

ENVIRONMENTAL & SOCIAL MANAGEMENT SYSTEM (ESMS) POLICY

1. Introduction

The socio-environmental dimension of business has become a structural and strategic element of successful companies due to the increasing awareness being created on this concept across the world. More focus on green products and support to green innovations and technologies are critical for the sustenance of the corporate and earth in the long run. An Environmental and Social Management System (ESMS) helps an organisation to integrate plans and standards into its core operations in order to anticipate environmental and social risks posed by its business activities and to avoid, minimize, and compensate for such impact. Lenders being channels of credit flow play a crucial role in promoting environmentally and socially sustainable projects.

Bank, as an environmentally aware and socially responsible institution, has had always strived to ensure that negative environmental and social impacts arising from the lending activity is nil/nominal. This policy reiterates the commitment of the Bank for the environmental and social causes while lending through Bank’s outlets, including IFSC Banking Unit (IBU).

2. Definitions & interpretations

- a) **“ESMS / SEMS”** means Environmental & Social Management System
- b) **“ESMS Policy”** means Environmental & Social Management System Policy of Bank.
- c) **"Coal Related Sub-Project"** means (a) the development or expansion of coal-fired power plants, coal mines, transportation assets used exclusively for coal, or infrastructure assets exclusively dedicated to support coal mines and coal transportation, or (b) any Person that, in the prior financial year, (i) generated more than 20 percent of its energy generation from coal-fired power plants, (ii) had an annual coal production of 10 million tons or more (iii) had installed coal-fired capacity of 5,000MW or more;
- d) **“Green Loans”** means loans to any borrower that meets the criteria detailed below. Green financing shall cover financial arrangements by way of credit facilities (fund-based and non-fund based) investments and derivative products that are targeted at projects / products which are environmentally sustainable and consider the aspects of climate changes. The eligibility criteria to classify as Green Loans are

	Eligibility Criteria
Energy Efficiency	Measures implemented aimed to acquire, replace, redesign or refurbish equipment, systems and / or contracting services/products to decrease in at least 15% the energy consumption for every unit of service output of the corporate entity. This includes utilizing waste energy and any other measure to improve the efficiency of energy use (or reducing specific energy consumption) of the system directly affected by the sub-loan based on minimum requirements. Coal related projects are not eligible.

Renewable Energy	Installation or construction measure implemented by the borrower and aimed at investing into fixed assets that enable generation or productive use of electricity, heat, cooling and any other form of energy from renewable resources, including but not limited to solar, wind, hydro, biomass, geothermal and tidal.
Green Buildings	A loan to a borrower will be accepted as a Green Buildings loan subject to receiving an eligible Green Building certification and proof of an improvement in Energy Efficiency of at least 20%.
Special Climate	This include projects related to climate smart agri, water management, waste management, recycling plants and other categories which aim at reducing emissions, reducing the consumption of water, conservation of energy or are related to any other activity which has a direct positive benefit related to the climate and environment

- e) "**E&S Officer**" means a senior officer of Bank to be responsible for administration and oversight of the E&S Management System.
- f) "**E&S Consultant**" is the external agencies to be engaged by Bank to undertake E&S categorization and to undertake E&S Due diligence of high-risk business activities to be financed by Bank.
- g) "**E&S Performance Standards**" shall mean national / international benchmark for identifying and managing environmental and social risks. The Environmental and Social performance standards defined by IFC being one of the best benchmarks adopted worldwide, Bank has adopted the IFC performance standards for managing environmental and social risks as E&S Performance Standards, along with the National benchmarks.

3. Objective

The objective statements articulated in the ESMS policy cover Bank's commitment in integrating environmental and social considerations into its lending activities. The broad objectives of ESMS policy are provided below.

- a) Incorporate environmental and social risk considerations into financing activities as part of credit risk governance.
- b) Set strategic environmental and social objectives. As part of the same, Bank shall endeavour to finance green loans.
- c) Bank shall not extend loans, which falls under the exclusion list, unless otherwise specified therein.
- d) Ensuring that clients establish environmental and social requirements verifying with national environmental and social regulations and international standards such as E&S Performance Standards.
- e) As appropriate, communicate environmental and social expectations to all staff, clients and other external stakeholders. Put in place a proper mechanism to enable stakeholders to raise queries / complaints with regard to ESM practices through Bank's website.
- f) Commit to improving the overall environmental and social performance of its portfolio through enhanced risk management.
- g) Commit to continually building capacity of its staff to identify environmental and social risks, including E&S and investment officers / analysts.

4. Scope

- a) The guidelines specified in this policy shall be applicable for all lending operations of Bank, including loans extended through IBU. However, as a priority, Corporate & Institutional Banking (CIB) & Commercial Banking exposures will be subjected to the application of policy in the initial years.
- b) Bank will desist from extending finance, irrespective of the amount, for activities coming under exclusion list and specified against item 5.a unless otherwise permitted therein.
- c) Other borrowers (other than those coming under exclusion list) falling under the purview of ESMS policy, will be classified into any one of the E&S categories viz., Category A, B or C. Categorisation of borrowers under A, B & C shall be to ascertain the appropriate E&S Due Diligence as mentioned under 'Risk Categorisation' (item 5.b) and subsequent processes to be followed for minimising E&S risks.
- d) An indicative list of activities / sectors that fall into Category A / B / C are provided below. Further, based on the borrower's E&S practices, preparedness to address various environmental and social impact in association with the project, clearances from authorities for the project etc, overall E&S risk categorization may improve compared to the classification mentioned in the table.

Category	Sectors (Indicative)
Category A	Road, Highways, Ports, Cement, Power (including large renewables), Mining & Quarrying, Petroleum, Large scale Plantations, Integrated Iron and steel plants, Railway, Shipping, Harbour, Terminals, Pipelines, Pulp & paper, Tanneries, Large Hospital chains, Large Metallurgical, Large scale Chemical.
Category B	General Manufacturing, Large service sector companies, Hospitality, Pharma, Standalone hospitals, Small / Midsized construction, Craft paper, Leather (without tannery).
Category C	All sectors not classified as Category A or Category B.

- e) In respect of borrowers that continue under Category A, even after considering the E&S risk mitigation steps available, may be required to consent for disclosures, if any, as per the requirement of Bank.
- f) No new Coal Related Sub-Project Exposure will be financed. Coal Related Sub-Project Exposure for this purpose shall be limited to on-balance sheet gross loan assets (including equity) and off-balance sheet commitments and contingencies of the Company, with an initial maturity of more than 36 months (and any extensions or refinancing thereof) to any Person (together with their subsidiaries) undertaking or comprising a Coal-Related Sub-project.
- g) Exposure fully secured by Bank's deposits and Derivative facilities (example: Hedging facility) is exempted from the purview of the ESMS policy.

5. ESMS Framework

ESMS framework covers the entire credit life cycle. The procedures to be complied in each stage of the life cycle, from an E&S perspective are provided below.

a. Screening against Exclusion List

The following activities will not be financed by Bank.

- a) Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements, or subject to international bans, such as pharmaceuticals, pesticides/herbicides, ozone depleting substances, PCB's, wildlife or products regulated under CITES.
- b) Production or trade in unbonded asbestos fibers. This does not apply to purchase and use of bonded asbestos cement sheeting where the asbestos content is less than 20%.
- c) Drift net fishing in the marine environment using nets in excess of 2.5 km. in length.
- d) Gambling, casinos and equivalent enterprises¹
- e) Production or trade in weapons and munitions¹
- f) Production or trade in alcoholic beverages (excluding beer and wine)¹
- g) Production or trade in tobacco¹
- h) Production or trade in radioactive materials. This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any equipment where Bank considers the radioactive source to be trivial and/or adequately shielded.
- i) Production or activities involving harmful or exploitative forms of forced labour²/harmful child labour³.
- j) Commercial logging operations and sand mining activities (Dredging of rivers to improve the ecosystem and reduce the impact of flood etc shall not fall under the purview of sand mining).
- k) Production or trade in wood or other forestry products other than from sustainably managed forests.
- l) New thermal coal mines or significant expansion of existing mines.
- m) New coal-fired power plants or expansion of existing plants
- n) Oil & Gas exploration activities.

When lending to microfinance activities, the Exclusion List will include the following too:

- o Production, trade, storage, or transport of significant volumes of hazardous chemicals, or commercial scale usage of hazardous chemicals. Hazardous chemicals include gasoline, kerosene, and other petroleum products.

¹ This does not apply to borrower's who are not substantially involved in these activities. "Not substantially involved" means that the activity concerned is ancillary to a borrower's primary operations (i.e., revenue from that particular activity is less than 20% of the total annual revenue of the borrower).

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

³ Harmful child labour means the employment of children that is economically exploitative, 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.

- o Production or activities that impinge on the lands owned, or claimed under adjudication, by Indigenous Peoples, without full documented consent of such peoples.

Bank shall not normally extend loans for activities which fall under the exclusion list. However, the Bank may extend credit facilities for the following activities in the exclusion list, on an exception basis, subject to the condition that aggregate exposure to such sectors does not exceed 3% of total loans & advances of the Bank.

1. Production or trade in alcoholic beverages (excluding beer and wine).
2. Production or trade in tobacco.
3. Gambling, casinos, and equivalent enterprises.

b. Risk Categorization

Bank, directly or with the help of E&S Consultants, shall analyse the environmental and social risks involved in financing projects and corporate loans coming under the purview of this policy and assign an E&S category to the enterprise / project under one of the three E&S categories, as mentioned below.

Classification	Standard definition	Risk indicators
Category A	Potential significant adverse environmental or social risks or impact that are diverse, irreversible, or unprecedented	A business activity that may include a) involuntary resettlement, b) risk of adverse impact on Indigenous Peoples, c) significant risks to or impact on the environment, community health and safety, biodiversity, cultural heritage or d) significant Occupational Health and Safety risks
Category B	Limited adverse environmental or social risks or impact that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures; or includes a very limited number of business activities with potential significant adverse environmental or social risks or impact that are diverse, irreversible, or unprecedented.	A business activity that will generally have smaller E&S footprint.
Category C	Predominantly minimal or no adverse environmental or social impact.	Minimal business processes, limited to medium size workforce, limited brick and mortar assets.

For identifying the E&S risks and to categorise the enterprise into any one of the E&S categories, Bank may call for legible copies of the Environmental & Social documents as deemed necessary. This may *inter alia* include, as applicable:

- i. the regulatory Environmental Impact Assessment (EIA) studies or similar assessments as may have been conducted by the company/ other agencies from time to time.
- ii. environmental licenses, approvals, clearances as applicable to the company and/or the business activity to be financed, viz, the environmental clearance, forest clearance, CRZ approvals, NGT or court orders, consent to establish/operate, etc. or NOCs and approvals from various national, state level and local authorities such as the municipality, panchayat, local urban bodies, factories inspectorate, labour commissioner, fire department, appropriate water authority etc.;

- iii. returns and reports filed with regulatory and statutory authorities such as environmental fees, cess, fines, compensation etc. or contributions towards employee social security funds, CSR, POSH returns, periodic monitoring report submitted to environment department / ministries or pollution control board or other such environment authority;
- iv. documents such as environment management plans, resettlement action plan, biodiversity action plan, chemical spill management plan, fire safety plan, disaster management plan, emergency response plan or any such plan as required by relevant statutory or regulatory authority or required by law.
- v. health and safety incidents data such as loss-time injuries, fatalities, fire incidents, strikes and lockouts.
- vi. information or clarification on any adverse media publication or civil society protests etc.

c. E&S Due Diligence (ESDD) and Corrective actions

Bank shall conduct an Onsite E&S due diligence on all or some of the environmental and social matters for project / long term loans in respect of high-risk borrowers and select medium risk borrowers. This onsite E&S due diligence may be conducted by the Bank officials or Bank may appoint an external agency ('Bank's E&S consultants") on its behalf, depending on the complexity of the proposal and/ or the potential E&S risks associated with the financing.

The scope of E&S due diligence shall be to cover the critical E&S risks, understand how the same are being managed by the borrower and the residual risks which are not capable of cure. It shall also include compliance of National E&S laws and E&S performance standards.

On completion of ESDD, an Environmental and Social (corrective) Action Plan (ESAP) shall be formulated which shall define the corrective measures to be taken by the borrower in the stipulated time and the Bank may specify the same as Condition of Commitment (COC) or Disbursement (COD).

d. Periodic monitoring of E&S covenants and Actions on default / delinquencies

The monitoring of the E&S risks shall be guided by the following principles

1. risk associated with region / industry / and client group,
2. categorization of the account - Category A / Category B / Category C and,
3. reputational risk due to public complaints, adverse media or E&S incidents.

6. External Communications Mechanism (ECM)

Bank's ECM procedure is intended to provide a means for the public to submit queries or concerns related to Bank's Environmental & Social Policy and/ or projects financed by Bank. Bank will respond to these in a timely manner, if the enquiries are found genuine by ascertaining the circumstances behind such enquiries and after proper identification of the enquirer.

A person, community or other external stakeholder, such as a civil society organization, can submit their questions or concerns to the Bank either by sending an e-mail to the following e-mail address: esg@federalbank.co.in or by sending a mail to the following address: [Service Quality Department, The Federal Bank Ltd, Corporate Office, Federal Towers, Aluva, Ernakulam, Kerala, India- 683101]. However, such enquiries shall be sent with the name and

mailing address of the sender/information seeker specifying the interest of the enquirer on the query raised.

Where the question or concern relates to credit facility financed by Bank, the interested or affected person(s) are first encouraged to discuss the matter directly with the company. In cases where the question or concern was not addressed sufficiently at the company level, interested parties may submit their query to Bank, in writing, providing the following information:

- a. Name and Contact Information of the sender,
- b. Name of the company to which the concern relates,
- c. Description of the concern and any supporting documentation,
- d. Date of the incident or action giving rise to the complaint (if applicable),
- e. Specific remedy sought (if applicable),
- f. Details of queries raised with the company and its response,
- g. Any other information as deemed appropriate by the sender.

The E&S Officer will provide confirmation of receipt to the sender within 48 hours of receiving the written question or concern and inform them that they will receive a response in writing within 15 working days. However, the Bank will not be bound to provide any response in writing if the inquiries are outside the scope of E&S risks or if the statute / agreement with the client does not permit such disclosure. However, in cases where the concern is found genuine, but Bank is bound by such statutes / client agreements, Bank will inform the sender about this limitation and will make efforts in good faith to resolve the issues as feasible.

Interested and affected parties may submit queries or concerns without fear of retribution and may request that Bank shall not disclose the names of individuals to the clients without prior explicit permission of the interested parties.

7. Conclusion

Adoption of ESMS practices for domestic lending activities will enable Bank to remain committed for the cause of sustainable development as desired by the government, regulators and other stakeholders. ESMS policy will enable Bank to minimise environmental and social impact posed by the lending activities. The policy proposes to ensure funding to the borrowers whose projects are sustainable and environment friendly. This will be achieved through meticulous risk categorisation of the borrowers and by ensuring that the funds lent by Bank will be used for purposes / activities which have minimal impact on the environment and the society.