

## **Welcoming the Act But Holding the Applause: The Equator Principles on Project Finance**

In June 2003, a coalition of investment banks will launch the Equator Principles, a set of voluntary project finance standards based on the social and environmental safeguard policies of the private finance arm of the World Bank – the International Finance Corporation (IFC). Banks that endorse the Equator Principles (EPs) commit to categorize projects based on their social and environmental sensitivity. For the most sensitive projects, banks would require corporate clients to prepare environmental assessments, do public consultation, and create mitigation plans. The banks would then require such mitigation as a part of its loan agreement with the client. Because many large and controversial projects such as oil pipelines and dams are often funded through project finance, the Equator Principles have the potential to promote more responsible corporate behavior.

Many non-governmental organizations (NGOs) welcome the fact that the Equator Principles recognize that private banks have a role in and responsibility for the social and environmental impacts of their transactions. In addition, the EPs represent an industry approach, in which several banks are working together. This collaboration helps level the playing field among banks, and reduces the ability for corporate clients to shop around for a bank that has lower environmental and social standards.

However, NGOs are holding their applause. The Equator Principles only apply to direct lending for project finance. Many sensitive transactions, such as mining and forestry activities, are more likely to be funded through lines of credit or corporate loans, and thus are exempt from the EPs. Most importantly, the EPs' limited scope and lack of accountability mechanisms could potentially prove to be fatal flaws.

For example, the lack of transparency requirements prevents endorsing institutions, peer banks and the public to monitor implementation. The EPs also do not require endorsing banks to hire staff or take other steps to oversee their implementation. Even with 30 environmental staff, the International Finance Corporation has a lackluster track record of implementing its own safeguard policies. Endorsing banks must prove that they are serious about implementation by taking actions such as rejecting projects that do not meet IFC environmental and social standards, dedicating adequate resources to implementation, disclosing their Environmental Management Systems (including how banks implement and monitor the Equator Principles and those individuals responsible for implementation), and disclosing social and environmental loan covenants.

Ultimately, banks will be judged not on the loftiness of their policies, but on the environmental and social impacts of the transactions they finance. Another yardstick the public will use to measure the efficacy of the Equator Principles is the Collevocchio Declaration on Financial Institutions and Sustainability – a statement that describes a broader vision of sustainability for the financial sector released by over 100 civil society groups in January 2003. The Equator Principles are consistent with, but fall far short of the commitments outlined in the Declaration. For example, the Collevocchio Declaration

embraces the precautionary principle, which would imply that banks should avoid transactions with certain characteristics (such as resource extraction in primary tropical forests, or projects resulting in involuntary resettlement of over 5,000 people). In contrast, the Equator Principles rely on mitigation, even for the most environmentally and socially harmful projects.

The creation of the Collevocchio Declaration is a tangible symbol of NGOs' increasing scrutiny of the private financial sector, which has fallen relatively far behind other corporate sectors in understanding its role and responsibilities in fostering social and environmental sustainability. Notably, all the banks that drafted the Equator Principles have been targets of NGO advocacy. Because of increasing pressure from NGOs and the public, private banks are beginning to develop initiatives like the Equator Principles in response to increasing public demands that private banks operate responsibly. Continued and increasing public scrutiny will certainly spur banks to develop similar collective initiatives.

Friends of the Earth hopes that the Equator Principles can serve as a helpful springboard from which private financial institutions can examine and confront their role in destructive projects, and develop creative and concrete solutions to advance sustainable development. However, banks and the voluntary initiatives they develop still will ultimately be judged by the real world impacts of the projects they finance.