DEBT FINANCING AND THE EQUATOR PRINCIPLES

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Introduction

The debate about appropriate processes for the integration of sustainability considerations into investment evaluation as an integral part of debt financing is gradually drawing in the financial sector (Commonwealth of Australia 2003, 14). The Equator Principles have been presented as a base level industry approach for financial institutions to use when determining, assessing and managing environmental and social risk in project financing. These Principles are briefly outlined below.

The Equator Principles and project risk

The Equator Principles provide a voluntary set of environmental and social screening criteria and guidelines and have been adopted by the following nineteen major international banks (as at 6 January 2004).

- ABN AMRO Bank, N.V.
- Barclays plc
- CIBC
- Citigroup, Inc.
- Crédit Lyonnais
- Credit Suisse Group
- Dexia Group
- Dresdner Bank
- HSBC Group
- HVB Group
- ING Group
- MCC
- Mizuho Corporate Bank
- Rabobank Group
- Royal Bank of Canada
- Standard Chartered Bank
- The Royal Bank of Scotland
- WestLB AG, and
- Westpac Banking Corporation

Screening of each proposed project is undertaken to determine the appropriate extent and type of assessment required. The International Finance Corporation (IFC), the private-sector investment arm of the World Bank, established the set of environmental and social screening processes behind the Equator Principles. Proposed projects are classified into one of three categories, A, B and C, depending on the type, location, sensitivity, and scale of the project and the nature and magnitude of its potential environmental impacts. The classification determines the tightness of the environmental assessment required. The environmental assessment includes assessment of environmentally induced social impacts that would be brought about by the project.

Category A: A proposed project is classified as Category A if it is likely to have significant adverse environmental impacts that are sensitive, diverse, or unprecedented. A potential impact is considered "sensitive" if it may be irreversible (e.g., lead to loss of a major natural habitat) or affect vulnerable groups or ethnic minorities, involve involuntary displacement or resettlement, or affect significant cultural heritage sites. These impacts may affect an area broader than the sites or facilities subject to physical work or activity. Environmental Assessment for a Category A project examines the project's potential negative and positive environmental impacts, compares them with those of feasible alternatives (including, the "without project" situation), and recommends any

measures needed to prevent, minimize, mitigate, or compensate for adverse impacts and improve environmental performance. For Category A risks a full environmental assessment is required which is normally an Environmental Impact Assessment (EIA).

Category B: A proposed project is classified as Category B if its potential adverse environmental impacts on human populations or environmentally important areas-including wetlands, forests, grasslands, and other natural habitats-are less adverse than those of Category A projects. These impacts are site-specific; few if any of them are irreversible; and in most cases measures for mitigation can be designed more readily than for Category A projects. The scope of Environmental Assessment for a Category B project may vary from project to project, but it is narrower than that of Category A. Like a Category A Environmental Assessment, it examines the project's potential negative and positive environmental impacts and recommends any measures needed to prevent, minimize, mitigate, or compensate for adverse impacts and improve environmental performance.

Category C: A proposed project is classified as Category C if it is likely to have minimal or no adverse environmental impacts. Beyond screening, no further Environmental Assessment action is required for a Category C project.

Based on the Principles signatories agree that they will only provide loans directly to projects when:

1. They have categorised the risk of a project in accordance with the environmental and social screening criteria of the IFC;

2. For all Category A and Category B projects, the borrower has completed an Environmental Assessment (EA), the preparation of which is consistent with the outcome of the categorisation process and addresses key environmental and social issues identified during the categorisation process.

3. In the context of the business of the project the EA report has addressed:

a) assessment of the baseline environmental and social conditions
b) requirements under host country laws and regulations, applicable international treaties and agreements
c) sustainable development and use of renewable natural resources
d) protection of human health, cultural properties, and biodiversity, including endangered species and sensitive ecosystems
e) use of dangerous substances
f) major hazards
g) occupational health and safety
h) fire prevention and life safety
i) socioeconomic impacts
j) land acquisition and land use
k) involuntary resettlement
l) impacts on indigenous peoples and communities
m) cumulative impacts of existing projects, the proposed project, and anticipated future projects
n) participation of affected parties in the design, review and implementation of the project
o) consideration of feasible environmentally and socially preferable alternatives
p) efficient production, delivery and use of energy
q) pollution prevention and waste minimization, pollution controls (liquid effluents and air emissions) and solid and chemical waste management.

In each case, the EA will have addressed compliance with applicable host country laws, regulations and permits required by the project. Also, reference will have been made to the minimum standards applicable under the World Bank and IFC Pollution Prevention and Abatement Guidelines. World Bank Guidelines are available for 41 industries. IFC Guidelines have been drawn up for 28 industries. In addition, for projects located in low and middle income countries as defined by the World Bank Development Indicators Database (see web site for country classifications at http://www.worldbank.org/data/countryclass/classgroups.htm), the EA will have further taken into account any applicable IFC Safeguard Policies (listed at http://www.equator-principles.com/documents/Equator_Principles.pdf). Safeguard policies are in place for: environmental assessment; natural habitats; pest management; forestry; indigenous peoples; involuntary resettlement; cultural property; child and forced labour; and international waterways). In each case, the EA will have addressed the project's overall compliance with (or justified deviations from) the appropriate Guidelines and Safeguard Policies.

4. For all Category A projects, and as considered appropriate for Category B projects, the borrower or third party expert has prepared an Environmental Management Plan (EMP) which draws on the conclusions of the EA. The EMP has addressed mitigation, action plans, monitoring, management of risk and schedules.

5. For all Category A projects and, as considered appropriate for Category B projects, the lender is satisfied that the borrower or third party expert has consulted, in a structured and culturally appropriate way, with project affected groups, including indigenous peoples and local NGOs. Information about the EA has been made available to the public for a reasonable minimum period in local language and in a culturally appropriate manner. The EA and the EMP will take account of such consultations, and for Category A Projects, will be subject to independent expert review.

6. The borrower has covenanted to:

a) comply with the EMP in the construction and operation of the project
b) provide regular reports, prepared by in-house staff or third party experts, on compliance with the EMP and
c) where applicable, decommission the facilities in accordance with an agreed Decommissioning Plan.

7. As necessary, lenders have appointed an independent environmental expert to provide additional monitoring and reporting services.

8. In circumstances where a borrower is not in compliance with its environmental and social covenants, such that any debt financing would be in default, we will engage the borrower in its efforts to seek solutions to bring it back into compliance with its covenants.

9. These principles apply to projects with a total capital cost of US$50 million or more.

Comment

The Equator Principles provide a framework for financial institutions to develop individual, internal screening practices and policies. Screening of loans is but one of a set of mechanisms that may encourage moves towards sustainable finance. The effectiveness of the screening processes and adoption of the Principles for any given financial institution stand or fall on the level of commitment of management to reducing

environmental and social impacts of the organization. People with an eye on the actual results from the adoption of the Equator Principles will be disappointed when they read the standard disclaimer from responsibility by the financial institutions if poor environmental and social loans are made by a signatory in the future. It states that "As with all internal policies, these principles do not create any rights in, or liability to, any person, public or private. Banks are adopting and implementing these principles voluntarily and independently, without reliance on or recourse to IFC or the World Bank."

Further information about the Equator Principles is available at http://www.equator-principles.com.

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Reference:
Commonwealth of Australia (2003) *Corporate Sustainability – an Investor Perspective. The Mays Report*, Department of Environment and Heritage, Canberra, Australia.

TRIPLE BOTTOM LINE ACCOUNTING: A FORESTRY TASMANIA PERSPECTIVE

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The traditional financial accounting model has been the measurement tool by which internal and external parties evaluate and measure an organisation's performance. The impacts of social and environmental issues on a business have changed the focus away from the financial elements of the business being the only tool by which a business can be measured. An organisation must now be measured on its sustainability. This is a paradigm shift for many businesses, but it is a shift that must occur if the business is to survive.

"Triple Bottom Line" accounting (TBL) is a concept that has been around since the mid 1990's which refers to organisations being accountable and reporting on their economic, social and environmental performance. The basis reporting against these components is tied to the concept and goal of sustainable development. The following description covers the TBL concept:

> "The perspective taken is that for an organisation to be sustainable it must be financially secure, it must minimise its negative environmental impacts and it must act in conformity with societal expectations. These three factors are highly inter-related."

Many organisations, including Forestry Tasmania, are directing their activities and efforts to ensure that all three components are being undertaken. The difficulty is how the organisation's performance in this regard can be reported by bringing together the individual components into an integrated report that can address the relationship