

ASN Bank Issue Paper

Supranationals

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A. Introduction

This issue paper is an elaboration of the special investment criteria that were drawn up specifically for the supranational institutions sector. The issue paper specifies the conditions under which supranational institutions can apply to the special investment criteria of the ASN Bank.

This issue paper uses the collective noun, 'supranationals', to refer to development banks, multilateral banks and other financial institutions with comparable objectives. Multilateral banks are public institutions that are owned by more than one national government. Multilateral banks often finance development projects. Besides the multilateral banks, there are also development banks that are owned by single governments (for an overview of supranationals, please refer to Appendix E.1).

Supranationals support enterprises, projects and government programmes in emerging economies, as well as in developed and developing countries in the form of loans, participations, guarantees and technical assistance. Some of those institutions operate on a regional basis, while others have worldwide operations. The World Bank is an example of a supranational that operates worldwide, while the African Development Bank operates on a regional basis. Another useful distinction that can be drawn between these institutions is the distinction between supranationals for governments (e.g. the World Bank) and supranationals for private enterprise (e.g. FMO, IFC).

The supranationals are partially dependent on public funds, but they also derive capital from the capital market via the issuance of bonds. Loans to those institutions could be taken out via funds, such as the ASN Bank portfolio, the ASN Bond Fund and the ASN Mixed Fund.

Despite the fact that their objectives target the financing of sustainable development, the supranationals regularly financed (and still finance) projects that contribute to the problem of climate change and / or social and environmental problems. They also financed projects that specifically gave rise to economic problems. ASN Bank is therefore not able to include the supranationals into its funds based on their objectives, but will need to test each individual instance based on its own criteria. The fact that this concerns financial institutions does not simplify matters either. For that reason, this paper is an elaboration of how the ASN Bank intends to do this specifically for the supranationals sector.

B. Testing supranationals on special investment criteria

Because supranationals are financial institutions, the ASN Bank has an indirect relationship with the projects in which the applicable supranationals invest when issuing loans to those institutions.¹ According to the ASN Bank criteria, those projects fall under the sphere of influence and chain of responsibility of the applicable supranational. Consequently, whenever the ASN Bank wishes to select a supranational, this effectively boils down to having to test the projects of the supranational against the special investment criteria of the ASN Bank and the elaboration of those criteria in the different issue papers (see Appendix E.2 for an overview of the Special Investment criteria applicable to the Supranationals). In most instances, however, the bank will not be familiar with all the projects of any given supranational, or there may simply be too many. In that instance, the testing cannot be done at project level, but must be done at policy level. In the latter type of testing, the ASN Bank relies on a number of different principles that must guarantee that the applicable supranational does indeed only operate actively in projects that fulfil the special investment criteria

¹ In many instances, a supranational will also invest in a local financial institution; for example, 200 out of the 400 FMO customers are financial institutions.

of the ASN Bank. In short, both testing methods can be reduced to the following:

- *Testing at project level:* All the projects of the applicable supranational are known to the ASN Bank. This makes it possible to test them at project level. Where the ASN Bank determines that none of the projects financed by the supranational are in conflict with its criteria, the supranational is adopted into the bank's universe.
- *Testing at policy level:* The ASN Bank determines that the mandate, objectives and working method, including monitoring of the supranational's projects, are recorded so clearly, robustly and unambiguously that it provides an adequate level of guarantee that the supranational is not financing projects that conflict with the special investment criteria of the ASN Bank. This means that it is not necessary for the ASN Bank to be familiar with all the projects of the supranational, but sufficient to be able to conduct random tests of the applicable supranational's policy practice. Once it is found that the supranational is in compliance with those conditions, it is adopted into the bank's universe.

The ASN Bank draws a distinction in its selection process between activities it wishes to exclude and activities it wishes to avoid. In practice, this mostly means avoidance leads to exclusion in the case of investment in projects in developed, Western countries and in enterprises. This does not however apply to investments in projects in poor or developing countries. In the latter instances, the bank *could*² also decide to permit an avoided activity. The special investment criteria and the underlying issue papers make a clear distinction between an 'avoided' and an 'excluded' activity.³

The actual share of 'avoided' projects in the overall investment portfolio of the supranational also plays a role: If the portfolio largely consists of 'avoided' projects, the ASN Bank would be more inclined to issue a negative recommendation than if the share were small.

Another criterion that is useful for the proper evaluation of projects for investment is the level to which the supranational actively invests in sustainable energy.

Testing at project level

The contribution of supranationals to the environment and the promotion of human rights takes place via the financed projects. Many supranationals finance projects that fulfil

the special investment criteria of the ASN Bank. That notwithstanding, there is always a risk of financing projects that do not fulfil the criteria of the ASN Bank. As far as the ASN Bank is concerned, investments in projects that do fulfil its criteria can never compensate for the possible negative impact of those that do not.

The following are examples of the kinds of projects that rarely fulfil the criteria of the ASN Bank and that are nevertheless often financed by the supranationals:

- Large-scale energy plants that do not provide energy for the poor.
- Large-scale dams that have a disruptive effect on the local population and the local environment, such as forced relocation without due compensation.
- Mining projects that yield limited or no benefits for the local population and / or countries or that lead to environmental and social problems.
- Palm oil plantations that have a major negative impact on both the environment and the population. This also includes climate changes due to deforestation, land impoverishment, expropriation and labour rights.
- Nuclear energy, because the ASN Bank excludes investment in nuclear energy.
- Projects with a real risk of forced labour or child labour.
- Projects that contribute to the preservation of dictatorships.

This means that project-level transparency is extremely important for enabling the ASN Bank to test the supranational at project level. To be able to do so, the institution would have to provide insight into all its financed projects. Where the institution fails to provide due transparency, it is harder to determine whether the institution fulfils the ASN criteria, as, then, the policy must be evaluated, as well as the internal processes that are designed to ensure that the policy is indeed applied effectively in practice. The section below outlines how the ASN Bank goes about achieving this.

Testing at policy level

In view of the fact that supranationals rarely (if ever) provide complete insight into all the projects they finance, the ASN Bank is bound to conduct tests at policy level in all instances. The testing amounts to the following: determining whether the policy is in compliance with the special investment criteria of the ASN Bank and testing, based on the available information on financed projects, whether the policy is actually applied⁴ in practice.

² This refers to the fact that it *may be permissible* for a supranational to have for example a limited number of fossil projects in its portfolio.

³ 'Exclusion' applies to, e.g. the financing of arms production, nuclear power stations and child labour.

⁴ This means that a supranational that does not divulge any projects, including for testing, may also be approved based on its policies.

When conducting tests at policy level, the bank checks (in no particular order) whether:

- The supranational has an investment policy in place that fulfils the special investment criteria of the ASN Bank. An important pointer in that regard is whether the supranational makes use of a list of exclusions⁵ and the use of the IFC Performance Standards. The IFC Performance Standards are viewed as a minimal policy.
- The institution must also have specific policies that are required prior to and during the term of the projects that are to be financed. This entails, for example, that the necessary precautions with respect to the environment and social impact are taken prior to the project being started. Did the institution conduct social and environment impact assessments and what did it do with the results? Does the local population have any say in the projects? How transparent is the institution about the aforementioned information and does it provide insight into the information? Does the supranational inform the local population of the project in the native language? How does the institution deal with the stakeholders and how does it deal with criticism? Do the stakeholders have any say and participation in the project? The institution must have developed a minimal policy on all the aforementioned issues.
- What does the selection process consist of? When is a project accepted or rejected, and when does the institute decide to conduct further research? Does the supranational bank give insight into this; both qualitatively in the process, and quantitatively⁶.
- Does the supranational bank monitor the progress of the project? Does it conduct interim evaluations and does it provide support as long as the applicable loans are running?
- In practice it is not unusual for the negative impact of a project on mankind and the environment to only become evident years after the start of the project. Many years could pass before the actual link with the project has been established and proved. This means that all current projects are important for consideration in the selection process.
- Does the institution have a progress report system? This is particularly important when extra financing is needed. Extra financing is often needed as a consequence of unforeseen expenditures in complex projects. Extra caution is advisable whenever this happens.

- Do random tests of financed projects show that the policy is indeed applied in practice?
- The supranational is involved in projects or activities that the ASN Bank specifically wishes to exclude by asking the supranational specific questions in that regard⁷.
- Where the supranational is financing (local) financial institutions, the supranational must be able to demonstrate that the local institution is also operating in accordance with the supranational's policies.

Tips for sustainable research

Areas in which minimal policy must be in place for admission:

- Transparency and dialogue
- Indigenous people
- Relocation
- Employee rights
- Arms
- Child labour
- Corruption
- Compensation of the local population
- Indirect impact⁸
- Preferably also an independent appeal mechanism

The following must be in place in the case of projects:

- Social research
- A department that is authorized to make independent decisions and that advises the management committee
- Social impact assessment
- Environmental management system and environmental impact assessment
- Openness of information on the above-mentioned issues
- The policy must be clear, including about the assessments; when, for example, is an impact assessment conducted? It is not enough to simply mention the existence of indigenous populations in the policy. It must also be clear what it entails with respect to the project. It is also important to ensure that the communication with the indigenous population is sound and comprehensible.

⁵ In some instances the institution may have a mandate that corresponds to the criteria of the ASN Bank. If this mandate does indeed exist, it can be used as a warning list and will form the basis for further investigation. There is no certainty that all projects will comply with the criteria of the ASN Bank. In most instances the mandate, while not available, does indeed exist; for example in the CEB mandate.

⁶ Insight into refused projects is not permissible based on related legal consequences.

⁷ For example, if a supranational does not specifically exclude nuclear energy, but research has shown that they do not invest in nuclear energy.

⁸ For example, the investments in Hedge Funds, as well as a number of other/new constructions. The institution might hold an interest in controversial projects and companies via external capital management.

C. Backgrounds

Different supranationals use exclusion lists that are comparable with the exclusion criteria of the ASN Bank; for example, the members of the Edfi (see Appendix E.3: Rome Consensus). In addition to the exclusions of the Rome Consensus, the ASN Bank also uses the following additional exclusions: Nuclear energy, animal experiments, non-sustainable palm oil, GMOs for foods and non-foods, and investments in Burma. Over and above the Rome Consensus, there are also a number of supranationals that use their own additional exclusion criteria (e.g. FMO).

Compensation for poor countries is another theme for testing, as many loans are being issued to corrupt dictators and undemocratic regimes that use the capital to suppress their own population. The population must then suffer the consequences of the repayment of the debts and are thereby punished doubly. The debts of those countries have accumulated to such an extent that this effectively renders the development of the country and the reduction of poverty impossible; as in the case of many sub-Saharan countries in Africa. This is in direct conflict with the objectives of the World Bank aimed at reducing poverty.

D. Sources

The following sources may be handy when testing supranational policy against the actual practice:

Organisations:

- www.Bankwatch.org
- www.bothends.org
- www.bicusa.org
- www.foe.org

Publications

- Dr M. van Putten (2006) 'Policing the World' Accountability Mechanisms for Multilateral Financial Institutions and Private Financial Institutions
- Dr M. van Putten (2007) Accountability Mechanism in other Multilateral Financial Institutions
- L. Krämer (2006) Mechanisms at EC level to hold the European Investment Bank accountable
- S. Herz (2006) An Environmental Policy Framework for the European Investment Bank for Non-EU Lending: The Need for Clear, International Standards-based Approach
- T. Griffiths (2006) Making the Grade: A survey of IFI social policies, international development standards and the policies of the European Investment Bank (EIB)

E. Appendices

Appendix E.1: List of supranational institutions

The following is the research universe of the different supranational institutions, development banks⁹ and institutions and other institutions:

European development banks / institutions and EDFI members¹⁰ (www.edfi.be):

- Belgian Investment Company for Developing Countries (BIO)
- CDC Capital Partners (VK)
- Compañía Española de Financiación del Desarrollo S.A. (Cofides)
- Deutsche Investitions und Entwicklungsgesellschaft mbH (DEG)
- Austria Wirtschaftsservice Gesellschaft mbH (AWS)
- Finnish Fund for Industrial Cooperation Ltd (FINNFUND)
- Netherlands Development Finance Company (FMO)
- Hungarian Development Bank (MFB)
- Danish International Investment Funds (IFU, IØ, IFV)
- Norwegian Investment Fund for Developing Countries (Norfund)
- Groupe Agence Francaise de Developpement (AFD) Société de Promotion et de Participation pour la Coopération Economique (Proparco)
- Belgian Corporation for International Investment (SBI-BMI)
- Swiss Investment Fund for Emerging Markets (Sifem)
- Società Italiana per le Imprese all'Estero (SIMEST)
- Sociedade Para o Financiamento do Desenvolvimento (Sofid)
- Swedfund International AB (SWEDFUND)

Supranational institutions:

- World Bank (WB)
- European Investment Bank (EIB)
- International Bank for Reconstruction and Development Bank (IBRD)
- Inter American Development Bank (IADB)
- Asian Development Bank (AsDB)
- African Development Bank (AfDB)
- European Bank for Reconstruction and Development (EBRD)
- Nordic Investment Bank (NIB)
- China Development Bank

Other institutions:

- Kreditanstalt für Wiederaufbau (KfW)¹¹
- Islamic Development Bank (IDB)
- Japan Bank for International Cooperation (JBfIC)
- Council of European Development Bank (CEB)

⁹ This list is not exhaustive.

¹⁰ The FMO, MFB and the AFD are the members of the EDFI with outstanding public loans.

¹¹ Not a true supranational, but a bank for the promotion of the German and European economy. Also plays an active role in, among other things, investment finance, export and project financing and financial partnerships with developing countries.

Appendix E.2: Special Investment criteria of the ASN Bank applicable to supranationals

1 Exclusion criteria

1.1 Human rights

In its activities and area of influence ASN Bank will ensure that human rights as set out in national and international law are respected, protected and promoted. To this end we apply exclusion and acceptance criteria in relation to countries and companies.

1.1.2 Underlying principle in the case of companies

In the case of companies the underlying principle is that they will be excluded, if they do not respect human rights in all of the countries in which they are active¹² based on the Universal Declaration of Human Rights and any human rights standards derived from it which relate to the relevant company's operations and sphere of influence.¹³

Consequently, those companies which are systematically guilty of the following violations of human rights will be excluded:

equality of opportunity

- companies which do not guarantee equal opportunity and non-discrimination;

arms and security

- companies engaged in or benefiting from war crimes, or the manufacture or trade in arms. Consequently, this also means that ASN Bank will refrain from providing any form of funding for or from investing in companies which are active in the development, manufacture, distribution or trade in arms. "Arms" refers to all types of conventional weapons, ammunition, parts, supporting technologies and associated expertise. For a precise definition of "arms" ASN Bank uses the Common Military List of the European Union, which the latter has drawn up. This list contains a wide-ranging summary of arms, parts and chemicals as well as ICT products and services. ASN Bank will also exclude companies that manufacture products which are primarily used in armaments in addition to having a civil application;¹⁴

- companies whose corporate security practices do not respect human rights;

children

- companies which do not offer safeguards against the exploitation of children;

employees

- companies using forced labour;
- companies which do not provide safe, healthy working conditions or which are involved in sexual exploitation and/or the commercial exploitation of pornography;
- companies which do not pay fair and proper wages;
- companies which do not respect freedom for trade unions;

national sovereignty and human rights

- companies which do not respect national sovereignty and human rights in that they fail to comply with legislation;
- companies involved in corruption;
- companies whose business operations have a deleterious effect on health or living conditions, or increase poverty;
- companies which violate social, cultural and economic rights;

consumers

- companies which supply products that are unsafe, of inferior quality or harmful, such as tobacco, gambling or games of chance;

environmental protection

- companies which do not protect the environment in that they fail to act in accordance with national and international guidelines and legislation.

1.2 The environment

1.2.2 Underlying principle in the case of companies

The starting point for companies is that they will be excluded if they are involved in the following activities:

nuclear energy

- companies which generate nuclear energy, operate nuclear power stations, or distribute or trade in nuclear products;

¹² Here ASN Bank is referring to the criteria set out in The Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with regard to Human Rights of 2003.

¹³ A company's operations and sphere of influence refer to the company itself, the parts of the supply chain in which it operates, and wherever it is capable of exerting any influence.

¹⁴ The term, "dual-use", is used to describe these products.

- companies which focus specifically on supplying this industry;

genetic engineering

- companies that apply genetic engineering to plants or animals in the food or non-food sector;
- companies that apply genetic engineering to plants or animals for medicinal and pharmaceutical purposes will be excluded unless a medical problem can only be remedied at the time of screening by using genetically modified plants and/or animals. This exception will only apply if genetic engineering is used in controlled conditions which limit the risks to people and the environment as far as possible;

fur, whaling, exotic and/or protected animal species

- companies are directly involved in hunting and/or trading in:
 - fur;
 - whales;
 - exotic and/or protected animal species;

tropical hardwoods

- companies active in felling and/or trading in non-sustainable tropical hardwoods;

palm oil

- companies setting up or running non-sustainable palm-oil plantations;

bio-industry

- companies engaging in bio-industry operations which are hostile to animals;
- companies which focus on developing and maintaining an animal-hostile bio-industry in their capacity as suppliers;

animal testing

- companies which use animal testing to develop non-medical products;
- companies which are required to use animal testing by law for medicinal production, but which do not have a transparent policy on this and are not developing alternatives;

supply chain responsibility

- companies which do not acknowledge any supply chain responsibility for the environment;
- companies which are not transparent or do not show a willingness to be accountable for their supply chain responsibility.

2. Acceptance criteria

2.1 Human rights

2.1.2 *Underlying principle in the case of companies*

Companies will earn a positive evaluation if they make an active contribution towards protecting and promoting human rights as defined by the Universal Declaration of Human Rights insofar as it relates to their activities and sphere of influence, by:

- implementing standards in internal policies, codes of conduct and contracts;
- arranging for the internal and external monitoring and verification of compliance with standards.
- ensuring the presence of a policy and mechanism to compensate victims whose human rights may have been violated.

2.2 The environment

2.2.2 *Underlying principle in the case of companies*

Environment

- Companies must demonstrate that they pursue an active, comprehensive environmental policy. In concrete terms the following factors will be assessed: the nature of the raw materials used and of their end products, their energy consumption, their use of clean water, the nature of the emissions they release, the solid waste resulting from production, the scope for recycling their end products and the extent to which this occurs. When assessing a company consideration will not only be given to the prevailing environmental conditions but also to the approach adopted by and within the company to bring about change and improvement in this respect.

Genetic engineering

- Companies must declare whether they apply genetic engineering and if so, how. Those businesses which use this technology must be able to show that they have a transparent policy on genetic engineering. The application of genetic engineering to micro-organisms will be considered acceptable, provided that it is done under controlled conditions which limit the risks to people and the environment as far as possible, and provided that a demonstrable contribution is made towards sustainable development or business operations.

Appendix E.3: Rome Consensus

The European Development Finance Institutions (EDFI) have, as a result of their harmonization process, mutually agreed on the following Exclusion List for co-financed projects, which forms part of the "Rome Consensus":

- 1) Production or activities involving forced labour¹⁵ or child labour¹⁶
- 2) Production or trade in any product or activity deemed illegal under host country laws or regulations or international conventions and agreements.
- 3) Any business relating to pornography or prostitution.
- 4) Trade in wildlife or wildlife products regulated under CITES¹⁷
- 5) Production or use of or trade in hazardous materials such as radioactive materials¹⁸, unbounded asbestos fibres and products containing PCBs.¹⁹
- 6) Cross-border trade in waste and waste products, unless compliant to the Basel Convention and the underlying regulations.
- 7) Drift net fishing in the marine environment using nets in excess of 2.5 km in length.
- 8) Production, use of or trade in pharmaceuticals, pesticides/herbicides, chemicals, ozone depleting substances²⁰ and other hazardous substances subject to international phase-outs or bans.
- 9) Destruction²¹ of Critical Habitat.²²
- 10) Production and distribution of racist, anti-democratic and/or Neo-Nazi media.

In addition to the above, the financing of projects is excluded where the following activities form a substantial²³ part of a project sponsor's primary operations or those of the project:

- 11) Production or trade in²⁴
 - a) arms and munitions
 - b) tobacco
 - c) hard liquor
- 12) Gambling, casinos and equivalent enterprises

15 Forced labour means all work or service, not voluntarily performed, that is extracted from an individual under threat of force or penalty, as defined by ILO conventions.

16 Employees may only be taken if they are at least 14 years old, as defined in the ILO Fundamental Human Rights Conventions (Minimum Age Convention C138, Art. 2), unless local legislation specifies compulsory school attendance or the minimum age for working. In such cases the higher age shall apply.

17 CITES: Convention on International Trade in Endangered Species or Wild Fauna and Flora.

18 This does not apply to the purchase of medical equipment, quality control (measurement) equipment and any other equipment where EFP considers the radioactive source to be trivial and/or adequately shielded.

19 PCBs: Polychlorinated biphenyls, a group of highly toxic chemicals. PCBs are likely to be found in oil-filled electrical transformers, capacitors and switchgear dating from 1950-1985.

20 Ozone Depleting Substances: Chemical compounds that react with and delete stratospheric ozone, resulting in "holes in the ozone layer". The Montreal Protocol lists ODs and their target reduction and phase-out dates.

21 Destruction means the (1) elimination or severe diminution of the integrity of a habitat caused by a major, long-term change in land or water use or (2) modification of a habitat in such a way that the habitat's ability to maintain its role (see footnote 10) is lost.

22 Critical habitat is a subset of both natural and modified habitat that deserves particular attention. Critical habitat includes areas with high biodiversity value that meet the criteria of the World Conservation Union (IUCN) classification, including habitat required for the survival of critically endangered or endangered species, as defined by the IUCN Red List of Threatened Species or as defined in any national legislation; areas having special significance for endemic or restricted-range species; sites that are critical for the survival of migratory species; areas supporting globally significant concentrations or numbers of individuals of congregatory species; areas with unique assemblages of species or which are associated with key evolutionary processes or provide key ecosystem services; and areas having biodiversity of significant social, economic or cultural importance to local communities. Primary Forest or forests of High Conservation Value shall be considered Critical Habitats.

23 A benchmark for substantial is 5 – 10 % of the balance sheet or the financed volume.

24 In Financial Institutions this is calculated with regard to the portfolio volume financing such activities.