Principles, Profits or just PR?

Triple P investments under the Equator Principles

An Anniversary Assessment

BANKTrack

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June 4 2004

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Front page: Women from the Omkareshwar submergence area in India. Over 50,000 people will be evicted for this dam project (photo; Urgewald)

Table of Contents

1. Introduction; public expectations of private banks

On June 4th, 2003, in response to growing international pressure, 10 private financial institutions announced the first collective norms addressing environmental and social issues in the sector. Led by Citigroup, ABN AMRO, Barclays and West LB, the banks presented a united approach to attempt to mitigate environmental and social risk associated with financing projects in the world's most fragile ecosystems. Today, at the 1st anniversary, twenty three banks and two public financial institutions (the Danish Export Creidit Agency, EKF, and the European Investment Bank, EIB) have signed on to the Equator Principles (EPs).

The announcement of the EPs marked one step toward sustainability for an influential sector of society that previously had been largely operating in anonymity. Since the beginning of the 1980s other financial institutions as the World Bank and the International Monetary Fund found themselves the subjects in the glare of a discerning public eye. In the late 1990s, the attention of NGOs expanded to include the regional development banks and the group of Export Credit Agencies (ECAs). All those years, private banks found their role usually too far removed from the centre of damaging projects to invite much direct scrutiny. However, in the last few years, that dynamic had begun to shift.

The private financial sector has quietly grown in power, with confounding dynamics with regard to accountability. These are private institutions with a fiduciary responsibility to their shareholders, yet a vast sphere of stakeholders is affected by every financing decision made by these banks. The insulation of these institutions from democratic decision making has led to an ever-widening circle of discontent, as lending capacity grew while provisions to protect the global environment and the rights of people remained non-existent.[1] A recent slew of mergers has created conglomerates with even more control over financial services, and national laws and regulations continue to struggle to keep pace with mega-banks who operate worldwide, some in more than 100 countries.

Commercial banks have been willing to move into regions and finance projects where those accustomed to the public eye and averse to scandal fear to tread

All of these factors have created a climate where commercial banks have been willing to move into regions and finance projects where those accustomed to the public eye and averse to scandal fear to tread. The infamous Three Gorges Dam in the Yangtze River Valley in China was financed by private institutions while the World Bank stayed away of the project. Investment banks also stepped in to finance the crude oil pipeline (OCP) which now traverses nine protected areas in Ecuador. This project is intended to double oil export capacity in a country already reeling from the impacts of unchecked oil development on an unprepared population. When public financiers fall short of their environmental and social guidelines, such as in the Baku-Tibilisi-Ceyhan pipeline, the commercial banks seem quick to drop their standards as well.

Non Governmental Organizations (NGOs) and civil society has, for some time, recognized the disproportionate leverage enjoyed by these distinctly undemocratic and non-transparent institutions. Northern advocacy groups, particularly those in the United States and Europe, have utilized strategies to lobby these banks as an opportunity to work in solidarity with affected communities on the ground in the Global South. In the late 1990s, in an effort to prevent environmentally and socially harmful investments from occurring, a group of NGO's began a coordinated and strategic attempt to pressure financial institutions to adopt systems and policies that would broaden banks' risk management systems to better consider sustainability issues.

Initial efforts to lobby banks have focused on a number of different areas including corporate governance, environmental management systems, and sector specific policies to address such critical issues as forest protection, climate change, and the impacts of large scale dams and oil and gas infrastructure. What is plainly evident is that the financial sector and specific leading banks found themselves in an uncomfortable spotlight as their lack of attention to these critical issues was revealed.

For example, in November, 2001, ABN AMRO led four Dutch Banks in developing a new far-reaching forest policy in response to a campaign against the Dutch funding of palm oil plantations in endangered orangutan habitat in Indonesia. Although focusing on one problem in one region, the written policy had broad application, and the resulting precedent set the stage for dialogue across the sector and with NGOs around forest protection through investment screening. Other banks such as WestLB, MorganStanley, Westpac, and Citigroup, felt increasingly uncomfortable with a rising number of protests at their doorsteps, challenging their involvement in projects causing environmental and social destruction.

The loose NGO coalition who had been actively engaged on these issues in 2002 penned a series of principles to serve as a guide for financial institutions to incorporate the critical social and environmental values into their business operations. Coined 'the Collevecchio Declaration on Financial Institutions and Sustainability', it was introduced as a pathway to reconcile economy with ecology.[2]

In the context of this growing pressure from both protesters and NGOs, and in light of banks' recognition how environmental and social controversies could impact the bottom line, the Equator Principles were drafted, outlining steps to identify critical areas and mitigate the environmental risk by requiring extra assurances from companies with regard to sensitive operations.

At the time of release, founding members of BankTrack wrote the following in response to the Equator Principles:

"As representatives of the non-governmental organizations (NGOs) that drafted the Collevechio Declaration calling for environmental and social responsibility from financial institutions, we applaud the efforts of leading banks to grapple with these critical issues. Whether or not the Equator Principles (EPs) represent a significant initiative or a negligible one depends on banks' commitment to strengthen them and be transparent in their implementation of the Principles**...** We believe that the EPs, aptly implemented, can be a helpful springboard from which financial institutions can examine and confront their role in destructive projects. Modelled after guidelines from multilateral lending institutions, the Principles are only as good as the commitment behind them."[3]

Whether or not the Equator Principles (EPs) represent a significant initiative or a negligible one depends on banks' commitment to strengthen them and be transparent in their implementation of the Principles...

Happy anniversary?
The question to ask at the anniversary of this public commitment to promote sustainability is whether or not the Principles have served their intended purpose. Have they promoted a true 'Triple P' approach to investments, balancing people, profit and planet in a way that can be called truly sustainable, or are the Principles a mere PR effort?

Certainly, they are a recognized forum for financial institutions to grapple with some of the most pressing problems the world faces today. As the Equator Principles website even states, 'the Equator Principles have become the project finance industry standard for addressing environmental and social issues in project financing globally.'[4]

However, since the announcement in June 2003, NGOs have grown increasingly impatient with the slow pace of implementation of the Principles, as well as the secrecy surrounding this process. Every now and then the EP website heralds in ever more jubilant terms the signing of yet another bank onto the Principles, but otherwise no substantial updates on the state of play are provided.

Ultimately, NGOs such as BankTrack tend to judge the success of the Principles by their effect on the ground, the projects that receive Equator bank financing and, more importantly, those that are significantly mitigated or rejected because of the Principles. When early 2004, several Equator banks announced their participation in the Baku-Tblisi-Ceyhan (BTC) oil pipeline, despite NGO findings of numerous violations of IFC and Equator standards, NGO caution turned into outright concern about the viability of the Principles.

A further move in April 2004 by eleven EP banks who sent a letter to World Bank President Wolfensohn, opposing the adoption of more stringent policies for World Bank extractive industries investments caused outrage; instead of a stepping stone towards stringent policies, the EPs were used here to block progress elsewhere; what were these Equator banks up to?[5]

There are positive signs as well. At the EP launch, NGOs were hopeful that the Principles, and banks' ensuing steps to implement them, could serve as a springboard for developing other environmental and social standards. In the last year, two banks, Citigroup and Bank of America, have bolstered their commitment to the Equator Principles with policies that go much further in the realm of forest protection and climate change and respecting indigenous rights. In the case of Citigroup, the bank also decided to apply the Principles to corporate loans where use of proceeds was known, and clearly viewed their additional forests commitment as an extension of their Equator pledge.

Bank of America's new environmental initiatives, adopted in May 2004, at the current time represent industry best practice, setting targets and timelines for reductions of direct greenhouse gas emissions and those resulting from investments, broadening the scope of industrial no go zones to include intact forest ecosystems, and refusing to lend to projects or operations where indigenous land claims are unresolved. The enhanced scope of these policies is further evidence that the Equator Principles alone is an insufficient solution – and that some banks are willing to take the lead. The decision of these leading institutions to move so quickly beyond Equator represents a momentum in the sector that provides some reason for optimism.

This report is an attempt to examine the past year's successes and failures. It analyses some of the highly controversial projects that, despite the existence of Equator principles, were financed or are about to be financed by EP banks. It also provides an overview of civil society expectations towards banks and offers recommendations on how the Equator principles can truly make a difference.

Transformation of an industry as embedded as the financial sector does not occur in a short time. Yet, never has there been a greater need for action from corporate leaders to address overwhelming environmental and social ills that exact a high cost on global health and stability. As with previous reports, the findings and recommendations offered in this paper should be seen as an invitation to Equator banks to enter into a transparent and open dialogue with BankTrack on how to move forward with the EPs.

June 2004, BankTrack team

2. The Equator Principles; business as usual?

The Equator Principles, if in any way relevant to "promote responsible environmental stewardship and socially responsible development", as stated in the EP's preamble, must result in a noticeable shift in the project portfolio of undersigning banks, away from unsustainable or outright destructive projects -or even entire sectors- and towards a greater share of projects with a clear positive effect on society and the environment. To put it differently, at least some projects should be significantly improved by the influence of Equator banks; and other projects that otherwise would have been approved must be rejected on the basis of non-compliance with the Equator Principles.

A full assessment of the EP should evaluate whether bank clients are making environmental and social improvements to project designs in order to qualify for Equator bank financing. It may be too early to tell whether this is occurring, particularly since the Equator banks as a whole do not publicly disclose this type of information. However, it is rumoured that some non-Equator banks have proudly advertised their lack of environmental and social standards as a way of attracting less scrupulous clients. Although the EP banks have tried to avoid this practice by gathering a critical mass of endorsers, such "bottom feeding" is a weakness of practically all voluntary initiatives.

A comprehensive assessment of the Equator Principles should also include an overview of non-eligible projects. However, while EP banks, in informal conversation, continue to stress that projects indeed get rejected, they refuse to provide concrete examples, for fear of jeopardising future business opportunities with prospective clients. This makes it difficult for outside observers to judge how rigidly the Principles are being applied. Although NGOs have observed a few cases in the last year where Equator banks have chosen to decline or discontinue their involvement in particular transactions, the reasons for such decisions are not conclusively known. Banks' Equator commitment, their worry over broader reputational risks, or basic financial concerns all could have played a role.

For example, after endorsing the Equator Principles, the Royal Bank of Canada decided to not finance the Rosia Montana mine in Romania, which has long been the target of NGO campaigns. Similarly, before the Principles were launched, Citigroup concluded that it would not renew its financial advising contract with the controversial Camisea gas project in Peru, which will have grave impacts on biodiversity and indigenous peoples. Finally, although several Equator banks financed the Baku-Tbilisi-Ceyhan pipeline, others who could have been involved ultimately were not.

What can be observed by NGOs are the projects that, although they would have been prime candidates for rejection or major mitigation because of their negative environmental or social impact, nevertheless got funded by Equator banks. In fact, none of the projects considered highly controversial by NGOs at the time of the adoption of the Equator Principles where put on hold or cancelled.[6]

The following projects are examples of environmentally and socially controversial transactions financed by Equator banks since the launch of the Principles. In particular, the Baku-Tbilisi-Ceyhan and the Kárahnjúkar projects, have been analysed by NGOs as failing to meet the standards and procedures outlined in the EPs. The other projects have not been the subject of such analysis, but they are offered as illustrative examples that the Equator Principles in their current form are not a panacea.

No matter how strong a bank's official policies may be, communities and the public ultimately judge a bank's sustainability by the on-the-ground environmental/social impacts of its portfolio.

For example, some cases are examples of environmentally/socially controversial deals where the Principles formally do not apply (as they may be below the threshold of $50 million or not financed in a non-recourse manner). These cases illustrate that a broader application of the Equator Principles could still provide value to banks in their due diligence and assessment processes. Other transactions may have been properly subjected to Equator processes and standards, yet banks may find that the deal's social and environmental controversies could continue to pose reputational and financial risk. These cases illustrate that no matter how strong a bank's official policies may be, communities and the public ultimately judge a bank's sustainability by the on-the-ground environmental/social impacts of its portfolio.

2.1. The Kárahnjúkar hydro project - Iceland

Within a few months after signing on to the Equator Principles, **Barclays Bank** came under attack for arranging support for the Kárahnjúkar hydro project. While the project technically was not subject to the Principles (as it was not project finance), Barclays to its credit recognized that its client Landsvirkjun was explicitly raising funds to construct the dams. Barclay's broader application of the EPs in this case suggests that it is possible and indeed consistent with the overall purpose of the Principles to employ Equator processes and standards for non-project finance transactions.

The Kárahnjúkar hydro project is a massive hydropower scheme based in the Icelandic highlands. It is to be made up of nine dams, three reservoirs, seven channels and 16 tunnels that will divert several glacial rivers in the Highlands to provide water to run a 630 megawatt hydropower plant to be run by the Landsvirkjun power company. The power generated from the Kárahnjúkar hydropower station will be used to provide cheap electricity for an aluminium smelter (Fjardaal) to be built by Alcoa and based on the coast in East Iceland.

Wilderness under threat

The highlands of East Iceland are one of the largest remaining wilderness areas in Europe. The area that will be affected by the Kárahnjúkar project is a dramatic system of glacial rivers, plateaus, lakes, waterfalls and canyons that covers nearly 3000 km2 (this includes indirect effects).

Icelandic reindeer will be under threat as the Kringilsarrani nature reserve, protected for reindeer conservation, will be flooded and the reserve will become inaccessible for reindeer because of the construction of Halslon reservoir. Other endemic species such as the Icelandic harbour seal and the pink footed geese are also severely threatened by the project.

Questionable socio-economic benefits

East Iceland, where the hydropower project is based has relatively low unemployment. Most of the construction jobs are being taken by foreign workers and there will be very few permanent jobs at the hydro power plant after it is built. Similarly it seems there are likely to be few jobs available for local people at the smelter.

If in the longer term the price for aluminium does not rise considerably and stay high, then Icelanders will even end up subsidising Alcoa's electricity. An economic assessment commissioned by the Iceland Nature Conservation Association (INCA) showed that, using only slightly different parameters based on historical industry trends and market rates, Kárahnjúkar will most likely result in annual losses of $36 million.

Financing the destruction of Iceland's Highland Wilderness

Barclays has played a key role in arranging financing to help ensure that the project goes ahead. In fact, Barclays may earn money from the deal and not even have to lend any money. Barclays Capital (part of Barclays Bank) along with three other banks was appointed by Landsvirkjun to arrange $400 million in loans under a financing arrangement known as multi-currency revolving credit.

The key advantage for Landsvirkjun of this sort of financial arrangement is that it can look for cheaper ways to seek finance while knowing that they can always use this revolving credit arrangement as a back-up if they are short of funds. The advantage for Barclays and the banks in the syndicate is that they will earn money regardless of whether Landsvirkjun uses any of the loans as they have to be paid for providing the service.

Broken principles

The project violates the Equator Principles on a number of counts:

(i) Significantly impacts sensitive high conservation ecosystems - The Kárahnjúkar project will have substantial and irreversible impacts on wildlife habitats of a high conservation value, including two internationally important bird areas, according to the project's Environmental Impact Assessment (EIA). The project would therefore violate the IFC's natural habitats policy and the Equator Principles' commitment to protecting sensitive ecosystems.

(ii) *Breaches best practice pollution levels* - Although the smelter is not part of the project under the IFC Operational Policy on Environmental Assessment, all ancillary aspects, which would include the smelter, should be considered. The aluminium smelter being built in East Iceland that will be the major user of power from Kárahnjúkar will be allowed to emit sulphur dioxide emissions up to 12 times higher than best practice as defined by the World Bank's Pollution Prevention and Abatement Handbook.

(iii) *Ignores the cumulative impacts of other projects* – According to the Equator Principles, any environmental assessment should include the cumulative impacts of existing projects, the proposed project and anticipated future projects. Landsvirkjun has plans to develop additional dams that would allow the country's smelting capacity to increase more than five-fold.

(iv) *Inadequately considers alternatives* - According to the Equator Principles, the Environmental Impact Assessment should include the consideration of feasible environmentally and socially responsible alternatives. The interim report of Iceland's Master Energy Plan for Energy Resources found that Kárahnjúkar was the 2nd worst option out of 15 sites considered in terms of environmental impacts. These conclusions were not seriously considered in the Kárahnjúkar EIA even though the interim Master Energy Plan was ready when the EIA was being developed.

www.irn.org
www.foe.co.uk

2.2. The Baku-Tbilisi-Ceyhan oil pipeline

Almost immediately after the launch of the Equator Principles, observers started speculating whether the Principles would prevent Equator banks from participating in the Baku-Tbilisi-Ceyhan (BTC) pipeline project. This $3.6 billion project gave banks an early three-part test of their implementation of the Principles – a test which they comprehensively failed.

In February 2004, the BP-led BTC pipeline received loans from fifteen major commercial banks, nine of which had adopted the Equator Principles. The banks involved were: **ABN AMRO** (Netherlands), **Citigroup** (US), **Mizuho** (Japan), **Société Générale** (France) – all of whom were lead arrangers – and **Banca Intesa** (Italy), **Dexia** (Belgium), **HVB** (Germany), **ING** (Netherlands), **KBC** (Belgium), **Royal Bank of Scotland** (UK), and **West LB** (Germany). Construction of the pipeline is now underway and oil is aimed to flow by mid-2005.

A political project

Widely recognised to be far more of a political project than an economic one, the 1,700 km pipeline will convey Caspian crude oil from Baku in Azerbaijan, via Georgia, to Ceyhan on the Turkish coast of the Mediterranean. It was conceived in the 1990s by the United States, as a means to supply thirsty western markets with non-Middle Eastern oil, to undermine the strategic position of Iran and Russia, and to assert US dominance in a former Soviet sphere of influence.

However, as the pipeline plans developed it became increasingly apparent to civil society groups that this geopolitical meddling would prop up undemocratic regimes, exacerbate tensions in the region and contribute to human rights abuses and environmental destruction.

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Worsening human rights situation

Fears about a negative effect on the human rights situation in the region were realised in November 2003 (five months after the Equator Principles' launch), when Azerbaijan's Presidential election was won by Ilham Aliyev, the son of the previous long-term Azeri ruler. The election, described by official observers from the Organisation for Security and Co-operation in Europe as 'fraudulent', was followed by a brutal clampdown against opposition parties. In his inauguration speech, Aliyev promised that he would use oil revenues to build up the army, and threatened to restart the war with Armenia. These disturbing comments were met with a deafening silence from the West, which was keen not to upset oil interests in the region.

Just a couple of weeks later, a revolution took place in neighbouring Georgia, which was generally seen as a response to the corruption of the Shevardnadze regime, and its failure to relieve the poverty of the majority of the population. Since taking power, new President Mikhail Sakashvili has repeatedly said that Shevardnadze overstated the benefits to the Georgian people of the BTC pipeline.

Meanwhile in Turkey, there is a history of decades of human rights abuses against the Kurds, and indeed of use by the state of infrastructure projects to displace Kurdish villages or to increase security measures.

Environmental concerns

The BTC pipeline also poses severe environmental risks. The pipeline route will run through a number of wetlands of critical importance for protected and endangered birds such as Dalmatian pelicans, black storks and imperial eagles. In Georgia, the pipeline will run through the Borjomi National Park, an important cultural and tourist site, and the source of Georgia's largest export – Borjomi mineral water, which is famous across the Former Soviet Union. The area of the pipeline is subject to high seismic activity, landslides and avalanches. A rupture in the pipeline and consequent oil leak could have devastating consequences for mineral water sources and wetlands.

Equator Principles not applied

Against this background of political, environmental and human rights risk, the value of a tool such as the Equator Principles becomes apparent -- but only if that tool is genuinely and effectively used.

The Equator Principles can be used in three ways – to exclude financing of projects which fail to meet certain minimum standards, to set markers for improving projects' design and performance, and to hold clients accountable for meeting environmental and social performance standards. In the BTC case, which the Equator banks themselves touted as a key test of the Principles, the banks failed all three parts of the test.

In October 2003, fourteen organisations from eleven countries wrote to the Equator banks, pointing out that the BTC plans violated the Equator Principles on numerous counts including the Indigenous Peoples policy on 30 counts, four other World Bank standards (with which the Equator Principles require compliance) on 97 counts, and nine other clauses of the Equator Principles on 30 counts.[7]

For example, many landowners were poorly compensated for losing their land, and some landowners were not compensated at all. The project's environmental impact assessment failed to adequately assess the pipeline damage – for example, the whole 1,000 kilometres of the Turkey section of the pipeline was surveyed in just a few weeks, with even highly sensitive and protected sites being visited only on one day. Consultation procedures were cursory at best, and often in the wrong language, or only carried out after all decisions had already been made.

One of the most disturbing breaches of the Equator Principles by the project was in the project sponsors' decision not to apply the World Bank's safeguard policy on Indigenous Peoples. That policy requires publication of a specific plan to ensure that ethnic minorities, such as the Kurds in Turkey, are not adversely affected by a project, and compliance with the policy is a clear requirement of the Equator Principles.

The impact of this failure is perhaps most stark in Turkey. There the BTC pipeline will be guarded by the notorious *Gendarmerie*, which has been repeatedly criticised by the Council of Europe and the European Court of Human Rights, and has been associated with displacement and destruction of villages, torture, and 'disappearances', especially against Kurdish people. It is almost inevitable that the Gendarmerie will use the pipeline as a pretext for carrying out raids on local Kurds – and the decision not to apply the safeguard policy leaves no protection against this. Already since the financing decision, at least one Kurdish human rights defender has been arrested and tortured, following his work to help affected landowners to obtain the compensation due to them.

The private banks did not effectively use their clout to advocate for significant improvements in the project's design or environmental/social impacts. In private, several banks admitted that they were not carrying out due diligence because they simply trusted BP and the International Finance Corporation to get it right. This occurred despite the fact that the Equator Principles state "The adopting institutions view these principles as a framework for developing individual, internal practices and policies…. Banks are adopting and implementing these principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank"

Pipeline technical failings

That trust proved to be misplaced. In February 2004, the *Sunday*

Times newspaper reported that the pipeline had been using an inappropriate weld coating, which risked causing major leakage. The findings came from an international expert in weld coatings, who had worked on the pipeline and advised against using the coating. He wrote to BP, "We are completely out on a limb … I have witnessed many failures in specifications . . . but the situation on the pipeline is unique in my 41 years' experience. There is no question in my own and many other people's minds that the wrong system has been chosen through a seriously flawed selection programme."[8] Cracks have now appeared in the pipeline coatings, yet arguments continue between BP, financial institutions and contractors over whether wrongly coated sections of pipeline should now be dug up and re-coated.

In the ensuing correspondence, financial institutions have contradicted themselves and each other in trying to explain away the problems. Reportedly, the bank syndicate requested that the consortium prepare an official report on these allegations, but the results of this report and any corrective action taken by the Equator banks is unknown. The private banks, including the Equator signatories, have refused to comment, citing commercial confidentiality.

Banks will be held to account

International NGOs have committed themselves to continuing to monitor the BTC pipeline, and to holding its financiers to account. As banks see themselves publicly associated with the problems of the BTC pipeline, including poor technical standards and increasing human rights fears, they should ask themselves whether the reputation damage and loss of credibility are really compensated by the returns from the BTC investment.

There are three sets of legal actions in process against the pipeline. One Georgian environmental group, Green Alternative, alleges that the pipeline consortium and Shevardnadze government violated Georgian environmental law in routing the pipeline through the Borjomi-Kharagauli National Park. They are appealing an unfavourable ruling on this case. Two international NGOs have initiated a case in the European Court of Justice, which argues that the project's legal agreements so undermined Turkey's ability to legislate that it was in breach of its Accession agreements with the European Union. Finally, 38 landowners living in Turkey have applied to the European Court of Human Rights, arguing that their property was expropriated unfairly and in violation of their rights.[9]

The banks themselves are now also under direct attack for their failed due diligence on the BTC pipeline. A Belgian NGO, Proyecto Gato, has made a formal complaint against three Belgian banks (Dexia, KBC and ING – all three Equator signatories) through the OECD's Guidelines on Multinational Enterprises. The complaint centres on the pipeline coating issue and on the undue constraint over the host governments' ability to regulate that is imposed through the project legal agreements.[10]

Banks can thus be sure they have not heard the last of the BTC *the BTC pipeline would seem to expose the signing of these banks to the Principles as a public relations exercise which allows them to continue with business as usual whatever the risks to people and nature*

project. As Jules Peck of WWF has commented, "As a test case, the BTC pipeline would seem to expose the signing of these banks to the Principles as a public relations exercise which allows them to continue with business as usual whatever the risks to people and nature."

www.carbonweb.org
www.panda.org/btc
www.baku.org.uk

2.3. Kainantu gold project - Papua New Guinea

ABN AMRO Bank (the Netherlands) in January 2004 arranged a $30.3 million loan for Highlands Pacific to finance the development of the Kainantu Gold Project in the Eastern Highlands' Province of Papua New Guinea. The mine should produce around 115,000 ounces of gold annually and Highlands Pacific hopes to start production in mid-2005. Total project costs are estimated at $39.6 million,[11] and ABN AMRO Bank committed $10.1 million itself.[12] The project is thus below the treshold of $50 million that would make it subject to the Equator Principles but otherwise poses exactly the sort of risks that banks try to deal with through the Principles.

Critics note that in its hurry to develop the mine, the company failed to address the complex social and landowner disputes between the 11 clans claiming interests in the area. The project has in fact aggravated these disputes, as the division of benefits from the mine is unresolved. In one incident in October 2003 at least three people were killed when police were called in to deal with fighting as a result of landownership conflicts in the mining area. [13]

Since the signing of the loan, criticism of the project has only increased. Community expectations of the economic opportunities attached to the project such as jobs, money and other benefits are very high. However, negative impacts of the mine are already surfacing, with growing social problems such as alcoholism and prostitution, and reported increases in HIV in the area.

Locals are wondering if the promised benefits will materialise. Reports from the area show that people from other regions such as the Western and Southern Highlands are being employed, and that locals are being overlooked in contracts the mine is giving out. Out of frustration, hundreds of angry locals took to the streets in Kainantu on March 12, 2004, rioting, tearing down walls, looting and turning over vehicles. Frustration was centred on the offices of Highlands Pacific, with an unruly crowd ripping off the roof and looting the premises.

Apart from these social issues, recently an independent review of the mine's environmental management commissioned by the Australian Mineral Policy Institute criticised the sub-standard environmental planning by the company. The review showed major gaps in the assessment and evaluation of the project’s risks, posing unnecessary threats to the local environment and waterways, which are the basis of subsistence livelihoods in the region.[14]

2.4. Lukoil D6 oil project - Baltic Sea

In March 2004, the Russian oil company Lukoil began the development of the oil deposit D6 (Kravtsovskoye), located offshore from Kaliningrad. Kaliningrad is a Russian enclave on the Baltic Sea, bordered by Poland and Lithuania. Located only 22 kilometres from the oil deposit is the Curonian Spit, a narrow strip of sand from 350 metres to four kilometres wide and 92 kilometres long that forms a lagoon along the Baltic Sea coast. The Curonian Spit is a national park in both Russia and Lithuania and was inscribed on the Unesco World Heritage List in 2000. The area has some of the highest sand dunes in Europe and its forests, planted in the 19th century to halt the sand erosion, carry a high level of biodiversity.[15]

This oil deposit, with estimated reserves of 24 million tonnes, was discovered in 1983. During drilling tests in the D6 structure in June 1983, approximately 70 tonnes of oil were spilled into the Baltic Sea and soon reached the coasts of the Curonian Spit and were cast ashore. Around 20 kilometres of coastline were polluted with oil, both on the Russian and Lithuanian sides. Because of this accident and ensuing public protest, the project was stopped in 1987, but Lukoil recommenced it in 2000.[16] Lukoil is planning to invest US$ 270 million in the project, to start production at the field in the summer of 2004, and to bring output to 600,000 tons per year by 2007.[17]

The inhabitants of the towns on the Baltic coast of Kaliningrad were left ignorant of the project, which does not bring any jobs to the area and could harm the local investment climate. In the case of an oil spill, an attractive sustainable tourism spot and fishing site would turn into a devastated area.[18]

Since 2000, the Russian NGO Ecodefense has campaigned against the D6 project, because of the high danger of oil pollution caused by accidents and the project’s overall negative impact on the Baltic Sea ecosystem. Ecodefense is accusing Lukoil of misleading and manipulating public opinion and disrespecting democratic legislation, by limiting access to information about the project during the drafting of the Environmental Impact Assessment and by countering the public’s efforts to participate in the assessment of the project.

In June 2003 Ecodefense received support from the Coalition Clean Baltic, a network of 27 environment NGOs comprising over half a million members in the countries around the Baltic Sea. The coalition urged the Helsinki Commission and the European Commission to take immediate action against the project. [19]

In March 2004 Nordic and Baltic government leaders urged the European Union to help stop Russian violations of environmental safety standards for shipping and drilling oil in the Baltic Sea.[20] In May 2004 the Parliamentary Assembly of the Council of Europe announced it will investigate the consequences of Lukoil's plans on the environment.[21]

To finance the D6 project and other expansion projects, Lukoil in November 2003 secured a $765 long term debt facility from an international syndicate of 28 banks arranged by **ABN AMRO Bank** (The Netherlands) and **Citigroup** (United States). The deal is split into a five year $465 million tranche and a $300 million seven year tranche. Other EP-signatories participating in the syndicate were: **Calyon** (France), **Dresdner Bank** (Germany), **Barclays** (United Kingdom), **KBC** (Belgium), **WestLB** (Germany), **HVB** (Germany) and **Dexia** (France).[22]

www.ccb.se

2.5. Maggi soybean expansion - Brazil

The rise of large-scale soybean farming in the central western part of Brazil is causing severe social and environmental problems. Deforestation of the *cerrado* (savannah) is increasing rapidly, while the soybean expansion is also threatening the Amazon rainforest more to the north. In the Interministerial Plan on Deforestation of the Brazilian government, released in March 2004, soybean cultivation is mentioned as "one important factor in recent Amazon deforestation".[23]

Monoculture is disrupting the hydrological balance in this area and is threatening its high biodiversity. Land conflicts with small peasants and indigenous groups have intensified, with several soybean farmers illegally occupying indigenous lands.[24]

Various social and environmental NGOs in Brazil and in soybean-importing countries such as the Netherlands, Belgium, Switzerland, Germany and the United States, are stepping up efforts to control the social and environmental consequences of the soybean boom in the Brazilian Midwest. In March 2004 the Brazilian Forum of NGOs and Social Movements adopted a set of minimum criteria for soybean cultivation in forest areas.[25]

Grupo André Maggi is the largest producer of soybeans in Brazil and probably in the world. Apart from its own production in Mato Grosso state, the company buys huge amounts of soybeans from other farmers and transports these to export markets. To finance advance payments to its suppliers before planting and to finance storage and transport of soybeans, Grupo André Maggi needs large working capital facilities.

In January 2004, Grupo André Maggi secured a $230 million working capital facility from an international banking syndicate of 11 banks, arranged by **Rabobank** (the Netherlands). $150 million will be used as working capital to finance soybean stocks. The other $80 million will be used to finance inputs for soybean farmers supplying soybeans to the group. The facility was increased from $200 million, because of the strong interest of banks to participate. In addition to Rabobank, the following EP signatories participated in the syndicate: **Crédit Suisse** (Switzerland), **HSBC** (United Kingdom), **ING Bank** (The Netherlands) and **WestLB** (Germany). [26]

2.6. Mindanao power plant – the Philippines

At the end of January 2004 the construction of the Mindanao Power Plant started in Villanueva near the provincial capital Cagayan de Oro on the northern coast of Mindanao island in the Philippines. The 232 MW hard coal-fired power plant project is developed, financed, built and operated by a joint-venture between the German company STEAG and the State Investment Trust. The plant is scheduled to be complete by December 2006 and will cost about US$ 355 million. STEAG claims that the plant is needed to meet swiftly rising power demand among the island's population of 20 million. It also claims that "highly efficient environmental protection systems will ensure that the Mindanao power plant meets all requirements of the Philippine regulatory authorities and the strict thresholds stipulated by the World Bank".[27]

Over the past few years local NGOs - headed by the Task Force Macajalar - have campaigned strongly against the project, because of fears that its air emissions would pollute the regional environment and threaten the health of the local population. Furthermore, to clear the site hundreds of farmers and their families in Villanueva had to be displaced according to the Task Force Macajalar. Foreign NGOs, including Friends of the Earth and a groups from Japan and Germany, joined the campaign.[28] In November 2002 the Archbishop of Cagayan de Oro stated its support for the protests, asking the authorities "to listen to our apprehensions, fears and anxiety regarding this plant that can turn out to be a monster and a beast instead of a friend".[29]

the Archbishop of Cagayan de Oro stated its support for the protests, asking the authorities "to listen to our apprehensions, fears and anxiety regarding this plant that can turn beast instead of a friend

To finance the project, sponsors in November 2003 secured a $201 million debt facility, comprising of a $60.6 million loan from Japan Bank for International Cooperation (Japan); a $40.4 million syndicated bank loan guaranteed by Nippon Export and Investment Insurance (Japan) and a $200 million syndicated bank loan guaranteed by Gerling Allgemeine Versicherungs (Germany). The two last banking syndicates were arranged by four banks, including **HVB** (Germany) and **Dresdner Bank** (Germany).[30] This project should have been subject to the Equator Principles; however it is unknown how HVB and Dresdner Bank categorized and assessed the project and what kinds of environmental conditions, if any, the banks imposed.

2.7. Trans Thai-Malaysia pipeline - Thailand

The state-owned oil companies of Malaysia and Thailand, Petronas and PTT, in 1999 started a joint project to build a natural gas pipeline and a separation plant at a total cost of $1.0 billion. The

Trans Thai-Malaysia pipeline will bring crude natural gas from the Gulf of Thailand onshore near Chana in Songkhla province. There, the LPG will be separated from the natural gas and will be sold in Thailand. The purified natural gas will be transported by pipeline to the Malaysian border in Perlis, where it will link into the Malaysian gas grid.[31]

The local population of the districts in southern Thailand where the pipeline passes through have appealed and fought against the project since the start. They claim the project will threaten their way of life and destroy their food sources, as well as jeopardise the country's food security. The villagers are very concerned about the effluents and air emissions which will be caused by the project. The small-scale fishermen and Chana's famed song-bird raising industry rely on clean air and water.[32]

The UN Special Envoy on Human Rights Hina Jilani criticized the government's harassment and intimidation of those using their freedom of expression to protest, creating a "climate of fear"

The legal procedures started by local villagers against the project have had some success: the Environmental Impact Assessment (EIA) of the separation plant was held up more than a year. Although the ministry's own expert panel voted against the project, the EIA was finally approved in December 2001.[33] Since construction started in 2002, the Thai military and police intervened several times to stop the demonstrations, blockades and other protests, leaving many injured and detaining a large number of protesters. Strong legal actions were taken against the protesters. After a visit to this region in May 2003, the UN Special Envoy on Human Rights Hina Jilani criticized the government's harassment and intimidation of those using their freedom of expression to protest, creating a "climate of fear".[34] And the situation has further escalated since then; in November 2003 the number of policemen permanently guarding the project site was raised to 400.[35]

Despite the protests, the project is expected to be finished in early 2005 with the first gas to be transported in mid-2005.[36] This is made possible to a large extent by a $524.3 million project financing arranged by **Barclays** (United Kingdom) in April 2004. Barclays itself provided $257.1 million, while fourteen banks joined as mandated lead arrangers. Due to the overwhelming interest among banks to participate in the loan, it was not even launched into general syndication. The following EP signatories participated in an amount of $19.55 million each: **Calyon** (France), **Dresdner Bank** (Germany), **HSBC** (United Kingdom), **ING Bank** (The Netherlands), **KBC Bank** (Belgium), **Mizuho Corporate Bank** (Japan) and **Standard Chartered Bank** (United Kingdom).[37] Again, it is unclear how various Equator banks implemented the Principles in this transaction.

2.8. Transredes network expansion - Bolivia

The Bolivian company Transredes operates a network of 6,000 kilometers of pipelines, transporting natural gas, crude oil and oil products within Bolivia and also transporting natural gas to Brazil and Argentina. The company was privatised in 1997, when, amongst others, Royal Dutch/Shell (Netherlands/United Kingdom) and Enron (United States) acquired a 50% shareholding.[38]

After recent discoveries of huge gas fields in Bolivia, Transredes is working on an expansion program which would increase its gas transport capacity from 7 to 11 billion m^3 natural gas per year. Capacity to transport natural gas liquids will increase to 71,000 barrels per day. The program will boost the country's export capacity while also meeting internal demand.[39]

In August 2003, Transredes secured a $220 million financial package to finance this expansion program. The financial package consisted of a $75 million loan from the Inter-American Development Bank; a $50 million loan from Corporación Andina de Fomento (CAF); and a $95 million commercial bank loan, provided by international banking syndicate led by **ABN AMRO** Bank (the Netherlands) and **BBVA** (Spain).[40]

Various environmental and indigenous NGOs, including Amazon Watch and Friends of the Earth, campaigned against this expansion program - especially the capacity expansion of the existing Yabog pipeline from Yacuiba in the south to Rio Grande, where it links to the Bolivia-Brazil pipeline - because of the possible consequences for the environment and indigenous peoples along the route. 97% of the forests along the route are dry Chaco forests and 3% are wet forests. Bolivia's dry forests are among the richest in the world and are classified as "globally outstanding" in the WWF/World Bank ecoregions conservation assessment. The biota of the region has affinities with the Amazon and contains many endemic species.

Concern over the environmental impacts of the Transredes project is aggravated by the company's poor environmental track record. In 2000, the spillage of 29,000 barrels of oil into the Desaguadero River from the Sica Sica-Arica pipeline resulted in major environmental damage. The spill caused $2.2 million of economic damage and affected 18 municipalities.

The Yabog pipeline project cuts through large sections of Guaraní and Weenhayek indigenous ancestral homelands. These indigenous people fear threats to their livelihood, food and water supply, cultural integrity and psychological well-being. They report that after 30 years of activity surrounding the Yabog pipeline, game has fled the area and communities are forced to travel long distances to hunt. They fear that renewed construction activity will worsen this problem. The Weenhayek rely principally on fishing for subsistence and fear water pollution.[41]

www.amazonwatch.org

3. Trouble Ahead?

The last chapter gave examples of projects that went ahead in the first year of the Equator Principles' existence. Positive-minded observers might attribute some of these decisions to the fact that the Principles have not yet found their way into everyday practices of EP banks and that, over time, such projects will either be mitigated or rejected altogether. Such a conclusion would gain credibility if the Equator banks disclosed more information on their sincere efforts to implement the EPs.

However, after one year, the basic lessons should have been learned. This chapter lists some of the projects that BankTrack, as well as numerous other organisations, consider outright treats for local communities and/or the global environment. While it is not always 100 percent clear that Equator banks are currently considering involvement in these projects, financing them in their current design would be considered incompatible with a good faith application of the Equator Principles, and would further erode confidence amongst civil society in the credibility of the Principles.

3.1. The Sakhalin II oil and gas project - Russia

Banks are being warned by NGOs to stay off a devastating new oil and gas project on Sakhalin Island in Russia's Far East. The project, which is being developed by a consortium led by Shell, will have severe environmental impacts, including threatening the critically endangered Western Gray Whale with extinction, damaging habitats of endangered bird and fish species, and polluting important fisheries. Experts have reported that the project design falls far short of industry best practice, and that its risk assessments are inadequate. As a result, the project risks causing a catastrophic oil spill, as well as having major routine impacts.

It is not just NGOs that are concerned. The European Bank for Reconstruction and Development (EBRD) has described the Sakhalin II EIA (Environmental Impact Assessment) as "unfit for purpose" and has indicated that it will not provide financing unless and until Sakhalin Energy provides additional information that adequately addresses their concerns. EBRD's President publicly commented further that "We are not yet satisfied with the answers we have received and the present situation, and we have said so to the sponsors of the project."

With a capital cost of at least $12 billion, the project is expected to seek project financing later in 2004. But any banks that agree to provide loans will face considerable reputational risk, such as being associated with causing the extinction of a whale species, and wider environmental impacts.

Threat to whales

The east coast of Sakhalin Island is the only known summer feeding ground of one of the world's most endangered species of whale, the Western Gray Whale. With a population of just around 100 remaining, and fewer than 20 breeding females, the very survival of the species is threatened. The species is classified as Critically Endangered (extremely high risk of extinction) by the IUCN (World Conservation Union).

Since 1999, scientists have reported seeing an increasing number of 'skinny' (under-nourished) whales – which reduces the population's chance of recovery. Although the cause of this under-nourishment is not known for certain, it has been observed since the Phase 1 Sakhalin II platform began operation.

Yet Shell has proposed to construct offshore pipelines on the seabed directly through the whales' benthic feeding ground. Since the whales feed by sucking up sediment from the seabed and filtering out benthos (small animals and plants that live there), it is feared that pipelines along the seabed will cause substantial disruption to feeding patterns, and further risk the population's viability.

There will also be major impacts on the whales from routine and accidental pollution from the oil and gas facilities, from sedimentation caused by construction activities, from potential collision with marine vehicles, and from constant operational noise. Shell has failed to adequately assess these impacts, or to demonstrate that the mitigation measures it proposes are adequate to protect the Western Gray Whale from negative impacts.

Violation of Equator Principles

The Sakhalin II project clearly fails to comply with the Equator Principles. The project's environmental impact assessment (EIA), mandatory for projects of such magnitude, is critically deficient on a number of counts.[42] These include:

(i) The EIA does not include key baseline data, including identification of specific information about endangered species, a prerequisite to adequate assessment of project impacts and the determination of necessary mitigation measures. These endangered species include the Western Gray Whale, Stellar's Sea Eagle, and Sakhalin taimen, masu salmon, and other wildlife species. Some of the baseline data conflicts with other expert reports. The EIA also fails to evaluate conflicts that may arise between the project's Production Sharing Agreement and Russian environmental law, and does not address legal challenges to the project.

(ii) The Equator Principles also require the EIA to assess the project's compliance with the World Bank's Pollution Prevention and Abatement Handbook. The EIA does not do this, nor does it provide sufficient information, in an appropriate form, for an external reviewer to assess compliance.

(iii) Key environmental impacts are omitted from the EIA, including the impacts on many wild salmon-bearing streams and the impact of oil spills. Other important impacts are inadequately analysed, such as those on the Western Gray Whale. Some mitigation measures are missing, flawed, or unsubstantiated in terms of their effectiveness, including mitigation of negative impacts on the Western Gray Whale population and of seismic risks.

(iv) Cumulative impacts with other oil and gas projects on Sakhalin Island are not considered; the EIA also does not systematically compare the project with feasible alternatives.

There are further problems in project design, which also constitute breaches of the Equator Principles:

(v) The siting of the offshore platforms and the routing of the offshore pipeline will degrade the Western Gray Whales' summer feeding ground, a so-called Critical Natural Habitat. The project also fails to apply the precautionary principle in relation to Western Gray Whale feeding grounds, to watercourse crossings, and to dumping of wastes in Gulf of Aniva. This constitutes a breach of IFC Safeguard Policy OP 4.04 on Natural Habitats and hence Principle 3 of the Equator Principles.

(vi) Consultation processes on the project were seriously flawed. The project failed to provide sufficient information to local and international stakeholders, and did not take consultees' views into account. (A breach of Principle 5).

(vii) The Equator Principles also require the production of an Environmental Management Plan which is yet to be published.

Just say no
Based on these project failings, NGOs recommend that, in the absence of fundamental changes to the project, Equator banks should refuse loans to the Sakhalin II project. They also insist that banks carry out their own rigorous due diligence of the project, rather than relying on that of project sponsors or other financial institutions; and that, in the interests of transparency, banks should publish their analysis of project compliance with the Equator Principles.

If the possible extinction of an entire whale species falls within the range of normal risks the Equator Banks want to 'determine, assess and manage' with their Principles, what good are such Principles then?

As one campaigner commented; "If the possible extinction of an entire whale species falls within the range of normal risks the Equator Banks want to 'determine, assess and manage' with their Principles, what good are such Principles then?"

www.carbonweb.org
www.sakhalin.environment.ru
www.pacificenvironment.org

3.2. The Omkareshwar Dam - India

A number of European private banks have been asked to provide support to India's National Hydroelectric Power Corporation (NHPC) for the construction of the Omkareshwar Dam in the Indian

State of Madhya Pradesh. The site for the 73 meter-high dam lies about one kilometre upstream of the sacred temple town of Omkareshwar on the Narmada River. It will displace over 50,000 small farmers and submerge up to 5,800 hectars of one of Central India's last intact natural forests. Construction work on the dam was taken up in November 2003 and is supposed to be finalized by March 2007. However, affected people have already captured the dam site once, and broad-based local opposition to the project makes it unlikely that construction will be able to proceed smoothly.

Violating Host Country Policies and Laws

In 1989, the Government of Madhya Pradesh decreed a "Rehabilitation Policy for the Oustees of the Narmada Projects." This policy specifies that farmers whose lands are expropriated for one of the Narmada projects are entitled to land-for-land compensation. Although the project sponsor claims to be following the Madhya Pradesh Resettlement Policy completely, villagers are in fact being driven off their lands by intimidation and forced to accept meager cash compensation. An NGO fact-finding mission to the Omkareshwar area in November 2003 documented the eviction of the first village to be affected by the dam (Panthiaji). The inhabitants of Panthiaji were forced to clear out their village overnight and were moved to two resettlement camps, which lack even the most basic facilities. There are no employment possibilities and no agricultural lands available in the area. The cash compensation that villagers received is so paltry that they are not able to buy new land elsewhere. Thus, a formerly self-sufficient farming community was turned into a group of development refugees living in tents and tin sheds, facing total destitution once their savings run out.

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In total, the fact finding mission visited over one-third of the villages in the submergence area. Although villagers' lands are already being acquired, not a single family has received or been offered land-for-land compensation. Instead, villagers' petitions are ignored and project officers have told people that they will receive only cash; if they protest, they will receive nothing. These practices are a clear violation of Madhya Pradesh's resettlement policy.

Environmental Impact Assessments (EIAs) for large dam projects have been routine administrative procedure in India since the late 1970s. In 1985, the Ministry of Environment and Forests issued its "Guidelines for Environmental Assessment of River Valley Projects," which specify the various studies that must be carried out under an EIA. Furthermore in 1994, the Indian Ministry of Environment and Forests issued a notification under the Environmental Protection Act, making EIAs a legal requirement for large dams. In spite of these requirements, no Environmental Impact Assessment was prepared for Omkareshwar.

Violating IFC's Safeguard Policies

The Omkareshwar Project violates five of IFC safeguard policies referenced in the Equator Principles.

(i) Indigenous Peoples: Between 30 – 50% of the population in the

submergence are indigenous ('Adivasi') and belong to the Bhil and Bhilala tribes, who are awarded special protection under the Indian Constitution. IFC's Indigenous Peoples Policy is based on the principle of informed participation and the establishment of an indigenous peoples' development plan. In the case of Omkareshwar, no such plan has been developed and indigenous people have neither been informed nor consulted.

(ii) Environmental Assessment: No Environmental Impact Assessment was undertaken for the Omkareshwar Project. This is a clear violation of the Equator Principles, under which the preparation of a full EIA is mandatory procedure for projects such as large dams.

(iii) Natural Habitats: IFC's policy prohibits financing projects that involve the significant conversion of critical natural habitats. It also includes a consultation requirement, to ensure that local communities' views and rights are taken into account. The dam reservoir will submerge up to 5829 hectares of natural forest, including parts of the Chandgarh and Nimanpur reserved forests on the North Bank of the Narmada and the reserved and protected forests of Punasa and Gunjari on the South bank. The Wildlife Institute of India has noted that the loss of these areas will intensify pressure on the remaining forest areas, and fears that these will be "drastically altered". None of the local communities have been consulted, although many of them depend on forest resources for part of their income.

(iv) Cultural Property: The project area contains many historic shrines and temples. In spite of the provisions in the Equator Principles and IFC's policy, no consultation or mitigation measures (such as relocations of culturally significant structures) were included in project planning. During the eviction of Panthiaji, a unique 13th century temple, which is listed by the Archeological Museum Department of Madhya Pradesh, was simply bulldozed. In addition, the famous temple town of Omkareshwar (which is situated on an island just one kilometre downstream of the dam) will encounter problems, as the expected erosion of the river banks will threaten the long-term stability of temples on the perimeter of the island. No measures have been designated to deal with this problem although Omkareshwar is considered to be the most sacred place in the entire Narmada Valley and attracts hundreds of thousands of pilgrims each year.

(v) Involuntary Resettlement: IFC's policy states clearly that cash compensation alone is normally inadequate and that preference should be given to land-based resettlement. It also calls for up-to-date socio-economic surveys of the affected population and requires a detailed resettlement plan, based on extensive consultation. In the case of Omkareshwar, no such surveys have taken place and no resettlement plan exists. While the project authorities claim that only 15,000 people will be affected, the actual number is likely to be over 50,000. In violation of the Equator Principles, even the most basic information is being withheld from project-affected people; and the project authorities have refused to provide any land-based compensation. The experience of Panthiaji (the first village that has been displaced)

shows that the project is driving affected communities into destitution rather than restoring their livelihoods.

Displacing the People and Damning the Principles

It would conceivably be hard to find a project that is more obviously out of line with the Equator Principles than Omkareshwar. Accordingly, the World Bank's Multilateral Investment Guarantee Agency (MIGA) turned down an application for the project in Spring 2004 because of "environmental and social concerns". Deutsche Bank, which is not an Equator Bank and was approached in early 2003, has in the meantime also declined financing for the project. It is therefore all the more surprising that three of the Equator Banks, **Standard Chartered**, **ABN AMRO** and **Calyon** (fomerly Credit Lyonnais), are still considering providing a loan for Omkareshwar. Furthermore, the Omkareshwar Project is indicative of the total lack of credible environmental and social procedures at NHPC and should be a warning to banks to refrain from further financing for this agency.

It would conceivably be hard to find a project that is more obviously out of line with the Equator Principles than Omkareshwar

www.urgewald.de
www.narmada.org

3.3. Nam Theun 2 hydropower project - Laos

The $1.2 billion Nam Theun 2 hydropower project in Laos is undertaken by the electricity companies Electricité du Laos (Laos), Electricité de France (France) and Electricity Generating Public Company (Thailand), together with the Thai construction company Italian-Thai Development. The hydropower project, situated some 250 kilometres to the southeast of Vientiane, will have a generating capacity of 1,070 MW. Of total output 93% will be exported to neighbouring Thailand.[43]

The Nam Theun 2 project is supposed to alleviate poverty in Laos. However, International Rivers Network argues in a recent publication that the project "will instead impoverish thousands, saddle the Lao government with more debt and devastate tropical river ecosystems upon which so many depend for their livelihoods." The IRN report summarizes the major concerns about the project as follows:[44]

- The project will forcibly displace 5,700 indigenous people from their ancestral lands and severely impact a river system on which over 120,000 people now depend for their fishing and farming-based livelihoods;
- It will have adverse impacts on biodiversity, including endangered bird, mammal and fish species;
- Nam Theun 2 is a risky project for the Lao government, which is relying solely on Thailand to purchase power for the next 25 years;
- The Lao government has a troubled history of implementing hydropower projects, which does not auger well for a project as large, complex and risky as Nam Theun 2;

- The project violates six out of seven of the World Commission on Dams' strategic priorities, including those on public acceptance and options assessment.

After a recent visit to the project area, NGOs from Italy, France and the US add some additional concerns to the ones mentioned above:[45]

- In the mid-1990s the Nakai Plateau (where the project is located) was extensively and illegally logged in anticipation of the Nam Theun 2 project. As a result, villagers lost the resource base from which they derived part of their income. Villagers were never compensated for these losses;
- The consultation process was undertaken by officials of the military government with no independent audits and no discussion of alternatives;
- Detailed information on resettlement and environmental and social mitigation plans for Nam Theun 2 was disclosed just recently and only via the web. The disclosure procedure and comment period chosen by the consortium does not comply with World Bank disclosure requirements.

To finance the project, the Nam Theun 2 Power Company is looking for $850 million of long term project financing, split in equal proportions between Thai Baht and US dollars. In February 2004 a group of nine banks was appointed to arrange the $420 million international project loan, including the following EP signatories: **Calyon** (France), **KBC Bank** (Belgium), **ING Bank** (The Netherlands) and **Standard Chartered** (United Kingdom).[46] Financing has not been arranged yet, as the World Bank and other multilateral banks and export credit agencies first have to decide if they are prepared to cover some of the risks of the bank loans. Decisions are expected at the end of 2004 or early 2005.[47]

www.irn.org
www.rwesa.org

3.4. East Siberia gas pipeline - Russia

In November 2003, China National Petroleum Corporation (China), Rusiya Petroleum (Russia) and Korea Gas Corporation (South Korea) approved a feasibility study for the construction of a natural gas pipeline from the Kovykta gas field in Irkutsk in eastern Siberia to China and South-Korea. This field contains 1,400 to 1,900 billion m3 of natural gas. The East Siberia gas pipeline will have a total length of 4,887 kilometres and will require a total investment of $17 billion. The pipeline will start in Irkutsk, skirt around the southern shore of Lake Baikal and enter China at Manzhouli on the Russian-Chinese border. [48]

China is very keen to advance the project, but the Russian government has not yet approved the feasibility study. It is pushing a stronger role for the Russian gas giant Gazprom in the project, by appointing Gazprom as "coordinator" of exploration and exports of gas from eastern Siberia. But Gazprom is not willing to invest in the project.[49]

Lake Baikal is the world's oldest and deepest lake. Its vast basin contains one-fifth of the world's freshwater and thousands of endemic species. The lake plays a crucial role today in Russian culture and national pride, remaining one of the most pristine wildernesses in a country scarred by Soviet-era industrial projects. Lake Baikal and the surrounding area was named a World Heritage Site by Unesco in 1996 and its shore is ringed by nature preserves. At the south of the lake lies the Tunkinsky National Park, which would be crossed by the gas pipeline. This is a mountainous, pristine area with unique Siberian pine and fir forests, curative springs, capricious mountain rivers and many endemic species. This area is threatened by two oil pipeline projects as well, but the East Siberia gas pipeline seems to be the most advanced.[50]

The Kovykta gas field and the Russian part of the pipeline are developed by Rusiya Petroleum, a company which is majority-owned by the British oil company BP and its Russian partner TNK. At a presentation for the financial community in London in October 2003, BP chief Lord Browne said the board of the TNK-BP joint venture would be considering project finance as an investment method, although BP nearly always funds its projects on-balance sheet. Only in rare circumstances, as with the BTC pipeline project, does BP share ownership, and seek non-recourse debt to manage commercial and political risk. Other reasons why a project finance structure might be attractive for the East Siberian gas pipeline include the facts that BP has to deal with other shareholders, high capital outlay is needed, reputational risks are high, and there may be financial restrictions imposed by Russian law.[51]

No steps have been taken yet to find project financing, but these can be expected in the coming year. If BP and TNK decide to finance their part of the project from their balance sheet, it is relevant to mention the most recent financing activities of the two partners: In April 2004 BP raised £ 250 million ($450 million) by issuing 3.5 year bonds on the European capital market, with **HSBC** (United Kingdom) as one of the two bookrunners.[52] In March 2004 the joint-venture TNK-BP started looking for a five-year $300 million syndicated loan. It was rumoured in May 2004 that **Citigroup** (United States) had won the mandate to arrange the loan, but this is not yet confirmed.[53]

www.baikalwave.eu.org

3.5. Rio Blanco copper mine - Peru

The small British mining company Monterrico Metals is developing several projects in Peru. The most promising of these is the Rio Blanco copper project undertaken by its subsidiary Minera Majaz. This project is situated in the Andes mountains at an altitude of 2,500 metres, near the town of Pan de Azucar in Huancabamba province, close to the Ecuadorian border. In May 2004 Monterrico Metals revised its production estimate upward to 200,000 tonnes of copper annually, together with significant amounts of molybdenum concentrate. This would make Rio Blanco into the second largest copper mine in Peru, behind Southern Peru.[54]

To start production in 2007, Monterrico Metals in April 2004 awarded contracts for a full bankable feasibility study. The company is looking for $400 million in debt (70%) and equity (30%). Monterrico has already been in talks with six London-based project finance mining teams ahead of awarding a mandate this year. The banks in the running include **Barclays** (United Kingdom), **HSBC** (United Kingdom) and **WestLB** (Germany).[55]

At the same time local resistance against Minera Majaz in the Pan de Azucar region is growing. Local peasants fear their own health and the health of their cattle and crops will be threatened when the mine pollutes water sources in the region with chemicals such as cyanide. The mine is located in the headwaters of the Blanco and Tomayaco rivers. Pollution could affect not only basins which stream off to the Pacific Ocean, but also the Amazon basin. Furthermore, the local population sees the mine as threatening (eco)tourism, which is fast becoming an additional source of income in the region. Based on similar experiences in other regions, they mistrust the promises of the mine company to create local employment and economic development.[56]

At the end of April 2004 a protest march to the project area by around three thousand local farmers was countered by a large police force using tear gas, batons and rifles. Several farmers were severely injured and one died. In response some of Minera Majaz's buildings were attacked. Twenty farmers were arrested and will face charges for demolition. Local resistance against the project will most probably intensify.[57]

4. Putting principles into practice

The previous chapters sought to assess EP implementation by examining projects financed by Equator banks and highlighting those that may be in the pipeline. Implementation can also be assessed by examining whether banks have instituted the appropriate systems, processes and procedures to effectively adopt the Principles.

Clearly, any good faith adoption of the Equator Principles will require banks to make substantial changes in their everyday practices. In December 2003, BankTrack presented a set of proposals to Equator signatories for implementing the EPs.[58] It was largely based on widely-recognized components of bank Environmental Management Systems (EMS), from staffing, to standards, to monitoring.

Any good faith adoption of the Equator Principles will require banks to make substantial changes in their everyday practices

This section briefly describes each set of these recommendations. Due to the lack of disclosure obligations associated with the Principles, this assessment offers only preliminary and largely anecdotal analysis regarding Equator banks' fulfilment of 10 recommended implementation measures.

Initial environmental review and Performance Indicators

An Initial Environmental Review allows the bank to identify the environmental and social impact of their existing project finance portfolio and create appropriate environmental and social Performance Indicators for measuring and managing their environmental and social 'footprint'.

The Equator Principles do not require or even suggest that banks undertake this type of exercise; indeed, very few banks have created sustainability indicators for their financing portfolios. Two notable exceptions in the past year are Citigroup and Bank of America, who have pledged to track and reduce the carbon dioxide emissions from their energy and utilities/ power plant portfolios. Understanding the greenhouse gas emissions 'footprint' of energy-related portfolios is a practical first step to developing and tracking sustainability-related performance indicators for financing portfolios.

Policy development

Integrating the Equator Principles into formal bank policy is critical to 'mainstreaming' the EPs.

The EPs allow individual banks to implement the Principles in any manner they deem appropriate. Although it is difficult to assess how and whether all Equator banks have made necessary policy changes to accommodate their Equator commitments, preliminary analysis suggests that policy development has been uneven among endorsing banks. In general terms, it can be assumed that those banks with existing environmental and social policies governing core business areas, including project finance, are currently ahead of those that do not.

A few leadership companies have also developed particular sector standards to complement the Equator Principles. For example, Citigroup has developed a forests policy that it clearly views as an extension of its Equator commitment. However, there has been other evidence that the Equator Principles may be having a limiting effect. For example, ABN AMRO has been an industry leader in creating sector standards. But according to Dutch environmental organizations, in an attempt to create Equator-consistent standards, ABN AMRO has to some extent limited the project finance portion of its new oil and gas policy to those of the IFC.

Organizational structure and personnel
In order to ensure implementation of the EPs, appropriate personnel and accountability systems must be in place.

Banks that seriously adopt the EPs will make appropriate changes in personnel, job responsibilities, and organizational structure. For example, at Westpac, responsibility for EP implementation has been allocated to the Project & Structured Debt team as a whole, and a Director within the team has been charged with implementing and monitoring adherence to the EPs.While some banks may have integrated the EPs into bankers' existing job responsibilities, others have chosen to draw on internal social or environmental experts. Relatively few banks have budgeted for additional staff, although two exceptions include HSBC and Citigroup, who have committed to hire additional environmental/social staff in part to facilitate EP implementation.

Environmental procedures and standards for transactions
The EPs outline a relatively specific set of procedures that include screening, categorization, due diligence, appraisal, etc. that should be implemented into existing bank practices.

Several banks claim that even before endorsing the EPs, they applied World Bank standards to their transactions. But even for these banks, the EPs requires the extra step of applying particular procedures such as screening, categorization, etc. Clearly, such procedures must be integrated into routine bank practices for proper EP implementation. Some Equator banks are making appropriate changes to their existing procedures to accommodate the Equator commitments; for example, HSBC is updating their Group Standards Manual and Group Lending Guidelines to integrate the Principles across the institution. Standard Charter has created new EP-related policies and procedures that were approved by its Wholesale Bank Reputational Risk Committee and also its Wholesale Bank Risk Committee. Similarly, other banks such as Citigroup have formally amended its credit policy to accommodate their Equator commitments.

Documentation
Any management system that is subject to internal or external audits relies on a 'paper trail' of documentation to ensure that policies and procedures are followed. In addition, the Principles themselves reference particular documents, such as Environmental Impact Assessments (EIA), Environmental Management Plans (EMP) and loan covenants.

In the absence of full transparency around banks' implementation of the EPs, it is difficult to determine the overall quality of banks' performance in this area. A few banks have reportedly created new checklists or other documentation to accommodate the new levels of due diligence that must be conducted because of the EPs. There is also little evidence regarding whether banks are ensuring that client-provided documentation explicitly required by the EPs, such as EIAs or EMPs are of high quality.

In the case of the BTC pipeline, independent NGO analysis demonstrated that the EIA conducted by the client was inadequate, and banks apparently did not demand better assessments. As a matter of competitive advantage and client confidentiality, banks have not and are unlikely to share other EP environmental documentation – particularly loan covenants or monitoring reports. However, BankTrack strongly encourages the public disclosure of environmental and social documentation (on request), so that affected communities can have a better understanding of the project sponsors' various environmental and social obligations.

Internal information and training

Clearly, to implement the EPs a bank must create both an internal communications plan and a training program on the Principles. Most Equator banks publicly announced their endorsement of the Principles with an external press release. It is not known how each bank rolled out the Principles internally, and whether the announcements came from the highest levels. What is more distinguishable are Equator-related training programs. The International Finance Corporation has made training courses available to the Equator banks that vary in length and format. By May 2003, IFC trained an estimated 365 professionals at 13 Equator banks. While almost all of the early Equator signatories have attended at least one version of the IFC session, it is unclear whether banks have integrated Equator-related training into their regular and ongoing training courses, and whether banks have created mechanisms for measuring the effectiveness of such trainings over time.

Transparency and external reporting

The only way the public and the Equator banks themselves can fully assess the effectiveness of the Equator Principles is through regular external reporting by Equator signatories. In addition, NGOs point out that transparency must occur at the transaction-level as well.

The only way the public and the Equator banks themselves can fully assess the effectiveness of the Equator Principles is through regular external reporting by Equator signatories

The Equator Principles do not explicitly require banks to publicly and regularly report on their implementation of the EPs, although some kind of public reporting is tacitly encouraged. Rather, accountability for implementing the EPs is expected to occur through informal self-policing, where Equator banks, encountering each other in loan syndications, are able to compare notes with how peer banks may have categorized a project. Although some Equator endorsers have committed to regularly disclose general project finance volumes/ project categorizations, or include Equator-related reporting into their voluntary corporate social and environmental reports, such spotty reporting among the Equator group is not adequate. Relying on such a meagre system of accountability will damage the long-term credibility of the Principles.

In the absence of proactive disclosure from Equator banks, in 2004 BankTrack will send a simple questionnaire to endorsing banks and share responses with corporate social research firms, investors, and the public. This questionnaire will be consistent with the Global Reporting Initiative financial sector services supplement that is currently in development.

Consultation and consent
The Principles require public consultation for Category A projects, and public consultation and consent is of the utmost importance for affected communities.

There has not been enough evidence to date to measure whether the Equator Principles promotes better public consultation and leads to more just and sustainable outcomes for project-affected communities

There has not been enough evidence to date to measure whether the Equator Principles promotes better public consultation and leads to more just and sustainable outcomes for project-affected communities. At this point, BankTrack is not aware of any Equator banks who have yet developed formal mechanisms to ensure that clients conduct public consultations in a "structured and culturally appropriate way." If anything, some Equator banks seem opposed to best practice consultation methods, which would strive to achieve free, prior and informed consent, as can be concluded from recent lobby efforts of some Equator banks banks. (see below)

Auditing, monitoring and corrective action
The "teeth" of the Equator Principles lie in the bank's ability to covenant a client to environmental and social performance standards, and to consider a loan to be in default if those covenants are not met.

It is unknown whether any bank that has created formal mechanisms to address monitoring and corrective action on individual deals. It also may be too early, after only one year, to determine whether banks have taken appropriate corrective actions on deals that fail to comply with social/environmental commitments. However, a number of Equator banks reportedly requested that the BTC Consortium prepare an official report on allegations that BP hid known safety defects associated with the Baku-Tibilisi-Ceyhan pipeline, in an effort to secure export credit financing. BankTrack is not aware of whether that report revealed breaches of environmental and social covenants, and whether/how the banks may have used their leverage to demand changes or remediation.

Management review and improvement
Finally, banks which are serious about implementation will create specific mechanisms for internally auditing the overall implementation of EPs, and taking corrective action in cases of internal non-compliance.

Only banks that already have mainstreamed the EPs by creating formal changes to existing policies, procedures and standards can begin to address the issue of auditing, management review and improvement. Citigroup, which has a compliance-based organizational culture, now covers Equator Principles implementation in internal audits, although it is unclear whether the auditors have appropriate expertise in environmental and social issues. Other banks reportedly are integrating Equator Principles into their internal audit functions as well.

Conclusion; implementation inconsistent at best

In sum, preliminary analysis suggests that one year after the launch of the Equator Principles, levels of implementation at endorsing banks varies greatly. Presumably, banks that have existing environmental management systems, including environmental personnel, procedures and standards, will have a significant head start in implementation. Conversely, banks that are newcomers to the entire field of environmental credit risk may discover that they need to build systems from the bottom up.

In private conversations, some Equator banks admit that certain endorsers have taken implementation very seriously, while others are expected to only make minimal efforts. Some observers also maintained that certain banks, particularly the ones that were peer-pressured into endorsing the Principles "didn't know what they signed up for", and thus may lack the political will to implement the Principles at all. Hopefully those banks who were early endorsers or leaders of the initiative signed up with full knowledge and sincere intentions.

certain banks, particularly the ones that were peer-pressured into endorsing the Principles "didn't know what they signed up for"

In any case, lack of information undermines the ability of the public and of the endorsing banks to assess EP implementation and effectiveness. This lack of transparency and accountability may undermine the integrity of the Principles, even in the short term.

5. Eroding confidence

This report has outlined several phenomena that have resulted in weakened public confidence in the Principles, including the financing of controversial projects, problematic projects in the pipeline, and the lack of transparency in implementation. However, in the year since the Principles were launched, NGOs have observed other behaviours which in sum have created a significant amount of scepticism about the good faith of the Equator banks.

A lack of stakeholder engagement

Although individual banks have participated in public panels on the Equator Principles, the banks as a group seem unwilling to substantively engage with NGOs on the overall implementation and content of the Principles. In fact, the Equator banks have pointed out that there is little formality to the group, and their professed lack of cohesion has made it difficult for stakeholders to find an "entry point" to spark a group dialogue. While NGOs in the past year may have been critical of banks when they have financed deals that appeared to be non-Equator compliant, NGOs generally are eager to see them work.

The reluctance of the Equator banks to stakeholder engagement is perplexing

The reluctance of the Equator banks to stakeholder engagement is perplexing, in light of their willingness to seek NGO input during the drafting of the Principles, and BankTrack's repeated attempts to offer feedback and renew dialogue. Given the fact that some Equator banks have a track record of being very amenable to stakeholder dialogue, it can only be assumed that certain Equator banks are resistant to the idea.

In a different but similarly illustrative example, NGOs were contacted by the Harvard Business School to be interviewed for a case study on the Equator Principles. Because such case studies are used to stimulate discussion, they usually present a balanced view of a complex issue, often highlighting decisions and trade-offs. After interviewing several NGOs and Equator banks, the Harvard researchers dropped their case study, citing banks' right of last refusal. Although Harvard case studies typically are produced with meticulous attention towards fact-checking and objectivity, one or more of the Equator banks disagreed with the researchers' characterization or analysis of the Principles and its genesis. It can only be assumed that the vetoing bank(s) opposed the perspectives and critiques offered by the NGOs who were interviewed for the case study.

Unfortunately, the lack of willingness to entertain feedback or third-party analysis has fostered the impression that the Equator banks as a group do not value stakeholder engagement/perspectives. While this stonewalling may be simply insensitive or ill-advised from a Northern NGO point of view, it causes serious concern from the perspective of affected communities. The banks' unwillingness to listen to other voices raises doubts about whether they are ensuring that in transactions, affected communities are provided with adequate public consultation, an important component of the Equator commitment.

Becoming lobbyists – for the wrong agenda

Although the Collevecchio Declaration specifically recognizes the important role financial institutions can play in public policy activities, naturally these efforts only advance sustainability if banks advocate for policies that benefit communities, workers, the poor and the environment.

In April 2004, eleven Equator Banks played an unfortunate role in undermining sustainability when they wrote to World Bank Group (WBG) President James Wolfensohn, urging him to reject some of the key recommendations of the Extractive Industries Review.[59]

The banks maintained that the "EIR has not given sufficient consideration to the fact that the extractive industries are essential to global economic growth and poverty reduction" – even though the entire purpose of the EIR was to determine how and under what conditions limited World Bank extractive investments could benefit the poor. In particular, the banks opposed the EIR recommendation that countries have robust governance criteria in place before WBG investment. They also expressed concern about EIR recommendations that project sponsors seek 'Free Prior Informed Consent' from communities to be affected by their projects, and stated the view that the current WBG Safeguard Policies already provide effective consultation with affected groups and tangible benefits for local communities.

The undersigning banks left no doubt that they consider themselves major or even preferential stakeholders in policy changes at the World Bank Group, a public institution owned by governments with a core mission to alleviate poverty: "We consider ourselves to be important stakeholders of the World Bank Group (WBG) by virtue of our adoption of the WBG safeguard policies and sectoral standards through the adoption of the Equator principles and through our role as co-financiers with the WBG of projects in the extractive industries and other sectors... should implementation of any EIR recommendations or other considerations require changes in the safeguard policies or sector guidelines, we expect that the banks that have adopted the Equator Principles .. will be fully consulted in this process".

The letter, with its obstructionist goal, dealt a significant blow to the integrity of the Principles in the eyes of NGOs

This letter marked a change in the Equator banks' mode of operating: until then the Equator banks had characterized themselves as a loose assembly, but by organizing themselves as a lobby group they clearly signalled not only a new level of coordination, but also a new of set activities around lobbying. The letter, with its obstructionist goal, dealt a significant blow to the integrity of the Principles in the eyes of NGOs. When a draft of the letter was leaked, BankTrack members expressed shock and outrage that the Equator banks would block rather than promote the adoption of more stringent environmental and social standards at the World Bank. It also caused alarm that the Equator banks might try to roll back a broader set of policies at the World Bank that are currently up for review.

The IFC Safeguard Policy Review

In 2002, when major banks first started contemplating the adoption of a common set of social and environmental policies, they considered several different options before settling on the IFC Safeguard Policies and sector guidelines as the best option.

EP banks might be willing to comply with a common set of policies, but not ready to follow all practices associated with a good faith implementation of such policies

But even their choice of IFC guidelines was somewhat selective, as the banks refrained from adopting the IFC's Categorical Prohibitions, its information disclosure policy, and avoided setting up an IFC-type independent compliance/ombudsman mechanism to allow for external scrutiny of the application of the principles. This was an early signal that the EP banks might be willing to comply with a common set of policies, but not ready to follow all practices associated with a good faith implementation of such policies.

Furthermore, the IFC has recently begun a series of policy reviews that will redefine a set of social and environmental policies for the institution. The question remains as to how the private banks will react to these reviews. During Principles' drafting phase, in January 2003, the IFC Compliance Advisor Ombudsman (CAO) presented her review of IFC's Safeguard policies, intended to be the starting point of a major overhaul of these policies.[60]

While praising IFC for having adopted the Safeguard policies in 1998, the report turned out to be very critical of the way the policies were formulated, the deficiencies in their scope, and the manner in which they were implemented in everyday business at IFC. The report provides stunning examples of projects where the project sponsor was not committed to the policies, or actively tried to avoid having to apply them. It also reports that a relatively large percentage of projects were wrongly categorised by IFC staff as 'B' (medium-impact) or even 'C' (low-impact), when an 'A' (high-impact) status should have been required, thus avoiding the need for conducting extensive environmental impact assessments and the development of environmental management plans.[61]

The report also makes several specific recommendations to improve the IFC's environmental and social safeguard system. Among other things, it promotes greater transparency as a means to "creating accountability among sponsors and IFC for upholding their commitments and for supporting better safeguard policy outcomes." It also recommends two issues for IFC to focus on; "the extent to which business confidentiality poses a legitimate constraint on information disclosure, and to what extent IFC's disclosure policy conforms to international norms."

Full review ahead

Since the publication of the Review and the Management Response to the Review, IFC has embarked on a comprehensive review of its Safeguard policies, as part of an even greater set of policy reviews, which include[62]:

- The Revision of IFCs Policy on Disclosure of Information, technically not part of the Safeguard polices –and not adopted by the Equator Banks- but a necessary prerequisite for them to be effective.

- The revision of the Operational Procedures, which guide the application of policies in a specific project environment.

- The revision of the Environmental, Health and Safety Guidelines as captured in the World Bank Pollution Prevention and Abatement Handbook (PPAH) and the Environmental Standards of IFC. This is a widely used reference book, specifying the level of emissions and discharges considered acceptable for a broad range of industries. The Equator Principles make explicit reference to these standards.

- A reassessment of the sustainability approach for Financial Intermediaries (FIs). The fact that IFC support for FIs is not subject to the safeguard policies is now recognised as a major shortcoming. If the review process leads to them being incorporated in the overall policy approach of IFC, this may have an effect on projects sponsored by Equator banks through FIs as well.

All these revisions are aimed at mainstreaming environmental and social considerations in all IFC operations, under the so-called Sustainability Initiative.

A separate, but closely related, process that will have a major impact on IFC policies is the aforementioned Extractive Industries Review (EIR). The final report of the EIR contains several far reaching recommendations, including issues that so far are have not been integrated into the Safeguard policies. Examples include granting the right of Free, Prior Informed Consent to communities potentially affected by projects, reference to human rights, several categorical exclusions (oil and coal extraction), and criteria for no-go zones and no-go technologies.[63]

The big question is whether the private sector, more specifically the private banks that adopted the EPs, will be allowed to determine the outcome and limitations of the revision process or not. Will they sit back and let this process unfold, unconditionally applying whatever the outcome may be? Certainly not. As the 11 banks' lobby effort on the EIR proved, there is too much at stake.

The big question is whether the private sector, more specifically the private banks that adopted the EPs, will be allowed to determine the outcome and limitations of the revision process or not

For IFC, the dilemma is clear. Immensely proud of having the EP banks embrace their Safeguard Policies –Peter Woicke, Managing Director of IFC recently called this 'our biggest achievement'[64]- the IFC cannot risk alienating such a powerful group by adopting policies that are far more stringent than what is currently at the table. But to be seen as giving the Equator Banks a preferential or even decisive say in the actual drafting process would completely ruin the legitimacy of the policies in the eyes of those whose interests and rights they are supposed to protect. Which interests prevail, remains to be seen.

6. Strengthening the Equator Principles

From the outset, NGOs have identified the Principles' major shortcomings, and urged Equator banks to improve and remedy them. For example, NGOs welcomed the fact that the Equator Principles focus on procedures to screen and categorise potential deals -- steps that are recommended in the Collevecchio Declaration – but also encouraged banks to go beyond the EPs by adopting "no-go areas" (certain geographical areas or types of activities that endorsing banks would avoid) or categorical prohibitions. Also, NGOs encouraged the banks to apply the Principles to smaller deals and non-project finance transactions -- such as corporate lending and bond underwriting -- where use of proceeds is known. It should be noted that although a few individual banks have chosen to apply the Equator Principles more broadly, this is not a common practice.

But perhaps most of all, NGOs have pointed to the need for transparency and accountability, the absence of which constitutes a potentially "fatal flaw" of the Principles. Without far more transparency on implementation processes and disclosure on bank performance, the NGO community and the banks themselves will be unable to assess whether the Principles are being implemented, and what contribution they may be making to advance sustainability.

6.1. An Independent Accountability Mechanism

the Equator Banks must agree to some mechanism to ensure compliance and to ensure that project-affected communities are provided the protections embodied in the Equator Principles

As mentioned, for the Equator Principles to be more than a set of voluntary aspirations, the Equator Banks must agree to some mechanism to ensure compliance and to ensure that project-affected communities are provided the protections embodied in the Equator Principles. In particular, the Equator Banks need to provide an independent, transparent and effective process for project-affected people to raise their concerns to top-level decision makers who have not been directly involved with financing decisions or loan preparation.

Such accountability mechanisms now exist at the World Bank Group, including IFC and the Multilateral Investment Guarantee Agency (MIGA), the European, Asian and InterAmerican regional development banks and export credit agencies in Japan and Canada.

Although each of the mechanisms vary to some extent, at a minimum every one of them is designed to ensure compliance with the institution's environmental and social policies and procedures. Every one of these mechanisms also gives direct access to project-affected communities to raise their unfiltered concerns about the project to the highest levels of management in these institutions. In some cases (for example, the IFC/MIGA's Compliance Advisor and Ombudsman) these mechanisms go beyond compliance to use the leverage of the financial institution to assist project-affected communities in resolving problems arising from the project. These mechanisms have also become the source of independent and valued advice regarding the environmental and social policies and practices of their respective institutions.

Basic principles of an accountability mechanism

In keeping with the experience at other institutions, any accountability mechanism for the Equator Banks must meet the following principles:

- The process must be **independent** of Bank operations, loan preparation and project finance decisions;
- The process must be **transparent** and allow for the public release of compliance reports and other findings of the mechanism;
- The process must at a minimum be **accessible** to project-affected communities and their representatives;
- The process has the resources and authority to be **fair, objective and effective** in reviewing project compliance and in responding to the concerns of the public.

Functions of an accountability mechanism

An accountability mechanism for the Equator Banks could fill several functions:

- **Compliance and accountability.** First and foremost, the accountability mechanism would review the bank's and borrower's project-specific compliance with the Equator Principles, applicable legal standards and any other environmental or social policy of the lending institution. The mechanism would report publicly and to the claimant on the results of their compliance review and make any appropriate recommendations. By providing an independent and objective means for ensuring compliance with the Equator Principles, the Equator Banks would demonstrate that they are serious about meeting the Principles at the project level. Such a compliance function would audit a transaction and not a bank's general implementation of the EPs.
- **Ombudsman.** The accountability mechanism could also provide a window for project-affected people to raise concerns with the impacts of specific bank-financed projects, even where there may not be any issues of policy compliance. The mechanism could provide affected communities with information about the Principles and what protections they receive under them. The Equator Banks could also use their leverage with project sponsors to ensure that there are effective and fair dispute resolution processes available to project-affected communities.
- **Continuous improvement.** Because the accountability mechanism will have substantial on-the-ground experience, it will be a source of important and objective advice regarding the Equator Principles and their implementation.

The mechanism, through banks' annual Equator implementation reports and otherwise, could promote best practice among the Equator Banks, derived both from the lessons it has learned through the compliance function and developments at individual Equator Banks and other financial institutions. In this way, the accountability mechanism would ensure the progressive evolution of the Equator Principles over time.

Structure of the accountability mechanism.
The Equator Banks could take one of several approaches to developing an accountability mechanism. Each is discussed briefly below.

- **Individual accountability mechanisms.** The Equator Principles could be amended to require that any signatory agree to create an independent, transparent and effective mechanism for project-affected people to raise concerns over compliance. Such a requirement would then lead each bank to create separate compliance review offices and separate procedures for receiving external complaints.

- **Joint independent accountability mechanism.** The Equator Banks could agree to establish a joint accountability mechanism, independent of any one of the Banks. This joint mechanism could be funded collectively through a revolving fund paid in according to a formula reflecting each Equator Banks' size. Having only one mechanism would reduce confusion and be more easily understood by project-affected people. A joint mechanism would also be less costly, promote consistent application of the Equator Principles and be perceived as more independent and objective than mechanisms beholden to one specific Bank.

- **Acceding to existing mechanisms or processes.** The Equator Banks could also explore using other existing mechanisms to received and evaluate claims from project-affected people. For example, each of the Equator Banks could accede to the jurisdiction of the Permanent Court of Arbitration (PCA) for the purposes of any claim from project-affected people regarding implementation of the Equator Principles or other environmental and social standards. The PCA offers a forum for resolving international disputes, typically involving governments or companies. The PCA can use flexible approaches and apply standards that are agreed in the beginning by both parties.

Any of these structures could be developed to work effectively. Indeed, all of the Equator Banks do not have to decide to meet their responsibility for compliance monitoring and accountability the same way. The key is to design a process that meets the core principles of independence, transparency, accountability, effectiveness, and fairness outlined above.

7. Now move on

One year after the launch of the Equator Principles, it is still difficult to measure how the Principles are being implemented by endorsing banks, and whether they are making a difference to the environment and communities. The promise of the Equator Principles – that clients will ultimately design and implement more environmentally and socially benign projects, spurring more sustainable development – still holds some hope, although the past year has not yielded proof that this is yet occurring.

On the other hand, by observing particular transactions financed or under consideration by Equator banks, especially the Baku-Tbilisi-Ceyhan pipeline, there appear to be early problems with implementation: not only in banks' decisions to approve the project, but also their apparent lack of corrective action. Attempts to analyse EP implementation from an institutional perspective (e.g. changes that individual banks have made in their daily operations) reveal that implementation among various banks is inconsistent, and that lack of transparency undermines the ability of the public to evaluate the EPs' overall effectiveness. These sobering observations, combined with Equator banks' reluctance for stakeholder engagement and its obstructionist lobby efforts, have eroded public confidence in the Principles.

The public interest community has not yet lost hope in the Equator Principles and their potential for advancing sustainability both within the financial services sector and on the ground. But NGO support for the Equator Principles is often not demonstrated by urging more banks to sign up, having infinite patience or providing unqualified praise. Instead, networks like BankTrack seek to support the EPs by promoting their integrity, credibility and effectiveness through monitoring, analysis and recommendations for improvement.

The public interest community has not yet lost hope in the Equator Principles and their potential for advancing sustainability both within the financial services sector and on the ground

Institutional courage required
In that spirit, BankTrack urges Equator banks to take the following high-level action in order to remedy implementation problems and restore a sense of good faith:

- *The Proof is in the Portfolio.* Equator banks must exclude projects which fail to meet their environmental and social standards –such as those mentioned in this report-, and actively seek corrective measures when project sponsors fail to comply with such standards and commitments. In particular, banks need to actively conduct their own social and environmental due diligence, and not rely on the IFC or other public institutions.

- *Promote Good Practice and Transparency.* In order to preserve public confidence in the EPs, the leaders of the initiative should shift their focus away from recruiting new signatories, and instead concentrate on assisting endorsers with implementation and promoting regular public reporting. Individual banks will have their own approaches towards 'mainstreaming' the EPs, but any serious adoption of the EPs will at least encompass the ten areas of implementation referenced in this paper. On a project level, banks should make environmental documentation, such as loan covenants, environmental management plans and monitoring reports available to the public.

- *Promote Accountability.* Promises are not enough. From the early stages of the Principles' development, the lack of accountability has been identified as a potentially fatal flaw; it is high time the Equator banks address this critical issue before it damages the overall credibility of the Principles. EP banks should therefore install an accountability system such as the Independent Accountability Mechanism described in this report.

- *Support Stakeholder Engagement.* Adopting a more collaborative and open approach towards stakeholder dialogue would increase public confidence in the Principles, and demonstrate that endorsing banks are willing to work with others in improving the effectiveness of the EPs.

- *Champion Continuous Improvement.* Banks should refrain from the sort of lobbying efforts as conducted by several Equator Banks on the Extractive Industries Review, which calls into question the good faith of endorsing banks. Instead, they should play a proactive role in further supporting improvements to international environmental and social policies and standards.

Appendix 1 The Equator Principles

The "Equator Principles"

An industry approach for financial institutions in determining, assessing and managing environmental & social risk in project financing

PREAMBLE

Project financing plays an important role in financing development throughout the world. In providing financing, particularly in emerging markets, project financiers often encounter environmental and social policy issues. We recognize that our role as financiers affords us significant opportunities to promote responsible environmental stewardship and socially responsible development.

In adopting these principles, we seek to ensure that the projects we finance are developed in a manner that is socially responsible and reflect sound environmental management practices.

We believe that adoption of and adherence to these principles offers significant benefits to ourselves, our customers and other stakeholders. These principles will foster our ability to document and manage our risk exposures to environmental and social matters associated with the projects we finance, thereby allowing us to engage proactively with our stakeholders on environmental and social policy issues. Adherence to these principles will allow us to work with our customers in their management of environmental and social policy issues relating to their investments in the emerging markets.

These principles are intended to serve as a common baseline and framework for the implementation of our individual, internal environmental and social procedures and standards for our project financing activities across all industry sectors globally.

In adopting these principles, we undertake to review carefully all proposals for which our customers request project financing. We will not provide loans directly to projects where the borrower will not or is unable to comply with our environmental and social policies and processes.

STATEMENT OF PRINCIPLES

We will only provide loans directly to projects in the following circumstances:

1. We have categorised the risk of a project in accordance with internal guidelines based upon the environmental and social screening criteria of the IFC as described in the attachment to these Principles.

2. For all Category A and Category B projects, the borrower has

completed an Environmental Assessment (EA), the preparation of which is consistent with the outcome of our categorisation process and addresses to our satisfaction key environmental and social issues identified during the categorisation process.

3. In the context of the business of the project, as applicable, the EA report has addressed:

a) assessment of the baseline environmental and social conditions
b) requirements under host country laws and regulations, applicable international treaties and agreements
c) sustainable development and use of renewable natural resources
d) protection of human health, cultural properties, and biodiversity, including endangered species and sensitive ecosystems
e) use of dangerous substances
f) major hazards
g) occupational health and safety
h) fire prevention and life safety
i) socioeconomic impacts
j) land acquisition and land use
k) involuntary resettlement
l) impacts on indigenous peoples and communities
m) cumulative impacts of existing projects, the proposed project, and anticipated future projects
n) participation of affected parties in the design, review and implementation of the project
o) consideration of feasible environmentally and socially preferable alternatives
p) efficient production, delivery and use of energy
q) pollution prevention and waste minimization, pollution controls (liquid effluents and air emissions) and solid and chemical waste management

Note: In each case, the EA will have addressed compliance with applicable host country laws, regulations and permits required by the project. Also, reference will have been made to the minimum standards applicable under the World Bank and IFC Pollution Prevention and Abatement Guidelines and, for projects located in low and middle income countries as defined by the World Bank Development Indicators Database, the EA will have further taken into account the then applicable IFC Safeguard Policies. In each case, the EA will have addressed, to our satisfaction, the project's overall compliance with (or justified deviations from) the respective above-referenced Guidelines and Safeguard Policies.

4. For all Category A projects, and as considered appropriate for Category B projects, the borrower or third party expert has prepared an Environmental Management Plan (EMP) which draws on the conclusions of the EA. The EMP has addressed mitigation, action plans, monitoring, management of risk and schedules.

5. For all Category A projects and, as considered appropriate for Category B projects, we are satisfied that the borrower or third party expert has consulted, in a structured and culturally appropriate way, with project affected groups, including indigenous

peoples and local NGOs. The EA, or a summary thereof, has been made available to the public for a reasonable minimum period in local language and in a culturally appropriate manner. The EA and the EMP will take account of such consultations, and for Category A Projects, will be subject to independent expert review.

6. The borrower has covenanted to:

a) comply with the EMP in the construction and operation of the project

b) provide regular reports, prepared by in-house staff or third party experts, on compliance with the EMP and

c) where applicable, decommission the facilities in accordance with an agreed Decommissioning Plan.

7. As necessary, lenders have appointed an independent environmental expert to provide additional monitoring and reporting services.

8. In circumstances where a borrower is not in compliance with its environmental and social covenants, such that any debt financing would be in default, we will engage the borrower in its efforts to seek solutions to bring it back into compliance with its covenants.

9. These principles apply to projects with a total capital cost of $50 million or more.

The adopting institutions view these principles as a framework for developing individual, internal practices and policies. As with all internal policies, these principles do not create any rights in, or liability to, any person, public or private. Banks are adopting and implementing these principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank.

Appendix 2 Signatories to the Equator Principles

As of June 4th 2004, the following financial institutions have signed on to the Equator Principles

Australia	Westpac Banking Corporation
Belgium	Dexia Group KBC Bank N.V.
Brazil	Unibanco
Canada	Canadian Imperial Bank of Commerce Royal Bank of Canada
France	Calyon Corporate and Investment Bank
Denmark	Eksport Kredit Fonden (Export Credit Agency)
Germany	Dresdner Bank AG HVB Group WestLB AG
Italy	MCC S.p.A.
Japan	Mizuho Corporate Bank, Ltd.
The Netherlands	ABN AMRO Bank NV ING Group Rabobank Group
Spain	BBVA S.A.
Switzerland	Credit Suisse First Boston
United Kingdom	Barclays plc HSBC Group Standard Chartered Bank The Royal Bank of Scotland
United States	Bank of America, N.A. Citigroup Inc.
European Union	European Investment Bank

Notes

[1] To illustrate; over the course of the 1990s, capital investment from public sources stayed relatively static at $50 - $60 billion per year, while private financial flows for development projects in the resource-rich Global South increased more than 700 percent in that same time period, skyrocketing from $30 billion to $210 billion annually.

[2] See banktrack.org/publications. These same NGOs later founded BankTrack.

[3] See www.banktrack.org/publications

[4] See www.equator-principles.com

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