# 1. Overview

Sometimes client's management can be reluctant to engage with an FI on environmental and social (E&S) factors. This reluctance can be caused by a variety of factors including capacity constraints, lack of familiarity with E&S or a failure to understand the materiality of E&S to their operations. Understanding the source of such resistance, and the specific E&S risks and opportunities that a client faces allows the FI to respond with empathy to such reluctance and provides a platform for informed discussions about a more proactive approach to management of E&S factors.

- Frequently encountered causes for resistance
  - **Capacity constraints:** management may be concerned about the consequences of committing staff or other resources to addressing 'additional' E&S factors. Perceived cost implications or additional calls on management time can also create reluctance to engage.

  - **Misaligned responsibilities:** Responsibility for E&S matters may reside with the wrong business function. For example, responsibility for community engagement may fall to the environmental manager, who does not have the skillset or time to engage with the community.

  - **Management intransigence:** Lack of management understanding, support, time or commitment to E&S matters. Management may not understand or be convinced by the business case. They may be unaware of how good E&S management can add value to their business.

  - **Business case:** The E&S business case might not have been made for the client (this can also be caused by misunderstanding the financial value driver's behind 'sustainability' or 'impact mitigation'). It is better to focus on how good E&S management can mitigate risks of default, reduce costs or offer opportunities to improve credit ratings. See example at the end of this Annex.

  - **Cost:** Management may have concerns that the outcomes from E&S due diligence (DD) could place additional strain on capital expenditure (CAPEX) which may already be tight. This is often coupled with concerns that costs will be incurred immediately (rather than brought in over time – as is usually the case).

  - **Staff incentive schemes:** These can conflict with the objectives of an environmental and social management system (ESMS) or Action Plan if they encourage and reward activities or behaviours that contribute to E&S risks and impacts. For example, production staff might be incentivised to maximise production with no regard for waste generation or energy use. Or the Occupational health and safety (OHS) Manager might be financially incentivised to reduce reported incidents.

  - **Competition:** Management may believe they are being asked to do more than their competitors and that this will make them uncompetitive.
  - **New set of requirements established by an FI with a long-standing relationship with the client:** Existing clients may be reluctant to comply with certain E&S requirements the FI never asked them to comply with.

## 2. Building an understanding with the client

It is important that FI's engage carefully with regards to E&S factors to establish deeper trust, greater awareness and to solidify existing relationships with clients. Care should be taken not to overwhelm management and E&S agendas should be presented in a measured and structured way that reassures clients that E&S management need not be disruptive or onerous. Good ways to establish a positive dialogue include:

- Initiate dialogue early
  - Start conversations about E&S at the beginning of the transaction cycle.
  - Be clear that E&S matters are central to the business process.
  - Describe how E&S improvements can result in improved efficiencies, better worker relations and productivity, better management and improved oversight.
- Align expectations
  - Clarify E&S expectations and be prepared to explain the FI's standards as well as

the likely DD and monitoring processes.

- Emphasize that the goal is to integrate E&S management into existing business practices rather than create new and burdensome functions. New policies and improvements to management systems will occur over time.
- Ensure that the Relationship office/manager, Credit Officer/Analyst, E&S Officer and any other representatives of the FI communicate the same expectations and are consistent in their messages.
- Listen to management's view of their key business needs and seek to align the discussion on E&S matters with their overall strategic ambition.
- Work with Financial Controllers to quantify how addressing E&S risks and impacts can positively influence financial performance.

- Speak of past upside associated with ESG improvements
    - Present a short list of opportunities/solutions linked to E&S performance based on prior experiences.
    - Connect with other clients in the FI portfolio that have overcome similar issues.

- Link action plan to added value

  Position good management of E&S matters as an operational and strategic value driver and a way to enhance the business through:

    - Increasing resilience to E&S risks and impacts (e.g. climate change, water scarcity).
    - Reducing costs by more efficient use of resources and improved production processes.

- Fulfilling supply chain expectations that require higher E&S performance and, thus, potentially gaining access to new markets / clients.
- Complying with current local and international legislation and regulation and proactively planning for future changes (e.g. there is increasing pressure from governments, investors, civil society, local communities and other stakeholders for companies to manage a large number of E&S matters, including issues around resource scarcity, climate change, land acquisition, gender, biodiversity, vulnerable communities)
- Improving the client's image and brand, bringing positive public relations outcomes.
- Increasing employment productivity and reducing staff turnover.
- Increasing favourable customer reaction.
- Reducing environmental and social risks and liabilities.
- Providing a safer working environment and reduced incident/accident rates.
- Enhancing staff environmental awareness, which is good for staff morale and retention.
- Accessing finance from international investors with certain E&S requirements / expectations.

- Ongoing focus
  - Encourage clients to incorporate E&S accountability and roles into job descriptions, and particularly KPIs. Where appropriate, link it to remuneration. This is especially important at senior management levels as leadership and commitment to E&S management can determine the success of the business.
  - Find areas to provide management with positive feedback on their E&S management.

- Look for opportunities to project a public profile that highlights the client's E&S efforts.