

# Equator Principles

## Promoting Greater Responsibility in Project Financing

BY NATASHA CAPPON

**Leading global financial institutions have taken important steps to promote sustainable business development through project lending. The Equator Principles are a testament to that progress.**

The Equator Principles (EPs) are a set of voluntary guidelines developed and adopted by financial institutions for assessing and managing environmental and social issues in project lending. Institutions that adopt the EPs commit to apply the principles to projects with total capital costs of USD 10 million or more. Established in 2003 and updated in 2006, the EPs are now applied by some 59 financial institutions from 21 countries in all industry sectors; from mining to oil and gas and forestry.

“The EPs are here to stay and the financial sector, project sponsors and local communities are better off because of them,” says Shawn Miller, Director of Environmental and Social Risk Management for Citi, one of the 10 founding members. “The principles have had a positive and deep impact on the financial sector’s approach to environmental and social responsibility.”

More than just statements of intent, the EPs oblige banks to require an environmental impact assessment for high-risk projects and, in some cases, a management plan, which addresses key emerging market issues, including socioeconomic impact, pollution prevention, indigenous rights, involuntary resettlement and labour standards. They also set guidelines for covenants pertaining to project monitoring in loan documentation.

The impact is being felt in many sectors. “It has certainly been a positive development for the Canadian mining industry,” notes Gordon Peeling, President and CEO of the Mining Association of Canada. “It puts everyone on a level playing field in terms of how companies can best conduct their business across a wide range of environmental and social performance standards. It allows the mining industry to understand what the expectations are on project development so as to ensure best results.”

### Gaining momentum

The EPs have been adopted by more than 85 per cent of the global project finance sector, including EDC, which formally adopted the principles in October 2007. EDC is the second export credit agency (ECA) after Denmark’s to do so and joins the five major Canadian banks – BMO, CIBC, RBC, Scotiabank and TD.

“Adopting the EPs enabled us to bridge the leading practices of both ECAs and private financial institutions,” explains Greg Radford, Chief CSR Advisor at EDC. Since 2000, EDC has helped shape the Organization for Economic Cooperation and Development’s (OECD) *Common Approaches on Environment* that bind ECAs and other public sector financial institutions to similar environmental commitments.

## Understanding EP at a Glance

EPs classify projects into three levels according to potential social and environmental impacts:

**Category A** - projects with potential significant adverse social or environmental impacts such as a new mine or petrochemical facility

**Category B** - projects with potential limited adverse social or environmental impacts that are site-specific and more easily mitigated, such as tourism or general manufacturing development

**Category C** - projects with minimal or no adverse impacts, such as a telecommunications project

EDC helps finance many global projects in which Canadian companies participate. “Because of our extensive project finance experience and demonstrated capacity to assess environmental and social issues, we found that we were increasingly being sought out by commercial banks to participate in project finance syndications or co-financing opportunities,” says Radford.

Since EPs have become the market standard for assessing sustainability issues in emerging markets, adopting the principles enabled EDC to speak the same language as our commercial partners.

EDC views the EPs as a complement to the OECD *Common Approaches*, and as an opportunity to better serve its customers. “Adopting the EPs essentially reduces the burden on our clients to meet different standards in producing their environmental impact assessments. It’s an opportunity for us to enhance coordination among lending institutions, and create consistency in the due diligence process,” adds Radford.

Financial institutions also see the EPs as a tool to help protect the bottom line. “A borrower’s ability to manage environmen-



Photo: Courtesy of Barrick

## Historical perspective: The push towards more principled financing

Around the turn of the millennium, public pressure mounted for international banks to more proactively encourage sound environmental management in projects they supported. This was particularly pronounced in mining and other extractive projects in emerging markets. While many top international institutions wanted to be associated with responsible environmental and social project development, they did not want to compete with each other on compliance issues. They also lacked a consistent set of international standards to apply across all project financing activities.

In October 2002, several leading commercial banks, including Citi, ABN AMRO, Barclays and WestLB, agreed to develop a common set of guidelines that lenders could use in assessing project-related environmental and social risk.

They based their standards on those used by International Finance Corporation (IFC), the private sector development arm of the World Bank Group. These standards were widely recognized internationally for mitigating social and environmental risk. In June 2003, the Equator Principles were launched by 10 leading banks from seven countries.

▲ The impact of the Equator Principles has been a positive development for the Canadian mining industry. Overall, the principles lead to better projects, reduced costs and raised expectations for sustainable development.

tal and social impacts can determine the profitability and even viability of a project,” says Lillian Ranalli, Director of Corporate Environmental Affairs at TD.

“The EPs can improve the risk management process, lead to better decision-making and ultimately ensure more secure investments in projects that are adhering to leading-edge practices in responsible business.”

### Advantages in emerging markets

For the Canadian mining industry, the EPs are increasingly being “rolled into a way of doing business,” explains Peeling. “It’s inevitable that you are going to have to apply them to ensure your project is attractive to the lending market, and it is to be expected that there will be oversight and due diligence against your performance.”

In emerging markets, EP standards are often more rigorous than local laws and regulations. “EPs create standards to drive project performance which also benefits developing countries, as they

now have a ready set of performance guidelines to which they can refer,” explains Peeling.

Looking ahead, the principles continue to evolve with the treatment of human rights increasingly at the forefront. Revisions to the principles in 2006, for instance, put additional emphasis on the social impacts of projects, with new provisions related to community consultation with affected groups.

As more financial institutions adopt the principles, the EPs are expected to lead to innovation in sustainability standards beyond project finance.

“For Citi, the EPs were the impetus for the development of a broader Environmental and Social Risk Management Policy that is now applied to other transaction types. We have witnessed this same positive evolution with at least a dozen other leading banks in the EP network,” says Miller.

Overall, the principles lead to better projects, reduced costs and raise expectations for sustainable development around the world. ■

### FOR MORE INFORMATION

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