

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

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April 21, 2010

In 2009, the World Bank issued some documents describing its plans to roll-out sweeping reforms in investment lending beginning in fiscal 2011 (July 1, 2010). 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, the reforms are unfolding in a surreptitious manner. Despite numerous requests, World Bank officials have refused to meet with civil society groups to discuss the anticipated reforms. They claim that there will be a public consultation but, meanwhile, key decisions about the reforms are being made and, in some cases, implemented.

Many of the reforms are discussed in papers entitled, “New World, New World Bank Group.” While the papers are dated February 2010, to our knowledge, they have not yet been publicly disclosed. The phrase “New World Bank Group” connotes that the reforms underway are quite sweeping.

Why is the World Bank planning to implement sweeping reforms? And, what is the nature of the reforms? This paper addresses these two questions.

Why reform? Reform became necessary for the following 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.

Second, there is evidence that the World Bank Group is competing with China and other emerging market countries and, with the Bank’s up-front costs for fiduciary and (social and environmental) safeguard policies, staff report that the institution is losing business to China.

Third, the 2005 [Paris Declaration on Aid Effectiveness](#), 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. As described below, the 2005 Paris Conference and the 2008 Accra Conference called for sweeping changes in the way that donor governments and creditors do business.

Fourth, the reforms are a response to a 2009 evaluation by the Bank's Independent Evaluation Group (IEG)¹ that found evidence of significant levels of non-compliance by IDA with its Articles of Agreement and Operational Policies in a variety of areas.² This evaluation, mandated by the IDA-14 Agreement, found most serious non-compliance relates to the area of fraud and corruption, however, there were also six groups of "significant deficiencies" relating to project management and oversight, among other things.

Two of the problems highlighted by IEG relate to: 1) the absence of a Risk Management Framework which could identify the levels and types of risks in its operations and 2) non-compliance with many Operational Policies.

Management agreed to establish a Risk Management Framework, overhaul its Operational Policies, and reconsider the nature of the project model.

Several aspects of the investment lending reforms are described below.

1. Risk Management Framework

In the aforementioned evaluation, Bank management expressed its interest in replacing the current "one-size-fits-all" project requirements with a risk-based approach to investment lending that would help tailor the institution's approach to "due diligence" based upon the level and type of risk implicit in each operation.

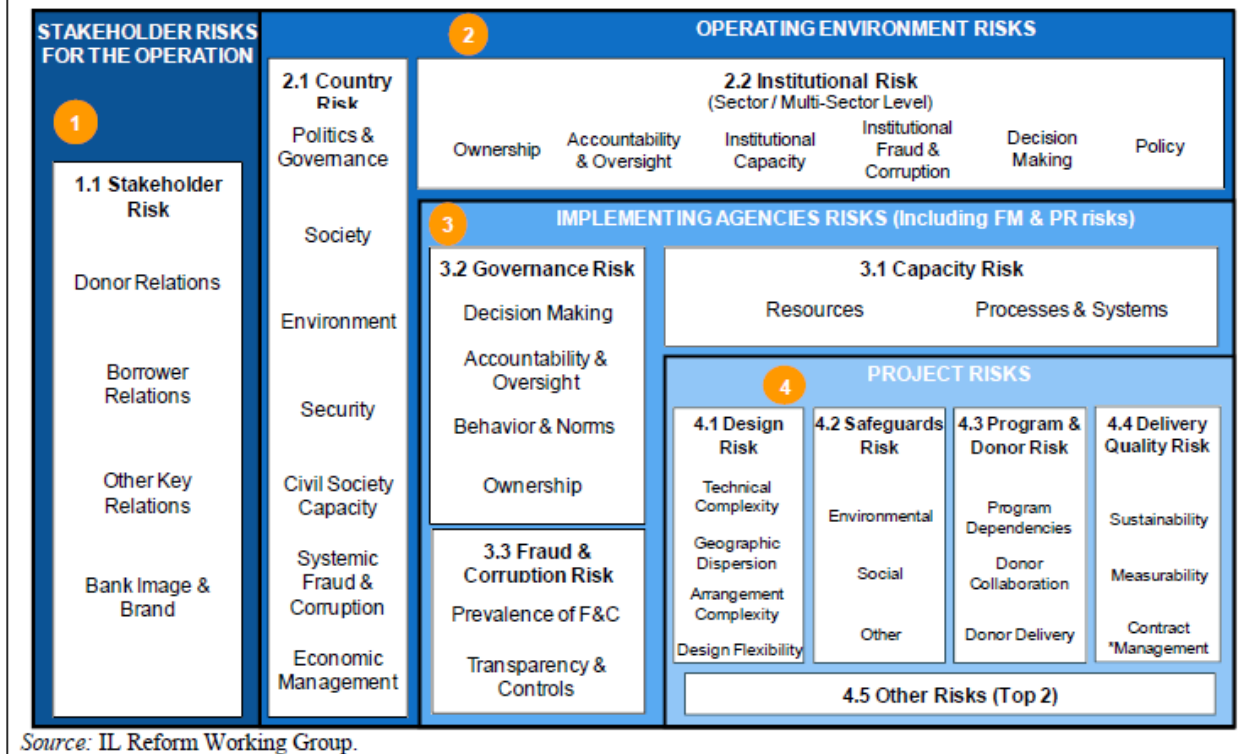
The management designed a new Risk Assessment Framework for its operations. As the diagram below illustrates, there are 38 types of risk grouped into four categories. The risks arising from non-compliance with social and environmental safeguard policies³ represent 3 of the 38 types of risk. (See chart below.)

¹ 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>

² For IEG, these "significant deficiencies" are identified as: (i) a need to maintain the currency of the Bank's Operational Policies and Bank Procedures (OP/BPs); (ii) a need for improved systems of document retention and accessibility; (iii) generic weaknesses in controls over financial management and procurement processes; (iv) a need for improved management oversight of project processing and supervision, coupled with improved staff incentive structures and performance accountability; (v) a need to improve risk management; (vi) a need for greater IT security in some areas.

³ 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>

Figure 2. Operational Risk Assessment Framework for Investment Lending



2. Decentralization

The “new” World Bank Group will be significantly decentralized, including four regional hubs, which will take responsibility for managing low-risk projects. Higher risk projects will receive more attention from headquarters in Washington, D.C.

3. World Bank Operational Policies

The institution’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. Stakeholders in borrowing countries can bring a complaint before the Bank’s Inspection Panel if there is evidence that the Bank has violated its own policies. Therefore, it was alarming that the IEG’s review 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.”⁴

The Bank concluded that, due to the multiplicity of Operational Policies and Business Procedures that are applied to investment lending -- some of which are perceived to be outdated or irrelevant – it should “consolidate⁵ and rationalize the policies and procedures

⁴ IEG, “IDA Internal Controls, Volume V, p. 18.

⁵ 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).

governing investment lending by creating a single principles-based ‘umbrella’ policy for investment lending that would govern projects from preparation through completion.”⁶

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 single umbrella policy affect the rights and abilities of stakeholders to bring a claim to the Inspection Panel?

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

The Bank has decided that the “blueprint” project instrument “was created for a different era...”⁷ and that it 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.”⁸

In the IEG review, Bank management stated that its new investment lending framework would:

“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.”

In response to our questions to Bank officials, it appears that the Bank will not abandon its ring-fenced project model, but rather replace many of these “ring-fenced” projects with a new instrument, the Results-Based Investment Loan (RBIL). From what little we have learned about the RBIL (nothing about it is in the public domain), it seems to be a “flexible” sector-wide investment instrument that would permit the extensive roll-out of sector programs (health, education, agriculture, industry) in a country. Therefore, for better or for worse, the RBIL would have far more extensive impacts than many “ring-fenced” projects.

We need to learn much more about the RBIL: Will it be governed by the aforementioned umbrella investment lending policy? Will the social and environmental safeguards apply to it? How will staff and country authorities manage the risks associated with the large operations implied by the RBIL? To what extent will the RBIL require country leadership through extensive civil society and parliamentary participation? Will grants also finance these operations in low-income countries?

We are told that the World Bank’s Board of Executive Directors will weigh such questions when it meets in June to approve the RBIL instrument. The Bank’s management reports that the safeguard policies will apply to the RBIL operations, but to the best of our knowledge, this

⁶ IEG, “IDA Internal Controls,” Volume I, p. 27.

⁷ 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/2009/09/09/00033303720090909235811/Rendered/PDF/502850BR0Box3410only10SecM200910442.pdf>

⁸ World Bank, “Investment Lending Reform, Concept Note,” January 26, 2009.

is only the decision of management and has not been approved by the legal department of the Board of Executive Directors.

It appears that the lending through RBIL instruments may constitute a high proportion of the Bank's portfolio (as ring-fenced projects are scaled back), so it is very important that the Board approve the application of safeguards to this new instrument.

5. Other “flexible” project operations

The RBIL instrument will join another “flexible” project instrument – namely Development Policy Loans (DPLs), which are called “Poverty Reduction Support Credits” (PRSCs) in low-income countries.⁹ 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.

Environmental and social safeguard policies do not apply to DPLs/PRSCs which represent a growing proportion of the Bank's total portfolio. Particularly in response to the global financial crisis, the level of DPLs issued by the IBRD rose sharply to 50% of disbursements. The percentage of IDA DPLs/PRSCs remained more or less constant at 25% of IDA disbursements. If the trends continue, the implications, at least for the IBRD, are that a higher percentage of lending operations will be exempt from safeguard requirements.

6. Flexible Assistance is the Modality for the Future

The 2005 Paris Declaration committed donors and creditors to providing two-thirds of all their aid via flexible, program-based approaches by 2010. This means aid is pooled in support of a particular strategy led by a recipient country—a national agriculture or energy plan for example—rather than fragmented into multiple individual projects. Already, the Bank plays a significant management role in budget support operations, which are pooled funds with contributions from a myriad of donors and creditors. In the future, the World Bank sees an even bigger role for itself in this area.

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.¹⁰ [Emphasis added.]

⁹ 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>

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

Flexible program assistance eases the strain on recipient governments, for example by reducing the large numbers of duplicative field missions and requirements to comply with different reporting procedures for dozens of donors and creditors. However, in some ways, it is more difficult to evaluate the impacts of such operations and more efforts are needed to mandate the application of social and environmental safeguards to flexible operations. As noted above, the World Bank does not apply safeguards to its DPLs/PRSCs.

7. Country Systems

At its heart, the Paris Declaration committed to supporting developing-country governments in their efforts to formulate and implement their own national development plans according to their own national priorities by using, wherever possible, their own policies as well as planning and implementation systems. A national government's policies, planning and implementation systems are called "country systems." There are many different types of country systems as they pertain to financial management, procurement, and social and environmental safeguards.

The follow-up to the 2005 Paris conference was the 2008 Accra conference. The 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."

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. 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.

How might this shift affect World Bank operations?

--Standards. Donors, creditors and recipient governments are harmonizing standards of performance and accountability so that the required attributes of country systems will be uniform in a number of areas: public financial management, procurement, fiduciary safeguards and environmental assessments. These systems are supposed to align with broadly accepted good practices, but this raises the question of what "good practices" and policies will be employed to harmonize fiduciary and social and environmental safeguard policies.

These safeguards have been developed over the course of twenty years with significant input to their content by governments, but also civil society groups.

--Accountability. Who will be accountable for the quality of flexible and "ring-fenced" project operations in a world of country systems? The Bank must attest to whether a country system is equivalent to its own policies and, if not, what "gap-filling measures" are needed to bring the system into line with its policies. After gap-filling measures have been implemented by a government, the Bank must attest to whether these measures are "acceptable" or bring the country systems up to the required standards.

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 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?

As noted above, the World Bank claims its authority to manage pooled funds – including Climate Investment Funds -- based upon its role as a standard-setter and its *“technical design, fiduciary assessments and implementation support for projects and programs.”* However, to make good on such claims, the World Bank’s standards must be “world class.” It is not the job of a public institution such as the Bank to compete with its member countries, such as China, but rather to use its public resources to safeguard the future.