

Environmental and Social Management Report
Banco General
PN-L1056

I. Project Description

The proposed transaction entails up to US\$40 million long-term financing to Banco General (“BG”) that will be used to broaden the scope of BG’s key business areas to develop a “green” loan portfolio, particularly focusing on projects that result in energy savings/efficiency including energy and industrial technology and/or integrated waste management, water and wastewater treatment projects (the “Green Facility”). The proposed A/B senior unsecured loan would provide up to US\$20 million senior A loan with a tenor of up to seven years. Furthermore, subject to market demand, the IDB will try to syndicate approximately US\$20 million senior B loan on a best effort basis.

Banco General (BG) initiated operations in 1955 as a general licensed bank focusing on mortgage lending. In 1990, BG decided to expand its market and broaden its product base by becoming a universal bank. BG entered in the corporate and retail markets while developing its private banking business and starting an insurance company. In September 2007, BG merged with Banco Continental (BC) becoming the second largest commercial bank in Panama with total assets of US\$7,524 million, a loan portfolio of US\$5,149 million, a network of 63 branches in Panama, one general licensed bank in Costa Rica, 5 representative offices (in Guatemala, El Salvador, Nicaragua, Mexico and Colombia), 205 ATMs and 2693 employees, based on information as of June 2008. BG has traditionally been the leader in the mortgage segment. BG activities are divided in main part into “Corporate Loans” and “Consumer Loans”

II. Project Status and Compliance

The Environmental and Social Strategy for the Project was presented and approved on August 5, 2009 by the Environmental Safeguards Review team; no further action was required.

Based on Policy Directive B.13, and given this is a financial intermediary project, this operation was not categorized.

BG has confirmed that it is in compliance with Directive B.2 (country laws and regulations) of IDB 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, such as those required by The National Environmental Authority of Panama (ANAM).

III. Environmental and Social Impacts and Risks

a. Potential risks and impacts associated with BG’s portfolio

This Facility will target Small and Medium Enterprises (SMEs), middle corporates and small scale renewable energy projects. As of June 2009 BG’s Corporate Loans portfolio (which includes Small and Medium Enterprises) consisted of 12,323 operations with a total value of

US\$2.6 billion. This is broken down into the following sectors: Commercial (32%) Construction (23%), Industry (21%), Agriculture (5%), Services (3%) and Others (14%) (including mostly cash-secured loans). As of June 2009 BG's Middle Market Client portfolio had a combined value of US\$600 million, with operations in the above sectors as well as commercial mortgages.

There may be specific ESHS and labor impacts and risks related to investment in activities in certain sectors of BG's portfolio, for example related to trade and commerce of products and substances subject to bans and international phase outs (commerce); occupational health and safety (industry, construction); poor land use (construction); noise and air pollution (industry, construction), increased greenhouse gas emissions (energy), natural disasters, such as earthquakes, forest fires and land slides.

These risks are considered moderate and may be mitigated and managed with the implementation of an Environmental Management System. Given that the Facility will focus investment on projects that result in energy savings/efficiency including energy and industrial technology and/or integrated waste management, water and wastewater treatment projects, the potential risks may be further reduced with the introduction of robust eligibility criteria to ensure that each investment has a positive environmental impact.

Under this Facility, BG has indicated interest in opportunities for energy efficiency and renewable energy projects, which may include small scale hydro (to be restricted to under 10MW installed capacity and biofuels projects (which will be subjected to the IDB biofuels scorecard). Other possible projects may include investments in technological improvements and in water and waste management and efficiency; however the Facility is not limited to these sectors.

BG has stated that it has no financial liabilities in its existing portfolio, related to environmental, social and health and safety issues. BG has stated that it has no outstanding environmental, social, health and safety concerns, through involvement in projects, companies or activities considered unacceptable to the IDB that could potentially generate significant public opposition or concerns, for example due to inappropriate development location¹. BG has also stated that its finance application and analysis process is equitable, fair, and unbiased in terms of social factors (e.g. gender, age, ethnicity, or cultural heritage).

b. Risks associated with Banco General's facilities and human resources

The risks associated with BG facilities and operations, such as environmental liabilities in their offices due to asbestos, lead paint, etc. or BG employees having occupational health and safety problems due to working conditions (e.g. inadequate emergency preparedness, lack of fire exits, etc) are considered to be minimal. BG's head office is located in the city of Panama. BG has a Security Procedures Manual ("Manual"), which includes a disaster contingency plan which includes instructions for evacuations, bomb threat, fire protection, and natural disasters, and

¹ During the due diligence process for a previous Facility, BG disclosed involvement in the Changuinola I Hydroelectric Project). Further information is available in the ESMR for this Facility <http://www.iadb.org/projects/project.cfm?id=PN-L1035&lang=en>. BG has provided IDB with the required documentation and is as part of this Facility, and is working with the IDB on undertaking an Independent Assessment of its involvement in this project.

details key roles and responsibilities. BG has a designated officer to manage security issues (including fire and evacuation). The head office is inspected by the fire department on a yearly basis and each floor has the corresponding fire extinguishers. BG has begun conducting training its staff on evacuation procedures and conducting evacuation drills in line with Acuerdo 1 (2007) of the *Superintendencia de Bancos de Panamá* requirements with respect to fire regulations, including evacuation, and has a roll out plan for new emergency signage.

BG has a series of Human Resources Policies implemented through an established Human Resources Strategy covering organization culture, people, compensation practices, communication, leadership and operations. BG's Code of Ethic includes stated reference to respect, fair and equal treatment as a basis for labor relations. All employees receive a copy of the Code, which must be signed and BG provides training on the Code. All BG employees have a private health plan (medical, hospital and emergency). BG has stated that they have no material health issues (including legal claims) and do not have any materials employee or labor disputes. BG has also stated that its finance application and analysis process is equitable, fair, and unbiased in terms of social factors (e.g. gender, age, ethnicity, or cultural heritage).

IV. Environmental and Social Management

a. Environmental and Social Risk Management System

Since August 2008, BG has been working on developing an Environmental Management System ("EMS") within the guidelines set out by the International Finance Corporation and other multilateral institutions. The EMS will apply to all BG activities. To assist them in this process, BG contracted the support of EcoConsulta, S.A., a consulting firm based in Costa Rica, whose founders and partners are members of INCAE and founders of the EcoBanking Project. This consultancy is financed through technical assistance provided to BG by the German Investment and Development Company (DEG). EcoConsulta worked closely with BG's Risk Management Department to further develop the EMS, which is based on a set of procedures, questionnaires and tools that will be used to ensure its efficient and effective implementation.

From this effort, BG now has the following:

- An approved Environmental and Social Risk Policy
- A well document credit policy with accompanying procedures that fulfill the Bank's E&S risk needs, which is consistent with international best practices, as well as international partner expectations
- Specialized information collection and internal analysis forms and tools, which have been designed with inputs from front line users and various senior managers, and tested in pilots in the field;
- Two team members with significant training and knowledge capable of running the system (including attendance in the 2008 IIC-IDB Environmental Management for FIs workshop ;
- A specialist Environmental and Social Risk Officer
- A system that has proven successful in its pilot phase;
- Over 100 staff (risk, credit and accounts) and managers have received basic training in E&S risk and are now prepared to implement their respective roles.

BG's Environmental and Social Risk Policy was approved by its Management Committee in January 2009. This approval also included the Bank's exclusion list, and authorized the risk department to implement the pilot and roll out the system.

In March and April, the Bank began a pilot to test the protocols and work-flow, and assess how their internal systems would respond. They selected 7 cases that had triggered follow-up analysis based on their E&S policy and screening protocol. The internal report of the pilot results can be provided by BG upon request. The EMS consulting team found the following points after reviewing the case files, and related work product:

- The policy and screening protocol was able to capture accurately cases that required analysis;
- All cases were correctly categorized (according to Bank policy, and consistent with international organization classifications);
- Data collected by the credit officers (in BG's structure, data collection and preliminary review is in the hands of the credit officers) was of good to excellent quality using the instruments created by BG;
- The data provided the right inputs for more detailed analysis and internal discussion, and allowed the Bank teams to identify precisely which areas required additional information and attention;
- No delays were caused in the workflow for cases that did not trigger review;
- Cases that required analysis did not cause unnecessary delays, only the additional time required to address the issues found in the E&S analysis – some of which were complex;
- The Risk staff was able to find sources of information to accurately identify risks that required attention (through IFC guidelines and other sources). However, they found that they did not have the technical expertise to define the specific conditions to include in the clauses or contingencies. Interestingly, in a number of cases they found that the risks of interest to the Bank were covered by the companies' environmental impact assessment (EIA), but were not being adequately addressed by the companies. BG's response was to ensure through conditions and clauses that the specific improvements defined in the EIA were implemented. (Note: this is a very reasonable and correct approach in Panama, where the approved EIAs are effectively "operating permits.")
- With a number of minor adjustments, BG's process and instruments will function extremely well for their needs.

In their final report, the EMS Consulting Team detailed that the schedule for the full rollout of the system has been established. Although the system is ready to be implemented, the enthusiasm among BG officials has led to more areas being included than previously considered, and with rather low thresholds that trigger analysis. This combination means that the case load could potentially overload the risk department's capacity – particularly during the first few months – as this analysis is very new for their analysts and their decision processes. Regarding the aforementioned, BG has informed us that the implementation phase is proceeding well, within the following plan:

Bank Divisions	Training	Implementation	Status
2009			
Investment Banking (Energy)	July	August	Completed
Interim Construction Lending	July	August	Completed
Comercial Banking	August	September	Completed
Residential Mortgages	September	October	In process
Corporate Banking	October	November	
2010			
Rep. Office – México	January	February	
Subsidiary Bank – Costa Rica	March	April	
Rep. Office – Guatemala	May	June	
Rep. Office – Colombia	June	July	
Rep. Office – El Salv., Nica., Hon.	July	August	

BG now possesses the internal capability to accurately screen projects and companies for potential E&S risk. Their system is appropriate for the scope and magnitude of risks to which the Bank is exposed. Their E&S system is based on international best practices in screening and analysis. The system and corporate policy are consistent and mutually reinforcing. The information flows to (and from) the correct decision points (Board, Risk, Credit, and the various decision committees) are well considered. BG's ability to provide detailed technical follow up on cases is limited. However, their new Environmental and Social Risk Official began in June, 2009. This new position fills the only human resources gap in the BG system.

b. Green Line Procedure and Eligibility Criteria

BG's experience to date implementing an EMS will provide a great deal of valuable information about E&S risk in Panama, actors and institutional relationships, and provides the BG risk department with the potential to acquire significant knowledge and valuable experience to both improve risk management and develop new business areas, including the development of new green financial products, with this Facility. In order to develop a successful Green Line to BG, however, BG must now look beyond the identification of E&S risk, to the identification of E&S opportunity. This implies (a) the application of BG's existing EMS to the Green line and the development of specific procedures and eligibility criteria to ensure the identification and qualification of clients and projects that may be financed under the Facility. BG have confirmed that their approach is likely to include the inclusion of "triggers" for certain project types that may qualify for the Green Line within their EMS and more detailed checklists to confirm eligibility of those projects triggered.

c. Corporate Social Responsibility

BG has a demonstrated strong commitment to Corporate Social Responsibility ("CSR"). BG has a dedicated CSR Officer, reporting functionally to the Human Resources Manager, who is responsible for the program and prepares an annual Social Report. A CSR Committee meets on a monthly basis. The CSR program has a particular focus on social programs through its program "*Fundacion sus Buenos Vecinos*", which fights malnutrition in children, improves education in marginal areas, supports improved health care among poor communities, creates new

opportunities for people with disability and gives shelter to the elderly. In addition to providing financial support to this program, more than 1000 BG employees participate in a Volunteer Corp “*Vecinos en Accion*”. BG has been a member of the United Nations Global Compact since 2001².

The CSR program has recently expanded to include environmental issues pertaining to their facilities, including energy efficiency and recycling. BG is in the process of selecting a Consultant to assist them in further developing the environmental component of the CSR program. In addition one Bank officer has undertaken the UNEP-FI e-learning course on Corporate Eco-efficiency for Financial Institutions.

V. Environmental and Social Requirements

The Bank will require as part of the Loan Agreement that BG comply with all applicable Panamanian environmental, social, health and safety, and labor regulatory requirements, IDB List of Excluded Activities for Non-Sovereign-Guaranteed (NSG) operations, and with the Fundamental Principles of the Rights at Work.

Prior to financial closure, the IDB will require BG to present an Environmental, Social and Health and Safety (ESHS) Action Plan in form and substance satisfactory to the IDB that specifically includes a chronogram for the implementation of their newly approved EMS, to the use of proceeds, and development and implementation of a specific green line procedures and eligibility criteria to enable the identification of opportunities to finance the development of green projects such as those promoting energy efficiency, renewable energy, sustainable biofuels etc.

Operations to be funded under the activity of this facility will be subjected to the green line eligibility criteria and to that end. Only projects that have passed through the EMS and comply with the determined green line criteria will be eligible. Given that a timeframe of up to six months for developing and implementing the green line procedure and eligibility criteria is considered necessary, during this time BG shall inform the IDB of *any* potential investments being considered for financing under this Facility, and seek non-objection before a commitment to the investment is made. Once implemented, BG will be required to submit information regarding prospective category A and high risk Bs investments only being considered for financing under this Facility, to the IDB for non-objection before a commitment to the investment is made during the first 12 months of the Facility. After this time, IDBs *visto bueno* will be required only for category A operations.

The IDB will supervise the environmental and social aspects of the Loan Agreement either by an in-house specialist or with external consultants, and require BG to present environmental and social compliance reports in form, content and frequency satisfactory to the IDB.

² The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption. By doing so, business, as a primary agent driving globalization, can help ensure that markets, commerce, technology and finance advance in ways that benefit economies and societies everywhere.