

Equator Principles and Nigeria's Financial Industry

The emergence of Equator Principles

Compliance with the Equator Principles 'EPs' is increasingly becoming a key consideration in projects requiring funding from the World Bank (and its subsidiaries) and other financial institutions. The Equator Principles 'EPs' were developed by 10 private international lending institutions (under the auspices of the World Bank Group) voluntarily in 2003 and later revised in July 2006.

The EPs evolved to address the environmental and social impact that large infrastructure projects could have on local communities. The EPs have to date been adopted voluntarily by 77 financial institutions known as Equator Principles financial institutions 'EPFI's (the latest being the adoption of the Principles by the Mauritius Commercial Bank Ltd. on the 15th of May 2012) and apply to all new project financings internationally with total project capital costs of US\$10 million or more, and across all industry sectors. The use of the word 'Equator' to qualify the Principles confirms its global application in project financing.

The EPs are a composite of voluntary social and environmental guidelines, that provide a credit risk management standard, and require the conduct of a minimum due diligence for assessing and managing environmental and social risks in project finance transactions. The EPs are directed primarily to private, commercial lending in developing countries and emerging economies where borrowers depend majorly on external project finance than is the case for investments in Organisation for Economic Cooperation and Development 'OECD' countries.

Prior to the development of the EPs, financial institutions were less concerned about the impact of project financing on social and environmental sustainability. However, the financial industry has had a considerable paradigm shift in the way it addresses the environmental and social impacts of projects it finances currently. Increasingly, the trend is to assess the costs and benefits of projects as well as ensure that projects are environmentally sound and socially responsible. As such, environmental and social considerations have moved from the side-line to the centre stage in Project Finance.

How are the Equator Principles applied?

The EPs are based on the International Finance Corporation 'IFC' Performance Standards on social and environment sustainability and on the World Bank Group Environmental, Health, and Safety Guidelines. The EPs incorporate these standards and guidelines and provide steps that 'EPFI's are to comply with in providing finance for projects.

Adoption of the EPs require a categorisation of proposed projects into high, medium and low risk classification, depending on the type, location, sensitivity, and its potential environmental and social impacts. Also, the EPs require the provision of mechanisms for addressing grievances of the project host community; independent review of a proposed project; compliance monitoring during the period of the loan; and imposes reporting obligations by independent social or environmental monitors, as well as reporting by each EPFI, about their EPs implementation processes and experiences annually at the minimum. In the case of high (and where appropriate medium) risk projects, borrower covenants ensuring compliance with EPs are incorporated into the finance documentation.

In practical terms, the EPs are very flexible and allow EPFIs to adapt to the different situations presented by projects. An endorsing entity of the EPs can establish internal policies and processes consistent with the EPs. Furthermore, the EPs do not create any rights or liability to any person, public or private. While a borrower must comply with the environmental covenants that lenders include in the loan agreement, lenders are not contractually obliged to comply with the EPs or to enforce them against their borrowers.

A downside of the EPs is that it makes no provisions for any sanctions to EPFIs that do not meet the minimum required compliance threshold. Also EPFI's are not allowed to disclose project names and categorisations in their reports, thus hampering transparency. However, efforts are being made to improve on the EPs and clarify vague and confusing aspects.

Effect and trends in the adoption of the Equator Principles in Nigeria

Nigeria is not left out of the countries with financial institutions that have adopted the EPs. However, only 3 EPFIs- Access Bank Plc, Aterios Capital, and Ecobank Transnational Incorporated (a transnational bank with operations in Nigeria) have adopted the EPs in Nigeria. This suggests that the EPs have not been well received by the financial community in Nigeria, and perhaps that the financial sector has not realised the need to balance the drive to maximise the returns on project financing with the demands of social and environmental sustainability.

The level of awareness of the existence of the EPs is still very low in Nigeria and it may not be surprising to find that only a few organisations needing to access funds for projects know about the EPs, and may experience difficulties when requiring funding from EPFIs. Banks too may find it difficult to access foreign credit lines and may not be able to participate in syndicated loans with EPFIs.

The effectiveness of the EPs has hardly been tested in projects requiring finance in Nigeria. Nigeria suffers a lot environmentally in the exploitation of her resources. Investors in the oil and gas sector for example have had little or no regard for the effect of their operations on the environment. An application of the EPs in providing funding to investors in the sector may help greatly to improve the environmental condition in the Niger Delta region for example, and in Nigeria at large.

In some project host countries, NGO pressure and state legislations have encouraged the adoption of Principles. These may be effective ways of increasing adoption of the EPs by financial institutions in Nigeria.

Conclusion

The EPs are an exemplary model for responsible banking and provide an excellent benchmark for assessing corporate social responsibility by financial institutions. Financial institutions in Nigeria must be prepared to accept the price of higher project screening and investigation costs, rejection of financially rewarding projects, and increased exposure to environmental monitoring, in the interest of social and environmental sustainability.

The EPs have greatly impacted environmental law as the EPs combine a performance-based and a process-oriented approach and ultimately ensure socially responsible investments. The EPs are expected to be an effective tool of managing the interaction of businesses and the environment.

Toolbox



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