Private Banks As Agents Of Environmental Protection: The Equator Principles

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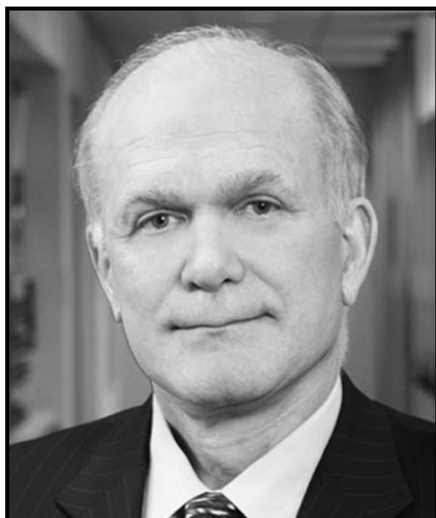
Responding both to public pressure and financial risk, private lenders are becoming more concerned about the environmental and social risks their borrowers' projects may create. Rather than experiment with different approaches to identifying these portfolio risks, the major banks agreed to collaborate and develop a common environmental and social risk assessment framework called the Equator Principles, adopted in June of 2003 by ten of the world's largest international lenders (see box). Ten more banks have since signed on. For details see www.equator-principles.com.[1]

Borrowers for projects in the US and abroad whose businesses are in the energy, natural resources, transportation, agriculture, and manufacturing sectors, take note: as a result of the Equator initiative, your major lenders have become private agents of environmental protection. They are now publicly committed to broad environmental and social reviews of your financing plans, not only under the Equator Principles, but also under an accumulating body of additional reviews regarding greenhouse gas releases, forestry practices, and environmentally and socially sustainable investment opportunities.

The Equator Principles are a set of voluntary project finance guidelines for management of social and environmental issues. The Principles were drafted by the International Finance Corporation (IFC) in collaboration with Citigroup, ABN Amro, Barclays, and WestLB with the input of non-governmental organizations (NGOs), such as the World Wildlife Fund and Friends of the Earth. Further, after public pressure by the Rainforest Action Network (RAN), Citigroup agreed to additional reviews to address forest biodiversity and climate. Then RAN recently gave nine large additional banks a deadline to "meet or beat" Citigroup's policies.

The heart of the Equator Principles is their adoption of the "safeguard policies" and environmental guidelines already in place at the World Bank and IFC. The new undertakings go well beyond standard environmental engineering reviews under the World Bank Pollution Prevention and Abatement Handbook and International Finance Corporation (IFC) environment-specific policies. The banks must now evaluate documentation involving protection of cultural property and indigenous lifestyles, a wider range of socio-economic impacts and mitigation, land acquisition and involuntary resettlement, cumulative impacts from the local to the global scale, culturally-appropriate involvement of affected parties in project design and operation, alternatives analysis (including a no-build option), adequacy of local government infrastructure, sustainable development, and energy and materials conservation and reuse.



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The framework may be common to all twenty banks, but each signatory still must use its best individual judgment in implementing the Principles. The Equator Principles are not subject to oversight by any independent authority. The creators of the safeguard policies, the World Bank and IFC, explicitly disavow any responsibility under the Principles. Nor does an independent dispute resolution mechanism exist. No independent environmental and social investigatory entity has been created similar to the World Bank's Inspection Panel or the IFC's Compliance Advisor and Ombudsman (CAO). The banks therefore are under considerable pressure to "get it right" the first time, because their customers, the NGOs, and host governments have no place to turn in case financing is improvidently granted or denied. A bank is literally an interested party, investigator, judge, and appeals tribunal, all rolled into one.

Despite extensive NGO involvement in World Bank/IFC review under their safeguard policies, some NGOs continue to oppose projects they believe are inconsistent with environmentally and socially sustainable development. For example, years of planning and extensive consultation went into identifying and mitigating the Chad-Cameroon oil pipeline project's impacts; nevertheless, NGO criticism remains strong today.

Banks and NGOs will continue to have opposing interests. But the skirmish line is now moving from principles to the individual projects in which the banks will want to invest worldwide. A multi-NGO campaign seeks to stop investment in international exploration and development in fossil fuels (coal, oil, gas), large hydroelectric, and mining. There are any number of other types of development banks may want to support in agriculture (large agro, genetically enhanced crops), infrastructure (gas and oil pipelines), and transportation that will not meet at least some NGOs' standards for sustainable, environmentally benign development.

Having submitted to strict project review, banks now take an anxious interest in where World Bank-IFC environmental policies may next lead them. Just recently, the 20 Equator signatories were poised to ask the World Bank to reject NGO calls to stop financing oil and coal projects in developing countries. The 20 banks said that recommendations made in the Bank's Extractive Industries Review – an independent review that asks the Bank to stop financing all oil and coal projects in the developing world – do not take into consideration the financial gain of those projects for poorer nations and therefore should not be adopted. Friends of the Earth called the banks' move "outrageous" and urged them to "honor the spirit of the Equator Principles and to publicly support the EIR recommendations" (*Financial Times,* April 5).

Whether the banks have bitten off more than they can chew, only time will tell. In the absence of independent oversight and dispute resolution and mediation mechanisms, the banks are pretty much on their own, with the NGOs more than willing to judge the banks' performance. First and foremost, the banks will need to show how they scrupulously reviewed each loan package. They may also want to put in place self-policing practices involving the same kind of painstaking effort, but up-front and prior to funding approval, that goes into after-the-fact investigations and inspections that often are called for only later when controversy erupts over project impacts.

The Equator Principles

The Principles apply to projects with a total capital cost of $50 million or more. Such projects represent most of the project finance market. The Equator banks first categorize proposed projects into high (A), medium (B), or low (C) environmental and social risk based on existing World Bank and IFC categories, taking into account the type, location, sensitivity and scale of the project and the nature and magnitude of its potential environmental and social impacts.

For high and medium risk projects, borrowers must:

- complete an environmental assessment (EA) addressing applicable environmental and social issues and compliance with applicable host country laws, regulations, and permits;
- ensure compliance with the numerous, extensive "safeguard policies" in place in the World Bank and IFC;
- complete an environmental management plan (EMP) addressing mitigation, action plans, monitoring, management of risk, and schedules;
- provide for independent expert review of the EA and EMP of all category A projects;
- consult with affected groups, including indigenous persons and local NGOs; and
- covenant to comply with the EMP.

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[1] *The 20 banks which have adopted the Equator Principles are: ABN AMRO Bank, N.V., Barclays plc, CIBC, Citigroup Inc., Crédit Lyonnais, Credit Suisse Group, Dexia Group, Dresdner Bank, HSBC Group, HVB Group, ING Group, KBC, MCC, Mizuho Corporate Bank, Rabobank Group, Royal Bank of Canada, Standard Chartered Bank, The Royal Bank of Scotland, WestLB AG, and Westpac Banking Corporation.*

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