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An Environmental Policy Framework for the European Investment Bank for Non-EU Lending: The Need for Clear, International Standards-based Approach

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Background paper

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An Environmental Policy Framework for the European Investment Bank for Non-EU Lending: The Need for Clear, International Standards-based Approach

By Steve Herz*

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1. Introduction

The European Investment Bank's (EIB) organizational mission is to finance projects that advance the European Union's priority policy objectives, including environmental protection and improvement. Towards this end, the EIB proactively seeks to finance projects that directly help to protect and improve the environment. When it finances other investments, it "supports action that minimizes any adverse environmental impacts."

For projects located outside of the EU, however, the EIB does not have a clear policy framework for achieving these objectives. While it endeavors to apply "the highest environmental standards – those established by the European Union,"¹ it has actually adopted a flexible, guidance-based approach that (1) is devoid of explicit performance levels or auditable criteria for compliance; (2) and lacks a clear management system to ensure consistent implementation. In absence of clear performance standards and procedures for implementing them, it is difficult to see how EIB can implement an effective citizen-driven compliance mechanism.

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¹ European Investment Bank, *Environmental Statement* 1 (2004).

This paper makes the case for a different approach that emphasizes explicit requirements based on international law standards, and a clear, consistent and effective framework for managing environmental issues as they arise throughout the project cycle. Specifically, it should:

- continue to emphasize EU laws and directives as the most important source of substantive and procedural standards for its approach to environmental governance outside of the EU.
- be far more explicit about when EU standards will apply—or, more precisely, under what circumstances the EIB will allow projects to derogate from those standards;
- be more explicit about how it will apply other international standards;
- develop specific policies to address issues of particular environmental concern;
- further strengthen its policies on transparency and public participation;
- strengthen and publicize its management systems for addressing environmental issues.

2. EIB's (Missing) Environmental Policy Framework for Lending Outside of the EU

The policy regime that the EIB has put in place to achieve its environmental policy objectives is set out in the 2004 Environmental Statement (Statement). For projects located in the EU—the vast majority of the projects financed by the Bank—the EIB's approach is reasonably straightforward. First and foremost, the EIB requires projects to comply with EU environmental policies and standards, including the Directive on Environmental Impact Assessment. This requirement, of course, is essentially a matter of legal compliance, since these projects must adhere to EU policies and standards regardless of whether EIB provides financing.

In addition, EIB also suggests that it may require these projects to meet some higher standards. The Environmental Statement explains that in addition to meeting EU standards, all projects must (a) apply “best available techniques,” as appropriate; (b) apply good environmental management practices during project implementation and operation; and (c) adhere to international good environmental practice. It is not clear, however, whether these provisions have any meaningful substantive content. For one thing, they are too vague to be applied consistently. For another, the EIB may not actually intend them to require more stringent management of environmental issues than would otherwise be required by EU law—after all, the EIB already considers EU requirements to be the “highest environmental standards.”²

² Indeed, there is good reason to believe that these provisions are not intended to “raise the bar” above EU standards. According to the Environmental Statement, “[t]he EIB applies the highest environmental standards – those established by the European Union.” That being the case, it is difficult to see how “good environmental management practices” or “international good environmental practice” could add much to this framework.

At a minimum, then, EIB financed-projects in EU countries must meet the requirements of EU law, and *may* be required to meet other, more stringent but ill-defined, requirements. But for projects located outside of the EU, the minimum standards for EIB financing are more difficult to discern. The Statement refers to several different policy regimes, but is often ambiguous about which are mandatory and which are not, and is entirely silent about how the EIB will determine whether non-mandatory policies should be applied in the context of any given project. The Statement makes clear that *every* project, including those located outside of the EU, must:

- (a) conduct an Environmental Impact Assessment (EIA) according to the requirements of the EU directives, if it is likely to have a significant environmental impact, and will not be eligible for financing if it is determined that it is likely to have a significant negative impact and/or be of high risk for the environment.
- (b) comply with the obligations and standards that the host country has committed to meet under any multilateral environmental agreements;
- (c) meet standards that are, at a minimum, equal to “international good practice.”³

Moreover, although as a legal matter EU standards do not apply extraterritorially, the Statement explains that EU standards will be used as “benchmarks.” Nevertheless, it is quite explicit that something less than EU standards will actually be required:

In regions outside the EU and the Candidate Countries, projects must comply with the principles and standards set by EU policies, subject to local conditions and law. Issues taken into account include income per head, institutional capacity and the costs and benefits of alternative standards. In certain circumstances, higher environmental standards may be introduced in stages; in others, a project may be designed in anticipation of future higher standards.⁴

In addition to EU standards, the EIB also “takes into account, as appropriate” other sources of international good practice, including (a) the policies and practices of other international financial institutions; (b) the “UNEP Statement by Financial Institutions on Environment and Sustainable Development;”⁵ (c) recognized international good practice for particular sectors such as the findings and recommendations of the World Commission on Dams; and (d) principles of good environmental management practice such as those enshrined in the EU’s Environmental Management and Audit System (EMAS) and ISO 14000. Finally, by its terms the Statement also appears to commit the EIB to follow the

³ European Investment Bank, *Environmental Statement*, 3 (2004).

⁴ European Investment Bank, *Environmental Statement*, 4 (2004). This approach is bolstered by EIB’s commitment to the European Principles for the Environment, which requires EIB to “comply with the appropriate EU environmental principles, practices and standards...subject to local conditions.” <http://www.eib.org/site/index.asp?designation=epe&childHeaderId=414>

⁵ <http://unepfi.net/fii/english.htm>.

Equator Principles,⁶ but EIB officials have disavowed any intent to adhere to the Equator Principles as a matter of mandatory policy, and EIB is not a “signatory” to the Principles.⁷

Overall, the Statement fails to provide a clear and comprehensive set of performance standards that EIB will require as a condition of financing. Rather, the Statement often reads like a description of the kinds of standards that EIB will consider in the exercise of its own discretion and professional judgment about what constitutes a good environmental project. This level of policy flexibility and discretion is an anomaly among multilateral financial institutions. Each of EIB’s peer institutions has adopted an environmental policy regime that is markedly more concrete in terms of substantive policy commitments. Ironically, then, EIB’s guidance-based approach to environmental issues does not meet its stated policy objectives of achieving international best practice in line with the policies and practices of other multilateral financial institutions. Given the consistent practice of these institutions to more explicitly state their environmental policy commitments, accepted international practice clearly compels the EIB to be far more explicit about its policy regime.

3. The Benefits of A Clear, Mandatory Environmental Policy Framework

In order for EIB to meet international standards of environmental governance for an international financial institution, it must therefore replace its current discretion-based approach with a new environmental framework based on clear, binding, and enforceable minimum standards. This would provide an opportunity for EIB to make its values and standards clear to all stakeholders, including its clients, staff and host communities. Each of these stakeholders would benefit from such a clear framework.

First, clients would know up front what is to be expected of them, and would have strong incentives to improve their practices to meet those expectations. Second, clear standards would provide staff with an important counterweight to the institutional incentives to lend. The experiences of the World Bank and other multilateral financing institutions have shown that when a financial institution has a proposed project and a willing client before it, the institutional incentives to “do the deal” will often undermine sound environmental decision-making. With a deal on the table, there will always be strong incentives to understate risks, overestimate the ability to mitigate them, and to uncritically accept the representations of the client. A commitment to adhere to clear standards that are articulated outside of the context of any given project tends to dissipate such pressures by introducing a countervailing imperative to adhere to stated public policy commitments. Thus, much like Homer’s story of Odysseus binding himself to the mast of his ship to resist the temptations of the Sirens, EIB should precommit itself to clear standards to steel investment staff against the entreaties of valued clients for special dispensations, or the glib assurances of purveyors of problem projects.

⁶ “The EIB’s approach is equivalent to the “Equator Principles” (2003) http://www.equator-principles.com/documents/Equator_Principles.pdf adopted by a number of commercial banks and based on the International Finance Corporation (IFC) guidelines. The Bank subscribes to these principles when operating outside the EU.”

⁷ <http://www.equator-principles.com/>

Third and most importantly, clear, verifiable standards would provide a basis for those who are potentially affected by projects to hold the EIB and its borrowers to account if they fail to uphold their commitments. EU policy and international best practice regarding the environmental governance of development projects increasingly recognizes the importance of meaningful participation of affected communities in project decision-making. (see Section 4(D)(2), below). A clear, mandatory policy regime can help facilitate such community participation by helping to establish appropriate expectations and by clarifying the rights and obligations of all stakeholders up front.

4. Some Considerations in Developing an Environmental Policy Framework

A. Establish Clear Requirements and Limited Exceptions

As a minimum basic requirement, a credible environmental policy framework must be explicit with regard to what the EIB will require as a condition of financing. It should establish clear performance benchmarks and auditable criteria so that it is possible to determine if a project is or is not in compliance with the policy's requirements. Clear exclusion lists and bright-line rules for determining "no go areas" or "no go technologies" are particularly useful in this regard.⁸ Moreover, if the policy is to allow derogations from these standards in certain circumstances, it should (a) include an explicit presumption that the policy will apply absent a compelling reason not to enforce them in a given circumstance; and (b) clearly define the circumstances in which it will allow such a showing to override the baseline requirements of the policy.

B. Incorporate International Standards

The great strength of the Environmental Statement is its recognition that externally-generated, best practice international standards are the appropriate basis of EIB's management of the environmental impacts of projects that it finances. This is a marked and welcome departure from the approach of the World Bank and other international financial institutions, which have often defined their operational policies without reference to accepted international standards.

EIB's approach implicitly recognizes that notwithstanding its public interest mission, it is still at the end of the day a bank, with relatively little capacity or legitimacy to make policy or generate international norms. Accordingly, EIB's references to international hard and soft-law standards pay due regard to its own technical and institutional limitations vis-à-vis other international institutions, commissions, and *ad-hoc* multi-stakeholder bodies. By explicitly deferring to the work of these organizations, EIB (1) leaves global standard-setting to the

⁸ IFC, for example has a clear Exclusion List in its *Environmental and Social Review Procedures* (April 2006). However, IFC's list does not preclude a number of activities that do not meet international standards and best practice. These include, for example, projects in or impacting upon World Heritage Sites, IUCN I-IV areas, critical habitats for species on the IUCN Red list, and recognised Marine Protected Areas; projects involving the use or production of persistent organic pollutants; riverine or shallow submarine tailings disposals for mining wastes; aquaculture that converts coastal mangrove areas; and projects that harm significant coral reef systems.

relevant experts; (2) facilitates consistency across international institutions, and (3) avoids duplicating other international efforts in these areas. In light of the virtues of this approach, EIB should incorporate international standards into any proposals for an environmental policy framework.

Moreover, as an entity of the EU, EIB appropriately emphasizes EU laws and directives as the most important source of substantive and procedural standards for its approach to environmental governance outside of the EU. EIB obviously should retain this emphasis in transforming its current approach into a more concrete policy framework. Indeed, the primary challenge for EIB in moving to a clear standards-based approach to managing environmental issues will be to be far more explicit about when EU standards will apply—or, more precisely, under what circumstances the EIB will allow projects to derogate from those standards.

C. Develop Policies to Address Specific Areas of Environmental Concern.

Like other international financial institutions, EIB appropriately bases its efforts to minimize environmental impacts on an EIA process. But unlike other public and private sector project financiers, it does not augment its EIA process with clear and specific substantive policies that address sectors and issues of particular environmental concern. By comparison, other international financial institutions have adopted policies to address issues such as:

- climate and energy;
- dams;
- biodiversity;
- forests;
- fisheries;
- extractive industries;
- sustainable agriculture; and
- chemicals.

As noted above, the best of these policies (1) establish clear performance benchmarks and bright line rules for eligibility for financing; and (2) adopt substantive standards that meet international norms and best practice. Four examples should illustrate the point. First, HSBC requires any dam that it finances to implement the recommendations of the World Commission on Dams. Second, IFC and the Equator Principle Banks require forestry operations that it finances to:

ensure that all natural forests and plantations over which they have management control are independently certified as meeting performance standards compatible with internationally accepted principles and criteria for sustainable forest management.⁹

⁹ *IFC Performance Standard 6: Biodiversity Conservation and Sustainable Natural Resource Management*, at www.ifc.org; *Equator Principles*, at <http://www.equator-principles.com/>.

Third, IFC and the Equator Principle Banks require clients that manufacture or use hazardous chemicals to (a) “avoid or, when avoidance is not feasible, minimize or control the release of hazardous materials resulting from their production, transportation, handling, storage and use for project activities;” (b) “avoid the manufacture, trade, and use of chemicals and hazardous materials subject to international bans or phase-outs due to their high toxicity to living organisms, environmental persistence, potential for bioaccumulation, or potential for depletion of the ozone layer;” and (c) comply with the FAO’s International Code of Conduct on the Distribution and Use of Pesticides. In each of these cases, the performance expectations are clear, and they are predicated upon internationally accepted standards.¹⁰ Finally, to ensure that it does not capitalize financial intermediaries that in turn finance environmentally risky projects, IFC requires its financial intermediary clients to “establish and maintain a Social and Environmental Management System to ensure that its investments meet IFC’s requirements,” and monitors the client’s performance to ensure compliance.¹¹

EIB should adopt the approach of other IFIs to managing environmentally sensitive projects by adopting clear policies with respect to particularly risky activities and issues of cross-cutting concern that meet international best practice standards.

D. Improve Transparency and Public Participation

1. Transparency

People and communities affected by a project have a basic right to be informed in a timely way about decisions that affect their lives, and to have an opportunity to participate in decision making by making their views known to decision-makers prior to any decision being made.¹² Public access to critical project information is essential for affected people to have a meaningful voice in how projects will be designed and implemented, how project costs and risks will be distributed among affected people, and how negative impacts will be mitigated and managed. Ultimately, access to project information is also a necessary prerequisite to ensure accountability--to hold project sponsors to account for how they conduct themselves, and to hold governments to account for how they respond to that conduct. For these reasons, EIB should publicize comprehensive and timely information about the project and its impacts throughout the design, planning and implementation stages of the project.

Ensuring public access to critical information on the environmental and social dimensions of a project may be in the EIB’s interests for three reasons. First, allowing the public to have access to such information is critical to their ability to meaningfully engage in project decision-making, and therefore for essential for EIB to reap the public benefits of such engagement. Second and relatedly, denying such information is often seen as an

¹⁰ *IFC Performance Standard 3: Pollution Prevention and Abatement*, Equator Principles, at <http://www.equator-principles.com/>.

¹¹ IFC Policy on Social and Environmental Sustainability, at www.ifc.org.

¹² See, e.g., Rio Declaration on Environment and Development, Report of the UN Conference on Environment and Development, A/Conf.151/26 (Vol. I), Annex I, Principle 10 (3-14 June 1992); Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Decision-making, Doc. ECE-CEP-43 (25 June 1998).

affront, or an effort to cover up publicly indefensible practices, and will therefore tend to subvert the effort to cultivate harmonious community relations. Finally, placing such information in the public domain may substantially improve its quality and rigor. Allowing affected individuals the opportunity to independently scrutinize the assumptions and methodologies of the project sponsor, and to test its conclusions against their own (much more intimate and nuanced) understanding of the local conditions, would help the EIB ensure that it receives the best project information possible.

EIB's new Public Disclosure Policy follows international best practice by explicitly adopting a presumption of disclosure with respect to environmental and social information.¹³ This presumption of disclosure should require EIB to adopt a narrow interpretation of what information can be withheld under claims of business confidentiality or professional secrecy. While confidentiality is a legitimate business concern, it should primarily protect material that could be advantageous to competitors, such as trade secrets or certain financial information. Very little information regarding environmental, social, health and safety impacts meets this criterion. But even where it does, the new policy properly requires that claims of business confidentiality or professional secrecy be subjected to a "public interest override." Thus, information that otherwise would be considered confidential must be disclosed if it is in the public interest to do so.

To effectively implement the presumption of disclosure and to meet international transparency standards, EIB should routinely disclose in a timely and culturally appropriate manner:

- Full draft and final environmental and social assessments for all transactions with significant impacts;
- draft and final environmental and social management plans;
- environmental and social covenants in financial documents;
- any compliance reports required from the client regarding commitments made in the EMP.
- amounts and conditions of all material payments by borrowers to host governments and all material revenues received by governments from royalties, taxes, and concessions;¹⁴ and
- foreign investment contracts, including host government agreements, power purchase agreements and any other contracts between the company and the host government.

¹³ Other international best practice standards for the transparency of international financial institutions can be found at Global Transparency Initiative (2006) *Transparency Charter for International Financial Institutions: claiming our right to know* Global Transparency Initiative http://www.ifitransparency.org/doc/charter_en.pdf

¹⁴ Extractive Industries Transparency Initiative, www.eitransparency.org.

2. Public Participation

There is now a broad recognition that development initiatives are more likely to be sustainable and effective if they are based upon affected people's own analyses of the problems they face and the appropriate solutions. Thus, the Brundtland Commission concluded that "securing effective citizen participation in decision-making" is one of the main prerequisites of sustainable development. Similarly, with respect to environmental decision-making, Principle 10 of the Rio Declaration on Environment and Development, adopted by 178 countries, recognized the importance of transparency, participation, and access to mechanisms of redress and accountability in effective environmental decision-making.¹⁵ These conclusions have been confirmed by the World Bank, which has consistently found a high correlation between the extent and quality of public participation and overall project quality.¹⁶

Accordingly, the countries of Europe have endeavored to integrate public participation in environmental decision-making and development assistance. Thus, the signatories of the Aarhus Convention have committed to "guarantee the rights of access to information, public participation in decision-making, and access to justice in environmental matters."¹⁷ And under the Cotonou Agreement, the members of the European Community agreed to include civil society organizations as partners in development assistance to developing countries.¹⁸

EIB policies include rudimentary provisions for public participation, but these fall far short of EU practice and that of other IFIs. The Environmental Statement provides that "[a]ll projects," presumably including those outside of the EU, that have a significant effect on the environment must conduct an EIA in accordance with the requirements of EU Parliament Directive 85/337/EEC, as amended by Directive 97/11/EC. This includes the public consultation provisions. However, the Environmental Statement does not refer to Directive 2003/35/EC of the European Parliament, which substantially expands public participation requirements in accordance with Aarhus Convention.¹⁹

Meanwhile, other IFIs are moving beyond 'consultations' towards more meaningful forms of public participation. For example, in addition to its baseline consultation requirements for Category A projects, the World Bank now requires that extractive industry projects and projects that affect indigenous people, must secure the "broad support" of affected communities through a process of "free, prior, and informed consultation" in order to

¹⁵ United Nations Conference on Environment and Development (UNCED), "Rio Declaration on Environment and Development" paper presented at the United Nations Conference on Environment and Development in Rio de Janeiro, Brazil, June 3-14 (1992).

¹⁶ See, e.g., World Bank "Annual Review of Development Effectiveness." Operations Evaluation Department (OED) (2002); World Bank, "World Bank Civil Society Progress Report 2000/2001," (2001); World Bank, "Assessing Aid: What Works, What Doesn't and Why," (1999); World Bank "Quality at Entry in CY99—QAG Assessment." Quality Assessment Group (QAG) (2000); World Bank, *The World Bank Participation Source Book*. Washington DC (1996).

¹⁷ Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Decision-making, Article 1, Doc. ECE-CEP-43 (25 June 1998).

¹⁸ *Cotonou Agreement*, Article 2.

¹⁹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32003L0035:EN:HTML>

be eligible for Bank financing.²⁰ Moreover, the International Finance Corporation (IFC) extended the application of the broad community support standard to all projects that will have “significant adverse impacts” on affected communities. For projects that affect the lands of indigenous peoples, the IFC replaced the broad community support standard with a requirement that the project sponsor engage in “good faith negotiations” with the affected communities, and demonstrate the “successful outcome” of the negotiation.²¹

Using EU Directives as a benchmark, the EIB should bring its participation policies in line with IFC and other IFIs that have begun to require these more empowering forms of participation. EIB should also much more clearly define the kinds of participation processes and outcomes it will require its clients to undertake as a condition of providing financial support.

E. The Need for a Comprehensive Environmental Management System

Just as important as adopting an appropriate set of policy standards is establishing an effective management system to ensure that they are implemented properly. Without such a system, even the best policies are not worth the chlorine free, FSC-certified paper that they are written on. EIB, however, does not have a comprehensive framework for the management of environmental issues--it does not have clear, publicly-available procedures for project screening and due diligence, project implementation and oversight, transparency and public participation in decision-making, enforcing compliance by its borrowers, or evaluation and organizational learning. By contrast, other international financial institutions have been much clearer in articulating their operational policies, and their management systems for implementing them. For example, the International Finance Corporation recently adopted a *Policy on Social and Environmental Sustainability*²² and revised its *Environmental and Social Review Procedures*²³ to strengthen its procedures and systems for addressing the environmental and social impacts of its operations.

In addition to the procedures of the IFC and other international financial institutions, other elements of an effective management system have been identified in a number of international instruments and multi-stakeholder processes, including the OECD Multinational Enterprise Guidelines, the World Commission on Dams, and the International Standards Organization's ISO 14001, the commonly-used standard for environmental management systems.²⁴ To meet these international standards, a comprehensive E&S management system should include:

²⁰ World Bank Group, *Striking A Better Balance -- The World Bank Group and Extractive Industries: The Final Report of The Extractive Industries Review, World Bank Group Management Response* (Washington DC: World Bank Group, 2004), pp. 7; World Bank, *Operational Policy 4.10: Indigenous Peoples* (July 2005).

²¹ International Finance Corporation, *Performance Standards on Social and Environmental Sustainability*, (April, 2006), pp 30.

²² [http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/pol_SocEnvSustainability2006/\\$FILE/SustainabilityPolicy.pdf](http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/pol_SocEnvSustainability2006/$FILE/SustainabilityPolicy.pdf)

²³ [http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/pol_ESRP2006/\\$FILE/ESRP2006.pdf](http://www.ifc.org/ifcext/enviro.nsf/AttachmentsByTitle/pol_ESRP2006/$FILE/ESRP2006.pdf)

²⁴ OECD Multinational Guidelines on Enterprises, Part IV, at 22 (2000) (Enterprises should “...establish and maintain a system of environmental management appropriate to the enterprise...”).

- A precautionary approach to environmental risks and impacts;
- Clear procedures for environmental and social assessment to identify impacts and risks;
- An environmental and social policy framework that establishes an overall approach and issue- and sector-specific policies;
- Prohibitions on financing particularly risky or harmful activities;
- Clear transparency and participation procedures;
- Effective mechanisms for monitoring and oversight, enforcing compliance, and taking corrective action;
- Effective grievance mechanisms for the public raise compliance issues and to seek accountability and redress;
- Clear procedures for evaluation, organizational learning and improvement; and
- Dedicated staffing, effective training, adequate budgetary support, clear lines of accountability, and an internal incentive structure that rewards environmental excellence.

5. Conclusion

EIB appropriately emphasizes EU laws and directives as the most important source of substantive and procedural standards for its approach to environmental governance outside of the EU. However, its policy framework is too discretionary and opaque to meet the best practice standards established by other international financial institutions. To meet these best practice standards, EIB must adopt explicit performance standards based on international law standards, and a clear, consistent and effective framework for managing environmental issues as they arise throughout the project cycle.

Specifically, it should:

- be far more explicit about when EU standards will apply—or, more precisely, under what circumstances the EIB will allow projects to derogate from those standards;
- be more explicit about how it will apply other international standards;
- develop specific policies to address issues of particular environmental concern;
- further strengthen its policies on transparency and public participation;
- strengthen and publicize its management systems for addressing environmental issues.