



SME Bank and Private Clients
Customised Finance and Public Clients

»» Sustainability guideline for domestic promotional business

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1 Abbreviations

Abbreviation	Term
EHS Guidelines	Environmental Health and Safety Guidelines
ESDD	Environmental and Social Due Diligence
ESMS	Environmental and Social Management System
EU	European Union
IFC	International Finance Corporation
ILO	International Labour Organization
LFI	Promotional institutions of the federal states
OECD	Organisation for Economic Cooperation and Development

2 Preamble

The KfW Group business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients" follow [KfW Group's sustainability mission statement](#) and contribute

- to the implementation of the German government's sustainability strategy,
- to achievement of Agenda 2030 with the Sustainable Development Goals (SDGs), and
- to meeting the requirements of the Paris Agreement.

The following guideline specifies KfW Group's mission statement for the KfW business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients" by describing the procedure for tackling environmental and social risks in financing from these business sectors.

For financing of KfW's business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients", the [Exclusion List of KfW Group](#) must always be observed. Financing may also fall within the scope of the [Paris-compatible Sector Guidelines of KfW Group](#); corresponding requirements are set out in the respective programme-specific conditions (e.g. in the programme information sheets).

In its [Policy Statement on Human Rights](#), KfW commits itself to respecting and protecting human rights in its sphere of influence. In that declaration, it pledges to avoid engaging in any violations of human rights.

3 Tasks in the business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients"

On the basis of the [Law Concerning KfW](#), KfW Group promotes financing in the above-mentioned business sectors that is provided by private individuals or companies, cities, municipalities and non-profit and social organisations.

The business sector "SME Bank & Private Clients" bundles the standardisable and digitisable large-volume business. The business area is divided into two segments according to customer groups: The "SME Bank" segment supports the German economy with a wide range of loans and grants. The promotional priorities of the "SME Bank" segment cover the topics of energy efficiency and renewable energies, environment and sustainability, digitalisation and innovation, corporate investment and start-ups. The financing is provided as part of KfW's promotional programmes via private banks, savings banks and cooperative banks as well as insurances to end borrowers (principle of on-lending). Promotional activities in the "Private Clients" segment include education financing (e.g. awarding of student loans), promotion of energy efficiency in the construction and refurbishment of residential buildings and promotion of the acquisition and construction of owner-occupied residential property. The promotional products are on-lending, standardised loan financing (some with repayment grants) as well as investment grants and – only in the case of education financing – also direct financing.

The business area "Customised Finance and Public Clients" is split into three further business segments: the "Municipal and Social Infrastructure" segment covers the wide range of basic promotion offers for municipalities, municipal companies and non-profit organisations focused on environmental protection, the energy transition and social change. This segment issues standardised loans on either a direct basis (business with municipalities) or through on-lending (municipal and social companies) and also issues grants. The "Customised Finance Corporates" segment focuses on tailor-made promotional solutions for businesses in the form of various external capital products. This includes project and syndicate financing. In the segment of "Individual financing for banks and promotional institutions of the federal states (LFIs)", KfW funds LFIs using programme-based global loans and global loans for general LFI refinancing. It also offers individual financing for banks, such as funding for government-backed export loans, global leasing loans and global loans to European (promotional) banks to promote SMEs and environmental protection.

The two KfW business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients" primarily finance projects with an investment location in Germany. In some cases, the programme provisions also permit investment locations outside Germany.

4 Applicability and aims of this guideline

This guideline enters into force on 1 March 2023 and applies to all new KfW commitments for financing of KfW's business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients", regardless of the type of financing (e.g. loans, grants, equity financing; direct and indirect financing via financing partners).

It describes the procedures and standards used to tackle potential adverse effects or risks to people and the environment.

The objectives of the guideline are in particular:

- Definition of a uniform and binding framework for taking environmental and social standards into account in (co-)financed projects within the aforementioned business sectors.
- Fostering transparency in the Environmental and Social Appraisal decision-making processes.

5 Typical elements of Environmental and Social Appraisal

The Environmental and Social Appraisal aims to identify, avoid, minimise to an acceptable level or, if unavoidable, offset possible adverse effects and risks that a project may pose to people and the environment.

An Environmental and Social Appraisal typically consists of the following steps: In the first step, a project's possible environmental and social risks are assessed (screening) and the project is categorised with regard to the existing risks (categorisation). In the second step, the actual test is carried out, the scope and depth of which depend on the previous categorisation.

The categories "high risk" (A), "substantial risk" (B+), "moderate risk" (B) and "low risk" (C) are customary internationally. Projects in the "high risk" (A) category imply potentially diverse, significantly adverse or irreversible effects/risks for people (social) or the environment. On the other hand, a project is classified in the category "moderate risk" (B) if its potential adverse effects or risks are generally foreseeable, temporary, reversible and restricted to the project's location. As a rule, these can be avoided or reduced with state-of-the-art countermeasures or with standard solutions. If projects in the "moderate risk" category still display isolated significant environmental and social impacts and risks, they are categorised as a "substantial risk" (B+). Projects in the "low risk" category (C) are likely to pose no or only minor environmental and social risks.

An illustrative list of projects that may fall into the categories "high" (A), "substantial" (B+) or "moderate risk" (B) can be found in the appendix.

The scope and depth of the appraisal itself depend on the category of the project. Whereas projects in the "high risk" category (A) require extensive appraisal, projects in the "low risk" category (C) generally do not require any further analysis of environmental and social risks and impacts. For projects in the category "moderate risk" (B) and "substantial risk" (B+), a decision must be made on the necessity, scope and depth of an appraisal in individual cases.

In the case of financing with an intermediary financing partner, the appraisal is based on the financing partner's environmental and social management system (ESMS) in accordance with internationally accepted procedures. The financing partner is generally responsible for assessing the environmental and social impacts and risks of the respective project. An ESMS defines, among other things, standards and processes to ensure the environmental and social compatibility of projects to be financed and provides corresponding organisational and personnel capacities and structures (see, for example, [IFC Performance Standard 1](#)).

The procedure for projects (co-)financed by KfW in the scope of application of this guideline is set out in the following section.

6 Procedure for Environmental and Social Appraisal in the business sectors “SME Bank and Private Clients” and “Customised Finance and Public Clients”

6.1 Minimum requirements and evaluation criteria

All projects (co-)financed by KfW must meet the environmental and social law requirements and standards in force in the investment country.

In the event of a required appraisal by KfW, national standards are applied as an appraisal standard for investments in EU countries (including Germany) and OECD high-income countries. If the investment location is outside this country group, in addition to the domestic standards, international standards are also used as a benchmark, as formulated, for example, in the IFC Performance Standards and the Environmental, Health and Safety Guidelines (EHS Guidelines) of the World Bank Group or similar standards as well as the ILO core labour standards. If the appraisal reveals that a financing project does not meet the aforementioned environmental and social law requirements, or that unacceptable environmental and social impacts or risks are to be anticipated that cannot be adequately mitigated by suitable mitigation measures, KfW will not participate in the financing.

6.2 Screening and categorisation of uses

With the support of external expert opinions, KfW conducted a screening in 2020 of all the purposes for which it was used at that time in the programmes within the “SME Bank and Private Clients” and “Customised Finance and Public Clients” business sectors in accordance with the usual international procedure (see also comments under 5.). As a result, each purpose of the loan was assigned to an environmental and social risk category. This approach allows an assessment of the potential environmental and social impacts and risks that a measure to be financed can typically have within the scope of an intended purpose. New purposes are assigned to the corresponding categories in the same way as the initial screening.

The initial screening showed that almost two thirds of the intended uses were classified as “low risk” (C) and nearly one third of the intended uses were classified as “moderate risk” (B). Only around five percent of the total intended uses could potentially be attributed to the category of “substantial risk” (B+) or “high risk” (A).

6.3 Environmental and Social Appraisal in direct financing

In the case of direct financing, there is usually direct contact between KfW and the customer. In accordance with the usual international procedure, KfW considers itself responsible for assessing the environmental and social compatibility of the projects to be financed.

6.3.1 Investment location within Germany, the EU and OECD high income countries (direct financing)

For projects with an investment location in Germany, the EU and OECD high income countries, KfW assumes that these countries possess and implement an expanded set of environmental and social law rules. The Environmental and Social Appraisal therefore follows a simplified appraisal approach. (For the procedure for projects with an investment location in all other countries, see 6.3.2).

To ensure the environmental and social compatibility of the projects to be financed, KfW selects a tiered appraisal approach based on KfW's own screening of the purposes of use (see 6.2) in accordance with internationally accepted procedures, depending on the risk category in question.

No Environmental and Social Appraisal is carried out for promotional programmes for which the intended use was only assigned to the category “low risk” (C) according to screening.

KfW also waives an explicit Environmental and Social Appraisal for promotional programmes with intended uses that were assigned to a risk level not exceeding “moderate risk” (B) according to the screening. According to screening, the potential impacts and risks of projects in the

“moderate risk” category (B) are foreseeable, temporary and reversible and restricted to the location of the project. These can generally be avoided with either state-of-the-art countermeasures or with standard solutions. According to assumptions, the approval procedures established in Germany, the EU and OECD high-income countries for the relevant domestic promotional business sectors are ambitious and routine. Against this background, KfW does not carry out its own appraisal. All projects must meet the environmental and social requirements and standards in force in the investment country as a minimum requirement (see 6.1).

KfW uses a simplified appraisal procedure for projects with the corresponding intended uses for promotional programmes in which the purpose of the “substantial risk” category (B+) can be financed. This is based on the assumption that the legislation in Germany, the EU and OECD high-income countries is ambitious in terms of environmental and social aspects and is reliably implemented. In the simplified appraisal procedure, KfW imposes additional requirements as part of the lending process. Before commitment, KfW may request additional information on the project and the status of the permits that serve to determine environmental and social compatibility. In certain promotional programmes, the existence of the necessary approvals must also be confirmed in the course of implementing the project in connection with proof of intended use. KfW also conducts random reviews of environmental and social compatibility aspects as part of existing control processes in a downstream process (monitoring).

KfW carries out an Environmental and Social Appraisal for promotional programmes in which “high risk” (A) category uses can be financed. In doing so, it analyses the possible environmental and social impacts and risks of the project and determines the scope, focus and depth of the appraisal accordingly. If applicable: Environmental and Social Due Diligence (ESDD) by an independent expert is required.

KfW reserves the right to request additional documents for the appraisal.

6.3.2 Investment location outside Germany, the EU and OECD high-income countries (direct financing)

To ensure the environmental and social compatibility of the projects to be financed, KfW also applies a tiered appraisal approach based on KfW’s own screening of the purposes of use in accordance with international standards, depending on the risk category in question.

Programmes that have been assigned to a low-risk (C) screening use only will not be subject to Environmental and Social Appraisal.

If a project is part of a promotional programme that, according to screening, can potentially be assigned to the category “high risk” (A), “substantial risk” (B+) or “moderate risk” (B), KfW carries out an Environmental and Social Appraisal. In doing so, it analyses the possible environmental and social impacts and risks of the project and determines the scope, focus and depth of the appraisal accordingly. Environmental and Social Due Diligence (ESDD) in accordance with international standards (usually IFC Performance Standards) by an independent expert is generally required.

KfW reserves the right to request additional documents for the appraisal.

6.4 Environmental and Social Appraisal for financing with intermediary financing partner

A large part of the promotional programmes of KfW’s “SME Bank and Private Clients” and “Customised Finance and Public Clients” business sectors are conducted as standardised high-volume business in a highly digitalised manner via the respective regular banks of the promotional recipients. In addition, global loans to intermediary financing partners, for example, are granted to refinance end-borrower loans. In accordance with internationally accepted procedures, it is the responsibility of the regular bank or global loan partner to assess the environmental and social compatibility of the projects to be financed in these cases.

As a minimum requirement, all projects (co-)financed by KfW must meet the environmental and social law requirements and standards in force in the investment country.

KfW assumes that the regular banks or global loan partners, regardless of their registered office, already use appropriate procedures today to take into account potential environmental and

social impacts and risks of the projects to be (co-)financed by KfW (including taking into account the size, sector and investment country) in the usual form for the bank. This basic assumption is backed up by a market analysis and corresponding observations by KfW and is communicated to its financing partners via established communication channels.

The procedures can be incorporated into current processes or explicitly established in the form of an environmental and social management system (ESMS; ideally in accordance with IFC).

KfW carries out random checks of the basic assumption on current procedures for carrying out Environmental and Social Appraisal as part of a downstream process.

In the case of individual projects to be (co-)financed by KfW with an investment location outside the EU and the OECD high-income countries, KfW initiates additional internal reviews. KfW assesses whether the planned project could result in adverse environmental and social impacts and risks (screening). If a project falls into a higher risk category ("high risk" (A), "substantial risk" (B+) or "moderate risk" (B)), KfW must examine the environmental and social impacts and risks more closely. The scope, focus and depth of the review as well as the need for monitoring are defined accordingly. If applicable: Environmental and Social Due Diligence (ESDD) by independent experts is required.

KfW reserves the right to request additional documents for the appraisal.

6.5 Environmental and Social Appraisal by third parties

If other parties involved in the financing (business banks, export credit agencies, consortium partners, etc.) have examined environmental and social compatibility using qualified documents (e.g. audit report from an independent environmental and social expert), KfW may refrain from carrying out its own appraisal.

This does not exclude the possibility of examining certain issues in depth.

7 Validity and review of the guideline

This guideline applies from 1 March 2023 for KfW's business sectors "SME Bank and Private Clients" and "Customised Finance and Public Clients". It is reviewed at regular intervals.

8 Notes

Example list of sectors and investment projects with potentially “high” (A), “substantial” (B+) or “moderate” (B) environmental and social risks and impacts (not exhaustive)

Examples of projects with high environmental and social risks (category A)

Projects in the “high risk” category (A) imply potentially diverse significantly adverse or irreversible effects or risks for people (social) or the environment (see Chapter 5). Examples include:

- Major infrastructure projects (e.g. motorways, bridges, airports, transmission lines, railway networks, other rail transport, ...)
- Major projects for energy generation (e.g. large wind farms, large-scale solar farms, ...)
- Use of water resources (e.g. large dams and other water-retaining structures, pump storage plants, hydropower plants, ...)
- Major hydraulic engineering projects (e.g. coastal protection, port facilities, river and canal construction)
- Major waste/waste water management and disposal projects (e.g. waste water systems, waste water treatment plants, landfill sites, recycling plants for household waste and hazardous waste)
- Major industrial projects (e.g. basic chemical industry, manufacture of pharmaceutical products)

Examples of projects with moderate environmental and social risks (category B)

A project is classified in the category “moderate risk” (B) if its potential adverse effects or risks are generally foreseeable, temporary, reversible and restricted to the location of the project. As a rule, these can be avoided or reduced with state-of-the-art countermeasures or with standard solutions. If projects in the “moderate risk” category nevertheless show isolated significant environmental and social impacts and risks, they are categorised as “substantial risk” (B+) (see Chapter 5).

- Infrastructure projects (e.g. roads, local public transport, ...)
- Energy generation projects (e.g. biomass plants, geothermal plants, ...)
- Projects for the use of water resources (e.g. irrigation and drainage projects, water management, water supply, ...)
- Hydraulic engineering projects (e.g. coastal protection, port and canal construction)
- Waste/waste water management (e.g. landfills, landfill remediation, pretreatment, ...)
- Larger construction projects (e.g. tourism facilities, industrial/commercial parks, shopping centres, ...)

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