

World Bank Safeguards & Development Policy Lending

A Primer on Why DPLs Should be Part of the Safeguard Review

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1) What are Development Policy Loans?

Development Policy Loans (DPLs) are programmatic loans that largely fund policy reform, often through rapidly-disbursed budgetary support, rather than project-based physical investments. DPLs were created in 2004 by merging Sectoral Adjustment Loans (SECALS), Structural Adjustment Loans (SALs), and other instruments. The World Bank has approved an average of 60 DPLs per year (compared to about 400 investment lending projects), but the size of each DPL is generally much larger than an investment loan. While the majority of DPLs go to middle income countries, at least a quarter of the loans are given to the world's poorest countries (IDA countries).

2) Why should civil society care about DPLs?

DPLs have on average constituted 30 to 40% of total Bank funding, but policy lending has in the past peaked above 50% of total funding (See Fig. 1 below). DPLs are governed by OP/BP 8.60 and since 2004 have been excluded from the scope of the Bank's environmental and social safeguard policies, including OP/BP 4.01 on Environmental Assessment. This is concerning because DPLs can have significant and long-term environmental and social impacts. In recent years, the Bank has approved over 60 DPLs to advance policy reforms in sectors related to natural resources and the environment, such as water, energy, agriculture, forestry, transport, and extractive industries. These sectors accounted for over 20% of all DPLs in FY08.¹

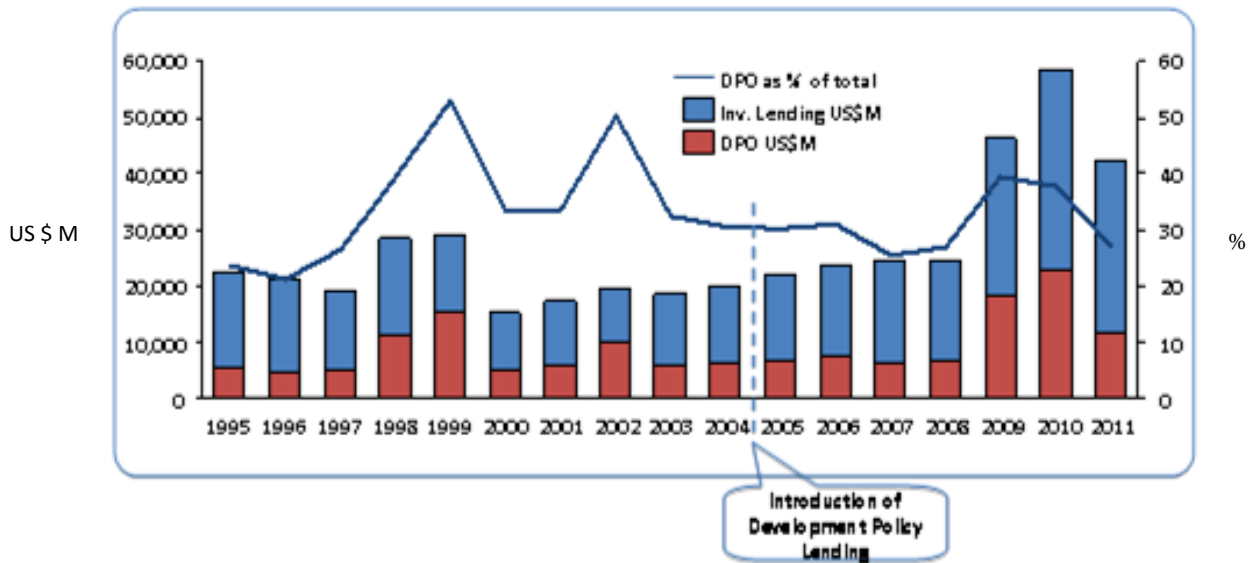


FIGURE 1: Total World Bank DPL and Investment Lending 1995-2011.
 Presentation by the World Bank Operations Policy and Country Services (2012)

Reforms such as private sector development, privatization or trade reform can also have major impacts on the environment. Based on the Bank’s assessment, very few DPLs have the “likelihood of significant [environmental or social] effects,” but this perception is misleading because the Bank’s identification of direct and indirect impacts has often been inadequate. This can lead to the misuse or

poor performance of DPLs in high risk sectors. As the Bank extends the use of DPLs to a greater array of reforms in sectors related to natural resources and the environment, including special DPLs for disaster response and climate change, there is an urgent need to sharpen its environmental and social risk analysis.

Lessons from Forest Sector DPLs:

The World Bank’s use of DPLs for forest sector reform illustrates the potential of DPLs to cause significant environmental impacts and the inadequacy of the Bank’s analysis of such risks. As noted in the recent Independent Evaluation Group (IEG) evaluation of the World Bank implementation of its Forest Strategy, DPLs were one of the main instruments used for forest policy reform between 2002 and 2011 (IEG Evaluation, Sec. 2.52) and were used extensively for industrial timber concession reform in Africa. The IEG noted that “[a]ny concession policy that the World Bank supports will have an asset transformation effect—that transforms the value of forests assets and the access that forest-dependent people will have to them. But development policy operations do not require the same level of risk assessment or mitigation systems as investment operations do under the Bank’s safeguard system.” It further notes that the use of DPLs “inhibited the Bank’s ability to apply rigorous risk assessment and related mitigation measures in its concession portfolio.” (IEG Evaluation, Sec. 2.61) These problems are demonstrated by the case studies below on forest policy reform in the Democratic Republic of Congo (DRC) and Cameroon.

3) Do DPLs have protections against environmental and social harm that are as robust as the safeguards for Investment Lending?

The DPL policy is much less protective against negative environmental and social impacts (see **Case Studies 1 & 2**). OP 8.60 requires the Bank to determine in its risk assessment “whether specific country policies supported by the operation are likely to have significant poverty and social consequences, especially on poor people and vulnerable groups” (para. 10) or “are likely to cause significant effects on the country’s environment, forests, and other natural resources.” (para. 11) The Bank must also assess whether a borrower has a system in place to manage those risks, and if gaps are observed in a borrower’s risk management systems, it must identify measures to fill those

gaps. However, the policy lacks detailed requirements on how risk assessment and mitigation should take place and how a country system analysis should take place, as well as clear and verifiable requirements for transparency, participation and accountability in policy design and implementation. Instead, such details are found in voluntary guidance (e.g. Good Practice Notes) and toolkits, which result in inconsistent implementation of the policy requirements. The DPL policy and accompanying internal Bank processes for protecting against environmental and social harms therefore fall far short of what the safeguard policies require for investment lending. This includes mandatory requirements for assessment and mitigation of environmental and social risks and impacts as well as disclosure and consultation requirements that are based on the overall

CASE STUDY 1: Transitional Support for Economic Recovery Credit (TSERO) to the DRC: Failure to identify significant social and environmental effects

The lack of robust risk assessment requirements in OP 8.60 was clearly illustrated in this US \$90 million DPL to the DRC. Approved in 2005, one of the main objectives of the loan was to improve governance in the forest sector in order to allow for more socially equitable and environmental sustainable use of its forest resources. The project aimed to do this by putting into place a regulatory framework for industrial logging concessions in the country’s tropical rainforests. The Bank determined there would be no significant social or environmental effects as a result of the proposed reforms. This resulted in a complaint to the Bank’s Inspection Panel brought by forest-dependent indigenous peoples in DRC.

The Inspection Panel found the Bank’s determination to be incorrect and noted in particular the absence of social and environmental analysis on which to base a determination. The Panel concluded that the policy’s “system for determining whether there will be significant effects on the environment and natural resources is flawed” (Inspection Panel Report No. 40746-ZR, p. xxv) and questioned whether a DPL was the right choice of instrument given the social and environmental risks associated with DRC’s forest sector (p. xxvi).

The Panel observed more generally that the Bank rarely determined that DPLs could have a significant impact on the environment, even for those loans that involve policy reforms in the forest sector despite this sector’s high potential for environmental impacts.

level of risk posed by the project. The Bank's use of Poverty and Social Impact Analyses (PSIAs) and Country Policy and Institutional Assessments (CPIAs) to assess risks for DPLs are not designed for environmental risk. Environment and social risk assessment and mitigation for DPLs must be made more predictable, objective, transparent and accountable in line with the requirements of OP 4.01.

DPLs also suffer from an accountability gap. Negatively impacted communities have difficulty holding the Bank accountable due to limited transparency and consultation requirements relative to investment projects. In addition, the Inspection Panel cannot review complaints relating to loans that have closed or are more than 95% disbursed (BP 17.55, Annex A, para. 14(c)). Due to the fast disbursing characteristic of DPLs, whereby

money is usually disbursed as a single tranche, impacted communities often have a very narrow window to assess DPL details after approval and can only base their claims on anticipated harm, where the causal connection between policy and harm can be difficult to prove.

4) Is the Bank currently working to improve the DPL policy?

To date, the Bank has never undertaken a comprehensive review of the environmental and social impacts of DPLs in the nearly ten years since the policy was put in place. The Bank has revised OP 8.60 five times since 2009, but not in ways that address how environmental and social risks are assessed and mitigated. The Bank's 2012 DPL Retrospective offers some recognition of weaknesses in the overall approach to risk assessment, but was a desk-based self-assessment that was not intended as an in depth review of the policy's environmental or social risk assessment process or its effectiveness (2012 DPL Retrospective p. 41 and Annex D).

The Retrospective concluded that the Bank's entire DPL portfolio during the three year period under review had virtually no negative direct or indirect environmental effects. However, the Retrospective assessment was based entirely on information in Project Documents and therefore would not identify any weaknesses in the underlying analysis. For example, the Peru DPL (**see Case Study 3 below**) was not identified as having possibly negative environmental effects by the Retrospective, demonstrating the potential for underestimation of these risks under the current Bank policy. The Retrospective assessment of potential environmental effects is unfortunately not backed by any detail on

CASE STUDY 2: Sustainable Environmental Management (SEM) DPL to Brazil: Weak risk assessment dilutes accountability for sustainability outcomes.

The SEM DPL to Brazil demonstrates the problems associated with the weak transparency and accountability requirements of OP 8.60. The DPL provided \$1.3 billion to Brazil in return for safeguard reforms at Brazil's largest public Bank, the Brazilian National Bank for Economic and Social Development (BNDES).

However, BNDES does not disclose its project documents and therefore the results of the DPL are unknown. In the absence of transparent and accountable results, the Bank could not show that BNDES was meeting DPL conditions to "effectively apply" a new environmental and social policy that purportedly screened and mitigated risks for a number of high risk projects funded by BNDES, including a bridge loan for the Belo Monte hydroelectric dam.

**CASE STUDY 3: Peru Environmental DPL:
Risk underestimation erodes
environmental governance**

Flawed risk assessment for this Environmental DPL contributed to the lack of mitigation measures when expected institutional reforms proved overly optimistic. Although the World Bank funded a high quality Country Environmental Assessment (CEA) for Peru in 2007 that covered many areas of potential Environment and Natural Resources Management reform, CSOs were not involved in the design of the DPL policy matrix, or in the implementation.

Lack of CSO participation in DPL preparation resulted in the exclusion of key sector reforms, such as forestry. The CEA did inform a prior action focused on strengthening the institutional capacity of Peru's Environment Ministry (MINAM) to ensure the effective implementation of environmental impact assessments (EIAs). However, the intended DPL contributions to building MINAM capacity were reversed by setbacks in the EIA system, as indicated by an ongoing review and by recent conflict over contested licensing decisions for mining projects.

MINAM conducted a review of EIA compliance with national law, indicating various inconsistencies and a pattern of EIA quality control issues. Recent unrest over the deficient analysis of the proposed Conga gold mine on local water resources in Cajamarca, among other environmental conflicts in Peru, have resulted in a recognition of gaps in the overall regulatory framework and the creation of a new inter-sectoral body (SENACE) to review and approve EIAs.

Rather than strengthening public confidence in MINAM, the DPL may have facilitated the erosion of confidence, and in turn undermined the fragile efforts to enhance MINAM's role in environmental governance.

the actual methodology used to assess and mitigate environmental risks when preparing DPLs, thus undermining the report's utility in helping the Bank to improve the policy.

5) Are DPLs covered by the Safeguard Policy Review?

Bank Management has so far stated that the safeguard policy review will not consider the application of safeguard policies to DPLs.² However, the Safeguard Review Approach Paper does not preclude consideration of DPLs. It states that "the Bank may review other relevant Operational Policies" (para. 31) besides those for investment lending, and the Bank "anticipates a new integrated framework that will articulate how all Bank instruments can achieve better development outcomes."³

6) Why should DPLs be discussed in the safeguard review?

The safeguard review presents a critical opportunity to ensure the Bank has robust risk assessment and safeguards across all instruments. As the IEG stated in a 2011 summary of its evaluation of the Bank's safeguards and sustainability policies, "it is vital to seek consistency among the approaches followed in these growing segments of the [Bank] portfolio to ensure coherence in environmental and social sustainability outcomes."⁴ The current safeguard review must consider whether, and if so how, the safeguard policies will apply to all Bank instruments, including DPLs. The credibility and utility of the review will be undermined if a large portion of the Bank's lending portfolio is excluded from the outset without a clear rationale.

DPLs have weak and poorly defined requirements for risk categorization, transparency, and consultation. Defining minimum requirements, particularly for higher risk DPLs, in the updated safeguard frameworks would close a loophole that allows non-investment lending instruments to operate with lower comparable standards of protection against social and environmental harm.

7) Is it feasible to extend the current safeguards to cover DPLs?

Consideration of safeguard application to DPLs can be dealt with efficiently and effectively in the review and update of the safeguard policies – it is not necessary, at this time, to open up the DPL policy to consider these issues. The safeguard policies already contain language about what types of Bank operations the safeguards do and do not cover; this language should be reviewed and updated to incorporate DPL coverage into the safeguard policies. We also note that OP 4.01 already includes environmental assessment tools – such as Strategic Environmental and Social Assessment (SESA) and Sectoral Environmental Assessment (SEA) – that were designed for use in policy-based operations, and could be updated as needed to increase their effectiveness for DPLs. Updating of OP 4.01 could provide systematic procedures on how environmental and social assessment and mitigation should be carried out for DPLs, in order to help clarify minimum requirements for conducting appropriate environmental and social risk management and consultation.

There is precedent for applying the environmental assessment requirements of OP 4.01 to DPLs, when they were SECALs prior to 2004 (See **SECAL Case Study 4 - Poland⁵ and Case Study 5 – Cameroon below**). In

particular, for a number of years OP 4.01 stated that “Sector adjustment loans (SECALs) are subject to the requirements of this policy,” and required the environmental assessment for a SECAL to assess “the potential environmental impacts of planned policy, institutional, and regulatory actions under the loan” (para. 10). During those years, OP 4.01 further noted that “Actions that would require such assessment include, for example, privatization of environmentally sensitive enterprises, changes in land tenure in areas with important natural habitats, and relative price shifts in commodities such as pesticides, timber, and petroleum” (fn. 15).

CASE STUDY 4: Poland Coal SECAL II: Benefits of SEA for high risk policy loan

The Poland Coal SECAL II demonstrates the benefits of proper risk assessment of DPLs under OP 4.01 and the importance of Strategic Environmental Assessments (SEAs) for higher risk DPLs. An Extractive Industries Review background paper by the Operations Evaluation Department (now the IEG) reviewed six SECALs, including this one, as part of a sample of 37 Extractive Industry Sectors projects in 2003.

According to the authors, the case “illustrates the appropriateness of carrying out an SEA followed by sub-project-specific EIAs.” The SEA found that the damage costs of saline water discharge were not as serious as previously estimated. Rather than investing in large desalination plants, the SEA identified less costly options as equally if not more effective. The SEA also identified land subsidence as an important environmental problem. In relation to mine-specific Environmental Assessments and Action Plans, the SEA provided numerous insights that facilitated the updating and strengthening of individual mine EAPs to bring them in line with the recommendations of the SEA.

Consistent with this precedent, the safeguard review could decide to include DPLs in the scope of coverage of OP 4.01 and therefore subject to environmental and social risk categorization and its associated requirements.

Moreover, other international financial institutions such as the Asian Development

Bank (ADB) have included policy-based instruments under the scope of its environmental safeguard policy. The ADB applies its safeguard policy to projects delivered through sector loans, emergency assistance loans, and other lending modalities (para. 62). This includes the requirement of risk categorization.

CASE STUDY 5: Forest and Environment Development Program (FEDP) to Cameroon: the importance of risk categorization and assessment of borrower system

The feasibility and importance of systematic risk categorization and the need for strengthened procedures for analyzing borrower systems for risk mitigation are illustrated by this DPL to Cameroon approved in 2006. A key objective of the loan was to promote the implementation of timber concession management policies.

The loan began as a SECAL and therefore initially was subject to the requirements of OP 4.01 and assigned a Category A risk categorization. The 2004 Integrated Safeguards Data Sheet explains that “the highly demanding Cat. A consultative process has given the project the broadest possible exposure to stakeholders and environmentally concerned groups both in Cameroon and abroad. This results in a richer feedback to help improve project design...” The initial detailed risk assessment also allowed for the identification of risks to the indigenous peoples living in and around the forest, unlike in the forest sector DPL to DRC approved the previous year (described in Case Study 1), and required the development of an Indigenous Peoples Plan. The loan was designed around the fulfillment of prior actions and conditions that would trigger the release of funds in three tranches.

The loan was subsequently transformed into a DPL after OP 8.60 took effect in 2004, which reduced the requirements for transparency and supervision despite indications from prior assessments that there was potential for significant social and environmental harm and weak institutional capacity to mitigate it.

For example, under the DPL the Bank was not responsible for overseeing the implementation of the Indigenous Peoples Plan, although its publication by the government was a required policy action for the release of the first tranche of the loan, and evidence suggests that the plan was not adequately carried out by the government. This is of great concern given that the negative impacts of timber concession policies on indigenous peoples in Cameroon are now well-documented.* The DPL was ultimately cancelled with two tranches undisbursed after the government failed to meet a key governance condition, with important implications for the environmental outcomes of policy reforms.

* For more information on Indigenous Peoples’ issues in Cameroon, see the following sources: Indigenous peoples’ rights in Cameroon: Supplementary report submitted in connection with Cameroon’s second periodic report, May 2010. Submitted to the African Commission on Human and Peoples’ Rights by Center for Environment and Development (CED), Réseau Recherches Actions Concertées Pygmées (RACOPY), and Forest Peoples Programme (FPP); International Work Group for Indigenous Affairs (IWGIA), Plan Finland, Plan Cameroon, 2012. What future for the Baka? Indigenous peoples’ rights and livelihood opportunities in south-east Cameroon.

8) How should the Bank's treatment of DPLs change?⁶

At the outset of the safeguard review, we suggested the following changes to OP 4.01, focusing on those DPLs which pose higher social or environmental risks. The addition of the procedures below, which are not exhaustive, would help to ensure that DPLs with the greatest likelihood of adverse social or environmental impact are properly identified and risks are mitigated.

- i. DPLs should be preceded by a Country Assistance Strategy (CAS) that is properly assessed for risk using a SESA, CEA, or other appropriate strategic assessment.
- ii. DPLs should be subject to environmental and social risk categorization based on a robust environmental and social screening process. The use of this approach for SECALS before 2004 and the approach at the ADB (and currently under consideration by the African Development Bank) indicate that this can be done. Categorization should consider factors such as the distribution of costs and benefits of policy reforms, implementation capacity to carry out reforms or reduce potential adverse effects, association with Category A sub-projects, and existence of environmental or social conflict in the policy area or sector.
- iii. DPLs should be subject to more objective and effective frameworks for assessing baseline institutional capacity of the government, gaps in their risk management systems, prior actions, and benchmarks for strengthening capacity, along the lines of suggested frameworks proposed by the Bank's environment department.⁷
- iv. Category A DPLs should be required to complete a thorough Environmental and Social Assessment (ESA) prior to appraisal, along with proper disclosure and consultation as outlined in OP 4.01. The Bank has already defined in OP 4.01 the types of ESA instruments that could be used: SESA and SEA. As with the relatively successful PSIA, the Bank should further specify requirements for the use of SESAs for DPL prior actions that are likely to have significant effects.
- v. Category A DPLs should require greater participation and transparency during each stage of the project cycle, beginning with consultation and disclosure of the SESA, followed by the disclosure of the draft Program Document and extending to documented evidence of results.
- vi. All DPLs should be subject to robust monitoring and evaluation mechanisms, which encompass longer term monitoring of reform process results. Category A DPLs should include provisions for participatory and independent monitoring and evaluation as well as satisfaction surveys or ex-post workshops at the end of the loan to examine key lessons.
- vii. All DPLs should provide more reliable grievance response mechanisms for stakeholders beyond the Bank's Inspection Panel, which has very limited jurisdiction over DPLs.

9) What needs to happen now?

The first step is for the Bank to formally recognize DPLs as part of the safeguard review and begin consulting with stakeholders on their experiences and views.

It is also important that the Bank review good practice and analyze lessons learned from policy-based operations. The Bank should consult with CSOs and relevant experts on the experience of applying environmental and social requirements to policy-based operations by the Bank, by other multilateral and bilateral development partners such as the Asian Development Bank, and by governments under their domestic laws. In particular, the Bank should review good practice regarding application of environmental and social assessment and mitigation requirements to policy-based operations. Various lessons can

be learned from the Bank's own experience in the use of OP 4.01 for policy-based lending. We think there could be useful roles for IEG and the Inspection Panel in this effort.

LIST OF ACRONYMS

ADB	Asian Development Bank
BP	Bank Procedure
CAS	Country Assistance Strategy
CEA	Country Environmental Assessment
CSO	Civil Society Organization
CPIA	Country Policy and Institutional Assessment
DPL	Development Policy Loan
ESA	Environmental and Social Assessment
IDA	International Development Association
IEG	Independent Evaluation Group
OP	Operational Policy
PSIA	Poverty and Social Impact Analysis
SECAL	Sectoral Adjustment Loan
SESA	Strategic Environmental and Social Assessment

The content in this document is based on case study research of several DPLs as well as meetings with World Bank, Government and IEG officials.

Questions or requests for further details on noted DPLs and other Case Studies may be directed to: Vince McElhinny, Bank Information Center, vmcelhinny@bicusa.org
Hana Heineken, Global Witness, hheineken@globalwitness.org

¹ Acharya, Kishore, and Semaan (2010), "The Role of Environmental DPLs in Supporting Environmental Sustainability: Assessing Experience, Learning Lessons," World Bank. (unpublished manuscript) [Draft Concept Note available [here](#)]

² Joachim von Amsberg, Vice President of World Bank Operations Policy and Country Services (Jan. 11, 2013), [Letter in response to Initial Comments by CSOs on the World Bank Safeguard Review](#).

³ World Bank (Oct. 10, 2012), [Approach Paper for the Review and Update of the Safeguard Policies](#), para. 29.

⁴ Anis Dani, Ade Freeman, and Vinod Thomas (2011), "Evaluative Directions for the World Bank Group's Safeguards and Sustainability Policies," IEG Evaluation Brief 15, World Bank, pg. 17.

⁵ Batstone, Roger (July 23, 2003), "Evaluation of the World Bank Group's Activities in the Extractive Industries Sector – Background Paper, Review of Implementation of Safeguard Policies of World Bank Extractive Industries Projects," World Bank Operations Evaluation Department, pg. 7-8

⁶ Many of these proposals are highlighted in two background papers for the 2010 Environment Strategy Review. See Eltz, Narain, Orfie and Schneider (2010), [Strengthening Environmental Institutions and Governance: What Should be the Role of the World Bank Group?](#); and Acharya, et al., op cit.

⁷ The paper by Eltz, et al. outlines four institutional abilities, of which accountability is found to be relatively underinvested in by World Bank ENRM operations, including 13 environmental DPLs.