The International Finance Corporation's Performance Standards – the new 'gold standard' or 'fool's gold'?

The International Finance Corporation – What is it?

The International Finance Corporation (IFC) is the private sector lending arm of the World Bank Group. Through the IFC, the World Bank provides financing to private corporations, for a variety of investments in lesser developed countries, such as pulp and paper mills, oil and gas pipelines, metal mines, and chemical and industrial facilities. The IFC is an important global financier and influences other international financial entities. In 2005, the IFC's committed portfolio reached US$19.3 billion and it helped to syndicate a further US$5.3 billion in financing.[1]

Over the past two decades, civil society organizations (CSOs) have drawn attention to the ecologically and socially harmful impacts of IFC-supported projects. In response to growing criticism in the late 1990s, the IFC developed a set of environmental, social and cultural safeguards and policies to minimize the impacts of their projects.

IFC's New Policy Framework

The IFC recently concluded a process to revise its safeguard policies. The review process was largely motivated by external critiques made by civil society regarding a number of highly problematic IFC-funded projects, as well as by internal critiques made by the IFC's ombudsman, the Compliance Advisor Ombudsman (CAO). In a 2003 report, the CAO criticized the IFC for failing to rigorously implement its policies, for supporting companies with negligible commitments to environmental and social responsibility, and for failing to invest in projects that reduce poverty and promote sustainable development.

IFC's new framework was an effort to address these critiques.[2] The framework includes seven key components These include the following: (1) the Policy on Social and Environmental Sustainability, which lays out IFC's responsibilities, (2) the Procedure for Social and Environmental Review of Projects, (3) eight issue-specific Performance Standards, (4) Guidance Notes for interpreting the Performance Standards, (5) Environmental Health and Safety Guidelines, the technical guidelines for projects, (6) the Action Plan, which lays out how the client will mitigate project impacts, and (7) the Disclosure Policy, which outlines what information must be publicly revealed.

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[1] For more information on the International Finance Corporation and the Multilateral Investment Guarantee Agency, see "Halifax Initiative Issue Brief - Private Sector Lending and the World Bank Group – IFC and MIGA"
[2] For more details on the new IFC framework, see "One Step Forward, One Step Back – An Overview and Analysis of the IFC's Sustainability Policy, Performance Standards and Disclosure Policy", available on-line at http://www.halifaxinitiative.org/updir/IFCAnalysis-HalifaxFINAL.pdf

Although the Performance Standards (PSs) are just one element of the IFC's new policy framework, they have received the most attention (perhaps because they relate most directly to the former Safeguard Policies).

Performance Standards – One Step Forward, One Step Back

The Performance Standards define the requirements for receiving and retaining IFC support, and set out IFC clients' roles and responsibilities for managing their projects. The Performance Standards apply to all of the IFC's investments.

There are eight Performance Standards against which IFC staff benchmark new projects. These include: Environmental Assessment and Management Systems; Labour and Working Conditions; Pollution Prevention and Abatement; Community Health, Safety and Security; Land Acquisition and Involuntary Resettlement; Biodiversity Conservation and Sustainable Natural Resource Management; Indigenous Peoples; and Cultural Heritage.

The Performance Standards are an improvement in some areas. They require more comprehensive and integrated social impact assessments. They now reference all four International Labour Organization core labour standards in their labour policy, and include a policy on community health, safety and security. In their policy on biodiversity not only recognize the Convention on Biological Diversity's definition, but also states that Standard is grounded in the Convention's objectives. That said, the Standards also suffer from significant weaknesses. For example:

- In some areas, the Performance Standards are not as rigorous as previous policies, particularly around issues of climate change, human rights, resettlement, and the protection of indigenous peoples.

- The Standards represent a shift towards a more flexible system that relies heavily on the discretion of clients and individual decision-makers at the IFC. A significant degree of leeway is permitted in their application, and non-compliance with the Standards is tolerated as long as clients continue to improve their performance.

- The Performance Standards stake out a bigger role for the client. They increase reliance on client-generated information and on self-monitoring by the private sector.

- Most importantly, the Standards do little to address the CAO's finding that the IFC has failed to select projects that meet its goal of poverty alleviation – one of the principal reasons for the review. The IFC, for example, does not provide information, on the development or poverty alleviation impacts of individual projects they support making it impossible to determine whether the investment has had a positive development impact.

The result is a system based on enhanced flexibility and subjectivity without the counter-weight of accountability and transparency. Given this, many stakeholders remain critical of the system despite some advances on particular policy issues.

The new 'gold' standard – fool's gold?

In announcing the revision process, the IFC said it aimed to position the institution as a leader in the development of international environmental and social standards that could be adopted by the private sector.

Over the years, these policies have increasingly been referenced by the private sector and public funding institutions. Many private commercial banks have adopted the IFC's Performance Standards through an initiative called the Equator Principles (EP). Through the Principles, more than 40 financial institutions, responsible for over 80 percent of global project finance, voluntarily apply the IFC's policies and environmental management system approach to their financing of projects.

In addition, through the Organisation for Economic Co-operation and Development (OECD), export credit agencies (ECAs)[3] have adopted a policy initiative called the Common Approaches. The Common Approaches sets out how ECAs take account of social and environmental considerations in their review of proposed projects. In the fall of 2006, ECAs will consider whether to reference or adopt the IFC's policies as part of the Common Approaches.

The Equator Principles however are completely voluntary, they only apply to project finance (which often forms a small portion of a bank's total portfolio), and the majority of EP bank's still disclose very little information on how the Principles are applied. The Common Approaches have also been criticized for their inconsistent application across the different OECD countries, and for having very little impact on the decision of many ECAs to finance projects despite the agreement.[4]

Furthermore, in reviewing the standards adopted by the IFC's peer institutions and the business sector, the Performance Standards are not always as rigorous, particularly around issues of climate change, human rights, the protection of indigenous peoples and biodiversity.[5]

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[3] Export credit agencies are (ECAs) are publicly owned agencies that lend or provide insurance to corporations to do business abroad.

[4] See for example, "Race to the Bottom – Take 2", ECA-Watch, http://www.eca-watch.org/eca/race_bottom_take2.pdf

[5] WWF/BankTrack, *Shaping the Future of Sustainable Finance: Moving from Paper Promises to Performance,* January 2006.

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