

## Challenge to Financial Institutions

### Summary

As the experience of the last few decades has shown, financing dams can be a risky business, both in financial and reputational terms. Yet, major investments in water and energy infrastructure are clearly needed. The recommendations of the *World Commission on Dams* (WCD) point the way forward. Set out below is the challenge which WWF is issuing to financial institutions to ensure, post WCD, that investment in dams and other large infrastructure projects becomes more financially viable, as well as environmentally responsible and socially sustainable.

More specifically:

- WWF recognises that there has been too little consultation with financial institutions on how they can interpret the WCD's recommendations.
- Clear benefits, in terms of financial as well as reputational risk, would accrue if the new WCD-recommended approach was utilised by financial sector players.
- WWF invites leading financiers and financial institutions to discuss its suggested agenda for application of the WCD Policy Framework in the financial domain.

### Why a World Commission on Dams?

The WCD was set up by the World Bank and IUCN (The World Conservation Union) to respond to the increasing controversy surrounding many large dam projects. The Commission's twelve members came from government, NGOs and the private sector.

### Independent global study

After two years' investigation, the WCD published its report in November 2000. It confirmed that dams have made an important contribution to human development, providing significant benefits, but also concluded that large dams constructed to date have yielded such benefits ineffectively and inconsistently with many not meeting their economic and technical targets. It found that significant and irreversible loss of species and ecosystems has been caused and that an estimated 40-80 million people have been displaced by reservoirs. Not only, observed the WCD, has the social and environmental price paid been unacceptably high, but also such a price is often unnecessary to secure the benefits of dams.

### Responding to Water and Energy Needs

As the WCD Report emphasised, underlying decisions are not about dams as such, but about ways of responding to water and energy needs, including mobilisation of much-needed finance for infrastructure. A key recommendation of the WCD Report is that consideration of dam projects be placed in the context of a wider planning cycle for management of water resources and energy development. As well as proposed dam projects, non-dam options need to be explored properly. Major infrastructure projects, once set in motion, tend to acquire substantial

momentum so that it is critical to determine strategic direction and goals before a particular project is begun.

### **Avoiding Conflicts, Improving Performance**

Past projects which did not pay proper attention to broader social, environmental and ethical aspects, alongside engineering and other technical challenges, have increasingly met with determined public resistance. Problems and delays have been encountered, particularly during the construction phase, with serious consequences for the interests and reputations of project sponsors and developers. The WCD recommends that, in future, planning and preparation anticipate the broad range of relevant issues up-front and arrive at public acceptance of the chosen option before project commencement - the only practicable way, argues the WCD, to prepare projects for successful implementation.

Financing institutions clearly have an interest in well-planned, smoothly managed and successfully completed water and energy projects. Disruption to projects tends to cause time overruns which delay the revenue stream as time and cost overruns undermine the ability of governments and project developers (and other borrowers) to make scheduled repayments. Re-scheduling of loans is time-consuming, distracting bankers' energies from new business.

The WCD proposes a new "*Policy Framework*" which, it is convinced, which should deliver more sustainable water and energy projects. Its recommendations relate to procedural (as opposed to substantive) decisions on dams; it is a framework for improved decision-making to improve project performance and avoid past conflicts.

### **Improving Investment Policies and Standards**

WWF challenges sponsors of major water and energy projects to discuss the WCD policy proposals from the financial viewpoint.

To date there has been little debate of the implications for banks and financial institutions of adoption - by governments, implementing agencies and other parties to such projects - of the WCD recommendations. A key issue for discussion is how new investment procedures and standards following the WCD approach can enable borrowers to obtain finance on reasonable terms and allow lenders to secure reasonable rates of return - whilst avoiding controversy and conflict and ensuring environmentally responsible and socially sustainable projects.

Financial institutions are under increasing pressure to adopt and implement policies and practices for responsible investment (socially, environmentally and ethically). WWF believes that the WCD Policy Framework provides the basis for development of improved procedures and standards for investment in infrastructure.

The Framework is not, in itself, a standard or a ready-made code of practice; nor is it directly applicable. Indeed, it was not intended to be and the WCD was careful to avoid proposal of a "blueprint". Instead it needs to be transposed by governments into national laws and standards, and translated by international lending agencies, export credit agencies and private sector financial institutions into their operational guidelines.

**WWF invites leading financiers and financial institutions to discuss its suggested agenda – attached - for application of the WCD Policy Framework in the financial domain.**

## **NEW INVESTMENT PROCEDURES AND STANDARDS**

### **Agenda for Application of the WCD Policy Framework in the Financial Domain**

#### **International Lending Agencies (including bilateral donors) (ILAs)**

- Adoption of *WCD Policy Framework*
- Updating of ILAs' investment guidelines in accordance with the *WCD Strategic Priorities*
- Transparent screening out of non-aligned programmes/projects
- Support to transposition by governments of the WCD Framework into national laws and standards (in collaboration with *Dams and Development Project* of UNEP)
- Support to development/strengthening of sectoral water & energy strategies, at national and sub-national levels (based on options assessment and public consultation)
- Support to building of national capacity to conduct planning and oversee implementation of programmes/projects in accordance with new standards (eg. options assessment, multi-stakeholder processes, impacts assessment, benefits-sharing etc.).

#### **Export Credit Agencies (ECAs)**

- Adoption of *WCD Policy Framework*
- Updating of ECAs' internal investment guidelines in accordance with the *WCD Strategic Priorities*
- Transparent screening out of non-aligned programmes/projects
- Support for alternative water & energy development/management options.

#### **Commercial Banks and other private sector Financial Institutions (FIs)**

- Endorsement of the findings of the WCD.
- Interpretation of *WCD Policy Framework* into FIs' lending/investment guidelines
- Transparent implementation of the above guidelines and screening out of non-aligned programmes/projects

- Channelling of investment towards programmes/projects following improved standards:-
  - advice on options for funding water & energy strategies;
  - provision of funding for developing alternative water & energy options;
  - selection of clients implementing improved water & energy programmes and projects.

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