



Governance

This guideline expands on what is expected by the criteria statements in the Hydropower Sustainability Tools (HST) for the Governance topic, relating to assessment, management, conformance/compliance, stakeholder engagement and outcomes. The good practice criteria are expressed for different life cycle stages.

In the Hydropower Sustainability Assessment Protocol (HSAP), this topic is addressed in P-2 for the preparation stage, I-2 for the implementation stage and O-2 for the operation stage. In the Hydropower Sustainability ESG Gap Analysis Tool (HESG), this topic is addressed in Section 9.

Governance refers to the combination of processes and structures that inform, direct, manage and monitor the activities of a project or entity towards the achievement of its objectives. This guideline addresses corporate and external governance considerations for the hydropower project and the operating hydropower facility. The intent is that the developer and owner/operator have sound corporate business structures, policies and practices; address

transparency, integrity and accountability issues; can manage external governance issues; and can ensure compliance.

All businesses are operated, regulated, and controlled according to a set of internal rules and processes, which are defined as **corporate governance**. Different corporate processes and structures will be required depending on internal characteristics of the business (e.g a single-project or multi-project entity; government-owned, privately held, or listed on the stock market; or a domestic or multi-national business). These requirements will be further shaped by the external governance environment, such as government regulatory requirements, legal frameworks, and risks.

External governance refers to the political, institutional, legal and regulatory system within which the project is developed and operates. Hydropower projects typically operate in complex external governance environments. A number of different institutions are likely to have responsibilities for different aspects of the hydropower development. These include regulators, which are responsible for electricity generation, transmission and distribution, dam safety, water resource management, environment, labour, and electricity pricing, and agencies, which are responsible for planning, land, emergency services, hydro-meteorology, geology, health, and culture.

Hydropower projects may have different proponents and business structures at different project life cycle stages which influence the ownership model and governance arrangements. Projects may be privately or publicly owned, or a public-private partnership (PPP). Projects may emerge from the public sector, transfer to the private sector at the preparation stage, and return to the public sector at a later stage. Reasons for ownership model changes could be, for example, to accelerate the development timetable by using private developers, to facilitate financing strategies, or to spread risk.

This guideline addresses corporate and external governance considerations that affect the sustainability of the hydropower development project or operating facility. This guideline is not directed at the external governance framework itself (e.g national policy, legislation, government agencies, or government capacity building). It focusses on the developer's and owner/operator's own corporate governance measures, as well as how the developer and owner/operator work within the external governance environment to identify and manage risks associated with external governance (e.g weaknesses, impending changes, emerging trends).

Assessment

Assessment criterion - Preparation Stage: Assessments have been undertaken of political and public sector governance issues, and corporate governance requirements and issues, through the project development cycle with no significant gaps.

Throughout the project cycle, the project and the business to which it belongs need to understand their external governance environment. The political, institutional, legal and regulatory system within which the project is developed and will operate, as well as any issues that may pose risks to the project and any opportunities that may arise, needs to be thoroughly assessed. Even in countries with stable and predictable governance environments, relevant policies and regulations evolve over time or could change after the next election. In countries with unstable governance environments, understanding the challenges can be critical to project success.

External governance roles relevant to the project can be broad and diverse. They include but are

not limited to: the elected government; the civil service/public sector institutions; political parties; anti-corruption organisations; the judiciary; grievance addressing agencies such as the ombudsman; law enforcement agencies; Freedom of Information; the media; local government; financial institutions; international institutions (e.g some provide peer review of anti-corruption efforts); audit/oversight institutions; and the public contracting system.

Examples of external governance issues that may be identified as relevant to a project include:

- gaps, uncertainties or contradictions in regulations, policies and/or standards;
- capacity shortfalls in public institutions in relation to, for example, staff numbers, expertise levels, and regulatory frameworks and policies;
- demands for illicit payments;
- disagreements between jurisdictions affected by the project;
- transboundary issues, e.g inconsistent regulations and standards, and their enforcement; and
- changes in government or policies.

Such issues can lead to delays or denials of approvals, reduced financial viability of projects, or reputational problems. On the other hand, opportunities may arise in the external governance environment, for example through developments in renewable energy legislation, emerging policies, synergies with other development objectives, and stronger institutional coordination (e.g the water-energy nexus). Businesses need to ensure that they have adequate information, whether by commissioning assessments (for example as part of feasibility studies and the Environmental and Social Impact Assessment (ESIA)), assigning staff specifically to following political and regulatory issues, or relying on analyses by business associations or external advisers.

Specific external governance risks that should be well-assessed at the project preparation stage include:

- **Political risk** – the risk of financial loss or inability to conduct business faced by investors, corporations, and governments due to, for example: government policy changes; government action preventing

entry of goods; expropriation or confiscation; currency inconvertibility; politically-motivated interference; government instability; or war.

- **Transboundary risks** – limitations or uncertainties in the institutional arrangements between neighbouring jurisdictions that address boundary-related issues, such as the management of project impacts in a river system, transport of goods and services, and information and resource sharing.
- **Corruption risks** – these may occur within the business, such as issues with how finances are managed; external to the business, such as bribery in the supply chain; or within the public sector, such as a failure to address licence or permit violations. Public sector corruption risk examples include short-cutting of assessment or preparation requirements, non-transparent approvals, and ignoring licence and permit violations.

Corporate governance requirements also need to be well-understood as they apply throughout the project cycle. Corporate governance components typically include: the roles of the Board of Directors and the executive management team; business structure and administration; policies and processes; risk; accountability; internal and external reporting; auditing; compliance; Corporate Social Responsibility (CSR); ethical business practices; culture; and stakeholder and shareholder relations and engagement.

Examples of corporate governance issues include: an absence of key policies such as for CSR, transparency, stakeholder engagement, or anti-bribery; key roles not filled; a lack of internal financial controls and weak audit processes; internal corruption risks; poor documentation of compliance; a lack of Board- or Executive-level focus on key performance indicators related to sustainability (e.g safety, working conditions, environment, stakeholders); or a lack of project management or other relevant capacities.

Corporate affairs, legal, audit and similar departments are often tasked with assessing corporate governance requirements or issues and monitoring the effectiveness of corporate governance arrangements over time. International standards for corporate governance can be referred to as a guide to good practice, and periodic independent review and advice can help ensure processes are comprehensive and up-to-date with evolving expectations.

Assessment

Assessment criterion - Implementation and Operation Stages: Processes are in place to identify any ongoing or emerging political and public sector governance issues, and corporate governance requirements and issues, and to monitor if corporate governance measures are effective.

In addition to all expectations outlined within the preparation stage assessment guidance, the processes for monitoring of effectiveness take on particular importance at the implementation and operation stages. Examples of mechanisms for monitoring the effectiveness of corporate governance measures include internal audit, external audit, independent reviews, benchmarking exercises, and topic specific evaluations (e.g on occupational health and safety).

Management

Management criterion - Preparation, Implementation and Operation Stages: Processes are in place to manage corporate, political and public sector risks, compliance, social and environmental responsibility, grievance mechanisms, ethical business practices, and transparency; policies and processes are communicated internally and externally as appropriate; and independent review mechanisms are utilised to address sustainability issues in cases of project capacity shortfalls, high sensitivity of particular issues, or the need for enhanced credibility.

Good international industry practice for the governance of hydropower projects requires that a number of key management processes are clearly demonstrated. These are outlined in turn below.

Corporate, political and public sector risks.

A risk management process should be in place. This should be based on a risk register that rates all risks by their probability and impact (often estimated in financial terms), describes mitigation measures, and assigns risk owners. The register should be updated periodically to reflect new information and be integrated with other corporate processes (for example setting performance targets for risk owners and budgeting for mitigation measures). Depending on their sensitivity and the organisational structure, corporate, political and public sector

risks may be handled separately from project-level technical, environmental and social risks. If risks have been identified, both risk management measures and follow-up monitoring should be evident.

Compliance. A standard compliance assurance process should be in place. This should be based on a register of all relevant legal and regulatory requirements, licence conditions, and reporting requirements. The compliance register would also ideally contain requirements resulting from internal policies and voluntary commitments. Responsibility for each requirement should be clearly assigned, and a central compliance role should update requirements and track compliance over time. A well-functioning compliance process will go a long way towards establishing good relationships with regulators and other stakeholders.

Social and environmental responsibility.

Policies, programmes, and plans for social and environmental responsibility should be in place. These should primarily cover the core business activities (i.e. responsible development and operation of hydropower projects) and secondarily any additional voluntary commitments such as under a CSR commitment, or in the form of benefit sharing or grants. Internal processes should allocate responsibilities and budgets and also establish transparent rules for decisions on external requests for support (for example under a community development fund or a research and development fund).

Procurement of goods and services. From a governance perspective, procurement is both a source of potential risks (primarily corruption and conflicts of interest) and an opportunity to have a positive influence beyond the direct scope of the business. Procurement plans and processes should include a procurement policy, pre-qualification screening, bidding, awarding of contracts, anti-corruption measures, and mechanisms to respond to bidder complaints (see the Procurement guideline).

Ethical business practices. The business should have a number of processes to ensure and demonstrate that unethical practices are avoided, detected and dealt with appropriately. Examples include: a business code of ethics; an employee code of conduct; a business integrity pact; anti-

bribery or anti-corruption policies; internal and external auditing; procedures for reporting and investigation; a whistle-blowing arrangement; and confidentiality limited to legally protected information. While they may take significant effort to put in place and administer, such instruments are designed to reduce expenditure as well as risks associated with ethics breaches and give confidence to business partners and investors.

Grievance mechanisms. Grievance mechanisms are processes by which concerns or complaints can be raised and will be reviewed and responded to in a timely manner. These should be open to any grievances related to the project and the business, including from project affected people and businesses, workers, contractors, customers, and civil society groups. These may be divided into several separate mechanisms for practical purposes, with some (e.g those relating to labour or procurement) based on mechanisms enshrined in law. A well-functioning grievance mechanism provides early warnings of issues so that they can be addressed before turning into major problems.

Transparency. Corporate policies, processes, activities and results should be communicated internally and externally as appropriate, taking into account business size, capacity, ownership, public interest in specific issues, and any legal requirements (such as regulations on the 'right to know' or 'freedom of information', and on privacy). Transparency is also a key aspect of effective stakeholder engagement.

Independent review. Independent review should be used for sustainability issues in cases of project capacity shortfalls, high sensitivity, aspects of uncertainty, or the need for enhanced credibility. Independent review is defined as review by experts who: are not employed by the project, have no financial interest in profits made by the project, are unaligned with the project in any other manner, and are generally perceived as being objective. An expert is a person with a high degree of skill in or knowledge of a certain subject as a result of a high degree of experience or training in that subject. In the absence of review by regulators, forms of independent review may vary from contracting an expert consultant to provide a written review of a particular assessment, plan or report to a Panel of Experts (PoE). A PoE usually comprises a mix of expertise appropriate to the project and provides

both periodic assessment and written reports on issues identified as being within its scope of review.

Additional governance measures may be necessary depending on the issues identified through the assessment process.

Stakeholder Engagement

Stakeholder Engagement criterion - Preparation, Implementation and Operation Stages: The business interacts with a range of directly affected stakeholders to understand issues of interest to them; and the business makes significant project reports publicly available, and publicly reports on project performance, in some sustainability areas.

Good corporate governance is based on and results in positive and productive relationships with other stakeholders. Understanding stakeholder interests is a precondition for targeting the right stakeholder groups with relevant information and relevant mechanisms for engagement. The process of stakeholder mapping and analysis is a good starting point for identifying the issues of particular interest to different stakeholders. This is usually complemented by direct questions to stakeholders through individual interactions, community meetings, inviting public comments, or surveys. Some businesses undertake a formal materiality analysis each year to ensure that what is published in annual reports reflects what stakeholders are most interested in hearing about. More details about approaches and expectations for stakeholder engagement are provided in the Communications and Consultation guideline.

The developer and owner/operator should make significant project reports publicly available. Which reports are significant will vary with project, but the ESIA or a non-technical summary of the ESIA should always be included. Provision of significant reports helps to engage stakeholders in a process of project improvement, minimise disinformation and rumours, focus stakeholder engagement on areas of particular interest, and create mutual trust and confidence. Information availability in the local language(s) of the target stakeholders is important to ensure accessibility.

Good practice also requires regular public reporting on sustainability aspects of the project or operating hydropower facility. Sustainability aspects might include those that relate to the environment, community, safety, engagement, project benefits, labour and ethics. This helps the developer or owner/operator to demonstrate its willingness to be transparent and provides a basis for sustained dialogue. Information on project progress and sustainability performance can be released through annual corporate, environmental, or sustainability reports; project progress and monitoring reports; independent evaluation reports; real-time access to data (for example on water levels and water quality); and by other means. Some projects have created independent monitoring mechanisms where relevant data is tracked over years and published to demonstrate baselines and project impacts.

Conformance/Compliance

Conformance/Compliance criterion - Preparation, Implementation and Operation Stages: The project and operating hydropower facility has no significant non-compliances.

Good practice requires evidence that the project and operating hydropower facility are fully compliant with the relevant jurisdictional requirements. These may be expressed in licence or permit conditions or captured in the relevant legislation. Compliance requirements may relate to, for example, standards to be met, the frequency and type of monitoring to be performed, audit schedules, and reporting to be submitted by the owner to government.

The compliance obligations for the project will need to be established and tracked with a compliance register. Compliance monitoring reports would document the project's compliance against legal obligations and may be a requirement of external regulators. There may also be compliance obligations arising from conditions of lenders to the project. Compliance requirements can change over time. In some jurisdictions the legislation, regulations and policies are changing rapidly, so there should be evidence that the compliance register is regularly updated.

The significance of a non-compliance is based on the magnitude and consequence of that omission and will be context-specific. For example, a failure to demonstrate delivery of a licence entitlement for resettlers is a significant non-compliance. A slight delay in delivery of a monitoring report could be non-significant, depending on the consequences. Repeat delays in meeting compliance requirements can erode trust and confidence in the developer, which can have longer-term ramifications.

Outcomes

Outcomes criterion - Preparation, Implementation and Operation Stages: There are no significant unresolved corporate and external governance issues identified.

It is to be expected that the hydropower developer or owner/operator will be required to address issues of varying types relating to corporate and external governance. Of

importance is that any governance-related issues are recognised and that actions are underway towards their resolution in a timely manner. An external review of governance-related issues for the business can help inform how well the business has avoided, minimised and addressed governance-related issues.

The significance of any unresolved issue would be with respect to the magnitude and severity of the consequences of non-resolution. In most cases, the actions underway are likely to lead to a resolution of the issue. An example of a significant unresolved governance issue could be a major court case against the project that has not yet concluded and could stop the development, or corruption charges against the CEO that are being investigated. A strong governance framework underpinned by good assessment, management, engagement and compliance measures should help ensure that significant unresolved governance issues are unlikely.