is allowed". <p>For the manufacture of beverages:</p> <ul style="list-style-type: none"> Manufacturing of alcoholic beverage is outright a violation of the PIAL. However, sale of alcoholic beverage is allowed.
Electricity, gas, steam and air conditioning supply	<p>(i) Electricity, gas steam and air conditioning supply: steam and air conditioning supply</p> <ul style="list-style-type: none"> Only repair, maintenance and installation will be allowed as category C per the Government of Sri Lanka's Prescribed Activities List (List C, item 22) <p>(ii) Specialized construction activities</p> <p>(a) Electrical, plumbing and other construction installation activities (b) Building completion and finishing (plastering, joinery installation, floor and wall covering, painting and glazing, other building completion and finishing)</p>
Wholesale and retail trade, repair of motor vehicles and motorcycles	<p>(i) Wholesale and retail trade and repair of motor vehicles and motorcycles</p> <p>(a) Sale of motor cycles (b) Maintenance and repair of motor vehicles (c) Sale of motor vehicle parts and accessories (d) Sale, maintenance and repair of motorcycles and related parts and accessories</p> <p>(ii) Wholesale trade, except of motor vehicles and motorcycles</p> <p>(a) Wholesale on a fee or contract basis (b) Wholesale of agricultural raw materials and live animals: wholesale of grain, unmanufactured, seed and animal feeds; wholesale of flowers and plants</p>

	<p>(c) Wholesale of food, beverages (d) Wholesale of household goods (e) Wholesale of information and communication equipment (f) Wholesale of other machinery, equipment and supplies (g) Other specialized wholesale</p> <p>(iii) Retail trade, except of motor vehicles and motor vehicles</p> <ul style="list-style-type: none"> • Live animals should be classified as either agricultural livestock or domesticated animals. • Endangered and exotic species not allowed. • Any business which trades any wildlife or wildlife products regulated under the Convention on International Trade in Endangered Species of Wild Fauna and Flora (ADB SPS [2009], PIAL) will not be allowed. • Production of or trade in tobacco is not allowed under ADB PIAL, item 5 <p>(iv) Postal and courier activities</p>
Accommodation and food service activities	<p>(i) Accommodation (hotels) (ii) Food and beverage service activities (restaurants and bars)</p>
Information and communication	<p>(i) Publishing activities (ii) Motion picture, video and television program production, sound recording and music publishing activities (iii) Programming and broadcasting activities (iv) Telecommunications (v) Computer programming, consultancy, and related activities (vi) Information service activities</p>
Financial and insurance activities	<p>(i) Financial service activities, except insurance and pension funding (ii) Insurance, reinsurance and pension funding, except compulsory social security (iii) Activities auxiliary to financial services and insurance activities</p>
Real estate activities	Real estate activities
Professional scientific and technical activities	<p>(i) Legal and accounting activities (ii) Activities of head offices, management consultancy activities (iii) Architectural and engineering activities, technical testing and analysis (iv) Scientific research and development (v) Advertising and market research (vi) Other professional, scientific and technical activities (vii) Veterinary activities</p>
Administrative and support service activities	<p>(i) Rental and leasing activities</p> <p>(a) Renting and leasing of motor vehicles: renting and leasing of cars and light motor vehicles, renting and leasing of trucks</p> <p>(b) Renting and leasing of personal and household goods: renting and leasing of recreational and sports goods, renting of video tapes and disks, renting and leasing of other personal and household goods</p> <p>(c) Renting and leasing of other machinery, equipment and tangible goods: renting and leasing of agricultural machinery and equipment, renting and leasing of construction and civil engineering machinery and equipment, renting and leasing of office machinery and equipment (including computers), renting and leasing of water transport equipment, renting and leasing of air transport equipment, and renting and leasing of other machinery, equipment and tangible goods not elsewhere classified</p> <p>(d) Leasing of intellectual property and similar products, except copyrighted works</p>

	<ul style="list-style-type: none"> (ii) Employment activities <ul style="list-style-type: none"> (a) Activities of employment placement agencies (b) Temporary employment agencies (c) Other human resources provision (iii) Travel agency, tour operator reservation service and related activities <ul style="list-style-type: none"> (a) Travel agency and tour operator activities (b) Other reservation service and related activities (iv) Security and investigation activities <ul style="list-style-type: none"> (a) Private security activities (b) Security systems service activities (c) Investigation activities (v) Services to buildings and landscape activities <ul style="list-style-type: none"> (a) Combined facilities support activities (b) Cleaning activities: general cleaning of buildings, other buildings and industrial cleaning activities, other cleaning activities (c) Landscape service activities (vi) Office administrative, office support and other business support activities <ul style="list-style-type: none"> (a) Office administrative and support activities: combined office administrative service activities; photocopying, document preparation and other specialized office support activities (b) Activities of call centers (c) Organization of conventions and trade shows (d) Business support service activities not elsewhere classified: activities of collection agencies and credit bureaus, packaging activities, other business support service activities not elsewhere classified
Public administration Social security	<ul style="list-style-type: none"> Public administration and defense; compulsory and social security <ul style="list-style-type: none"> • Sale of alarm systems and other mechanisms to ensure household safety and security is allowed. • Production of or trade in weapons and munitions, including paramilitary materials, is not allowed.
Education	Education
Human health and social work activities	<ul style="list-style-type: none"> (i) Human health activities (ii) Residential care activities (iii) Other residential care activities
Arts, entertainment and recreation	<ul style="list-style-type: none"> (i) Creative, arts and entertainment activities (ii) Libraries, archives, museums and other cultural activities (iii) Sports activities and amusement and recreation activities
Other service activities	<ul style="list-style-type: none"> (i) Activities of membership organizations (ii) Repair of computers and personal and household goods (iii) Other personal service activities
Activities of households as employers; undifferentiated goods and services producing activities of households for own use	<ul style="list-style-type: none"> (i) Activities of households as employers of domestic personnel (ii) Undifferentiated goods and services producing activities of private households for own use
<p>Overall Conditional Criteria for Category C Projects</p> <ul style="list-style-type: none"> • Projects with construction/civil works activities will not be allowed • Projects which involve massive cutting of trees and destruction of vegetation will not be allowed • Projects which generate harmful emissions (GHGs, CFCs), hazardous and infectious wastes will not be allowed 	

- Projects belonging to the (PIAL under ADB SPS (2009) will not be allowed
- Projects belonging to the Government of Sri Lanka National Environment Act Prescribed List of Activities A and B will not be allowed

ADB = Asian Development Bank, PIAL = Prohibited Investment Activities List, SPS = Safeguard Policy Statement.

INDIGENOUS PEOPLES AND INVOLUNTARY RESETTLEMENT CHECKLISTS

A. Involuntary Resettlement Impact Categorization Checklist

Probable Involuntary Resettlement Effects	Yes	No	Not Known	Remarks
Involuntary Acquisition of Land				
1. Will there be land acquisition?				
2. Is the site for land acquisition known?				
3. Is the ownership status and current usage of land to be acquired known?				
4. Will easement be utilized within an existing Right of Way (ROW)?				
5. Will there be loss of shelter and residential land due to land acquisition?				
6. Will there be loss of agricultural and other productive assets due to land acquisition?				
7. Will there be losses of crops, trees, and fixed assets due to land acquisition?				
8. Will there be loss of businesses or enterprises due to land acquisition?				
9. Will there be loss of income sources and means of livelihoods due to land acquisition?				
Involuntary restrictions on land use or on access to legally designated parks and protected areas				
10. Will people lose access to natural resources, communal facilities and services?				
11. If land use is changed, will it have an adverse impact on social and economic activities?				
12. Will access to land and resources owned communally or by the state be restricted?				
Information on Displaced Persons:				
Any estimate of the likely number of persons that will be displaced by the Project?] Yes				[] No [
If yes, approximately how many? _____				
Are any of them poor, female-heads of households, or vulnerable to poverty risks?] Yes				[] No [
Are any displaced persons from indigenous or ethnic minority groups?] Yes				[] No [

Note: The project team may attach additional information on the project, as necessary.

B. Indigenous Peoples Impact Screening Checklist

KEY CONCERNS (Please provide elaborations on the Remarks column)	YES	NO	NOT KNOWN	Remarks
A. Indigenous Peoples Identification				
1. Are there socio-cultural groups present in or use the project area who may be considered as "tribes" (hill tribes, scheduled tribes, tribal peoples), "minorities" (ethnic or national minorities), or "indigenous communities" in the project area?				
2. Are there national or local laws or policies as well as anthropological researches/studies that consider these groups present in or using the project area as belonging to "ethnic minorities", scheduled tribes, tribal peoples, national minorities, or cultural communities?				
3. Do such groups self-identify as being part of a distinct social and cultural group?				
4. Do such groups maintain collective attachments to distinct habitats or ancestral territories and/or to the natural resources in these habitats and territories?				
5. Do such groups maintain cultural, economic, social, and political institutions distinct from the dominant society and culture?				
6. Do such groups speak a distinct language or dialect?				
7. Has such groups been historically, socially and economically marginalized, disempowered, excluded, and/or discriminated against?				
8. Are such groups represented as "Indigenous Peoples" or as "ethnic minorities" or "scheduled tribes" or "tribal populations" in any formal decision-making bodies at the national or local levels?				
B. Identification of Potential Impacts				
9. Will the project directly or indirectly benefit or target Indigenous Peoples?				
10. Will the project directly or indirectly affect Indigenous Peoples' traditional socio-cultural and belief practices? (e.g. child-rearing, health, education, arts, and governance)				
11. Will the project affect the livelihood systems of Indigenous Peoples? (e.g., food production system, natural resource management, crafts and trade, employment status)				

KEY CONCERNS (Please provide elaborations on the Remarks column)	YES	NO	NOT KNOWN	Remarks
12. Will the project be in an area (land or territory) occupied, owned, or used by Indigenous Peoples, and/or claimed as ancestral domain?				
C. Identification of Special Requirements <i>Will the project activities include:</i>				
13. Commercial development of the cultural resources and knowledge of Indigenous Peoples?				
14. Physical displacement from traditional or customary lands?				
15. Commercial development of natural resources (such as minerals, hydrocarbons, forests, water, hunting or fishing grounds) within customary lands under use that would impact the livelihoods or the cultural, ceremonial, spiritual uses that define the identity and community of Indigenous Peoples?				
16. Establishing legal recognition of rights to lands and territories that are traditionally owned or customarily used, occupied or claimed by indigenous peoples ?				
17. Acquisition of lands that are traditionally owned or customarily used, occupied or claimed by indigenous peoples?				

D. Anticipated Project Impacts on Indigenous Peoples		
Project Component/Activity/Output	Anticipated Positive Effect	Anticipated Negative Effect
1. List all project component / activity / outputs here	-- Indicate effects to IPS or put N/A as necessary	
2.		
3.		
4.		
5.		

Note: The project team may attach additional information on the project, as necessary.

ENVIRONMENTAL SAFEGUARDS ASSESSMENT

1. Asian Development Bank reviewed the safeguards procedures of all 10 banks to determine their screening capacities and potential ability to manage class B environmental projects. General observations are:

- (i) **Screening and categorization.** Of the 10 banks, screening and categorization activities take on a similar form where lending officers do the environmental assessment, conduct site inspection, recommend obtaining environmental protection licensing, and check for documentary completeness. Depending on the size and scale of the projects, the environmental assessment is referred to the environment and social management unit for expert review and endorsement to the management. Further, all the local banks interviewed have existing small and medium-sized enterprise (SME) centers in the different regions of the country. Various branches, especially those closest to the SME centers, coordinate with the latter for any concerns regarding loan applications that come to their offices.
- (ii) **Monitoring and reporting.** Since project origination is at the branch level, lending officers conduct annual site inspection visits, in time for the borrowing companies' renewal of their environment protection licenses. Inspection reports are then prepared and archived at the different branches. Again, depending on the size, scale and risk involved in the projects, regional officers or head office representatives conduct site inspection activities to ensure that the projects are compliant and the businesses operate without any encumbrances.
- (iii) **Grievance redress mechanism.** In the event that households or inhabitants of a community need to voice a complaint, the first and usual step taken is go to the local police. This is then taken to the business owner. Due to the confidentiality agreement between the bank and the business owners, the community does not have any knowledge which entity finances the business which may be the cause of their complaint. Moreover, since business owners are also inhabitants of the communities where their businesses are located, there are, more often than not, good relationships with the community. Of the 10 banks, no complaint cases have yet been brought to fore.

2. All of the participating financial institutions (PFIs) indicated that they finance projects belonging to both category B and C due to the diverse nature of their clients. Among the 10 PFIs, 6 indicated that they have their own environment and social management system, which makes them potential class B/C PFIs, namely: (i) Commercial Bank of Ceylon, (ii) Hatton National Bank, (iii) National Development Bank, (iv) People's Bank, (v) Sampath Bank and (vi) Nations Trust Bank.

3. During due diligence, the list was narrowed down to three banks, namely: (i) Commercial Bank of Ceylon, (ii) Hatton National Bank, and (iii) National Development Bank due to procedural completeness, previous experience with a similar multilateral development bank-financed project, and adequate staffing for their environment and social management unit, as indicated in the table below.

Bank	Assessment
Commercial Bank of Ceylon	<ul style="list-style-type: none"> • PFI has an existing EMS which has been used in a previous MDB SME line of credit under European Investment Bank. • Comprehensive procedures on screening, categorization, monitoring, and reporting. • Commercial Bank has a dedicated environment and social management unit to address all safeguard related matters. Commercial Bank's risk management unit is in charge of their social and environmental management system (SEMS) per a circular issued in the bank. All project proposals are subject to SEMS screening by the respective lending officers of the bank. Proposals are then routed through the social and environmental officer of the said unit.
Hatton National Bank	<ul style="list-style-type: none"> • PFI has an existing EMS, which was developed in 2012 with the help of DEG (a German development bank) and guided by policy of International Finance Corporation. • Comprehensive procedures contained in the EMS • Hatton National Bank has a dedicated environment and social management unit at their head office to address all safeguard related matters. Credit officers in their branches receive training on the skills and knowledge to properly assess different projects' environmental impacts. They are trained to prepare the due diligence documents and risk categorization using a tool developed internally at the bank. Depending on the risk/category, the project is referred to the ESMS coordinator for further evaluation.
National Development Bank	<ul style="list-style-type: none"> • PFI has an existing EMS, which was developed in 2008 and has undergone two updates, the latest of which was in November 2014. • Comprehensive procedures contained in the EMS. • National Development Bank has a dedicated environment and social management unit headed by a senior management personnel and consisting of a five-member cross-functional team representing both the Corporate Banking and Small and Medium Enterprise Departments.
DFCC Bank	<ul style="list-style-type: none"> • PFI developed their own ESMS which was approved by ADB in January 2017. • A sustainability unit has been established to formalize the bank's environment and social management compliance check. DFCC will extend the authority of the sustainability unit to their branch network. This has been documented in the ESMS.
Sampath Bank	<ul style="list-style-type: none"> • PFI developed their own ESMS in February, which was approved by ADB on March 2017. • A sustainability cell has been established to tend to the bank's safeguards-related transactions. Sampath is currently in the process of capacitating the cell's staff at the main office to later expand to the regional branches. The central cell will conduct periodic assessments on the work of regional staff. This has been documented in the ESMS.

ADB = Asian Development Bank, EMS = environmental management system, ESMS = environmental and social management system, LOC = line of credit, MDB = multilateral development bank, PFI = participating financial institution, SME = small and medium-sized enterprise.

Source: Asian Development Bank.

4. The other PFIs are still in the process of developing their own environmental management system (EMS). This process is expected to accelerate because all the local banks are signing a directive that will commit them to formulating their EMS.

5. **Suggestions to strengthen EMS implementation in class B/C PFIs.** In spite of the comprehensiveness of the three PFIs' EMS, the following points are suggested to strengthen their existing systems in the course of implementation:

- (i) **Checklists and other tools need to be institutionalized and standardized.** In the process of screening and categorization and to implement a standard for

environmental assessment, the checklists included in the EMS need to be better institutionalized, especially at the branch levels, who are at the forefront of project loan application submissions.

- (ii) **Monitoring reports need to be standardized and systematically collected.** Site inspection reports need to follow a template depending on what head office mandates. More so, these reports should also have a system of archiving in order to facilitate a more efficient recording the various projects' progress.

6. **Suggestions for the EMS formulation of class C PFIs.** In the formulation of an EMS, class C PFIs who wish to shift to class B/C PFIs, need to prioritize the following:

- (i) **Institutionalization of current practices.** Current practice, especially those that are effective and efficient, need to be institutionalized in a framework. Processes and procedures need to be organized, systematized, and laid out in a framework document which can be replicated across different branches and users.
- (ii) **Allot human resources for the environment and social management unit.** From the head office to the different regional branches, there need to be representative(s)/human resource allotted to address matters pertaining to environment and social safeguards. Despite the decentralized nature of the institution, this will help direct all safeguards related matters and concerns to a focal person(s) in the bank.

**SAMPLE FORMAT FOR ANNUAL MONITORING REPORT FOR SUBPROJECTS
CLASSIFIED AS CATEGORY B FOR ENVIRONMENT**

A. Subproject Name and Summary Information

1. Company name
2. Location (address, coordinates, land use, surrounding environmental feature)
3. Sector/subsector
4. Nature/type of business
5. Sub-loan amount
6. Purpose of subloan
7. Term of subloan

B. Relevant Environmental Permits or Compliance Certificates

1. Due diligence and/or audits undertaken during the year (list the number and type of investigations undertaken)
2. Non-conformances report (NCR) and corrective actions report (CAR) (Number of NCRs/CARs resulting from inspections / monitoring / audits etc. on approved subprojects)
3. Environmental incidents (any incidents provided by subborrowers, provide details)
4. Training delivered (awareness training on the project ESMS to the environmental staff of SPG and subproject companies)
5. Other environmental impacts including health and safety or social issues arising

Name and signature

Name:

Date:

Position:

Phone:

Signature:

Email:

ENVIRONMENTAL INCIDENT REPORT

An environmental incident is an unexpected event that may result in harm to the environment and requires some action to minimize the impact or restore the environment.

Business unit:			
Project name:			
Project number:			
Date of incident:		Time (24:00 format)	
Exact location of incident (see note 1):			
What type of activity the team engaged in when incident occurred:			
Who notified you of the incident? (e.g. employee, local authority, member of public)			
Name and phone number of complainant			
Nature and level of incident (see note 2)	Level <input type="checkbox"/> Major <input type="checkbox"/> Minor Nature <input type="checkbox"/> Chemical spill (including fuel) <input type="checkbox"/> Air emission <input type="checkbox"/> Noise complaint <input type="checkbox"/> Contaminated water discharged (not muddy water) <input type="checkbox"/> Erosion and sedimentation <input type="checkbox"/> Unauthorized removal of vegetation	<input type="checkbox"/> Other (specify)	
Description of the incident (see note 3)	Estimated quantity, volume or area involved (include unit of measure)		
Immediate actions taken and control measures implemented (see note 4)			
Proposed corrective (or preventive action) (see note 5)			
Follow up actions undertaken (see note 6)			

 Signature over Printed Name

Position

Date

GUIDANCE NOTES

NOTE 1: Exact location of the incident

Provide details of the location of the incident in relation to the project site. Include:

- (i) Name of the region
- (ii) Distances from environmentally sensitive areas (e.g. watercourses, conservation reserves)
- (iii) Landmarks, cross streets, etc.

NOTE 2: Major or minor incident?

A major incident has occurred if:

- (i) Material has escaped from site, or
- (ii) Clean-up requires external assistance (fire brigade or other emergency services)

If neither of these conditions apply, the incident is rated 'minor'

NOTE 3: Description of the project

Provide a brief, succinct, factual description of the incident including:

- (i) What happened leading up to the incident
- (ii) The material involved (if leak or spill)
- (iii) The estimated volume of spilled or leaked material
- (iv) The area of land or water affected

NOTE 4: Immediate actions and control measures

Describe the actions taken immediately to minimize the impact of the incident.

NOTE 5: Corrective and preventive action

Provide details of actions implemented to clean up and remediate the affected area and actions implemented to prevent the incident from occurring again. Raise a CAR if appropriate.

NOTE 6: Follow-up actions

- (i) Include any actions undertaken or proposed to be undertaken as a result of the incident (e.g. additional training, purchasing new plant, using alternative materials)
- (ii) Forward a copy of the incident report to the project management office following company management review.

**PERIODIC ENVIRONMENTAL PERFORMANCE REPORT FOR CLASS B/C PARTICIPATING
FINANCIAL INSTITUTIONS
(INDICATIVE FORMAT)**

Please provide responses to the questions below. Please include additional sheets or attachments as required to provide details on questions that have been answered Yes. The responsible PFI is required to submit the periodic performance report to ADB.

Name of organization	
Completed by (name and designation)	
Reporting period	

A. Progress on the Environment and Social Management System (EMS)

POLICIES AND PROCESSES	YES/NO	REMARKS
Have there been any updates to the ESMS or policy and procedures adopted by your organization during the reporting period?		If yes, please provide copy of the updates
Has senior management signed off on the updated policy/procedure?		If yes, please provide date and internal communication indicating the same
Please give details of any transactions rejected due to environment and/or social concerns		
Please state any difficulties and/or constraints related to the implementation of the ESMS		
Please give details of any material social and environmental issues associated with clients during the reporting period		
In case the existing ESMS is undergoing improvements, what is the action plan being implemented by your organization?		Please provide information or cite recommendation made by ADB's review mission to improve the ESMS and its implementation
CAPACITY	YES/NO	REMARKS
Have there been any changes to the staff tasked to implementing the ESMS?		If yes, please provide details
Please provide the name and contact information of the Environmental/Social Officer or Coordinator who has the overall responsibility for the implementation of ESMS	n/a	Please describe the training or learning activities the Environmental/Social Officer or Coordinator attended during the year
Please provide current staffing of other core ESMS persons in the organization involved with ESMS implementation.	n/a	Please describe the training provided to the ESMS persons and other team members during the year.
What was the budget allocated to the ESMS and its implementation during the year?	n/a	Please provide budget details including staff costs and training as well as any actual costs.
MONITORING	YES/NO	REMARKS
Have there been any accidents / litigation / complaints / regulatory notices and fines? Any		

CAPACITY	YES/NO	REMARKS
incidents of non-compliance with the applicable Environmental and Social Requirements? Any covenants/conditions imposed by the Bank to a subproject company as a result of any safeguard non-compliance?		

B. Summary of Subprojects that are Category B for Environment

No.	SME Company	Type of Business	Environmental Safeguard Updates	Compliance Status vis-à-vis ADB Safeguard Policies	Corrective Action Required of Participating Financial Institution to Ensure Compliance