

## Annex VII: Accreditation assessment of Applicant 037 (APL037)

### I. Introduction

1. Applicant 037 (APL037), XacBank LLC (XacBank), is a national private sector entity in Mongolia. The applicant serves clients from individuals and micro-, small- and medium-sized enterprises to Mongolia's largest corporations with a full spectrum of inclusive banking, fair investment and other financial products and services. The applicant strives to be a dynamic leader in the Mongolian financial sector, setting the highest standards in corporate governance and social and environmental responsibility, while returning fair value to its shareholders.

2. The applicant submitted its application for accreditation to the Secretariat via the Online Accreditation System on 30 July 2015. The Stage I institutional assessment and completeness check was completed on 25 December 2015 and was progressed to Stage II (Step 1), accreditation review, which was concluded on 13 May 2016. The applicant has applied to be accredited for the following parameters under the fit-for-purpose approach of the GCF:

- (a) **Access modality:** direct access, national. The applicant received a national designated authority or focal point nomination for its accreditation application from Mongolia;
- (b) **Track:** normal track;
- (c) **Maximum size of an individual project or activity within a programme:** small;<sup>1</sup>
- (d) **Fiduciary functions:**<sup>2</sup>
  - 1. Basic fiduciary standards;
  - 2. Specialized fiduciary standard for project management; and
  - 3. Specialized fiduciary standard for on-lending and/or blending (for loans, equity and guarantees); and
- (e) **Maximum environmental and social risk category:** medium risk (Category B/Intermediation 2 (I-2)).<sup>3</sup>

### II. Stage I institutional assessment and completeness check

3. The applicant applied, and was assessed by the Secretariat during Stage I, under the normal-track process.

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<sup>1</sup> As per annex I to decision B.08/02 (annex I to document GCF/B.08/45), "small" is defined as "maximum total projected costs at the time of application, irrespective of the portion that is funded by the GCF, of above USD 10 million and up to and including USD 50 million for an individual project or an activity within a programme".

<sup>2</sup> Decision B.07/02.

<sup>3</sup> As per annex I to decision B.07/02 (annex I to document GCF/B.07/11), category B is defined as "Activities with potential mild adverse environmental and/or social risks and/or impacts that are few in number, generally site-specific, largely reversible, and readily addressed through mitigation measures" and intermediation 2 is defined as "When an intermediary's existing or proposed portfolio includes, or is expected to include, substantial financial exposure to activities with potential limited adverse environmental or social risks and/or impacts that are few in number, generally-site specific, largely reversible, and readily addressed through mitigation measures; or includes a very limited number of activities with potential significant adverse environmental and/or social risks and/or impacts that are diverse, irreversible, or unprecedented".

## 1.1 Legal status, registration, permits and licences

4. The Secretariat reviewed the information provided by the applicant regarding its legal status as well as relevant and applicable registrations, permits and licences.

## 1.2 Institutional presence and relevant networks

5. The applicant has provided a variety of banking products and services to over 650,000 clients through 93 branches operating across the country. The retail banking transformation, piloted from July 2013, to implement international best practices was expanded to cover all 30 branches and sub-branches in Ulaanbaatar as well as 13 rural branches and sub-branches in 6 rural provinces.

6. The applicant became the first commercial bank in Mongolia to focus on providing 'eco' services in 2007 and introduced the first dedicated eco-banking unit in Mongolia in 2009. It is the only commercial bank in Mongolia with a dedicated eco unit. The applicant has successfully introduced specialized financial products that support energy efficient and renewable energy technologies for business sustainability and Green living in both Ulaanbaatar and in its extensive branch network in every Mongolian province.

7. The applicant is seeking accreditation to the GCF in order to create market incentives for Mongolian industries to move towards sustainable production, investing in energy efficiency and renewable energy, increasing energy security, and bettering the environment. It will do this by establishing financial products designed specifically to finance efficient greenhouses that utilize solar power in order to lengthen the growing season and produce more healthy food domestically. The applicant intends to scale up its focus on climate change in its operations in the future.

## 2.3 Track record

8. Since 2010, the applicant has partnered with international organizations to support energy efficiency and renewable energy in Mongolia. The applicant has disbursed USD 9.7 million in loans to producers, retailers and end users of products that reduce carbon emissions. The scope of the projects and programmes related to climate change financed by the applicant include:

- (a) A USD 49.3 million eco-product distribution programme focused on the distribution of energy-efficient products (including over 143,000 improved heating stoves, over 6,200 energy-efficient boilers and other products to low income families in Mongolia's capital, Ulaanbaatar);
- (b) A USD 15 million Green loan programme in order to provide financing options to help to spur a Green growth path for developing the Mongolian private sector by incentivizing sustainability throughout the value chain; and
- (c) A USD 10 million Mongolia sustainable energy financing facility aimed at corporate and industrial clients looking to upgrade their processes and equipment so as to save resources and energy.

## III. Stage II accreditation review assessment

9. The applicant has been assessed by the Accreditation Panel (AP) during Stage II (Step 1) against the standards of the GCF.

10. As part of this assessment, the AP consulted the applicant's website and various third-party websites to complement the information provided in the application.

## 1.1 Fiduciary standards

### 3.3.1 **Section 4.1: Basic fiduciary standards: key administrative and financial capacities**

11. The applicant has an organizational and corporate governance structure that is appropriate to the size and scope of its activities. Its board of directors has three oversight committees: risk management, audit, and governance nominating and compensation committees. The applicant has a process for preparing annual budgets and three-year budget and business plans, as well as systems for monitoring budget and business plan performance against targets.

12. The applicant's annual financial statements are prepared in accordance with the International Financial Reporting Standards. All financial statements include comparisons of financial performance for the year under review with the three preceding financial years. The applicant has transparent and consistent payment and disbursement systems in place with documented procedures and a clear allocation of responsibilities.

13. The applicant has an internal audit division the activities of which are directly and regularly monitored by the applicant's audit committee. The division adheres to risk-based internal audit principles and implements the "International standards for the professional practice of internal auditing" developed by the Institute of Internal Auditors.

14. The applicant has a well-developed internal control framework, which is outlined in the corporate governance section of the applicant's annual reports. The functions that make up the internal control framework include internal audit, risk management and the applicant's various governance oversight committees. An assessment of the adequacy of the applicant's internal controls relating to core financial management areas is undertaken annually by the applicant's external auditors during the audit exercise.

15. The applicant has procurement policies and procedures which are consistent with international and national procurement standards. Periodic procurement audits are carried out to ensure that the applicant, and the entities executing the development projects/programmes which it finances, comply with the applicant's policies and procedures.

### 3.3.2 **Section 4.2: Basic fiduciary standards: transparency and accountability**

16. The applicant has a code of conduct which defines expected ethical behaviour by its staff and all individuals contracted or functionally related to the organization. While the applicant does not have a separate ethics committee to exercise oversight of the institution's ethics function, this role is played by the governance nominating and compensation committee whose terms of reference were provided. The applicant also has a conflict of interest policy which defines what constitutes a conflict of interest and sets out the procedures for disclosing and addressing conflicts of interest.

17. To enforce its ethical standards, the applicant has a whistle-blowing policy through which whistle-blowers are encouraged to report financial mismanagement and other forms of misconduct and are offered confidentiality protections, as well as protection against dismissal or other reprisals. The applicant's website has a live webchat service, a 24-hour call centre, and a feedback section for submitting complaints and reporting misconduct.

18. The applicant has issued a clear statement on its policy of zero tolerance for fraud and corruption. The statement is posted on the applicant's website along with information on avenues for reporting suspected or detected fraud and corruption.

19. The applicant's internal audit division is responsible for investigating cases of violation of its code of conduct. While the terms of reference for the investigation function are set out in the audit charter, the applicant did not have documented procedures for handling complaints received by the division or for managing the investigation process. To address this gap, the applicant developed comprehensive procedures for the investigation of cases of misconduct which were recently approved by its board. However, the applicant has yet to demonstrate effective use of these procedures. In order to fully meet GCF requirements, the applicant would need to provide evidence of the effective use of its investigation procedures.

20. The applicant has an anti-money laundering (AML) and combating the financing of terrorism (CFT) policy, as well as detailed 'know-your-customer' (KYC) procedures. Copies of annual monitoring reports on AML/CFT for 2012 to 2014 were provided. A copy of extracts from an on-site inspection report by Mongol Bank (Mongolia's regulator of commercial banks) shows that the applicant's AML/CFT and KYC procedures are quite robust and comply with the national standards. In order to improve on the implementation of the AML regulations, an annual client risk assessment is performed, which enables the identification and further monitoring of high risk customers and suspicious transactions, with regular reporting of the latter to the national regulator. Sample reports on KYC activities carried out in the past three years were provided. The applicant has recently implemented initiatives, aimed at improving the existing KYC processes, including the review and updating of customers' files, accounts and relevant information, as well as the adoption of new guidelines embracing international best practices.

21. As a major national bank, the applicant handles thousands of electronic transfers on a daily basis. All of these transactions are tracked and recorded within the applicant's management information system. A summary of the applicant's weekly AML monitoring reports, provided in the application, shows that the applicant has a sound mechanism for tracing electronic/wire transfers. In order to enhance the process, all electronic/wire transactions, with the exception of SWIFT international wire transfers, have daily and single transaction limits to safeguard against risks.

### 3.3.3 **Section 5.1: Specialized fiduciary standard for project management**

22. The applicant has detailed policies and procedures that guide its project identification, appraisal, monitoring and evaluation functions. These include loan appraisal and monitoring procedures, general lending procedures and a lending operations manual.

23. Until recently, however, the applicant did not have in place some of the procedures required by the GCF's fiduciary standards, namely procedures for:

- (a) The preparation of project implementation plans;
- (b) Project closure; and
- (c) The independent evaluation of project results.

24. In order to address these gaps, the applicant has developed the required procedures, which were recently approved by its board. However, the applicant is yet to demonstrate the effective use of these procedures. In order to fully meet GCF requirements, the applicant would need to provide evidence of the effective use of procedures for the aforementioned points.

25. The applicant has procedures for monitoring projects under implementation whose purpose is to ensure that project risks/problems are identified and addressed in a timely manner. To ensure objectivity and independence of the monitoring function, responsibility for monitoring projects is assigned to staff who are not involved in the project appraisal process.

### 3.3.4 **Section 5.2: Specialized fiduciary standard for grant award and/or funding allocation mechanisms**

26. The applicant did not apply for assessment against this standard at this time.

### 3.3.5 **Section 5.3: Specialized fiduciary standard for on-lending and/or blending**

27. The applicant has extensive experience with on-lending and blending funds received from major international and multilateral funding sources, such as the International Finance Corporation, the European Bank for Reconstruction and Development and the Asian Development Bank. Technical assistance provided by various development partners has especially enhanced the applicant's sustainable energy financing capabilities and its status as the premier domestic partner for Green finance in Mongolia.

28. The applicant has a documented framework for undertaking due diligence with clearly defined roles and responsibilities and applicable guidelines and procedures for assessing the capabilities of the organizations seeking financing from the applicant. Sample due diligence reports in respect of its on-lending and blending operations show effective use of and compliance with the existing policies and procedures.

29. Until recently, the applicant did not have in place a policy on the disclosure of information to the public on project beneficiaries, project results achieved and lessons learned as required by the GCF fiduciary standards. In order to address these gaps, the applicant has developed the required procedures which were recently approved by its board. However, in order to fully meet GCF requirements, the applicant would need to provide evidence of the effective implementation of its new information disclosure policy.

30. The applicant has also demonstrated sound financial risk and management policies, procedures and governance/organizational structures that ensure appropriate segregation of duties of the treasury function and operations.

31. The applicant has been rated by three rating agencies: 'B3/Not prime' (for short term issuer rating) by Moody's Investors Service; 'B' (for ST foreign currency issuer default rating) by Fitch Ratings; and 'A' by Planet Ratings (a specialized microfinance rating agency).

## 3.2 Environmental and social safeguards

### 3.2.1 **Section 6.1: Policy**

32. The applicant has a well-established environmental and social management system (ESMS) in place that is compliant with the ISO 14000 standards. The development and approval of the ESMS was based on the experience gained and lessons learned by other international development organizations. The ESMS policy document includes a comprehensive statement of the applicant's commitment to the principles of being environmentally and socially-sound, and of sustainable development, and the policy adheres to national environmental and social (E&S) laws and regulations. The ESMS is complemented by E&S management guidelines as well as by the applicant's loan policy, which are applied to ensure that the applicant promotes sustainable development throughout its operations by conducting E&S project loan appraisals in a consistent manner. The roles and responsibilities of specialized units or individuals who collectively ensure the conformity of operations with the applicant's ESMS policy are clearly assigned. The ESMS policy is fully consistent with the GCF interim environmental and social safeguards (ESS) and is well-communicated to all staff in the organization.

### 3.2.2 **Section 6.2: Identification of risks and impacts**

33. The applicant has a well-developed and comprehensive E&S risk and impacts identification and categorization process that is fully consistent with the GCF interim ESS. The risk identification and categorization process is outlined in the applicant's ESMS policy document, which covers all potential E&S risks contained in performance standards 1 to 8. The policy is supported by a scoring system and guidance to staff on identifying E&S risks and impacts of the project/programme over the project life. Evidence of the applicant's experience

in conducting E&S risk and impact assessment and categorization was provided in the form of loan appraisal reports on specific projects and programmes.

### 3.2.3 **Section 6.3: Management programme**

34. The applicant's ESMS policy supported by the risk scoring system provides the guidance for managing mitigation measures and actions stemming from the E&S risk identification process, distinguishing between different categories of risk. As evidence for the implementation of the policy, the applicant provided examples of the E&S assessment and monitoring reports for the investment activities, where minimal to no (Category C/Intermediation 3) and medium (Category B/I-2) E&S risks were identified, corresponding corrective action plans were developed and mitigation measures were undertaken.

### 3.2.4 **Section 6.4: Organizational capacity and competency**

35. The applicant provided information and policy documents describing its organizational structure, as well as roles and responsibilities for E&S reporting on the loans it provides. The E&S Coordinator is responsible for the consistent implementation of the ESMS policy across the applicant's investment activities.

36. E&S risk identification and assessment of investment activities consists of two stages:

- (a) Initial review of the projects by the Loan Officer with regard to the environmental, health and safety requirements of the national legislation, and the applicant's exclusion list of activities contained in its ESMS policy; and
- (b) E&S assessment for further compliance with performance standards 1 to 8 and determination of the grade of the risks and the risk category by the Compliance Officer.

37. The applicant's dedicated eco-banking department undertakes the disbursement of loans for climate change mitigation and adaptation projects/programmes.

38. The applicant's staff responsible for E&S assessment and monitoring has undergone the necessary training conducted by international development organizations, the records of which were provided.

### 3.2.5 **Section 6.5: Monitoring and review**

39. The applicant has established procedures for E&S assessment and monitoring processes for all business loans and microloans provided to its clients. The E&S monitoring and reporting procedure describes the roles and responsibilities of the dedicated committees and staff conducting the initial assessment and regular monitoring and reporting on the loans approved. The dedicated regulatory bodies include the credit committee, the compliance team headed by the Compliance Officer, the sustainability team, the eco-banking department, the Chief Risk Officer and the E&S Manager. The compliance team ensures overall compliance of the applicant's business activities with national environmental legislation and bilateral agreements with investors and shareholders, and also with internationally recognized environmental norms and standards.

40. The applicant undertakes a quarterly survey for branches to affirm that they are properly screening clients for environmental and social risks. The supporting documentation provided includes samples of the reporting sheets from monthly and quarterly updates to final project assessments for environmental projects. The compliance team also compiles and provides E&S performance reports on a regular basis to the applicant's investors, board of directors and partner institutions.

41. In addition, the applicant is a member of the Global Reporting Initiative on good corporate governance, economic, environmental and social performance, as built around the 'three P's': the planet, people and profit.

### 3.2.6 Section 6.6: External communications

42. The applicant has several procedures in place that regulate its process for external communications that is the receipt and processing of inquiries and complaints from the public via a digital feedback section and a live chat feature on its website. In addition, the applicant maintains 24-hour telephone lines and e-mail accounts that can receive communications or complaints from consumers. Apart from the online complaint management system, the applicant works with external surveying organizations to ensure customer satisfaction. The applicant has provided its register of inquiries and complaints received, including the actions taken from each quarter of the last year. The applicant's information disclosure procedure enables it to disclose E&S information on the projects based on the agreement of the stakeholders involved in line with GCF requirements.

## 3.3 Gender

43. The applicant has established a set of separate procedures and practices that regulate gender specific issues. The applicant's approach towards gender mainstreaming is fully consistent with the principles in the GCF Gender policy. Evidence of the competency of staff managing gender-related matters was provided and found sufficient.

44. The applicant tracks the implementation of gender-sensitive approaches for particular projects/programmes. Examples of project documentation indicating the data and information collected on the gender-related outcomes of the projects financed by the applicant were presented. The projects include the distribution of energy-efficiency products, social and financial education programmes, and lending programmes for women entrepreneurs. The presented evidence clearly demonstrates the applicant's practices of collecting and analysing gender and climate data, as well as gender and climate change accountability.

45. In addition, the applicant provides training on its gender policy and project-level gender analyses to relevant staff, such as its Human Resources Officer, Compliance Officer, ESMS Coordinator, and new employees.

## IV. Conclusions and recommendation

### 4.2 Conclusions

46. Following its assessment, the AP concludes the following in relation to the application:

- (a) The applicant partially meets the requirements of the GCF basic fiduciary standards for transparency and accountability, the specialized fiduciary standard for project management, and the specialized fiduciary standard for on-lending and/or blending (for loans, equity and guarantees);
- (b) The applicant meets the requirements of the interim ESS of the GCF in relation to the medium E&S risk (Category B/I-2); and
- (c) The applicant has demonstrated that it has policies, procedures and competencies to allow it to implement its gender policy, which is found to be consistent with the gender policy of the GCF, and has demonstrated that it has experience with gender considerations in the context of climate change.

## 4.2 Recommendation on accreditation

47. The AP recommends, for consideration by the Board, applicant APL037 for accreditation as follows:

(a) **Accreditation type:**

(i) **Maximum size of an individual project or activity within a programme:** small (including micro<sup>4</sup>);

(ii) **Fiduciary functions:**

1. Basic fiduciary standards;
2. Specialized fiduciary standard for project management; and
3. Specialized fiduciary standard for on-lending and/or blending (for loans, equity and guarantees); and

(iii) **Maximum environmental and social risk category:** medium risk (Category B/I-2) (including lower risk (Category C/I-3<sup>5</sup>)); and

(b) **Conditions:** the applicant will be required to submit to the AP, through the Secretariat, information on how it has complied with the condition(s). The AP will thereafter assess whether the condition(s) has/have been met. This assessment will be communicated by the Secretariat, on behalf of the AP, to the Board for information purposes.

(i) Condition(s) prior to the first disbursement by the GCF for an approved project/programme to be undertaken by the applicant:

1. Provide evidence of the effective application of procedures for the investigation of fraud, corruption and other forms of malpractice;
2. Provide evidence of the effective implementation of the procedures for:
  - a. The preparation of project implementation plans;
  - b. Project closure; and
  - c. The independent evaluation of project results; and
3. Provide evidence of the effective implementation of its information disclosure policy.

48. The applicant has been informed of the recommendation for accreditation, including the accreditation type and condition(s), as identified in paragraph 47 above, and agrees to the recommendation.

## 4.3 Remarks

49. The applicant is encouraged to seek readiness and preparatory support to assist it with:

(a) Meeting the condition(s) identified in paragraph 47(b) above.

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<sup>4</sup> As per annex I to decision B.08/02, "micro" is defined as "maximum total projected costs at the time of application, irrespective of the portion that is funded by the GCF, of up to and including USD 10 million for an individual project or an activity within a programme".

<sup>5</sup> As per annex I to decision B.07/02, category C is defined as "Activities with minimal or no adverse environmental and/or social risks and/or impacts" and intermediation 3 is defined as "When an intermediary's existing or proposed portfolio includes financial exposure to activities that predominantly have minimal or negligible adverse environmental and/or social impacts".





50. Following the provisions of its information disclosure policy, the applicant is encouraged to align its disclosure of E&S reports to the requirements of the GCF Information disclosure policy.