Via Electronic Mail

Mr. Philippe Le Houérou
Executive Vice President and Chief Executive Officer
International Finance Corporation
2121 Pennsylvania Avenue, NW
Washington, D.C. 20433

January 11, 2019

Dear Mr. Le Houérou

We are writing to you as NGOs who have engaged with the IFC on its financial intermediary lending policy and practices for many years now, including supporting communities who have been adversely affected by FI financed projects to seek redress through the CAO.

Over the past couple of years, we have welcomed some of the changes you have brought in at the IFC, and we appreciate your openness to meeting with civil society, especially during the Annual meetings.

We welcome the steps you have taken both to improve disclosure and to steer financial intermediary lending out of coal, as well as the explicit language in the newly-released Interpretation Note. We believe that there is still some way to go to ensure that the IFC can be open about the way its money is being used, and to decarbonise its FI portfolio in line with the Paris Agreement. From conversations with your staff, we are also aware that the IFC is currently developing a strategy to articulate the implementation of your commitments in full, and that in early 2019 it will release further public details of what this commitment requires. We believe that this represents a critical opportunity for consultation and collaboration with civil society.

While we recognise this progress, we still have many concerns about this model of lending through intermediaries, in particular about the social, environmental and human rights impacts of high-risk sub-projects and companies, and the lack of transparency about where the money ends up.
You have said that you are listening to the critiques and recommendations from civil society and acting to address our concerns, and it is in this spirit that we would like to be involved in the development of IFC's strategy to implement the new and important commitments that you outlined in your recent blog. We would encourage the IFC to be as bold as possible, to meet the huge challenge laid down in the recent IPCC report that you also cited in your speech in Bali.

In defining the parameters of the strategy and reforms, we urge you to open the discussion and consider the following steps, which are based around three complementary goals: greater transparency, rigorous ring-fencing of investments and action by the IFC to decarbonise its FI portfolio.

Disclosure
In order for civil society to be able to hold the IFC and its clients accountable to their environmental and social commitments and responsibilities and to ensure that affected communities know what entitlements and protections they have and what recourse mechanisms are available if they are harmed, it is vital that the IFC takes a roadmap approach to disclosure, which makes clear that the voluntary disclosure initiative is only a stepping stone towards mandatory disclosure after the two year pilot. This roadmap should set clear, time-bound targets and incentives for those working inside financial intermediary institutions to embed a culture of transparency, good governance and progress towards a more systematic approach to disclosure. Otherwise, a voluntary pilot without

clear objectives and targets runs the risk of creating perverse incentives for FI clients not to disclose their higher risk lending during the pilot in order to influence IFC's policy against disclosure and argue that the market is not ready, especially in emerging markets.   The roadmap should:

- Develop and offer incentives for FI clients willing to disclose the name, sector and location of higher risk sub-projects not only on the IFC's website but also on the FI client's website– regardless of the financial instrument: loan, equity or bonds. Incentives could include requiring higher-risk management standards and supervision where disclosure does not occur, providing more favourable financing terms where disclosure exists, or ranking disclosure in selection processes and setting time-bound commitments to phase in increased disclosure for all financing.

- Require and support all financial intermediaries to develop a disclosure policy and set up the appropriate mechanisms for disclosure and transparency as part of the Environmental and Social Management System (ESMS), including publicising the FI and the IFC's involvement in sub-projects at the project sites among affected communities. Transparency and disclosure of information is an integral part of the ESMS.

- Screen out financial intermediaries that are not willing to develop a transparency policy and step up with their clients to promote a global norm of higher-risk project-related information disclosure regardless of the financial instrument, in the same manner as IFC approaches its direct investments.

- Adopt a requirement for all FI equity and debt clients to track and disclose in IFC's website as well as the FI's website their coal and other fossil fuel investments (not just coal exposure as currently promised).

Developing clear parameters and requirements for ring-fencing

One of the most significant reforms to IFC's approach to FI lending that you have announced in recent months is achieving the ring-fencing of 95% of new FI investments "to ensure that the financing only supports targeted areas, such as projects promoting energy efficiency, renewables, women business owners, or small and medium-sized enterprises." We note, however, that the CAO has found that the IFC has not been adequately ring-fencing these investments, and thus continuing to allow IFC funds to be used for high-risk sub-projects. In its Third Monitoring Report of IFC's Response to the FI portfolio audit, the CAO found that in the vast majority of the SME targeted FI investments that CAO examined, IFC's legal agreement with the FI fails to actually ring fence the use of funds, even when it purports to do so on its public project portal. Of a sample of 28 such investments that CAO looked at, only 10 had legal agreements that actually limited the use of funds and only 3 of those 10 included a mechanism that would also allow traceability of IFC funds to ensure that they were actually used only for SMEs. The CAO views both of these conditions (legally restricted and traceable) as necessary for a loan to be considered ring-fenced. In another example, the CAO found an investment in a commercial bank exposed to high risk sectors that was targeted to SMEs whereby the IFC had relaxed its SME definition to include bigger companies (with annual revenue up to $60 million). The CAO noted: "Given the expanded definition of SME lending for this project, however, IFC is potentially exposed to higher (E&S) risk sub-projects than would usually be the case for an SME loan. IFC's supervision has not engaged with this issue nor has it considered whether the bank has complied with the restriction against lending to support business activities in the environmentally sensitive region."[1]

If ring-fencing is the primary means that the IFC is using to address the concerns that the CAO and civil society have been raising for many years about FI lending, then it is essential that the IFC applies a much more rigorous approach than it has in the past to these ring-fences. It should also be much more transparent on its project disclosure portals about how funds will be used, managed and supervised. To give the public more confidence that IFC funds are being used solely for the purposes described on IFC's Project Information Portal, we urge the IFC to adopt a procedure that ensures that all targeted FI investments meet the same standards as the Green Bonds Principles. These would include:

- Ensuring that the designated projects provide clear environmental and/or social benefits;
- Setting aside IFC proceeds in a designated account for lending exclusively for the targeted purpose of the FI investment (eg SME lending, renewable energy, etc) and ensuring that the end use of funds are traceable;
- Requiring FI clients to report on the use of proceeds, including a list of the projects financed, on at least an annual basis, including their expected social and/or environmental impact; and
- Requiring independent external reviews of the use of proceeds against relevant standards.

Decarbonizing the FI portfolio:
In order to clean up its FI lending portfolio and help to achieve a transformational shift in global finance flows, we urge the IFC to take on board the following recommendations in developing its green equity approach:

- Ensure that none of its investments result in an increase in coal use: whether for power generation or industrial uses, and associated facilities such as transmission lines and railways or ports primarily meant for the transportation of coal;
- Exclude upstream oil and gas from 2019, as the World Bank Group has already committed to do in its direct lending;
- Not invest in clients with more than 5% portfolio exposure to coal. Dutch Bank ING has stated it will no longer finance utilities sector clients that will be over 5% reliant on coal in 2025; additionally, existing ING clients in the utilities sector should have ended their reliance on coal by 2025 for ING to continue the relationship. BNP Paribas will only provide services to, or invest in, companies that diversify away from coal. While IFC's clients differ from those of ING and BNP Paribas, these banks are not development institutions like the IFC. Both the Dutch and the UK development finance institutions, FMO and CDC, which are similar operators to the IFC, investing in the same markets, have a fixed percentage portfolio coal exposure limit in place, demonstrating that such target-setting is possible.
- Invest only in FI clients who commit to develop a portfolio decarbonisation plan within a year of investment, which aims to achieve emissions reductions in line with goals set under the Paris Climate Agreement.

Some of the signatories of this letter recently held meetings with IFC senior management in Washington DC, who offered to meet with civil society to present the reforms. We welcome this move and request that there is an inclusive space for all of us who are following developments in IFC's financial intermediary lending, to engage with the IFC to press for the fundamental reforms

[1] Compliance Advisor Ombudsman, Third Monitoring Report of IFC's Response to: CAO Audit of a Sample of IFC Investments in Third-Party Financial Intermediaries, 6 March 2017

necessary to bring IFC's financial intermediary lending portfolio into line with its commitment to environmentally and socially responsible investment.

We look forward to continued engagement with you and your staff in coming months,

Yours sincerely

Abibiman Foundation, Ghana
Accountability Counsel, US
Alliance Sud, Switzerland
Bank Information Center Europe, Europe
Bank Information Center, US
Big Shift Global, International
Both Ends, Netherlands
Bretton Woods Project, UK
CEE Bankwatch Network, International
Center for Financial Accountability, India
Center for International Environmental Law (CIEL), US
Center for Research on Multinational Corporations, (SOMO), Netherlands
Christian Aid, UK
Counter Balance, Czech Republic
Eurodad, Europe
Equitable Cambodia, Cambodia
FUNDEPS (Foundation for the Development of Sustainable Policies), Argentina
Gender Action, US
Inclusive Development International, US
International Accountability Project, US
London Mining Network, UK
NGO Forum on ADB, Regional
Oil Change International, US
Oxfam International, International
Oyu Tolgoi Watch, Rivers without Boundaries Coalition, Mongolia
Phenix Center for Economic and Informatics Studies, Jordan
Philippine Movement for Climate Justice, Philippines
Rivers without Boundaries International Coalition, International
RSPB, UK
Social Justice Connection, Canada
Third Generation Environmentalism (E3G), UK
Urgewald, Germany