Presented:
2013 International Upstream Energy Transactions

January 17 - 18
Houston, TX

Equator Principles: Project Finance and Emerging Sustainability Requirements

Gwendolyn Wilber Jaramillo

Equator Principles: Project Finance and Emerging Sustainability Requirements

UTCLE: International Upstream Energy Transactions

January 17-18, 2013

Gwendolyn Wilber Jaramillo

1. What are the Equator Principles?

The Equator Principles are the key metric by which a growing number of international financial institutions assess and manage environmental and social risks associated with project financing. Launched in 2003 by a group of private sector banks, the Equator Principles have now been adopted by 78 financial institutions in 29 countries, covering over 70 percent of international project finance debt in emerging markets.[1] These institutions include retail and investment banks, national and industry sector development companies, multi-lateral lending institutions, and export credit agencies.

The ten Equator Principles form an implementation framework for the International Finance Corporation (IFC) Performance Standards on social and environmental sustainability and the World Bank Group Environmental, Health, and Safety Guidelines (EHS Guidelines). Equator Principles Financial Institutions (EPFIs) commit not to make loans to finance development projects where they deem that the borrower will not or is unable to comply with these social and environmental policies and procedures.

The common framework of the Equator Principles, applied across projects in multiple industries and countries has permitted greater consistency, a more level playing field, in the approach and application of environmental and social risk management within the project finance industry globally. In addition, the Equator Principles are perceived to have enhanced bank – client dialogue on social and environmental issues, and provided expanded opportunities for early dialogue with affected communities and greater protection for project-affected communities and ecosystems.

Perhaps most importantly for the extractive sector, however, the Equator Principles are an increasingly robust aspect of the triad of hard and soft-law norms that govern the environmental and social risk mitigation and management of major projects: governmental regulation and requirements, internal company policy and commitments, and third party covenants and obligations. Whether as a result of partner financing obligations or a company's own choice of lender, projects subject to the Equator Principles are becoming more common. As the scope of the Equator Principles themselves expands beyond their original project finance and non-OECD country focus,

---

[1] http://www.equator-principles.com/resources/Frequently%20Asked%20Questions.pdf

it is crucial for the industry to understand their requirements and prepare to bring internal reporting and compliance structures into alignment.

2. History of Equator Principles

The Equator Principles provide a framework for the implementation by financial institutions of the substantive requirements found in the IFC Performance Standards, and also require an EPFI to commit to annual reporting of its implementation of the Equator Principles. The Performance Standards cover issues from biodiversity to community health, safety and security, were instituted in 2006, and provide guidelines for the IFC staff and its borrowers on how to prevent and mitigate social and environmental issues in the identification, preparation, and implementation of projects. The Performance Standards evolved from and replaced the IFC Safeguard Policies which were instituted by the IFC beginning in the late 1980s, and which provided guidance regarding issues ranging from indigenous people's rights and labor issues, to sector-specific guidance for forestry and dam safety.

The Performance Standards have become the de facto governing standard for social and environmental assessment of project impact. The IFC guidelines state that the IFC will only finance investment activities that are expected to meet the requirements of the Performance Standards within a reasonable period of time. Certain risks associated with an investment or business activity may require the IFC to refrain from supporting that activity. Likewise, persistent delays in meeting the requirements of the Performance Standards can lead to loss of financial support from the IFC or recourse by the IFC to contractual remedies.

As important and influential as the IFC Safeguard Policies (and later, the Performance Standards) were, they applied only to projects financed by the IFC or other institutions that elected to use them as a frame of reference. Beginning in 2002, however, a small group of private-sector banks with high profiles in the emerging markets project finance sector began seeking a way to incorporate the same types of environmental and social due diligence and risk mitigation strategies into their investment activity.

Recognizing that the IFC Safeguards presented the most recognized and well-tested standards for such, the Equator Principles were designed to provide a context for the IFC standards in private sector project finance. The four banks which initially agreed to develop a private sector banking standard – ABN Amro, Barclays, Citi and WestLB – soon grew into a group of ten initial adopting institutions. Within the first three years after the launch of the Equator Principles in June 2003, more than forty financial institutions had adopted the Equator Principles.

Following the adoption of the IFC Performance Standards, and the banks' own implementation experience, the EPFIs engaged subsequently in a review exercise to update the EPs. A revised set of Equator Principles (also known as EP II) was launched in 2006. Key changes incorporated into EP II were the lower of the dollar threshold for application of the EPs to US$ 10 million from US$ 50 million; the inclusion of Project

Title search: Equator Principles: Project Finance and Emerging Sustainability Requirements