Reconciling Enforcement Weaknesses and Lender Liabilities in the Equator Principles: How Further Revisions Can Help Ensure Adherence to the Private Sector's Claims of Environmental Stewardship

by Lindsay Hall*

Total global energy demand is expected to expand by over 33% between 2012 and 2035.[1] As developing countries increase in wealth and population, so do their respective appetites for energy.[2] Although energy generation from renewable sources is rising, fossil fuels remain the world's premier energy source,[3] predicted to supply over 80% of projected global energy demand increase between 2005 and 2030.[4] Electricity demand grows at nearly twice the rate of total energy consumption, and meeting this demand is made harder by a shortfall of modern energy infrastructure.[5] An average investment of $49 billion per year from 2011 until 2030, including the cost of infrastructure, would be needed to achieve universal electricity access by 2030.[6] The private sector is expected to provide $15 billion of this investment.[7]

An example of the pressing disparity between available energy resources and available energy infrastructure can be seen in Latin America. Latin America possesses nearly 10% of the world's proven oil reserves,[8] yet over fifty million people in the region are without reliable or affordable access to electricity.[9] The International Energy Agency estimates that Central and South America alone will need nearly $1.3 billion in new energy infrastructure investments before 2030 to meet new power demands.[10] A significant portion of this funding could come from the private sector.[11] However, the private sector has been criticized by public interest groups for its support of numerous damaging energy infrastructure projects in other developing regions around the world.[12] The Three Gorges Dam project in China,[13] the Narmada Val-

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1. Int'l Energy Agency, World Energy Outlook, Executive Summary 1 (2012).
2. Robert Jackman, Stanford University's Rural West Initiative: Fossil Fuels, Foreign Trade, and Foreign Investment in the American West 5 (2001) (China's economy has grown annually by more than 7.5% since the early 1990s. In 1990, China consumed 2.3 million barrels of oil per day, and, by 2008, its consumption had grown to 7.83 million barrels per day, behind only the United States in worldwide consumption.).
3. Int'l Energy Agency, *supra* note 1, at 1. (Fossil fuels were funded by $523 billion in subsidies in 2011, which was six times more than renewable subsidies during the same time frame.).
4. J. Wagner & K. Armstrong, *Managing Environmental and Social Risks,* 3 J. World Energy L. & Bus. 140, 142 (2010); The World Bank, Environmental Governance in Petroleum Exporting Countries: Findings From a Comprehensive Survey 12 (2009) (finding that by 2030, fossil fuels are still predicted to account for 80% of the world's primary energy mix, with oil remaining the dominant fuel).
5. Int'l Energy Agency, *supra* note 1, at 6.
6. Int'l Energy Agency, *supra* note 1, at 538.
7. Int'l Energy Agency, World Energy Outlook, Energy for All: Financing Access for the Poor: World Energy Outlook 7 (2011).
8. C. Arnson et al., Woodrow Wilson Int'l Ctr. for Scholars, Energy and Development in South America: Conflict and Cooperation 9 (2008).
9. *Id.* at 10.
10. *Id.* at 15.
11. In recent years, Brazil has increasingly relied on private enterprise energy development. *Id.* at 5; Int'l Energy *supra* note 7, at 3.
12. "Developing" is intended to mean non-OECD member countries. *See List of Member Countries–Ratification of the Convention of the OECD,* OECD, http://www.oecd.org/general/listofoecdmembercountries-ratificationoftheconventionontheoecd.htm (last visited Oct. 9, 2013).
13. Peter H. Gleick, Three Gorges Dam Project, The Pac. Instit., Water Brief 3, 1 (2008–2009) (noting "growing threats from landslides, pollution,

ley dams in India,[14] the Sakhalin II Oil and Gas Project in Russia,[15] and the Madeira River Hydroelectric Dam in Brazil[16] have all been criticized for their significant negative environmental impacts, including widespread deforestation, river pollution, and pervasive, negative impacts on local ecology. Because many governments of these and other fossil fuel-rich countries fail to properly protect the environment, a private sector regulatory framework is needed that would fill the gap in environmental protection that exists for large energy infrastructure projects.

Energy infrastructure projects present unique opportunities for identifying creative methods of providing such environmental protection and promoting sustainable development. Large-scale energy projects in developing countries face environmental, financial, and regulatory challenges. Done correctly, energy infrastructure projects can facilitate the efficient and equitable use of a nation's resources to further that country's development. Done incorrectly, energy infrastructure projects can create a destructive precedent for developing countries and can saddle a country or a region with long-term financial burdens and environmentally degrading resource consumption practices. Because of the environmental impacts expected from growing global energy infrastructure development, private sector and governmental decisionmakers should give significant weight to expected environmental considerations in determining how an infrastructure project will go forward, and who will participate.[17] Allowing greater stakeholder and investor participation in planning and implementing these large-scale infrastructure projects will empower more responsible environmental stewardship from all project participants and affected communities.

The Equator Principles ("Principles") require participating large lending institutions to identify and minimize the negative environmental impacts of their borrowers' projects.[18] The Principles serve as a voluntary industry guide for assessing and managing environmental risks.[19] This private regulatory system helps ensure both the use of long-term regional environmental stewardship practices, and the long-term viability of the project.[20] Unfortunately, the Principles have not fully fulfilled their goal, in part because of their lack of effective grievance, monitoring and disclosure, and enforceability mechanisms.[21] This Note discusses project finance's potential to address environmental issues stemming from large energy infrastructure projects and how further revisions of the Principles by its member institutions can remedy the industry's current environmental protection shortcomings.

This Note proposes that the Principles be revised to improve their current grievance, monitoring, and disclosure mechanisms in order to enhance compliance by its member institutions. Improved transparency and disclosure mechanisms would hold non-compliant member banks accountable to a proposed Board, which would be authorized to publicize non-compliance and demand adherence to the Principles.[22] This more transparent regulatory system would enhance both community members' and shareholders' access to information, thereby allowing market forces to guide the behavior of firms involved in these projects in a socially beneficial direction and creating greater incentives for lenders to abide by the Principles' regulations.[23] These incentives would come directly from Board sanctions or shareholder disapproval manifested in a declining stock price, or indirectly from domestic enforcement mechanisms like shareholder derivative suits.

Part I of this Note will provide an overview of project finance and the history and modern form of the Principles. Part II will survey current environmental and lender liability issues in the project finance arena. Part III will present accountability issues with the Principles and the loopholes that negate compliance. Finally, Part IV will articulate the proposed solution to improve grievance collection, monitoring, and reporting and describe the scope and authority of the proposed Board.[24]

I. Factual Background: Project Finance and the Principles

A. *Introduction to Project Finance*

Project finance is a funding method in which revenues generated by the project act as the source of the loan repayment and collateral for the loan itself.[25] Unlike direct finance, in which the assets of the borrowing entity secure repayment of borrowed money, project finance transactions are largely secured by the viability of the project.[26] For example, under a project finance arrangement, revenues generated from the sale of electricity generated by a hydroelectric dam would be used to repay the loan that financed the construction of the dam.[27] Because of the risks involved in these infrastructure projects, project financing is commonly used in large, com-

and flooding, as well as growing social and political unrest and dissatisfaction associated with relocating millions of people").

14. J. Conley & C. Williams, *Global Banks as Global Sustainability Regulators?: The Equator Principles,* 33 L. & Pol'y 542, 543 (2011).
15. Marissa Marco, *Accountability in International Project Finance: The Equator Principles and the Creation of Third-Party-Beneficiary Status for Project-Affected Communities,* 34 Fordham Int'l L.J. 452, 474–76 (2011); Erin Marie Daly, *Russia's Sakhalin Oil Project Under New Legal Fire,* Law 360 (Oct. 3, 2008).
16. Marco, *supra* note 15, at 480.
17. *See* United Nations, Achieving Sustainable Development and Promoting Development Cooperation 180–81 (2008).
18. Equator Principles Ass'n, Equator Principles III 2 (June 2013) [hereinafter EP III], *available at* http://www.equator-principles.com/resources/equator_principles_III.pdf.
19. *Id.*
20. *Id.*
21. *Id.; see infra* Part I.C.
22. *See infra* Part IV.
23. *See infra* Part IV.A.1.
24. Social issues, although considered by the Principles, fall outside of this Note's scope, as do the Principle's elements related to corporate loans, bridge loans, and advisory services.
25. Int'l Fin. Corp., Project Finance in Developing Countries 8 (1999) [hereinafter IFC Project Finance]; Basel Comm. on Banking Supervision, International Convergence of Capital Measurement and Capital Standards 53 (2006).
26. ICF Project Finance, *supra* note 25, at 8.
27. *See* Chris Head, World Bank Discussion Paper No. 420, Financing of Private Hydropower Projects 109-10 (2000). The Upper Bhote Koshi hydroelectric dam in Nepal is capable of producing 41 MW of power. Financing for the $98 million project is based on a 70:30 percent debt to equity ratio, with all the debt being provided by IFC in two separate loans ("A" Loan of $21 million and a syndicated "'B" Loan of $47 million). The loans are repaid based on the funding from a power purchase agreement with a local utility company,

plex, and expensive projects such as dams, pipelines, mines, and power plants.[28]

Project financing relies on elaborate contracts to limit a borrower's discretion to act, to mitigate risks potentially impacting the project's expected income stream, and to ensure loan repayment.[29] Project finance is a particularly attractive financing option for banks interested in investing in countries where domestic corporate laws provide weak investor protection.[30] Through using unique loan covenants, or promises made by the borrower to do or not do certain actions, project financing agreements can act as a substitute for domestic corporate laws.[31] Weak governments, armed conflicts, and political instability frequently plague fossil fuel-rich countries where these energy infrastructure projects are located, amplifying the inherent risks of projects where energy infrastructure is needed.[32] In these regions, environmental and corporate finance considerations are rarely a priority for the host government.[33] As a result, private companies have historically been reluctant to invest in countries where national regulatory deficiencies prevent the government from playing its traditional oversight role.[34] In these situations, private sector actors must assume the responsibility to protect themselves against non-repayment when the state cannot.[35]

For large energy infrastructure projects, financing deals frequently involve numerous lending institutions with risks allocated among multiple investors.[36] The loan covenants used by private lending institutions become a substitute for a functioning public administration, which is necessary to ensure environmental protections by contractually distributing risks.[37] Lenders operating under a project finance agreement can use financial leverage to influence their borrowers to adhere to certain environmental standards.[38] However, the timing of a lending institution's exploitation of its leverage is critical, as once the loan agreements are finalized, lenders have limited abilities to introduce new environmental protections into the agreements as covenants.[39] The Principles provide guidelines to use this financial leverage and include covenants in the final loan documents requiring compliance with environmental protection plans as a condition on which lenders will provide financing for a project.[40] Should a borrower breach the environmental protection demands in the finalized loan agreement, the lending institution may exercise certain remedies under the contract, including stopping the loan's disbursement or accelerating loan repayment, in order to bring borrowers into compliance with their covenants.[41]

B. *The Structure of the Principles*

1. History of the Principles

The Principles are based on the World Bank's environmental, health, and safety guidelines[42] and the International Finance Corporation's ("IFC") performance standards, focused on private sector lending.[43] The Principles are adopted to fit projects funded by the private sector, but mirror the World Bank and IFC's reference documents for performance levels and measures that are considered acceptable for infrastructure projects in emerging markets.[44]

The Principles are a relatively recent addition to the project finance market.[45] When lending institutions such as the World Bank and the International Monetary Fund ("IMF") began to withdraw their support from environmentally destructive infrastructure projects in the 1980s and 1990s due to pressure from non-governmental organizations ("NGOs"), large private lending institutions came to hold a greater share of the project finance market.[46] Subsequently, these same NGOs began pressuring the private lending groups to avoid supporting projects with environmentally destructive characteristics.[47] This increased NGO attention created widespread public opposition to environmentally damaging projects, which in turn motivated a group of prominent international lending institutions to attempt to avoid public criticism of their support of controversial projects and the loss of business to less scrupulous lenders.[48] Ten banks decided to develop a series of industry guidelines for how to implement infrastructure projects without environmentally disastrous

and over the period of 11 years, the profits from the sale of electricity will repay the banks for the total project cost.

28. Conley & Williams, *supra* note 14, at 544.
29. Christopher Sozzi, *Project Finance and Facilitating Telecommunication Infrastructure Development in Newly-Industrializing Countries,* 12 Santa Clara Computer & High Tech. L.J. 435, 446 (1996); 26 U. Pa. J. Int'l Econ. L. 69, 75 (2005).
30. Sozzi, *supra* note 29, at 446.
31. *Id.*
32. Wagner & Armstrong, *supra* note 4, at 143.
33. Org. for Econ. Co-Operation & Dev., Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones 42 (2006) (defining a "weak governance zone" as "investment environments in which governments cannot or will not assume their roles in protecting rights . . . providing basic public services [*i.e.,* social programs, *infra*structure development, law enforcement] and ensuring that public sector management is efficient and effective").
34. Jacques Cook, *Infrastructure Project Finance in Latin America,* 24 Int'l Bus. L. 260, 261 (1996). Risk allocation in project finance is achieved and codified in the contractual arrangements between the project company and other participants. The loan documents match perceived transactional risks and corresponding returns to the lending banks most capable of successfully managing them. Bruce Comer, The Wharton School, Project Finance Teaching Note 4 (1996).
35. *Id.* (noting that current South American capital markets are not able to shoulder the financial requirements of these energy sectors).
36. IFC Project Finance, *supra* note 25, at 3.
37. Wagner & Armstrong, *supra* note 4, at 144.
38. Bianca Zambdo, *Brazil's Launch of Lender Environmental Liability,* 18 U. Miami Int'l & Comp. L. Rev. 47, 87 (2011).
39. Natalie Bridgeman & David Hunter, *Narrowing the Accountability Gap: Toward a New Foreign Investor Accountability Mechanism,* 20 Geo. Int'l Envtl. L. Rev. 187, 192 (2008).
40. David Hunter, *Civil Society Networks and the Development of Environmental Standards at International Financial Institutions,* 8 Chi. J. Int'l L. 437, 470 (2008).
41. Bede Nwete, *The Equator Principles: How Far Will It Affect Project Financing?,* 2005 Int'l Bus. L.J. 173, 184 (2005).
42. Keith Larson, *Putting Carbon and Equator Together,* 27 Int'l Fin. L. Rev. 62, 63 (2008).
43. William Thomas, *The Need to be Sustainable,* 25 Int'l Fin. L. Rev. 62, 65 (2006) ("The IFC's policy and performance standards have two components: the policy on social and environmental sustainability and the performance standards on social and environmental sustainability.").
44. Larson, *supra* note 42.
45. Conley & Williams, *supra* note 14, at 543.
46. *Id.*
47. Nigel Clayton, *The Equator Principles and Social Rights,* 11 Envtl. L. Rev. 173 (2009).
48. Benjamin Richardson, *Can Socially Responsible Investment Provide a Means of Environmental Regulation?,* 35 Monash U. L. Rev. 262, 279 (2009).

side effects.[49] The initial banks to sign onto the first draft of the Principles, referred to as the Equator Principle Financial Institutions ("EPFIs"), accounted for nearly 30% of the global project finance capacity at that time.[50]

The resulting Principles, signed on June 4, 2003, became the financial industry's benchmark for identifying, mitigating, and managing risks stemming from the environmental impacts caused by their projects.[51] As projects are frequently financed by more than one bank, the Principles provided a standard guideline for the borrower to adhere to, reducing inconsistent requirements among lenders for each project.[52] Under the Principles, the EPFIs must make borrowers aware of the Principles' content and goals and agree to not provide loans to projects where the borrower will not or cannot comply with the Principles.[53]

On the tenth anniversary of the Principles' ratification, June 4, 2013,[54] the EPFIs passed their third iteration of the Principles.[55] These revisions were intended to address the changing global financial landscape as well as financial institutions' emerging environmental challenges.[56] While the original Principles applied only to project finance transactions with project capital costs over $50 million, the Principles were revised to increase the number of projects within its scope.[57] The Principles now encompass all project finance transactions over $10 million and also provide guidelines for certain advisory services, corporate loans, and bridge loans.[58]

As of 2013, seventy-eight financial institutions follow the Principles, including banks such as JPMorgan Chase, Citigroup, and Wells Fargo Bank.[59] These EPFIs provide funding to over 80% of global project finance agreements.[60] As such a large percentage of the project financing transactions now adhere to this voluntary agreement, the Principles have reduced the likelihood that developing countries will engage in an environmental regulatory race-to-the-bottom to attract private investment.[61] Thus, the Principles serve as a screening tool for lenders to identify those projects that meet a certain level of environmental quality.

2. Categorization of Projects

Projects subject to the Principles are categorized according to their location, nature, sensitivity, and size.[62] This initial assessment breaks projects into three categories. Category A projects have "potential significant adverse environmental and social risks and/or impacts that are diverse, irreversible or unprecedented."[63] Category B projects include those with "potential limited adverse environmental and social risks and/or impacts that are few in number, generally site-specific, largely reversible and readily addressed through mitigation measures."[64] Finally, Category C projects are those "with minimal or no adverse environmental and social risks and/or impacts."[65] The Principles require lenders to undertake a correspondingly greater level of due diligence or investigation into the project's viability and likelihood to create negative impacts based on the project's categorization.[66] Both Category A and Category B projects require that EPFIs conduct an Environmental and Social Assessment ("ESA"),[67] in which risks involving current environmental conditions, the legal and regulatory requirements of the project's host country, and potential mitigation matters are considered.[68] Category C projects do not require an ESA, are not subjected to further assessment, and are not reassessed during the project's life.[69]

3. Application of the Principles

After project categorization, the Principles require that lending institutions incorporate ten elements of the Principles into their loan covenants for Category A and Category B projects to ensure that negative environmental impacts are identified and minimized.[70] This Note will discuss Principles 6, 8, and 10 in detail, as they encompass the Grievance, Cov-

49. The first signatories to the Principles were Barclays, Citigroup, Credit Suisse Group, Credit Agricole Corporate and Investment Bank, Rabobank Group, Royal Bank of Scotland, UniCredit Bank AG, and Westpac Banking Corporations. *Members and Reporting,* Equator Principles Ass'n, http://www.equator-principles.com/index.php/members-reporting (last visited Jan. 3, 2014).
50. Conley & Williams, *supra* note 14, at 551.
51. Clayton, *supra* note 47, at 176.
52. Nwete, *supra* note 41, at 180.
53. EP III, *supra* note 18, at 2. The Principles also require the client to covenant in the financing documentation to comply with all relevant host country environmental laws, regulations and permits in all material respects.
54. Although the second revision of the Principles produced much needed changes, this Note will focus specifically on the third revision, and on the changes necessary in future iterations to ensure that the Principles remain relevant and responsive to newly emerging issues.
55. *See* Andrew Hardenbrook, *The Equator Principles*, 40 Vand. J. Transnat'l L. 197, 199 (2007); EP III, *supra* note 18, at 1.
56. Equator Principles Ass'n, Equator Principles III—Frequently Asked Questions on the EP III Update 4, *available at* http://www.equator-principles.com/resources/EPIII_FAQs.pdf (last visited Mar. 15, 2013).
57. Hardenbrook, *supra* note 55, at 200–01 (2007); EP III, *supra* note 18, at 3.
58. EP III, *supra* note 18, at 3. "The EP III applies to (1) All project finance transactions with project capital costs that exceed US $10M, (2) All project finance advisory services with project capital costs that exceed US $10M, (3) All corporate loans if: (i) related to a single project over which the client has effective operational control, (ii) the total aggregate loan amount is at least $100M, (iii) the EPFIs' individual commitment is at least $50M and (iv) the loan tenor is at least 2 years, and (4) Bridge Loans with a tenor of less than 2 years that are intended to be refinanced by the above project financing or project-related corporate loans."
59. *Members & Reporting,* Equator Principles Ass'n, http://www.equator-principles.com/index.php/members-reporting/members-and-reporting (last visited July 4, 2013).
60. Hardenbrook, *supra* note 55, at 199; Franck Amalric et al., *The Equator Principles: A Step Towards Sustainability* 1 (Ctr. for Corp. Responsibility & Sustainability, Working Paper No. 01/05, 2005).
61. Bridgeman & Hunter, *supra* note 39, 197 (2008).
62. Hardenbrook, *supra* note 55, at 201.
63. EP III, *supra* note 18, at 5 (2013).
64. *Id.*
65. *Id.*
66. Hardenbrook, *supra* note 55, at 201.
67. *Id.* These ESA's are analogous to the National Environmental Policy Act's Environmental Impact Statement requirements. *See Environmental Assessments & Environmental Impact Statements,* U.S. Envtl. Prot. Agency, http://www.epa.gov/reg3esd1/nepa/eis.htm (last visited Apr. 5, 2013).
68. Thomas, *supra* note 43, at 64.
69. Paul Watchman et al., *The Equator Principles: Why Hard-Nosed Bankers Are Embracing Soft-Law,* 1 L. & Fin. Mkt. Rev. 85, 89 (2007).
70. The 10 Principles are: (1) Review and Categorization; (2) Environmental and Social Assessment; (3) Applicable Environmental and Social Standards; (4) Environmental and Social Management System and Equator Principles Action Plan; (5) Stakeholder Engagement; (6) Grievance Mechanism; (7) Independent Review; (8) Covenants; (9) Independent Monitoring and Reporting; (10) Reporting and Transparency. EP III, *supra* note 18, at 1.

enant, and Reporting and Transparency mechanisms and are in need of further revision.

Principle 6, "Grievance Mechanism," requires that all Category A and some Category B projects establish a grievance mechanism "designed to receive and facilitate resolution of concerns and grievances about the [p]roject's environmental and social performance."[71] Principle 6 requires that the grievance mechanism has the "Affected Communities as its primary user," and emphasizes that there be 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."[72]

Principle 8, "Covenants," demands that in all projects, the borrower covenants to (1) comply in all material respects with all relevant host country environmental laws, (2) comply with the Environmental and Social Management Plan and Action Plans during the construction and operation of the project, (3) provide periodic reports (not less than annually) that document compliance therewith, and (4) decommission the facilities, where applicable and appropriate in accordance with a decommissioning plan.[73]

Principle 10, "Reporting and Transparency," requires that the borrowing entity disclose a summary of the assessment of the project's environmental and social risks and impacts online.[74] In addition, the borrower must "take account of, and document, the results of the Stakeholder Engagement process."[75] For projects with adverse environmental impacts, disclosure should occur early in the assessment process, before the construction begins, and should be conducted on an ongoing basis.[76] Principle 10 also requires that the EPFIs publically report on greenhouse gas emission levels for projects emitting over 100,000 metric tons of CO_2 annually.[77]

C. *Enforceability of the Principles*

Currently, the Principles include a disclaimer that they "do not create any rights in, or liability to, any person, public or private."[78] Therefore, although the EPFIs can demand a borrower's compliance with the Principles by withholding money or by demanding accelerated repayments of the loans, there is no enforcement mechanism to ensure that the EPFI will demand such adherence. Therefore, a lender's adherence to the Principles is voluntary, unenforceable by a third party and not legally binding in any jurisdiction.[79]

Incorporating these environmental protections directly into the loan documentation is a successful tool to alert all parties to the project's prioritization of environmental protection and to create contractual obligations for the borrower to comply with environmental standards. Inclusion of these protecting covenants, however, does not necessarily ensure that the lender will take the required action to address a borrower's breach of environmentally-protective covenants. If the lender does not exercise the remedies in the loan documentation that are triggered by a breach of the covenants, the environmentally destructive actions creating the breach may go unaddressed.[80] Further, third parties may lack standing to enforce the covenants[81] and inadequate transparency in the grievance, monitoring, and disclosure mechanisms prevent third-party communities and international organizations' from adequately voicing their concerns and demanding a resolution of identified environmental degradation.[82]

Due to the importance of these energy infrastructure projects for developing countries and the amount of control that lending institutions retain over the activities of the borrowers, there is a significant opportunity to revise the Principles to address these current shortcomings. With these revisions, infrastructure projects funded by EPFIs have the ability to create significant change in the growing energy sector and contribute to global environmental sustainability.

II. Legal Background: Issues in Lender Liability

To ensure that a project will operate and generate the profits needed for loan repayment, lending institutions must assess the risks inherent in each project.[83] These risks include environmental liabilities, negative impacts on local communities, and reputational risks, which may delay or prevent a project's construction and operation.[84] Due to increasing regulatory requirements from host governments[85] and NGO scrutiny of large-scale projects, private lending institutions face growing challenges in identifying and mitigating legal, economic, and reputational business risks.[86] Banks engaged in financing energy infrastructure projects are targeted by NGO campaigns designed to undermine a bank's reputation

71. *Id.* at 8.
72. *Id.*
73. *Id.* at 9.
74. *Id.* at 10. Further, Annex B to EPIII requires data and implementation reporting to be published on the EPFI's website in a single location and in accessible format.
75. *Id.* at 7.
76. *Id.*
77. *Id.* at 10.
78. *Id.* at 11.
79. *Id.*
80. Marco, *supra* note 15, at 467 (noting the lender "may" exercise remedies, but there is no requirement to do so).
81. *Id.* at 491 (no lawsuit has been reported, thus no guiding precedent exists as to whether affected communities would have standing to sue under U.S. contract law).
82. *Narrowing the Accountability Gap, supra* note 39, at 192.
83. Lenders engaged in project finance determine the feasibility of the project, based on its susceptibility to certain adverse conditions, and its technical and economic strength. Comer, *supra* note 34, at 4.
84. Wagner & Armstrong, *supra* note 4, at 140–41 (noting that energy industry activities involve a variety of environment, health, safety, and social issues that need to be carefully managed alongside geologic, political, and economic risk factors).
85. For example, the Brazilian Law No. 9,605 of December 2, 1998 (Environmental Crimes Law) states that all citizens have the right to an ecologically balanced environment, which is an asset of common use and essential to a healthy quality of life, and that both the government and the community shall have the duty to defend and preserve it for present and future generations. Further, this Brazilian law subjects offenders who conduct activities hurtful to the environment to administrative and criminal sanctions, in addition to requiring remediation of the damage. Mabel Alves de Faria Correa, Participants' Papers, The Brazilian Legal Framework for Investigation, Prosecution and Trial of Corporate Crime and the Criminal Liability of Corporate Entities 48–49 (137th International Training Course).
86. Wagner & Armstrong, *supra* note 4, at 145.

for involvement in environmentally destructive projects.[87] A bank's costs in defending itself against public attacks would be exacerbated by the costs of delaying projects due to simultaneous on-site environmental protests.[88] These combined impacts can complicate a lending institution's risk assessment, lead to long-term reputational damage, and can ultimately injure a lending company's bottom line.[89]

A. *The Financial Impact of Environmental Harm*

Public investors increasingly expect private companies to accept greater responsibilities for managing their negative impacts on the environment.[90] If, however, environmental issues have no perceptible negative financial implications for public investors, lending institutions may ignore them. Yet, if the impacts of cumulative environmental harms are significant enough, they can affect the project's operational timeline, revenue generation, and ultimately the borrower's ability to repay the loan.[91] Thus, calculating environmental and reputational risks is not only important for corporate social responsibility reasons, but also for a company's financial vitality.[92] However, reputational and environmental risks are inherently complex and difficult to evaluate.[93]

There is a direct link between the environmental risks of the project and the credit risks, or the risk of borrower default, which is assumed by the lenders.[94] Between 50–70% of an average publically traded company's economic value is based on intangibles like reputation.[95] When a project loses its formal regulatory permit to operate, or its informal community support due to an environmental violation, the project's credit risk will increase.[96] Should a company participate in too many risky transactions that create public opposition from environmental degradation, this may attract unfavorable attention that could damage the lenders' reputations, increase operating costs, and decrease stock value.[97]

Based on a 20-year study of 478 environmental violations by publically traded companies, allegations or charges of environmental violations resulted in "statistically significant losses in the firm's share values."[98] A single press announcement of an environmental violation was associated with a 1.69% drop in stock price within 48 hours of the announcement.[99] These initial losses were compounded by a drop of 2.26% of share values from any resulting legal expenses incurred.[100] While losses from environmental violations are not as high as those from allegations of fraud or other white-collar crimes, they are nonetheless significant.[101] On average, the overall reputational penalty for a company charged with an environmental violation accounts for 20.5% of the total losses experienced.[102] Stock price drops were even higher for those companies that were considered to have historically "bad environmental and safety records."[103] A second study of seventy-eight environmental crises experienced by publically traded companies since 2007 found that 60% of companies had a peak in "negative sentiment" within a month of the environmental disaster.[104] After 6 months, average stock prices were down 15% from pre-crisis levels, and, after a year, over 25% of the companies had not regained pre-crisis stock prices.[105] Perhaps recognizing the potential financial impact of poor project selection and risk management, Barclay's, an EPFI, revealed in a corporate responsibility report that the company rejected nearly a third of the highest risk project finance deals considered in 2005, choosing not to participate in a total of twenty-five out of a possible sixty-eight project finance transactions.[106]

B. *Examples of Environmental Risk Mismanagement*

In establishing a solution to the problems created by the current Principles' framework, it is critical that those capable of publicizing regulatory and contractual violations have greater access to information, as the threat of a drop in stock price may incentivize lending institutions to comply with regulatory and contractual commitments.[107]

There are several examples that demonstrate the impact that mismanagement of environmental risks has on lending institutions. Following the BP Deepwater Horizon rig explosion and devastating spill into the Gulf of Mexico, BP's shares fell 11%, resulting in a nearly $20 billion reduction of its market capitalization.[108] Although stock prices eventually recovered, reports of lawsuits and award assessments continue to impact its share value.[109] Unease over an $18 billion judgment against Chevron's involvement in the pollu-

87. Amalric, *supra* note 60, at 5.
88. Wagner & Armstrong, *supra* note 4, at 142.
89. *Id.* at 141.
90. *Id.* at 140; The Economist Intelligence Unit, *The Importance of Corporate Responsibility*, Economist 3 (2005) (noting that in 2005, 85% of executives and investors surveyed said Corporate Responsibility was a "central" or "important" consideration in investment decisions, as opposed to 44% of executives and investors surveyed in 2000).
91. Hardenbrook, *supra* note 55, at 211.
92. Richardson, *supra* note 48, at 269.
93. Benjamin Richardson, *Putting Ethics Into Environmental Law: Fiduciary Duties for Ethical Investment*, 46 Osgoode Hall L.J. 243, 285 (2008).
94. Almaric, *supra* note 60, at 9.
95. Richardson, *supra* note 93, at 250.
96. Nwete, *supra* note 41, at 184; Hunter, *supra* note 40, at 458 (Rainforest Action Network's campaign against Citibank revealed to the entire financial sector how failing to address the environmental impacts of their operations could damage their reputation and reduce stock value.).
97. Richardson, *supra* note 48, at 273; Jonathan Karpoff et al., *The Reputational Penalties for Environmental Violations: Empirical Evidence,* 48 J.L. & Econ. 653, 656 (2005).
98. Karpoff, *supra* note 97, at 654 (surveying the years 1980–2000).
99. *Id.*
100. *Id.* (based on an average damage award, in year 2000 dollars, of $13.2 million).
101. *Id.* at 668.
102. *Id.*
103. Paul Maidment, *How Does the Stock Market Respond to Petrochemical Disasters?,* Forbes (May 6, 2010), forbes.com/sites/davos/2010/05/06/how-does-the-stock-market-respond-to-petrochemical-disasters/.
104. J. Blain & S. Long, Freshfields Bruckhaus Deringer, Environment, Planning and Regulatory News 2 (2012), *available at* http://m.freshfields.com/uploadedFiles/Environment%20planning%20and%20regulatory%20news%20December%202012.pdf.
105. *Id.*
106. Oliver Balch, *Building a Better World (for Investors and Whales),* The Banker (July 3, 2006), http://www.thebanker.com/Markets/Climate-Carbon/Building-a-better-world-for-investors-and-whales?ct=true.
107. Maidment, *supra* note 103.
108. Tom Bergin, *BP Shares Drop as Oil Spill Worsens,* Reuters 2 (Apr. 29, 2010), http://uk.reuters.com/article/2010/04/29/us-bp-idUKTRE63S3A720100429.
109. *Id.* at 1.

tion of an Amazonian waterway led to a shareholder petition to require the company to nominate an independent board member with environmental expertise and to allow a review of disclosures to the Security and Exchange Commission.[110] In May, 2008, public outcry in Asia caused the Australia and New Zealand Banking Group, an EPFI, to withdraw from a controversial pulp mill that caused serious risk to the health of the local community and gravely polluted the environment surrounding the mill site.[111] Similarly, in 2006, a group of NGOs succeeded in pressuring ING Group, another EPFI, to withdraw from a $480 million paper mill project in Uruguay.[112]

As seen in these examples, many lending institutions versed in traditional risk-management techniques are ill-equipped to identify, understand, and manage complex environmental issues that are frequently fact-intensive and location-specific.[113] Yet this traditional deficiency may be changing as companies place growing importance on the environmental impacts of their operations.[114] Proactive companies now take steps to preemptively reduce uncertainties and manage environmental and reputational risks early on in the lending process to prevent last-minute withdrawals or surprises.[115] Companies now strive to create broader social support for projects, which ultimately increase the likelihood of project success and loan repayment.[116] According to the head of sustainable business advisory at ABN AMRO, one of the largest banks in Europe:

> Protecting our assets in a traditional sense is risk management and protecting shareholder returns . . . if we are financing potentially socially and environmentally egregious projects in far-flung corners of the world, then we also have the commitment to ensure that the social and environmental footprint of those projects is well managed.[117]

The Principles must take advantage of this changing corporate dynamic and solidify their role as the best practices standard for the industry. Although not all environmental harms caused by infrastructure projects create such widespread publicity as the harms detailed above, small, but continuous, violations may be cumulatively as damaging.[118] Because of strategic NGO involvement, certain projects receive disproportionate attention, which results in many smaller or isolated violations of environmental regulations going unnoticed.[119] Thus, it is imperative that all environmental harms and related contractual violations are made public quickly and prominently to induce lending institutions to complying with the Principles, in order to help ensure adherence to the private sector's claims of strong standards environmental stewardship.

III. Analysis: Problems With the Principles

A. *Lack of Legally Binding Obligations for Lending Institutions*

The Principles present an opportunity to harness the tremendous power of the market in driving environmentally responsible investment in energy infrastructure projects. While the Principles have helped abate the destructive pattern created by many large-scale infrastructure projects and helped promote environmental stewardship in the private sector,[120] they have not gone far enough. Currently, the Principles are purely voluntary for project lenders, they fail to articulate a clear legal standard,[121] and they do not adequately require the disclosure of project information.[122] Although borrowers may be required to comply with the Principles in the form of loan covenants, the EPFIs themselves are not required to exercise remedies in the event that the borrower breaches the covenants.[123] No independent supervisory organization is responsible for certifying a borrower's compliance with Principles that are incorporated into loan covenants; instead, the Principles are effective only if banks self-enforce their borrowers' compliance.[124] With each EPFI varying in their prioritization of compliance and allocation of resources to project monitoring,[125] the principles are vulnerable to "greenwash," a term describing participation in an environmentally conscious program on paper, but not in practice.[126]

The Principles' frequently vague mandates and lack of transparency and accountability make it difficult to determine their effectiveness. Without targeted requirements and publicized measurements, it is nearly impossible to hold EPFIs accountable for their borrowers' compliance violations.[127] This situation results in both borrowers and EPFIs often failing to implement the Principles in practice.[128] Should companies continue to benefit from association with the Principles without being required to adhere to the spirit of their provisions, the world will have lost a significant chance

110. Gretchen Morgenson, *Chevron Takes Aim at an Activist Shareholder,* N.Y. Times 1–3 (Dec. 8, 2012), http://www.nytimes.com/2012/12/09/business/chevron-takes-aim-at-an-activist-shareholder.html?_r=0.
111. Richardson, *supra* note 48, at 32; The Wilderness Society, *NGOs Welcome ANZ Decision Not to Finance Gunns Proposed Pulp Mill,* BankTrak News (2008).
112. Vivian Lee, *Enforcing the Equator Principles: An NGO's Principled Effort to Stop the Financing of a Paper Pulp Mill in Uruguay*, 6 Nw. U. J. Int'l Hum. Rts. 354, 361–64 (2008).
113. Wagner & Armstrong, *supra* note 4, at 145.
114. *Id.* at 146.
115. *Id.*
116. Int'l Fin. Corp., Good Practice Note: Addressing the Social Dimensions of Private Sector Projects 1 (2003).
117. Balch, *supra* note 106.
118. Allegations of repeated violations of environmental regulations decrease a company's reputation. Caroline Rees, *Grievance Mechanisms for Business and Human Rights: Strengths, Weaknesses and Gaps* 22 (Harvard Univ. Corp. Social Responsibility Initiative, Working Paper No. 40, 2008). Stock price drops were higher for those companies that were considered to have "bad environmental and safety records," than those with good environmental protection reputations. Maidment, *supra* note 103.
119. Watchman, *supra* note 69, at 115.
120. *See, e.g.,* Joshua A. Lance, *Equator Principles III: A Hard Look at Soft Law,* 17 N.C. Banking Inst. 175, 195 (2013); Hardenbrook, *supra* note 55, at 200.
121. Marco, *supra* note 15, at 470.
122. Hardenbrook, *supra* note 55, at 209.
123. EP III, *supra* note 18, at 11 (discussing the lack of liabilities created under the Principles).
124. Conley & Williams, *supra* note 14, at 544.
125. Some banks externally audit environmental reports, while others merely publicly reporting the funding on their finance transactions. Hardenbrook, *supra* note 55, at 228.
126. Hunter, *supra* note 40, at 471.
127. Hardenbrook, *supra* note 55, at 209.
128. Marco, *supra* note 15, at 469 (referencing the Sakhalin II Oil and Gas Project).

to take advantage of a global trend toward corporate social responsibility. Additional steps are needed to prevent banks from reaping the benefits of association with the Principles without fully complying with them.

B. *Obstacles to Creating Legally Binding Language*

While simply revising the Principles to include enforcement mechanisms might seem like the most straightforward solution, there are several reasons why removing the enforceability disclaimer and inserting a uniform enforcement mechanism would be problematic. First, as the Principles are a voluntary organization, the creation of legally binding obligations may reduce participation in such a way that could completely undermine the program.[129] The creation of enforcement mechanisms could detract from the net environmental benefit that the voluntary framework has created by encouraging a lending institution's withdrawal from participating in the Principles, negating the purpose of improved overall environmental protection sought by the enforcement mechanism.[130]

Second, because of the international scale of the Principles, there is no adequate universal forum to hear the quantity and complexity of cases alleging violations of the Principles.[131] In the International Court of Justice, only *states* may be parties in cases before the Court.[132] While the IFC or World Bank forums might at first be amenable, ultimately they are likely to be ineffective, as international legal institutions have limited jurisdiction over private, or non-state actors.[133] Further, many international tribunals are currently focused on bringing justice to perpetrators of past war crimes, as opposed to having the scientific and financial expertise to address ongoing environmental harms requiring quick action, as dictated in lender agreements.[134]

Third, direct enforcement of a Principle provision in U.S. courts would be problematic because there are many barriers to accessing domestic courts for violations of foreign projects. For example, the doctrine of *forum non conveniens,* which provides a court with discretion to decline to hear a case better suited for resolution elsewhere, could be used to send the case outside of the United States.[135] Also, *comity*, or legal deference to the laws and interests of a foreign country, could encourage domestic courts to defer to the inadequate environmental protection granted by the laws of the countries where the problematic projects are located.[136] Finally, the *political question doctrine* could be used by courts to refuse to hear a case on the basis that interference with large-scale projects in a foreign country would impede upon United States foreign policy or energy security issues.[137]

Fourth, it may not be in the EPFI's best interest to incorporate provisions into the Principles that would allow a third party to enforce stated commitments. Even current loan covenants that require compliance with the Principles are infrequently used.[138] Current covenants that trigger a default for non-compliance with the loan agreements allow the EPFIs to withhold money, to accelerate repayments of any loans, or to insist on immediate repayment of the loan in full.[139] Yet, because of the structure of project financing, such severe actions run counter to a lending institution's interest in recouping the money distributed.[140] Allowing a default would result in the failure of the project to reach its earning potential, deny the lending institution its repayment, and leave lending institutions in the unwanted position of both owner and operator.[141] Thus, these extreme remedies have typically been avoided in practice, and further provisions strengthening current capacities might similarly go underutilized.[142]

IV. The Proposed Solution

Banks are more likely to support and engage in a regulatory system that is self-enforced and flexible to meet their chang-

129. There is no incentive for banks to voluntarily assume legal liability for compliance with a voluntary initiative if they have access to the same market share without such legal obligations. *See generally* Paul Watchman, Visiting Fellow, London School of Economics, Address to the LSE Sustainable Finance Project 31 (Nov. 22, 2010) (stating that a bank's unwillingness to adopt the existing Principles is caused by a variety of reasons, including skepticism, "bottom feeding," or a lack of internal systems in place to implement the required procedures), *available at* http://www.lse.ac.uk/collections/law/projects/lfm/New%20EP%20Presentation%202.ppt.

130. Lance, *supra* note 120, at 195 (2013) ("even the most skeptical NGO would admit that the adoption and implementation of the Principles, at a minimum, has raised the level of awareness concerning social and environmental impacts of the projects financed under the EPs").

131. *See* Hardenbrook, *supra* note 55, at 218.

132. Statute of the International Court of Justice [I.C.J.], art. 34(1), 59 Stat. 1055, 33 U.N.T.S. 993 (June 26, 1945).

133. Hunter, *supra* note 40, at 472.

134. *See generally* Ivan Simonovi´c, *Dealing With the Legacy of Past War Crimes and Human Rights Abuses,* 2 J. Int'l Crim. Just. 701, 707 (2004) ("[The work of the ICTY and ICTR] was also quite slow, violating the principle of expeditious dispensation of justice"); Gillian Higgins, *Fair and Expeditious Pre-Trial Proceedings,* 5 J. Int'l Crim. Just. 394, 394 (2007) ("In the past decade, the length of time taken by international tribunals to try those accused of war crimes has been the subject of fierce criticism."); Ralph Zacklin, *The Failings of Ad Hoc Tribunals,* 2 J. Int'l Crim. Just. 541, 543–44 (2004) ("The delays in bringing detainees to trial—and the trials themselves—have generally been so lengthy that questions have been raised as to the violation by the tribunals of the basic human rights guarantees . . . Justice delayed is justice denied, which also raises the question of whether justice has been done to the victims.").

135. *See* Tuazon v. R.J. Reynolds Tobacco Co., 433 F.3d 1163, 1177–78 (9th Cir. 2006); Piper Aircraft Co v. Reyno, 454 U.S. 235, 235 (1981). The doctrine has been invoked to dismiss several cases brought by foreign communities who alleged environmental damage from the activities of U.S. corporations in their country.

136. Joel R. Paul, *Comity in International Law,* 32 Harv. Int'l L.J. 1, 5–6 (1991) (noting that "[t]he larger reaches of comity in the United States encompass a wide range of cases in which U.S. courts limit domestic prescriptive, adjudicatory, and enforcement jurisdiction, even where the rights of U.S. parties are adversely affected. Under the rubric of comity, U.S. courts have justified this deference as a sign of respect for foreign sovereignty, as a means of protecting the parties' expectations in the interest of international commerce, and as a mechanism for avoiding conflict with the management of foreign relations."); Torres v. Southern Peru Copper, 113 F.3d 540, 544 (1997).

137. In several cases involving environmental allegations against global companies for their activities abroad, the Department of Justice has submitted 'Statements of Interest' in an attempt to trigger dismissal based on the political question doctrine. For example, Sarei v. Rio Tinto, PLC, 671 F.3d 736, 756 (9th Cir. 2011), *cert. granted, judgment vacated sub nom.* Rio Tinto PLC v. Sarei, 133 S. Ct. 1995 (2013) (dismissing the case after receiving a Statement of Interest arguing that the continued adjudication of the case would interfere with the Bush administration's U.S. foreign policy interests in Papua New Guinea).

138. *See* Tim Baines, *Integration of Corporate Social Responsibility Through International Voluntary Initiatives,* 16 Ind. J. Global Legal Stud. 223, 243 (2009).

139. *Id.*

140. *See id.* at 242.

141. Hunter, *supra* note 40, at 473.

142. *Id.*

ing business needs. Thus, this Note proposes that to enhance environmental stewardship in developing countries through compliance with the Principles, the Principles should be revised *without* imposing legal liability on EPFIs. Instead, the Principles should be revised to capitalize on the factors most likely to induce compliance: a lender's reputation and, by extension, its bottom line. Both shareholders and lending institutions benefit from having access to an independent fact-finder that can provide credible reporting on environmental harms and can recommend ways to remedy violations of the Principles. If bank shareholders had greater access to information about the negative impacts of their bank's projects, they could express their preference for environmentally-conscious companies by divesting in banks that do not comply with the Principles. To that end, both shareholders and lending institutions would benefit from having access to an independent fact-finder that could provide credible reporting on environmental harms and recommend ways to remedy violations of the Principles. Further, banks compliant with the Principles would not need to expend resources defending against public attacks for violations, thereby decreasing project costs and increasing project profits.[143]

This approach also allows shareholders to more easily compare EPFIs by providing them with a uniform benchmark against which to measure banks. A compliance comparison benchmark would incentivize a bank's compliance with the Principles to attract business from environmentally-conscious investors.[144] Thus, greater disclosure of the environmental impacts of a bank's loans would increase the chance that any deviation from the Principles would be identified and publicized and the court of shareholder opinion would hold banks accountable.[145] The cumulative effectiveness of such a revision, however, relies on assigning more concrete responsibilities and tasks to lenders under the Principles' current grievance, monitoring, and disclosure mechanisms.

A. Enhanced Grievance, Monitoring, and Disclosure Mechanisms

Current grievance and monitoring mechanisms are insufficient in disclosing information needed to generate the public exposure essential for inducing lender compliance with the Principles.[146] Unlike the existing Principles, the revisions proposed in this Note would provide more guidance for EPFIs and impose more demanding disclosure obligations on lending institutions.

1. Grievance Submission and Resolution

The grievance process is the first step in remedying gaps in compliance with environmental provisions in loan documents. For the process to be successful, it is imperative that there be adequate stakeholder engagement and a relationship of trust between communities and borrower-employed project administrators.[147] Community members must be able to understand and utilize the grievance mechanisms, trust the process, and not fear retaliation for their submissions.[148] The grievance process under the current Principles is broad and general, focusing on overall goals of prompt and transparent resolution of concerns of project impacts.[149] Yet this vague mandate makes it difficult for any challenger to pinpoint non-compliance. Thus, this Note proposes the inclusion of more specific language in the Principles, concrete targets, and easily identifiable levels of action to facilitate identification and reporting of violations of the Principles.

a. Revised Language

Language: Currently, Principle 6 makes it the responsibility of the *borrower* to conduct the grievance and monitoring processes.[150] Principle 6 dictates that the EPFI require its client to establish a grievance mechanism "designed to receive and facilitate resolution of concerns and grievances about the [p]roject's environmental and social performance."[151] Currently, the borrower is responsible for collecting and addressing all grievances on site.[152] However, only the *lender* is signatory to the Principles and thus is responsible for adherence to the Principles.[153] The borrower is only responsible for compliance with the loan covenants and, unlike the lender, who is a signatory to the Principles, violation of the loan covenants has no ramifications beyond the project itself.[154] Because the lender has the greater incentive to protect the reputation of the Principles within the industry, the lender must have the responsibility for addressing problems brought forward through the grievance mechanism. Thus, instead of allowing the borrower to independently manage grievances collected on-site, Principle 6 should be modified to mandate that the borrower disclose *all* grievance and monitoring violations related to environmental conditions to the Independent Environmental and Social Consultants, further explained below, to be channeled to the lending institutions. This would ensure that the lender, or the ultimate party responsible for compliance with the Principles, becomes aware of current environmental issues and can participate in their resolution, instead of relying on the borrower to independently manage grievances.[155]

Standing: Current constraints on access to a grievance mechanism lie in restrictions on who can bring a grievance complaint. Under the current Principles, the grievance mechanism targets Affected Communities, or "local communities

143. *See* Baines, *supra* note 138, at 241.
144. *Id.* at 230.
145. Hunter, *supra* note 38, at 477.
146. Freshfields Bruckhaus Deringer, Envtl. Plan. & Reg. News, Environmental Disasters Have Biggest Long-Term Effect on Shares 2 (2012); Richardson, *supra* note 48, at 273.
147. Int'l Fin. Corp., Addressing Grievances From Project-Affected Communities 2 (2009).
148. *Id.*
149. EP III, *supra* note 18, at 8.
150. *See id.* at 20.
151. *Id.* at 8.
152. *Id.*
153. *Id.*
154. *Id.*
155. Limiting this reporting of grievances to environment-related grievances minimizes the lender's micro-management of the borrower's employment or facility administration that is best handled by the borrower.

within the Project's area of influence, directly affected by the Project." In contrast, grievance processes should grant standing liberally and allow non-local groups to submit grievances or act as advocates on behalf of these Affected Communities. The current vague mandate provides inadequate guidance for lenders to require a consistent grievance mechanism among all EPFI-funded borrowers[156] and makes it difficult for any non-local aggrieved party to participate.

The revised mechanism should include broad language such as: "any person or group of people who may be negatively affected by a project are eligible to submit a claim." Representation by both local community organizations and non-local, international NGOs should be permitted if they clearly identify the individual on whose behalf the grievance submission is made. The grievance process should tap into the local knowledge of environmental conditions, and should provide a hierarchical mechanism to channel concerns from those on the ground to those overseeing project decisions.[157] Community leaders should continue to be educated about the grievance process during borrower-led initial outreach sessions, because the same communities contacted as part of the prior informed consent process are likely those that may experience negative impacts from the projects.

Substance and Format: Currently there is no uniform requirement for what grievance submissions should look like; rather, the borrower creates each grievance on a project-by-project basis. To ensure uniformity among all grievances collected in EPFI-funded projects, and to ensure that any grievances appealed to the Board include consistent information, there must be increased guidance on the format of the grievance submissions and the substance of the complaint. This consistency will not only allow the Board to review grievances more thoroughly, but will assist international NGOs participating in a grievance process in numerous projects to familiarize themselves with the process more rapidly.

A grievance should identify (1) the project in question, (2) the description of the direct harm experienced, (3) the person submitting the grievance, and (4) the desired remedy. In order to ensure that responses can be addressed to the correct party, anonymous grievances should not be accepted, unless speech-chilling concerns of borrower retaliation against the parties submitting grievances are identified. Grievances may be submitted in any form and oral complaints should be accepted and recorded by site administrators. In addition, grievances should be accepted in either the host country's national language or the language used by the borrower's workforce communications.[158]

b. Collection and Resolution of Submissions

To induce accountability, the revised grievance mechanism must also include more detailed provisions on how submissions are collected and addressed. This will help promote the Principles' overarching goals of trust and transparency.[159] Due to conflict of interest concerns, the party collecting grievances against themselves cannot be the same group addressing these grievances. Thus, there must be a separation of functions between the two processes, with the borrower collecting the grievances and then submitting them to the Independent Environmental and Social Consultants identified under Principle 9, or the "a qualified independent firm or consultant (not directly tied to the client) acceptable to the EPFI."[160] Principle 9 requires the appointment of an Independent Environmental and Social Consultant to monitor ongoing compliance with the Principles and this Note proposes expanding the responsibilities attributed to this existing independent position.

Submitted grievances should be collected, registered or recorded, and categorized based on the severity of the allegation and the similarity to previously received grievances to identify ongoing issues. The adoption of concrete timetables would also help remedy the current ambiguity in the Principles' expectations. To emphasize grievances with particular severity, this Note proposed a tiered system of grievance categorization. This recommended multi-track system would allow prioritization of certain issues, and create an organized way to monitor ongoing problems. For example, a grievance about a heavy rainfall causing a chemical or sedimentary leak into a nearby waterway damaging fish populations could be categorized as Track 1, as it demands a more rapid remedy than a Track 2 grievance about temporary soil compaction during heavy material storage.

The process of collection, registration, and categorization should be conducted immediately, in order to provide affected communities with rapid resolution of the environmental problems with greatest negative implications. Then, depending on the grievance's categorization, the Independent Environmental and Social Consultant will prioritize its time schedule and proceed to engaging in a consultation process with the impacted party to attempt to remedy the alleged negative impacts. This informal resolution process, requiring greater time, should nonetheless take no more than 45 days from the date of the grievance was submitted, during which time the Consultant will investigate alleged violations of procedures that have resulted, or are likely to result, in negative impacts on project-affected groups, and to make recommendations to ensure project compliance.[161] If the issue is not resolved within this 45-day timetable, the grievance should be automatically appealed to the Board, detailed below.

2. Independent Monitoring and Disclosure

To remedy insufficiencies in the current monitoring reporting and transparency elements, the Principles should adopt the greater transparency and recording process recommended by

156. EP III, *supra* note 18, at 8, 15. *But see* Guidance Note on Equator Principles Implementation Reporting, *available at* http://equator-principles.com/resources/ep_implementation_reporting_guidance_note.pdf
157. *See, e.g.,* EP III, *supra* note 18, at 8 (for the generalness of the current Principle).
158. *See id.* at 16.
159. *See id.* at 10.
160. *Id.* at 17.
161. Asian Development Bank, Review of the Inspection Function: New Accountability Mechanisms 11 (2003).

this Note for the Principle 6 Grievance mechanism, as well as for Principles 9 and 10. Principle 9 requires an Independent Environmental and Social Consultant to monitor ongoing compliance with the Principles.[162] Principle 10 requires the borrower to disclose on its website its initial assessment documentation or information gathered during the course of the categorization and due diligence process when assessing the project's potential environmental risks and impacts.[163] It also requires disclosure of the stakeholder consultation, meant to initially inform communities and incorporate their input on project elements that affect them directly into project mitigation or implementation issues.[164] In addition to the above borrower's disclosure requirements, the EPFI itself is further required to report publicly, at least annually, on transactions that have reached Financial Close and on its Principles implementation processes and experience.[165] However, these minimal oversight and disclosure requirements are inadequate to remedy some of the potential violations that may arise during the course of the project because of the lack of current integration with the grievance process and the infrequent occurrences of the ongoing monitoring and disclosures.

This proposed enhanced monitoring supplements the initial grievance collection and remediation process to ensure that problems are adequately addressed and any additional problems are immediately identified. Should issues addressed during the grievance collection process be ongoing or should issues become apparent that have not been identified by a community member through the grievance process, then this Note proposes that it be the responsibility of the Independent Consultant to identify this and engage in an expanded Principle 9 Monitoring and Reporting process. To ensure uniformity and consistency along the way, the Independent Consultant should categorize ongoing problems in the same manner as the proposed grievance mechanism, requiring greater uniform collection of information and allocating more resources to monitoring Track 1 problems as opposed to Track 2 issues. Additionally, this monitoring and disclosure should occur more frequently: monitoring updates from the Consultant should occur monthly and disclosures from the EPFI should occur bi-annually. Further, although currently the EPFI is required to report publically "taking into account appropriate confidentiality concerns,"[166] it is imperative that the Consultants be given complete access to both the borrower and the lender's documentation free of confidentiality concerns and be permitted to access the project site and discuss grievances and observed issues with both community members and project administrators.

B. Creation of an Oversight Appeals Board

The revisions proposed in this Note incentivize compliance by EPFIs through market forces and through the creation of an Oversight Appeals Board ("Board") with sanctioning power to which all submitted grievances collected from the Independent Consultants could be appealed, the results of which would be publically available. All EPFIs would be subject to the rulings of this Board, which would not be tied to any country's judicial system but would create a centralized forum for disputes. If disclosures from the Board reveal violations of the Principles, local communities, international non-profit groups, and private citizens could publish and protest these companies' actions, resulting in the negative public portrayal of these publically-traded companies. If any reported harm is so grave as to cause a drop in stock value, the Principles then may be enforced through domestic legal causes of action in U.S. courts, such as shareholder derivative suits.[167]

1. Scope of the Board

The most significant revision of the current Provisions proposed in this Note is the adoption of a Board. This Board would be comprised of representatives of member banks with multi-stakeholder oversight. Grievance and monitoring mechanisms limited strictly to individualized projects often insufficiently address environmental issues because local authorities are not always able to resolve the problem or create the systematic changes needed to prevent the issue's reoccurrence.[168] As a solution, this Board would provide a centralized forum independent of any one bank, but functioning as a way to harmonize existing monitoring and grievance mechanisms proposed to be directed toward the Independent Consultant. There are a multitude of oversight forums based on global best practices, such as the World Bank Inspection Panel, created in 1993 to address complaints from people who may have been adversely affected by a project funded by the World Bank.[169] However, in keeping with the independent regulatory system of the Principles, the Board would

162. EP III, *supra* note 18, at 10.
163. *Id.*.
164. *Id.*.
165. *Id.*, Annex B.
166. *Id.* at 8, 10.

167. Shareholders' monitoring of company projects and their support or disproval subtly directs the lending institutions' operations, and as a result, directs the project finance industry. The unique relationship between the shareholders and the business director's makes derivative suits an alternative mechanism for ensuring compliance with the Principles. Risky investments in environmentally destructive *infra*structure projects are more likely to fail, resulting in slower or no return on investment. Yet, because of the inherent ambiguities in environmental risk-calculation, it is difficult to find that the director acted against their best business judgment in supporting a project. Thus, the magnitude of a director's miscalculation must be very high before their risk-miscalculation triggers the shareholder's initiation of a derivative suit that survives the pleading stage. Further, imposing liabilities on lending institution directors may discourage such risk-taking, perhaps preventing the support of new environmentally friendly technologies. These problems brought about by imposing liability as a corporate governance mechanism show that derivative suits are simply an additional, although imperfect, compliance mechanism to ensure compliance with the Principles. *See* Bert Scholtens, *Finance as a Driver of Corporate Social Responsibility,* 68 J. Bus. Ethics 19, 21 (2006).
168. Rees, *supra* note 118, at 22.
169. The six current citizen enforcement mechanisms are: (1) the World Bank Inspection Panel; (2) the International Finance Corporation's Compliance Advisor and Ombudsman; (3) the Asian Development Bank's Accountability Mechanism; (4) the Inter-American Development Bank's Independent Investigation Mechanism; (5) the European Bank for Reconstruction and Development's Independent Recourse Mechanism; and (6) the African Development Bank's Independent Review Mechanism. *See* Jonathan Fox et al., Demanding Accountability: Civil-Society Clams and the World Bank Inspection Panel (Dana Clark et al. eds., 2003).

not, and should not be perceived as replacing national and international litigation forums.[170] Yet as the widespread commitment to the Principles suggests, the EPFIs are amenable to coordinated regulation and thus should agree to take a coordinated approach to accountability.

2. Structure of the Board

The Board would be comprised of a review panel with members from different banks. Because of the large number of participating financial institutions, each bank would submit one representative for majority approval and confirmation to create a largely independent forum.[171] From this pool, a group of five to seven members would be selected at random to decide individual cases or groups of similar cases. Although to ensure objectivity, no member would review their own bank's cases to ensure consistency among similar reoccurring problems, a public precedent for previous rulings would eventually result in a common law-like guidance for reoccurring problems similar in nature.

Appeals to the Board would be reviewed on an anonymous basis. Identifying information from the project would be redacted so that panelists would not know the project name, location, or which bank was involved until the case was decided. As no Board member would be eligible to decide a case in which their bank was involved, each year one Board member would be responsible for screening for all conflicts and allocating all cases to Board members. The Board could be funded through a revolving fund based on each lending institution's size or by a small percentage of each project's profit. Because the current EP membership dues are a meager £3,100, or just over $4,600 annually, there is significant room for an increase in dues to cover Board administration costs.[172]

This Board would address grievances not adequately addressed locally or ongoing issues identified by the Independent Consultant that are not amenable to local resolution. Lending institutions, borrowing institutions, or stakeholders unsatisfied with the resolution of the grievance process could request a Compliance Review to be seen by the Board. The Board would further have the capacity to recategorize a project, reducing the potential for Category C projects with unforeseen impacts to avoid the additional requirements applicable to a Category A or Category B project.

Due to the pressing nature of appeals that the Board reviews, decisions must be decided quickly or are automatically decided in favor of the aggrieved party with a recommended mitigation plan. Due to its targeted jurisdiction, this Board may ultimately provide a more speedy remedy and a smaller financial burden than a litigation settlement or court order.[173] This independent system would further promote clear and consistent application of the Principles, ensuring uniformity and legitimacy because of the objective nature of a multi-member forum reviewing cases with which they have no affiliation.[174]

3. Enforcement Powers of the Board

To implement the Board review, the financing agreement between the lending and borrowing institutions would need to contain a provision, requiring both lending and borrowing companies to adhere to the Board's findings and recommendations. Although the recommendations would likely not be legally enforceable elsewhere,[175] the Board would be given the authority, through the loan documentation covenants, to require the lending institutions to act or to refrain from acting based on Board review of a grievance. Additional deterrent powers would include the imposition of fines, increased supervision and reporting requirements, or even greater penalties such as prohibiting a bank from lending to similar types of projects in the future.[176] Yet, because each Board member is a representative of a lending institution engaging in similar projects, penalties are unlikely to be this harsh in all but the most egregious cases to prevent other members from mandating similarly harsh retaliatory penalties.[177] The greatest power the Board would have is the authority to expel a lending institution from membership in the Equator Principle community, and thus extreme violators would lose the benefit of association with the Principles and would be subject to public sanction.[178] All projects currently underway would be exempt from the Board's oversight, and lending institutions would be given a grace period to choose whether to comply with the additional requirements for future projects or to withdraw from affiliation with the Principles.

4. Board Reporting and Disclosure

Stemming from this Board power are greater opportunities for publication of information to induce compliance without Board sanctions. This Board would provide a centralized database that would publish a summary report of each resolved grievance or monitoring statement appealed to the Board. This report would disclose: (1) the lending and borrowing institutions involved, (2) the project involved, (3) the elements of the alleged violation or impact, (4) the core elements of the process, and (5) the resolution of the grievance reached by the Board. Because there are concerns that full disclosure would stifle open communication and raise issues of disclosure of proprietary information, all publications would be disclosed in light of privacy concerns.[179] Information on

170. Bridgeman & Hunter, *supra* note 39, at 232.
171. Due to political difficulties in involving the appointment of an NGO representative, Board memberships would be limited to bank employees.
172. *Equator Principles III—Annual Fee,* Equator Principles Ass'n, http://www.equator-principles.com/index.php/adoption/annual-fee (last visited Mar. 15, 2013).
173. Clayton, *supra* note 47, at 183.
174. Andrea Durbin et al., *Shaping the Future of Sustainable Finance: Moving the Banking Sector From Promises to Performance,* WWF & BankTrack, (Jan. 26, 2006), http://www.banktrack.org/show/news/new_wwf_banktrack_report_shaping_the_future_of_sustainable_finance.
175. Bridgeman & Hunter, *supra* note 39, at 232.
176. Clayton, *supra* note 47, at 183–84.
177. *Id.*
178. Baines, *supra* note 138, at 245.
179. Although this privacy could be potentially subject to abuse, it is meant to protect construction methods or infrastructure technology, and not to protect

Board cases would be available on the Principles' website in both the host country's language and the language of the operating lending institution. This information would thus be available and publishable in lending institutions' shareholder reports or NGOs scorecards of lending institutions.

Improved accountability and oversight by the EP community would not only improve environmental protection at the local level, but also the reputation of the EPFIs and the Principles as a whole.[180] This Board would provide lending institutions with yet another tool to induce compliance with loan documentation provisions, and another deterrent for non-compliance, as borrowers' violations would be seen by peer banks and disclosed in a public forum.[181] The proposed addition of the Board to the current Principles seeks to enforce the express agreements between lending and borrowing institutions to make lending banks more accountable for harms created by the energy infrastructure projects with which they are associated.

V. Conclusion: Summary of Proposed Revisions

This Note proposes revised grievance, monitoring, and disclosure mechanisms to be adopted into the Principles to ensure that future energy infrastructure projects developed under the Principles will be conducted in an environmentally conscious manner. With the information gathered from the revised grievance, monitoring, and disclosure mechanisms, and published through the Board, there are increased opportunities to encourage lending institutions to comply with their commitments under the Principles. Through this process, not only will those responsible for overseeing the project be notified of potential non-compliance, but those ultimately dictating the choices of the banks themselves, the shareholders and directors, will be alerted to it. Viewed together, these revised mechanisms provide interested parties with a greater power to induce compliance with the Principles. This approach, although less coercive than direct litigation, arguably is more effective due to its market-driven, information-based focus. This approach presents the most cumulatively beneficial solution, encouraging private sector sustainability initiatives, while allowing impacted communities the access to decisionmakers they need to ensure that their local environments are protected.

Because the Principles are a manifestation of a growing desire to incorporate corporate social responsibility ideals into specific transactions, the proposed recommendations can be helpful for those looking for creative ways to use private financial capacity to incentivize responsible energy infrastructure development in the future. While it is unrealistic to expect perfect compliance with the Principles by any lending institution,[182] or to expect that no negative environmental impacts will arise from a large-scale energy infrastructure project, this Note proposes revisions to the Principles that will encourage further environmental stewardship by lending institutions' participating in the Principles.

disclosure of the environmental damages caused by the project.

180. *See supra* Part II.A.

181. *Cf.* The Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 15 U.S.C. and 18 U.S.C. (2002)) (Sarbanes-Oxley created extensive reforms to the way that publicly held corporations account for and make public disclosures in an effort to deter further corporate fraud after the late 1990's Enron scandal.).

182. *See generally* Andrew Lee Nguyen, Investigating Compliance/Non-Compliance With the Equator Principles (2007), *available at* http://irps.ucsd.edu/assets/021/8418.pdf.