

Ensuring Public Accountability for Private International Financing of Natural Resource Development Projects: Implications of the UN Rule of Law Project for the Equator Principles

by

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Abstract

A striking feature of public international financing of natural resource development projects in developing economies is the introduction of public accountability mechanisms to ensure that these projects comply with social and environmental principles and standards. For example, natural resource development projects funded through the World Bank group are subject to the Inspection Panel mechanism in relation to complaints about the negative social and environmental impacts of such projects. As the public international financing of such projects is increasingly giving way to private international finance, this paper will examine whether similar accountability mechanisms have been developed for this type of private international financing for such projects. Within this context, the third iteration of the Equator Principles Financial Institutions (EPFIs). By comparing the accountability mechanisms established by public and private international finance institutions against

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objectively set criteria for such mechanisms, based on the UN's international 'rule of law' project, this paper will assess whether there has been adequate replication of public accountability standards in the movement from public to private international financing of natural resource projects, especially within developing economies.

Introduction

As humankind's global search for natural resources both widens and deepens across the world, the international finance packages for funding resource development projects in remote developing countries, situated far away from the final market destinations of these resources, have become ever more intricate. A number of different forms of international financing mechanisms are available for such infrastructure projects, namely, 'government funding', 'corporate (or on-balance sheet) finance', and 'project finance'. In summary, arguably the simplest form of international infrastructure financing is through government funding, when a national government chooses to fund some or all of the capital investment in a project and looks to the private sector to bring in expertise and efficiency. This is generally the case in a so-called 'Design-Build-Operate' project where the operator is paid a lump sum for completed stages of construction and will then receive an operating fee to cover operation and maintenance of the project. In the corporate (or on-balance sheet) finance model, the private operator finances some of the capital investment for the project through corporate financing – which involves the private operator getting finance for the project based on the balance sheet of that private operator. This is typically the mechanism used in lower value projects where the cost of the financing is not significant enough to warrant a project financing

mechanism (summarized below) or where the operator is so large that it chooses to fund the project from its own balance sheet. The benefit of corporate finance is that the cost of funding will be the cost of funding of the private operator itself and so it is typically lower than the cost of funding of project finance. It is also less complicated than project finance. However, there is an opportunity cost attached to corporate financing because the company will only be able to raise a limited level of finance against its equity (debt to equity ratio) and the more it invests in one project the less it will be available to fund or invest in other projects. Finally, one of the most common - and often most efficient - financing arrangements for public-private partnership (PPP) projects is 'project financing', also known as 'limited recourse' or 'non-recourse' financing. Project financing normally takes the form of limited recourse lending to a specifically created project company/entity (also known as a special purpose vehicle (SPV)) which has been awarded the right to carry out the construction and operation of the project. It is typically used in a new build or extensive refurbishment situation and so the SPV has no existing business. The SPV will be dependent on revenue streams from the contractual arrangements and/or from tariffs from end users which will only commence once construction has been completed and the project is in operation. It is therefore a risky enterprise and before they agree to provide financing to the project the lenders will want to carry out an extensive due diligence on the potential viability of the project and a detailed review of whether the project risk allocation protects the project company sufficiently. This is known commonly as verifying the project's "bankability". The increasing popularity of this form of international financing model for large infrastructure projects will be the focus of this paper in terms of the public accountability of these SPVs, as well as the private international

finance institutions that are their lenders.¹

Prior to embarking on the above analysis, it is also important to note that new international financing models are being contemplated and implemented all the time. For example, the Resource Financed Infrastructure (RFI) initiative is latest type of international finance vehicle being contemplated by international finance policy decision-makers. The World Bank's Public-Private Infrastructure Advisory Facility (PPIAF) describes the RFI model as 'a contractual arrangement that permits governments to link expected revenues from production rights granted to investors for the development of natural resources, to a loan for construction of unassociated infrastructure today. In the RFI model, the government pledges its future revenues from the resources to finance the development of infrastructure.'² However, like many other international financing models being utilized for major infrastructure development and maintenance projects within developing economies, legal and institutional challenges arise, especially in relation to public accountability for these projects.³ International investment risk management is a significant

¹ See: 'Major Financing Mechanisms for Infrastructure Projects', in World Bank Group *et al*, Public-Private Partnership in Infrastructure Resource Center, at:

<http://ppp.worldbank.org/public-private-partnership/financing/mechanisms#corporate>

² <http://www.ppiaf.org/feature-story/resource-financed-infrastructure-discussion-new-form-infrastructure-financing>

³ Halland, Håvard, John Beardsworth, Bryan Land, and James Schmidt, *Resource Financed Infrastructure: A Discussion on a New Form of Infrastructure Financing*. World Bank Studies.

Washington, DC: World Bank (2014) Accessible from: <http://www->

aspect of all these public/private international financing arrangements, with the diversity and extent of different types of risk being important factors to be considered in any international finance package. Among these different types of investment risks, both social resilience and environmental protection are increasingly becoming imperative considerations. As these social and environmental risks become a central plank of the international financial planning process for these types of projects, the inability of domestic government structures to adequately address these types of risks in itself becomes a significant political risk factor within any international financial decision-making process. The actual (or perceived) inadequacies of domestic governmental accountability mechanisms has resulted in the prescription of international governance systems to take their place.

Thus, a striking feature of *public* international financing of natural resources development projects in developing economies is the introduction of public accountability mechanisms to ensure that these projects comply with social and environmental principles and standards. For example, natural resource development projects funded through the World Bank group are subject to the Inspection Panel mechanism in relation to complaints of the negative social and environmental impacts of such projects. As the *public* international financing of such projects increasingly acts in tandem with *private* international finance mechanisms (summarized above), this paper will first examine whether similar

wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2014/06/06/000333037_20140606143941/Rendered/PDF/884850PUBoBox300EPI2102390May292014.pdf

public accountability mechanisms have been established for projects relying on this type of private international financing. Within this context, a third iteration of the Equator Principles (EP) has recently been adopted by a growing number of private international financing institutions in the project finance field, namely, the Equator Principles Financial Institutions (EPFIs). By comparing the accountability mechanisms established by public and private international finance institutions against objectively set criteria for such mechanisms, based on the UN's international 'rule of law' project, this paper will assess whether there has been adequate replication of public accountability standards in the movement from public to private international financing options for natural resource projects, especially within developing economies.

Prior to engaging fully with these accountability mechanisms, this paper will first consider the separate but recent United Nations (UN) engagement with the international 'rule of law' project and in particular, attempts to assimilate the 'rule of law' into the sustainability objective of UN development goals. The challenge articulated and addressed in this paper is to examine whether the international normative framework currently being developed through the UN's international 'rule of law' project can be extended to include the private, transnational economic actors that have agreed to establish similar accountability mechanisms under the Equator Principles. In previous writing on the Equator Principles, I postulated the argument that the promulgation of these Principles represented a transnational social and environmental norm-

iteration (as opposed to norm-making) process designed to encompass private entities within the ambit of international environmental law.⁴

In this paper, the analytical focus shifts to an examination of the grievance mechanisms mandated upon *private*, international finance institutions under the Equator Principles.⁵ This examination will be undertaken within the context of the UN's international 'rule of law' project currently aimed, *inter alia*, at improving *public* institutional accountability both within and across States. Thus far, the international 'rule of law' project, and specifically, the UN-sponsored efforts on its behalf, has shown an appreciation of the need to link 'rule of law' considerations and criteria to those of sustainable development, most notably in the enhancement of public participation opportunities within governmental decision-making processes to ensure the accountability of *public* authorities for their efforts at achieving sustainable development. More recent UN-based activities, especially under the auspices of the UN Environment Programme (UNEP) have paved the way towards an 'environmental rule of law'. Following this analytical pathway, it is notable that both (public) governmental and (public/private) governance structures are envisaged as delivering the 'environmental rule of law', thereby allowing the Equator Principles to become the focus of this paper in terms of whether these Principles

⁴ David M. Ong, 'From 'International' to 'Transnational' Environmental Law? A Legal Assessment of the Contribution of the 'Equator Principles' to International Environmental Law', *Nordic Journal of International Law* (NJIL), Vol.79, Issue 1 (2010) 35-74.

⁵ Specifically, Principle 6 of the Equator Principles, which proposes the establishment of local grievous mechanisms.

can deliver the goods on this front. The present line of enquiry will reflect on the public/private nature of the 'rule of law' project itself. Specifically, can accountability mechanisms established by private, transnational agreements such as the Equator Principles assist the delivery of the 'rule of law' in relation to the social and environmental risks arising from such natural resource development projects. Contemplating this apparent dichotomy between public and private accountability, it is proposed to re-cast this relationship as one that is dialectical in nature, rather than intrinsically public or private in its constitutive elements. This dialectical relationship between public and privately established accountability mechanisms arguably follows a similar dialectic identified within a 'rule of law' research project whereby the term 'dynamics' is utilized to refer not only to the increasing international and transnational dimensions of rule of law promotion, but also to the interaction between the international and domestic levels of law, in an era of international and transnational governance. Within this two-way relationship, international law and especially international institutions, try to inculcate the development of the 'rule of law' at the domestic and municipal levels; while at the same time, common 'rule of law' standards are being sought at the international level itself.⁶

⁶ Michael Zürn, André Nollkaemper & Randy Peerenboom, Introduction to *Rule of Law Dynamics in an Era of International and Transnational Governance* (CUP, 2012)

I. The International ‘Rule of Law’ Project

Writing on the role of the ‘rule of law’ in societies generally, and political orders specifically, Fukuyama defines it as ‘a set of rules of behavior, reflecting a broad consensus within the society, that is binding on even the most powerful political actors in the society, ...’⁷ In this sense, he distinguishes between the ‘rule of law’ and the ‘rule by law’, the latter of which he characterizes as law in the form of commands issued by the ruler that are not binding on the ruler herself.⁸ Similarly, when addressing the rule of law and democracy nexus, a concept note by the International Institute for Democracy and Electoral Assistance (IDEA) and the International Development Law Organization (IDLO) draws a fundamental distinction between the ‘rule by law’, whereby law is an instrument of government and government is considered above the law, and the ‘rule of law’, which implies that everyone in society is bound by the law, including the government. Essentially, constitutional limits on power, a key feature of democracy, requires adherence to the rule of law.⁹ However, as Walker has recently emphasized, this notion of the ‘rule of law’ as simply the converse of the ‘rule of man’ tends to be narrowly focused on the control of government and/or other institutions of the State, as opposed to reining in

⁷ Francis Fukuyama, *Political Order and Political Decay*, London: Profile Books (2014) at 24.

⁸ *Ibid.*

⁹ International Institute for Democracy and Electoral Assistance (IDEA) and International Law Development Organization (IDLO) Informal Discussion note on ‘Linkages between the Rule of Law, Democracy and Sustainable Development’, 19 April 2012, at the Permanent Mission of Italy to the UN in New York, USA. 6pp, at 2. Accessible at:

<http://www.idea.int/un/upload/Concept-Note-IDEA-IDLO-Italy-rev-5-0-Final.pdf>

corporate and other private interest groups.¹⁰ Moreover, the traditional ‘rule of law’ objective of limiting State power tends to negate the capacity of the State to enable private entities to undertake activities hitherto regarded as solely within the province of the State, as well as allow market forces to control their relationship with the general public,¹¹ subject to, *inter alia*, social and environmental constraints established by public international law. Mazzucato goes even further, arguing recently that through different types of public-private interaction, States can lead the creation of markets and indeed entire new economic landscapes.¹²

These insightful observations allow us to turn our attention to the specific question posed here as to whether, and to what extent, the goals/objectives of the international ‘rule of law’ project can be achieved through the intervention of *private* entities, especially in the mitigation of such social and environmental risks. Returning to the specification of the ‘rule of law’ for practical purposes, Chesterman established at least three possible meanings of the ‘rule of law’, the third of which denotes the emergence of a ‘global’ rule of law, constituting a normative regime that touches individuals directly without formal mediation through existing national institutions.¹³ It is this third meaning of the ‘rule of

¹⁰ Neil Walker, *Intimations of Global Law*, CUP (2015) at 83.

¹¹ Walker (2015) *ibid.*, at 83, citing Bruce Z. Tamanaha, *On the Rule of Law: History, Politics, Theory*, CUP (2005)

¹² Mariana Mazzucato, ‘The Innovative State: Governments should make markets, not just fix them’, *Foreign Affairs*, Vol.94, No.1 (January/February, 2015) 61-68, at 62-63, & 68.

¹³ Simon Chesterman, ‘An International Rule of Law?’ *American Journal of Comparative Law*, Vol. 56, No. 2 (Spring, 2008), 331-361, at 355-56.

law’ which resonates most with the focus of this paper, namely, the relationship between the international ‘rule of law’ project, the Equator Principles (EP) and its members – the Equator Principles Financial Institutions (EPFIs), and the accountability of public/private financing of natural resource development projects for their social and environmental risks.

As alluded to above, the UN is spearheading global efforts at achieving the ‘rule of law’ both within and across States around the world. Both the UN General Assembly and the Security Council have addressed the importance of the rule of law for the UN and its Member States, the highlights of which are summarized here as follows: In 2004, the Secretary-General stressed that for the UN, the ‘rule of law’ is ‘a principle of *governance*, rather than just *government*, in which all persons, institutions and entities, public and private, including the State itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and which are consistent with international human rights norms and standards. It requires as well measures to ensure adherence to the principles of supremacy of the law, equality before the law, accountability to the law, fairness in the application of the law, separation of powers, participation in decision-making, legal certainty, avoidance of arbitrariness, and procedural and legal transparency.’¹⁴ It is noteworthy that even at this early stage of the UN’s project, the ‘rule of law’ was conceived as a principle of *governance*, thus denoting a pluralistic attitude to

¹⁴ ‘The rule of law and transitional justice in conflict and post-conflict societies’, Report of the UN Secretary-General to the UN Security Council, S/2004/616 (23 August, 2004) at para.6, p.4.

the multiple forms of accountability required to ensure the application of the ‘rule of law’ at the international and national levels of jurisdiction. The Guidance Note of the Secretary-General on the UN Approach to Rule of Law Assistance (2008) then provides overarching guiding principles and a policy framework to guide UN rule of law activities at the national level.¹⁵ Referring explicitly to the 2004 definition of the ‘rule of law’ in his 2009 Guidance Note on Democracy, the Secretary-General also added that the UN provides expertise and support to ‘the development of legislation and the strengthening of, in particular, legislative, executive and judicial institutions under such principles to ensure that they have the capacity, resources and necessary independence to play their respective roles.’¹⁶

The third annual report of the Secretary-General on ‘Strengthening and coordinating United Nations rule of law activities’¹⁷ informed UNGA deliberations on this issue, which were concluded by the adoption of resolution 66/102 in December 2011, which held that the advancement of the rule of law at the national and international levels is essential for, *inter alia*, sustainable

¹⁵ Guidance Note of the UN Secretary-General, UN Approach to Rule of Law Assistance, April, 2008. Accessible at:

<http://www.unrol.org/files/RoL%20Guidance%20Note%20UN%20Approach%20FINAL.pdf>

¹⁶ Guidance Note of the UN Secretary-General on Democracy, at p.7. Accessible at:

http://www.un.org/democracyfund/sites/www.un.org.democracyfund/files/file_attach/UNSG%20Guidance%20Note%20on%20Democracy-EN.pdf

¹⁷ A/66/133, 8 August 2011.

development.¹⁸ The UN Security Council debate on ‘The promotion and strengthening of the rule of law in the maintenance of international peace and security’ on 19 January 2012, then addressed the rule of law dimension from the angle of its contribution to peaceful coexistence and the prevention of armed conflict.¹⁹ In March 2012, the Secretary-General issued a further report on an action programme for *Delivering Justice*,²⁰ which prescribed, *inter alia*, policy actions on relevant issues, such as ‘strengthening the rule of law at the national level’, as follows:

‘19. Within justice, security and law-making institutions, it is important to enhance transparency, accountability and oversight, and to widen participation in decision-making processes, in order to build public confidence and trust. In this connection: Member States should ensure that their legal frameworks include basic principles of open government, such as fiscal transparency, access to information, disclosures related to public officials, accountability, remedies and oversight mechanisms, protection measures for whistle-blowers and witnesses, and public engagement in policy and decision-making, and that such legal frameworks are effectively implemented.’

¹⁸ UNGA Resolution 66/102, ‘The rule of law at the national and international levels’, adopted: 9 December, 2011, A/RES/66/102, 13 January, 2012.

¹⁹ Statement by the President of the UN Security Council, S/PRST/2012/1, 19 January 2012.

²⁰ Report of the Secretary-General, *Delivering justice: programme of action to strengthen the rule of law at the national and international levels*, UNGA Sixty-sixth session, Agenda item 83, The rule of law at the national and international levels, A/66/749, 16 March 2012. Accessible at:

Within this context, support for the role of ‘civil society’ and ‘traditional and informal justice systems’ in the ‘rule of law’ project is explicitly acknowledged as follows:

‘22. The rule of law is strengthened when all individuals are empowered to claim their rights, to request effective remedies and to express legitimate demands on public institutions for accountability in the fair and just delivery of public services. Civil society organizations, including professional associations of lawyers, prosecutors and judges, academic and policy research institutions, paralegal organizations and advocacy organizations focusing on the rule of law, all make important contributions to strengthening services that ensure the rule of law, especially by empowering and informing individuals. In this connection: Member States should commit themselves to granting all individuals their full right to association and assembly, and to supporting civil society organizations and giving them the necessary legislative and political space to thrive. ...

23. Member States may have justice mechanisms based on tradition, custom or religion operating alongside State institutions. These systems can play an important part in the delivery of justice services, including the adjudication and determination of disputes. In this connection:

(a) Member States and the United Nations should ensure that all laws and justice mechanisms, including traditional and informal justice mechanisms, are in line with international norms and standards;

(b) Member States should develop strategies for clarifying and strengthening the relationship between traditional and informal justice systems and formal justice systems;

(c) Member States should develop strategies for ensuring that everyone, particularly women and those belonging to vulnerable or otherwise marginalized groups, enjoys equal access to justice within all justice delivery mechanisms.’

Significantly for our purposes in this paper, the UN Secretary-General also explicitly acknowledged the ‘rule of law’ as an essential component when ‘fostering an enabling environment for sustainable human development’, as follows:

‘26. Sustainable human development is facilitated by a strong rule of law. The provision and implementation of stable and predictable legal frameworks for businesses and labour stimulate employment by promoting entrepreneurship and the growth of small and medium-sized enterprises, and attracting public and private investment, including foreign direct investment. The link between economic development and the rule of law has long been established. Rising inequalities in wealth within and among countries are now a key concern with the potential to weaken and destabilize societies. The United Nations supports the development of a holistic sustainable human development agenda that addresses the challenges related to inclusive growth, social protection and the environment. In such an agenda, the rule of law must play a critical role in ensuring equal protection and access to opportunities.’

Curiously, these social and environmental concerns apparently do not necessitate inclusion within the next section of the UN action programme, namely, ‘strengthening the nexus between the rule of law at the national and

international levels.’ Thus, there remains an abiding feeling of disconnection between these UN institutional initiatives on the ‘rule of law’ and action on the ground, especially in relation to the social and environmental issues of the sustainable development agenda.

II. The Rule of Law and Sustainable Development

Enlarging upon the relationship between the two concepts, it is a truism that many facets of the rule of law form essential components of sustainable development. As the IDEA and IDLO assert in their note, the rule of law provides the normative and institutional framework by which to enable the equitable realization of basic rights and fair access to benefits accruing from the resources available to the country and its society. It also helps to ensure stability, clarity, precision, predictability and transparency in public and private law processes including in contractual, commercial and foreign direct investment sectors. These processes, if they operate with consistency, fairness and on a non-discriminatory basis, help to spur growth, create wealth and reduce rent-seeking and corruption.²¹ As the UN Secretary-General pointed out in his Report on ‘Delivering Justice’: ‘Environmental degradation, rapid urbanization, conflict, fragility, severe income inequalities and exclusion of vulnerable groups constitute major challenges to human development and security. Robust principles are needed to underpin the management of our

²¹ IDEA & IDLO Informal Discussion note (2012), *op. cit.*, at pp.3-4.

future. The rule of law is a core principle of governance that ensures justice and fairness, values which are essential to our humanity'.²² This approach echoes the UN General Assembly's unequivocal position on the interconnection between rule of law and sustainable development: 'The advancement of the rule of law at the national and international levels is essential for the realization of sustained economic growth, sustainable development, the eradication of poverty and hunger and the protection of all human rights and fundamental freedoms.'²³ The IDEA/IDLO note reiterates that the international community has affirmed on many occasions that strengthening the rule of law and bringing the law closer to the people are effective tools by which to promote economic and social advancement in the global efforts to achieve the Millennium Development Goals (MDGs) and to meet other pressing global challenges.²⁴

A further critical element of rule of law approaches to development identified by the IDEA/IDLO is the need to empower traditionally marginalized social groups, including women, in political decision-making as well as in the marketplace, and in particular, though unimpeded access to remedies in case of the violation of rights. Development is less likely to take root in a sustainable fashion unless reforms are owned by civil society and supported by NGOs, and in this connection, the rule of law forms a pivotal point of reference for the empowerment and participation of marginalized groups. Empowering people

²² 'Delivering justice: programme of action to strengthen the rule of law at the national and international levels', 16 March 2012, A/66/749, at para.1.

²³ UNGA, A/RES/66/102 of 13 January 2012.

²⁴ IDEA & IDLO Informal Discussion note (2012), *op. cit.*, at pp.3-4.

to use law and legal processes strengthens the capacity of local communities to guarantee access to justice on a fair and non-discriminatory basis. It also allows individuals and groups to engage more equitably with justice systems rooted in non-state, informal and traditional fora. Considering that these non-state systems, including indigenous, customary and religious legal orders, alternative dispute resolution mechanisms and popular justice fora, figure as important or even principal avenues through which the poor can access justice, engagement with such systems to bring them into closer line with international norms and standards becomes key to strengthening the rule of law in development contexts.²⁵ The IDEA/IDLO note also observed that the past forty years have shown that the rule of law at national and international levels can make a significant contribution toward forging an enduring partnership between the environment and development founded on ecological and social sustainability. Judging by the continuing trajectory of rapid environmental degradation and natural resource depletion, it is, however, universally recognized that its full potential has yet to be realized. Recognizing environmental law as a foundation for environmental sustainability and realizing its full potential is ever more urgent in our quest towards sustainable development and new economic growth, but also towards just and fair societies vis-à-vis growing environmental pressures.²⁶

That the rule of law plays an important role in environmental matters was re-

²⁵ *Ibid.*

²⁶ *Ibid.*

affirmed through the Rio+20, UN Conference on Sustainable Development,²⁷ and UNEP's World Congress on Justice, Governance and Law for Environmental Sustainability,²⁸ both held in June 2012. At the World Congress more than 250 of the world's Chief Justices, Attorneys General and Auditors General seized a generational opportunity to contribute to the debates on the environment and declare that any diplomatic outcomes related to the environment and sustainable development from the Rio+20 Conference, would remain unimplemented without adherence to the rule of law, in the form of open, just and dependable legal orders. Similarly, the outcome document of Rio+20, namely, the UNGA Resolution entitled: 'Future We Want',²⁹ reaffirms the central role to be played by the rule of law on the path towards sustainable development and makes it a prerequisite for a successful transition to greener economies. This Resolution also highlights the crucial role played by national judiciaries in ensuring fairness and equity in the implementation of policies to further sustainable development. These developments are underpinned and bolstered by the recently adopted UNGA Resolution on the Rule of Law,³⁰ which underlines the importance of fair, stable and predictable legal

²⁷ Held at Rio de Janeiro, Brazil, 20-22 June, 2012. Documentation accessible at:

²⁸ Held at , 20-22 June, 2012. Documentation accessible at:

²⁹ UNGA Resolution 66/288, adopted on 27 July, 2012. A/RES/66/288 (11 September 2012)

Accessible at:

³⁰ A/RES/67/1

frameworks for generating inclusive, sustainable and equitable development and maintaining peace and security.³¹

Both the International IDEA and IDLO resolved that the work of the UN must link the rule of law, democracy building and sustainable development. Such linkages are increasingly emerging in key areas, at least three of which, *inter alia*, are significant for our purposes here, as follows:

- □ □ Engagement with non-state and informal legal and justice systems: How can informal justice systems assist in realizing social and economic rights and promote inclusive development? To what extent should the international community engage with such systems as part of a broader rule of law debate/ quest for definition?
- □ □ The empowerment of civil society, inclusive development and engaging with non-state actors: How could non-state actors, including civil society organizations, participate more meaningfully and effectively in processes aimed at strengthening the rule of law?
- □ □ Public-private partnership and the role of the private sector: How can rule of law support development through engagement with and integration of private and corporate sectors in the development discourse?³²

³¹ UNGA Resolution, 67/1. Declaration of the High-level Meeting of the General Assembly on the Rule of Law at the National and International Levels, A/RES/67/1, 30 November, 2012. Accessible at: <http://www.unrol.org/files/A-RES-67-1.pdf>

³² IDEA & IDLO Informal Discussion note (2012) *op. cit.*, at p.6.

III. From the ‘Rule of Law and Sustainable Development’ to an ‘Environmental Rule of Law’

This critical nexus between the rule of law and environmental sustainability in the context of sustainable development was then highlighted by the World Congress on Justice, Governance and Law for Environmental Sustainability that UNEP organized on the eve of the Rio+20 Conference, in 2012. At this World Congress, which has been described as the most encouraging and progressive work of Rio+20 from a legal perspective,³³ over 250 of the world’s Chief Justices, Attorneys General and Auditors General seized a generational opportunity to contribute to the debates on the environment and declare that any diplomatic outcomes related to the environment and sustainable development, including from Rio+20, would remain un-implemented without adherence to the rule of law, in the form of open, just and dependable legal orders.³⁴

This was followed by UNEP Governing Council Decision 27/9, on ‘Advancing Justice, Governance and Law for Environmental Sustainability’, adopted by the first universal session of UNEP’s Governing Council in February 2013,³⁵ which recognized the growing importance of rule of law in the field of the environment

³³ Ann Powers, ‘The Rio+20 Process: Forward Movement for the Environment?’, *Transnational Environmental Law*, Vol.1, Issue 2 (October, 2012) at 403-412, at 412.

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³⁵ Accessible at: http://www.unep.org/delc/Portals/24151/Documents/Decisions27-9Advancing_Justice_Governance&Law.pdf

in order to reduce violations of environmental law and to achieve sustainable development overall. Decision 27/9 is the first internationally negotiated document to utilize the term ‘environmental rule of law’, requesting the UNEP Executive Director, *inter alia*, ‘(t)o lead the United Nations system and support national Governments upon their request in the development and implementation of *environmental rule of law* with attention at all levels to *mutually supporting governance features*, including information disclosure, public participation, implementable and enforceable laws, and implementation and accountability mechanisms including coordination of roles as well as environmental auditing and criminal, civil and administrative enforcement with timely, impartial and independent dispute resolution; ...’³⁶ The constituent elements of environmental rule of law can be said to include, *inter alia*, adequate and implementable laws, access to justice and information, public participation, accountability, transparency, liability for environmental damage, fair and just enforcement, and human rights.³⁷ Inclusion of the phrase ‘mutually supportive governance features’ is arguably both recognition as well as paving the way for these collective environmental rule of law services to be facilitated by private entities, either alongside, or possibly even in place of traditional public authorities. Here is where the grievance mechanisms

³⁶ Para.6(a) of Decision 27/9, adopted at the Twenty-seventh session of the Governing Council/Global Ministerial Environment Forum, Nairobi, 18–22 February 2013, UNEP/GC.27/17, 12 March, 2013. (emphasis added)

³⁷ See 1st Asia-Pacific International Colloquium on Environmental Rule of Law, Putrajaya Statement, Putrajaya, Malaysia, 12 December, 2013. Accessible at:

envisaged by the Equator Principles can be located within the broad context of the rule of law and sustainable development of natural resources.

Implementation of UNEP Governing Council decision 27/9, UNEP/Env.Law/MTV4/MR/1/2/Add.1, 20 August 2015, Report on the implementation of the Fourth Programme for the Development and Periodic Review of Environmental Law (Montevideo Programme IV) for the period 2010–2014. Meeting of senior government officials expert in environmental law on the midterm review of the fourth Programme for the Development and Periodic Review of Environmental Law (Montevideo Programme IV) Montevideo, 7–11 September 2015. Accessible at: <http://www.unep.org/delc/Portals/119/documents/montevideo/addendum-gc27-9.pdf>

Institutionally, UNEP has continued to pursue the ‘environmental rule of law’ project through the establishment of a UN Environment Assembly (UNEA), as well as the convening of a symposium on the ‘environmental justice and sustainable development’ theme in June, 2014 on the occasion of the 1st session of the UNEA.³⁸ However, the uneven treatment of the application of the ‘rule of law’ continues in the UNEP concept note for this symposium. Although it is initially described ‘a central attribute of good governance’, the ‘rule of law’ is then held to revert to its traditional role as a constraint to the arbitrary exercise of public power, without mentioning its potential utility for constraining private power as well. Nor does this description of the ‘rule of law’ appear to allow for

³⁸ Environmental Justice and Sustainable Development - A Global Symposium on Environmental Rule of Law, on the occasion of the 1st Session of the United Nations Environment Assembly (UNEA), 24 June 2014, Nairobi, Kenya, Preliminary Background Note – Version of 3 June 2014.

Accessible at: http://www.unep.org/unea/docs/background_note_erol.pdf

the establishment of grievance mechanisms by private entities, as envisaged by the Equator Principles, for example.

IV. Implementing the ‘Environmental Rule of Law’ through Accountability Mechanisms for Public and Private International Finance Institutions

The growing calls for accountability and even responsibility of these public and private international finance institutions are being answered through further institutional developments. In *Policing the Banks*, for example, van Putten calls for the global accountability of *all* powerful financial players, including the ‘transnational’ private banks that are now co-funding, usually alongside public international finance institutions, many development projects in third world countries. Describing how such private financial institutions have been slow to accept responsibility for the consequences of their investments, even when they cause significant social and environmental damage in developing countries, she argues that new accountability mechanisms are necessary to reduce or prevent such damage. Moreover, because such institutions operate on a global scale, only semi-judicial accounting mechanisms can provide the necessary accountability. According to van Putten, it is time for the private financial sector to follow multilateral financial institutions in creating independent mechanisms, mediation procedures, and access to decision makers for people harmed or potentially harmed by projects financed by their institutions.³⁹

³⁹ Maartje van Putten, *Policing the Banks: Accountability Mechanisms for the Financial Sector*, McGill-Queen’s University Press (2008)

A. Accountability of Public International Finance Institutions: The World Bank Group

The establishment of World Bank's Inspection Panel offers lessons for advocates of greater accountability for decision-making within both public, and increasingly also private, international finance institutions. One of these lessons is arguably to focus advocacy policy and campaigning practice not just on the institution itself, but also on its own sources of finance. In the case of the World Bank, human rights and environmental NGOs targeted both the Bank itself but perhaps more significantly, its main donor – the United States (US) government and specifically, US congressional leaders who controlled funding to World Bank agencies. Indeed, so successful was this NGO lobbying exercise that the corresponding pressure placed by the US Congress on World Bank accountability for its operational policies and funding strategies has recently been held up as an example of how to ensure the democratic legitimacy of international organizations generally.⁴⁰

According to Szablowski, this pressure ultimately resulted in the establishment of the Inspection Panel in 1993.⁴¹ He observes however that: 'While the Panel

⁴⁰ Kristina Daugirdas, 'Congress Underestimated: The Case of the World Bank', *American Journal of International Law* (2013) 517-562.

⁴¹ David Szablowski, *Transnational Law and Local Struggles: Mining, Communities and the World Bank*, Hart (2007) at 90-91, citing, *inter alia*, J A Fox and I D Brown (eds), *The Struggle for Accountability: The World Bank, NGOs and Grassroots Movements*, MIT Press (1998) at 8; S Schlemmer-Schulte, 'The World Bank Inspection Panel: A Record of the First International Accountability Mechanism and Its Role for Human Rights', *Human Rights Brief*, Vol.6:2 (1998) 279.

operates autonomously of Bank management and with significant public transparency, it lacks independence of a judicial institution.’⁴² Moreover, as Fox notes, ‘the panel’s very existence challenges key assumptions of national sovereignty’⁴³ by allowing the citizens of borrowing countries (that are hosting the projects funded by these international finance institutions) to present their claims directly before an international complaints mechanism.⁴⁴ This last point resonates with the aims of the present exercise in seeking to determine possible avenues for exerting accountability against these public international finance institutions, for compliance with social and environmental protection norms. However, it also exposes the potential pitfalls of such an approach, if it is perceived to go against the democratically legitimate sovereign decisions of any country that chooses to prioritize socio-economic development at the expense of certain human rights and environmental protection standards.

On the other hand, Darrow observes that the establishment of the Inspection Panel helps ensure that the compliance of both the in-country Task Manager, and therefore indirectly also the borrowing country, with the World Bank’s Operational Standards, including those on human rights and environmental protection.⁴⁵ The normative significance of the establishment of such an institutional compliance and accountability mechanism, along with the

⁴² *Ibid.*, at 91.

⁴³ J A Fox, ‘The World Bank Inspection Panel: Lessons from the First Five Years’, *Global Governance*, Vol.6 (2000)

⁴⁴ Szablowski (2007) *op. cit.*, at 91.

⁴⁵ Mac Darrow, *Between Light and Shadow: The World Bank, The International Monetary Fund and International Human Rights Law*, Hart (2003) at 143.

jurisprudence it has since generated is notable.⁴⁶ This is especially the case when it is observed that, in the performance of its latter function, the Panel is the first forum in which individuals can hold an international organization directly accountable for the consequences of its failure to follow its own rules and procedures.⁴⁷ Both the International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA), as the so-called private sector components of the World Bank, are also held accountable to the Compliance Advisor/Ombudsman (CAO), which is an independent recourse mechanism available to project-affected people. According to Darrow, the success of the Inspection Panel in this path-breaking role is evidenced by ‘... the establishment of similar grievance mechanisms across a range of other international financial institutions’, although he goes on to note that the powers of the Compliance Advisor/Ombudsman (CAO) of the International IFC are more focused on conciliation and arbitration.⁴⁸ Both these public international finance institutions also have policy commitments that require the establishment of grievance mechanisms within their Policy and Performance Standards on Social and Environmental Sustainability and Guidance Notes. Similar principles are applied in the context of Principle 6 of the EP, which is derived from the World Bank approach and will be considered further in the next section. However, if a grievance cannot be initially resolved by the local

⁴⁶ Benedict Kingsbury, ‘Operational Policies of International Institutions as Part of the Law-Making Process: The World Bank and Indigenous Peoples’, in G Goodwin-Gill & S Talmon (eds) *The Reality of International Law: Essays in Honour of Ian Brownlie* (1999) 323-42, at 332.

⁴⁷ D Bradlow, ‘International Organizations and Private Complaints: The Case of the World Bank Inspection Panel’, *Virginia Journal of International Law* Vol.34(3) (1994) 553-613, at 554.

⁴⁸ Darrow (2003) *op. cit.*, at 144, fn.148.

grievance mechanism established by the IFC or MIGA the complainant may refer to an external party such as the court system, traditional systems of justice or the CAO. Torrance suggests that within this context, such grievance mechanisms are a form of alternative dispute resolution (ADR) that must be seen to co-exist with judicial avenues available to complainants.⁴⁹ This relationship is made clear in the IFC Performance Standards, which requires for example that grievance mechanisms must not operate in such a way as to foreclose access to judicial remedies for claimants. Any concern or complaint to these grievance mechanisms arising from a legitimate stakeholder will also foretell of possible legal risks to the borrower and both the public international finance institutions (under the IFC Performance Standards) and private international financial Institution (under the Equator Principles) involved in the project.⁵⁰

B. The Equator Principles: A Private International Finance Accountability Mechanism?

This section will assess the Equator Principles as a means of implementing the environmental rule of law. In doing so, it should be borne in mind that these Principles are a form of *private*, transnational agreement for ensuring compliance with international social and environmental norms. However, within the context of the ‘environmental rule of law’ project, it is the capacity of

⁴⁹ Michael Torrance, ‘Grievance Mechanisms and the Equator Principles’, 13 December, 2013, posted on Lex Sustineo website, accessible at:

<http://lexsustineo.blogspot.co.uk/2013/02/grievance-mechanisms-and-equator.html>

⁵⁰ *Ibid.*

the Equator Principles to both provide for, and establish, *public* accountability mechanisms for these social and environmental stakeholders in the resource development projects that the EPFIs are involved in that will be scrutinized here. The Equator Principles (EP) is an agreement amongst signatory Financial Institutions (known as EPFI) to assess and manage environmental and social risks associated with certain project and asset based financings in accordance with procedural requirements, internationally accepted standards and host country and international laws and regulations. EPFI will not provide project-related loans and project finance advisory services within the scope of the EP, to projects where the borrower cannot or will not comply with the EP. The EP was originally developed in 2003 and then reviewed and revised in 2006, giving rise to the second iteration, EP II framework. Another review took place during 2011-12, culminating in the release of a further revised version of the EP agreement known as EP III, adopted by EPFI in early 2013. The release of EP III follows a major revision of the World Bank's IFC Performance Standards on Environmental & Social Sustainability in 2012 (hereinafter, IFC Performance Standards), a set of guidelines that is incorporated by reference into the EP framework. Together, these changes mark an important evolution in best practice in sustainable finance of particular importance for both bankers and those seeking access to capital.

The IFC Performance Standards that the EP are based upon pertain to the management of certain types of environmental and social risks, including (1) Labour and Working Conditions (including Occupational Health and Safety); (2) Resource Efficiency and Pollution Prevention; (3) Community Health Safety and Security; (4) Land Acquisition and Involuntary Resettlement; (5)

Biodiversity Conservation and Sustainable Management of Living Natural Resources; (6) Indigenous Peoples; (7) Cultural Heritage. Human rights risks are also addressed through the foregoing aspects of the IFC Performance Standards and significant human rights risks may require human rights due diligence in accordance with IFC Performance Standard One – Assessment and Management of Environmental and Social Risks and Impacts. These IFC Performance Standards reflect and embody the ‘sustainable development’ mandate of numerous global organizations, including the World Bank and its financing arm the IFC, and is enshrined as the explicit object and purpose of over 50 treaties. The IFC Performance Standards and the EP were borne out of efforts by the World Bank to ensure its private sector partners also took the appropriate steps to meet best practice in sustainable development.⁵¹ The IFC Performance Standards and Equator Principles are also increasingly relevant within international trade and investment treaty disputes, in light of increasing recognition of concepts/themes such as ‘sustainable development’ and ‘corporate social responsibility’ in international investment agreements.⁵² Thus, Export Credit Agencies (ECA) may be legally obligated to apply environmental and social risk management standards in extending their export credit facilities in accordance with the OECD Common Approaches, which refers to the IFC Performance Standards. Moreover, the environmental and

⁵¹ *Equator Principles III: An Introduction and Guide*, Norton Rose Fulbright (January 2014) at 5.

⁵² Norton Rose Fulbright report (2014) *ibid.*, at 6, citing the Canada-Peru Free Trade Agreement and role of the Environmental and Social Impact Assessment (ESIA) of the IFC in the Case Concerning Pulp Mills on the River Uruguay (Argentina v. Uruguay), before the International Court of Justice [2010] I.C.J. Rep. 14.

social review process is an ideal time to consider other legal and sustainability risks affecting a project, such as corruption and bribery risks.⁵³

In terms of the effectiveness of the EP, the basic statistics are that to date, 80 EPFIs from 34 countries have committed to the EP. This number is set to grow with an emphasis on the inclusion of banks from newly industrializing economies, especially those that are lending to investors in emerging markets across the world. Weber has examined the compliance records of 79 Equator Principles Financial Institutions (EPFI), analysing how often members of the EP report and what content should be disclosed in relation to the seven mandatory requirements: annual reporting, disclosure of the number of transactions, assessment, risk categories, sector, region and implementation.⁵⁴ Using institutional theory as the theoretical framework for the analysis, he used seven criteria (annual reporting, disclosure of screened transactions, the categorization of projects with respect to their assessment status, risk category, sector, region and implementation experience) to test whether EPFIs report according to the EP's guidelines. The three main findings from this study are first, that all EPFIs that are required to disclose information are compliant, at least partially. Second, only about five percent disclose all the information required by the EP guidelines, although 85 percent meet at least four out of the seven reporting criteria. While the majority of EPFIs report about risk

⁵³ Norton Rose Fulbright report (2014) *op. cit.*, at 6.

⁵⁴ Olaf Weber, Equator Principles Reporting: Do Financial Institutions meet their Goals?, Centre for International Governance Innovation (CIGI), Canada, Paper No.38, 19 August, 2014. Accessible at: <https://www.cigionline.org/sites/default/files/no38.pdf>

categories, sectors and regions, only a minority of these EPFIs report them in a way that enables readers to combine the figures and to analyze how risk occurs in certain regions and sectors. Moreover, as projects are not usually listed in a way that they are identifiable, the reports are non-transparent, making it impossible to allocate social and environmental impacts to certain projects, sectors and regions. Third, the larger the EPFI, with respect to its total assets, and the longer the duration of its membership, the higher is the reporting quality. In conclusion, Weber recommends that further mechanisms are needed to guarantee transparent reporting of environmental and social project finance impacts. These recommendations should include additional mechanisms to guarantee that the EPFIs follow the EP's demands include enforcement, standardization reporting or third party validation could help to increase the credibility and the transparency of the EP reporting.⁵⁵

While the EP is an agreement amongst EPFI, many of the obligations of the EP must be carried out wholly or in part by borrowers with EPFI oversight. Borrower expectations may be set out in contractual agreements between the EPFI and borrower, conferring upon the EPFI certain rights and remedial avenues should the requirements of the EP not be met by the borrower. Where borrowers are unable or will not comply with the EP, no loans are to be extended by the EPFI. Where loans are extended, the role of the EPFI is analogous to that of a regulator, establishing rules and obligations for borrowers and monitoring their implementation, with the possibility of adverse consequences (in the form of contractual remedies) being imposed on the

⁵⁵ *Ibid.*

borrower for non-compliance with EP requirements.⁵⁶ The primary legal significance of the EP derives from the incorporation of EP obligations into contractual relations between the EPFIs and their borrowers through covenants. However, it remains an open legal question whether public commitments and contractual agreements to apply the EP give rise to third party beneficiary rights (such as in relation to Affected Communities) through tort or contract law.⁵⁷ This is due to the structural difficulty in that EPFIs face when seeking to ensure that their clients/borrowers implement the Equator Principles in the projects they (the EPFI) finance relates to the nature of the relationship between the EPFI concerned and the borrowing entity, which utilizes the loan to finance the actual project on the ground. While the EPFI itself may well be committed to, and in compliance with, the application of the Equator Principles, there is an understandable concern as to how far such a commitment can be translated into effective action on the environmental and social fronts by the borrowing (SPE) project company itself, given that it would usually be operating in a separate, foreign territorial jurisdiction from the EPFI concerned. Here, the EPFIs' main compliance mechanism is contractual, binding their borrowers to covenants in their funding documentation to comply with the relevant international and domestic laws on social and environmental issues.⁵⁸ Moreover, the EPFIs require borrowers to arrange third-party, independent monitoring and reporting of their project financed projects,⁵⁹ with

⁵⁶ *Ibid.*, at 5-6.

⁵⁷ Norton Rose Fulbright report (January, 2014) *ibid.*, at 6.

⁵⁸ Principle 8, of the Equator Principles *op. cit.*

⁵⁹ Principle 9, *ibid.*

the clear implication being that poor performance by the borrowing company on the social and environmental fronts can jeopardize future tranches of scheduled funding for the project. However, given the repayment structure for project finance loans described above, the EPFI concerned may thereby be placing its own source of revenues from the repayment of the Project Finance loan at risk of default if it impinges too heavily on the operations of the borrowing company on social and environmental compliance issues. A further source of control that can be exercised by the EPFIs in respect of errant borrowers is to blacklist these companies from future project finance-type lending. On the other hand, the competitive nature of the project finance market and the presence of new entrants (especially from non-Western countries) which have not yet been inducted into the 'Equator Principles' raises possible 'free rider' issues and thereby acts as a deterrent against the use of this form of sanction. As van Putten notes, '... the Equator Principles could still be undermined by the fast-increasing flows of foreign direct investment from new large investors such as Chinese banks'⁶⁰, especially within the African continent. It is therefore in the interests of the current EPFIs to induce as many of these new entrants into accepting the Principles as part of their lending policy in order to reduce the potential for 'free riders' within the project finance lending market.

The next question to be addressed is what, if any, are the compliance-inducing or enforcement methods to be employed against the EPFIs themselves for their non-compliance with the 'Equator Principles'? Initially, this question might be

⁶⁰ van Putten (2008) at 214.

considered superfluous given the self-regulatory, non-binding nature of these Principles. In this regard, the ‘Disclaimer’ attached to the end of the ‘Equator Principles’ list is apposite. It indicates, *inter alia*, that: ‘...these principles do not create any rights in, or liability to, any person, public or private. Institutions are adopting and implementing these Principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank.’⁶¹ Yet the depth of the commitment to the Principles by the EPFIs in their PF-type lending activities is indicated by the fact that they are willing to lose potential profits by withdrawing from PF projects that fail to meet the requirements established by these Principles. Moreover, the EPFIs concerned are acutely aware of their exposure to NGO, media and general public scrutiny over their lending activities. Thus, despite their consensual, rather than compulsory, character, most if not all these EPFIs are now able to show a significant level of internalization of these Principles within their lending criteria and practice. As Meyerstein argues, while measuring how individual EPFIs have changed their organizational structures, policies and procedures following adoption of the EPs is not a perfect proxy for measuring ground-level impacts, it is a useful gauge for the study of how transnational private regulation engages with corporate human rights accountability issues.⁶² Principle 10 also requires these EPFIs to commit to publicly available reports, on at least an annual basis, about

⁶¹ See ‘The Equator Principles’, *op. cit.*, at p.5.

⁶² Ariel Meyerstein, ‘Transnational Private Financial Regulation and Sustainable Development: An Empirical Assessment of the Implementation of the Equator Principles’, *New York University Journal of International Law & Politics*, Vol.45 (Winter, 2013) 487-594 (including Tables) at 499.

its Equator Principles implementation processes and experience. While this information requirement will assist others (especially NGOs) to monitor the EPFIs' implementation records in this regard, the voluntary nature of this requirement will not prevent 'shirking' of responsibilities from occurring.

A further, institutional requirement that emulates, but does not fully replicate, the grievance mechanisms epitomized by the World Bank's Inspection Panel and IFC's CAO, is provided through the Equator Principles in the form of *Principle 6: Grievance Mechanism*. Principle 6 provides *inter alia* as follows: For all Category A projects and Category B projects 'as appropriate' that are located in non-OECD or non-High Income countries, the borrower is enjoined to establish a grievance mechanism; the existence of which the borrower has to inform the affected communities. The borrower must create a 'grievance mechanism' as part of the Environmental and Social Management System (ESMS) for the project and it must be designed to receive and facilitate resolution of concerns about the project's environmental and social performance. According to (Equator) Principle 6, 'the grievance mechanism is required to be scaled to the risks and impacts of the Project and have Affected Communities as its primary user. It will seek to resolve concerns promptly, using an understandable and transparent consultative process that is culturally appropriate, readily accessible, at no cost, and without retribution to the party that originated the issue or concern. The mechanism should not impede access to judicial or administrative remedies. The client will inform the Affected Communities about the mechanism in the course of the Stakeholder Engagement.'

The grievance mechanism to be established is thus subject to the following qualifiers: 1) this mechanism is scaled to the level of risk and adverse impacts of the project; and 2) it is part of the management system. The former qualifier is understandable, albeit affording the borrower much discretion to decide on the scope and method of the grievance mechanism employed. This is especially pertinent when it is considered that Category B projects will be subject to a grievance mechanism only ‘as appropriate’, presumably from the borrower’s perspective? The second qualifier is subject to more serious concerns, as follows: First, it is clear that this mechanism does not have to amount to an independent and objective dispute settlement mechanism for addressing community grievances. Its explicit attachment to the project management system undermines any notion of such objectivity or independence in its procedures. Second, there is nothing in this requirement under Principle 6, or indeed in the consultation and disclosure requirements under Principle 5, that deal with the issue of standing for Non-Governmental Organizations (NGOs) concerned with nature conservation and wildlife protection issues to participate in such grievance mechanisms, where these issues are not raised by the ‘affected communities’ concerned. Such NGOs will not necessarily be encompassed within the definition of ‘affected communities’, except perhaps if they have among their membership, individuals from these ‘affected communities’.

Nevertheless, according to the EP Association of EPFIs, the provision of grievance mechanisms is a very important component of the EP framework and the requirements enable Project Sponsors to proactively address grievances and concerns at project level. Here, the EP III aim to reflect the IFC’s current thinking on the subject (as detailed in the updated IFC Performance Standards

and Guidance Notes). However, questions persist about the adequacy of these local grievance mechanisms at both the *institutional* and *implementation* levels in terms of their relationship (or lack of it) with the EPFIs. First, unlike the Inspection Panel and CAO, the grievance mechanisms established under EP 6 do not provide for accountability against the lending institutions (*i.e.*, the EPFIs) themselves. As Richardson observes, the EPFIs do not see the Principle 6 ‘Grievance Mechanism’ as a formal dispute resolution system that can confer obligations or liabilities against them.’⁶³ Second, while the IFC Performance Standards and Equator Principles require the ‘project sponsors’ (in other words, borrowers from these lending public/private international finance institutions) to implement project-level grievance mechanisms, these mechanisms are not required to meet any minimum due process standards.⁶⁴

This third iteration of the EP (EP III) also introduces ‘human rights’ into the EP framework for the first time, to bring them in line with UN and World Bank initiatives. As part of the EP updating process for the third iteration of these

⁶³ B. J. Richardson, ‘Financing Sustainability: The New Transnational Governance of Socially Responsible Investment’, 17 *Yearbook of International Environmental Law* (2008) 73–110, at 92.

⁶⁴ Steven Herz, Kristen Genovese, Kirk Herbertson, and Anne Perrault, THE INTERNATIONAL FINANCE CORPORATION’S PERFORMANCE STANDARDS AND THE EQUATOR PRINCIPLES: RESPECTING HUMAN RIGHTS AND REMEDYING VIOLATIONS? A Submission to the U.N. Special Representative to the Secretary General on Human Rights and Transnational Corporations and other Business Enterprises from Bank Information Center, BankTrack, Center for International Environmental Law, Oxfam Australia, World Resources Institute (August 2008) Accessible at: http://www.ciel.org/Publications/IFC_Aug08/Ruggie_Submission.pdf

Principles (EP III) it was agreed that the updated EP (III) would acknowledge the ‘Guiding Principles on Business and Human Rights: Implementing the United Nations ‘Protect, Respect and Remedy’ Framework’, which were developed by John Ruggie, the Special Representative of the UN Secretary-General on the issue of human rights and transnational corporations and other business enterprises. The Special Representative annexed these Guiding Principles to his final report to the UN Human Rights Council,⁶⁵ and the Human Rights Council endorsed the Guiding Principles in its resolution 17/4 of 16 June 2011.⁶⁶ The second pillar of the UN’s ‘Protect, Respect and Remedy’ framework sets out the corporate responsibility to respect human rights as follows: ‘business enterprises should act with due diligence to avoid infringing on the rights of others and to address adverse impacts with which they are involved.’⁶⁷ In this regard, the EP provides relevant private international financial institutions with the required ‘due diligence’ framework to identify, assess and manage project impacts by defining the processes and standards for stakeholder engagement with affected communities (including for indigenous peoples), labour rights, and occupational and community health and safety. The further requirement for project-level grievance mechanisms also allows affected communities to address grievances proactively with Project Sponsors, *i.e.*, the borrowers of EPFI loans, which is an important component in driving greater accountability at project level.

⁶⁵ A/HRC/17/31

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⁶⁷ Para.11

Within this context, it is important to note that the UN Business and Human Rights Framework has itself not been immune to criticism, especially as to the extent of its provision for grievance mechanisms to respond to alleged human rights abuses perpetrated by businesses. As Herz *et al* note, in his 2008 report to the UN Human Rights Council,⁶⁸ the Special Representative provided insights into how initiatives like the IFC Performance Standards (PS) and Equator Principles (EPs) can improve the human rights performance of project sponsors. The Special Representative affirmed that companies have a 'baseline responsibility' to respect all internationally recognized human rights.⁶⁹ He then explained that corporations must do two things to ensure that they meet this baseline responsibility. First, they must implement a robust due diligence framework that will enable them to identify, prevent, and address adverse human rights impacts.⁷⁰ This includes both substantive benchmarks to provide detailed guidance on acceptable outcomes and clear procedures to assess potential impacts, devise avoidance and mitigation strategies, and ensure that substantive standards are achieved.⁷¹ Second, companies must ensure that stakeholders have access to effective grievance mechanisms to redress adverse human rights impacts.⁷² The Special Representative has also noted that in order to fully discharge their responsibility to respect human rights, companies must provide a means for people who have had their rights adversely affected

⁶⁸ *Protect, Respect and Remedy: A Framework for Business and Human Rights*, A/HRC/8/5
7 April 2008.

⁶⁹ *Protect, Respect and Remedy*, paras. 24, 54.

⁷⁰ *Ibid.* at paras. 25, 56.

⁷¹ *Ibid.*, at paras. 61-63.

⁷² *Ibid.*, at paras. 93, 94.

by the company to seek redress.⁷³ Such grievance mechanisms may take a variety of forms: they may be specific to a given project or company, or they may be linked to multi-stakeholder or industry initiatives.⁷⁴ Whatever form grievance mechanisms take, however, they must meet baseline due process standards to be credible and effective. At a minimum, a grievance mechanism must be legitimate, accessible, predictable, equitable, rights-compatible, and transparent.⁷⁵

Of all the institutions that adhere to the PS/EPs, only the IFC has an institution-wide grievance mechanism that comes close to meeting the minimum due process standards articulated by the Special Representative, in the form of the IFC's Compliance Advisor/Ombudsman (IFC/CAO). The IFC/CAO operates under a set of fair, transparent and predictable grievance and dispute resolution procedures that explicitly empower it to consider claims based upon violations of international law.⁷⁶ Despite considerable public pressure, the EPFIs have not adopted an analogous institution-wide grievance process.⁷⁷ The EPs only require project sponsors to establish a project-level grievance mechanism 'to receive and facilitate resolution of the affected communities' concerns and grievances about the client's environmental and social performance',⁷⁸ whereas as noted above, the IFC operates both institution-wide as well project-

⁷³ *Ibid.*, at paras. 82, 93.

⁷⁴ *Ibid.*, at paras. 93, 100.

⁷⁵ *Ibid.*, at para. 92.

⁷⁶ IFC Compliance Advisor/Ombudsman, *Operational Guidelines*, (2007) at 21.

⁷⁷ *Protect, Respect and Remedy*, *op. cit.*, at para. 100.

⁷⁸ Equator Principle #6.

level grievance mechanisms.⁷⁹ The grievance mechanisms contemplated by IFC's Performance Standards meet the Special Representative's minimum due process criteria insofar as they must be accessible, transparent and not impede access to judicial or administrative remedies. Also, in other respects, these grievance mechanisms lack minimum substantive or procedural standards. For example, the PS/EPs do not require that the grievance mechanism be independent of the project sponsor to ensure legitimacy. To the contrary, the Guidance Notes anticipate that the mechanism will be staffed by the project sponsor and housed within its organizational structure.⁸⁰ Moreover, the PS/EPs do not specify acceptable procedures, time frames for hearing and resolving disputes, or appropriate remedies. And they do not require that the mechanism's outcomes and remedies accord with internationally recognized human rights norms. Rather, all of these fundamental issues appear to be left to the unguided discretion of the sponsor. And in practice, many projects have received financing without a functioning grievance mechanism in place, let alone a rights-compliant one.

The voluntary nature of the Principles itself effectively means that the reach of the Principles depends on a given EPFI's conscience, unless those trying to force compliance are able to mount a public shaming campaign of such magnitude as to force the EPFI to comply. Moreover, if the EPFI claims and the IFC finds that the project does comply with IFC Safeguards, procedural compliance alone may still be insufficient to ensure that private financial

⁷⁹ IFC Performance Standard 1, para. 23.

⁸⁰ IFC *Guidance Notes* at 20.

institutions are financing projects less likely to cause social and environmental harm. On the other hand, the EPs nevertheless remain a stepping-stone to a future mechanism of more substantial, if not binding, commitments by financial non-state actors to responsible investing. Despite their shortcomings, such voluntary commitments create a forum in which interested non-state actors - individuals, NGOs and corporations - may participate actively in the development of corporate human rights responsibilities.

Created as a result of voluntary commitments, the Equator Principles also invite corporations to develop and improve their own position on sustainable development. It is in this sense that the development and continued existence of voluntary commitments are not only crucial for the potential of NGO public shaming campaigns and access to formal adjudicatory venues, but are also an invaluable contribution to the corporate responsibility movement.⁸¹

In recognition of a decade-long experience, application outcomes and stakeholder input, the EPs have undergone changes meant to share lessons learned, but also to proactively engage with evolving contemporary issues, concerns and stakeholders. Olaf and Acheta observe that at least three changes have occurred in the EP's evolution: first, strategic changes, such as integrating evidence of climate change and greenhouse gas emissions into the EP scope and reporting; second, changes that followed modifications of the International Finance Corporation's policies and guidelines as the basis for the EPs; and the third change addressed the consistency of the principles and support with the

⁸¹ Vivian Lee, *Enforcing the Equator Principles: An NGO's Principled Effort to Stop the Financing of a Paper Pulp Mill in Uruguay*, 6 *Nw. J. Int'l Hum. Rts.* 354 (2008) at 358.

implementation of the EPs, specifically, information sharing, country designation and language clarification.⁸²

Conclusions

The initial results of a recent major research project entitled ‘rule of law dynamics’ *inter alia* maps the interaction between rule of law *promotion* (donor strategies) and rule of law *conversion* (the ways it is promoted and the ways it is received), and the relevance of rule of law *diffusion* (the modalities that cause the spread of expectation that one complies with the rule of law).⁸³ This research project found that both literature and practice pay too little attention to the recipient’s perspective and needs, resulting in failures in the rule of law conversion stage and its negative effect on the success of rule of law promotion programmes. One-size-fits-all programmes, top-down strategies, transplants by developed states of their own rule of law standards without the capacity of the recipient to cope with them, are still principal features of today’s rule of law promotion efforts. Almost no attention is paid in literature and practice to rule of law diffusion, *i.e.* the acceptance of the applicability of the rule of law, for example, to inter-governmental organizations (IGOs) and other international/transnational actors, with the resulting lack of legitimacy of rule of law promotion. Contemporary rule of law promotion strategies should

⁸² Weber, Olaf and Emmanuel Acheta, ‘The Equator Principles: Ten Teenage Years of Implementation and a Search for Outcome’, CIGI Papers No. 24. Waterloo, Ontario, Canada: CIGI (2014B), as cited in Weber (2014A), at 5.

⁸³ Michael Zürn, *et al*, CUP (2012) *op. cit.*

therefore be based on an understanding that rule of law promotion, conversion and diffusion are inextricably linked.

In this paper a different type of rule of law dynamic is explored, namely, the dialectical relationship between public and private accountability mechanisms for ensuring that social and environmental risks of large natural resources development projects are successfully addressed, focusing on the grievance mechanisms required under EP Principle 6. The need for such mechanisms to be established arguably represents further evidence of the importance of the *conversion* and *diffusion* elements identified within the ‘rule of law dynamics’ paradigm described in the above research project. The findings of this paper also echo other, multi-disciplinary studies on the ten-year life span of the Equator Principles in concluding that there is a further need for a complaints mechanism against the private international finance institutions (EPFIs) that adopted these Principles.⁸⁴

⁸⁴ Isabel Feichtner and Manuel Worsdorfer, Symposium: 10 Years Equator principles: A Transdisciplinary Inquiry, *Transnational Legal Theory*, Vol.5, No.3 (2014) 409-416, at 411.