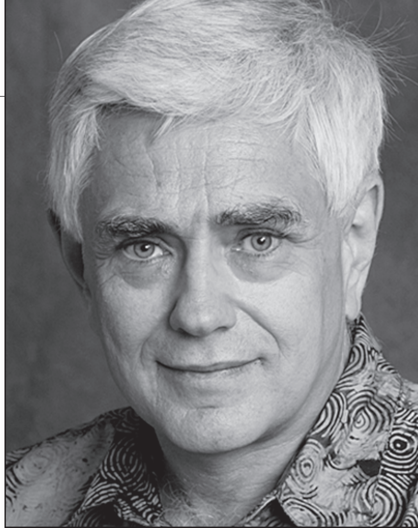

By Bruce Rich

# Climate Finance and Bank Reform

The commitment by industrialized nations of new funds for climate change mitigation and adaptation in developing nations is already a reality. The World Bank, in partnership with other multilateral development banks, has become the main financial administrator of these "climate investment funds": $4.3 billion for the Clean Technology Fund, to support low carbon energy investments in developing nations, and about $1.88 billion in the Strategic Climate Fund. Donor countries also have entrusted to the bank over the past decade some $2.5 billion in capital for 12 different carbon funds. This has helped to jump start trading of emission rights and carbon offsets under the Kyoto Protocol.

Before still more money is committed, governments and donors would do well to consider major institutional problems that have come to light in the management by the bank of its environmental lending and carbon finance.

The environmental integrity of World Bank carbon fund projects is undermined by critical problems in calculating whether they finance real overall greenhouse gas reductions. A growing literature has documented the lack of real additionality in many projects; i.e., whether emission credits bought by industrialized countries in developing nations through projects really contributed to net additional reductions in GHG emissions. The problem is, as the U.S. Government Accountability Office concluded in a report in 2008, "it is nearly impossible to ensure that projects are additional." The bank acknowledged this huge methodological hole in its promotion of carbon trading in a recent review of its carbon funds.

Every year the World Bank's internal operations evaluation unit, the Independent Evaluation Group, publishes an Annual Review of Development Effectiveness on the bank's operations. Last year the IEG focused on the bank's record in supporting environmental sustainability. The findings are disturbing. The 2009 review noted that in 2001 the bank launched a new environmental strategy, the goal of which was to "mainstream" environmental concerns in major lending sectors affecting the environment. Perversely, starting in 2002 the review found that "mainstreaming has decreased in some sectors such as agriculture, energy and transport." For example, as the bank has gathered in billions in new additional climate funds from donors over the past two years it has lent over $4 billion for giant new coal plants.

The report cites several major constraints on the bank's relatively weak environmental performance: first there is low demand from the borrowing countries, compounded by "corruption surrounding resource rents." The U.S. Senate Foreign Relations Committee has found that the bank itself needs to do much more to fight corruption, particularly in its own lending concerning natural resources and large energy infrastructure projects.

*Given this record it would be negligent to not demand overdue reforms*

Borrowing countries often have weak capacity to manage environmental projects, but more alarming, within the bank "internal knowledge gaps, inadequate technical and operational skills to integrate environment concerns into investment and policy reform projects, and poor dissemination of evidence on effectiveness within the bank impede effectiveness and limit growth [of environmental lending]." The bank only bothers to track results for one quarter of the environmental initiatives it finances; no analytical effort is made to examine the success or failure of the three quarters of environmental lending that is embedded in larger projects or programs. "Finally, internal staff and management incentives favor large projects, such as infrastructure or power, which disadvantages the typically smaller environmental projects," according to the IEG report.

Another 2009 IEG report found that the pressure to push money out the door for large projects has fostered a systematic neglect by the bank of investment opportunities in energy efficiency, despite the fact that "numerous analyses show that much of the demand for energy services over the next 30 years can be more cheaply provided through increased efficiency than through increased generation."

Most egregious of all, these findings of perverse institutional incentives in the bank are decades old. The "pressure to lend" and "loan approval" culture were denounced in an internal 1992 bank review of the performance of its lending portfolio and repeated in numerous internal and external studies over the past two decades. In 1986 the bank's energy department published a study examining the huge opportunities that already existed for investments in energy efficiency in China and India, a report whose recommendations the bank largely ignored.

Given this record, it would be the grossest negligence of governments to not demand long overdue institutional reforms in the World Bank as they continue to discuss mechanisms for managing still larger sums of climate finance over the coming years.

**Bruce Rich** is an attorney and author who has served as senior counsel for major environmental organizations. His email is brucemrich@gmail.com.



Copyright © 2010, Environmental Law Institute®, Washington, D.C. www.eli.org.
Reprinted by permission from The Environmental Forum®, Sept./Oct. 2010