

# **The World Bank Reboots: Sweeping Investment Lending Reforms in the Works**

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(Updated)

## **Executive Summary**

The World Bank's Investment Lending Reforms (ILR) could significantly shift the way in which the institution operates. In 2010, the World Bank will begin holding worldwide public consultations on its proposed design of investment lending reforms, even though many of the reforms are already being implemented. This paper raises questions about the nature and the implications of the Bank's investment lending reforms as a prelude to this consultation process.

At present, even after decentralization of staff to country offices, the Bank's headquarters in Washington generally calls the shots. In the future, the Bank may have regional hubs (in addition to country offices) that will administer all projects deemed "low risk." (However, currently the European members of the Bank's Board of Executive Directors are resisting this plan.) In the past, the Bank's portfolio consisted primarily of what it calls "ring-fenced" project operations in a particular sector (energy, agriculture, or health). Financing for "ring-fenced" projects is allocated to concrete tasks (e.g., construction of a power plant or hospital) and disbursed over several years. In 2009, such projects comprised about half the Bank's portfolio. The other half was comprised of programs that financed national budgets (i.e., "development policy loans), which disburse immediately upon loan approval. In the future, lending for traditional "ring-fenced" projects will continue to decline as the Bank introduces a "Results-Based Investment Loan" (RBIL).

*Introducing...the RBIL.* While still under design, it is expected that the RBIL will finance on-going or new government expenditure programs for particular sectors. The loans will disburse in tranches after results (outputs/outcomes) are achieved. Bank management intends to employ RBILs in order to scale up local community projects in a particular sector (e.g., education, forestry) on a national or even international scale. As with budget support loans, the RBIL provides a platform for "pooled funds" – that is, funds to which many donors and creditors contribute. As discussed below (Part 4), the day is coming when sovereign wealth funds and, possibly, private corporations will also contribute to these funds, initially, in energy, infrastructure, and real estate sectors.

*Principles of the Paris Declaration.* The "old" World Bank that financed mainly specific projects—as required by the Bank's Articles of Agreement-- is much different than the "new" Bank which will increasingly provide a platform for "pooled funds" for injection into national or sector budgets. In theory, the "new" Bank would operate in accord with some of the principles set forth in the 2005 Paris Declaration and the 2008 Accra Agenda for Action. The Declaration called for all donors and creditors to provide two-thirds of their financing in the form of flexible budget or sector support by 2010.

The intentions of the Paris Declarations sound appealing. However, even though the intention of the Declaration is to increase country ownership, the country-level administration of pooled funds by finance ministries significantly centralizes power and authority over the development process, often to the detriment of local communities and particularly the poor, whose political voice to command resources remains weak in many countries. In some countries the “new” World Bank could undermine, rather than strengthen, fundamental building blocks of democratic development.

*Power Shift Impacts Policy.* The power shift underway at the Bank provides greater voice above all to finance ministries in developing countries. And, many developing country governments are reiterating a decades- old demand, that the Bank attach fewer “strings” to its operations. But the “pooled fund” is not only a mechanism for pooling financial resources, it also pools a myriad of donor and creditor policy conditions in ways that can sometimes cripple real ownership of development investments by the very people and clients the Bank purports to serve—the poor.

*Skewed Vision of Safeguards.* The “strings” to which some governments object also include some basic fiduciary and environmental and social safeguard requirements. The Paris Declaration calls donors and creditors to harmonize their requirements and align their financial resources with the national or sector strategy of the recipient country. Though some borrowing governments may object to such requirements, weakening them would critically undermine the likelihood that loans will support sustainable development and the kind of fiduciary responsibility that taxpayers of donor countries expect to see when they provide financial support for the Bank.

*The Bank and recipient countries emphasize the costs of implementing safeguards rather than the costs of NOT implementing safeguards, e.g., cleaning up environmental disasters or dealing with aggrieved populations. One generally recognizes the value of regulatory safeguards after the “cow has left the barn” – after the oil spill, after the decimation of an indigenous population or after a critical tropical forest is destroyed. Yet those in the Bank who support the application of the full suite of safeguards are sometimes derided as “fundamentalists.”*

Even now, the Bank’s full suite of safeguard policies and its gender policy only apply to half of Bank operations – the “ring-fenced” projects. They do not apply to national budget support. The World Bank has yet to decide which social and environmental safeguards will apply to RBILs, but it is important that the “full suite” of safeguards apply.

When asked about the relative value of safeguard policies, many World Bank staff reply, “If we apply all of these policies, we will never be able to compete with China.” *However, the World Bank is a public institution and its job is not to compete with some of its member countries, but rather to be a trend-setter in responsible lending.*

The World Bank claims its authority to manage pooled funds – including Climate Investment Funds -- based upon its role as, among other things, a standard-setter. However, to make good on such claims, the World Bank’s standards must be “world class.” To be “world class,” the Bank should work with its public and private partners to harmonize social and environmental standards “upward” and ensure that such standards are applied to its entire portfolio. To transfer more responsibility and accountability to borrowing governments for performance and development results is a positive, needed step. But the prerequisite for future Bank lending has to be strengthened fiduciary controls to ensure that significant percentages of its loans are no longer stolen and that basic environmental and social safeguards are better implemented to ensure that investments do not irreversibly destroy critical ecosystems nor harm vulnerable communities.

## The World Bank Reboots: Sweeping Investment Lending Reforms in the Works<sup>1</sup>

In 2010, the World Bank is expected to undertake sweeping reforms of its operations, particularly those pertaining to investment lending (i.e. project lending). These reforms are shifting considerable responsibility for the quality of World Bank-financed operations to recipient countries. This would be a positive development if it were being done properly, but there are many open questions about whether this is the case.

In addition to questions about the nature of the reforms that the Bank is undertaking, there are questions about the process. Major decisions about the reforms have already been made, yet world-wide public consultations about the reforms will not begin for several months.

This paper examines the nature of the reforms as well as the factors driving the reforms.

### 1. Operational Risk Management Framework

The Bank's Investment Lending Reform (ILR) process is expected to consolidate the types of investment loans.<sup>2</sup> In addition, Bank management characterizes many of its project requirements as standardized or "one size fits all." Thus, as of July 2010, management is initiating an approach that, according to its claims, would tailor the requirements for each specific operation depending upon the level and type of risk implicit in the operation. The Bank may utilize third parties to classify operations, but this remains to be seen.

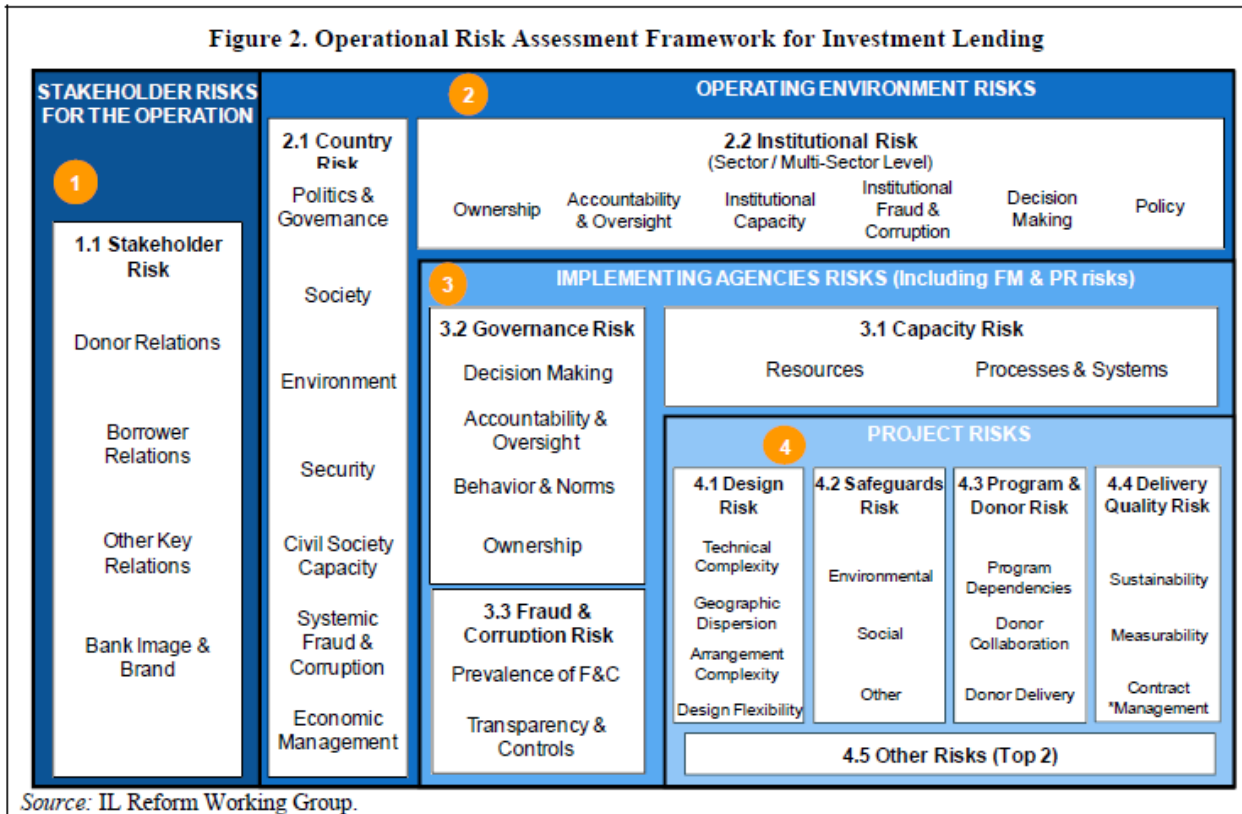
The institution will use a new Operational Risk Assessment Framework for its operations in which are 38 types of risk grouped into four categories. The risks arising from non-compliance with social and environmental safeguard policies<sup>3</sup> represent 2 of the 38 types of risk. (See chart below.)

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<sup>1</sup> The author acknowledges Bruce Rich, attorney, for his helpful comments and suggestions.

<sup>2</sup> The Bank's Investment Lending Reform process will consolidate the current instruments, such as the following: Adaptable program loan (APL); emergency recovery loan (ERL); financial intermediary loan (FIL); learning and innovation loan (LIL); specific investment loan (SIL); sector investment and maintenance loan (SIM); and technical assistance loan (TAL).

<sup>3</sup> There are 10 safeguard policies, comprising the Bank's policy on Environmental Assessment (EA) and policies on: Cultural Property; Disputed Areas; Forestry; Indigenous Peoples; International Waterways; Involuntary Resettlement; Natural Habitats; Pest Management; and Safety of Dams. They are described here: <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/ENVIRONMENT/0,.contentMDK:20124315~menuPK:559747~pagePK:148956~piPK:216618~theSitePK:244381,00.html>



## 2. Decentralization

The World Bank Group designed a plan which would accelerate the decentralization of its offices and create a few regional hubs. According to the plan, the country and regional offices would take complete responsibility for managing the implementation of low-risk projects while higher risk projects would receive more attention from headquarters in Washington, D.C. However, due to the opposition of European shareholders, this plan has not been approved.

## 3. The future of the “ring-fenced” project model

The Bank has decided that the “blueprint” project instrument “was created for a different era...”<sup>4</sup> and observed that this model is “being increasingly criticized inside and outside the Bank because of its inability to adapt to the varied needs of the Bank’s clients and the inefficiency, rigidity, and insularity of the processes and requirements that apply to it.”<sup>5</sup>

Bank management stated that its new investment lending framework would:

<sup>4</sup> World Bank, “Moving Ahead on Investment Lending Reform,” Risk Framework and Implementation Support,” September 3, 2009: [http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/09/09/000333037\\_20090909235811/Rendered/PDF/502850BR0Box3410only10SecM200910442.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/09/09/000333037_20090909235811/Rendered/PDF/502850BR0Box3410only10SecM200910442.pdf)

<sup>5</sup> World Bank, “Investment Lending Reform, Concept Note,” January 26, 2009.

*“Replace the rigid “ring-fenced” project model with a flexible menu of design and funds flow options to better meet development and funding needs of IDA’s varied clients.”<sup>6</sup>*

Upon further questioning, Bank officials claim that they will not totally abandon the institution’s putatively antiquated project model, but rather reorient investment lending to focus in the future much more on a new, “flexible” instrument, the Results-Based Investment Loan (RBIL).

#### 4. The expansion of “flexible” loan instruments

**a. The Results-Based Investment Loan (RBIL).** In the next few months, the World Bank’s Board of Executive Directors is scheduled to consider a “concept paper” on investment lending reform and the RBIL. To date, the institution has not publically disclosed much information about the new instrument. From what we can gather, the RBIL will be:

- A “flexible” sector instrument for scaling up operations.
- Often, a platform for “pooled funds.”
- Support for on-going or new government expenditure program.

In addition, the RBIL will:

- Disburse in tranches after results (outputs/outcomes) are achieved.
- Focus on systems rather than individual transactions.

*Scaling up assistance.* The RBIL will permit a community-based project in a particular sector (health, forestry, agriculture, industry) to be scaled up nation-wide or, eventually, internationally. As the World Bank and its partners implement similar RBIL designs in a specific sector on an international scale, it could undertake cross-country comparisons and benchmarking of performance.

*Decision-making processes.* Given the scale of many RBILs, these instruments will have far more extensive impacts (for better or for worse) than many “ring-fenced” projects. Therefore, more will be at stake when a RBIL succeeds or fails. To succeed, history shows that operations must be crafted by affected communities.

Bank lending has been criticized in some sectors and cases as taking a “one size fits all” approach without sufficient input by local communities. The use of RBILs for even more ambitious replication of project models may pose still greater risks for development effectiveness, since a growing development literature suggests that successful investments tend to be locally-designed to suit specific local conditions.

Yet, finance ministries generally manage pooled funds -- often with little regard for the needs of line ministries or parliaments, where they exist. While the design of RBILs will, undoubtedly, entail a consultative process, such processes cannot replace the functioning of representative government at national and local levels.

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<sup>6</sup> Ibid.

*Who Plays in the “Pool.”* Frequently, the RBIL will be a platform for “pooled” resources. As the term implies, multiple donors and creditors contribute to a platform of “pooled” or “basket” aid which is injected into a national or sector budget when the recipient government has met certain conditions. Already, a significant number of the Bank’s operations are platforms for pooled aid (e.g., budget support operations and sector-wide approaches (SWAps)).

Members of the Group of 20 (G-20) have encouraged the World Bank to “develop with institutional investors a privately financed ‘Fund of Funds’ for SWFs [Sovereign Wealth Funds] and others, facilitating investment in infrastructure in LICs [low-income countries] and other developing countries.”<sup>7</sup>

Bank President Zoellick emphasized the potential for such a “Fund of Funds,” stating, *Today, sovereign wealth funds hold an estimated \$3 trillion in assets. If the World Bank Group can help create the platforms and benchmarks, the investment of even one percent of their assets would draw \$30 billion to African growth, development, and opportunity.*”<sup>8</sup>

We need to learn much more about the RBIL: How will staff and country authorities manage the risks associated with the large-scale operations implied by the RBIL? To what extent will the RBIL require country leadership through extensive civil society and parliamentary participation? What role could SWF and private finance play? Will grants also finance these operations in low-income countries?

**b. The Development Policy Loan.** The RBIL instrument will join another “flexible” project instrument – namely, the Development Policy Loan (DPL), which, when used in a low-income country, is called a “Poverty Reduction Support Credit” (PRSC).<sup>9</sup> According to the Bank, “Development policy operations provide untied, direct budget support to governments for policy and institutional reforms aimed at achieving a set of specific development results.” DPLs are disbursed as their progenitors – Structural Adjustment Programs (SAPs) – were, namely, into national treasuries.

## 5. Flexible Assistance is the Modality for the Future

The Bank’s expansion of so-called “flexible” lending responds to the call for such lending by the 2005 [Paris Declaration on Aid Effectiveness](#) and the 2008 Accra Agenda for Action. The Paris Declaration, which represents a consensus among the international community about how to make aid more effective, garnered 100 signatories—from donor and developing-country governments, multilateral donor agencies, regional development banks and international agencies. The consensus calls for sweeping changes in the way that donor governments and creditors do business.

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<sup>7</sup> HM Government, “Supporting Global Growth” -- “A preliminary report on the responsiveness and adaptability of the IFIs,” UK, September 2009, p. 14.

<sup>8</sup> Zoellick statement of April 2, 2008:

<http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:21711325~pagePK:64257043~piPK:437376~theSitePK:4607,00.html>. FDI-Net (November 2008) identifies the preferred sectors for SWFs – namely, infrastructure, real estate and energy.

<sup>9</sup> The Bank describes the distinction between types of loans and the reform of investment loans here:

<http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/0,,contentMDK:20120732~menuPK:268725~pagePK:41367~piPK:51533~theSitePK:40941,00.html>

As it is, recipient governments are called upon to manage hundreds or thousands of individual projects financed by dozens of donors and creditors – each with its own reporting and procurement requirements.

The Paris Declaration supports a process wherein developing-country governments formulate and implement their own national development plans according to their own national priorities. Then, donors and creditors were tasked with 1) harmonizing their requirements relating to financial management, procurement, reporting, and so on; and 2) aligning their aid with the priorities of national governments.

The Declaration viewed “flexible” and “pooled” aid arrangements as ideal mechanisms for harmonization and alignment processes. In the future, the World Bank sees an even bigger role for itself as a platform for pooled aid:

*New bilateral donors with significant resources, such as China, India and Brazil, are now active in their support of infrastructure development in Africa. Sovereign wealth funds and foundations are expanding their outreach and impact...The Bank's role as a partner for other multilateral and bilateral donors has grown to respond to requests for using the Bank's work as a platform for pooled resources, taking advantage of the Bank's technical design, fiduciary assessments and implementation support for projects and programs.<sup>10</sup> [Emphasis added.]*

The Declaration committed donors and creditors to providing two-thirds of all their aid via flexible, program-based approaches – such as the Development Policy Loan and the Results-Based Investment Loan – by the end of 2010. In 2009, half of the IBRD's disbursements and a quarter of IDA's were in the form of DPLs. The launch of the RBIL is likely to take the Bank beyond the target.

The harmonization and alignment processes are intended to improve “ownership” by a recipient government of its development future, but they often fall short.<sup>11</sup> For instance:

- The national and sector plans of recipient governments are often designed in order to obtain external assistance. For this reason, such plans, even when they are developed through consultative processes, often lack “buy-in” by parliaments or civil society.
- The World Bank and the Working Groups on Aid Effectiveness set up by the Paris Declaration rate the quality of national plans and strategies. This undermines national ownership, particularly since the definition of “quality” is in the “eye” of the beholder.
- The IMF rather than the recipient government generally establishes the size of the resource envelope;
- Whereas “ring-fenced” projects have been administered by “line” agencies of recipient governments, “pooled” aid is administered by finance ministries which often lack the capacity to address sector-specific concerns—let alone the needs of local communities and the poor.
- By their own admission, donors and creditors do not have a good track record of aligning their aid successfully with borrowing governments’ priorities;

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<sup>10</sup> World Bank, Investment Lending Reform Concept Note, January 26, 2009, pp. 2-3.

<sup>11</sup> “Aid Effectiveness After Accra: How to Reform the Paris Agenda,” ODI, July 2008: <http://www.odi.org.uk/resources/download/1885.pdf>

- Alignment is hindered by the large numbers of policy conditions attached to the “flexible” assistance. Some budget support operations have hundreds of conditions.

## 6. World Bank Operational Policies

The World Bank’s Operational Policies are mechanisms for ensuring that the Bank’s Articles of Agreement are fulfilled and that resources are used for their intended purpose. Indeed, the Bank’s Articles of Agreement also require that the Bank lend for “specific projects” “except in special circumstances.” (Article III, Section 4 [vii]) This provision was insisted upon by the framers of the Bank’s charter at Bretton Woods in 1944 because of the experience of private international bank lending in the 1920s to sovereign governments for what we would characterize today as general budget support.<sup>12</sup>

A 2009 review by the Bank’s Independent Evaluation Group (IEG) found that “there appear to be a significant number of Operational Policies... – some 50% – which were not directly linked by Management to any key controls or business processes.”<sup>13</sup> The evaluators’ singled out the project appraisal and supervision policies as examples of extreme non-compliance due to the lack of linkage between the policies and internal controls.

Importantly, many cases that come before the World Bank’s Inspection Panel are based on the allegation that the World Bank has violated its policy governing the process of project appraisal. It is not surprising that, witnessing the downstream operational consequences of non-compliance, stakeholders bring such cases before the Panel with some frequency.

The Bank’s management may respond to its evaluators by downgrading the status of some thirty policies, including those governing appraisal and supervision. Specifically, management has announced its intention to: “consolidate and rationalize the policies and procedures governing investment lending by creating a single principles-based ‘umbrella’ policy for investment lending that would govern projects from preparation through completion.”<sup>14</sup>

However, this raises many questions: how will the principles differ from the Bank’s Operational Policies? Since there will be one umbrella policy for investment lending, will some of the Operational Policies – particularly the social and environmental safeguards -- lose their importance or become non-binding? Would the existence of a single umbrella policy affect the rights and abilities of stakeholders to bring a claim to the Inspection Panel?

## 7. Country Systems

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<sup>12</sup> Massive sovereign defaults by national governments in the 1930s showed that this was an unwise lending pattern. The delegates at Bretton Woods hoped that -- if Bank lending was mainly limited to specific investments in economically productive projects -- this would lessen the long-term risk of misuse of funds by borrowing governments and of sovereign default.

<sup>13</sup> IEG, “IDA Internal Controls, Volume V, p. 18.

<sup>14</sup> *Ibid.*, Volume I, p. 27.

The Paris Declaration calls for donors and creditors to work with recipient governments to improve their financial management, procurement and environmental and social safeguard systems. These systems – which encompass a government’s policies, procedures, implementation, and enforcement efforts -- are called “country systems.” As a follow-up to the Declaration, the 2008 Accra Agenda for Action (AAA) calls for donors “to use country systems as the first option for aid programs in support of activities managed by the public sector.”

When “country systems” are functional and credible, the Paris Declaration calls for donors and creditors to: 1) channel assistance through the governments’ financial management and procurement systems and 2) rely on the environmental and social laws and regulations of the recipient government. Over some years, the World Bank has been shifting primary responsibility for implementation and compliance with fiduciary and safeguard policies from itself to recipient countries on a “pilot” basis. The Bank is having very limited success in this process. For instance, the numbers of projects cancelled due to violations of the Bank’s environmental and social policies has climbed in recent years (e.g., the Asian oil palm debacle and the cancellation of the Bertin cattle ranching project in Brazil’s Amazon).

Ironically, the Bank’s Independent Evaluation Group (IEG)<sup>15</sup> has found evidence of violations of the Bank’s charter in the area of fraud and corruption<sup>16</sup> (due to faulty financial management and procurement controls) and several other “significant deficiencies.” Therefore, the process of strengthening country systems will require that the Bank first strengthen its own internal systems.

Gradually, recipient governments are supposed to take responsibility for both *up-grading* their country systems to be equivalent to World Bank fiduciary and safeguard policies and *enforcing compliance* with its own systems.

The Bank has four critical roles in this process.

1. It must attest to whether a country system is equivalent to its own policies.
2. If a system is not equivalent, the Bank designates the “gap-filling measures” (which may take many months if not years) that a government must take in order to bring the system into line with its policies.
3. The Bank (or private or non-governmental actors) must provide “implementation support” to assist the government with the gap-filling measures.
4. After these measures have been implemented by a government, the Bank must attest to whether these measures are “acceptable” insofar as they bring the country systems up to the required standards. However, the Bank routinely initiates loans (e.g., DPLs) prior to the acceptability determination.

However, even if the World Bank and a recipient government develop “acceptable” country systems, who will take responsibility for compliance and enforcement? And, what will the functions of the Bank’s Inspection Panel be in the future when recipient governments have the primary responsibility for designing, implementing and enforcing the application of fiduciary

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<sup>15</sup> The IEG findings are set forth in 5-volumes entitled, “Review of IDA Internal Controls”:  
<http://web.worldbank.org/external/default/main?contentMDK=22142204&theSitePK=1324361&piPK=64252979&pagePK=64253958>

<sup>16</sup> Alexander, N., Bruce, R., Edwards, B., “Evaluation of the Bank Finds Evidence of Failure to Control Corruption,” <http://www.boell.org/web/index-545.html>.

and safeguard policies? Will complainants affected by non-compliance be able to bring cases to the Inspection Panel only on the claim that the Bank wrongly issued equivalency and acceptability determinations? How might this shift affect World Bank operations?

## 8. The Future of Standards (e.g., Environmental and Social Safeguards)

As mentioned above, the World Bank has ten environmental and social safeguard policies relating to: Environmental Assessment (EA) and policies on: Cultural Property; Disputed Areas; Forestry; Indigenous Peoples; International Waterways; Involuntary Resettlement; Natural Habitats; Pest Management; and Safety of Dams. (See link to full text of policies in footnote 2.)

Developed over the course of two decades, these policies are intended to ensure that projects “do no harm,” particularly to vulnerable populations (e.g., indigenous peoples) and the environment.

At present, this full suite of safeguards as well as the Bank’s gender policy only apply to “ring-fenced” project lending. Since resources for this type of lending will be shifted to Results-Based Investment Lending, *it would appear that the full suite of safeguards will be applied to a shrinking proportion of World Bank-financed operations.*

According to an estimate by the Bank Information Center, the full suite of safeguards applies to only 44% of the World Bank Group’s operations. One reason for this is that about half of the World Bank’s operations are in the form of national budget support, or DPLs. The full suite of policies does not apply to this form of lending.<sup>17</sup>

**The critical question is: Will the safeguard policies as well as the Gender Policy apply to the RBIL operations? The Bank management answers “yes,” however, there are numerous indications that only a watered down version of safeguards will be used.**

## 9. World Bank Supervision and Compliance Activities

The World Bank’s management characterizes an emphasis on supervision and compliance as “out of sync” with the new development paradigm. Management reports that its reform:

“aims to change the philosophy of the Bank’s approach to post-[Board] approval project activity, with a shift from an emphasis on supervision and compliance to one of implementation support...”<sup>18</sup> (Emphasis added.)

And that,

“At a time when the development community is focused on results, accountability, and partnership, current supervision efforts place most of the emphasis on inputs, process,

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<sup>17</sup> Also, the International Finance Corporation’s version of safeguards (i.e., the Performance Standards) do not apply to lending to financial intermediaries. Such lending comprises nearly half of the IFC’s portfolio.

<sup>18</sup> World Bank, “New World, New World Bank Group: The Internal Reform Agenda,” February 2, 2010, p. 7.

and oversight of compliance... What is needed is a culture shift—from a culture of *supervision* to a culture of *implementation support*...<sup>19</sup> (Emphasis added.)

For Bank staff, supervision procedures are perceived as too complex, unclear, and burdensome.

Bank management claims that the shift to “implementation support” will facilitate improved development results. However, *increased* supervision and compliance efforts are critical to achieving results. For instance, if a country were unable or unwilling to comply with safeguard policies, would the Bank step in?

Monitoring and evaluation (M&E) are a critical aspect of supervision, since there is a significant and positive association between these processes and project outcomes. However, in reviewing projects that closed in fiscal 2007 and 2008, IEG found that only 37% of projects exiting the portfolio received ratings of high or substantial M&E systems, while the remaining 63% were rated modest or negligible.<sup>20</sup> Indeed, if one looks at IEG evaluations of various types of World Bank work (e.g., environment, gender, health and education), each one says that results and outcome are impossible to assess because monitoring and evaluation or results frameworks are missing.

## 10. Conclusion

The Bank is undertaking investment lending reforms for several reasons. First, the global financial crisis empowered the developing countries members of the World Bank and the G-20 to demand a larger role in World Bank decision-making relating to the institution’s lending operations. In particular, the Bank’s borrowing countries demanded that there be fewer “strings” attached.

“Strings” – in this case – refer to a host of fiduciary and environmental and social safeguard requirements as well as economic policy conditions. *However, the Bank and recipient countries emphasize the costs of implementing safeguards rather than the costs of NOT implementing safeguards, e.g., cleaning up environmental disasters or compensating aggrieved populations and dealing with political unrest resulting from environmental disruption and impoverishment of vulnerable communities.* The scale of the political and economic risk of long term negligence of basic social and environmental safeguards can be illustrated by the case of India where, in the majority of states, Maoist-Naxalite insurgencies are spreading where indigenous and tribal people in forest areas have been displaced by large investments in extractive industries and industrial infrastructure.

Second, there is evidence that World Bank Group management views itself as competing with China and other major emerging market countries in making development loans. The corollary of this assumption is that Bank management views the Bank’s up-front costs for fiduciary and (social and environmental) safeguard policies as a major reason that the

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<sup>19</sup> World Bank, “Moving Ahead on Investment Lending Reform,” Risk Framework and Implementation Support,” September 3, 2009: [http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/09/09/000333037\\_20090909235811/Rendered/PDF/502850BR0Box3410only10SecM200910442.pdf](http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2009/09/09/000333037_20090909235811/Rendered/PDF/502850BR0Box3410only10SecM200910442.pdf).

<sup>20</sup> IEG, “Annual Report on Development Effectiveness: Achieving Sustainable Development,” World Bank, 2009, p. 27.

institution is losing business to China. When asked about the relative value of safeguard policies, some World Bank staff reply, “If we apply all of these policies, we will never be able to compete with China.” Some staff who defend the policies are derided as “fundamentalists.” *However, the World Bank is a public institution and its job is not to compete with some of its member countries, but rather to be a trend-setter in responsible lending.*

Third, the World Bank Group continues to finance coal-fired plants (South Africa’s Medupi coal, India’s Tata coal, and Botswana’s Mongbwalu coal) and, in general, seems unaware of the seriousness of global warming trends. Deforestation, including Bank-financed operations, has reduced the sequestration of greenhouse gases by forests, while ocean sequestration is also diminishing. In addition, patterns relating to the decline of biodiversity and concentration of land ownership do not bode well in light of rapid rate of population growth, given dependence of the poor on subsistence and small-scale farming. This is only one of the many ways in which population growth intensifies dependence on the environment. Finally, worldwide, inequality is on the rise and, as financial sector losses are being borne by societies (rather than the financial institutions, themselves), impoverishment is deepening. These trends, among others, call for strong environmental and social standards to maintain and improve the ecosystem and the societies that rely upon them.

As noted above, the World Bank claims its authority to manage pooled funds – including Climate Investment Funds – is based upon its role as, among other things, a standard-setter. However, to make good on such claims, the World Bank’s standards must be “world class.”

To be “world class,” the Bank should:

- work with its public and private partners to harmonize “upward” social, environmental, and gender safeguard policies and ensure that such standards are applied to its entire portfolio;
- strengthen its fiduciary controls for fraud and corruption as the Bank’s Independent Evaluation Group strongly recommends; and
- strengthen supervision and compliance services as it shifts responsibility for fiduciary and safeguard policies to recipient countries. This is particularly important, since the Bank’s evaluators point out, many countries have “weak to non-existent” country systems.

**Excerpt from  
World Bank Operational Policy (OP) 8.60 –  
Development Policy Lending  
2004**

**EXCERPT REGARDING WORLD BANK OBLIGATIONS RELATING TO SOCIAL  
AND ENVIRONMENTAL ASPECTS OF DEVELOPMENT POLICY LENDING (OR  
NATIONAL BUDGET SUPPORT)**

10. *Poverty and Social Impacts.* The Bank determines whether specific country policies supported by the operation are likely to have significant poverty and social consequences, especially on poor people and vulnerable groups. For country policies with likely significant effects, the Bank summarizes in the Program Document relevant analytic knowledge of these effects and of the borrower's systems for reducing adverse effects and enhancing positive effects associated with the specific policies being supported. If there are significant gaps in the analysis or shortcomings in the borrower's systems, the Bank describes in the Program Document how such gaps or shortcomings would be addressed before or during program implementation, as appropriate.

11. *Environmental, Forests, and other Natural Resource Aspects.* The Bank determines whether specific country policies supported by the operation are likely to cause significant effects on the country's environment, forests, and other natural resources. For country policies with likely significant effects, the Bank assesses in the Program Document the borrower's systems for reducing such adverse effects and enhancing positive effects, drawing on relevant country-level or sectoral environmental analysis. If there are significant gaps in the analysis or shortcomings in the borrower's systems, the Bank describes in the Program Document how such gaps or shortcomings would be addressed before or during program implementation, as appropriate.

For the full text of this OP, see

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