

Environmental and Social Management Report

Emerging Energy Latin America Fund II, L.P.

I. Project Summary

- 1.1 **Borrower.** The purpose of Emerging Energy Latin America Fund II, L.P. (the “Fund” or the “Partnership”) is to make investments in a diversified portfolio of renewable energy infrastructure and clean technology companies in the Latin American and the Caribbean Region (the “Region” or LAC). The Fund will not take technology, start-up business model, or early stage development risk, and will seek to commit capital once such risks have been mitigated.
- 1.2 **Fund Management.** The Fund Manager is CleanTech Latin America Advisors, LLC, a Delaware limited liability company (the “Manager”) and affiliate of Emerging Energy and Environmental, LLC, a Connecticut limited liability company (“EEE”). EEE is an alternative investment firm based in Stamford, Connecticut, with an office in Mexico, Brazil and Panama. EEE specializes in clean and renewable energy, energy services and clean technologies, climate change and environment, and low-carbon infrastructure investments and advisory. The Manager will be responsible for providing management services to the Partnership. The Fund Manager will also be responsible for originating investment opportunities and will have primary responsibility for managing each element of the investment process.
- 1.3 **Fund Size and Investments.** The Fund size is targeted at approximately US\$150 million, which will be funded by an IDB senior loan of up to US\$30 million and US\$ 120 million in capital contributions. It is anticipated that the Fund will make between 8-12 investments, assuming the Fund reaches its target size. The Fund is targeted to multilateral institutions, other development banks and private equity investors. It is intended and expected that a majority participation in voting shares will be held by investors from IDB Member Countries. The Fund has already received equity commitments from IFC (US\$20 million), European Investment Bank (US\$ 18.1 million) and CAF (US\$10 million). The General Partner will invest 2% of the Fund up to a total of US\$3 million.
- 1.4 **Proposed Financing.** The proposed debt financing is in the form of an IDB secured senior loan to the Fund of up to US\$30 million not exceeding twenty percent of the Fund’s contributed capital after giving effect to the disbursement. The Loan’s disbursements will increase gradually consistent with the capital commitments from the investors and the Fund’s investment ramp up period. The Loan tenor is expected at up to 10 years including a commitment period consistent with the life and the investment period of the Fund and expected at 5-years.

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II. Project Status and Compliance

- 2.1 Based on Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), and given that the proposed transaction is considered a financial intermediary (FI), this operation is not categorized according to its potential environmental and social impacts and risks. However, given the Fund target investments in renewable energy infrastructure, it is probable that some of the individual transactions will fall into categories A and B under the IDB's classification system.
- 2.2 **Environmental and Social Due Diligence.** The environmental and social due diligence focused on (i) review of the Fund Manager's actual and pipeline portfolio to identify the potential range of Environmental, Social, Health and Safety (ESHS) and labor impacts and risks as well as any potential reputational risks associated with the Fund's investments; and (ii) an assessment of the Fund Manager's track record with Fund I, supported by the Multilateral Investment Fund (MIF), which required the development of an Environmental and Social Management System (ESMS), as well as its capacity to manage environmental and social aspects, specifically the Fund Manager's existing environmental and social policies, systems and processes, to ensure consistency with IDB safeguard policies and processes.
- 2.3 The Fund Manager has confirmed that it is in compliance with Directive B.2 (country laws and regulations) of IDB's Environmental and Safeguards Compliance Policy, complying with all applicable legal and regulatory environmental, social, health and safety, and labor laws and regulations including permits and authorizations.

III. Potential Environmental and Social Impacts and Risks of Fund Investments

- 3.1 The Fund will finance small renewable energy infrastructure and on growth stage energy services and clean technology companies. The Fund will invest in projects that have not yet been identified and thus, its potential environmental and social impacts cannot be assessed ex-ante. The impacts and risks will have to be identified, analyzed and managed on a project-by-project basis. The Fund's investments are likely to be in projects of small scale and in sectors that may have a full range (from minimal to significant) of environmental, social, health and safety and labor impacts and risks (direct, indirect or cumulative). The specific environmental and social impacts and risks will be those related to or caused by each specific project investment, depending on its characteristics, such as size, sector, and location.
- 3.2 More specifically, these may include, in addition to risks of pollution and contamination from the operations of the facilities required for these types of projects and labor management aspects including workers' health and safety, impacts and risks related to the insertion of the projects in certain specific

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contexts, including resettlement, impacts on indigenous peoples, impacts on natural habitats and other social and environmental impacts that could trigger other Bank's safeguard policies such as the ones on Involuntary Resettlement (OP-710), Indigenous Peoples (OP-765), and Disaster Risk Management (OP-704). Some of these projects are also likely to require public disclosure in accordance with both the Environmental and Safeguards Compliance Policy (OP-703) and Disclosure of Information Policy (OP-102). The preliminary review of the Fund's pipeline did not indicate the existence of impacts or risks that might pose reputation risks to the Bank or impair the viability of the Fund.

- 3.3 The investment strategy of the Fund has the following targets: (i) no more than 40% of the aggregate commitments in Brazil or in Mexico, (ii) no more than 30% of the aggregate commitments in any country in the Region other than Brazil and Mexico, (iii) 80% of its commitments in the renewable generation sectors (including wind, solar, small hydropower, biomass, biogas and geothermal), and (iv) 20% in emerging areas of energy services and clean technology including but not limited to waste-management, bioenergy, and biomass, hybrids, energy efficiency, demand side management and smart-grid, (v) maximum investments in any single company or project, including the original investment, plus any follow-on investments, will not exceed 15% of the aggregate commitments, and (vi) the Fund will not take technology, start-up business model, or early stage development risk, and will seek to commit capital once such risks have been mitigated. Table 1 details the expected sector diversification of the Fund:

Table 1: Investment Limits by Sector

Sector	Description	Portfolio Participation
Renewable energy	Renewable energy ("energy generation value chain"): small hydro, wind, solar, geothermal and biomass, in what is typically referred to as "grid-connected" renewable energy and distributed generation business models, such as in solar and other renewable energies	50%-60%
Energy Efficiency ("distributed generation solutions")	Energy services companies, industrial cogeneration, and demand-side management related service or product companies	10%-20%
Transportation Efficiency	Distribution and logistical infrastructure for clean fuels fleet vehicle conversion	10%-15%
Climate and Environment	Carbon finance and emissions credit projects upgrades and products	10%-20%

IV. Environmental and Social Management and Capacity

- 4.1 **Environmental and Social Management System.** The Fund has enhanced the

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ESMS that applied for CleanTech I operations, to include requirements from Fund II's new sponsors and potential lenders, and to allow for the flexibility and resources to address a wide range of environmental and social impacts, risks and mitigation and management schemes.

- 4.2 The enhanced ESMS is the current "state of the art" and it has the key elements for this type of systems such as: Screening of projects against an exclusion list, impact categorization of proposed projects, undertaking of due diligence and monitoring procedures commensurate to the levels of impacts, the structuring of projects so that they meet environmental requirements, and where necessary require corrective actions. The different elements of the enhanced ESMS follow IFC's Performance Standards, EIB's Statement on Environmental and Social Principles, as well as IDB's Environmental and Safeguards Compliance Policy.
- 4.3 As per the enhanced ESMS, the Fund will not invest in any projects related directly or indirectly in biofuels or bioliquids, and investments in the areas of biomass, energy efficiency and hydropower will need to comply with specific EIB's requirements. In addition, when a project is classified as a Category A operation, and for the first three proposed portfolio investments, the Environmental and Social Due Diligence Report (ESDD) needs to be delivered to the IFC and the EIB no later than 15 days before presentation of the proposed portfolio investment to the Investment Committee. However, the Fund Manager believes it is unlikely that the Fund will invest in any Category A projects.
- 4.4 The Fund believes that environmental and social investment enhancements will benefit the investment portfolio and increase the opportunity for superior returns. Thus the Fund will consider prior to making an investment and in monitoring a portfolio company environmental and social aspects such as carbon emissions, GHG emissions, climate change, ecosystem change, hazardous waste disposal/cleanup, toxic chemical use and disposal, child labor, discrimination, diversity, among others. By doing so, the Fund expects the investments to boost energy efficiency, reduce carbon footprint, sustain renewable resources, and mitigate negative environmental and social effects.
- 4.5 **Responsibilities and Resources.** Fund II's business model is based on having an efficient organization with a lean core staff structure and an efficient process for the investment process. For the enhanced ESMS administration, a structure has been created, with an Environmental Manager with overall responsibility for environmental and social issues; and an Environmental Coordinator who will manage and coordinate the environmental and social review process (together the "ESMS Team"). Responsibilities for environmental and social risk management have been assigned at the highest level, with Senior Managing Director, John Paul Moscarella, as the Environmental Manager and EEE's Senior Associate, Ramon Olivas, as the Environmental Coordinator. The ESMS Team with the support of the Fund Managers will make recommendations to the Fund's Investment Committee regarding the environmental and social eligibility of each proposed

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investment.

- 4.6 As the organizational structure of the Fund is lean, the Fund Manager envisions continuing reliance on external consultants to conduct EIAs and specialized environmental and social studies depending on the requirements of the specific potential investment. To that end, the Fund Manager will should prepare the Terms of Reference (ToR) to ensure that all the necessary due diligences are conducted.
- 4.7 **Track Record.** The Fund's ESMS Team includes experienced professionals in equity investments in renewable and clean technology industries in the region including experienced project finance and private equity specialists. They also have a good understanding and experience on the importance of managing the environmental and social aspects of the Fund's investments.
- 4.8 Through their experience in CleanTech I, they have managed investments in seven projects, which were all categorized as "B" under the old ESMS. Three of those projects are in the small hydro sector and the rest in compressed natural gas, starch and by-products, hybrid transportation and landfill gas to energy conversion. For most of Cleantech's I investments, the Fund Manager relied on EIA from external consultants due to the small size of the team and the technologies and specific situations presented by such projects. The Fund Manager accounts for only one project that could have potentially posed reputational risk, however it was effectively managed thanks to early detection of the issues during the due diligence process.
- 4.9 **Training.** EEE's staff responsible for the ESMS is required to attend environmental management courses especially designed for financial institutions or other equivalent training to educate staff regarding the relevance and need for procedures for managing ESHSL issues in the appraisal and supervision process. Such training should address the impact of ESHSL issues in investing, the reputational and project level risks involved, and how these can be managed to reduce risk and achieve compliance. EEE's Environmental Manager has attended the IIC/IDB environmental training course. The Fund is planning to continue sending staff responsible for the ESMS to these types of trainings.

V. Environmental and Social Requirements

- 5.1 This analysis concludes that Emerging Energy Latin America Fund II is formally in compliance with the requirements of the IDB loan, including the implementation of an ESMS and the capacity of its staff members. However, the following additional requirements shall be implemented:
 - a.) Investments made through the Fund supported with IDB's use of proceeds must comply with: (i) all ESHS and labor regulatory requirements applicable

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in the countries where the Facility and its projects are operational, (ii) List of Excluded Activities for NSG operations, (iii) the Fundamental Principles of Rights at Work (together referred to as the IDB Environmental and Social Requirements), and (iv) the IFC Performance Standards. Furthermore, the IDB will require the Fund to use all reasonable efforts to keep operational its enhanced ESMS and apply it to all investments to be financed with IDB funds.

- b.) For investments funded with proceeds from the IDB Loan, the Bank will provide non-objection to the Fund's investment on projects with the potential to generate significant environmental and social impacts (Category A). The Fund will formalize a process with the IDB as to obtain the Bank's non-objection for Category A projects, without regard to the transaction type or the total amount of the deal.
- c.) The enhanced ESMS needs to be approved by the relevant authority within the Fund's structure and any material changes to the same must be informed to the Bank.
- d.) The Fund Manager will provide appropriate environmental and social impact risk management training to designated individuals within the Fund.
- e.) The IDB will supervise the Environmental and Social Requirements of the Loan Agreement either by an in-house specialist or with external consultants, and require the Fund to present environmental and social compliance reports in form, content and frequency satisfactory to the IDB.