Global Private Regulation, Global Finance and the Future of Corporate Human Rights Accountability

Ariel Meyerstein, University of California, Berkeley
Global Private Regulation, Global Finance and the Future of Corporate Human Rights Accountability

Ariel Meyerstein*

August 20, 2012

DRAFT: Please do not cite or circulate without author’s permission

* Forthcoming, N.Y.U. J. INT’L. L. & POL. (Winter 2013). PhD, UC Berkeley School of Law (Jurisprudence & Social Policy); J.D., UC Berkeley School of Law; B.A. Columbia; ariel.meyerstein@gmail.com. Previous versions of this article were presented at the United Nations Principles on Responsible Investment/Mistra Foundation Dynamics of Responsible Investment Conference, Sigtuna, Sweden (September 25-27, 2011) (awarded best student paper) and a panel on “Global Regulation of Markets and Risk: The Intersection of Public and Private Regimes,” at the Law and Society Association Annual Conference, San Francisco (June 3, 2010). I am grateful to Robert Kagan, Andrew Guzman, Neil Fligstein, Martin Shapiro, Tom Ginsburg and Jodi Short for their comments on previous versions. All views expressed herein are the author’s alone.
GLOBAL PRIVATE REGULATION, GLOBAL FINANCE AND THE FUTURE OF CORPORATE HUMAN RIGHTS ACCOUNTABILITY

ABSTRACT

Large-scale infrastructure projects often impose a variety of environmental and social harms on local, marginalized (often indigenous) populations, many of whom, particularly in countries with weak regulatory capacity, have very little political voice in the project approval process. Responding to pressure from transnational activists and the changing norms and practices of development finance institutions such as the World Bank, some of the largest commercial banks in the world created a global private regulatory regime—the Equator Principles (“EPs”)—to standardize their review of the environmental and social risks flowing from their investments in these projects. This Article contextualizes the emergence of the Equator Principles among the broader shift to new forms of global governance and explores how the impact of such governance regimes can be measured. Drawing inspiration from recent scholarship by regulation scholars of domestic voluntary regimes, the Article explores how “process”-focused metrics can be an important measurement of regime effectiveness.

Implementing this empirical approach, the Article presents the first global survey of the implementation of the participating banks—Equator Principle Financial Institutions (“EPFIs”)—measured along two dimensions: (a) how individual institutions have changed their organizational structures, policies and procedures following their decisions to adopt the EPs and (b) how they have contributed to the growth and evolution of the regime. While institutional change is not a perfect proxy for measuring impacts “on the ground,” I argue that it is a particularly useful measurement for the study of global private regulation related to corporate human rights accountability, which both the United Nation’s Guiding Principles on Business and Human Rights and the OECD’s Guidelines for Multinational Enterprises suggest should be carried out primarily by the development of robust due diligence mechanisms not unlike those required by the Equator Principles.
Table of Contents

I. Introduction .......................................................................................................................... 2

II. Global Governance Gaps and the Emergence of the Equator Principles .......................... 9
   A. The Origins of Problem Projects ................................................................................. 9
   B. From the World Bank to Commercial Banks: The Sustainable Development Agenda Strikes the Private Sector ................................................................. 13
   C. The Normative Content of the Equator Principles ....................................................... 16
   D. Evolution of the Equator Principles ............................................................................ 17
   E. Persisting NGO Concerns and Future Evolution ......................................................... 20

III. The Rise of Self-Regulation and The “Greenwashing” Debate ...................................... 22
   A. The Demands for Governance and the Rise of Self-Regulation ................................. 22
   B. A Taxonomy of Global Private Governance .................................................................. 24
   C. The “Greenwashing” Debate ....................................................................................... 27
   D. Strong Swords and Weak Swords ............................................................................... 30
   E. Looking Beyond Outcomes in Measuring Regime Effectiveness .............................. 31
      1. Data Availability and Measurability .......................................................................... 33
      2. The Challenge of Measuring Outcomes .................................................................... 34
      3. The Politics of Measuring Outcomes ....................................................................... 35
      4. The Threat of Decoupling ....................................................................................... 37

IV. Research Design .............................................................................................................. 39
   A. Methodology ................................................................................................................. 39
   B. Data Limitations ........................................................................................................... 41
   C. Further Data Considerations ....................................................................................... 42

V. Discussion of Findings ...................................................................................................... 44
   A. Individual Institutional Growth in Environmental and Social Risk Management (ESRM) ......................................................................................................................... 44
      1. ESRM Personnel and Policies .................................................................................... 44
      2. Training ...................................................................................................................... 45
      4. Depth of Due Diligence ............................................................................................ 45
      5. Reporting .................................................................................................................. 47
   B. Other Measures of Regime Effectiveness: Social Interactive Processes and Regime Building ............................................................................................................... 52
      1. Creating a Regime-Sustaining Ethos and Platform For Social Learning ...................... 52
      2. Measuring Frequency and Quality of Peer Contact .................................................. 53
      3. Gauging “Civic Duty” Among EPFIs – Increased Formalization and Enhanced Governance .............................................................................................................. 55

VI. Conclusion: Financiers as Policymakers and the Rise of Human Rights Due Diligence ......................................................................................................................... 57
I. INTRODUCTION

The global financial crisis is widely characterized as having been precipitated by a period of deregulation of global financial institutions\(^1\) coupled with the epidemic-like spread of high risk transactions\(^2\) and what can now be safely identified as a misguided blind-faith by key regulators that these institutions and “the market” more broadly would self-correct such system-threatening practices.\(^3\) In other words, the pre-crisis and crisis periods have been characterized as an era of rampant and reckless irresponsibility. As this Article will demonstrate, an under-appreciated narrative of this same period is, ironically, the rise of global financial institutions as integral actors and even policy-makers addressing the intersection of foreign direct investment and issues of human rights, sustainable development and even climate change. While it is too early to tell whether these immensely powerful institutions have deeply internalized the concept of “responsibility,”\(^4\) there are significant trends in that direction that merit closer evaluation.

\(^1\) Although the causes of the 2008 global financial crisis are complex and beyond the scope of this Article, two pieces of federal legislation—The Gramm–Leach–Bliley Act (“GLB Act”), also known as the Financial Services Modernization Act of 1999, and the Commodity Futures Modernization Act of 2000—have been identified as having had significant effects that enabled many of the other causes of the crisis to have amplified ramifications. See Marcus Baram, *Who’s Whining Now? Gramm Slammed By Economists ‘Nation of Whiners’ Comments Criticized by Finance Experts in Light of Current Crisis*, ABC News (Sept. 19, 2008), at http://abcnews.go.com/print?id=5835269 (quoting Nobel Prize-winning former chief economist of the World Bank, Joseph Stiglitz, as stating that “as a result” of GLB, “the culture of investment banks was conveyed to commercial banks and everyone got involved in the high-risk gambling mentality. That mentality was core to the problem that we’re facing now”); see also Mark Summers, *John McCain: Crisis Enabler*, THE NATION (October 6, 2008), at http://www.thenation.com/article/john-mccain-crisis-enabler (noting that by passing the GLB Act the “deregulators” “chose to create monster bankeragurance businesses whose downfall (and existence) was enough to threaten the whole system” and that the Commodity Futures Modernization Act provided these institutions with the “needed fuel” by shielding risky transaction such as “credit default swaps” from regulatory scrutiny, which in turn made it easier and more convenient for these large institutions to share these instruments and their attendant risks, thereby encouraging the banks to seek out new sources of risk, which flooded the housing market with easy credit, leading to the creation of the mortgage-backed securities market and the derivative market for trading the default swaps, even though no one really knew how to properly value them).

\(^2\) See generally MICHAEL LEWIS, THE BIG SHORT (NORTON 2010).

\(^3\) See Congressional Testimony of Alan Greenspan, former Chairman of the Federal Reserve, on Thursday October 23, 2008 (“I do have an ideology. My judgment is that free, competitive markets are by far the unrivaled way to organize economies.... And what I'm saying to you is, yes, I found a flaw. I don't know how significant or permanent it is, but I've been very distressed by that fact.... [A] [f]law in the model that I perceived is the critical functioning structure that defines how the world works, so to speak.”).

This Article provides an historical and theoretical context to support this claim by tracing the emergence of the Equator Principles (“EPs”), a voluntary regime of global private regulation adopted by multinational banks to standardize their environmental and social risk management of their investments in large-scale infrastructure projects in developing economies. The Article first evaluates the impact of the EPs on the regulation of foreign direct investment (“FDI”) with empirical data on the changes that adopting institutions, known as Equator Principles Financial Institutions (or “EPFIs”), have undergone since adopting the EPs. The Article then considers the broader implications of the EPs’ rise for the global private regulation by corporate actors—particularly those in the financial sector—over issues of human rights and sustainable development.

Unlike cross-border trade in goods and services (regulated by the World Trade Organization), FDI has never been subject to a comprehensive multilateral governance regime. A particularly problematic subset of FDI is “project finance”—bank lending through loans and bonds for large-scale infrastructure projects, such as mines, oil pipelines and hydroelectric dams. The incapacity of the regulatory systems in many of the host countries in which these projects are built results in “problem projects” developed in an unsustainable fashion, causing unnecessary harm to local populations and ecosystems by forcefully dislocating people from their homes, ancestral lands and way of life, and in some instances threatening to destroy irreplaceable cultural sites, unique habitats or species.

According to United Nations High Commissioner for Human Rights Navi Pillay, “many of the estimated 370 million indigenous peoples around the world have lost, or are under imminent threat of losing, their ancestral lands, territories and natural resources because of unfair and unjust exploitation for the sake of

---

5 Other similar codes or voluntary initiatives exclusively involving financial institutions can be cited as well, such as the Wolfsberg Principles and the United Nations Principles for Responsible Investment, but the focus here is on the EPs.


8 Natalie Bridgeman & David Hunter, *Narrowing the Accountability Gap: Toward a New Foreign Investor Accountability Mechanism*, 20 GEO. INT’L ENV’T. L. REV. 187 (2008). This is particularly so in the case of the extractive industries. Indeed, nearly half of all existing complaints by individuals against corporate actors that have been registered with National Contact Points under the OECD Guidelines for Multinational Enterprises, a global soft law human rights instrument applicable to corporate actors, have involved the extractive sector. See Institute for Human Rights and Business, OECD NCP Norway Workshop Report: OECD National Contact Points and the Extractive Sector (23 March 2012), available at http://www.ihrb.org/pdf/IHRB-NNCP-OECD-National-Contact-Points-and-the-Extractive-Sector-FINAL.pdf (last visited 8 July 2012).
‘development.’”  Problem projects can be found at the epicenters of national and international conflicts throughout the world, some of them violent.  The effects of this global governance gap have become more pronounced as FDI has come to outpace Official Development Assistance (“ODA”) by bilateral donors.  After years of mounting pressure, by the turn of the new millennium NGOs had successfully pressured the World Bank Group to enhance its environmental and social policies and procedures related to large project financing.  But this achievement was only partial and left a governance gap with respect to the environmental and social risk management (“ESRM”) deployed by commercial banks, which had been increasing their role in financing projects since the 1990s.

To address this disparity, NGOs launched a series of public advocacy campaigns directed at the leading commercial lending institutions, all of which were invested to varying degrees in problem projects.  In 2003, in response to this pressure, these and other market-leading institutions created the EPs. The goal, as the name suggests, was to “level the playing field” by establishing one standard of project review that would apply globally, i.e., on both sides of the Equator. The regime has grown from ten initial founding members with about 30 percent of the global market share to 77 institutions from over 30 countries whose transactions now cover 70 percent of all emerging market project finance transactions.

The EPs are a paradigmatic example of the phenomenon of global private regulation, also called “transnational ‘new governance’.” As with the broader

10 See infra Part II.A and B.
11 See infra Part II.C.
15 Kenneth Abbott & Duncan Snidal, The Governance Triangle: Regulatory Standards Institutions and the Shadow of the State, in THE POLITICS OF GLOBAL REGULATION (WALTER MATTLI & NGAIRO WOODS, EDs., 2009); see infra Part III.B.
phenomenon of global private regulation,\footnote{16} the EPs have only started to garner scholarly attention and there thus remains considerable uncertainty over the EPs’ true impact. To date, no prior research on the EPs has provided a systematic, global empirical study of their implementation by participating institutions.\footnote{17}


17 The earliest research on the EPs first focused on the various strategic motivations compelling the banks to adopt them. See Franck Almaric & Jason Hauser, Economic Drivers of Corporate Responsibility Activities 20 JOURNAL OF CORPORATE CITIZENSHIP 27-38 (2005); Benjamin C. Esty, Carin-Isabel Knoop, Aldo Sesia, Jr., The Equator Principles: An Industry Approach to Managing Environmental and Social Risks (Harvard Business School Publishing Case No. 9-205-114; Teaching Note No. 5-205-115; Technical Note No. 205-065) (2005); Benjamin C. Esty, An Overview of Project Finance & Infrastructure Finance - 2006 Update, Harvard Business School (2007). Later research performed a neoinstitutional analysis of the patterns of adoption among the first banks to join, offering strong support for the view that they were created “as tools for maintaining or enhancing corporate reputation in institutional environments where it is threatened,” that is, in countries with well developed governance and open societies, i.e., in Europe and North America, where regulation was strong and NGOs flourished. See Christopher Wright & Alexis Rwabizambuga, Institutional Pressures, Corporate Reputation, and Voluntary Codes of Conduct: An Examination of the Equator Principles, 111 BUSINESS & SOCIETY REVIEW (00453609) 89 (2006). Other scholars conducted a financial analysis of the adopting institutions in comparison with other banks to determine whether the EPFIs were really different based on their cost outlays, although the utility of this comparison is perhaps minimized because it was impossible for these scholars to isolate the expenses related specifically to project finance risk management as opposed to other institutional overhead related to other business products (after all, project finance typically occupies only 1-5% of banks’ balance sheets). See Bert Scholtens & Lammertjan Dam, Cultural Values and International Differences in Business Ethics (2007). A project finance lawyer familiar with the bankers at the leading EPFIs has also issued various insightful reports largely based on interviews with a number of insiders that highlighted important policy aspects of the regime and anticipated some of its shortcomings and challenges. See Paul Watchman, Angela Delfino, & Juliette Addison, EP2: The Revised Equator Principles: Why Hard-Nosed Bankers are Embracing Soft Law Principles, LAW AND FINANCIAL MARKETS REVIEW (2007). Another article has used a legitimacy analysis to trace the evolution of the EPFIs’ relationships with their main interlocutors: the NGOs. See O’Sullivan & O’Dwyer, supra note 13. Most recently, a study focused on the content of the annual sustainability reports produced by a couple Equator banks. See Richard Macve & Xiaoli Chen, The “equator Principles”: A Success for Voluntary Codes?, 23 ACCOUNTING, AUDITING & ACCOUNTABILITY JOURNAL 890 (2010). A more recent article has provided the initial findings from interviews with “fifteen bankers; two NGO representatives; two government officials, one of whom is a scientific advisor; another private-sector scientist who consults on EPs projects; four lawyers who practice in the field; one World Bank Group official; one consultant to the IFC on its environmental performance standards; and three investment advisors.” See John M. Conley & Cynthia A. Williams, Global Banks as Global Sustainability Regulators?: The Equator Principles, 33 LAW & POLICY 542 (2011). Most recently, the EP Association itself engaged very knowledgeable and experienced consultants to do a “Strategic Review” of the regime. Suellen Lazarus & Alan Feldbaum, Equator Principles Strategic Review: Final Report (17 February 2011), at http://www.equator-principles.com/resources/exec-summary_appendix_strategic_review}
This Article provides such an empirical assessment by gathering data on
(i) institutional changes to EPFIs’ policies and procedures, (ii) interactions
between the adopting institutions within the regime, and (iii) interactions with
external stakeholders, principally NGOs.

The EPs are particularly significant among other nascent global private
regimes because they target what are arguably the key actors in the global
economy: multinational banks. Whereas most voluntary codes affect just one
industry (e.g., the Kimberley Principles’ focus on diamonds or the Forestry
Stewardship Council’s focus on forests), the EPs, in the words of then-IFC Vice
President Peter Woicke, affect “dozens, ranging from forestry and manufacturing
to infrastructure and extractive industries.” In his view, they are “far and away the
biggest response by the private sector to the globalization debate.” In addition,
Woicke noted, the “amount of investment [the Equator Principles] will affect is
massive. Even if you use an extremely conservative estimate, [the Equator
Principles] will change the rules of the game for about $100 billion in global
investment over the next 10 years.” It should also be kept in mind that national
decisions about infrastructure development are inherently tied to the global
economy. Thus, for example, to the extent that financiers have started to exercise
influence over the kinds of energy projects that are built or the relative
environmental impacts caused by projects, they have an increasingly powerful
role in shaping global climate policy.

Given their importance to global affairs, the aim of this Article is to
provide an empirical assessment of the extent to which the Equator Principles
have contributed to the global governance of infrastructure development. In the
process, it also aims make theoretical contributions to the study of global private
regulation. In particular, the article builds upon recent work by regulation
scholars who have argued for taking a broader view of the possible contributions
of domestic self-regulatory regimes rather than focusing too obsessively on short-
term “outcomes.” Studying outcomes in this global regulatory context is
particularly challenging, but so is the subsequent question of discerning the
various other metrics by which self-regulatory regimes can be measured,
including, but not exclusive to outcomes. I propose a few such measures and
present data on how the Equator Principles fare in light of these metrics.

The Article proceeds in several parts. Part II presents a diagnosis of
“problem projects”—the specific global governance gap related to large-scale
infrastructure projects the Equator Principles were created to address. This Part
also traces the spread of sustainable development practices from the global

---

18 Esty, Knoop, Sesia, Jr., supra note 17.
19 Thomas P. Lyon & John W. Maxwell, Environmental Public Voluntary Programs
Reconsidered, 35 POLICY STUDIES JOURNAL 723 (2007).
20 See infra Part IV and V.
development finance institutions, principally the World Bank Group, to commercial investment banks that lead to the emergence of the Equator Principles. It then describes the history of the regime, its normative content and the persisting concerns NGOs have about it.

Part III begins by providing an historical and analytical framework for understanding the emergence of self-regulation, which is a story about the quest for organizational legitimacy and maintenance of collective industry reputation. Historically, self-regulation has developed in response to legitimacy crises in particular industries, which affect the most visible firms disproportionately to others and force them to take action to preserve their reputations and their “social license” to operate.21 But the mere formation of such governance “clubs” is often not sufficient by itself to maintain legitimacy; rather, the informational asymmetries of typical market conditions22 persist and industry clubs must develop some mechanism to effectively signal the differences in the behavior of the club’s membership and that of “bad apples” in the industry.

The rest of this Part then provides a brief sketch of the landscape of global private regulation and the “greenwashing” debate over the effectiveness of self-regulation in both the domestic and transnational contexts. Though results have been mixed, the prevailing view of self-regulation from domestic contexts (and some evidence from transnational contexts) has been skeptical of the power of self-regulation. However, recent scholarship in the domestic context has sought new ways to appreciate the effects of private regulation that look beyond “outcomes,” the traditional focus of scholars in this relatively young field. These process-oriented scholars have argued that too narrow a focus on the outcomes of voluntary programs or self-regulation can overshadow other potentially useful ways of understanding regime effectiveness and impact.

Part V applies these theoretical and methodological insights to studying the EPs and other global private regulatory regimes and lays out the study’s methodology. I argue that outcomes are hard to study not only because the banks’ client confidentiality concerns prevent linking their overall internal processes with decision making about particular projects, but also because outcomes in this context are an inherently unstable unit of analysis: defining project successes and failures entails a very subjective and politicized determination that varies with different stakeholders’ viewpoints. In addition, the “big tent” approach of many private regulatory regimes, which seeks to bring as many actors into the fold with appealing low entry costs in the hopes of later “ratcheting-up” standards, suggests that longer time horizons are needed to study regime impact. Thus, hasty...

---


conclusions focused on either end results and/or too-short time horizons risks missing the broader evolutionary narrative that many self-regulatory institutions and voluntary regimes undergo.\textsuperscript{23}

The remaining challenge, which this article begins to address, is to identify the metrics other than outcome metrics that might be indicative of private regime effectiveness or impact. Although other measures could be discussed as well, Part VI of the paper presents data tracking two general kinds of metrics of both individual institutional change and regime-wide dynamics: (i) evaluating implementation of the EP norms through changes EPFIs have made in their ESRM policies, procedures and organizational structures; and (ii) examining the utility of the regime as a mechanism for social learning among participants and non-participants, which includes measuring the individual institutions’ contribution to regime-building activities and outreach to both participants and non-participants.

In line with the insights of signaling theory in economics, I argue that in situations such as this, when the banks’ environmental and social outputs are somewhat obscured from observation and are only available as post-experience goods, the expenditures involved in implementing the regime would not be rational to incur if they were not serious about implementation.\textsuperscript{24} While the EPs do not mandate such expenditures and have not as of yet implemented mandatory certification of policies and procedures, they are nonetheless inherent to properly implementing the EPs. In short, if participating institutions are not expending significant resources and dramatically transforming their institutional structures and procedures, it is likely that they are not taking their commitment to the EPs seriously. While institutional change is not a perfect proxy for measuring impacts “on the ground,” I argue that it is a particularly useful measurement in the context of the newest formulations of the responsibilities of corporations to respect human rights norms, namely, the United Nations’ Guiding Principles on Business and

\textsuperscript{23} See generally Steven Bernstein and Benjamin Cashore, \textit{Can non-state global governance be legitimate? An analytical framework}, 1 REG. & GOV. 347-71 (2007) (describing the paradigm of “non-state market driven” governance, which they describe as “dynamic governance” wherein actors “purposely steer themselves toward collective goals and values and in which adaptation, inclusion, and learning occur over time and across a wide range of stakeholders.”); see also Abbott & Snidal, \textit{supra} note 15, at 63-64 (noting that while terms within their effective governance paradigm such as “monitoring” and “enforcement” evoke the “logic of consequences” built on sanctions, the governance process can also “accommodate a ‘logic of appropriateness’... In schemes built on appropriateness,... [m]onitoring might aim to communicate the commitment and concern of managers and stakeholders, promoting socialization and an appropriate corporate culture, while [e]nforcement might invoke community approval or disapproval, enmeshing the firm in a normative conversation with customers, investors, and other interested groups. Clearly the two approaches can be mutually reinforcing.”).

Human Rights and the newly revised Guidelines for Multinational Business Enterprises of the Organization for Economic Cooperation and Development. Both sets of principles have emphasized the importance of the procedural process of human rights due diligence, which is what the EPFIs’ environmental and social risk assessments are.

The methodology employed here does not allow for strong causal claims that institutions studied made these changes because they adopted the EPs. The data nonetheless offers proof from across a wide spectrum of the participating institutions suggesting that, while far from perfect, the banks participating in the EPs are engaging in more than mere “greenwashing.” While the EPFIs’ NGO interlocutors are far from satisfied with the rate of change to date, the undeniable fact is that the EPs have permanently and significantly altered the practice of project finance, at least as it is deployed by the vast majority of the largest, most active and influential institutions of global finance in Western Europe, North America and in pockets of Latin America, Asia and Africa. Moreover, while the EPs and the EPFIs should continue to evolve to address the NGOs’ concerns, the NGOs might also have to accept that their role as global ombudsmen and accountability officers might never be completely supplanted by such further evolution. As Abbott and Snidal and others have proposed, contemporary global governance is most often a project of “collaborative governance” in which the activities of different actors endowed with disparate strengths, weaknesses and core missions combine to collectively provide the functions of governance necessary to address problems of global concern.  

II. GLOBAL GOVERNANCE GAPS AND THE EMERGENCE OF THE EQUATOR PRINCIPLES

A. The Origins of Problem Projects

A particularly challenging aspect of large-scale infrastructure development is that it is often undertaken as part of a national growth strategy for the supposed

---

25 See Abbott & Snidal, supra note 15. Abbott & Snidal propose that regulatory processes occur in roughly five-stages (although they do not always occur in an orderly fashion): Agenda-setting, Negotiation, Implementation, Monitoring, and Enforcement (a process they short-hand as “ANIME”). Truly effective regulatory schemes, they argue, must address all five stages. Throughout these stages, actors (States, firms and NGOs) involved with governance regimes to varying degrees can exhibit four competencies: independence, representativeness, expertise, and operational capacity. Abbott & Snidal consider all of these competencies—which vary in their importance depending on the stage of the ANIME process—to be necessary, though not sufficient for a regime to be effective (63). The authors then assess the competencies of the primary “actor groups” (states in both the domestic and international context, firms and NGOs) throughout the various ANIME stages. They note that collective actors might possess different competencies than those of their members (for example, they note that “industry associations may be relatively independent of particular firms”).
benefit of an entire country, but the project must be located somewhere, and inevitably, that somewhere is often the backyard of indigenous peoples or other marginalized populations. However, the regulatory frameworks in place in developing countries are often not up to the task of enforcing international or national environmental and human rights laws relevant to the development of large-scale infrastructure projects, and as a result, project-affected populations often have no political voice in determining whether, where and how a project should be constructed. When project planning is not carefully done, problem projects result, often entailing environmental degradation, forceful dislocation of people from their homes, ancestral lands and way of life, and in some instances, destruction of irreplaceable cultural sites, unique habitats or species.

In many developing countries effective project-level impact assessment remains a distant dream. While there are laws on the books and environmental regulators exist, that is often where the regulatory impacts end. A recent World Bank survey of thirty-two oil-producing developing countries found that most of the countries surveyed had a “sufficiently appropriate, but largely theoretical, environmental policy and legal framework” in place for managing impacts of the oil and gas industry which often had been transposed from more developed countries.

---

26 The IFC Performance Standards Guidance Note 7 provides a useful description of how indigenous peoples are vulnerable to project development:

Indigenous Peoples, as social groups with identities that are distinct from mainstream groups in national societies, are often among the most marginalized and vulnerable segments of the population. In many cases, their economic, social, and legal status limits their capacity to defend their rights to, and interests in, lands and natural and cultural resources, and may restrict their ability to participate in and benefit from development. Indigenous Peoples are particularly vulnerable if their lands and resources are transformed, encroached upon, or significantly degraded. Their languages, cultures, religions, spiritual beliefs, and institutions may also come under threat. As a consequence, Indigenous Peoples may be more vulnerable to the adverse impacts associated with project development than non-indigenous communities. This vulnerability may include loss of identity, culture, and natural resource-based livelihoods, as well as exposure to impoverishment and diseases.

IFC Performance Standards Guidance Note 7 – Introduction.

27 Bridgeman & Hunter, supra note 8; Miles Scott-Brown & Marcello Iocca, Environmental Governance in Oil-Producing Developing Countries: Findings from a Survey of 32 Countries (Washington, D.C.: World Bank, 2010).

28 See Scott-Brown & Iocca, supra note 27 (emphasis added). The countries surveyed were assessed in comparison to “ideal” governance benchmarks synthesized from the practices of Brazil, Canada, Italy, Malaysia, and Norway. The surveyed countries included: Argentina, Algeria, Angola, Afghanistan, Colombia, Egypt, Arab Rep. Cameroon, Azerbaijan, Ecuador, Syrian Arab Republic, Congo, Rep. Cambodia, Mexico, Yemen, Rep. Gabon, China, Peru, Mauritania, Indonesia, Trinidad and Tobago, Nigeria, Kazakhstan, Venezuela, R.B. de São Tomé and Principe, Papua New Guinea, Philippines, and Thailand.
But such transplants of legal rules and institutions had been ineffective in most of the countries surveyed. Many had dedicated institutions in place for managing the environmental and social impacts of the oil and gas industry, such as a ministry of environment, but these systems existed primarily on paper, and the institutions on the whole were found to be “empty boxes” whose regulatory effectiveness is “compromised by the lack of a sufficiently organized administrative structure that enables efficient regulatory compliance and enforcement,” and further undermined by “the lack of the human and financial resources needed for effective environmental governance.”

Indeed, the survey found that in many countries, much of the emphasis of any impact assessment process “appears to be directed toward regulatory approval of oil and gas projects rather than toward developing a life-cycle approach for minimizing environmental and social impacts across the entire project life.”

Indeed, host country governments are often directly involved in project development through profit-sharing agreements, or more illicitly, through corruption. Such involvement of host country governments and officials creates a perverse incentive to approve projects as quickly as possible because the faster a project reaches completion and begins producing its outputs, the faster the payments will flow to the host country government, sub-governmental entity or perhaps, illegally, to individual officials’ private coffers, leading to an inequitable distribution of wealth and the attendant social problems known as the “resource curse.”

Problem projects are also often the epicenters of conflicts throughout the world, some of them violent. For example, civil and ethnic conflict in Burma has escalated along with the proposed plans by Thai, Chinese and Burmese companies to generate electricity for Thailand by developing a cascade of five dams on the Salween River that runs between Burma, Thailand and China. According to the international NGO International Rivers, the proposed dams in Burma are located in active civil war zones and militarization has increased in these areas since project development started, which allegedly occurred in secret and without any community involvement or consultation.

---

29 Id. In 89 percent of the countries responding, the responsible institutions for environmental management have little (74 percent) or insufficient (15 percent) resources (budget, staff, training, technology, information systems, etc) to effectively implement their strategies and fulfill their regulatory mandate.

30 Id.


32 See generally, International Rivers, Salween Dams, http://www.internationalrivers.org/en/southeast-asia/burma/salween-dams. The Salween (known as the Nu River in China and the Thanlwin River in Burma), the longest undammed river in Asia, runs from the Tibetan mountains in Burma through to the Adaman Sea off the west coast of Thailand and supports almost 10 million people—mostly ethnic minorities—with its rich fisheries and fertile farmland. International Rivers reports that ethnic minority groups, who are already marginalized and repressed by the Burmese military junta, are “not only being systematically and forcibly moved from their homes, but also robbed, tortured, raped or executed.” See id. NGOs warn that local
While investors in problem projects have for decades benefited from a increasingly comprehensive regime of legal protections provided by bilateral and multilateral investment agreements, project-affected communities have virtually no effective judicial remedies for their grievances at the international level. This governance gap is perfectly illustrated by the case of the paper pulp mills on the Uruguay River, which has engulfed in dispute that otherwise calm border between Argentina and Uruguay. What is significant about this case is the exhaustive list of legal and quasi-legal mechanisms the opponents of the projects utilized in their attempts to create accountability over the pulp mills’ alleged impacts: national courts in Argentina and Uruguay, the Inter-American Commission on Human Rights, and the Organization for Economic Cooperation and Development’s Guidelines for Multinational Enterprises’ National Contact Points in Finland, Sweden and Norway, among others. Ultimately, however, none of these mechanisms, including the International Court of Justice, was in the position to actually help these communities or resolve the conflict between two otherwise cooperative neighboring states (never mind the broader conflict between local communities, the project sponsors and their financial backers). However, the negative publicity brought by the transnational campaigns and the mere initiation of some of these accountability mechanisms was too much for some of the funders to bear, and so they withdrew their support. Nevertheless, the circumstances surrounding the Paper Pulp Mills case illustrate perfectly the fractured nature of global governance over foreign direct investment in large-scale infrastructure projects, and the inadequacy of current accountability mechanisms and governance regimes.

To be sure, many countries have struck upon ex ante bargains and resolutions to these conflicts by empowering government entities at various levels with some form of the power of eminent domain. However, this power can be wielded more or less equitably and transparently. If national institutions fail to address citizens’ concerns, or if they only nominally address insufficiencies in project approval processes with only the most bare approximation of the rule of law, then conflict will no doubt ensue. Even if processes are relatively robust, local and transnational activists may still be dissatisfied with the results, at which point they can also internationalize the struggle by seeking accountability from ethnic groups, particularly in regions that are not ethnically Burmese and typically enjoy considerable autonomy over their own affairs, could lash back in resentment at what are perceived to be deals that do not provide any local benefits and worse, trample on their rights in the process. Indeed, in April 2010, a series of bombs exploded at the site of a controversial hydropower project sponsored by a Chinese company. As one expert explained the violence, “[w]hen you're in a situation where you can't retaliate against your own government, you can retaliate against perhaps investment by outsiders.” Reuters, China risks backlash with Myanmar investments, July 9, 2010, at http://af.reuters.com/article/energyOilNews/idAFTOE66804H20100709?sp=tru.


transnational regimes and courts, directly from private actors, or in the global court of public opinion and through reputation-based market forces. As the next section describes, this is gradually what transpired from the 1980s-2000s.

B. From the World Bank to Commercial Banks: The Sustainable Development Agenda Strikes the Private Sector

The vision of large-scale development exported by the World Bank and other development institutions for most of the latter half of the 20\textsuperscript{th} century gave rise to popular movements opposing “big development.” These movements from all over the global South began demanding that the World Bank comply with the principles of sustainable development articulated first through the Stockholm Declaration of 1972 and later vigorously reaffirmed in the Rio Declaration of 1992. Later, the “anti-” or “alter-” globalization movement (also known as the “global justice movement”) reached its apex at the “Battle of Seattle” in November 1999, with activists violently protesting against the perceived harms threatened by what they described as the neoliberal agenda of the World Trade Organization and other international organizations. These demands led to the creation of accountability mechanisms such as the World Bank’s Inspection Panel, the International Financial Corporation’s Compliance Advisor Ombudsman and a host of continually updated environmental and social policies. These mechanisms have provided some limited means for affected communities to have project approval processes reviewed, but they often have been belatedly applied Band-Aids that do not quite achieve “justice” in the eyes of project-affected populations.

Just as some progress was being made in incorporating sustainable development concerns in development finance institutions, loans to private sector entities by commercial lenders began to supplant public development financing.

---


In 1990, for every dollar of Official Development Assistance from multilateral development banks and the International Monetary Fund there was less than one dollar of long-term private capital flows of FDI. However, already as of 2003, FDI had eclipsed ODA four times over.\textsuperscript{39}

Indeed, while investment in large-scale infrastructure was for decades a large portion of the World Bank Group’s lending book (particularly its lending to sovereigns for the construction of large dams through the International Bank for Reconstruction and Development (“IBRD’’),\textsuperscript{40} which constituted around 40 percent of the IBRD’s activity until the late 1990s), the IBRD’s involvement in infrastructure investment of all kinds declined sharply in the 1999-2003 period to $5.7 billion per year, or less than 30% of total lending (an all-time-low). The IBRD’s departure from the scene was mirrored by a drastic decline in other official sources of aid to governments, which dropped forty-percent between 1991 and 1997.

This decline has been attributed to the emergence of a global market for private investment in infrastructure spurred by privatization and deregulation of many industrial sectors all over the world and the continued globalization of financial markets through the harmonization of tax regimes and the lowering of restrictions on foreign capital.\textsuperscript{41} Multinational corporations and their financiers, large multinational banks from OECD countries responded to the new favorable investment environment by increasing the financing of infrastructure in developing countries by nine-fold between 1990 and 1997, with annual project finance volumes multiplying tenfold.\textsuperscript{42} At the same time, the World Bank’s private lending arm, the IFC, picked-up the IBRD’s slack in this area along with the rise of privatization, often lending to private entities as part of syndicates in concert with commercial banks.\textsuperscript{43} Indeed, multilateral and bilateral financing of private entities in developing countries nearly tripled in the early part of this


\textsuperscript{40} The IBRD began financing large dams in the 1950s to the tune of over $1 billion per year. The IBRD’s involvement in infrastructure sectors grew slowly from 1970 to 1975 (from $1.5 billion to $2 billion per year, or half of the Bank’s balance sheet), before exploding in the period between 1975 and 1987, quadrupling to almost $8.5 billion and remaining about half of its overall lending activity. This rapid increase can be attributed in part to the Bank’s overall growth: between 1970 and 1985, thirty five countries joined the Bank, including many needing vast infrastructure investments, such as Bangladesh, Hungary, Mozambique, Papua New Guinea, Romania, and Zimbabwe.


\textsuperscript{42} From less than $5 billion to over $50 billion. World Bank, \textit{supra} note 41 (2006). During this period, nearly three-quarters of all commercial infrastructure financing in developing countries came from the United States, France, the United Kingdom, Germany, the Netherlands and Japan.

\textsuperscript{43} Wright, \textit{supra} note 37.
period, with the IFC accounting for nearly one-quarter of all of the multilateral and bilateral financing, which increased further in the ensuing years. Overall, since the global loan and bond markets for infrastructure were first tracked in 1993, they have grown from US $18 billion annually to a peak of over US $251 billion in 2008.

The IBRD’s partial retreat from infrastructure lending was also a result of the substantial reputational costs that these investments had imposed on the institution due to the very public and vocal protests to which the adverse impacts of project development had given rise.

Despite these developments, at the turn of the new millennium there remained a gap between the level of scrutiny applied to project finance transactions by development banks and the processes (or lack thereof) for environmental and social risk review deployed by commercial banks, even though the commercial banks often participated directly in project finance alongside the World Bank Group’s private lending arm – the International Financial Corporation (IFC). With this gap in mind, civil society groups sought to build on their accomplishments vis-à-vis multilateral development banks and focus on private financiers of large development projects. This intent manifested itself in several very public advocacy campaigns against the leading project finance lending institutions. In response, in late 2002 a core group of four banks – ABN Amro, Barclays, Citi (then Citigroup) and West LB – formed a working group to explore the creation of an industry standard for ESRM procedures for commercial banks relying for technical guidance on the IFC. The group decided to base their new framework on the IFC’s Performance Standards because of the utility of having one global standard applicable throughout the entire project finance industry. After further refinement, on June 4, 2003, the senior executives of ten commercial banks met at the IFC in Washington, D.C and formally adopted the Equator Principles.

46 See Project Finance International annual surveys from 1994 through 2009.
47 See O’Sullivan & O’Dwyer, supra note 13.
48 Wright, supra note 37.
49 Id.
C. The Normative Content of the Equator Principles

The Equator Principles’ Preamble states that they were adopted “in order to ensure that the projects we finance are developed in a manner that is socially responsible and reflect sound environmental management practices.” Accordingly, the Preamble declares that “negative impacts on project affected ecosystems and communities should be avoided where possible, and if these impacts are unavoidable, they should be reduced, mitigated and/or compensated for appropriately.” Significantly, the banks were never coy about the mutual benefits of this approach, i.e., their faith in the “business case” for sustainability; the Preamble notes further, “[w]e believe that adoption of and adherence to these Principles offers significant benefits to ourselves, our borrowers and local stakeholders through our borrowers’ engagement with locally affected communities.” The Preamble then hints at the potential for such regimes: “[w]e therefore recognise that our role as financiers affords us opportunities to promote responsible environmental stewardship and socially responsible development.” Finally, the banks make an important qualification about what adopting the EPs means for each institution:

These Principles are intended to serve as a common baseline and framework for the implementation by each EPFI of its own internal social and environmental policies, procedures and standards related to its project financing activities. We will not provide loans to projects where the borrower will not or is unable to comply with our respective social and environmental policies and procedures that implement the Equator Principles.

This closing remark in the Preamble emphasizes that there is no prescribed method or procedure for implementing the EPs; rather, each institution is free to devise the processes it deems most appropriate.

The ten Equator Principles correspond loosely to the various phases of the project finance lending cycle, which also relate to the banks’ project development cycle. The first phase is the lender’s due diligence (EPs 1, 2, 3, & 7), which occurs during the pre-construction activities of project design and permitting. The second phase is loan negotiation and documentation (Principles 4 & 8). The third phase is portfolio management (Principle 9), which correlates with project implementation. The disclosure, consultation, and grievance mechanism requirements (Principle 5 and 6) may apply throughout the lending cycle, depending on the anticipated extent of impacts on local communities. All requirements flow from the first Principle 1, EP1 on the categorization of projects, which dictates that borrowers categorize projects as either Category A (projects with potential significant adverse social or environmental impacts that are diverse, irreversible or unprecedented), Category B (projects with potential limited adverse social or environmental impacts that are few in number, generally site-specific, largely reversible and readily addressed through mitigation measures), or Category C (projects with minimal or no social or environmental impacts). The
relative rigor and applicable law of further risk assessment and mitigation flows from the project’s categorization.

When developing projects in high-income OECD countries, borrowers’ environmental and social risk assessment must comply only with national law as the applicable environmental and social standards governing the project. However, as the examples in the introduction suggest, the national law even in high-income countries is not necessarily an ironclad guarantee against problem projects.\(^5\) Regardless, when a project is being developed in an emerging market context, i.e., a non-OECD country or low-income OECD country, the EPs insist that project sponsors also take into account the International Financial Corporation’s Performance Standards on Social and Environmental Sustainability, which include detailed environmental and social assessment policies and procedures related to specific thematic areas: (1) Social and Environmental Assessment and Management systems; (2) Labor and Working Conditions; (3) Pollution Prevention and Abatement; (4) Community Health, Safety and Security; (5) Land Acquisition and Involuntary Resettlement; (6) Biodiversity Conservation and Sustainable Natural Resource Management; (7) Indigenous Peoples; and (8) Cultural Heritage. Each of these Performance Standards are interpreted by Guidance Notes. In addition, the EPs also reference the World Bank’s Environmental, Health and Safety (EHS) Guidelines, which identify specific performance levels and technical guidance for 63 sectors.

\(D.\) Evolution of the Equator Principles

From the start there were concerns that the EP regime did not go far enough in meeting the ideals expressed in the Collevecchio Declaration, a manifesto announced by 100 NGOs at the World Economic Forum in 2003, which called for financial institutions to recognize their role and responsibility for financing unsustainable projects and other global social problems, from global warming to armed conflicts. In the months following the creation of the EPs, a new coalition of NGOs—Banktrack—formed to monitor sustainability practices.

\(^5\) Another example is the financing by EPFIs of Iceland’s Karahnjukar hydropower scheme that will be based in the Icelandic highlands—the second largest remaining wilderness in Europe. Iceland’s Planning Authority initially had rejected the environmental impact assessment for the project, but the Environment Minister overturned this ruling. Environmental NGOs complain that the project would have substantial impact on several species and others have raised concerns about the socio-economic impacts of the project, which will rely heavily on foreign workers, will provide few jobs for Icelanders after completion, and takes substantial risks on the future price of aluminum: the hydropower plant will be relying largely on the Alcoa smelter, and if the price of aluminum does not rise considerably to meet the project’s estimates, Icelander might ultimately be subsidizing Alcoa’s electricity. See Friends of the Earth and International Rivers Network, Briefing: Barclays and the Karahnjukar project (2004), at http://www.foe.co.uk/resource/briefings/barclays_karahnjukar.pdf (last visited December 21, 2010). It must be emphasized, however, that the project is not strictly being financed through “project finance,” although Barclays, which is helping to arrange the $400 million loan to the project, has stated it will apply the Equator Principles to the project.
in the financial sector. Banktrack quickly designated itself as a watchdog of the EPFIs, releasing report after report analyzing the banks’ implementation and apparent commitment levels.\textsuperscript{51} Banktrack later devoted a special section of its website to featuring “dodgy deals,” serving as a clearinghouse for information on controversial projects, including NGO activities and complaints as well as an opportunity for banks to respond to concerns.\textsuperscript{52}

Unrelenting pressure from the NGO community\textsuperscript{53} and the linkage between the EPs’ normative content and the IFC’s Performance Standards caused the regime to spread beyond its initial Western European core group of banks and “ratchet-up” its requirements. By its first anniversary in June 2004, twenty-five financial institutions had adopted the EPs, including Unibanco, the first emerging market (and South American) bank to adopt. A little over a year later, in November 2005, the first African bank—South Africa’s Nedbank—adopted. Between 2004 and 2006, the EPFIs participated in the IFC’s review and update of its Performance Standards. When in February 2006 the IFC adopted its new Performance Standards (effective April 30, 2006), the EPFIs conducted a further consultation from March to May 2006 with NGOs, clients, industry associations, and export credit agencies which led to the substantially revised Equator Principles II (EPII), which was to be based on the IFC’s updated Performance Standards.

EPII launched on July 6, 2006, at which time forty institutions re-adopted the EPs. The most important revisions in EPII were the lowering of the project cost threshold from fifty to ten million; the extension of the EPs to advisory activities; the inclusion under coverage of upgrades and expansions of existing projects (over those not built under EP review); and perhaps most importantly, the EPs’ first set of “teeth”: Equator Principle 10 – the requirement to report annually on progress and performance—and more robust public consultation standards. When the IFC later updated its Environmental Health and Safety Guidelines in April 2007, the EPFIs incorporated this revision into the EPs as well. In the EPs’ sixth year, in September 2008, Bank Itau-Unibanco S/A, a Brazilian bank that is one of the largest emerging market banks in the world, took the role of Steering Committee Chair. The following month, the first domestic Chinese institution (Industrial Bank) adopted the EPs.

When they were first introduced, the original ten EPFIs represented over 30% of the 2002 project finance market share.\textsuperscript{54} The EPFIs have tried to continually expand their reach through sponsoring conferences in geographic

\textsuperscript{51} See generally Banktrack, The Outside Job: Turning the Equator Principles towards people and planet (Banktrack submission to the Equator Principles update process) (October 2011).


\textsuperscript{53} See Banktrack (2010), supra note 51, for a detailed timeline of interactions.

\textsuperscript{54} See Wall Street Journal (June 4, 2003); Table 2.
areas not known for heightened attention to sustainability, including India, Russia, China and the Middle East. In fact, the EPs, while conducting their own outreach efforts, simultaneously “coordinate closely” with the IFC on outreach activities in the emerging markets, which according to an IFC staffer, allows the IFC to extend its reach with commercial banks in those regions more easily.

The number of adopting institutions has steadily grown over the years and now totals 77 institutions from over 30 countries all over the world that lend to projects in over 100 countries. Their ranks include commercial banks, export credit agencies, and development finance institutions. Currently, the EP website declares that the EPFIs financed over 70 percent of project finance in emerging markets, which is, after all, the area of greatest importance in terms of the Principles’ intended effects of raising global standards of project regulatory review on both sides of the Equator. In 2009, 26 of the top 50 League Leaders,

55 See Koyel Manal, Environmental and Social Risk Analysis for Financial Institutions in India (Centre for Development Finance), at http://cdf.ifmr.ac.in/?project=environmental-and-social-risk-analysis-for-financial-institutions-in-india (last visited Aug. 14, 2012) (noting that “[t]he absence of Indian Financial Institutions from the list of participants in Equator Principles reflects the lack of concern for environmental and social issues. It also reflects the lack of awareness and concern for the environment in general, as there is no pressure exerted on the Project Financiers to adopt Equator Principles or similar environmental initiatives.”).


57 See generally Green Watershed, Environmental Report on Chinese Banks (2011) (Executive Summary), available at http://www.banktrack.org/manage/ems_files/download/executive_summary_for_environmental_report_on_chinese_banks_2011_executive_summary_for_report_2011_report.pdf (last visited August 14, 2012) (noting general improvement across 16 banks since 2009 as measured across 11 indicators, particularly with respect to information disclosure, but observing that “[a]s for environmental policies and measures, except for few banks (e.g. Industrial Bank [an EPFI]), most listed banks still constrained their environmental and social risk management toward credits and investments in policies…[that]…lacked the basic elements for determining, evaluating and preventing banks’ environmental and social risks,” and that these policies “often were not executed efficiently in practice,” and moreover, “[f]ew banks carried out and allocated their environmental and social functions and responsibilities by establishing specialized departments and personnel or by clarifying Green Finance responsibilities for relevant departments.”).

58 A superficial look by a Malaysian commentator noted that in April 2010, a “quick review of ten established Islamic banks in various countries” shows that only one in ten mentioned sustainability in their annual reports. See Nik Sharihzal Sulaiman, Sustainability and Equator Principles in Islamic Banking, The Edge – Malaysia (April 19, 2019).

ranked by the total amount financed by market share were EPFIs, and there were 40 of the top 224 League Leaders were EPFIs, accounting for over 50% of the market; in 2010, there were 42 Equator Banks in the 233 League Leaders, covering 40% of the project loan market.

As much as the EPs have grown to become an industry standard, they have thus far not successfully penetrated key emerging markets where a tremendous amount of project finance and some of the largest individual deals—have been done in recent years, namely, India, China and Russia. In the first quarter of 2011, the top 25 lending banks were split almost evenly between the EPs and Indian and Chinese institutions: Indian and Chinese banks covered 38.6 percent of the market and EPFIs covered 33.9 percent. Moreover, the very largest individual projects sponsored in the first quarter of 2011 were nearly all in either India, China or Russia, with the exception of one project in the United Kingdom, Australia and Singapore, respectively. To date, however, no Russian or Indian banks have adopted the EPs and only one Chinese bank, the Industrial Bank Co., Ltd., has done so. Thus, while the EPs have expanded tremendously in their eight years of existence, the global playing field still has some uneven patches on it, and those patches are where much of the development is taking place and where some of the most vulnerable populations reside.

E. Persisting NGO Concerns and Future Evolution

The NGOs’ complaints about the Principles have remained fairly constant from the start, although some of them have been addressed partially or completely by the EPFIs, leading the perceived legitimacy of the regime to wax and wane over time in the eyes of its main interlocutors. One early success by the NGOs was achieved when the EP Secretariat published its Management Structure on its website in 2007. The Management Structure was the organizational governance structure of the Steering Committee members and a modest secretariat staff (of one person) that divided-up the work of administering, strengthening and growing the EP regime. This governance structure included subcommittees known as Working Groups that focus on various substantive aspects of maintaining and enhancing the EP regime, including Working Groups on (a) adoption, (b) best practice, (c) climate change, (d) outreach (divided again by region), (e) scope review – corporate loans, (f) scope review – export finance, (g) social risks, (h) stakeholders—NGOs, (i) stakeholders—SRI (socially responsible investment), and (j) stakeholders—industry outreach.

The long-standing relations between the EPFIs and the Banktrack network of NGOs reached its lowest point in early 2010 when the NGOs announced a

---

60 See Project Finance International – League Leaders, January 2011 (First Quarter 2011).
61 Id.
63 See generally O’Sullivan & O’Dwyer, supra note 13.
boycott of the EPFIs’ large annual meetings at which the NGOs had become regular participants. Banktrack stated that they no longer believed these large annual meetings to be productive fora for advancing their objectives and announced that they would not participate in them until real progress was made by the EPFIs.

The major persisting criticisms in the NGOs’ eyes are the EPs’ insufficient transparency on the project, institution and regime levels and the related lack of an independent monitoring, verification or enforcement mechanism. The NGOs also find the project level grievance mechanisms insufficient and have criticized the EPs’ limited scope of application only to project finance transactions as opposed to all project-related transactions regardless of financing structure. Finally, they have long complained that the EPs failed to proactively address climate change.

Two of the NGOs’ previously longstanding and most important complaints—the EPs’ lack of a coordinated governance structure and the lack of any enforcement mechanisms—were partially addressed within a few months after the NGOs’ temporary disengagement in early 2010 when the EPFIs’ ad hoc governance structure became even more institutionalized. In July 2010 the EPFIs launched the “Equator Principles Association,” a legally binding governance structure complete with bylaws, voting mechanisms, membership dues, and rules for excluding members found not to be complying with the obligations of membership. This enhanced formalization also responded in part to another of the NGOs’ concerns, as it introduced a de-listing procedure for removing EPFIs who are not compliant with the annual reporting requirement in EP 10. With the launch of the Association, the EPs have drastically improved their operational capacity, one of the four competencies necessary for “effective” regulation according to the model for transnational private governance advanced by Abbott and Snidal. Nevertheless, there remains much room for improvement.

Shortly after the launch of the Association, the EPs underwent a seventh month-long Strategic Review led by external consultants that overlapped in time with the IFC’s comprehensive overhaul of its Performance Standards. The EP

---

65 Id. at 7-9.
66 Id. at 8.
67 Id. at 10-12.
68 Id. at 13-14.
70 See generally Abott & Snidal, supra note 15.
71 See Lazarus & Feldbaum, supra note 17.
Association offered a response to the Strategic Review, but after the revised IFC Performance Standards were finalized, the EP Association launched a further complete update – towards Equator Principles III – to be completed by late 2012, early 2013.

III. THE RISE OF SELF-REGULATION AND THE “GREENWASHING” DEBATE

A. The Demands for Governance and the Rise of Self-Regulation

All research into the problems of governance is in many ways conducted in the shadow of Hobbes’ *Leviathan* and its pessimistic view of the potential for cooperation absent the presence of a Sovereign, or regulator with a monopoly on coercive power to enforce social norms or legal rules. But it is precisely in such a situation of incomplete oversight and emaciated coercive power (or complete lack thereof) that much governance is conducted, particularly in the international sphere which lacks a global sovereign. In such situations, it is argued, a logic of “collective action” governs, with its attendant “free-rider” problems. In “free-rider” scenarios, the benefits extractable from a public good (e.g., clean air and water) exceed the cost of supplying that good, and individual actors, left to themselves, prefer to enjoy the benefits without paying their equal share of the costs. The challenge that arises is to create a cost-sharing mechanism that induces each individual actor benefitting from the public good to pay a fair share of the costs for supplying the good. Elinor Ostrom’s foundational work in the self-regulation of small-scale, commonly held resources, including water, forests and fisheries demonstrates that such institutions and rules can and do arise in the context of commonly-held natural resources.

Similarly, in more complicated markets involving a diffuse set of actors, self-regulatory institutions have emerged in response to a “risk of common sanctions” and informational asymmetries. In any industry, amongst a bunch of bad firms there inevitably are individual “good apples” (or less bad ones), and

---

72 See IFC Performance Standards 2012.
74 See Oran R. Young, Governance for Sustainable Development in a World of Rising Interdependencies, in GOVERNANCE FOR THE ENVIRONMENT: NEW PERSPECTIVES 12 (MAGALI A. DELMAS & ORAN YOUNG, EDs., 2009).
77 Andrew Toffel & Michael W. King, Self-Regulatory Institutions for Solving Environmental Problems: Perspectives and Contributions from the Management Literature, in Delmas & Young, *supra* note 74.
78 Sandler, *supra* note 75.
even though these firms constantly attempt to signal to the public that they
deserve their “social license to operate”\textsuperscript{79} and how they are also far better than
their competitors, an industry as a whole nevertheless can acquire a collective
negative reputation—e.g., the tobacco industry or the financial industry following
the 2007 financial crisis. When this occurs, the stakes of the game change,
particularly for the firms whose reputational exposure is greater than others due to
the scope of their businesses and because of their market share, they have more at
stake in the rise and fall of the industry’s reputation.\textsuperscript{80} These firms constitute a
privileged group.\textsuperscript{81} Because of this heterogeneity and resulting disequilibrium,
the privileged group members have extra incentives to improve the overall
reputation of the industry,\textsuperscript{82} which they might do by unilaterally forming a self-
regulating institution (or governance “club”), through which greater control can
be exerted over the industry’s shared reputation.\textsuperscript{83} The organization of
governance clubs historically has followed “exogenous shocks”\textsuperscript{84} or crises within
the industry that have created the need and opportunity for innovation, which is
often taken advantage of by those in the privileged group because they have more
at stake if there is no response or adaptation to the expectations of external
shareholders that have been revised in light of the moment of crisis or change.

The last half century is littered with examples of industry self-regulation
in the United States that offer support for this theoretical paradigm: rechargeable
battery manufacturers formed a recycling corporation when faced with a regulatory
threat of landfill bans and end-of-life take-back requirements;\textsuperscript{85} the pulp and
paper industry association established a voluntary agreement with the United
States Environmental Protection Agency when faced with more rigorous waste
management standards;\textsuperscript{86} and electric utilities created the Climate Challenge in

\textsuperscript{79} See Kagan, \textit{supra} note 21.


\textsuperscript{81} MANCUR OLSON, JR, \textit{THE LOGIC OF COLLECTIVE ACTION} (1965).


cooperation with the EPA to forestall new legislation related to climate change. This also is clearly what happened among nuclear facilities’ executives in the United States following the Three Mile Island accident. These executives organized to create the Institute of Nuclear Power Operation, which develops standards, conducts inspections, and investigates accidents. Oil industry executives following the Exxon Valdez spill organized in the same way, which led to the creation of the “Valdez principles,” which eventually were renamed the CERES Principles. The Chemical Industry’s Responsible Care program also emerged out of concerns by several different national chemical associations over the possibility of new national laws following the explosion of the Dow Chemical plant at Bhopal, India in 1984.

B. A Taxonomy of Global Private Governance

Because the likelihood that firms perceive an imminent common sanction increases the more similar they consider themselves to be, and because the threat of multilateral action by governments is less likely, it stands to reason that such coordination on a global level would be less common. However, other institutional pressures have substituted for government inaction; where governments have failed to instill sufficient fear in industry, global coalitions of ever more sophisticated activists and non-governmental organizations increasingly have stepped-in proposing innovative, often multi-stakeholder solutions (see Table 1). Thus, both impending government regulation and NGO activism can instill a sense of a “shared fate” among firms that may stimulate these actors, who are almost always competitors, to consider collective action to forestall apparently imminent common sanctions. Additional incentives and benefits have been identified that can be seen as variations on this primary motivation, including firms’ hopes at shaping future regulations, or improving

90 King & Lenox, supra note 79.
91 Toffel & King, supra note 77.
92 Vogel, supra note 16.
94 Toffel & King, supra note 77.
relations with government regulators and with other stakeholders, including consumers, investors, civil society and other firms in an industry.\footnote{Madhu Khanna, \textit{Non-Mandatory Approaches to Environmental Protection}, 15 \textit{Journal of Economic Surveys} 291 (2001).}

The diverse regulatory phenomena that have emerged in response to global regulatory gaps have been typologized as transnational “new governance” or “regulatory standard-setting”\footnote{Abbott & Snidal, \textit{supra} note 15.} and “civil regulation” or “private regulation.”\footnote{Vogel, \textit{supra} note 16.}

They are direct responses to a series of missed opportunities by state actors to collectively create effective regimes of global international business regulation. For example, the Forest Certification Council emerged directly out of the frustration by environmental groups at what they considered to be the complete failure of governments at the 1992 Rio Earth Summit to conclude a binding international treaty on forestry issues. Similarly, the International Tropical Timber Organization developed to overcome objections by timber-exporting countries that more rigorous certification mechanisms would present non-tariff barriers to trade.\footnote{Tim Bartley, \textit{Certifying Forests and Factories: States, Social Movements, and the Rise of Private Regulation in the Apparel and Forest Product Field}, 31 \textit{Politics and Society} 452 (2003).}

What has resulted, however, is a “new global public domain” that does not “replace states” so much as “embed systems of governance in broader global frameworks of social capacity and agency that did not previously exist.”\footnote{John Ruggie, \textit{Reconstituting the Global Public Domain -- Issues, Actors, and Practices}, 10 \textit{European Journal of International Relations} 499-531 (2004).} Indeed, a few of the more well-known initiatives were created in close collaboration with state actors, including the Fair Labor Association (originally the Apparel Industry Partnership promoted by the Clinton Administration), the Extractive Industries Transparency Initiative and Ethical Trading Initiative (both started by the United Kingdom), and the Principles on Security and Human Rights, started with cooperation of the United States and several other governments. Other initiatives were created under the auspices of multilateral international organizations, such as the Organization for Economic Cooperation and Development’s Guidelines for Multinational Enterprises and the United Nation’s Global Compact. Though the Equator Principles are in many ways closer to pure industry self-regulation, such a taxonomy obscures the very extensive role played by the International Financial Corporation (IFC), the private-lending arm of the World Bank Group, in developing them, and thus, the EPs can be seen as emblematic of this public institutional support as well.

It is appropriate, then, that others have theorized these new arrangements of regulatory power as the emergence of a complex “governance triangle”\footnote{Abbott & Snidal, \textit{supra} note 15.} in
which international standards are now created, implemented, monitored and enforced by varying combinations of states, firms and NGOs seeking to transform whole supply chains and global networks of operations spanning multiple jurisdictions.\(^\text{101}\) Others have also referred collectively to these new forms of governance as the “new” corporate social responsibility, identifying seven ideal types.\(^\text{102}\) There are now over 300 such initiatives attempting to introduce governance into nearly every major global economic sector, including energy, the extractive industries, forestry, chemicals, textiles, apparel, footwear, sporting goods, coffee, and cocoa.\(^\text{103}\) One of the most prominent – but also most criticized regimes – is the United Nations Global Compact, which had accumulated over 8,700 participants, of which 6,200 were corporate signatories.\(^\text{104}\) More than 2,300 corporations have endorsed the Business Charter for Sustainable Development created by the International Chamber of Commerce, and over 46,000 firms’ operational plants have received certification as compliant with the International Standards Organization’s 14001 Standard on environmental management systems.

Unlike previous efforts at corporate social responsibility (“CSR”), which were largely about corporate philanthropy, often in pursuit of creating positive publicity about a corporation to counter other publicity, the “new” CSR is about “internalizing a firm’s negative externalities” and directly addressing the problems that arise from a company’s core business activities.\(^\text{105}\) Thus, the scope of the business practices in question can no longer be cubby-holed into discrete problem areas. Rather, they involve labor, environmental and social developmental concerns anywhere within a corporations’ sphere of influence, including supply chains and “business relationships” over which the corporations have “leverage.”\(^\text{106}\) Many of the new initiatives aim to transform entire corporate

\(^\text{101}\) Bartley, supra note 98.

\(^\text{102}\) Graeme Auld, Steven Bernstein, & Ben Cashore, The New Corporate Social Responsibility, ANNUAL REVIEW OF ENVIRONMENT AND RESOURCES 413-35 (2008) (identifying: (1) individual firm efforts (thousands of examples); (2) individual firm and individual NGO agreements; (3) public private partnerships between government or international organizations and firms (EPA star preferred treatment, U.S. voluntary standards program, the Global Compact, United Nations Environment Program Financial Initiative, United Nations Principles for Responsible Investment); (4) information-based approaches (Global Reporting Initiative); (5) environmental management systems (EMSs) (ISO 14001); (6) industry association corporate codes of conduct (Responsible Care, Equator Principles, American Forest and Paper Association’s Sustainable Forestry Initiative, Australian Forestry Standard); and (7) private-sector hard law typologized as non-state market-driven (NSMD) governance (Forest Stewardship Council, Marine Stewardship Council, Fairtrade Labeling Organizations).

\(^\text{103}\) For a list of 31 multi-stakeholder industry initiatives, see Ethical Corporation, Guide to Industry Initiatives in Corporate Social Responsibility (2009), available at www.ethicalcorp.com/initiatives (last visited 8 October 2010).

\(^\text{104}\) See Ten Years of Setting the Record Straight, at http://unglobalcompact.wordpress.com/2010/11/ (last visited 5 November 2010).

\(^\text{105}\) Auld et al, supra note 102.

cultures and approaches to risk management; indeed, the business models of entire industries are purportedly transforming before our eyes, or at least, that is the stated goal. Of course, when these numbers (see Table 1) are compared to the total numbers of transnational corporations in the world—at the end of 2007 there were some 79,000 TNCs engaged in international production, with about 790,000 affiliates abroad, with value added by foreign affiliates accounting for an estimated 11 percent of world GDP—it becomes clear that we are perhaps witnessing the gestation period of the era of corporate social accountability.

C. The “Greenwashing” Debate

But the mere formation of a governance club does not solve the problems of governance. Rather, information asymmetries can persist if the individual and collective performance of firms within a governance club are not transparent; similar to “post-experience goods,” the true commitment levels and implementation activities of participants in such clubs may be hidden from view, causing outsiders to seek assurance about their credibility. Thus, the challenge for industry clubs and self-regulating institutions is the same as that faced by individual firms before organization of the governance regime: to maintain credibility and legitimacy so that their industry-club “brand name” remains pure.

To achieve this, the club must take measures to signal that the “goods” it produces live up to the brand name and do not get diluted by “laggards” who join the club to benefit from its positive collective reputation but fail to meet the standards of membership. Without some mechanism of assuring quality, the regime’s ranks would become bloated with “laggards” looking to “free ride” off the collective reputation of the regime, thus ruining the clarity of the signal sent by individual actors by their decision to participate in the regime, and in the process, any legitimacy the regime might have built. This is, in short, Hardin’s “tragedy of the commons,” where the “commons” freely consumed by all is in fact the legitimacy and reputation of the governance club.

The science of studying self-regulating institutions is still relatively young, particularly with respect to those regimes established to respond to the exigencies of governance arising from economic globalization. With the exception of Elinor Ostrom’s foundational work on successful self-regulation of commonly held resources\(^{109}\) and Joseph Rees study of industry self-regulation in the nuclear power industry,\(^{110}\) as of the year 2000, little research had been done on the potential for self-regulation, particularly by industry associations or other regimes with limited coercive power.\(^{111}\) The passage of a decade has allowed both for the proliferation of many more regimes of self-regulation on the domestic and global levels and an opportunity for scholars to catch-up to the trend.\(^{112}\) Political scientists and business school management scholars have developed a robust literature on *domestic* self-regulation that has focused largely on program outcomes, and, on the whole, has led to a rather dismal view of their effectiveness.\(^{113}\)

The literature on *global* private regulation, however, remains partial and incomplete, with too few studies of private actors’ internal compliance with such regimes\(^{114}\) or comparative studies across regimes.\(^{115}\) Anecdotal evidence on the

\(^{109}\) Ostrom (1990), *supra* note 76.

\(^{110}\) Rees, *supra* note 88.


\(^{113}\) Madhu Khanna & Keith Brouhle, *The Effectiveness of Voluntary Environmental Initiatives*, in Delmas & Young, *supra* note 74.


\(^{115}\) See Büthe, *supra* note 16.
effectiveness of private regulation on the global level is not encouraging: for example, global initiatives in the extractive industry sector, such as the Kimberley Process, the Extractive Industries Transparency Initiative (EITI) and the Voluntary Principles on Security and Human rights have all faced recent legitimacy challenges, as has the United Nations Global Compact, the largest of existing private global governance regimes. Indeed, the more trenchant contemporary critiques of CSR and self-regulation suggest that they are nothing more than increasingly sophisticated “greenwashing” by corporations to demonstrate environmental and social commitments publicly while privately continuing past practices.

While some studies have suggested that codes of conduct and private monitoring can improve conditions for workers on certain conditions, others have pointed to their limitations. Moreover, some worry that the privatization of regulation can only lead to the reification and legitimation of the status quo: business practices that have poor track records with respect to health, safety, human rights and the environment. In addition, the apparent success of some initiatives—such as the Forestry Stewardship Council (FSC)—on further inspection is of limited impact because of their modest scope. The difficulty with much of the scholarship to date, however, has been that it’s been limited to small qualitative studies limited by number of participant plants or firms, or otherwise constrained by geography. In short, the jury is still out and we will need much more empirical work on a global scale to reach a well-considered verdict.

---


117 See Vogel, supra note 16 (citing critics).

118 Rüya Gökhan Koçer & Luc Fransen, Codes of Conduct and the Promise of a Change of Climate in Worker Organization, 15 EURO. J. OF INDUS. REL. 1-20 (2009).


120 See Vogel, supra note 16.

121 Id.
D. Strong Swords and Weak Swords

The first global voluntary program to receive scholarly attention was the Chemical Industry’s Responsible Care initiative, although it was only studied within the context of U.S. chemical companies’ implementation.\(^{122}\) Confirming Hardin’s “tragedy of the commons,” King and Lenox’s study concluded that absent a sanctioning mechanism or a monitoring mechanism, such as third-party monitoring or public disclosure of self-audit information, firms will not likely achieve high levels of compliance with voluntary regulation.

Potoski and Prakash later reevaluated this claim, creating ideal types of voluntary programs based on combinations of possible “swords” — the mechanisms of a voluntary regime that could coerce compliance from participants. These possible swords include third-party monitoring without public disclosure, third-party monitoring with public disclosure, and sanctioning by club administrators: “strong sword” programs, which impose all three possible forms of obligations on club members, “medium sword” programs, which require third-party auditing with public disclosure of results and “weak sword” programs, which require only third-party audits without public disclosures, but do not impose sanctions, and “no sword” programs, which lack all three components.\(^ {123}\) Potoski and Prakash then argued that even a relatively “weak sword” program, such as ISO 14001 – a global environmental management standard adopted by individual firms that has only third-party monitoring without public disclosure of the audit information, may be enough to combat shirking by club members.

When their research demonstrated higher-levels of compliance than would be expected from a “weak sword” program like ISO 14001, they theorized that this was not due simply to the introduction of outside observers, which is known to have an impact on the behavior of the observed party. Rather, they attributed the effect to the fact that the third-party audits in the ISO 14001 regime placed non-trivial costs on those seeking the certification granted by the third-party auditors. As they noted, these audits can be very expensive, and further, the requirement for annual recertification mitigates in part what is lost by having the auditing be completed by third-parties as opposed to a more stringent monitoring and enforcement regime (i.e., one with public disclosure of audit information).\(^ {124}\) The costs of the third-party audits, then, are this regime’s “sword,” albeit a weak one. Thus, Potoski and Prakash conclude that it is clearly essential to any voluntary regime’s success and legitimacy that membership exact real costs from members so that the decision to join the regime remains a meaningful signal that conveys useful information to external stakeholders about the commitments of the regime’s members.\(^ {125}\)

\(^ {122}\) King & Lenox, supra note 82.

\(^ {123}\) Potoski & Prakash, supra note 24.

\(^ {124}\) Id.

Later research has strongly suggested that voluntary programs need some form of mechanism to exact compliance, although it remains unclear whether overt sanctions are strictly necessary. One study found that effective forest certification accreditation programs tend to have third-party oversight, performance standards, and credible sanctions for firms that do not meet program objectives.\textsuperscript{126} A meta-analysis of both first-party and third-party audited voluntary programs noted that the most important conditions for effective strictly voluntary programs are (i) specific performance-based standards; (ii) periodic third-party audits of individual companies; and (iii) rewards that publicly recognize the performance obtained by each participants following third-party verification.\textsuperscript{127}

\textit{E. Looking Beyond Outcomes in Measuring Regime Effectiveness}

But what if the conventional wisdom on voluntary programs and self-regulation is based on a misconceived premise that the \textit{only way} to gauge compliance among participants or the overall efficacy of a regime is by looking at outcomes? These will clearly always remain the gold standard and most important measurements of regime success, but they also presuppose that outcomes and performance can be reliably measured, which includes choosing a realistic time horizon in which to observe the institutionalization of best practices.

Recent studies of voluntary programs have suggested that the focus on outcomes has perhaps been too narrow, potentially excluding observation of the real power and utility of these regimes. \textit{First}, by focusing on the \textit{rate or extent of environmental enhancement}, what is missed is that participation in the voluntary program maybe be a decision made \textit{after} the implementation of enhancements.\textsuperscript{128}

For example, there is empirical evidence in the case of ISO 14001\textsuperscript{129} and in the Environmental Protection Agency’s 33/50 program,\textsuperscript{130} that many participants implemented performance-improving environmental practices \textit{prior} to the existence of the program, which suggests that firms may use membership as a means of capitalizing on the reputational benefits such programs can confer on participants’ \textit{previously implemented} improvements.\textsuperscript{131} Significantly, this is a

---

\textsuperscript{126} P. Tashman & Jorge Rivera, \textit{Are Members of Business for Social Responsibility More Responsible}? 38 POL’Y STUD. J. 487 (2010).


\textsuperscript{128} Id.


\textsuperscript{131} King, Lenox & Terlaak (2005), \textit{supra} note 129.
benefit offered uniquely by the voluntary regime, since absent the regime these improvements could not likely be credibly communicated unilaterally.\textsuperscript{132}

\textit{Second}, the focus on outcomes may overlook evidence related to the importance of the socialization process initiated by the creation of a voluntary program. This socialization process involves external peer and industry-wide forces that pressure program participants to self-regulate in order to gain or maintain a collective “green” reputation among their corporate peers, regulators, and other stakeholders.\textsuperscript{133} It is argued that voluntary programs’ flexible structures enable participants to foster collaborative relationships that promote shared learning and capacity development that can contribute towards better environmental management in the long-term – improvements potentially overlooked by a short-term focus on outcomes.\textsuperscript{134}

\textit{Third}, and more significantly, Lyon and Maxwell have re-oriented studies of voluntary programs to consider their \textit{broader impact}, hypothesizing that if information on pollution abatement techniques does in fact diffuse to nonparticipants as well as participants, then the studies evaluating public voluntary programs (i.e., those sponsored by governments) have arguably pursued empirical strategies that cannot possibly identify the true impact of these programs.\textsuperscript{135} If a public voluntary program is effective in disseminating information about pollution prevention throughout a given sector, then \textit{all} firms would be reducing their emissions at roughly the same rate, which Lyon and Maxwell argue, appears to be the case in the manufacturing sector. If this is what is happening, there would be no evidence that the program participants performed better than nonparticipants, even if the program was achieving meaningful goals.\textsuperscript{136}

Others argue similarly that to study private regulation requires an evolutionary perspective: while a static definition may be easier to operationalize, “it can limit understanding of dynamic change within firms, the interaction of CSR choices with the broader public policy arena and organizational fields … and the motivations for support. These factors are the most important for understanding the sources of behavioral change/commitment and how CSR innovation might lead to direct change or to learning that ultimately is influential

\textsuperscript{132} Nicole Darnall & Stephen Sides, \textit{Assessing the Performance of Voluntary Environmental Programs: Does Certification Matter?} 36 POL’Y STUD. J. 95 (2008).

\textsuperscript{133} Id.

\textsuperscript{134} Id. at 99 (noting, in the context of government-sponsored voluntary environmental programs, that “outside of creating environmental goals and providing technical assistance, VEPs generally establish peer networks among member firms. These networks allow for the exchange of information on best management practices. Information exchange also helps facilitate VEP implementation and may further assist participants in gaining knowledge that helps strengthen their environmental management capabilities.”).

\textsuperscript{135} Thomas P. Lyon & John W. Maxwell, \textit{Environmental Public Voluntary Programs Reconsidered}, 35 POL’Y STUD J. 723 (2007).

\textsuperscript{136} Id.
through other policy innovations and/or governmental processes.” 137 International relations scholars Abbott and Snidal concur: “[i]n examining a highly political activity like regulation, effectiveness must be conceptualized broadly.” 138 Furthermore, they argue, it is difficult to measure “real-world impact” because “too many variables influence the outputs and effects of regulation, and the counterfactuals are too complex.” Given this, they choose to focus on “what attributes, capacities, and skills—what inputs or “competencies”—an institution needs to operate successfully throughout the regulatory process. 139 In their view, by identifying competencies that are “necessary to effectiveness, we can conclude that schemes lacking one or more of those competencies are likely to be ineffective.” They emphasize, however, that the competencies identified are not sufficient for regime success: a scheme that possess all of them might still be paralyzed by infighting, adopt an ineffective monitoring systems or otherwise fail. 140

1. Data Availability and Measurability

Finally, a major challenge in studying the effectiveness of nearly all private regimes is the availability and measurability of data. The availability of public data, in part because many voluntary programs lack monitoring and reporting requirements, has limited empirical work to analyzing a few measures of performance 141 and also explains why so much research into voluntary programs has focused on the question of participation. 142 This challenge is exacerbated in the case of global private regulation such as the Equator Principles, which focus on the notoriously secretive financial sector. Indeed, the greatest challenge posed by studying the EPs—and arguably the greatest challenge to the legitimacy of the regime itself—is that, citing their legal fiduciary duties of client confidentiality, EPFIs (and non-EPFIs) are very guarded about their ESRM practices as they relate to specific projects and borrowers. This guardedness makes the study of “on the ground implementation”—i.e., outcomes, very difficult, as noted by project finance lawyer Paul Watchman:

information on the positive impacts of the EP is scant and difficult to find. This is due to the fact that information in this area tends to be partial, sporadic and not necessarily representative of the full picture concerning a project; a “snapshot” in time rather than a balanced review of the impacts of the project. Furthermore, certain projects tend to receive far more attention than others, perhaps due in part to the fact that NGOs tend to get involved in certain cases – and not others – because they have been requested to do so by movements and

137 Auld et al, supra note 102.
138 Abbott & Snidal, supra note 15.
139 Id.
140 Id.
141 Khanna & Keith, supra note 113.
other organisations on the ground. This highly biased selection process means that many projects which perhaps ought to receive stakeholder attention avoid the spotlight whilst others remain permanently under its glare as coverage about it increases....

However, neither the EPFI nor sponsors help themselves in this regard. The approach of some NGOs in turning a blind eye to the positive impacts of the EP is reinforced by the EPFI which, except in the highest profile cases, evince a reluctance (no doubt, partly based on fears of legal or professional disciplinary sanctions for breaching client confidentiality), to make transparent their dealings with clients in respect of the EP. The approaches adopted by NGOs and the EPFI are matched in some cases by an understandable reluctance on the part of some sponsors to discuss their projects openly with outsiders, even very high profile projects, where a candid exchange of views may have been more beneficial to all parties.\textsuperscript{143}

2. The Challenge of Measuring Outcomes

But even if such data was more readily available, the study of the impact of corporate codes like the EPs is in many ways different from more conventional research into the effectiveness of voluntary environmental programs focused on reducing participating plants’ pollution output, which is readily ascertained through public databases on toxic releases and comes measured in easily quantified units. In contrast, voluntary codes of conduct, though directed at arguably measurable outcomes—i.e., limiting environmental degradation, preventing or minimizing the harms of forced displacement of project-affected populations, etc—primarily seek to produce less-quantifiable outcomes, such as the creation and efficient operation of due diligence procedures and accountability mechanisms. In other words, measuring levels of compliance with the EPs is inherently difficult because of the nature of the obligations imposed by the norms, forcing researchers to identify proxy variables that are correlated or associated with the underlying variables of concern.\textsuperscript{144}

Indeed, the purpose of the EPs and other voluntary codes is to create an approach to project assessment that does not yield concrete results as much as it aims to achieve non-results, if done successfully, that is; if a bank does not demand compliance or lets certain of the borrower’s obligations slide, this will only become a problem if the issue gets ignored or glossed over and becomes a much bigger problem later on, which is far from a certainty and is contingent on many actors and factors beyond the bank’s control. Moreover, many problems develop during the construction phase, putting borrower’s environmental management plans to the test; should things go awry, this may or may not reflect any laxity in the quality of the bank’s initial due diligence in reviewing the project or even the management plan, but rather, reinforces the inherent complexity of large infrastructure projects and the difficulties in constructing them without

\textsuperscript{143} Watchman et al, \textit{supra} note 17.

\textsuperscript{144} JONATHAN C. BORCK, CARY COGLIANESE & JENNIFER NASH, EVALUATING THE SOCIAL EFFECTS OF ENVIRONMENTAL LEADERSHIP PROGRAMS (2008).
complications. Of course, if something does go awry in construction, an EPFI remains obliged to intervene by threatening to declare an event of material default. The downside, however, is that depending on the stage of a project’s development the bank might have more or less leverage over its client (depending on how much of the financing has been disbursed).

3. The Politics of Measuring Outcomes

In addition to the complex array of actors involved in eradicating “problem projects,” the very dependent variable of “problem projects” is inherently unstable because of the competing perspectives of different actors engaged:

The focus of BankTrack, Greenpeace, Friends of the Earth, WWF, Human Rights Watch and the army of NGOs, often is the negative rather than the positive aspects of such projects, on bad news rather than good. In reality, one finds NGO opposition is often based upon political rather than social or environmental grounds (for instance, to developments such as dams and nuclear power stations). Consequently, it is therefore often difficult for the EPFI to satisfy such NGOs by adopting a particular social or environmental objective, given this underlying political agenda.

A perfect example of the subjectivity on outcomes is the San Antonio dam on the Amazon River in Brazil, which is currently under construction and is much heralded for its mitigation of environmental and social risks. The dam will displace 1,400 families, which has raised the ire of an activist group, Movement of the Dam Affected, which has tried, unsuccessfully, to spark protests among those targeted for displacement. One explanation offered for the lack of interest among the soon-to-be-displaced persons is that they currently often live in wooden shacks but the builders of the San Antonio dam are building new riverside communities for them that will include streetlights, and concrete row homes with running water. These plans have even caused even some families in surrounding areas not targeted for resettlement to try to move into the targeted area in the hopes of benefitting from these new homes.

Although it is not unheard of for populations outside a project’s relocation zone to clamor for the same benefits promised to their neighbors who find themselves more directly in harm’s way, the San Antonio dam is quite exceptional in this regard. Nevertheless, in the age of the globalization, what one person—whether a global banker or a local fisherman—sees as harmful development to local lifeways another might seize upon as “progress.” The content of these diverging views cannot be decided upon other than through the transparent, participatory and democratic decisionmaking processes embodied in

145 Watchman et al, supra note 17.
the norm of “free prior and informed” consent (FPIC). But here again, the emphasis is on process and whether project sponsors and banks’ project review procedures ensure for FPIC.

Moreover, it also difficult to account for the unintended consequences of large project construction. For example, the local population of Porto Velho could supply only 30% of the 12,000 workers needed to construct San Antonio. In less well-managed dam constructions, outsiders or foreign workers would be brought in to supplement this shortfall, leading to a wide array of social problems. Anticipating this, the builders of San Antonio dam created a job-training program that has trained 20,000 people. Presently, around 80% of all workers are local, with some people’s incomes rising from $110 a month to close to $750 monthly. Still, like any boom-town development, there are other unintended effects from large-project construction that while being somewhat foreseeable are very hard to mitigate against: upriver from San Antonio the French utility GDF Suez SA (one of the largest water companies in the world) is partnering with a Brazilian company to build another low-impact dam (there are 24 currently planned for the Amazon). On weekends, project workers head into the nearby town of Jaci Parana. This influx has converted Jaci Parana, an ordinarily sleepy place, into a violent center of prostitution.

As suggested, the limitations in studying outcomes in this context counsel towards a focus on process metrics (adoption of particular management practices within institutions) and more broadly, a focus on regime processes. Perhaps the most useful indicator of implementation next to outcome effectiveness is institutional change following adoption of the EPs; indeed, you cannot have successful outcomes without robust institutional change.

This coheres with research from regulation scholars in other contexts. It has been hypothesized that compliance systems might contribute—along with internal values and good management—to improve overall compliance outcomes by improving “compliance management in practice”—how organizational managers and employees “actually manage and respond to compliance issues on a day-to-day basis, whether they notice them, whether they are dealt with according to corporate commitments to compliance, and whether conflicts about compliance are reported up the line and resolved appropriately”. These authors propose tracking implementation of compliance systems along six elements: (a) a written policy, (b) a dedicated compliance function; (c) a clearly defined system for handling complaints; (d) a clearly defined system for handling compliance failures; (e) training in compliance systems; (f) external review of compliance systems.

A parallel analysis was performed in a cross-sectional meta-study of voluntary environmental programs in the United States, which focused on three

---


149 Id.
types of requirements that were most likely to send accurate signals about the participating institutions’ environmental performance, including (1) “environmental requirements” (e.g., “value and goal statements,” setting of a environmental plans or targets, and management systems); (2) “administrative requirements,” which establish communication between programs and include various forms of written agreements, such as memoranda of understanding and membership pledges; and (3) “conformance requirements,” which are determined through various levels of monitoring and sanctions. These indicators fit comfortably with Potoski and Prakash’s suggestion that it is essential to any voluntary regime’s success and legitimacy that membership in the regime extract real costs from members so that the decision to join the regime remains a meaningful signal that conveys useful information to external stakeholders about members’ commitments.

4. The Threat of Decoupling

The immediate challenge that an approach focused on processes must overcome is the phenomenon of “decoupling” identified by neoinstitutional scholars in the late 1970s. The concern these scholars expressed is that organizations might only “ceremonially” adopt the dominant norms and practices in their institutional environments while continuing to act inconsistently with these norms. Similarly, international relations and international law scholars have bemoaned a “compliance gap” between state actors’ signature and ratification of international human rights treaties and their actual respect for human rights. Recent analyses have suggested, however, that decoupling occurs to varying degrees and that the loose conformity between ceremonially adopted practices

150 Nicole Darnall & J. Carmin, Greener and Cleaner? The Signaling Accuracy of US Voluntary Environmental Programs, 38 POLICY SCIENCES 71 (2004).
151 See Potoski & Prakash, supra note 24.
154 Amy Binder, For Love and Money: Organizations’ Creative Responses to Multiple Environmental Logics, 36 THEORY & SOC’Y. 547–571 (2007); Frank Dobbin and John R. Sutton,
and actual organizational activities can later become more tightly linked, i.e., recoupled.\(^{155}\)

Moreover, in analyzing patterns of decoupling between structural commitments and concrete practices in states’ acculturation of global human rights norms and practices, Ryan Goodman and Derek Jinks argue that all instances of decoupling are not necessarily bad: some decoupling is problematic, some is benign and some can even be facilitative.\(^{156}\) Thus, when acculturation (i.e., norm diffusion) leads to a big implementation gap, the analysis does not end but rather, the real question to ask is whether this gap can be expected to narrow over time.\(^{157}\) According to Goodman and Jinks, in the context of state acculturation, there is substantial evidence that in many cases it would, but this will (in the case of States) depend on (1) domestic political opportunity structures (relative openness of institutionalized political system; stability of elite alignments supporting the polity; presence of elite allies for a given movement or issue; the state’s capacity and propensity for repression); (2) the civilizing force of hypocrisy, i.e., internal and external factors audience effects, including consistency in public commitments; (3) escalating demands by global civil society; and (4) evolutionary learning. According to Goodman and Jinks, all of these factors might have analogues in the particular industry contexts.\(^{158}\)

In many ways, the sociological scholarship on “re-coupling” and this more recent (sociologist) international relations scholarship on human rights protection by state actors complements the views of the process-oriented regulation scholars who warn against missing the true impact of private regulation and who suggest that the flexibility and low-commitment levels of some voluntary regulation can be improved upon over time.

Given this theoretical background, this study focuses on two ways to measure a voluntary regime’s impact or effectiveness: (i) evaluating implementation of the EP norms through changes EPFIs have made in their policies, procedures and organizational structures related to ESRM; and (ii) measuring the utility of the regime as a mechanism for social learning among participants and non-participants as well as the increased participation of regime participants in regime-building activities, what I call regime “civic duty.”

---


\(^{157}\) *Id.*

\(^{158}\) *Id.*
This focus is not only recommended based on practical considerations related to data availability and measurability, but also based on the twin realities of global private regulation. First, as noted, the U.N. Guiding Principles on Business and Human Rights’ foremost innovation over past global efforts to impose human rights obligations on corporate actors is their endorsement of an approach or process of human rights due diligence as opposed to endorsing any specific norms of conduct as binding on corporate actors. Second, to the extent that most global corporate self-regulation is embedded principally in global markets as opposed to any one particular jurisdiction, compliance effects will be generated primarily through the reputation and legitimacy-based social processes that are the hallmark of market competition. Thus, individual performance is very much a reflection of what the crowd is doing and how this is perceived by global opinion and by competitor institutions. If this is the primary mechanism by which compliance is achieved then it is fruitful to measure such interactions.

The market-embeddedness of these regimes has a further ramification for how we should study them. Regimes of global corporate self-regulation will only be as effective as their participating institutions allow them to be: they can be funded and organized adequately or in a way that leads only to dysfunction. Additionally, their normative requirements and means of compelling compliance can be more or less robust. Accordingly, what individual participants do to support the regime and help it grow and evolve is arguably as important as what they do individually to comply as subjects of the regime. Measuring these activities in the aggregate is thus a useful way of measuring a regime’s potential for effective regulation.

IV. Research Design

A. Methodology

Data was collected through two phases: a round of qualitative interviews and an online survey instrument. To get a broad understanding of how the norms of the EPs were being institutionalized and implemented across all aspects of the institutions’ project finance activities, interviews were arranged with both “front office” bankers and with ESRM managers at eight of the EP Steering Committee banks (in New York, Paris, London, Germany, Italy and Japan) as well as with knowledgeable individuals in the project finance sector, including project finance staff at the International Finance Corporation actively engaged in assisting EPFIs with capacity development and outreach; activists at NGOs, and environmental and social risk consultants at several leading consulting firms. The interview process was very helpful in gaining an “insider’s” perspective on the project finance industry and the challenges in implementing the Equator Principles, which insights were used to refine the survey instrument used during Phase II.

Following the successful completion of the interview phase, the initial results were shared with the EPFI Steering Committee, which then agreed to circulate the online survey, subject to approval of the survey instrument itself. Their review was to ensure that the questions asked were appropriate, and thus,
more likely to be answered, by the EPFIs. After further refinement, the survey instrument was circulated to the larger EPFI population in March 2010. Because the contact information for the responsible personnel at all institutions is not always publicly available and because the banks are generally bombarded with research requests, I chose to work closely with the EPFI Steering Committee as a means of ensuring that the survey would be circulated among all EPFIs.

I expected that respondents would primarily consist of those EPFIs who were most committed to implementing the EPs. It was further anticipated that respondents would overstate the extent of their implementation efforts. To combat this (and as a means of enticing participation because of the confidentiality concerns discussed above), the survey gathered the data anonymously, so that no individual institution had any motivation to overstate their efforts, as they would not get any public recognition for doing so.

Phase II of the study launched in late March 2010. The Equator Principles Secretariat circulated invitation letters to all EPFIs (then numbering 65 institutions). It was expected that the EP contact point, typically an environmental and social risk manager, would be the respondent because of their extensive knowledge of institutional practices related to ESRM. Over the course of the survey period (through early June 2010), forty-two institutions opened the survey instrument, with twenty-four banks fully completing the questionnaire, yielding a 35 percent response rate. This is a bit higher than the twenty percent rate identified as typical for surveys of quality managers, of which the EPFI ESRM managers are arguably a variety (although it should be kept in mind that other studies of quality managers focused on manufacturing and similar industries were there are far greater number of potential survey subjects, and they thus had a much larger N and sample sizes). Once the survey data was collected it was recoded to facilitate statistical analysis.

---

159 Darnall & Sides, supra note 132.
161 Although it is not the focus of this Article, Fisher’s exact tests (see Table 3) and gamma tests (see Table 4) were used to examine the association between reputational exposure variables and measures of implementation. There was an association between levels and riskiness of finance activity and the relative pressure experienced from different stakeholders prior to adoption. For example, the number of estimated projects financed annually was associated with the relative level of pressure banks claimed to have experienced from NGOs in their home countries (p = .013, FET). In addition, the number of estimated “high risk” projects financed since 2003 was associated with both (1) the relative pressure felt from shareholders (p = .018, FET), and (2) whether an institution was in fact targeted by a public campaign prior to adoption (p = .037, FET). These associations suggest that the more exposed banks did “feel the heat” more than others.
B. Data Limitations

Table 3 shows that the sample is superficially representative of the larger pool of EPFI at the time of the research (there are now approximately 10% more). The characteristics focused on here are those that reflect some of the considerations of neoinstitutional theory, for example, the concern that early adopters make more substantive changes, while later adopters only make ceremonial or symbolic changes. Wright and Rwabizambuga showed that the earliest adopters of the EPs were those in High-Income OECD countries with high levels of governance and thus strong support structures for civil society actors who put pressure on the banks.\footnote{See Wright & Rwabizambuga, supra note 17.} My research bore this relationship out as well: a statistically significant higher proportion of banks from high-income OECD countries were early adopters (81%) than the proportion of early adopters from low-income OECD or non-OECD countries (25%) (p = 0.01, Welch’s t-test). In addition, as indicated, the involvement of institutions in “regime-building” activities might be a useful indicia of regime effectiveness, so Table 2 shows the representativeness of the sample for this criteria as well.

Nevertheless, the data has two layers of selection bias. First, the sample is non-random, which flows from the decision to focus only on participants in the EPs, thus excluding other multinational banks that might have experience with project finance lending. To evaluate how participation in the EPs is associated with increased levels of environmental and social risk management, it is necessary to determine what would have been the firms’ practices in the absence of participation in the EPs (actual levels of ESRM practices could be compared with estimated counter-factual levels). If adoption of the EPs were random across all banks, a simple comparison of average levels of ESRM exhibited by EPFIs and non-EPFIs would establish the “effect” of being an EPFI. But adopting the EPs is not random; rather it is driven by a self-selecting process, likely determined by key bank institutional characteristics. This selection bias makes it difficult to draw any conclusions regarding the causal effect of participation in the EPs as a driver of the organizational changes observed; any number of confounding variables (such as bank characteristics) may be equally or more responsible for the observed changes.\footnote{Khanna & Keith, supra note 113.} Where possible, the survey attempted to compensate for this difficulty by asking questions that put the respondents in the position of evaluating causation as part of their responses.

A second layer of potential selection bias lies in the response rate and the self-selection by respondents to choose to participate in the survey. The researcher anticipated the low-response rate from the start of the study, but accepted that it might be inherent to the exploratory nature of the project, particularly given the confidentiality concerns of the research subjects. This second layer of bias ordinarily would tend to inhibit the power of any extrapolation from the experiences of the sample to the broader EPFI population,
but, as discussed below, the sample is in fact quite representative along a number of important factors.

A further difficulty with the data is the sample size, which restricts the power of the statistical tests performed. This means that there is an increased risk of Type II errors—that is, an increased chance of failing to observe effects that are present. Another limitation that might have an effect on the conclusions drawn is the problem of multiple-testing resulting from the exploratory nature of the data testing. The problem of multiple testing exacerbates the typical false-positive (Type I) error rate, which is equal to the threshold for statistical significance (.05)).

C. Further Data Considerations

Nevertheless, in considering these caveats it is important also to keep in mind two important and distinguishing structural aspects of the project finance market: the loan syndicate structure and the historically highly concentrated nature of the market among a relatively small number of institutions uniquely well-positioned to compete in the highly complicated and multi-disciplinary practice of project finance. Both of these characteristics contribute to making the project finance market a highly “social” marketplace that is particularly well-suited for norm diffusion and isomorphic outcomes.

The amount of capital required for project finance and the riskiness of such complex projects has led to the creation of the primary distinguishing characteristic of contemporary project finance: what is alternately referred to as the special purpose entity, vehicle or corporation (SPE, SPV or SPC), which is an entity created by the sponsor/borrower to shield its own assets from lenders.\footnote{The Equator Principles define project finance as it is defined by the Basel Committee on Banking Supervision: a method of funding in which the lender looks primarily to the revenues generated by a single project, both as the source of repayment and as security for the exposure…. In such transactions, the lender is usually paid solely or almost exclusively out of the money generated by the contracts for the facility’s output, such as the electricity sold by a power plant. The borrower is usually an SPE (Special Purpose Entity) that is not permitted to perform any function other than developing, owning, and operating the installation. The consequence is that repayment depends primarily on the project’s cash flow and on the collateral value of the project’s assets. Equator Principles Preamble, note 1 (quoting Basel Committee on Banking Supervision, International Convergence of Capital Measurement and Capital Standards ("Basel II"), November 2005), available at www.equator-principles.com (last visited November 20, 2010).} The sponsor/borrower becomes the primary shareholder in the SPE by contributing equity, which is then combined with smaller shares of equity from other partners, including often a government entity, but none of the shares held is large enough so that the SPE could for legal or accounting purposes be considered
a subsidiary of any of the partners in the joint venture. To these contributions of equity banks add debt financing in the form of syndicated loans.

The non-recursive nature of the loans shields corporate parents of the SPE from liability in case of default and typically the loans are repaid from project proceeds, making them exceptionally risky. The sheer volume of capital and the extraordinary levels of risk make it that no individual bank is willing to finance these projects on their own. Rather, most large-scale infrastructure projects are co-financed in syndicates of loans arranged by a “lead-arranger” bank or banks that pull together various streams of capital from several other institutions. The delicate balancing of lender and borrower risk and the transnational, cross-jurisdictional nature of the transactions has led many to liken the structuring of these deals more to the creativity of art than the cold-calculation of financial balance sheet, and the banks capable of such artistry are few, making them virtually indispensable to almost any project finance transaction of any appreciable size.

While this has led the project finance industry to develop into what some describe as an unhealthy “oligopolistic” market dominated by the handfuls of banks capable of evaluating deals and pooling sufficient capital from other institutions, this oligopoly is not necessarily a bad thing from the standpoint of norm diffusion. On the contrary, the EPs are structured so that the EPFIs must apply to a deal as long one bank among a syndicate of institutions lending to a project is an EPFI. Historically, the top lead arrangers have traditionally dominated the market and the EPFIs have always been among the crème de la crème: as of April 2007, there were fifty EPFIs; 19 of these (many in the Steering Committee) were in the top 40 lead arrangers of project loans in 2006, responsible for arranging 47% of all project loans. Accordingly, over the years project sponsors have become increasingly aware that to bring a project to the international capital markets, they would need to make their projects EP-compliant; otherwise, they could not attract a large enough syndicate which would by necessity involve an EPFI.

The particular structure of the project finance market has thus enabled the EPFIs to effectively impose new “rules of the game” on the rest of the market. Although the assurgency of Chinese and Indian lenders in recent years has created

---


166 ROY C. SMITH & INGO WALTER, GLOBAL BANKING (SECOND EDITION ED. 2003) (“[r]elatively few financial institutions seem to have the necessary legal, accounting, tax, financial, and technical skills, either at their head offices or at strategically located regional offices, to become major players. When this constraint is combined with the need for large-scale financing in various maturities, the capability of effective syndicate leadership, and close sponsor contact, it is not surprising that the number of major participants is limited.”).

167 Id.

168 See Fligstein & McAdam, supra note 84.
a hurdle to truly global standard-setting, even with this consideration, the EPFI claim that that the EPs still apply to 70% of all emerging market transactions (this might not be equivalent, however, to 70% of all capital financed in emerging markets, i.e., a few very large and therefore probably very risky projects are being financed by Indian and Chinese lenders). These structural dynamics suggest that the overall effectiveness of the EP regime’s ability to regulate the bulk of the project finance industry rests in the regime’s ability to instill compliance among these core institutions.

In any event, the high concentration of EPFI is perhaps not as unique as one might think relative to other global industries whose operations have considerable impacts on human rights: the extractive industry is dominated by a core group of main players in oil and energy, there are only a handful of global players in water infrastructure and in pharmaceuticals. The relative concentration of the market in which a global private regulatory regime is situated and the degree to which market participants have financial or strategic motivations to cooperate and coordinate their activities—as opposed to remaining purely atavistic competitors—may have predictive power with regard to the extent to which they will engage in the kinds of social learning that might be integral to regime effectiveness. This question is not explored here in contexts other than the EPs, but it suggests a hypothesis for future research.

V. DISCUSSION OF FINDINGS

A. Individual Institutional Growth in Environmental and Social Risk Management (ESRM)

1. ESRM Personnel and Policies

A significant indicia of change and individual commitment to implementing the EPs is the creation of designated ESRM personnel or departments. The creation or designation of specialized personnel or departments indicates that banks are “willing to not only state a formal policy of commitment to compliance but are also actually devoting resources to hiring people with the skills and job description to help the organization actively manage compliance.”

Prior to the EPs’ creation, there were virtually no rigorous ESRM systems in place, and those systems that were in place were perhaps rudimentary compared to what is in place now. Indeed, while approximately 40 percent of the banks surveyed were “aware” of ESRM issues and would discuss them with potential borrowers before adopting the EPs, only about 25 percent (6 banks) benchmarked their ESRM review to existing World Bank standards, and significantly, only 3 claimed to do so in a rigorous systemized fashion.

169 Parker & Nielsen, supra note 112.
Following adoption or in preparation for adopting, 75 percent (21 banks) reported having made some changes of varying degrees to their ESRM, with the other 25 percent (6 banks) reporting that they had not made “significant changes.” It should be emphasized, however, that all six of the banks reporting that they did not make significant changes were institutions who reported that they were already benchmarking their ESRM to World Bank standards prior to adopting the EPs.

The most common evolution in practices (45.8 percent, 11 banks) involved standardizing procedures in a more formal process that linked project review to the EPs and IFC benchmarks and incorporated these standards in detailed loan covenants. An additional twenty-five percent (the six banks mentioned above) reported going “beyond Equator” by applying ESRM review to non-project finance transactions as well.

In addition, fifty-four percent (13 banks) reported that they had “designated personnel and/or created a department to review projects for ESRM because [they] were adopting the Equator Principles” (29 percent (7 banks) already had designated personnel for reviewing projects prior to adoption).

2. Training

Beyond the creation of ESRM departments or designation of ESRM specialists, all of the banks but one also conducted extensive training of their project finance teams.

3. Power of ESRM Personnel in Review Process

Although institutions structure their ESRM and position it relative to their overall credit approval processes in different ways, it appears that most banks have endowed their ESRM personnel and review procedures with a significant stake in the outcome of credit decisions: 45 percent of respondents indicated that ESRM personnel can strongly recommend against pursuing a project further already at the marketing stage, which recommendation, they report, is generally accepted, and 50 percent of the banks represented that ESRM approval is required before a project is presented to the credit committee for final approval. In addition, it is also worth noting that a majority (sixty percent) of the banks have their ESRM personnel function outside of the project finance teams’ bonus structures, which suggests at least superficially that they are not incentivized to compromise on their own independent judgment with respect to particular projects, though of course they might feel other internal office and career pressures to not stand in the way of projects that others are ready to finance.

4. Depth of Due Diligence

Another important aspect of implementing the Equator Principles is how institutions utilize these new environmental and social risk review procedures. If
procedures are in places that fail to rigorously scrutinize projects under consideration, then these procedures amount to nothing more than a fig leaf. To get some sense of how these procedures work, the survey looked into how banks handle difficult funding decisions.

The survey revealed that when focusing on tough funding decisions, most credit committees strive for consensus. If on particularly challenging and risky credit decisions this cannot be achieved, many banks have also created quasi-appellate levels of review going to the very tops of their management structures for decisions on particularly challenging and risky credit decisions. Generally, these secondary levels of review are by default reserved for the most challenging projects with the greatest potential reputational risks. The creation of these heightened review mechanisms suggests that banks take very seriously potential reputational risks arising out of complicated, often politically sensitive transactions. This does not mean, of course, that bank management will always side on the cautious end of the spectrum with respect to environmental and social risks, which often are judgment calls (by independent consultants) both with respect to their eventuality and scope of impact “on the ground” as well as to their potential ramifications for bank reputation. While the technical calculation of environmental and social impacts should be the same for each bank (as they are based on the independent expert’s analysis which is shared among all participants in a bank lending syndicate), the reputational risk analysis might vary depending on the bank, its connection to the host country, the relative level of resulting civil society pressure, and even by the particular environmental or social issue implicated.

Another important aspect of ESRM review is the depth of due diligence, particularly during project construction. Typically, external consultants are the front line investigators. They do periodic site visits that are relatively frequent at the start of construction and operation (quarterly, perhaps) but drop in frequency once the project reaches completion and begins operation (to an annual or biannual basis).

In addition to the consultants’ visits, a large percentage of banks (70 percent) reported doing their own site visits, which some of my interview subjects suggested typically occur when certain construction completion goals are reached, since the further drawing-down of loan funds is often contingent on the sponsor meeting certain construction deadlines. However, only a relatively small number of banks (12.5 percent, three banks), reported having set-up complaint mechanisms or secondary lines of communication that would serve to compensate for any breakdowns in information-flow in the complaint procedures offered by project borrowers. It was assumed before the research began that secondary complaint mechanisms would be a reasonable check on the overall compliance of a project, which Equator Principle 6 puts at the feet of the banks themselves. It might be that this is in fact too complicated to achieve in practice, or that this is an area where the banks are simply not doing enough.

One banker suggested candidly that attention to ESRM issues by each loan syndicate member might decline somewhat after financial close, but he clarified
that this slack is then picked-up by the “agent” bank, one of the syndicate members that extracts an additional fee for monitoring the borrower’s compliance with the loan covenants that incorporate the EP requirements (such as an environmental action plan and management plan, including complaint mechanisms). The agent gathers the reports of the consultants, and if the borrower fails to submit these, they are put on notice of the delinquency. When one combines the roles played by the borrower, the independent consultant, the agent bank, and the rest of the banks within the syndicate, not to mention national and international NGOs, what results is a complex web of governance—what Abbott and Snidal have termed “coordinated governance.”

Whether this governance translates adequately into actual accountability remains an open empirical question.

5. Reporting

Finally, a major implementation related issue of significant concern is EPFI disclosure under EP 10. As noted, in 2006, the Equator Principles were reborn as the “Equator Principles II” to keep pace with upgrades to the IFC’s Performance Standards. A significant aspect of the revision was considered to be an enhancement: the newly created EP 10, under which EPFIs are required to “commit[] to report publicly at least annually about its Equator Principles implementation processes and experience, taking into account appropriate confidentiality consideration.” EP 10 further clarifies in a footnote that “such reporting should at a minimum include the number of transactions screened by each EPFI, including the categorization accorded to transactions (and may include a breakdown by sector or region), and information regarding implementation.” In May 2007, the EPFIs released a guidance note (“Guidance Note to EPFIs on Equator Principles Implementation Reporting”), which established minimum requirements for reporting and provides further suggestions on the extent of information to be disclosed as well as different formats for presenting this information.

The requirement for disclosure of EP-related activities has been treated by NGOs as both a means to an end and an end in itself. On the one hand, NGOs have tracked overall disclosure progress while at the same time criticizing the reporting requirement as not being comprehensive enough, and therefore, not useful to communities affected by projects or by the public at large, which has an interest in independently assessing whether the EPs are being properly implemented by particular banks. In particular, a glaring criticism of the EP reporting requirement is that, in contrast to the disclosure requirements at some multilateral development banks (e.g. the Asian Development Bank), which require the public disclosure of all projects under review for financing, the EP requirement is a post-hoc disclosure of only the aggregate results of such

---

170 Abbott & Snidal, supra note 15.
171 See Banktrack’s report, Silence of the Banks (2007) and Table 5.
reviews. The newly revised IFC Performance Standards have significantly enhanced the project disclosure process in this regard, and as of this writing, the EPIII draft has incorporated these enhancements.\textsuperscript{172}

A related critique, which for a long time went to the heart of the perceived inadequacy of IFC Performance Standards as well, is what the NGOs historically have considered to be a “watered-down” version of the principle of “free, prior and informed consent,” or FPIC.\textsuperscript{173} As of this writing, this insufficiency has been

\textsuperscript{172} See EPIII Draft Principle 5, available at http://www.equator-principles.com/index.php/ep3 (last visited August 20, 2012) (“To facilitate Stakeholder Engagement, the borrower will make the Assessment documentation and the [Environmental and Social Management Plan] readily available to the public in the relevant local language and in a culturally appropriate manner. Refer to Principle 10 for Project Reporting requirements”); EPIII Draft Principle 10 (“For all Category A and, as appropriate, Category B Projects located in non-OECD countries and OECD countries not designated as High-Income, the EPFI will require the borrower to disclose the Assessment documentation and the ESMP online. The borrower will take account of and document the process and results of the stakeholder consultation, including any actions agreed resulting from the consultation process. For Projects with adverse environmental or social impacts, disclosure should occur early in the Assessment process, and in any event before the Project construction commences, and on an ongoing basis. For all Category A and, as appropriate Category B Projects, in all countries, the EPFI will require the borrower to publicly report greenhouse gas emission levels during the operational phase for Projects emitting over 100,000 tonnes of CO2 equivalent annually. Refer to Annex A for detailed requirements on greenhouse gas emissions reporting.”).

\textsuperscript{173} A full review of the philosophical and legal foundations for FPIC is beyond the scope of this Article, but it bears noting the recent developments on its contours. It remains an open question whether the norm of FPIC has achieved the status of customary international law. To be considered custom, a rule must be “generally accepted as a rule of conduct,” which can only be demonstrated if state practice is consistent with the rule and states act according to the rule out of a sense of legal obligation, rather than out of a sense of moral or political compulsion. See American Law Institute, Restatement of the Law, Third, the Foreign Relations Law of the United States. St. Paul, Minn.: American Law Institute Publishers, 1987, §102(2) (“[c]ustomary international law results from a general and consistent practice of states followed by them from a sense of legal obligation”). The Restatement’s formulation is based on Article 38 of the Statute of the International Court of Justice. See Statute of the International Court of Justice, Art. 49.

The two main obstacles to FPIC attaining the status of custom is that state practice of the rule is not nearly extensive enough, furthermore, in the places where it is applied to some degree, its application has not been consistent. The interpretation of what FPIC entails remains very much open to debate and further evolution, particularly between civil society, the World Bank, and the commercial banks studied here. See IFC Performance Standard 7 (1 Jan 2012), at http://www1.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+sustainability+framework/2012+edition/performancestandard7 (“There is no universally accepted definition of FPIC.”). Indeed, the most recent version of the Performance Standards recognizes three different levels of consultation and consent, depending on the specific context. See Performance Standard 1, paras. 30 (“When Affected Communities are subject to identified risks and adverse impacts from a project, the client will undertake a process of consultation in a manner that provides the Affected Communities with opportunities to express their views on project risks, impacts and mitigation measures, and allows the client to consider and respond to them. The extent and degree of engagement required by the consultation process should be commensurate with the project’s risks and adverse impacts and with the concerns raised by the Affected
substantially addressed by the IFC in the revised Performance Standards released in July 2011, which added additional levels of scrutiny and a “consent” – rather than mere “consultation” – requirement with respect to Indigenous Peoples in “certain circumstances.”\(^{174}\) This, too, has been incorporated into the EPIII draft.

\(^{174}\) See id. at para. 32 (“For projects with adverse impacts to Indigenous Peoples, the client is required to engage them in a process of ICP and in certain circumstances the client is required to obtain their Free, Prior, and Informed Consent (FPIC)” as defined in Performance Standard 7). Guidance Note 7 to Performance Standard 7 elaborates further, noting that

FPIC comprises a process and an outcome. The process builds upon the requirements for ICP (which include requirements for free, prior and informed consultation and participation) and additionally requires Good Faith Negotiation (GFN) between the client and Affected Communities of Indigenous Peoples. GFN involves on the part of all parties: (i) willingness to engage in a process and availability to meet at reasonable times and frequency; (ii) provision of information necessary for informed negotiation; (iii) exploration of key issues of importance; (iv) use of mutually acceptable procedures for negotiation; (v) willingness to change initial position and modify offers where possible; and (vi) provision of sufficient time for decision making. The outcome, where the GFN process is successful, is an agreement and evidence thereof.

Guidance Note 7 at para. 25. Nevertheless, the Performance Standards recognize the tension between sovereign prerogative in economic development and FPIC:

States have the right to make decisions on the development of resources pursuant to applicable national law, including those laws implementing host country obligations under international law. Performance Standard 7 does not contradict the state’s right to develop its resources. A state may have obligations or commitments to ensure that Indigenous Peoples provide their free, prior, and informed consent for matters pertaining to the overall development of indigenous territories. Such state-level obligations are distinct from the project-level FPIC requirements described in Performance Standard 7. As described in GN62–65, where government processes involve project-level decision and actions, the client should review these processes in relation to the requirements of the Performance Standard and address identified gaps where feasible.


\(^{175}\) See EPIII Draft Principle 5, supra note 172:

….EPFIs recognize that indigenous people are often a vulnerable segment of Project-Affected Communities. Projects affecting indigenous peoples will be subject to a process of Informed Consultation and Participation, and will comply with applicable national law, including those laws implementing host-country obligations under international law. In non-OECD countries and OECD
The importance of the reporting requirement needs to be put into context. Notably, several interviewees explained that the current data on projects – particular the numbers of projects rejected – is not necessarily as revealing as might be hoped. As several banks’ CSR reports make clear (see, e.g., Citibank and Barclays), projects can be rejected on any number of grounds, not just those related to environmental or social risks. As one financial expert has noted in previous business journalist accounts, “an absolute no would be unlikely based on the principles alone.”

In fact, my data shows that the banks surveyed were evenly split on whether they had ever rejected a project primarily because of ESRM issues. Indeed, credit approval committees often reject projects because project sponsors’ backgrounds not only raise questions about their capacity for environmental and social risk management, but also about their credit histories and general business practices; indeed, the two often go hand-in-hand. Others have noted that even getting to a “no” stage is pretty unlikely because few banks would let negotiations progress to that point if warnings signs had already manifested themselves.177 Moreover, it is rare that projects are considered solely on an absolute yes or no basis; rather, “[o]nce the assessment has been done, if there are elements of a project that breach the standards, the response is not to refuse the project but to put processes in place to manage it so it does become compliant.”178 Thus, figures on rejection of projects must be taken with a grain of salt; they are not likely truly revelatory of the depth of banks’ commitment to ESRM as much as they point to the banks’ appreciation of a variety of reputational risks. The survey also found that the level of detail in disclosures varied by bank, but that over 20 percent of the banks’ disclosure statements met the Guidance Note on Disclosure and over 60 percent exceeded the minimum requirement.

With this in mind, a further problem with placing too much emphasis on the EP reporting requirement is that because of confidentiality concerns, EP reporting comes in the least credible fashion according to the schema described by Prakash and Potoski: it is first-party auditing (indeed, these authors contend that first- and second-party auditing is definitively not credible).179 Indeed, the EP Strategic Review completed in February 2011 noted several problems with the reporting requirement as it stands, including that: (i) “[d]ue to lack of a reporting standard, implementation reporting is inconsistent and often limited and inadequate to provide information on how the EPs are being implemented by an

countries not designated as High-Income, consistent with special circumstances described in IFC Performance Standard 7, Projects with adverse impacts on indigenous people will require their free, prior and informed consent (emphasis added).

177 Id.
178 Id.
179 Prakash & Potoski, supra note 24.
institution”; (ii) “[i]t is difficult to find reporting data and not possible to aggregate it”; (iii) “[i]t is difficult to determine whether an EPFI is fulfilling its responsibilities under the EPs; (iv) “[s]takeholders cannot assess what the EPs are achieving.” The Strategic Review laid-out several useful recommendations for how the reporting requirements and processes might be improved. The EPIII Draft begins to respond to these concerns as well, as the proposed revised Principle 10 requires both aggregated reporting, as in the past, as well as project-specific reporting for certain qualifying transactions, to be reported to the EPFI Secretariat and published on its website or the EPFI’s website.

All this being said, the survey results indicate that 70 percent of the institutions reported using external auditing firms to verify the disclosures in their CSR reports, which Prakash and Potoski characterize as the gold standard among voluntary programs (because in practice there is no fourth-party certification—external auditors not paid for by the firm). Generally, assurance auditors from large accounting firms read EPFIs’ corporate social responsibility (and other) reports to verify that the contents disclosed are accurate (see Table 6). An assurer for a major EPFI has argued, however, that the value of assurance is sometimes limited by the roles played by a bank in different syndicates: if a bank that has hired an assurer has not acted as the lead arranger or the “environmental bank” for the deals on which it is reporting, it makes limited information available to the assurer regarding project implementation data (post-financial close, however, the Agent bank is supposed to update all syndicate members of any issues reported by consultants, so all syndicate members should have this information, but perhaps it comes in summary form). The EP Strategic Review also noted that “[t]here

---

180 Lazarus & Feldbaum, supra note 17, Appendix B at 7.

181 See id. (proposing that (i) disclosure include “at minimum, project names (with client consent) and related categorization, by financial close or before, in annual reporting”; (ii) creation of an “independently managed Equator Principles League Table”; (iii) development of “a detailed standard for consistent implementation reporting through use of a survey, a reporting template or a [Global Reporting Initiative] protocol; (iv) Elimination of the one year grace period in reporting for new adopters and requiring reporting within the first year on implementation procedures; (v) development of an “EP assurance standard to use for third party auditing of EPFIs’ internal implementation processes” including “an audit procedure for verification of implementation capacity of new members”; (vi) publishing an “EP Annual Report highlighting the achievements and challenges of the year.”

182 The project level reporting requirement will be (a) applicable only to Project Finance transactions that have reached Financial Close; (b) subject to obtaining client consent; (c) subject to applicable local laws and regulations; and (d) “subject to any reduction in the rights, or increase in the liability, of the EPFI.”

183 The EPFI will seek client consent at a time during the loan documentation process deemed appropriate by the EPFI or at Financial Close to disclose: (a) Project name (as per the loan agreement); (b) Sector: Mining, Infrastructure, Oil and Gas, Power, Others; (c) Region: Americas, Europe Middle East and Africa, Asia Pacific; (e) The calendar year in which the loan reached Financial Close.

are no agreed standards for audits” and accordingly has recommended that the EPFIs develop an “EP assurance standard to use for third party auditing of EPFIs’ internal implementation processes” including “an audit procedure for verification of implementation capacity of new members.¶185

Such functional critiques of the disclosure requirement are quite valid: how can people comment on project viability or protest projects without sufficient advance knowledge? Moreover, how can consultation (let alone consent) occur without sufficient advance release of information? The banks counter, however, that disclosure brushes up against the banks’ fiduciary duties: revealing project information, the banks argue, would be highly unprofessional, if not illegal, which is why the reporting requirement’s Guidance Note prescribes that annual reporting on EP implementation “take[e] into account appropriate confidentiality considerations.” This significant constraint remains in place in the EPIII Draft Principle 10 and in the introductory “Statement of Principles” that now preface the Principles in Draft EPIII.¶187

Still, while it needs to be reiterated that the content of the information disclosed in the banks’ reporting is not valuable in and of itself (compared to disclosure of project-level information well in advance of financial closure), it is nevertheless important because it is costly to produce this reporting and even greater resources are expended in hiring external auditors to certify the disclosures. Thus, under signaling theory’s approach, the outlay of non-trivial costs increases the likelihood that the information related to those costs is accurate. To reiterate, what we do not have here is evidence that banks made certain funding decisions related to particular categorizations of projects; what we do have here, and which arguably is significant, is evidence that they engaged in the process of categorization, which is the first—and essential—step in environmental and social risk management.

**B. Other Measures of Regime Effectiveness: Social Interactive Processes and Regime Building**

1. Creating a Regime-Sustaining Ethos and Platform For Social Learning

As noted (see supra section III.E), recent research into voluntary regulation has emphasized its capacity to engender a social interactive process

---

¶185 Lazarus & Feldbaum, supra note , Appendix B at 7.

¶186 Gaskin, supra note 176.

¶187 See Draft EPIII, supra note 172 “Statement of Principles” (“Recognising business confidentiality and applicable laws and regulations, mandated EPFIs will endeavour to share relevant environmental and social information with other mandated financial institutions with a view to seeking, where appropriate, consistent application of the Equator Principles to Projects financed.”) and Principle 10 (“The EPFI will report publicly at least annually on transactions screened and closed, and about its Equator Principles implementation processes and experience, taking into account appropriate confidentiality considerations.”).
among its participants, which can yield long-term benefits, such as creating a space or mechanism for collaborative social learning where none previously existed, that a short-term outcomes-based evaluation might overlook. There is anecdotal evidence that the Responsible Care program transformed the chemical industry in just this way, with the industry’s “old ethos” of “every company for itself” being replaced by “a culture of sharing and mutual aid” because “with the reputation of the industry only as strong as its the weakest link member, companies have a vested interest in ensuring best practices are broadly shared.”\(^{188}\) Others have noted similar transformations of the interactions between nuclear facilities in the United States after the creation of a similar industry association.\(^{189}\) Indeed, this is the primary function served by the United Nations Global Compact, which is now the world’s largest corporate social responsibility initiative.

To measure the effectiveness of this element of the EPs, this study tried to gather data to answer the question of whether the regime has centralized and coordinated the resources of competitor institutions and whether it has effectively disseminated knowledge and norms that might otherwise find barriers to widespread dissemination. Beyond the mere sharing of knowledge and expertise, a further marker of regime growth and potential effectiveness is the development of more formalized governance structures. The mere creation of a formalized governance structure is significant, but is perhaps even more informative to examine the extent to which regime participants, out of recognition of their shared fate, have sought to help maintain this governance structure rather than let it whither through neglect or opposition? Arguably, this is what separates a governance structure established to be a fig-leaf and one intended to create real change. Building on these observations, this study also tried to quantify the various “regime-building” activities in which EPFIs participated.

2. Measuring Frequency and Quality of Peer Contact

One way of gauging the extent to which the EP regime has facilitated social learning is to measure the contact and discussion of environmental and social issues between banks before adoption and after adoption. As noted (see supra section IV.C), project finance lending is necessarily a very social enterprise: very few projects can be developed without syndicating project loans on the international credit markets. Thus, there are competitive advantages to being a bank that has the expertise necessary to serve as a lead arranger of large deals or to act in an advisory role, both activities garner fees beyond that which a mere participant in a syndicate would earn. Given this, it is in individual institutions’ strategic interests to keep such expertise to themselves so that they are always viewed as a necessary participant to most deals.

\(^{188}\) King & Lenox, supra note 82.

\(^{189}\) REES, supra note 88.
On the one hand, this would suggest that banks would not be in a hurry to disseminate expertise and capacity to conduct extensive ESRM due diligence. However, to the extent that the strategy of leading banks in creating the EPs has been to “set a level playing field,” a primary goal would in fact be dissemination of norms and practices supportive of the EP becoming the gold standard in the industry (which also serves the leading institutions’ interests). To the extent that this latter, regime-focused imperative has trumped more individualistic strategic goals, we should see increased contact and dissemination of knowledge between EPFIs. To that end, the survey measured the level of contact that institutions had with their peers regarding ESRM issues both before and after implementing the EPs (see Table 5).

According to the survey, over fifty-four percent of respondents (13 banks) had been active in “outreach to a non-adopting institution to encourage them to adopt the EPs,” and a little more than twenty percent of respondents (five banks) had done “outreach to a non-adopting institution to provide capacity development.” Indeed, there is a Working Group committed to outreach that has several members divided into regional foci and as noted, the EPFIs have also sponsored conferences to expand adoption in geographic sectors not known for heightened attention to sustainability, including India, Russia, China and the Middle East.190

The research and the survey, as well as prior scholarship,191 raised the question of whether the extensive involvement of the IFC is the real root cause of the extensive adoption of the EPs and the spread of EP-consistent best practices? After all, the IFC was integral in founding the EPs and the EPs refer back to the IFC’s own Performance Standards. It is a difficult counter-factual to entertain, but one wonders what the state of ESRM practices in commercial banks globally would be if the EPs never developed and the IFC was continuing its engagement of the private sector financial institutions as it did before the EPs were created.

A partial answer is suggested by looking at the IFC’s outreach work in the early years of the EPs. Before the EPs reached a critical mass (approximately 2006, after the release of EPII and their adoption by forty banks), the IFC had only done outreach on an ad hoc basis by engaging the financial intermediaries it interacted with on “B loans” to projects. In 2007, however, the IFC hosted its first Community of Learning event, which approximately 80-100 banks have attended every year since.192 Other initiatives targeting the financial sector, primarily the United Nations Environment Program’s Financial Initiative, have operated since 1992, but have never achieved the same level of sustained activity, interaction and cooperation between large banks as that experienced since the launch of the EPs.

190 See supra note 58 (a “quick review of ten established Islamic banks in various countries” shows that only one in ten mentioned sustainability in their annual reports).

191 See generally Wright, supra note 37.

192 Interview with IFC staff on file with author.
In fact, according to an IFC staff person, the EPs, while conducting their own outreach efforts, simultaneously “coordinate closely” with the IFC on outreach activities in emerging markets. As an IFC staff person explained, having commercial banks intimately involved in their outreach is extremely useful because non-adopting commercial banks sometime need to be convinced of the merits of applying the Performance Standards by other commercial banks; the argument is not as persuasive when it comes from a development finance institution such as the IFC, which has a different organizational mission and a different set of stakeholders than a commercial bank.

3. Gauging “Civic Duty” Among EPFIs – Increased Formalization and Enhanced Governance

Ad hoc contact or even organized meetings held periodically arguably do not constitute a level of coordination sufficient to transform an industry’s practices and the relations between competitors in a lasting way. Accordingly, an important step toward fostering a community of social interactive processes to facilitate norm diffusion is the creation of a self-sustaining architecture for governance. The creation and maintenance of such structures suggests that regime participants take the regime and its aims seriously. Why else would such institutions commit the resources necessary for creating such structures?

The EPFIs have closely collaborated from the start through the Steering Committee structure and its Working Groups and has more recently formalized and legalized these structures even further with the creation of the EP Association and its membership rules, dues and voting procedures. The survey tried to measure individual EPFIs’ contributions to the regime, what could be described as expressions of their “civic duty” to help build and maintain the governance structure or community they had joined by virtue of adopting the Principles.

Of the respondents, 37 percent (9 banks) reported that they had served on the Steering Committee and 54 percent (13 banks) reported that they had served as members of one of the thematic Working Groups (seven of these were also Steering Committee members). Thirteen banks (54 percent) also reached out to other institutions, either to a non-adopting institution to encourage them to adopt, or to an adopting institution to provide capacity development.

The importance of the formation of a governance structure cannot be understated: in addition to deepening their ties (and collective fates) to one another in a way that is quite unusual for competitors, the EP Association also gives NGOs and other stakeholders a concentrated focal point for accountability, or stated otherwise, a bigger target: though each bank retains its own reputation, they now share a complaint box address. A derivative effect (or benefit,

---

193 See Aizawa & Yang, supra note 59.
194 The period of the survey covered activities prior to the creation of the EP Association in July 2010.
depending on whom you ask) of this concentrating, or multiplying effect can be seen in the changes in the level and frequency of contact between banks and NGOs pre- and post-adoption (see Table 7). The data shows that following adoption, there was a considerable increase in the numbers of banks reporting that they had been targeted by public advocacy campaigns prior to (50%) and after (67.7%) adoption.¹⁹⁵

¹⁹⁵ The survey asked about both project finance deals (which the EPs cover) and non-project finance deals (which technically are beyond the pale of EP governance, although some banks do apply an “EP-lite” review to these as well and the “scope” of EP application is one of the most contentious issues even among EPFIs, let along between EPFIs and NGOs). The conflicting views on this issue are clear from the Uruguay paper pulp mills dispute (see supra note 33 and accompanying text): whereas ING, a Dutch bank, pulled US $480 million in financing following the IFC’s Compliance Advisory Ombudsman’s conclusion that the project was in violation of the IFC’s Social and Environmental Safeguards, Calyon, a French bank, continued to support the project despite the concerns expressed by its internal environmental and social risk team, with the Calyon management claiming that the Equator Principles were not applicable to their financing of the project, which came in the form of a corporate loan to Finnish sponsor Botnia. See Banktrack, “International Court of Justice rules on Uruguayan Botnia case World Bank’s IFC, Nordea, Calyon and Finnvera complicit in violations of International Law,” at http://www.banktrack.org/show/news/international_court_of_justice_rules_on_uruguayan_botnia_case (last visited February 24, 2012). Indeed, some EPFIs expressed the concern during the recent Strategic Review process that the “narrow definition of project finance has diminished the relevance of the EPs to a small and declining portion of their financial portfolios, especially in light of general financial market trends of recent years.” Lazarus & Feldbaum, supra note at iii. Accordingly, one of the Strategic Review’s suggestions is to extend the EPs to cover corporate loans for which over 50% of the capital is being used to finance a single asset. Id., Appendix B, at 8. The Draft EPIII responds to this concern as well by proposing to make them applicable for the first time to “project-related” corporate loans so long as (i) the loan is related to a single project; (ii) the total aggregate loan amount is at least US$100 million; (iii) the EPFI’s individual initial exposure is at least US$50 million; (iv) the loan tenor is at least two years, and (v) the borrower has Effective Operational Control (either direct or indirect) over the 120 Project. See EPIII, supra note 172 “Scope.” The EPIII Draft also proposes to extend the EPs to “bridge loans,” which are financial instruments extended to cover short-term needs, so long as they have a tenor of less than two years are intended to be refinanced by a project finance or project-related corporate loan.

The divergent views present an empirical issue: whether to include only campaigns directed at project financing or to include campaigns directed at all project-related funding. In the words of one survey respondent, “[t]he external media/NGO world rarely understands project finance – they just protest activities – the finance vehicle doesn’t much matter to them.” In other words, the claim by some banks is that NGOs either do not understand the differences or choose to gloss over them in favor of focusing on any and all problematic project-related activities, regardless of financial structuring or whether they officially fall under the Equator Principles’ purview. It is likely not a misunderstanding, however, the hopes of the Collevechio Declaration were to have environmental and social sustainability considerations factored into all elements of financial institutions’ portfolios.

While it is worth keeping in mind the distinction between strictly “project finance” and other project-related financing from a legalistic point of view, from the perspective of “pressure” experienced by institutions, it was decided to inquire about all campaigns conducted, regardless of whether a project might technically have fallen under purview of the EPs and thus legitimately earned the ire of the campaigners.
Significantly, other statistical tests run show that the increase in pressure experienced by nearly 60% of the banks following adoption (Table 4 and 5) cannot be attributed to their own individual reputational risk variables, such as the number of projects financed or the number of high risk projects financed, or a bank-specific factor, such as such as governance of bank home country, although it is of course difficult to isolate these dynamics in a rigid causal relationship.

The shared governance structure should also be appreciated for its positive benefits: first, given the wide diversity of institutions participating in the regime, the ability to manufacture consent has proven difficult at times. Accordingly, having a formal governance structure and membership creates a pre-commitment device that will hopefully keep the regime together in the more difficult moments rife with discord. Without institutionalization, including voting rules and membership dues, every crisis confronted by the banks could be a potential threat to its long-term vitality.

Second, if a shared governance structure is equivalent to a shared complaint box, then the flip-side is that it can also serve as a collective bull horn: the strength in numbers provided by the formation of a governance structure allows the EPFIs to respond to criticism with a single voice, which ultimately allows the regime to maintain solidarity between its members and move their collectively agreed-upon agenda forward, whether it is on adopting new standards and benchmarks or making policy interventions, such as on climate change. This development’s significance thus far has been most evident in the way that the EP Association has made itself a crucial actor in the ongoing negotiation of the IFC Performance Standards: while the IFC ultimately makes its own decisions in accordance with the views of its Member States, it is clear that the EPFIs were a significant and vocal constituency in the recently completed IFC Performance Standard review., which makes sense given that the EPFIs are now the Performance Standards’ most frequent users.

VI. CONCLUSION: FINANCIERS AS POLICYMAKERS AND THE RISE OF HUMAN RIGHTS DUE DILIGENCE

Responding to the call from regulation scholars for more empirical work on global private regulation and corporate codes of conduct, this Article has offered the most comprehensive picture to date of the implementation of the Equator Principles by global banks. In the process it has sought to work through, albeit imperfectly, some of the methodological impediments that stand in the way of broader and more penetrating empirical research on corporate human rights accountability. While measuring outcome effectiveness may remain the “gold standard” from a purely methodological perspective, this Article has sought to present research on what can be observed with the hopes that it will serve as a foundation for future research conducted under conditions and practices of greater transparency by the subject institutions, which seem likely to come about with the new disclosure requirements proposed in the Draft EPIII framework.
This Article has suggested that a focus on processes of institutional change may also be particularly well suited to the context of corporate human rights accountability, where the goal is foremost to improve the approach and processes of assessing human rights impacts of corporate activities. Indeed, this is the approach to corporate human rights accountability recently arrived at through several years of multi-stakeholder negotiation under the auspices of the UN Special Representative for Business and Human Rights. At the start of the process it was wisely discerned that it would be difficult for NGOs, states, corporations, labor unions and other powerful global actors to agree upon the exact substantive content of corporate responsibility for human rights if these were to be considered binding norms. Indeed, that very approach failed with the Human Rights Council’s rejection of the earlier Draft Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights.196

But there was a clear need for an overhaul of processes, and the Special Representative deemed such a normative evolution to be pragmatic and ultimately achievable by corporate actors.197 And while the revolution was not predicted to

196 UN Doc. E/CN.4/Sub.2/2003/12 (2003). As John Ruggie, who, at the designation of the UN Secretary-General, took over the project of developing the norms, observed at the start of his mandate:

The draft Norms enumerated rights that appeared to be particularly relevant to business, including non-discrimination, the security of the person, labor standards, and indigenous peoples’ rights. But the list included rights that states have not recognized or are still debating at the global level, including consumer protection, the “precautionary principle” for environmental management, and the principle of “free, prior and informed consent” of indigenous peoples and communities. At the same time, the draft allowed that not all recognized rights pertain to business but provided no principled basis for making that determination. In response to the criticism that the list was overly inclusive, some Norms’ advocates have suggested a shorter set of “core” rights said to enjoy the most widespread support, and which business could easily grasp. But that move in turn is subject to the riposte that the very concept of core rights is “a very significant departure from the insistence within the international human rights regime on the equal importance of all human rights.” The issue remains unresolved and has led some observers to conclude than any detailed ex ante specification of rights for which companies might bear some responsibility is an inherently fruitless exercise – that in principle all rights could apply, but in any particular instance some will not.


occur overnight, it was anticipated that the flexibility of voluntary norms and a focus on processes would allow for much greater impact in the short term than would yet another binding human rights treaty.198 The OECD Guidelines for Multinational Enterprises adopted a very similar approach, incorporating the Guiding Principles into their revised chapters and placing a similar emphasis on human rights due diligence.199

In addition, like “soft law” international regimes, which scholars have argued offer distinct advantages over hard law because of their low costs and expediency,200 private regulation’s low barriers to entry and relatively inexpensive coordination costs should be seen not solely as a sign of “cheap talk” (commitments whose violation do not engender costly sanctions) but rather as an opportunity structure for rapid evolution. Thus, the focus on processes here is the result of an honest and realistic assessment that, particularly in the early, formative years of a private regime, judging regime effectiveness based solely on outcomes might be premature: like other regimes of global private regulation, the EPs remain in a state of dramatic flux and will continue to evolve in the future, most likely with the pace of markets, not the glacial pace of international treaty negotiations. This is not to mention the reality that project finance transactions and the resulting projects take years (and even decades) to plan and construct, and thus, one measure of the success of the EPs will be what the project sponsors designing projects now produce in anticipation for the more rigorous requirements that EPFIs will impose on them when their projects are ready to bring to international markets.

It is of course recognized that measuring institutional change is far from a perfect proxy for measuring impacts on the ground. Nevertheless, under the theoretical framework presented here, which suggests that rational actors would

198 See John G. Ruggie, Treaty road not traveled, ETHICAL CORPORATION (May 2008) (noting that treaty-making “can be painfully slow, while the challenges of business and human rights are immediate and urgent. Second, and worse, a treaty-making process now risks undermining effective shorter-term measures to raise business standards on human rights. And third, even if treaty obligations were imposed on companies, serious questions remain about how they would be enforced.”).


200 See Charles Lipson, Why Are Some International Agreements Informal?, 45 INT’L ORG. 495 (1991) (arguing that informal agreements can be negotiated more quickly, are more flexible, require less information, and can avoid publicity, but provide less of a commitment, than legal agreements).
not expend significant costs to implement non-binding normative commitments, there appears to be substantial evidence that a critical mass of the EPFIs are taking very seriously their commitments to the Principles. This is clear from the substantial resources they committed to implementation individually and the significant degree to which the banks have enhanced their collective governance capabilities. While such expenditures alone are not sufficient to guarantee effects “on the ground,” the costs and resources expended are far more than would be reasonably if all the banks were doing was trying to pull-off an elaborate “smokescreen,” that is if the EPs were no more than mere “greenwashing.”

The final significant aspect of the EPs’ growth and development that deserves comment is the way in which they have made themselves an indispensible party to future debates on finance and human rights, including those debates occurring at multilateral development finance institutions such as the IFC. Because the EPs linked themselves normatively to the IFC’s Performance Standards, the EPFIs have claimed a privileged status in the ongoing process of refining the Performance Standards. While the IFC does not consider the EPFIs to have veto power over its further standard setting, as the EPFIs are now the primary users of the Performance Standards, the IFC will likely take to heart their views on proposed changes.

Such developments are not limited to the EPs, however. In fact, there have been signs that the financial sector is assuming a considerably more active role in directing the global governance of their own activities, and by extension, much of the global economy. For example, leading into renewed climate negotiations in Cancun in late 2010, 259 investors from Asia, Africa, Australia, Europe Latin America and North America with collective assets under management totaling over $15 trillion\(^{201}\) called for governments to take action on climate change. These investors were not necessarily united by their passion for the environment, but more likely by their realization of the financial risks related to climate change, which they claimed could amount to GDP losses of up to 20 percent by 2050, as well as the economic benefits of shifting to low-carbon and resource-efficient economies.\(^{202}\) According to Ole Beier Sørensen, Chairman of the Institutional Investor Group on Climate Change and chief of Research and Strategy at the Danish pension fund ATP (with EUR 56 billion in assets), past experience in the renewable energy sector suggests that private sector investment in climate solutions has been driven, “almost without exception” by structured government policies that can “bolster investor confidence” and drive investments in renewable energy.

In addition to grand policy interventions, new private governance initiatives have launched in the financial sector. For example, the Principles for

---

\(^{201}\) This is equivalent to more than one-quarter of global market capitalization.

Responsible Investment were created in 2005 by the instigation of Kofi Annan, then-United Nations Secretary-General.²⁰³ Not unlike the EP, the PRI provide guidance to investors in how to integrate issues of environmental and social governance into their investment policies. As of October 2011 over 915 investment institutions from over 45 countries have become signatories, with assets under management equaling approximately US$ 30 trillion.²⁰⁴ PRI counts in its membership some of the members of the Private Equity Growth Capital Council,²⁰⁵ a “lobby group for major private equity firms,”²⁰⁶ which announced that it would sign on to the UN PRI in February 2009.²⁰⁷ What is remarkable about such developments is that private equity firms are barely regulated in major domestic jurisdictions such as the United States,²⁰⁸ and yet, they are now participating—at least superficially—in transnational private governance.

Indeed, while the UN PRI are not as detailed as the EPs are in the standards and demands they impose upon signatories, the UN PRI have already distinguished themselves by their preparedness to call-out “laggards”—albeit those lagging in a separate but closely-related governance regime: the UN Global Compact. In January 2008, a coalition of 38 investors worth over US $ 3 trillion wrote letters to the CEOs of 130 major listed companies that are signatories of the UN Global Compact. In their letters the investors praised twenty-five Global Compact signatories for meeting their obligations under the Compact to produce


²⁰⁴ A full list of current signatories can be found at www.unpri.org/signatories.

²⁰⁵ See About the Private Equity Growth Capital Council, at http://www.pegcc.org/about/ (last visited December 21, 2010). The Council’s membership includes some of the world’s best known private equity firms.


²⁰⁸ Under the 1940 Investment Advisors Act, hedge funds and private equity funds had met the definition of “investment advisor,” but also generally qualified for the “private adviser” exemption from having to register with the SEC under § 203(b)(3) of the Act (this exemption is open to any adviser that has fewer than 15 clients and does not generally hold itself out to the public as an investment adviser; hedge funds organized as limited partnerships have traditionally been themselves viewed by the SEC as the “client” in §203(b)(3), rather than to the investors constituting its limited partners). After the implosion of the US $125 billion Long Term Capital Management of Connecticut in 1998, the SEC adopted the “Hedge Fund Rule” in 2004, which effectively reinterpreted the definition of “client” under the Advisers Act so that general partners of hedge funds had to “pierce the veil” of their fund to reach its beneficial owners to determine how many clients they advise. However, in 2006, the D.C. Circuit Court of Appeal vacated the “Hedge Fund Rule” as “arbitrary,” leaving the exemption in place. It was not until June 2011 that the exemption was eliminated by the Dodd-Frank Act. See Press Release: SEC Adopts Dodd-Frank Act Amendments to Investment Advisers Act (June 22, 2011), at http://www.sec.gov/news/press/2011/2011-133.htm (last visited March 4, 2012).
an annual “Communication on Progress,” but simultaneously identified over 100 other companies as “laggards,” who were mainly based in emerging markets, and demanding them to comply with their obligations.\(^{209}\) One of the collaborating institutions remarked:

There is now a critical mass of institutional investors who believe management of corporate responsibility or ESG issues is highly relevant to the long-term financial success of their investments. And the UN Global Compact’s system of reporting, which demands the production of a “Communication on Progress” (COP), provides an important way for the investment community to analyze a company’s performance on those ESG issues. . . .

The UN Global Compact system provides investors with a universe of “good COPs” and “bad COPs.” Companies that produce a “good COP” send a powerful message to a valuable audience of institutional investors. Those who have failed to submit a report will trigger alarm bells among investors who want real details about a company’s business practices on ESG issues.\(^{210}\)

This intervention by the investors illustrates the dynamism and possibility for cross-fertilization of these new regimes of global self-regulation. Indeed, although the Global Compact is managed by the United Nations, it is the market share of its private sector, voluntary participants that gives these initiatives their potential power in shaping the global policies of both governments and corporations.

We must be cautious not to mistake for altruism what is really long-term risk management driven by the profit motive. The call for action by investors to governments in Cancun was not a product of enlightened capitalism, but of risk-avoidance: investors now appreciate the potential financial impacts of climate change and wish that governments would make it easier on corporations and others to pursue alternative energy strategies in the forms of tax-incentives and other benefits. This is not internalizing social costs as “triple bottom line” business models and corporate social responsibility dictate, but asking governments to subsidize research and development, and consequently, share the financial risk inherent in developing new technologies. With these goliaths of the global economy making such moves, it is likely only a matter of time before we see true innovation of the global economy around the sustainability agenda that the financial sector is championing—with thanks, of course, to the constant prodding of the NGO community.


In placing too much emphasis on measuring voluntary regimes or private regulation solely by their immediate effects “on the ground” we risk missing their broader contribution to global policy. Global private regulatory initiatives like the EPs, the UN PRI and even the United Nations Global Compact provide platforms for the dissemination of the ideas and organizational practices that undergird the sustainability agenda and create the social linkages and governance structures among competitor institutions which facilitate the kind of peer pressure dynamics that combine with the natural competitive spirit of capitalism to force organizations to change. With the benefit of enhanced project-level and regime-wide disclosure, future research can paint a richer picture of how the various actors involved—the banks, their borrowers, the host and origin country governments, and last but not least, host country and transnational NGOs—are beginning collectively to fill the global governance gaps in this important area of economic activity that has such a direct bearing on human development all over the world.
## APPENDIX

Table 1 – *Participation Levels in Selected Multi-stakeholder Initiatives*

<table>
<thead>
<tr>
<th>Initiative</th>
<th>Entities</th>
</tr>
</thead>
<tbody>
<tr>
<td>ISO 14001 Certification</td>
<td>129,199</td>
</tr>
<tr>
<td>United Nations Global Compact</td>
<td>6,200</td>
</tr>
<tr>
<td>Global Reporting Initiative</td>
<td>2,667</td>
</tr>
<tr>
<td>Forest Stewardship Council</td>
<td>913 forest management and chain of custody certificates</td>
</tr>
<tr>
<td>Marine Stewardship Council</td>
<td>52 fisheries or fisheries in assessment</td>
</tr>
<tr>
<td>Partnerships for Sustainable Development</td>
<td>332 partnerships registered on the UN Commission for Sustainable Development</td>
</tr>
<tr>
<td>SA 8000</td>
<td>1,373 certified facilities</td>
</tr>
<tr>
<td>Ethical Trading Initiative</td>
<td>43</td>
</tr>
<tr>
<td>Fair Labor Association</td>
<td>21 “Participating Companies”; 2,900 licensees selling goods to FLA affiliated colleges and universities</td>
</tr>
<tr>
<td>Extractive Industries Transparency Initiative</td>
<td>37 companies (including an additional nine that are members of the International Council on Mining and Metals</td>
</tr>
<tr>
<td>Voluntary Principles on Security and Human Rights</td>
<td>17 corporate participants; several NGO participants and other observers; several “participating” governments (Netherlands, Norway, United Kingdom, United States of America); several “engaged” governments (Canada, Colombia, Switzerland)</td>
</tr>
</tbody>
</table>

Adapted from (Clapp 2009).
Table 2 – The First EPFIs among Top Global Lenders – 1999-2003

<table>
<thead>
<tr>
<th>BANK</th>
<th>Country</th>
<th>2003 Rank (mid-year, based on Dealogic’s ranking of amount lent)</th>
<th>2002 Rank (Project Finance International)</th>
<th>2001 Rank (Project Finance International)</th>
<th>PROJECTS</th>
<th>Percent of Total Loans Arranged in 2002 (Project Finance International)</th>
<th>Percent of Total Market in 2002: 31.4%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Citigroup</td>
<td>U.S.</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>35</td>
<td>10%</td>
<td></td>
</tr>
<tr>
<td>The Royal Bank of Scotland</td>
<td>U.K.</td>
<td>2</td>
<td>3</td>
<td>15</td>
<td>32</td>
<td>5.2</td>
<td></td>
</tr>
<tr>
<td>HypoVereinsbank</td>
<td>Germany</td>
<td>3</td>
<td>8</td>
<td>26</td>
<td>38</td>
<td>2.3</td>
<td></td>
</tr>
<tr>
<td>WestLB</td>
<td>Germany</td>
<td>7</td>
<td>4</td>
<td>2</td>
<td>28</td>
<td>4.7</td>
<td></td>
</tr>
<tr>
<td>ABN Amro</td>
<td>Netherlands</td>
<td>8</td>
<td>11</td>
<td>8</td>
<td>24</td>
<td>2.3</td>
<td></td>
</tr>
<tr>
<td>Crédit Lyonnais</td>
<td>France</td>
<td>11</td>
<td>14</td>
<td>14</td>
<td>26</td>
<td>1.7</td>
<td></td>
</tr>
<tr>
<td>Barclays</td>
<td>U.K.</td>
<td>15</td>
<td>5</td>
<td>10</td>
<td>22</td>
<td>4.1</td>
<td></td>
</tr>
<tr>
<td>Westpac</td>
<td>Australia</td>
<td>28</td>
<td>63</td>
<td>53</td>
<td>13</td>
<td>0.3</td>
<td></td>
</tr>
<tr>
<td>Rabobank</td>
<td>Netherlands</td>
<td>47</td>
<td>NR</td>
<td>NR</td>
<td>12</td>
<td>0.0</td>
<td></td>
</tr>
<tr>
<td>Credit Suisse First Boston</td>
<td>Switzerland</td>
<td>97</td>
<td>51</td>
<td>5</td>
<td>4</td>
<td>0.4</td>
<td></td>
</tr>
</tbody>
</table>

TABLE 3 – Sample Validity

<table>
<thead>
<tr>
<th>Year of Adoption</th>
<th>Study Participants (24)</th>
<th>All EPFI (65)(^{212})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Early Adopter</td>
<td>63 % (15 banks)</td>
<td>61.5 % (40 banks)</td>
</tr>
<tr>
<td>(2003-2006)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Late Adopter</td>
<td>37 % (9)</td>
<td>38.5 % (25)</td>
</tr>
<tr>
<td>(2007-2010)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Governance Level of Home Country</th>
<th>Study Participants (24)</th>
<th>All EPFI (65)(^{212})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Non-OECD</td>
<td>29.2 % (7)</td>
<td>23% (15)</td>
</tr>
<tr>
<td>Low-income</td>
<td>4.2 % (1)</td>
<td>3 % (2)</td>
</tr>
<tr>
<td>High-income</td>
<td>66.7 % (16)</td>
<td>74% (48)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Type of Institution</th>
<th>Study Participants (24)</th>
<th>All EPFI (65)(^{212})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial bank</td>
<td>83 % (20)</td>
<td>89.2% (58)</td>
</tr>
<tr>
<td>Export Credit Agency</td>
<td>8.3 % (2)</td>
<td>7.7% (5)</td>
</tr>
<tr>
<td>State-owned</td>
<td>8.3 % (2)</td>
<td>3.1 % (2)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Leadership Activities</th>
<th>Study Participants (24)</th>
<th>All EPFI (65)(^{212})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Steering Committee</td>
<td>37.5 % (9)</td>
<td>23% (15)</td>
</tr>
<tr>
<td>Working Group</td>
<td>41.5 % (10)</td>
<td>26% (17)</td>
</tr>
<tr>
<td>No Leadership Role</td>
<td>21 % (5)</td>
<td>46% (30)</td>
</tr>
</tbody>
</table>

\(^{212}\) The survey closed in early June 2010. This was before BMCE (Morocco) or Eksporfinans (the Norwegian ECA) joined. It is unclear whether ABN Amro and Fortis Bank (Nederland), which as of July 1, 2010 had merged into one entity (ABN Amro) participated separately or together or at all in the survey. For purposes of this analysis, I assume that by time the survey was circulated, these banks had already brought together their ESRM over project finance, and if they responded, they would have done so as one entity. Additionally, because of their self-declared lack of project finance activity, JP Morgan and Wells Fargo are also not considered as part of the EPFIs in the study, leaving 65 institutions.
Table 4 – *Reputational exposure and stakeholder pressures* (Fisher’s exact test (p value))

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) size</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) oecd</td>
<td>1.00</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(3) projrev</td>
<td>0.02</td>
<td>0.14</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(4) projfin</td>
<td>0.03</td>
<td>0.02</td>
<td>0.00</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(5) projrisk</td>
<td>0.32</td>
<td>0.003</td>
<td>0.04</td>
<td>0.01</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(6) advisor</td>
<td>0.25</td>
<td>0.27</td>
<td>0.00</td>
<td>0.00</td>
<td>0.00</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(7) presstransngo</td>
<td>0.04</td>
<td>0.24</td>
<td>0.51</td>
<td>0.14</td>
<td>0.16</td>
<td>0.15</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(8) pressngoorig</td>
<td>0.005</td>
<td>0.62</td>
<td>0.04</td>
<td>0.01</td>
<td>0.33</td>
<td>0.21</td>
<td>0.002</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(9) pressngohost</td>
<td>0.06</td>
<td>0.29</td>
<td>0.11</td>
<td>0.28</td>
<td>0.08</td>
<td>0.14</td>
<td>0.01</td>
<td>0.0003</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(10) pressregorig</td>
<td>0.33</td>
<td>0.67</td>
<td>0.33</td>
<td>0.43</td>
<td>1.00</td>
<td>0.16</td>
<td>0.76</td>
<td>0.445</td>
<td>0.146</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(11) pressreghost</td>
<td>0.04</td>
<td>1.00</td>
<td>0.15</td>
<td>0.48</td>
<td>0.46</td>
<td>0.41</td>
<td>0.45</td>
<td>0.055</td>
<td>0.044</td>
<td>0.000001</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(12) pressmedia</td>
<td>0.13</td>
<td>0.90</td>
<td>0.26</td>
<td>0.31</td>
<td>0.41</td>
<td>0.13</td>
<td>0.01</td>
<td>0.108</td>
<td>0.014</td>
<td>0.343</td>
<td>0.045</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(13) pressshare</td>
<td>0.81</td>
<td>0.71</td>
<td>0.95</td>
<td>0.56</td>
<td>0.02</td>
<td>0.46</td>
<td>0.46</td>
<td>0.289</td>
<td>0.389</td>
<td>0.348</td>
<td>0.038</td>
<td>0.309</td>
<td>-</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(14) presssri</td>
<td>0.17</td>
<td>1.00</td>
<td>0.09</td>
<td>0.09</td>
<td>0.23</td>
<td>0.01</td>
<td>0.17</td>
<td>0.031</td>
<td>0.00001</td>
<td>0.003</td>
<td>0.001</td>
<td>0.013</td>
<td>0.011</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(15) pressintorg</td>
<td>0.35</td>
<td>0.56</td>
<td>0.51</td>
<td>0.14</td>
<td>0.34</td>
<td>0.12</td>
<td>0.56</td>
<td>0.122</td>
<td>0.001</td>
<td>0.021</td>
<td>0.004</td>
<td>0.122</td>
<td>0.001</td>
<td>0.000001</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>(16) targetpreadopt</td>
<td>1.00</td>
<td>0.03</td>
<td>0.28</td>
<td>0.45</td>
<td>0.04</td>
<td>0.10</td>
<td>0.14</td>
<td>0.034</td>
<td>0.046</td>
<td>1.000</td>
<td>0.761</td>
<td>0.857</td>
<td>0.873</td>
<td>0.256</td>
<td>0.581</td>
<td>-</td>
</tr>
<tr>
<td>(17) targeted</td>
<td>0.25</td>
<td>0.00</td>
<td>0.01</td>
<td>0.06</td>
<td>0.01</td>
<td>0.19</td>
<td>0.03</td>
<td>0.040</td>
<td>0.02</td>
<td>0.85</td>
<td>0.15</td>
<td>0.90</td>
<td>0.41</td>
<td>0.17</td>
<td>0.56</td>
<td>0.001</td>
</tr>
</tbody>
</table>

*Size* = Global/Regional or National; *Oecd* = Non-OECD/Low-Income OECD or High-Income OECD; *Projrev* = number of projects reviewed annually on average (over last ten years), by banks’ own estimation; *Projfin* = number of projects financed annually on average (over last ten years), by banks’ own estimation; *Projrisk* = number of “high-risk” projects reviewed annually on average (over last ten years), by banks’ own estimation; *Advisor* = number of times served as an advisor to a deal in the last ten years, by banks’ own estimation; *Presstransngo* = relative level of pressure/contact experienced from transnational NGOs (ranging from no contact/pressure to intense contact/pressure); *Pressngoorig* = NGOs in country of origin pressure/contact; *Pressngohost* = NGOs in host countries pressure/contact; *Pressregorig* = regulator in country of origin pressure/contact; *Pressreghost* = regulator in host countries pressure/contact; *Pressmedia* = media pressure/contact; *Pressshare* = shareholder pressure/contact; *Presssri* = social responsible investment fund pressure/contact; *Pressintorg* = international organization pressure/contact; *Targetpreadopt* = whether targeted by public advocacy campaign prior to adopting Equator Principles; *Targeted* = targeted at any point.
Table 5 – Gamma test for reputational exposure and stakeholder pressures

<table>
<thead>
<tr>
<th>Reputational Exposure Variable</th>
<th>Stakeholder Pressure Variable</th>
<th>Gamma score (descending order of association)</th>
<th>P-value (level of significance)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Size</td>
<td>Pressregorig</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Size</td>
<td>Pressreghost</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Size</td>
<td>Presssri</td>
<td>1</td>
<td>0</td>
</tr>
<tr>
<td>Size</td>
<td>Pressngoorig</td>
<td>0.97</td>
<td>1.07E-120</td>
</tr>
<tr>
<td>Size</td>
<td>Pressngohost</td>
<td>0.93</td>
<td>1.89E-33</td>
</tr>
<tr>
<td>Size</td>
<td>Presstransngo</td>
<td>0.85</td>
<td>0.0000000007</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Pressshare</td>
<td>0.74</td>
<td>0.000001</td>
</tr>
<tr>
<td>Size</td>
<td>Pressshare</td>
<td>0.73</td>
<td>0.001</td>
</tr>
<tr>
<td>Projfin</td>
<td>Pressngoorig</td>
<td>0.73</td>
<td>0.000001</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Pressngoorig</td>
<td>0.63</td>
<td>0.002</td>
</tr>
<tr>
<td>Oecd</td>
<td>Pressngoopre</td>
<td>0.61</td>
<td>0.005</td>
</tr>
<tr>
<td>Projfin</td>
<td>Pressmedia</td>
<td>0.59</td>
<td>0.0003</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Presssri</td>
<td>0.58</td>
<td>0.005</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Pressmedia</td>
<td>0.55</td>
<td>0.01</td>
</tr>
<tr>
<td>Projfin</td>
<td>Presstransngo</td>
<td>0.53</td>
<td>0.01</td>
</tr>
<tr>
<td>Projrev</td>
<td>Presssri</td>
<td>0.51</td>
<td>0.01</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Pressngoopre</td>
<td>0.51</td>
<td>0.02</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Presstransngo</td>
<td>0.50</td>
<td>0.01</td>
</tr>
<tr>
<td>Size</td>
<td>Pressmedia</td>
<td>0.50</td>
<td>0.01</td>
</tr>
<tr>
<td>Projfin</td>
<td>Presssri</td>
<td>0.48</td>
<td>0.02</td>
</tr>
<tr>
<td>Oecd</td>
<td>Presstransngo</td>
<td>0.47</td>
<td>0.04</td>
</tr>
<tr>
<td>Projrev</td>
<td>Pressngoopre</td>
<td>0.46</td>
<td>0.02</td>
</tr>
<tr>
<td>Projrisk</td>
<td>Pressngohost</td>
<td>0.46</td>
<td>0.03</td>
</tr>
<tr>
<td>Projrev</td>
<td>Presstransngo</td>
<td>0.45</td>
<td>0.02</td>
</tr>
<tr>
<td>Projrev</td>
<td>Pressngoorig</td>
<td>0.43</td>
<td>0.03</td>
</tr>
<tr>
<td>Projfin</td>
<td>Pressngohost</td>
<td>0.39</td>
<td>0.04</td>
</tr>
<tr>
<td>Projrev</td>
<td>Pressmedia</td>
<td>0.33</td>
<td>0.059</td>
</tr>
</tbody>
</table>
Table 6 – Implementation of EP 10: Reporting Requirement

<table>
<thead>
<tr>
<th>Banktrack Report (2007) (58 EPFIs Reviewed, 11 in grace period)</th>
<th>Not Meeting Minimum</th>
<th>Meeting Minimum Number of Projects, &amp; Categorization</th>
<th>Exceeding Minimum Number of Projects, Categorization &amp; (i) Sector or (ii) Regional Breakdown</th>
</tr>
</thead>
<tbody>
<tr>
<td>40% (19) *12 did not report at all</td>
<td>19% (9)</td>
<td>40% (19)</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Current Study (2010) (24 EPFIs reporting, 4 in grace period)</th>
<th>No Contact</th>
<th>Infrequent, informal one-on-one discussions</th>
<th>Regular contact through formal meeting</th>
</tr>
</thead>
<tbody>
<tr>
<td>16.7 % (4) in grace period</td>
<td>50%</td>
<td>33%</td>
<td>78%</td>
</tr>
</tbody>
</table>

Table 7 – Frequency and Quality of Peer Contact Before and After Adoption
Table 8 – *Change in NGO pressure post-adoption*

<table>
<thead>
<tr>
<th>Description</th>
<th>Percentage</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>We had no prior contact or pressure and still have none</td>
<td>8.3%</td>
<td>(2 banks)</td>
</tr>
<tr>
<td>There has been MORE contact and/or pressure</td>
<td>58.3%</td>
<td>(14 banks)</td>
</tr>
<tr>
<td>There has been LESS contact and/or pressure</td>
<td>1.1%</td>
<td>(1 bank)</td>
</tr>
<tr>
<td>No change - the level of prior contact and pressure has remained about the same</td>
<td>29.2%</td>
<td>(7 banks)</td>
</tr>
</tbody>
</table>