

ARAB AFRICAN INTERNATIONAL BANK
Cairo, Egypt

**Report on Arab African International Bank's
Implementation of the Equator Principles**

2009

5 March 2010

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1. Background

Having chosen to adopt the Equator Principles (EP) in February 2009, Arab African International Bank (AAIB) set out a process to ensure the implementation of these principles in its operations in order to ensure that the projects financed and those advised on over USD 10 Million are developed in a manner that is socially responsible and reflect sound environmental management practices and thereby in full conformity with the Equator Principles.

2. Objectives of this report

This report covers:

- The process by which AAIB implemented the Equator Principles (“the Principles”); and
- Our 2009 Reporting obligation under the Principles.

AAIB had commissioned an external independent consultant to assist with the application and reporting of the Principles. This report outlines the steps taken to achieve full implementation in our first year of adoption of the principles. In addition, the report providing a summary of the procedures by which AAIB uses in respect of the Principles.

The Principles are a framework to help financial institutions to address potential environmental and social risks when providing project finance loans or project finance advisory services. They consist of 10 principles – the first nine refer to the process to determine and manage environmental and social risk, while the final one requires institutions to report publicly on their application of the Principles. AAIB adopted the Principles in February 2009 and completed the implementation on November 2009. For the purposes of reporting 1 December 2009, has been used as the start date.

3. Process by which the EP implementation project was carried out

3.1 Consultant selection

We undertook the process of selection and contracting of the consultant over a period of 3 months with an offer being made to the consultant (see Appendix A) during August 2009. The project was carried out over an agreed project plan (Refer Appendix B) by undertaking the following phases.

3.2 Review of the current lending operations at Arab African International Bank in terms of policies, procedures and departments involved in the project life cycle (Impact Analysis).

It was imperative to gain an understanding of how the implementation of the Equator Principles would affect AAIB in terms of its operational workflows and organisational structure. As such, initial planning reviewed all applicable lending policies, procedures and workflows and assess how best to implement the Equator Principles within the Bank.

Once the Impact Analysis report was delivered by the consultant, various discussions covering the issues raised took place to ensure all impacts were covered appropriately. These issues covered staffing requirements, curtailing of some operations that represented excluded activities going forward and mechanisms to be used to facilitate client awareness and buy-in.

3.3 Integration of the Equator Principles within AAIB's policies and procedures.

Once the impact analysis and assessment stage was completed, the consultant proceeded with the writing up AAIB-specific policies and procedures in respect of the Equator Principles.

The policies and procedures outlined the detailed manner in which qualifying AAIB-financed projects will abide by the Equator Principles. The procedures also identified how the responsibilities, in the implementation of these principles, were apportioned between the various concerned departments and committees where applicable (Refer below).

Deliverable received was the written AAIB Policy and Procedures and matrix of departmental responsibilities.

3.4 Training of the Credit Department and/or Risk Management Department staff in the new Equator Principles Policy and Procedures (Including initial screening and categorisation).

A 2 day training session X 2 took place off site in which around 50 credit and risk management staff took part which covered the new adopted Equator Principles as well as the amended policies, procedures and processes.

3.5 Identification of companies within Egypt which AAIB would be able to accredit in order to provide its clients with required Environmental and Social Assessments.

The process of implementing the Equator Principles and AAIB client conformance to applicable Egyptian legislation (e.g. Law no. 4 dated 1994 issued by the Ministry of State for Environmental Affairs etc) required that AAIB be satisfied with the firms contracted by its clients to carry out the required environmental and social assessments.

In this connection, we identified 5 companies directly and received from them acceptable pre-qualification information in order that AAIB may accredit them for potential future assignments by AAIB clients. We also issued an Invitation for an Expression of Interest (Refer Appendix C) in the press to add to the list of companies able to perform the required assessments and assignments under the Equator Principles.

4. AAIB's new EP policy and procedures

AAIB's internal policies and procedures for applying the Principles are contained as a separate section within its Credit manual (Manual). The Manual sets out AAIB's policies for credit risk, including environmental and social risk, and applies to AAIB and its subsidiaries.

Policies and procedures are based on the format of the Principles themselves and is provided below (n.b. Italics indicates terminology summarised from the Principles). We outline below the procedures going forward as we have laid them out in our new section of our Credit manual.

Firstly, the division of the responsibilities is covered as follows:

Role	Responsible Department/Ownership
Initial Project Screening	Corporate Marketing and Corporate Finance & Investment Banking
Project Review and Categorisation	Corporate Marketing, Corporate Finance & Investment Banking and Risk Management
Social and Environmental Assessment	AAIB Appointed External Consultant
Environmental and Social Action Plan	AAIB Appointed External Consultant
Consultation and Disclosure	Borrower/AAIB Appointed Consultant
Grievance Mechanism	Borrower/AAIB Appointed Consultant
Independent Review	AAIB Appointed External Consultant
Loan Agreement Covenants	AAIB Legal Affairs/AAIB Appointed Legal Counsel
Independent Monitoring and Review	Risk Management, AAIB appointed External Consultant and Corporate Marketing
Annual Reporting	Risk Management

Secondly, we dealt with each Equator principle as follows:

Principle 1: Review and Categorisation

When a project is proposed for financing, the EPFI will, as part of its internal social and environmental review and due diligence, categorise such project based on the magnitude of its potential impacts and risks in accordance with the environmental and social screening criteria of the International Finance Corporation (IFC).

We have implemented the above as follows:

AAIB will now categorise each project finance loan as Category A, B or C according to the potential environmental and social impacts, as described in the Social and Environmental Assessment, an Independent Report or an internal report, using this categorisation to then adopt the relevant credit and approval procedures.

Principle 2: Social and Environmental Assessment

For each project assessed as being either Category A or Category B, the borrower has conducted a Social and Environmental Assessment (“Assessment”) process² to address, as appropriate and to the EPFI’s satisfaction, the relevant social and environmental impacts and risks of the proposed project (which may include, if relevant, the illustrative list of issues as found in Exhibit II). The Assessment should also propose mitigation and management measures relevant and appropriate to the nature and scale of the proposed project.

We have implemented the above as follows:

- AAIB will apply this Principle to all Category A and B projects. Upon receiving the referred Assessment from the borrower, AAIB will undertake a review to confirm whether the project meets the Equator Principles and that the assessment includes appropriate mitigation and management measures for the risks and impacts identified.
- Where the information in the Assessment is not sufficient or the proposed mitigation and management measures are not satisfactory, AAIB will request further information/action from the borrower.

Principle 3: Applicable Social and Environmental Standards

For projects located in non-OECD countries, and those located in OECD countries (n.b. AAIB has no operations in OECD countries) not designated as High-Income, as defined by the World Bank Development Indicators Database, the Assessment will refer to the then applicable IFC Performance Standards and the then applicable Industry Specific EHS Guidelines (“EHS Guidelines”). The Assessment will establish to a participating EPFI’s satisfaction the project’s overall compliance with, or justified deviation from, the respective Performance Standards and EHS Guidelines.

We have implemented the above as follows:

In respect of Category A and B projects;

- AAIB will review the Assessment to determine whether the project meets the relevant Performance Standards and EH&S Guidelines.

- If the project does not meet the relevant Performance Standards and EH&S Guidelines, AAIB will determine whether a deviation can be justified by the circumstances of the project. In making such a judgement, AAIB will take into account the nature and scale of the deviation, the borrower's response, as well as the projected benefits of the project, and documents the basis of its decision.
- Where a deviation is not justified, AAIB will engage with the borrower in order to seek an improvement in the project, so that it meets the relevant Performance Standards and EH&S Guidelines, otherwise failing that AAIB would have to decline the project. Where a deviation is justified, AAIB will document any mitigating action with the borrower.

Principle 4: Action Plan and Management System

For all Category A and Category B projects located in non-OECD countries, and those located in OECD countries not designated as High-Income, as defined by the World Bank Development Indicators Database, the borrower has prepared an Action Plan (AP)³ which addresses the relevant findings, and draws on the conclusions of the Assessment. The AP will describe and prioritise the actions needed to implement mitigation measures, corrective actions and monitoring measures necessary to manage the impacts and risks identified in the Assessment. Borrowers will build on, maintain or establish a Social and Environmental Management System that addresses the management of these impacts, risks, and corrective actions required to comply with applicable host country social and environmental laws and regulations, and requirements of the applicable Performance Standards and EHS Guidelines, as defined in the AP.

We have implemented the above as follows:

AAIB will apply this Principle to all Category A and B projects as follows.

- AAIB will review the AP to check it addresses the findings and conclusions in the Assessment.
- Where the AP does not immediately address the findings in the Assessment AAIB will engage with the borrower to correct the AP.
- AAIB will then confirm that the borrower has or will develop a Social and Environmental Management System that will help to ensure that the project complies with the applicable social and environmental standards.

- Where the Social and Environmental Management System is considered inadequate, AAIB will tackle the inadequacies and ensure corrective actions are implemented.

Principle 5: Consultation and Disclosure

For all Category A and, as appropriate, Category B projects located in non-OECD countries, and those located in OECD countries not designated as High-Income, as defined by the World Bank Development Indicators Database, the government, borrower or third party expert has consulted with project affected communities in a structured and culturally appropriate manner. For projects with significant adverse impacts on affected communities, the process will ensure their free, prior and informed consultation and facilitate their informed participation as a means to establish, to the satisfaction of the EPFI, whether a project has adequately incorporated affected communities' concerns.

We have implemented the above as follows:

- AAIB will apply this Principle to all Category A projects and, based on its analysis of the Assessment and AP, to relevant Category B projects, documenting the rationale.
- Where consultation is required, AAIB will obtain and will review documentation to confirm that consultation with project-affected communities is undertaken in a structured and appropriate manner. In addition, we will seek to determine that the process ensures their free, prior and informed consultation and facilitates their informed participation as a means to establish whether a project has adequately incorporated affected communities' concerns.
- AAIB will also ensure that the Assessment and the AP, or non-technical summaries of these documents, are made available to the public by the borrower for a reasonable minimum period and in an appropriate manner. In addition, AAIB will verify that the borrower documents the process and results of the consultation, including any actions agreed resulting from the consultation.

Principle 6: Grievance Mechanism

For all Category A and, as appropriate, Category B projects located in non-OECD countries, and those located in OECD countries not designated as High-Income, as defined by the World Bank Development Indicators Database, to ensure that consultation, disclosure and community engagement continues throughout construction and operation of the project, the borrower will, scaled to the risks and adverse impacts of the project, establish a grievance mechanism as part of the management system. This will allow the borrower to receive and facilitate resolution of concerns and grievances about the project's social and environmental performance raised by individuals or groups from among project-affected communities. The borrower will inform the affected communities about the mechanism in the course of its community engagement process and ensure that the mechanism addresses concerns promptly and transparently, in a culturally appropriate manner, and is readily accessible to all segments of the affected communities.

We have implemented the above as follows:

AAIB will apply this Principle to Category A projects and, based on its analysis of the Assessment and the AP, to relevant Category B projects, documenting the rationale for the decision. Where a grievance mechanism is required, AAIB will obtain and review relevant documentation to confirm that:

1. Consultation, disclosure and community engagement continues throughout the construction and operation of the project.
2. The borrower receives and facilitates resolution of concerns and grievances about the project's social and environmental performance raised by individuals or groups from among project-affected communities.
3. The borrower informs the affected communities about the mechanism in the course of its community engagement process and ensures that the mechanism addresses concerns promptly and transparently, in an appropriate manner, and is readily accessible to all segments of the affected communities.

Principle 7: Independent Review

For all Category A projects and, as appropriate, for Category B projects, an independent social or environmental expert not directly associated with the borrower will review the

Assessment, AP and consultation process documentation in order to assist EPFI's due diligence, and assess Equator Principles compliance.

We have implemented the above as follows:

- AAIB will apply this Principle to all Category A projects and, based on its analysis of the Assessment and the resulting AP, to relevant Category B projects, documenting the rationale.
- AAIB will establish that the social or environmental expert is independent from the borrower.
- AAIB will analyse the Independent Review to determine the borrower's adherence to the Principles and whether the categorisation remains appropriate.
- The findings from the review will be documented and, where appropriate, raised with the borrower.

Principle 8: Covenants

An important strength of the Principles is the incorporation of covenants linked to compliance.

We have implemented the above as follows:

Loan agreement covenants have/will be enhanced with those relevant to the project Assessment and AP. Where the borrower is not in compliance with its social and environmental covenants, AAIB will work with the borrower to bring it back into compliance reflecting AAIB's role in the transaction, documenting the process. If the borrower fails to re-establish compliance within an agreed grace period, AAIB will reserve the right to exercise appropriate remedies, documenting the process.

Principle 9: Independent Monitoring and Reporting

To ensure ongoing monitoring and reporting over the life of the loan, EPFIs will, for all Category A projects, and as appropriate, for Category B projects, require appointment of an independent environmental and/or social expert, or require that the borrower retain qualified and experienced external experts to verify its monitoring information which would be shared with EPFIs.

We have implemented the above as follows:

- AAIB will apply this Principle to all Category A projects and, based on its analysis of the Assessment and AP, to Category B projects where appropriate, documenting the rationale where that is the case.
- AAIB has procedures in place to ensure that reports are received over the life of the loan.
- AAIB will review the monitoring reports to check that the project is operating in accordance with the AP.
- Where the project is not operating in accordance with the AP, AAIB has procedures to discuss such issues with the borrower and to address them in accordance with the covenants.

5. Project Reporting

In line with our annual reporting responsibilities and effective 1 December 2009, the date at which we commenced the implementation of the Equator Procedures, we wish to advise as follows:

Table 1 Category and number of Projects Reviewed

EP Category	No. of Projects reviewed
A	1
B	0
C	0

The project in question was an installation of a plant involving the manufacture on an industrial scale of substances using chemical conversion processes.

Appendix A – Consultant

About ToneStar Consulting Ltd

With a base in London and Cairo, ToneStar Consulting Ltd (ToneStar) comprises a group of 10 professionals possessing significant experience in the Banking sector concentrating on risk management, compliance and internal audit. Recently, ToneStar added Environmental Diagnostics, Appraisal and Monitoring as a new banking risk management tool.

Tarek Rouchdy BA ACIB FCCA AMCT – Managing Director

Most recently the Head of Internal Audit of the European Bank for Reconstruction & Development (EBRD), London for over 15 years, Tarek has over 30 years of experience in the Banking industry both as a chief accountant and as an internal auditor. In 2007, after leaving the Central Bank of Egypt where he was CFO, he formed ToneStar Consulting Ltd, a specialised London-based consulting company.

During his career, reported directly to two IMF Managing Directors, one of which is the current President of Germany. During his 30 year career, his experience covered:

1. Audited all lending operations at the EBRD across 23 countries including the operations of the Environmental Appraisal Unit.
2. Participated in the EBRD's 'Sarbanes Oxley' exercise and member of the project Steering Committee. Responsible for ensuring that Internal Audit Department reviewed the implementation of the year long project. In doing so, all risks, control mapping and control testing were fully reviewed by Internal Audit during management's assessment of the effectiveness of controls over financial reporting.
3. Participated in EBRD's Operational Risk Management Group ensuring that all operational risks were identified, measured and mitigated and all process improvements followed up on and implemented.
4. Lead all Fraud and compliance tasks/investigations for the EBRD between 1991-2001 covering over 15 investigations in Central and Eastern Europe. Assisted in the write up of the Bank's Fraud and Investigation Procedures.
5. Pension sector reform at the Egyptian Ministry of Finance.
6. Expert on investigations with a variety of external clients (UNDP, UNESCO etc).

7. Participated in the IMF Safeguard Assessments of the Central Bank of Belarus.
8. Currently, trainer at the Egyptian Banking Institute on internal audit and risk based auditing.

Professional qualifications

- Fellow of the Chartered Association of Certified Accountants-UK
- Associate member of the UK's Chartered Institute of Bankers
- Associate member of the UK's Association of Corporate Treasurers

Appendix B-AAIB Project Timetable-Equator Principles Implementation

Phase/Action	Start Date	Target End Date
Project Commencement Policies/Procedures Review	7 October 2009	13 October 2009
Interviews with Key Project Stakeholders from Credit/Risk/Compliance Departments	14 October 2009	15 October 2009
Synthesis of Planning Results/Impact Analysis	18 October 2009	20 October 2009
Policies and Procedures	21 October 2009	10 November 2009
Meetings with Key stakeholders	11 November 2009	11 November 2009
Training sessions (x 2)	15 November 2009	20 November 2009
Pre-qualification Criteria and external consultant identification	22 November 2009	23 November 2009
Final Exit Meetings	25 November 2009	25 November 2009

Appendix C

Invitation for Expressions of Interest

Type of Contract: Consultancy

Type of Notice Invitation for Expressions of Interest

Issue Date 01 December 2009

Closing Date 31 December 2009

Ref: DKader

Assignment Description

This invitation for *Expressions of Interest* is in connection with Arab African International Bank's lead as the first Egyptian Bank to adopt the Equator Principles (EP) in its project financing in January 2009.

Arab African International Bank SAE has established a reputation as a market innovator in banking products as well as a recipient of a number of international awards most recently Euromoney's 'Best Bank in Egypt' for 2008. The adoption of the Equator Principles is therefore a step along the same path that the Bank has forged within the Egyptian market and a continuation of the Bank's strategic mandate to practice Corporate Social Responsibility in its operations.

The banks that have adopted principles that safeguard social and environmental issues in their project finance operations, the Equator Principles Financial Institutions (EPFIs), have consequently adopted these Principles in order to ensure that the corporate finance projects they finance or advise on over USD 10 Million are developed in a manner that is socially responsible and reflect sound environmental management practices.

In this connection, the Arab African International Bank (AAIB) intends to select a number of suitably qualified consultancy firms which will provide AAIB borrowers and clients with the requisite environmental and social assessment and monitoring services that comply with the Equator Principles. For full information on the Equator Principles, please refer to www.equator-principles.com

Suitably qualified firms are to assist the Bank's clients by carrying out varied and wide ranging environmental and social due diligence as well as monitoring to enable the Bank to appraise, subsequently finance and monitor qualifying projects.

Consultant Profile

The Consultant should be a firm or a consortium of firms with substantive expertise and experience in the following fields:

- Environmental and social impact assessments;
- Environmental and social audits;
- Environmental and social management and training;
- Environmental and social capacity building.

Submission Requirements

In order to determine the capability and experience of consulting firms seeking to be shortlisted, the information submitted should include the following:

- (1) Company profile, organisation and staffing;
- (2) Details of experience or similar assignments undertaken in the previous five years, including their locations;
- (3) CVs of staff available to work on qualifying assignments.

The above information should not exceed 30 pages excluding CVs, and Expressions of Interest should be submitted, in English as well as electronically.

The *Expressions of Interest* will be scrutinised by members of a panel selected from within AAIB. Firms which are deemed to meet these criteria will be accepted by the Bank as accredited firms from which AAIB borrowers and clients may select from in soliciting services such as those mentioned above.

5 copies of the above information, in English (along with an electronic copy to the e-mail below), should be submitted to the address below in envelopes marked "Expression of Interest for the Supply of ES Consulting Services" to arrive at AAIB not later than 12:00rs on 29 December 2009 and clearly marked for the attention of:

Dr. Dalia Abdel Kader
Arab African International Bank

Address : 5 Midan Al-Saray Al Koubra Garden City – Cairo

Telephone : (2 02) 2792-4770

Postal Office : Box 60 Magless El Shaab (11516) Cairo – Egypt

E-mail : dkader@aaib.com