# FirstRand environmental and social risk assessment report

2016

FIRSTRAND

FIRSTRAND

## highlights

# 6 530

**LENDING TRANSACTIONS** screened for environmental and social risks in the group's South African operations

# 3 166

**TRANSACTIONS** involved engaging clients on their environmental and social processes

# 92%

of these were **FNB TRANSACTIONS**

# 35%

**OF REVIEWED DEALS** were from the real estate sector, **24%** from agriculture and **17%** from the industrial sector

# 5

**RENEWABLE ENERGY TRANSACTIONS** underwent a review for environmental and social risk

# 1

**PROJECT FINANCE ADVISORY DEAL** took place (on a renewable energy project located in Africa)

# 7

**PROJECT FINANCE** transactions screened and close[RA]

RA – Reasonable assurance

# 94%

**OF WESBANK EMPLOYEES** have completed ESRA training; the figures for RMB and rest of Africa are **84%** and **81%** respectively

## initiatives

**FNB South Africa** is revising its ESRA **e-learning programme** and will launch the new training during 2017

**FIRSTRAND** implemented the **ESRA process for all commercial sector transactions** across all of its large African subsidiaries

**ASHBURTON INVESTMENTS**, the group's asset management franchise, launched a review of its current investment analysis practices to establish **the best approach for implementing UN PRI (Principle of Responsible Investment)**

**THE GROUP** included the **review of contaminated land risk indicators** as part of its property valuation process as an initial step in identifying contaminated land on all property-related transactions

## 1 WHY MANAGING ENVIRONMENTAL AND SOCIAL RISKS IN FINANCING IS IMPORTANT TO FIRSTRAND

**FirstRand has formalised processes for proactively measuring, monitoring and managing the environmental and social risk associated with its client activities. By incorporating environmental, social and governance aspects into lending due diligence, investment and asset management practices, the group is expanding traditional lending and investment analysis of clients to include new short- and long-term, non-financial factors.**

These processes are underpinned by the group's adherence to internationally recognised standards and principles such as the principles of the United National Global Compact, United Nations Environment Programme Finance Initiative, Equator Principles, and United Nations Principles for Responsible Investment.

In addition, FirstRand supports industry initiatives such as the Banking Association of South Africa's Principles on the Management of Environmental and Social Risk. These principles promote the role of financial institutions in supporting the development of South Africa and the incorporation of environmental and social risk management into the management of the group's operations, procurement practices, lending practices, products and services.

## 2 HOW FIRSTRAND MANAGES ENVIRONMENTAL AND SOCIAL RISK IN LOANS AND INVESTMENTS

In conjunction with its franchises, FirstRand has developed policies, procedures and processes in the lending and investment areas which allow the franchises to identify environmental and social risks.

Each of the group's operating franchises has formalised credit and compliance processes for implementing ESRA, with oversight provided by the franchise social and ethics committees, risk and compliance officers, and credit committees.

**FirstRand has formal governance processes for managing environmental and social risks.** These processes involve integrating environmental and social information into the relevant sections of risk reports at group and franchise level. Tolerances and mitigating actions are defined at group and franchise level, and progress on these actions is tracked through existing risk reporting structures. Provision is made for the escalation of significant environmental and social issues to the board via the group's oversight structures.

The ESRA process is incorporated in the FirstRand credit risk management framework as an aspect of transaction risk management. Oversight is provided by the group ethics committee as well as the franchise ethic and conduct committees.

*OVERVIEW OF GOVERNANCE FRAMEWORKS FOR IMPLEMENTING THE ESRA PROCESS*

| | |
|---|---|
| **FIRSTRAND ETHICS FRAMEWORK** | The FirstRand ethics framework sets the strategy, programmes and operational culture and conduct risk standards and requirements within which the group operates. The ethics framework covers culture risk, business conduct and market conduct requirements. |
| **FIRSTRAND GROUP ENVIRONMENTAL RISK FRAMEWORK AND GUIDELINES** | Defines consistent standards for identifying, assessing and managing environmental risk.<br>Defines excluded and sensitive sectors or activities from an environmental and social perspective.<br>Includes criteria for referring transactions to the conduct committee and ethics office. |
| **FRANCHISE-SPECIFIC ESRA POLICIES AND PROCESSES** | Designed to support the FirstRand group guideline.<br>Details franchise-specific structures, roles, systems and processes. |

FirstRand's policies are subject to formal annual review. Under the environmental risk framework, the FirstRand environmental and social risk team is responsible for developing the policy and processes, and assisting business units to assess environmental and social issues, and associated risks.

## 2.2 FirstRand's sensitive industries matrix and exclusions list

FirstRand has developed an exclusions list of activities that it will not finance. Reasons include legal constraints, financing restrictions under international financing agreements, or because FirstRand may suffer reputational damage as a result of involvement in specific industries. For monitoring purposes, the group integrated the process of identifying these activities into the ESRA screening tool.

## 3 ESRA SCREENING

Specialists in the franchises serve as technical advisors to franchise senior management and employees involved with credit transactions and provide assessment, review, consultation and specialist advice on lending transactions.

The ESRA process is outlined as follows:

| ESRA PROCESS | | | | | | |
|---|---|---|---|---|---|---|
| **STAGE IN PROCESS** | **SUBMISSION OF TRANSACTION** | **RISK IDENTIFICATION** | **RISK ASSESSMENT** | **RISK OPINION** | **DECISION MAKING** | **POST-TRANSACTION FOLLOW-UP** |
| **ACTIVITIES UNDERTAKEN IN STAGE** | • Transaction entered into ESRA tool as part of credit application process<br>• Activities excluded from finance and sensitive activities are identified using tool, and an initial level of potential environmental and social risk allocated to transaction | • Transaction referred electronically to environmental and social (E&S) expert<br>• E&S expert identifies potential environmental and/or social risks through due diligence process | • Collate information about transaction and client, and engage with client to conduct ESRA review<br>• Where necessary and in advisory capacity only, FirstRand works with client to develop measures to mitigate risks | • Review transaction's risk profile, develop opinion on level of associated risk in transaction and compile recommendation for credit or investment committee<br>• If the risk profile is significantly high, transaction is escalated to senior risk management for discussion | • Credit committee reviews ESRA team's recommendations and makes decision on transaction<br>• If committee is not comfortable about making decision on high-risk transaction, it is escalated to senior risk management and FirstRand ESRA team | • Monitor client's progress towards taking agreed measures |
| **KEY RESOURCES** | Relationship managers for clients | Divisional E&S risk expert | Divisional E&S expert with relationship manager | Divisional E&S expert<br>Senior risk managers | Credit or investment committee and FirstRand E&S team<br>Senior risk managers | Business unit with support from divisional E&S expert |

All transactions in the ESRA process are categorised according to the level of potential environmental and/or social risks that may be related to the financed client-activities.

The transactions are categorised as follows:

| HIGH RISK | MEDIUM RISK | LOW RISK |
|---|---|---|
| **CATEGORY A** | **CATEGORY B** | **CATEGORY C** |
| • High risk of potential environmental and social impact<br>• Incudes transactions with potentially significant adverse social or environmental impacts that are diverse, irreversible or unprecedented. Issues relating to these risks may lead to work stoppages, withdrawal of legal authorisations and reputational damage. Examples could include projects involving physical displacement of natural environment or communities | • Medium risk of potential environmental and social impact<br>• Includes transactions with potentially limited adverse social or environmental impacts that are few in number, generally site-specific, largely reversible and readily addressed through mitigation measures. Issues relating to these risks may lead to fines, penalties or legal non-compliance and reputational damage. Examples could include increased use of energy or increased atmospheric emissions | • Projects with minimal or no social or environmental impacts |

The FirstRand ESRA tool separates transactions into Equator Principles-related transactions and general ESRA transactions. Where a transaction is identified as an Equator Principles-related transaction, the group requires clients to comply with the requirements of the Equator Principles.

FirstRand's ESRA specialists may engage with clients to:

- review  environmental and social risk processes;
- review policies, procedures and commitments;
- review performance and publically available information related to their environmental and social risk performance; and
- conduct site visits, where required, in accordance with the IFC Performance Standards, IFC EHS Guidelines and the Equator Principles.

FirstRand may then incorporate selected risk mitigation measures into loan documentation in agreement with clients.

If a transaction is identified as sensitive, controversial or of significantly high risk, or if an exception to the defined process occurs, the relationship manager, franchise chief risk officers and franchise heads of credit are informed through a formalised escalation process.  Final approval is provided by franchise risk officers and reported to relevant franchise ethics and conduct committees for noting.

The following table indicates transaction types where ESRA is applied.

| TRANSACTION TYPE | THRESHOLD AMOUNT AFTER WHICH AN ESRA REVIEW IS TRIGGERED |
|---|---|
| PROJECT FINANCE TRANSACTIONS | Total project capital costs at or above USD10 million: Equator Principle review<br>All category A (high-risk) and B (medium-risk) transactions with a total project capital cost of less than USD10 million: in-house ESRA review |
| PROJECT FINANCE ADVISORY | Total project capital costs at or above USD10 million: Equator Principle review |
| CORPORATE LOANS | No threshold applied, all corporate loans: in-house ESRA review |
| CORPORATE LOANS (PROJECT-RELATED) | Total aggregate loan amount is at least USD100 million, of which the member banks' individual commitment (before syndication or sell-down) is at least USD50 million and loan tenor is at least two years: Equator Principle review |
| BRIDGE LOANS (SUBJECT TO EQUATOR PRINCIPLES) | Bridge loans with a tenor of less than two years that are intended to be refinanced by project finance (at or above USD10 million): Equator Principle review |
| EQUITY INVESTMENT DEALS | No threshold applied, all equity investment deals: in-house ESRA review |
| AFFECTED COMMERCIAL LOANS (INCLUSIVE OF PROPERTY FINANCE) | No threshold applied, all property finance or property securitised loans: in-house ESRA review.<br>Commercial loans (non-property related) with a total facility amount above R7.5 million: in-house ESRA review<br>Asset finance to a business entity: no threshold applied |

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## ROLLING OUT ESRA TO INTERNATIONAL OPERATIONS

**As part of FirstRand's continuous improvements to the ESRA programme, it included all its international operations in the ESRA process during the year.** The scope of the ESRA process outside South Africa remains the same as its scope inside the country. Most subsidiaries now have in place:

- country-specific ESRA policy;
- country-specific legal framework of environmental and social related legislation;
- training for the country's executive committee on importance and process of environmental and social risk assessment;
- online ESRA e-learning for all affected employees; and
- access to the FirstRand ESRA tool.

Countries have developed an incremental, three-year implementation plan under which financial thresholds for the ESRA process are reduced until all business-related transactions are sent for risk categorisation by the ESRA tool.

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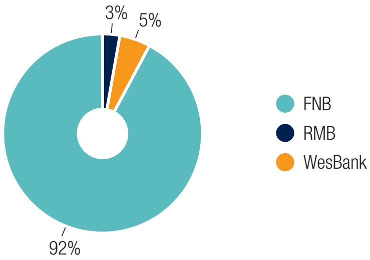
## HOW FIRSTRAND PERFORMED

**During the reporting period, the FirstRand Group screened 6 530 lending transactions for environmental and social risk in its South African operations and engaged with clients on their environmental and social risk management processes relating to 3 166 transactions during the same period.**

This number relates to transactions that were identified as having high or medium potential for environmental and/or social impact as a result of the activity that the client intends to carry out using finance from the bank.

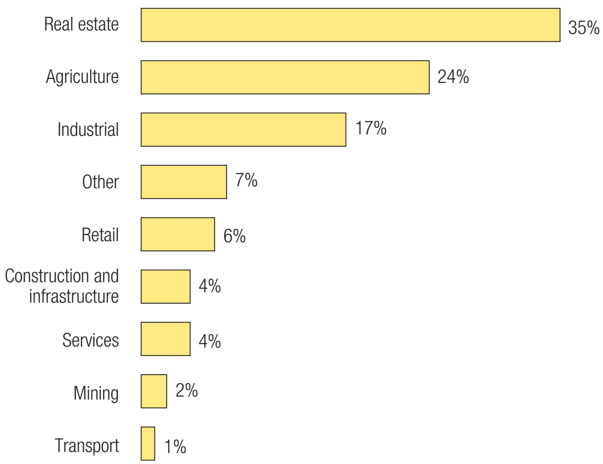
*% OF TOTAL ESRA TRANSACTIONS PER FRANCHISE: CLIENT ENGAGEMENT CONDUCTED*




These figures combine Equator Principles-related transactions and general ESRA transactions.

Due to the nature and size of the FirstRand franchises, the majority of the transactions originated from FNB's Business segment.

*% OF TOTAL ESRA TRANSACTION REVIEWED PER SECTOR*



## 6 ANALYSIS OF EQUATOR PRINCIPLES TRANSACTIONS

**FirstRand became a signatory to the Equator Principles in 2009. The Equator Principles are a set of global best practice standards to manage environmental and social risks and financing and investment. The projects reported are structured Equator Principle-defined deals, which were reviewed by in-house environmental and social risk specialists.** These specialists provide technical advice to divisional senior management and employees involved with credit transactions and provide assessment, review, consultation and specialist advice on lending transactions.

All category A and B transactions underwent independent Equator Principle reviews to establish each project's environmental and social risks, and reached financial close during the reporting period. Financial close is assumed when all conditions preceding the initial debt draw down have been satisfied or waived.

Equator Principle reporting is externally assured for public disclosure by an independent third party in line with the requirements set out by the Equator Principle Association.

The number of Equator Principle transactions screened per industry category and regions are listed below.

### Project finance advisory services

Total number mandated in the reporting period: 1

During the reporting period, one project finance advisory took place on a renewable energy project located in Africa.

### Project finance transactions

Total number reaching financial close in the reporting period: 7

| TOTALS* | 0 | 2 | 5 |
|---|---|---|---|
| **SECTOR** | **CATEGORY A** | **CATEGORY B** | **CATEGORY C** |
| Mining | | | |
| Infrastructure | | | |
| Oil and gas | | | |
| Power | | 2 | |
| Other** | | | 5 |
| **REGION** | **CATEGORY A** | **CATEGORY B** | **CATEGORY C** |
| Americas | | | |
| Europe, Middle East and Africa | | 2 | 5 |
| Asia Pacific | | | |
| **COUNTRY DESIGNATION** | **CATEGORY A** | **CATEGORY B** | **CATEGORY C** |
| Designated# | | | |
| Non-designated | | 2 | 5 |
| **INDEPENDENT REVIEW†** | **CATEGORY A** | **CATEGORY B** | **CATEGORY C** |
| Yes | | 2 | |
| No | | | 5 |

* *Reasonable assurance provided*

** *Transactions listed under other related to retail sector.*

\# *Designated countries are those countries deemed to have robust environmental and social governance, legislation systems and institutional capacity.*

† *An independent review may not be required for all projects. e.g. not required for Category C projects.*

## 6.1 ESRA in FirstRand's asset management franchise

Ashburton Investments, FirstRand's asset management franchise, became a signatory to the United Nations Principles for Responsible Investment (PRI) during the current period.

Ashburton Investments aims to develop a suite of sustainable investment product offerings by integrating environmental, social and governance (ESG) aspects into its investment decision-making processes. During the year, it began a review of the current investment analysis practices to establish the best approach for implementing ESG aspects into the various product investment analysis processes.

## 7 ENVIRONMENTAL AND SOCIAL RISK INITIATIVES

The following initiatives were undertaken during the financial year.

| | |
|---|---|
| **AGRICULTURE** | FirstRand continuously participates in the review and commentary on draft legislation that may impact this sector and the ability of clients to obtain credit or maintain credit as a result. It conducts its engagement through its membership of Business Unity South Africa, the National Business Initiative and Banking Association South Africa |
| **HUMAN RIGHTS** | Human rights considerations are integrated in various aspects of the ESRA process, HR processes, ethics framework, business conduct programmes and many other operational processes. FirstRand is committed to respecting the human rights of its employees, avoiding human rights violations through its business relationships with clients, and to avoiding human rights violations through engagement with its vendors and service providers |
| **CONTAMINATED LAND** | FirstRand supports the development of legislation in South Africa to manage and mitigate the risk of contamination of property and engages on what impact this legislation has on a financial services provider, and the role that this may play in property finance and securitisation of property as collateral<br>FirstRand participates and submits commentary on legislation governing the management of contaminated land in South Africa via its engagement with the Department of Environmental Affairs through Business Unity South Africa and the Banking Association South Africa |
| **CARBON EMISSIONS** | FirstRand participates in the review and commentary on draft legislation related to carbon emission reporting, carbon tax and carbon offsets. Engagement is conducted through membership of Business Unity South Africa, the National Business Initiative and Banking Association of South Africa |
| **BIODIVERSITY** | FirstRand recognises that client activities can impact areas of high biodiversity value/high-sensitivity ecosystems, or areas of high conservation value. Where these impacts have been identified, the group expects clients to conduct a biodiversity assessment as part of the due diligence requirement, using widely accepted international guidance and best practices |

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## TRAINING AND AWARENESS

**Training plays an important role in helping FirstRand employees to understand the requirements of the ESRA framework, processes and policies.** Each franchise is responsible for delivering training to its affected employees. Affected employees are defined as:

- current and new staff members who will be directly involved in/affected by the credit submissions or approval processes;
- current and new staff members who will be directly/indirectly involved in the ESRA process; and
- current and new staff members involved in the monitoring/compliance of the ESRA process.

*PERCENTAGE OF AFFECTED EMPLOYEES TRAINED ON ESRA*

| FNB First National Bank | RMB | WesBank |
|---|---|---|
| Rest of Africa 81% | Various segments 84% – 98% | 94% e-learning |

FNB is in the process of revising its current ESRA e-learning programme in South Africa to include ESRA and will launch the new training during 2017.

RMB is continuously updating ESRA/EP online training to specific roles.

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## LOOKING AHEAD

The National Environmental Management Waste Act 59 of 2008: Part 8 was promulgated on 1 May 2014. Part 8 of the Act relates specifically to the management of contaminated land.

Impacts related to this part of the Act have brought an additional focus to FirstRand's lending processes around the valuation of property that is contaminated, securitisation of contaminated property and how this is evaluated as part of the credit approval decision on a transaction.

**The ESRA programme is in the process of expanding its scope to include transaction types it previously did not include.** This expansion is due to the risk of contamination to property that may be used as collateral against a loan. In the current ESRA process, working capital transactions and overdraft transactions in FNB are excluded from the ESRA review process. However, the property evaluation process and due diligence now includes a review of possible property contamination. The property that is being used as security against this type of loan will be reviewed for contamination risk and due diligence will be conducted to establish the current status of possible contamination of the property. The ESRA risk categorisation tool will be adapted to incorporate due diligence checks for contamination.

As part of the ongoing rollout of ESRA to the group's international operations, FirstRand Bank India branch is in the process of ESRA implementation, and there are processes to incorporate Mozambique and Ghana during 2017.

Ashburton Investments is in the process of implementing the requirement to analyse ESG risks as part of its analysis of investee companies. It is building a product- and sector-specific ESG risk framework to implement these requirements. It is anticipated that this will be rolled out during 2017.

## INDEPENDENT ASSURANCE PROVIDER'S REASONABLE ASSURANCE REPORT ON SELECTED NON-FINANCIAL INFORMATION

### To the directors of FirstRand Limited

We have undertaken a reasonable assurance engagement on selected non-financial information, as described below and presented in this FirstRand environmental and social risk assessment report for the year ended 30 June 2016 (the report). This engagement was conducted by a multidisciplinary team including social, environmental, assurance and sustainability specialists with relevant experience in sustainability assurance reporting.

### Subject matter

We are required to provide reasonable assurance on the Equator Principles (EP) transaction performance, prepared in accordance with the Equator Principles, marked with RA on page 1 and set out in the table on page 9 in the report.

### Directors' responsibilities

The directors are responsible for the selection, preparation and presentation of the selected non-financial information in accordance with the Equator Principles. This responsibility includes the identification of stakeholders and stakeholder requirements, material issues, commitments with respect to sustainability performance and design, implementation and maintenance of internal control relevant to the preparation of the report that is free from material misstatement, whether due to fraud or error.

### Our independence and quality control

We have complied with the independence and all other ethical requirements of the Code of Professional Conduct for Registered Auditors issued by the Independent Regulatory Board for Auditors (IRBA) that is consistent with the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (Part A and B), which is founded on fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour.

KPMG Services Proprietary Limited applies the International Standard on Quality Control 1 and accordingly maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

### Our responsibility

Our responsibility is to express an opinion on the selected non-financial information based on the evidence we have obtained. We conducted our reasonable assurance engagement in accordance with the International Standard on Assurance Engagements (ISAE) 3000 (Revised), Assurance Engagements other than the Audits or Reviews of Historical Financial Information, issued by the International Auditing and Assurance Standards Board. That Standard requires that we plan and perform our engagement to obtain reasonable assurance about whether the selected non-financial information is free from material misstatement.

A reasonable assurance engagement in accordance with ISAE 3000 (Revised) involves performing procedures to obtain evidence about the quantification of the selected non-financial performance information and related disclosures. The nature, timing and extent of procedures selected depend on the practitioner's judgement, including the assessment of the risks of material misstatement, whether due to fraud or error. In making those risk assessments we considered internal control relevant to FirstRand's preparation of the selected non-financial information. A reasonable assurance engagement also includes:

- assessing the suitability in the circumstances of FirstRand's use of Equator Principles as the basis for preparing the selected non-financial information;
- evaluating the appropriateness of quantification methods and reporting policies and internal guidelines used, and the reasonableness of estimates made by FirstRand; and
- evaluating the overall presentation of the selected non-financial performance information and whether the information presented in the report is consistent with our findings, overall knowledge and experience of Equator Principle management and performance at FirstRand.

Our work included the following evidence-gathering procedures:

- Interviewed management and senior executives at corporate level to obtain an understanding of the internal control environment, risk assessment process and information systems relevant to the Equator Principle reporting process. Inspecting documentation to corroborate the statements of management and senior executives in our interviews.
- Tested the processes and systems to generate, collate, aggregate, monitor and report selected key performance indicators and inspected related documentation, more specifically:
  - Interviewed and discussed with relevant management, key personnel and/or stakeholders of FirstRand to confirm definitions and boundaries for selected performance information, and gathered information on the data collection and report preparation processes.
  - Evaluated internal data management controls based on system walkthroughs.
  - Inspected selected internally and externally generated documents and records and performed comprehensive data analyses.
  - Recalculated the selected non-financial information, where relevant.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Opinion

In our opinion, the selected non-financial performance information set out in the report for the year ended 30 June 2016 is prepared, in all material respects, in accordance with the Equator Principles.

## Other matter

The maintenance and integrity of the FirstRand website is the responsibility of FirstRand's management. Our procedures did not involve consideration of these matters and accordingly we accept no responsibility for any changes to either the information in the report or our independent reasonable assurance report that may have occurred since the initial date of its presentation on FirstRand's website.

## Restriction of liability

Our work has been undertaken to enable us to express an opinion on the selected non-financial information to the directors of FirstRand in accordance with the terms of our engagement, and for no other purpose. We do not accept or assume liability to any party other than FirstRand, for our work, for this report, or for the conclusions we have reached.

KPMG.

KPMG Services Proprietary Limited
Per Neil Morris
Director

18 November 2016

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