Social accountability and the finance sector: the case of Equator Principles (EP) institutionalisation
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Citation for published version (APA):

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“While robust policies are important, our organisations measure the effectiveness of the EPs by how they are applied to projects and day-to-day operations, including whether the lives of project affected communities are improved as a result.” (BankTrack, 2006a, p.3)

“You go into any Equator bank and everyone will be different because they’ve each got different structures and different litigation authorities and different all sorts of things.” (Dutch EPFI 1, Interviewee 1)

9.1 Introduction

While it is beyond the scope of this PhD to investigate the impacts of the EP at grassroots level amongst project affected communities, a more in-depth examination of the implications of the EP for daily project finance activities can be undertaken. As previous chapters have focused on the institutionalisation of the EP at broad societal, organisational field and organisational levels, the aim of this chapter is to provide a more detailed insight into the institutionalisation of the EP at intra-organisational level i.e. within the actual project financing process, as led by front office/project financers in consultation with (E&S) risk managers. The objective is to evidence the EP as a fully “accepted” or institutionalised facet of the project financing process for EPFIs. In doing so, this analysis also attempts to extend the Dillard et al. framework to intra-organisational level, and to reveal how the interplay between EP criteria and practice at this level affects, and is affected by, EP institutionalisation at organisational, organisational field and societal-project levels.

The chapter is structured around the various stages of a project financing process and how EP criteria are being incorporated into this in practice. This is undertaken while being mindful of the fact that project finance deals are complex and “non-linear” in nature and influenced by a myriad of factors, for example, their type, size and location. In addition, as commercial banks can be structured differently,85 their approach to project financing can also differ. Hence, any attempt to “generalise” the project finance process is quite difficult,

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85 This can influence where project finance is positioned in a bank, e.g. whether it is a department in itself, whether it is part of a “Structured Finance” department or whether it is incorporated into different business lines e.g. investment banking activities and managed by specific sector teams (e.g. mining and metals).
making any generalised study of EP implementation within EPFIs equally difficult. However, an attempt is made here to capture a certain generic pattern to project financing that emerged from interviewee material. While the specific execution of project finance deals, and the application of the EP therein, may not always follow the exact pattern outlined in this chapter, the approach taken here may not be “inaccurate” in itself, as one EPFI interviewee commented:

“You are trying to describe a very loose process that can vary widely from deal to deal depending on the FI, sponsor, project location and project technicalities, in a very precise way. A lot of the ratios, structuring, who is involved etc. depends on not only which FI but also which individuals are involved! There’s not a set process and a set way of doing things, I know you think it will be very well set out and organised but even different individuals do things slightly differently…I mean the end product is obviously generally quite similar but there’s just different ways of going through it and different relationships and who drives the process, things like that…It is all case and institutional-specific. So I wouldn’t be too concerned if you’re a little bit vague in areas because there probably isn’t a more precise answer…and being vague wouldn’t actually be inaccurate.” (UK EPFI 1, Interviewee 2, emphasis added)

This chapter enlists the perspectives of not only EPFI interviewees, but also that of an EP consultant, EP lawyer and two EPFI clients from the mining industry, to critically discuss this EP-project financing process. In doing so, it emphasises how EP practice at intra-organisational level is highly case-specific and dependent on human agency, irrespective of any existing EP criteria (e.g. policies, guidelines, manuals) at organisational or organisational field levels.

9.2 The “Green Light”/Marketing Stage

It is often the “relationship managers” (i.e. those with a direct relationship with clients), involved in project financing within commercial banks that learn of a potential project/installation through clients and/or the project finance market. If interested in the project, small FIs may become the financial advisor for the project while large FIs, especially those heavily involved in the project finance market, normally prefer to become lead arrangers. In some cases these large banks may seek to become the financial advisor for the project with the view to eventually becoming the lead arranger at a later stage (UK EPFI 1, Interviewee 2).

86 The terms “client”, “project sponsor” and “borrower” will be used interchangeably in this chapter.
When considering becoming a financial advisor and/or as part of their initial role as advisor, FIs may undertake a “preliminary check” of the client and proposed project in order to assess the potential risks, including E&S risks, of involvement:

“We have to commercially and reputationally decide do we want to be associated with a project. So we have to go through background checks. You’ve got to know who the company is you’re dealing with, what their background is, how they’ve acquired the operation. This is a stage we would also do environmental checks as well. We wouldn’t go into a huge amount of detail ... it’s not a kind of formal due diligence, it’s more a preliminary check...Because obviously you don’t want it to come out that they’ve [project sponsors] been associated with something that was unsavoury or you know...previously polluted a river and things like that. Obviously as I said, there’s not actually a risk that we’re going to lose money because we’re only advising them but it’s more of a reputational thing, which ties in with the environmental side.” (UK EPFI 1, Interviewee 2)

The extension of the EP to project finance advisory services, as opposed to just direct financing, was one of the new requirements of EP II introduced in 2006. This means that the potential E&S risks associated with the project and host country etc., as well as specific EP requirements, should be discussed and/or incorporated into the ‘information memorandum’87 prepared by the advisor for project sponsors at this stage. Hence, the significance of E&S issues, and the associated threat of reputational risks, appears to “legitimise” their consideration by financiers in the early evaluation stages of a project. This also influences subsequent stages of project financing practice at intra-organisational level as the following sections will illustrate.

9.3 The Due Diligence Stage (Equator Principles 1, 2 & 3)

If a bank becomes a financial advisor and/or “mandated” lead arranger,88 project finance staff may consult with the E&S risk management personnel, during this “due diligence” phase of the project to, as requested in Equator Principle 1:

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87 The information memorandum includes “a detailed summary of project technical and economic feasibility; the proposed financing structure and proposed terms; a description of the experience of participants; a summary of the underlying project risks; and a description of each of the project contracts and credit support” (Hoffman, 2008, p.74).

88 A bank may be referred to as a “mandated” lead arranger until such time as full due diligence has been completed and credit risk approval has been granted, then allowing the bank to be the “lead arranger” for the project.
1) Categorise the project as A (high risk), B (minimal risk) or C (low risk), in accordance with International Finance Corporation (IFC) E&S screening criteria (Appendix 4/Exhibit I); and

2) Provide advice on the types of E&S impacts and risks potentially associated with the project (in reference to Appendix 4/Exhibit II and/or IFC Performance Standards and EHS Guidelines\(^{89}\)).

The level of consultation between project financiers and E&S risk managers can depend on a number of factors. These include: the type of project, the severity of its E&S risks, the client’s experience with E&S issues and the autonomy of the project financiers to review the project. In addition, EPFIs’ integration of EP requirements into credit and/or E&S risk policies, lending guidelines/manuals, as well as staff training, have assisted project financiers to take more responsibility when dealing with E&S issues in project financing.

“...Well for each transaction, first there is a check on whether the principles apply. If they apply, what is the initial categorisation, is it an A, B or C? If it’s the C, you [Front office/project financier] only need to inform risk management on the deal statistics also to be able to report on it, but the assessment you can do yourself. Then we have a scheme regarding how you can check the different principles. If it’s any project in a high income OECD country, it’s the same, so the front office [project finance] can just do the due diligence. If it’s an A or a B, not in a high income OECD country, then it requires our [Sustainability Risk] involvement. For A’s, and also for B’s, that usually happens in an early stage to just get the initial go ahead, and also to discuss how we are going to tackle all the risks involved in this project to eventually get it done.” (Dutch EPFI 2)

EPFI interviewees claimed that the earlier the EP are applied, through their project financiers/relationship managers’ contact with clients, the better. As one interviewee outlines below, this is beneficial for both bank and borrower alike, especially regarding the potential credit risks associated with the E&S impacts of the proposed project.

“...These front office bankers [project financiers] are driven by making deals and they want to satisfy their clients’ demands and be able to sign off on deals and get them implemented. They have learned very quickly over the years that it is easier for them to get to the final sign off internally as well as with a client if they have things arranged from early on. It was a learning curve in the sense that they came to us [E&S Risk Managers] at the beginning as part of the [credit] risk process, which was too late. And we always communicate that the earlier they come the

\(^{89}\) Are technical guidance documents providing general and industry specific information on environmental, health and safety (EHS) issues and examples of good international industry practice (GIIP) (IFC 2008; EP II, 2006, p. 9).
better it is … If you have to change things on a project [early on], then quite often the smaller capital outlay upfront [to do that], and I speak now in the hundreds or thousands or few million dollars for a large project, can make a huge difference as opposed to trying to rectify things technically further down the track, which can easily go into tens of millions of dollars.” (Dutch EPFI 1, Interviewee 4)

During this “due diligence” stage, the financial advisor/mandated lead arranger requests the project sponsor of all Category A and B projects to produce a feasibility study. The feasibility study entails a detailed overview of the proposed project (including technical/engineering and financial projections) and should also include details of the potential E&S impacts and risks associated with the project. The inclusion of such E&S data in the feasibility study is normally informed by the parallel production of a more detailed environmental and social impact assessment (ESIA) of the project (as stipulated by Equator Principle 2; see below).

Yet as one interviewee explained, some agency issues may arise during this due diligence phase. This could be regarding for example, individual relationship managers’ awareness and understanding of the EP and willingness to inform their prospective clients of what might be required of them:

“I found it always that the debate internally is harder than the debate externally. The debate between a relationship banker and the internal risk management function to get a relationship banker to put things to a client is harder than speaking to the client. Relationship bankers are very protective and very concerned with their clients and sometimes they act a bit like over-concerned parents, being over-protective of their children, whereas actually things are not that difficult always. I found in the meetings I had with clients in the [mining] sector, and that was CFOs and CEOs as well as environmental practitioners on the ground in Australia, they were quite open to these discussions, and they were also very much aware of the standards.” (Dutch EPFI 1, Interviewee 4)

From a clients’ perspective, the reluctance to inform them about the need to apply the EP can also pose problems. For example, the South African mining company interviewee outlined how the local branch of a leading UK EPFI (and one of the EPFI interviewees in this research), was not forthcoming about EP requirements in their initial negotiations about a project finance loan:
“They didn’t [inform them about the EP initially]. It’s always who you deal with, you know. It’s the individual that you deal with normally. It was one of their [UK EPFI] mining project finance guys here in South Africa [and] no, he wasn’t upfront about it.” (South African Platinum Mining Company, emphasis added)

This section highlights how the varying “significance” of the EP criteria to different EPFI actors, and their interpretation of them, may have an impact upon the level of EP practice within a particular EPFI. It also provides some insight into the ongoing need to “legitimate” the integration of the EP into daily project finance activities amongst some more “challenging” staff, as well as the relative “dominance” or persuasive power of the E&S risk/EP managers to enforce this. Similar agency factors will be a reoccurring theme throughout the following sections.

9.3a “The Assessment” (Equator Principle 2) and Applicable Social and Environmental Standards (Equator Principle 3)

For all Category A and B projects, Equator Principle 2 requires the borrower to produce an ESIA, or “the Assessment” as referred to in the Principles. The objective of the Assessment is to identify the relevant E&S impacts and risks of proposed projects and to recommend mitigation and management measures to address these (Equator Principles II, 2006). The ESIA firstly, highlights the applicable E&S standards or host country laws that the client has to abide by, dependent on whether the project is in a non-high income OECD country or not. Equator Principle 3 states that if the project is located in a non-High Income OECD country90 the borrower is obligated to meet all relevant IFC Performance Standards and Industry Specific EHS Guidelines. However, in High Income OECD countries, relevant E&S laws and standards are deemed to meet or exceed these Performance Standards and Guidelines, and the borrower is to produce an ESIA that meets relevant host country E&S laws, regulations and permits (Equator Principles II, 2006). Secondly, the ESIA forms the basis for the Action Plans (AP) and Management Systems (Equator Principle 4), that borrowers are covenanted to produce should financial approval for the project be granted later (see sections 9.4 and 9.7 below).

The completion of an ESIA is the sole responsibility of the borrower and normally undertaken by specialist consultants hired by them. The project financiers review the ESIA

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90 As designated by the World Bank Development Indicators Database.
and feasibility study as part of their overall due diligence of the project. In doing so they may consult with the E&S risk managers about the E&S details of the studies. In addition, independent consultants/experts, often referred to as the Independent Technical Engineers (ITE), are normally employed by the FIs to review both the technical aspects of the project as well as the borrowers’ ESIA and feasibility study. This acts as a “third party” audit of the project. In certain cases where the social impact of a project is very high for example, if a resettlement programme has been proposed, then a separate consultant with more specific social expertise may also be employed to evaluate the project (UK EPFI 1, Interviewee 2) (see also section 9.7a-9.7c).

“Oh we don’t do any technical consultancy ourselves because we’re not really qualified to do that… but we do talk to our clients about the risks. And if the risks are high enough then we’ll commission some consultants who are experts in that area to go and do an initial study really, that’s the way it works.” (UK EPFI 2)

“The first line of responsibility is each transactor on a particular project but we need to make sure they’re following the correct process. They often come through to me directly at that stage and then if they’ve got the social and environmental management assessment from the client or from the independent consultant - they often you know, ask me just to review and check whether that complies with Equator Principles standards.” (South African EPFI)

Within the bank, there may be a number of different departments/personnel involved in what is known as a “Deal Team” which assist in the management of the project from this due diligence stage onwards. Ultimately, however, it is the project financiers that manage the deal moving forward should final credit approval be granted for the project (UK EPFI 1, Interviewee 2).

This section introduces how EP practice at intra-organisational level affects and is affected by EP criteria and practice at organisational field level, through interaction with EP clients and consultants; as well as broader societal/project level through the E&S impacts associated with project finance. Such dynamics are continuous throughout the entire project financing process as will be illustrated in the following sections.

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91 For example a deal team could be made up of: senior and junior project financiers/relationship managers; internal and external legal advisors; credit risk department representatives and commodity traders.
9.4 Credit Risk Approval

Following the due diligence phase the project financiers will make a decision, based upon the acceptability of the client’s feasibility study, to submit a formal application to the Credit Risk Department, or special Credit Review Committees, for approval to bid to become the lead arranger, for the project.

“[The approval committee is made up of] The Risk Department, the front office and [representatives] from the Executive Board [but] the final decision lies with Risk.” (Dutch EPFI 2)

A review of E&S risks is integrated into the main credit risk approval process of a project. One interviewee outlined how irrespective of project/loan size and location, that, in his organisation, the E&S risk review would in all cases have to be done in consultation with their Environmental Risk Department at Head Office. However, the majority of interviewees mentioned that it was Category A (and in some cases Category B) projects, that would require consultation with E&S risk managers and final sign off by Credit Risk (Committees), at Head Office.

“I get involved in signing off the transactions that have the highest risks, and generally we try to make sure that the lower risks are signed off at a local level…[but] we do give guidance on what can be signed off at a local level…So if it’s a Category A it would have to come here [Sustainability Risk Management at Head Office] for sign-off because we’d want to make sure that was being done correctly. I also have a sort of network of what we call Sustainability Risk Managers around the world, so we’ve got about 25/26, based in different countries. And these are fantastic in helping us to manage the issues because we feel that we can’t and don’t want to manage everything from Head Office as we don’t really know what’s going on in some of these countries half as well as the local people…And if they need to they’ll refer up to us for more advice or send the transaction up to us for clearance.” (UK EPFI 2)

In the case of Category A, and sometimes Category B, projects the E&S risk manager’s advice about the project has an influential role to play in the final approval of a project. If the project is also a controversial or high profile project, then the Communications Department or a special Reputational Committee may also be involved to advise on the potential reputational risks associated with it (UK EPFI 1, Interviewee 2). However, projects seem to be seldom rejected on the basis of E&S grounds alone, as there are a
myriad of risks\(^2\) associated with projects that determine the final approval by the Credit Risk Department/Committees.

“We [interviewee organisation] don’t reject projects generally just on environmental grounds and social grounds; there’s usually a whole raft of project grounds [and] we [E&S risk managers] provide advice, and opinion, when a project’s going to go to credit [Risk Department]. So there’s liaison, yes, between us, the account managers and credit as well so that there’s three or four parties involved…. I think if we raise questions and objections they [Credit Risk] take them very seriously. There’s always a follow-up process, further investigation or further information, further documentation, further permitting, whatever it happens to be, but if we raise questions then things tend to cascade from there. So they do tend to take it quite seriously.” (Dutch/Belgian EPFI, Interviewee 2)

This does not necessarily mean that E&S issues are not taken seriously in the credit approval process. Rather, the general attitude is that rejecting a project is the very last thing that the bank would like to do. Instead they prefer to engage with the client to bring the project up to the best, accepted standards possible – including E&S (thereby meeting all of the EP) – to ensure that the potential impacts and risks associated with the project are mitigated/minimised or avoided outright. Yet, one interviewee also stated that E&S risks that were not surmountable would mean the end of their organisation’s consideration of the project.

“For us it is not the desired outcome to say ‘no’ to a transaction, for us the desired outcome is to make complex transactions in difficult countries possible: safer for the bank and safer for the stakeholders…If you say no nothing is helped, not the environment, not the client, not the people on the ground, not the economy on the ground. The financing will still come from somewhere but probably on a different level of involvement, so for us it is most important to make it doable. And if it is really a case where E&S Risk Management believes it is absolutely not doable, no matter what you have tried – look I’m not speaking for the Bank’s Senior Credit Committee – but it’s basically the end point of the project.” (Dutch EPFI 1, Interviewee 4)

If the project is approved by the credit risk committee, having taken the E&S risks into consideration, the bank may then bid to become the lead arranger of the project.

This section highlights the intra-organisational dynamics between E&S risk managers and project financiers, as well as E&S risk managers and credit risk managers, within the EP-

\(^2\) For example: 1) project type, location, size, proposed capital expenditure verses revenues; 2) client creditworthiness and availability of necessary equity; 3) project sponsor partnerships to develop the special purpose entity (SPE); 4) project permits/licence, ESIA approval in host country; and 5) political risk.
project financing process. In doing so, it outlines how EP criteria is being incorporated into credit risk approval procedures and how, in the majority of cases, economic rationale dominates this process.

9.5 Term Sheet and Loan Documentation Stage

It is the lead arranger(s)’ responsibility to set the final “terms”/structure of the loan. Client requirements to comply with the EP are integrated into the proposed loan covenants for the project in what is known as the “Term Sheet”. These “terms” are then negotiated with the borrower and when agreement is reached, the lead arranger(s) move to final documentation of the legal and credit requirements of the loan in the “Terms Agreement Documentation/Common Facility Agreements”. The specific requirements of Equator Principles 2-8/9 (see Appendix 4) should be outlined in this loan documentation, with most emphasis placed on the EP covenants (Principle 8). Therefore, EP criteria become a formal part of a project financing through the loan documentation. The EP loan covenants will be discussed in more detail in section 9.7.

9.6 Bank Syndication

The lead arranger(s) agree(s) with the borrower to underwrite the loan, and then go to the syndication market for extra financing for the project. Today, due to the large uptake of the EP, most of the big project finance banks (lead arrangers) and smaller banks in a project finance syndicate are EPFIs. Should some syndicate banks be non-EPFIs, then it is the lead arranger’s role to articulate the accepted loan standards to other syndicate members. As one EPFI interviewee, whose bank normally acts as a lead arranger, stated:

“If we are syndicating a project then it will be EP compliant and meet our requirements. It does not matter to us if a syndicate bank is not an EPFI, as this makes no difference to the project – they are accepting a standard above their minimum. The lead arrangers dictate the nature of the deal to the syndicate for all aspects.” (UK EPFI 1, Interviewee 2)

A lead arranger acts as a Technical Agent and/or Documentation Agent for projects, depending on, for example, the number of lead arrangers involved. The Technical Agent is normally responsible for monitoring borrower EP compliance over the life of the loan i.e. from construction to “steady state”/operation when the bank receives remuneration from the project. However, it is the Documentation Agent that normally informs other syndicate
members of for example, any client “breaches” of their EP covenants, and follows-up with them accordingly (see also section 9.7):

“If it [project] went out of Equator Principle compliance, then a Technical Agent would inform the Documentation Agent/ the Facility Agent and they would then sort of distribute it [the information] to the lenders or take the necessary action as documented.” (UK EPFI 1, Interviewee 2)

However, the “quality” of the relationship between, for example, two or more lead arrangers in a syndicate may have some impact on the consistent application of the EP, since having multiple lead arrangers can be a potential source of tension alone:

“The problem is of course that it can become more cumbersome if there’s three lead arrangers because they’ve got to kind of argue it all out amongst themselves ….for example, we have a deal where we’ve got two lead arrangers. We’re the Technical Agent and the other one’s the Documentation Agent, so that splits the responsibility…There can be [issues] but we usually sort them out… it can just become a bit more cumbersome because…if there’s more than one lead arranger, you’ve got to negotiate between yourselves to come to a common approach to take to negotiate with the sponsor. So we can take a bit more time but communication is usually fine [between banks].” (UK EPFI 1, Interviewee 2)

Yet, as one mining company interviewee outlined, communication between lead arrangers on a particular deal may not always be so positive and can make loan negotiations more difficult, and in some cases “frustrating”, for a client:

“[Name of South African bank] and [Name of UK EPFI] are joint lead arrangers … I mean it’s a pity they don’t actually talk a lot together, which is quite frustrating. You know, it’s really frustrating because we have to almost have a conversation twice you know…banks are funny, they never really want to sit round the same table with each other, even if they’re in a consortium, it’s quite funny…But we find it rather frustrating because they’re always making telephone calls one at a time and asking you questions and you answer the same question to each one.” (South African Platinum Mining Company) 93

This is of course one particular clients’ impression of one specific situation, and cannot be taken as representative of the relationship between all lead arrangers. Nevertheless, it does prompt this researcher to question the possible impact of the lead arranger relationships on the EP process.

93 However, one EPFI interviewee commented, when he saw this quote while reviewing this research; that banks may deliberately adopt this approach to ensure that the information that the mining company is giving them is “correct”.

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In addition, in terms of the possible impact of broader syndicate members on the EP process, when questioned whether interviewees may have experienced any tension between EPFIs and non-EPFIs, or, active and “less-active” EPFIs within a syndicate, EPFI interviewees outlined how this had not been the case (to date).

“No, no, we never had any tensions [with other members in a syndicate] (Dutch-Belgian EPFI, Interviewee 1). We know a lot about each other; the EPFIs. We know a lot about how it has been rolled out, who is responsible, who is behind the implementation [in the other EPFIs] and that maybe sometimes gives [us] an idea about how a bank is dealing with it. But I think you can very well identify the issues and the more active EPFIs there, and the other parties, which are maybe a little more passive. So we indeed look at which EPFI banks are behind the deal [before getting involved]. (Dutch-Belgian EPFI, Interviewee 2)

This section (9.6) illustrates how EP practice at intra-organisational level can influence, and be influenced by, EP criteria and practice at organisational field level, through the syndication process.

9.7 Loan Covenants (Equator Principle 8)

Equator Principles 8 states that for all Category A and Category B projects the borrower is covenanted to:

a) Comply with all relevant host country E&S laws, regulations and permits;
b) Comply with the Action Plan (AP), where applicable, during the construction and operation of the project;
c) Provide periodic reports \(^\text{94}\) (no less than annually), documenting AP compliance and evidencing compliance with E&S laws, regulations and permits; and

d) Decommission the facilities, where appropriate, in accordance with an agreed decommissioning plan (Equator Principles II, 2006).

If a borrower is not in compliance with the EP covenants, the EPFI is to work to bring them back into compliance within an agreed grace period, and if this is not successful EPFIs “reserve the right to exercise remedies, as they consider appropriate” (EP II, 2006, p.4).

The loan covenants essentially “lock-in” borrower EP commitments into the loan documentation and any failure to meet these covenants could place them in default of the loan, with the risk of it being “drawn in” by the lead arranger/Technical Agent. However, as

\(^{94}\) Prepared by in-house staff or third party experts.
the below EPFI interviewee suggests, project sponsor EP compliance can be very case
specific requiring variant levels of attention from deal-to-deal.

“This isn’t a factory function and you have to look at individual projects on a case-
by-case basis; where are the sensitivities, where are there perhaps lingering
concerns with regard to the capacity and the commitment of the client to see these
things through? How many of them do think that Equator is just a bit of a rubber
stamp and let’s move on? And on those, where there are real sensitivities that can
come back and potentially haunt the bank, then obviously we’ll put more attention
there in securing interim monitoring reports, chasing them up when they’re not
present and not being forthcoming. And there’s one transaction at the moment
where technically there’s a default because we’re not seeing the [client] reports.
And so the Agent bank chase it up, and now the client is aware that some of their
lenders actually take these things quite seriously.” (UK EPFI 1, Interviewee 1)

The significance of legal covenants and the importance of a “case specific” approach to
their compliance was echoed by the EP lawyer interviewee. However, she also mentioned
that she felt that some EPFIs may not fully appreciate the myriad of factors influencing a
project sponsor’s ability to meet their EP covenant requirements, and suggested this needed
some further consideration by EPFIs.

“There is a difficulty with the covenants and it’s a difficulty that the lending
community has not properly grappled with. That is that if you have very significant
projects in countries where the infrastructure is weak and where the workforce is
not accustomed to best practice, health and safety and environmental systems, you
inevitably have breaches…. The issue that you have is even if you have an ESIA
that identifies mitigation actions; actually getting those mitigation actions to be
accepted and adopted by the local regulator and by the workforce who are
implementing the construction is a very big ask. [This is] partly because of a big
expectation gap between the banks and the project sponsors, as to what is
appropriate and best practice as well as the skills gap that often exists…. [So] I
think the issue is less a question of understanding what is needed; it’s more how
you deliver that in quite difficult terrain… [And] it seems to me that the emphasis
should not be on the breach as the trigger of an event of default, but on the
adequacy of the project sponsor’s response to the breach…I think Equator needs to
address [this] in future.” (EP Lawyer)

Similarly, one of the mining company interviewees highlighted how there was an equal
need for international EPFIs to take more experienced project sponsors’, as well as
consultants’, local expertise, into account during loan negotiations:

“It irritates me a little bit that you’ve got somebody sitting in Europe coming into
Africa for the first time and trying to tell me how I should run my business. I’m
five steps ahead of them…They’ve [UK EPFI] come out with a list of things that
we must do and one of the examples to me is a bit bizarre. I mean they all came out
on site and we took them round and showed them the project...but now they say ‘okay, so what impact is your project going to have on AIDs in South Africa?’ So I tell them exactly what it’s going to be because I’ve been working in this industry for 28 years and part of my job has always been to manage the AIDs side of the business. But then they said ‘but that’s not good enough, you need to go and find a third party to do a study for you.’ And I’ve just gone out and found out how much that’s going to cost and it’s going to cost me $63,000 to do that exercise...and it’s a UK company that has to come in here with expenses and it will take them six months to do it... Why not get a local consultant and let them do it and then just peer review the information? There are plenty of good companies here [that] they [UK EPFI] need to take a little bit more cognisance of.” (South African Platinum Mining Company)

This section (9.7) highlights some of the complexities of the project finance process, especially regarding an EPFI’s need to “know” their clients and their ability to meet EP covenant requirements. It once more draws attention to the case specific nature of the project finance-EP process at intra-organisational and organisational field level, and with it the inherent heterogeneity of the EP institutionalisation process across different EPFIs. This is a process, which, as continuously outlined throughout this chapter, is highly dependent on the various actors tasked with EP implementation and their interpretation (signification), rationalisation (legitimation) and control (domination) of EP criteria.

The specific requirements of Equator Principles 4-6, which contribute to client compliance with the afore-mentioned covenants, will be outlined in the following sections. These requirements are often considered the most complex and controversial aspects of the EP.

**9.7a Action Plan and Management System (Equator Principle 4)**

For all Category A and B projects, borrowers are obliged to produce an Action Plan. If located in a non-High-Income OECD country the demands on borrowers are more stringent than those located in High-Income OECD countries. In the case of the latter, EPFIs may require the development of an AP based on relevant permitting and regulatory requirements, and as defined by host-country law. In contrast, if the project is to be located in a non-High-Income OECD country, further procedures have to be undertaken. Here, an additional aspect of the AP is the establishment, maintenance or improvement of an E&S management system that outlines measures to mitigate or avoid the impacts and risks associated with the projects. The proposed measures are also required to comply with both
host country E&S laws and also applicable IFC performance standards and EHS Guidelines as identified in the AP.

9.7b Consultation and Disclosure (Equator Principle 5)

In addition to the AP, for Category A, and as appropriate, B projects in a non-High-Income OECD country, the client, government or third party expert is required to consult with project affected communities in a structured and “culturally appropriate manner” (Equator Principles II, 2006, p.3). The process is aimed at ensuring the “free prior and informed consultation”95 (Ibid) of affected communities’. This is to allow the EPFI to determine whether the local communities have been adequately engaged with in the project planning and construction phases, and on an ongoing basis thereafter over the life of the loan. To assist this process, the ESIA and/or AP documentation (or their non-technical summaries) are to be made available to the public for a certain period of time, in relevant local languages (EP II, 2006)96. The borrower then has to document this process and its results for independent review (Equator Principle 7).

“There are two stages; one is the consultation before the project gets approved and the go ahead to build it and then there’s obviously an ongoing programme of consultation. Again, it’s not kind of clearly defined, neither by the Principles or by the ESIAs, but usually, there’ll be a set of consultations that they [project sponsors] have to go through before they could present it as part of the ESIA or with the feasibility study and say ‘these are the consultations we’ve done and we’ve taken into account these views’. And obviously once you start building, that sort of consultation should carry on...So, what we always say to companies is you know, the earlier you start that the better because you get bigger buy-in and we can manage local expectations.” (UK EPFI 1, Interviewee 2)

One mining company interviewee outlined the importance of the public consultation process to their operations:

“Mining companies can only operate with the support and assistance of the local communities and they’re not going to get that if they don’t show that they’re willing and they’re concerned about both the environment and the local community

95 It should be noted however that this is different to “free prior and informed consent” recognised in international laws and standards. It also does not stipulate the need to follow the “broad support” (of affected communities) approach taken by the World Bank and IFC (Herz et al., 2007). This has been heavily criticised by NGOs.

96 In certain cases, a specific Public Consultation and Disclosure Plan (PCDP) may be developed as part of the project sponsor Action Plan and/or Management System.
and social issues. [So] consultation and disclosure is an ongoing activity [for us].”
(Australian Gold Mining Company)

However, as the EP do not provide specific guidance on how a consultation process should or could take place, the public consultations that are undertaken, and their relative complexity and success, are thus highly context specific.

“You know, I don’t think there’s any way you could say that it’s [public consultation] ever been done perfectly. And that would include well developed Western democracies as well as countries who don’t have that experience…There are fundamental principles that we [interviewee’s organisation] follow which come from the [IFC] Performance Standards, but beyond that, we would look at the context of the country, the project, the client and also obviously the impacts. It [also] depends on the length of the project. You know, there are a whole range of variables that we have to take on board to be adapted to the consultation process.”
(EP Consultant)

“There’s certainly been projects where it [public consultation problems] hasn’t really been an issue. There have also been projects where the project sponsor’s been absolutely bound by the local regulator from doing any form of consultation. Which makes it quite difficult for everybody.” (EP Lawyer)

The lack of EP guidance on how consultation processes could be designed and undertaken is largely reflective of the case-specific nature of most project finance deals. Subsequently the variant nature, efficiency and transparency surrounding these processes are often regarded as one of the most controversial aspects of the EP.

“It’s [public consultation] often the most controversial aspect of the Equator Principles and the one that the clients fear most in terms of the cost, in terms of the unpredictability, particularly when you want to consult people who usually don’t have a voice, who aren’t particularly empowered and therefore have nothing to lose but have real concerns about the project…[And] unfortunately a lot of clients and also some consultants think of the old fashioned way of public consultation where you just have two meetings, one at the beginning and one at the end of the process, very often with officials and then it’s done and dusted. But I think if you have the time and the right approach it [free prior and informed consultation] does mean something; where you give people appropriate information in appropriate form and you make the information accessible to them so they can enquire and register concerns as well.” (EP Consultant)

9.7c Grievance Mechanism (Equator Principle 6)

An equally important and controversial procedure for Category A and, as appropriate, Category B projects (located in non-High-Income OECD countries), is the establishment of
a grievance mechanism. Grievance mechanisms are to allow project sponsors to receive community concerns about the E&S performance of the project and to address them promptly. Project-affected communities are to be informed that a grievance mechanism exists during the community engagement process, and these mechanisms are to form part of the project management system moving forward. The aim is to ensure that community engagement, consultation and disclosure continue throughout project construction and operation phases.

One of the mining company interviewees provided some insights into the type of grievance mechanism they have in place for project-affected communities in the vicinity of one of their gold mining projects in South-East Asia; a project that was subject to EP-project finance.

“We have to have a grievance mechanism in place because we have to get local feedback. If there’s anything that we’re doing which they object to, and we don’t take it into account, then we’re liable not to get [mining] licences issued. It can take many [forms]. In [name of project], they did a full survey…they had community feedback sessions, they gave the local community the facility and ability to put in grievances anonymously. Somebody physically went round every residence in the area that was going to be affected and I think that was several thousand … and sat down and went through a little survey/questionnaire with each of them … And from that, we drew up a programme … we’ve put in fresh water systems, assisted with school buildings, clinics, ambulances and all sorts of things. So it’s that sort of activity.” (Australian Gold Mining Company)

However, similar to Equator Principle 5 (consultation and disclosure), specific guidance on what a grievance mechanism constitutes, what form(s) it can take and how it can operate and be managed in practice, are currently not outlined in the EP. In turn, grievance procedures are also very case specific and, as some interviewees outlined, “seem to be incredibly hard to run effectively” (EP lawyer), with the continuous need to “make it clear to the stakeholders what it is and how they can go about triggering it.” (UK EPFI 1, Interviewee 2)

When some interviewees were asked if the EP in their current form would allow for adequate avenues of redress for affected communities - an ongoing bone of contention for NGOs - there was a mixed response, with one interviewee suggesting that extant legal frameworks were sufficient in this regard:
“[That’s a] difficult question, there cannot be a perfect system but they [EP] are a step in the right direction.” (UK EPFI 1, Interviewee 2)

“I mean first of all the Equator Principles are voluntary, secondly all these organisations work in countries that have their own legal framework which people have redress to. The majority of countries also …are signatories to the Declaration on Human Rights and other human rights treaties. So people also have that redress. And I’m not quite sure what an additional sort of Equator Principles Ombudsman function would be, given that you have a national legal framework and an international legal framework. And of course you can always appeal to the headquarters of the organisation that you’re complaining against.” (EP Consultant)

In general, sections 9.7b and 9.7c suggest that despite the existence of certain EP criteria on project consultation, disclosure and grievance mechanisms, at EP organisational field and intra-organisational level, what occurs in practice is very much dependent on a raft of project-specific variables, as well as numerous EP actors’ interpretation, rationalisation and control of the Principles.

9.8 Client Compliance (Equator Principles 7 & 9)

For all Category A and, as appropriate, Category B projects, borrowers are required to have an independent E&S expert - not directly associated with them - conduct a review of their ESIA, AP and consultation documentation (Equator Principles 7). In addition, Equator Principle 9 stipulates that EPFIs are to appoint, or have project sponsors retain, an independent environmental and/or social expert to review and verify their EP monitoring and reporting over the life of the loan. EPFIs therefore rely heavily on external E&S consultants to assist in their initial and ongoing assessment of borrower EP compliance.

“The actual monitoring process itself [over the life of the loan] depends very heavily on external consultants which is part of the Equator Principles. So you have A and certain B Category projects and you have to appoint some sort of independent, monitoring organisation/consultants …and they provide a periodic report which contributes to the annual review undertaken by risk managers in consultation with other banks. So in terms of gathering information and checking against Action Plans and goals achieved, or things which are not compliant, that’s a process that relies very heavily on the external consultant which is appointed [by the client] in agreement with the lender.” (Dutch/Belgian EPFI, Interviewee 2)

In terms of the initial independent review (Equator Principle 7), some interviewee evidence suggests that the “independence” of the consultant (from the project sponsor) carrying out the review may be questionable at times. For example, the EP consultant highlighted how
the consultants employed to prepare the ESIA were not supposed to conduct the independent review of it, despite the fact that the client would in some cases prefer this.

“No you can’t be involved in the initial [E&S assessment] and the independent review, it has to be one or the other. And sometimes our clients don’t understand that…so essentially you can’t obviously review your own work.” (EP Consultant)

Such issues prompted NGOs to request some form of guarantee of the independence and validity of the “expert” information EPFIs were using to assess project sponsor EP compliance:

“Given that EPFIs rely on outside expertise for objective information and assessment, we recommend that the EPFIs require the independent expert – the [for example] preparer of the SEA [social and environmental assessment]- to sign an agreement attesting to its validity and factually based information. In order to make informed choices and minimize risks…it is necessary for the EPFIs to build in measures such as these that guarantee that the information they receive is objective and accurate.” (BankTrack, 2006a, p.8)

To the best of this researcher’s knowledge, no formal provision for such expert “guarantee” has been developed, short of any possible private EPFI arrangements with the consultants they employ. However, interviewees did explain that EPFIs’ reliance on external consultants, for both the initial review and ongoing client monitoring, was quite simply based on their own lack of in-house E&S expertise. In addition, addressing the social dimension of projects, and finding suitable consultants to assist with this, appeared to be most challenging for EPFIs.

“Banks can only use the best advice and guidance they can get, we’re not human rights experts, we’re not environmental experts etc. So we have to use advice as best we can.” (UK EPFI 3)

“On the social side, once you have lost the trust of people and you have the reputational damage it is extremely hard. So it is important to get it right from the beginning: to do the right consultation, to get the information to the people [as] they need to make an assessment for themselves. That is extremely important, even more so than the environmental side I believe. But it is also harder because it is the newer discipline… [And] it is harder to find good advisors on the social side than on the environmental side.” (Dutch EPFI 1, Interviewee 4)

There was also some evidence of interviewees questioning the “quality” of consultants more generally, with, for example, one interviewee remarking: “we sometimes feel that we might have perhaps a better consultant to be frank” (Dutch/Belgian EPFI, Interviewee 1).
While this may raise questions about the extent to which consultants influence the “quality” of EP evaluations, interview material in general shows that specialised E&S consultants are considered invaluable to EPFIs’ ongoing monitoring of borrower compliance. This is especially the case in the review of the borrowers’ periodic reports on EP compliance. While the EP lawyer commented that these reports usually “tend to be quarterly during construction and then once a year post-construction”, an EPFI interviewee stated that reports from for example, the mining sector, could be produced on a monthly basis and outlined that process below.

“Technical reports are usually monthly and these contain environmental and social issues referring to the environmental management plans. These are reviewed by the consultant, and us, during the life of the loan. As a guide, the consultants would also visit the site quarterly through completion [steady state production] and thereafter annually, usually until the end of the loan life… That might be; say it’s a ten-year project it might be for seven years or something… Unless there is a specific event or change we would not expect the client to specifically report on EP compliance outside these reports.” (UK EPFI 1, Interviewee 2)

Within the majority of EPFI interviewee organisations it is the project financiers that are encouraged to take “ownership” of this project monitoring process, in association with the external consultants and/or relevant E&S risk managers within the bank.

“The Commercial guys, the Product guys, who do the transaction and who structure the deal…those people, they have to manage EP, it’s part of their package. It’s not in the ivory tower, it’s their daily business.”(Dutch EPFI 1, Interviewee 3)

“We just need actual accountability in the business unit that’s dealing with it [EP] on a daily basis. I think there’s still sometimes a perception that you know, it’s my department’s [Governance and Sustainability] issue… [So] as much as possible, I’m trying to make sure that they now take accountability for it themselves…Just with the proviso that there needs to be a very strict process around how they deal with it.” (South African EPFI)

Yet interviewee material also suggests that it is quite rare for an issued loan to be “drawn-in” in the event of an EP covenant breach, such as borrower failure to produce these reports. Rather, EPFIs prefer to issue “warnings” to the borrower and/or work with them, in association with the various external experts, to bring their operations back into compliance. It appears that the threat of a loan “withdrawal” alone is enough to ensure EP compliance.

“The Equator Principles requirements are part of the documentation on the credit side, so the client is very much aware what his obligation is technically or legally.
If they would not follow through their obligations they would be risking the event of default on their credit. …Frankly, that is not something which is envisaged to be used to really tip a project into the situation of default, but it can be used as a leverage to say to the client, ‘Well we need to sit around the table, you are not in compliance with your credit requirement’ and that is something which every client understands very well. When you have that capacity to say you are not formally complying with your credit requirements, that financing might be pulled from them; that is a very powerful position. It has never come to that situation, but that’s the strong part of the Principles, as you have it as part of the [loan] documentation.”(Dutch EPFI 1, Interviewee 4)

This section highlights a “chain of accountability” in the EP compliance process, running from an EPFIs’ responsibility to ensure borrower compliance, to borrower obligations to produce periodic reports of compliance, to consultants’ responsibilities to provide accurate and impartial accounts of the adequacy of borrower compliance. The success of EP monitoring and compliance is hence highly dependent on the “accountability relationships” between these actors at intra-organisational, organisational, organisational field and societal-project levels. EPFI compliance will be discussed further in the next section.

9.9 EPFI Compliance and Reporting

The implementation of the EP into EPFI project finance processes should be incorporated into their internal reviews and independent audit functions. One interviewee explained that this should occur because, if the EP become a requirement for project financing under a bank’s credit guidelines, then they become part of the permanent credit documentation for the projects. The bank then has a fiduciary responsibility to review every general credit line/project at least once a year to ensure that the default rate of their project portfolio is as low going forward as it was in the approval and development of the project. Hence, these credit lines/projects will undergo internal credit risk reviews (by, for example, a group from Risk Management) and annual audit (by an internal independent audit function) as part of the bank’s credit risk processes. As the EP are a key aspect of the credit requirements, documentation and approval for project finance deals, they should therefore form part of these reviews/audits. In addition, internal staff competence regarding EP implementation should technically also be included in these reviews.

“Every project, every credit is reviewed once a year by the bank as a fiduciary requirement. And projects quite often on a ratings scale, internally within [name of interviewee organisation] actually have a requirement to be reviewed more frequently; so half yearly. So as the Equator Principles are a key part of the credit
documentation, and part of our approval process, they [front office/project financiers] have to report back on the status towards the Principles with every credit review. And that review is usually coming to the specialist teams, so to the E&S Risk Management team, to see how the project has progressed against its commitment...So within Credit Risk Management there is a group which is called Risk Review which goes out and checks what the countries or the product areas are doing on the credit risk process...And on top of that is an independent audit function which every bank has and ... it does checks on all the processes in place. So the bank has processes which are basically the law of the bank…and as the Equator Principles is a requirement for any project financing under our credit guidelines, it is [also] checked as part of that.” (Dutch EPFI 1, Interviewee 4)

However, the monitoring of project financier’s application of the EP took a more “informal” role in another EPFI, where emphasis was placed on the level of interaction between them and the E&S risk managers as opposed to an “audit” of their procedures. This interviewee felt that this was mainly reflective of the small number of teams working on project finance within this EPFI:

“On the environmental side, all those aspects will go through Group Environmental Risk and then you know, they might ask for the last report and just have a meeting with us [Mining & Metals Team] or just you know, monitor us… but there’s not an audit of what we’re doing, there’s kind of ongoing involvement…To be honest, there’s not a lot of teams here that actually do project finance, it’s only really us I would guess and the Infrastructure people… So that’s how it works.” (UK EPFI 1, Interviewee 2)

Despite the fact that some interviewees stated that their internal EP-project finance activities were subject to internal credit risk reviews and/or independent audit, this is something that needs further transparency across EPFIs; especially within EPFI reports of their EP implementation and compliance procedures. This will be discussed further in the next section.

9.9a EPFI Reporting (Equator Principle 10)

Equator Principle 10 requires EPFIs to produce a report, at least annually, about their EP implementation processes and experience.

Over the course of this research (2005-2009) the level and quality of EPFI transparency and disclosure regarding EP implementation has in general greatly increased. The majority of EPFIs are now, as an EPFI “membership” condition, meeting the basic EP reporting
requirements of Principle 10. Those EPFIs not doing so are listed as in the “first year grace period” on the “Reporting” page of the EP website (http://www.equator-principles.com/reporting.shtml). As of April 2010, out of 68 EPFIs, there was only one EPFI, Wells Fargo, listed with “No information made available” next to its name on this website.

In addition, many EPFIs, and certainly those interviewed in this research, have gone beyond the basic minimum reporting requirements to include, varying levels, of information on aspects of their EP implementation procedures, who is responsible for this within their organisations, brief case studies on “dilemmas” regarding challenging or high profile projects and the stakeholder/NGO engagements associated with these. This information is dispersed amongst EPFI interviewee sustainability/CSR Reports or summaries, and/or relevant sustainability/E&S risk management pages on their websites. EPFI “leader” organisations have been, and continue to be, at the forefront of such EP disclosure. This forms part of what appears to be a certain movement towards more “exposure” of internal E&S policies and risk management approaches amongst EPFI leaders. An example is the very recent trend, amongst some leaders, to provide a more detailed overview of how the EP are applied throughout the project financing process in their 2008 reports or relevant web links. In the case of one EPFI interviewee organisation, this is a six-page document structured around the ten Principles. For another, a table of the key stages of the project financing process and where the EP are applied (similar to that laid out in this chapter), is included in their corporate citizenship report.

While these are welcome developments, this researcher still questions the level of assurance associated with EP reporting. One EPFI interviewee organisation’s pioneering move to provide an assurance statement for their EP implementation procedures alone, in addition to the standard assurance of their sustainability report, from 2006 onwards, does not seem to have become a general trend for other EPFIs thus far. The broad approach remains to be

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97 This includes a breakdown of EP projects screened or approved by category, region and sector (as per the EP Reporting Guidance Document, 2007).
98 Yet, it appears that this EPFI has not been asked to “leave” the EPFI network thus far as a result.
99 That is, the reporting of information for 2008, in sustainability/CSR reports produced in 2009.
100 This interviewee organisation has, in their 2008 report, limited the scope of their overall assurance to their EP implementation and their carbon neutrality. However, this now also raises questions about the assurance of the additional reported information falling outside this limited scope.
the provision of an assurance statement for the sustainability/CSR reports, in which EP reporting forms part. Yet in doing so, unless it is explicitly mentioned in the EP section of these reports (or in the “scope” of assurance) that EP implementation has been subject to internal and/or external audit, external observers are left to presume that EP implementation has been audited and included in the general assurance approach.

It should be noted however, that another EPFI interviewee organisation has indicated under their EP tables,¹⁰¹ in their report for 2008, that the quoted figures have been audited by an international auditing firm. Yet, this is currently not the norm throughout the majority of interviewee reports.

Therefore, this researcher suggests that there is the need for greater transparency by EPFIs about the auditing of their internal EP implementation; as well as the need to develop the external assurance process of EP reporting in general. Perhaps one immediate way to begin to address this is through greater use of the Global Reporting Initiative (GRI) Financial Services Sector Supplement (FSSS). Here, indicator FS9: “Coverage and frequency of audits to assess implementation of environmental and social policies and risk assessment procedures” (GRI, 2008 p.2) could assist. While the majority of EPFI interviewees are now using the GRI Financial Supplement as part of their application of the GRI G3 Guidelines in their sustainability reports, in many cases their use of it could be improved. For example, in the GRI Index at the back of interviewee reports - outlining which GRI indicators are being used and where related information can be found in the report/online - readers are, in the majority of cases, being referred to the assurance statement of the sustainability reports for information on indicator “FS9”. Yet this assurance statement does not always make explicit which “environmental and social policies and risk assessment procedures” have actually been audited. Only one EPFI leader interviewee organisation (one of the afore-mentioned interviewees in this section) explicitly stated in the body of their 2008 report that independent compliance audits of their E&S risk management policy, and hence their EP procedures as part of this, were conducted on a regular basis. In turn readers are referred to this information, as well as the assurance statement, when it comes to reporting against FS9 at the back of their report. Therefore, there is the need, and opportunity, for other EPFIs to be equally, if not more, transparent about the internal audits of their EP implementation.

¹⁰¹ Which disclose the number of deals covered by category, region and sector.
procedures; as well as the external assurance of this. This would provide some reassurance that EPFIs are taking their EP procedures seriously internally, especially for those external observers that are not fortunate enough to conduct interviews with EPFIs about their experiences with EP implementation.

Sections 9.9 and 9.9a have illustrated how EPFIs’ compliance with EP criteria at intra-organisational level has affected their organisational level reporting on EP implementation, as well as EPFI accountability trends at organisational field level and perceptions of the same at societal level. The next section will now consider how these trends may develop in the future.

9.10 The Future of EP Institutionalisation

This section briefly considers some of the outcomes of EP institutionalisation at intra-organisational level and how this may affect the projection of EP institutionalisation at organisational, organisational field and societal-project level in coming years.

This chapter has evidenced how the EP are being implemented within the project finance process and thus how they have and are continuing to be institutionalised at intra-organisational level. Some EPFI interviewees summarised how this had affected change within their daily project finance operations as follows:

“They [EP] are making differences in which decisions [are made]… [Name of interviewee organisation] turn down transactions for non-Equator compliance, I know other banks that have done the same thing. The Equator Principles allow banks to get into discussions with clients to try and change things.” (Dutch EPFI 1, Interviewee 1)

“I think we can probably say that the Equator Principles have stopped us getting involved in two or three basically bad projects …[so] you can say it has demonstrated the feasibility of environmental and social risk management as a practical, applicable, useful tool, which has shown that it can be done quite well. (Dutch/Belgian EPFI, Interviewee 2)… And it doesn’t hurt. It’s [created] more awareness within the business of these kinds of things, so it’s really increased …[their] acceptance. I mean, you almost cannot afford not to do it the right way [now].” (Dutch/Belgian EPFI, Interviewee 1)

This practice also influenced, and was influenced by, EP institutionalisation at organisational, organisational field and societal level over 2003 to 2008. For example, one
interviewee outlined how the EP have created a “community” of broad stakeholders, in which the EP criteria allow for common recognition and communication (significance) of E&S issues within project finance practice:

“There are all sorts of benefits surrounding Equator. Benefits to the bank and benefits to the client, and Equator is now just part of the terminology, it’s part of the lexicon surrounding project finance. The biggest success to me is not about the 54\textsuperscript{102} banks that have adopted it, it’s actually the fact that lawyers talk about the Equator Principles and environmental consultants talk about Equator Principles, and the banks. And now it’s...created a community and it’s made it more efficient in terms of communication. As soon as you say ‘Equator’ you should know what environmental management standards we’re talking about.” (UK EPFI 1, Interviewee 1)

With regard to future developments, some EPFI interviewees felt that the accountability trends established by the EP II criteria and EPFI governance work at organisational field level were set to continue, despite the legal and commercial constraints EPFIs faced at organisational level:

“I think that in the coming years probably we’ll have to go a little further and allow more information to be made public. And the debate now is about who will make it public. We’re finding we can encourage the sponsors to make it public or to give us the right to speak with the NGOs, to discuss the projects and so on. But it’s still very difficult because it’s true that it’s not at all in the culture or the tradition of the bank [to do this].”(French EPFI, Interviewee 1)

There also appeared to be a growing consensus amongst EPFIs that there was a need for them to be “consistent” with regard to their E&S responsibilities across all of their activities at organisational and intra-organisational level, and to explore how aspects of the EP might be extended to enable this.

“Banks need to be consistent, and what I mean by that is if you don’t want to do project financing for a client for a certain asset, you shouldn’t be doing any other financing for that asset. You shouldn’t be underwriting the equity…or have an equity hold in the client.” (Dutch EPFI 1, Interviewee 1)

“I think that you’ll see over the next few years probably environmental advocates and stakeholders requesting that maybe Equator be broadened. Which you know, that’s I think something that we’ll just have to take a look at and have a discussion on because there’s a great deal of development out there that’s been financed

\textsuperscript{102} As of September 2007 when interviewed.
through the capital markets and through equity and all of that and I think it’s a big challenge.” (US EPFI)

Yet, interviewees also cautioned against expecting the EP to be capable of addressing all financial sector E&S responsibilities, when they were, and would continue to be, explicitly designed for project finance. One EPFI leader stressed how there was a need to distinguish between the EP criteria for project financing and other forms of E&S risk assessment criteria for other financial practices:

“The frustrating thing is when people are starting to use Equator as some sort of euphemism for any environmental credit risk assessment…That’s almost because Equator has been a victim of its own success … It has gone from you know, an idea through the embryonic phase to launch and now something like 54 banks[103] [adopting] in less than four and a half years … Now because of that success people then think ‘okay, well why don’t we hitch this onto it and let’s hitch that onto it’…that’s the sort of thing that will bring it down because then it’s doomed for failure because people see Equator and say well it’s not fulfilling its expectations. And actually, if it’s applied properly for the purpose for which it’s intended, then it does its stuff. But people almost see it as being some sort of ‘cure-all’…So what’s important to me is to decouple Equator and project finance due diligence, from other environmental credit risk assessments.” (UK EPFI 1, Interviewee 1)

Nevertheless, as previous chapters have also outlined, the application of the “spirit” of Equator, to other financial activities has and is occurring. In fact another EPFI leader outlined how he felt the success of the EP lay in the E&S awareness it had managed to stimulate at organisational field level, allowing EPFIs to transfer this experience to the development of different sustainability initiatives “beyond” project finance at organisational level. He therefore felt that the EP’s legacy would be more significant in what it had catalysed or enabled outside project finance per se.

“I mean I think if you want to analyse the value of Equator, I actually think it’s done more as a catalyst to create sustainability thinking across banks than it probably will ever do in the area of project finance alone, which is an increasingly small part of our business…And it’s interesting, I mean working on other initiatives outside of Equator, I mean I think the Equator experience is causing people to do things slightly differently. I mean I think we’re currently working on some climate principles which may or may not happen[104], this is outside of Equator, and the banks involved, I mean some of them are Equator banks and you know, they were saying ‘well look, if we’re going to do this we do need to establish upfront what disclosure we have to undertake, how we report on what we’re doing’.

[103] As of September 2007 when interviewed.
[104] The Climate Principles were launched by a group of international banks and insurance companies in December, 2008, while a group of US banks launched the Carbon Principles earlier that year in February.
And I mean they’re addressing that upfront. [So] I think that’s very definitely based on previous experience…[So] I think Equator has been a catalyst for more things outside of project finance than people actually give it credit for. I mean I think that’s its biggest legacy.” (Dutch EPFI 1, Interviewee 2, emphasis added)

In summary, interviewee material suggests that ongoing implementation of EP criteria within project finance practice at intra-organisational level had, and would continue to, influence the projection of EP institutionalisation over organisational, organisational field and societal levels, as well as the general institutionalisation of E&S issues within broader financial services activities in future.

9.11 Chapter Summary

This chapter has provided more detailed evidence of the EP as an accepted or institutionalised facet of project financing processes at EPFI intra-organisational level i.e. within the actual project financing process, as led by front office/project financers in consultation with (E&S) risk managers. A summary of this EP-project financing process is captured in diagrammatic form in Figure 9 (below).

This chapter has extended the Dillard et al. framework to intra-organisational level through the analysis of the interplay between EP “criteria” and “practice” within project financing and how this influenced, and was influenced by, EP institutionalisation at organisational, organisational field and societal-project levels. Here, interviewee material has illuminated the complex and extremely case specific nature of the project finance process. This, plus the fact that EP implementation is highly dependent on a variety of actors’ interpretation (meaning), rationalisation (legitimation) and control (domination) of the Principles, once more emphasises the inherent heterogeneity associated with the EP institutionalisation process. As a result, the reciprocal and iterative relationship between EP structures and agency as the basis of the ongoing EP institutionalisation process is reinforced. The chapter ended with the consideration of how EP institutionalisation at intra-organisational level had, and would continue to, influence the EP institutionalisation process in general moving forward.
Figure 9: The Project Financing - Equator Principles (EP) Process

Client & Project

Green Light/Marketing: Front Office/Project Financiers (EP triggered)

Due Diligence (EP 1: Review & Categorisation; EP 2&3: ESIA)


Credit Risk Approval (ESIA/AP/C&D/GM evaluated)

Final Terms/Loan Documentation (EP 8: Covenants)

Monitoring of Client Compliance (EP 7&9: Independent reviews)

Internal & Independent Audits of EPFI Credit Lines (EP procedures included)

EPFI External Reporting of EP Implementation (EP 10)

KEY:
ESIA: Environmental and social impact assessment
APMS: Action plan & management system
C&D: Consultation & disclosure
GM: Grievance mechanism
* Ongoing requirements over the life of the loan

The solid arrows indicate the progression of the project finance-EP process (the double arrows representing interrelationships therein). The dotted line indicates the ongoing interrelationship between the client/project and the various phases of the project finance-EP process.