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Is the EIB's Climate Change Loan to Brazil sustainable?

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This policy note synthesises the findings from a field visit to Rio de Janeiro by Both ENDS in August 2012.

Interviews:

- Brent Millikan - International Rivers
- Oriana Rey - Amigos da Terra
- Carlos Tautz and João Pinto - Instituto Mais Democracia
- Roland Widmer - OneAdvisory
- Mariana Werneck – Ibase
- BNDES refused a meeting to discuss this loan or any of the issues discussed in this policy note.

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1. Introduction

In 2011, the European Investment Bank (EIB) announced it would provide a €500 million Climate Change Framework Loan (CCFL) to the Brazilian Development Bank (BNDES), mainly for projects in the renewable energy sector supporting climate change mitigation. BNDES' track record of supporting a number of highly controversial hydropower projects in the Amazon, combined with its support for polluting energy companies like PetroBras, put civil society organisations in Europe and Brazil on alert, and they have followed this loan with a critical eye. The loan has also raised questions in the European parliament. However, attempts to obtain more information on the type of projects to be supported by the loan and the safeguards to be applied were not fruitful due to BNDES' refusal to disclose any information or engage with civil society organisations.



photo: Da Gaveta
<http://dagavetaproducoes.wordpress.com/2012/02/13/bndes-divulga-resultado-dos-projetos-selecionados-1o-periodo-de-2012/>

Based on discussions with civil society organisations in Brazil, a web and literature review, and the limited information obtained from BNDES and the EIB, this report attempts to find answers to four basic questions:

- Are EIB climate change investments deployed where they are most needed?
- Is BNDES's development model climate-friendly?
- Does BNDES comply with basic EIB rules on public participation, accountability, and transparency?
- How can the EIB's CCFL to BNDES contribute to promoting a sustainable energy path?

1.1 Brazil and clean energy – major challenges ahead

Brazil boasts having the cleanest energy mix in the industrialised world, with 45.3% of its total energy provision coming from renewable sources. The main sources are water, biomass, and ethanol, along with solar and wind power. At this moment, 75% of Brazil's total electricity generation comes from hydropower stations. Further expansion is foreseen in the hydropower sector, as only about a third of the total generation capacity is currently exploited. Specifically, large dams are planned in

the Brazilian Amazon region.¹ Both large hydropower projects and the large-scale use of biomass are already having detrimental environmental and social impacts in Brazil. The Belo Monte mega dam on the Xingu River in the Amazon, supported by BNDES, is expected to cause huge devastation to the rainforest and destroy the livelihoods of thousands of tribal people who depend on the forest and river (see text box 1).² But even slightly smaller dams, like the ones planned on the Tapajos River, will contribute to opening up the Amazon, leaving it vulnerable to deforestation, methane emissions, land disputes, and infringement on indigenous lands - some of the well-documented problems related to these forms of energy.³ This calls into question the common practice of labeling these energy sources as 'clean'. Moreover, the exploration of Brazil's new offshore oil reserves puts extra pressure on Brazil's clean energy reputation.

1.2 The EIB's Climate Change Framework Loan

It is in this context that the EIB announced, on 5 October 2011, that it would provide a €500 million CCFL to BNDES. Although the contract was signed on that same date, almost a year later the money has not yet been disbursed. BNDES declared⁴ it has not yet requested the disbursement, without giving further explanation. The bank affirms it will file the request for disbursement when 'the time is appropriate'.

The objective of the CCFL to BNDES is articulated as follows:

*'to support investments that generate environmental benefits with respect to combating climate change. The majority of the schemes will contribute to reducing greenhouse gas emissions by generating renewable energy. Other schemes may focus on increasing energy efficiency, including in industrial applications, the heating and cooling sectors and in power generation or support investments for climate change adaptation.'*⁵

More information was obtained upon request from the EIB, specifying that the EIB's Brazil CCFL will provide financing for small- and medium-size investments in the renewable energy and energy efficiency sectors. The framework loan will be made up of a maximum of 25 investment schemes in the following sectors: energy and energy efficiency including small hydropower schemes (less than 30 MW), biogas- or biomass-fired heat and power plants, medium-scale hydroelectric power plants and wind farms, energy efficiency and climate change adaptation investments, as well as manufacturing facilities for renewable energy equipment.

The objectives behind the CCFL for Brazil indicate the intention to address the need to finance smaller and mid-size projects, although leaving open the possibility to

¹ <http://www.brasil.gov.br/cop/panorama/o-que-o-brasil-esta-fazendo/matriz-energetica>

² <http://www.survivalinternational.org/about/belo-monte-dam>

³ <http://www.bothends.org/nl/Publicaties/document/55/Safeguarding-the-Amazon>

⁴ In a telephone call with Vivian Machado dos Santos Correa Pereira (BNDES Manager for International Organisations) on 8 August 2012

⁵ <http://www.eib.org/projects/press/2011/2011-143-brazil-eur-500-million-loan-for-climate-change-mitigation-projects.htm>

fund large projects. However, an average investment amount of €20 million⁶ remains relatively large for potential projects such as access to clean energy for the poor or adaptation projects for the poor. Another worrying issue is that in the case of hydropower (one of the types of energy promoted through the CCFL), small dams can also be problematic, specifically in cases where a cascade of many dams is planned in a single river basin, leading to the same need for adequate (cumulative) due diligence as for large dams.⁷ As will be explained below, BNDES's current safeguards system does not meet this demand.

Although no concrete information can be given on the expected effectiveness and impacts of the projects that this loan will fund, this policy note will examine the broader question of the choice for BNDES as the vehicle for promoting a clean development path in Brazil. Will this loan be beneficial, both in helping Brazil and BNDES to embark on a more sustainable energy path while at the same time reaching the poor with these efforts?

2. The EIB and climate finance

This loan is provided under the €4.5 billion Energy Sustainability and Security of Supply Facility (ESF). The EIB's role in international climate finance has been on the rise; between 2011 and 2012, the bank's overseas lending directed to climate change protection increased by €2 billion.⁸ The ESF is available for African, Caribbean, and Pacific states (ACP); Asia and Latin America (ALA); Neighbourhood countries; and South Africa, and only allows for EIB lending at its own risk (without EU guarantee). Countries of EIB operations where sovereign lending is possible under ESF are currently Brazil, Chile, China, India, Israel, Kazakhstan, Mexico, Peru, Tunisia, and the Republic of South Africa.⁹ The predicate 'at own risk' needs to be read with care, however: thanks to European guarantees, the EIB has a AAA credit rating, which allows the bank to raise funds in capital markets on advantageous terms, such as attractive interest rates and long maturities. The EIB promotes its integrated way of doing project appraisal as covering 'technical, economic, financial, environmental and social aspects as well as credit risks and providing for the appropriate mitigants and conditionality and helping structure projects in line with EU standards'. Thus, the EIB states, it 'acts as a flag carrier for EU policies outside the EU, contributes to the dissemination of best practices and facilitates the participation of other financiers in EU priority projects'.¹⁰

Along with loans for specific clean energy projects, the EIB has also signed several similar Climate Change Framework Loans with governments or financial intermediaries in other countries. The first of such CCFLs was given to China in 2007, and since then the total amount dedicated to CCFLs has reached almost €2 billion, mostly disbursed to intermediaries in emerging countries and for substantial amounts of money per loan (see Figure 1).

⁶ This is the total amount of the loan divided by the maximum 25 projects that will be supported under this loan.

⁷ <http://www.coolearth.org/306/news-32/rainforest-news-155/brazilian-indians-take-action-against-amazon-development-1486.html>

⁸ <http://www.euractiv.com/climate-environment/commission-teams-eib-climate-fin-news-495238>

⁹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52010SC0443:EN:NOT>

¹⁰ http://www.eib.org/attachments/country/eib_factsheet_latin_america_en.pdf

Figure 1: EIB Climate Change Framework Loans

Loan	Country/Region	Signature date	Amount (in € million)
Central America CCFL	Central America	15/12/2011	100
Investec Climate Action FL	South Africa	28/10/2011	50
Brazil CC Mitigation FL	Brazil	05/10/2011	500
Crescent Clean Energy Fund	Turkey +	12/09/2011	25
ICICI Bank CCFL	India	25/08/2011	200
China CCFL II	China	03/12/2010	286
Pakistan Renewable Energy FL	Pakistan	24/11/2009	100
Vietnam CCFL	Vietnam	26/05/2009	67
Exim Bank of India FL	India	02/12/2008	100.5
China CCFL	China	28/11/2007	500
Total			1928.5

Source: <http://www.eib.org/projects/loans/sectors/energy.htm>

As demonstrated by the figures above, as well as from the allocation of the World Bank-managed Climate Investment Funds, climate finance allocation disproportionately favours middle-income countries.¹¹ The Clean Development Mechanism (CDM) of the Kyoto Protocol for example also has a poor record of supporting the most cash-strapped countries in need of climate finance. Indeed, 72 CDM projects were registered across Africa in 2011, accounting for only 2% of international CDM projects. The majority of these projects were in South Africa and Egypt, with the rest distributed broadly among the remaining African countries.¹² In addition to the more fundamental issue related to CDM (namely the compensation of continued CO₂ emissions in the Global North through projects in the Global South), this confirms the picture that emerging economies where emission reductions are most economically beneficial and which are not the most cash-strapped are supported through climate change funding.

Although this policy note focuses on the Brazilian CCFL and the EIB, the geographical choice of recipient countries for the EIB's CCFLs does raise the question of whether enough efforts are made to reach the countries and populations most in need of climate finance. For the European Union as a climate change donor, more so than for the EIB (which can only provide loans and no grants), this raises the issue that there is still a huge gap between the need to support poor farmers and other vulnerable people and groups in their adaptation efforts and the funding made available. Whereas the UNFCCC Copenhagen Accord and Cancun Agreements promised balanced allocation between adaptation and mitigation, the current situation clearly shows an imbalance in the way climate funding is spent.¹³ Moreover, there is a strong appeal to make adaptation funding as grants and not loans, given the historic patterns of climate change.

¹¹ <http://www.brettonwoodsproject.org/doc/env/afaultymodel.pdf>, p.3

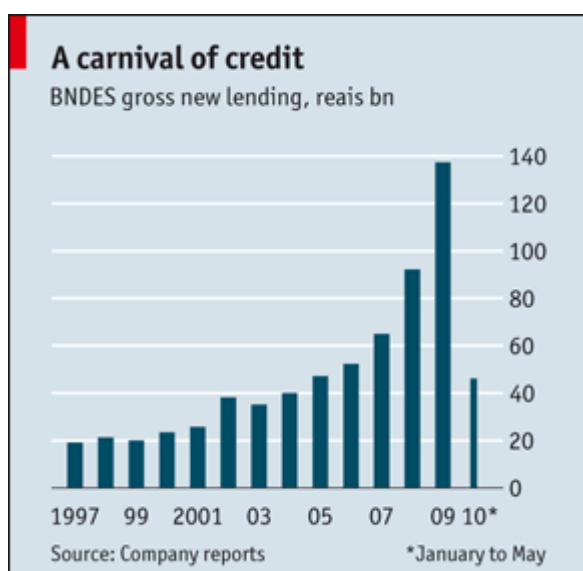
¹² <http://www.odi.org.uk/sites/odi.org.uk/files/odi-assets/publications-opinion-files/7480.pdf>, p.2

¹³ For example only 9 to 25% cent of fast-start climate finance is for adaptation; <http://pubs.iied.org/pdfs/17115IIED.pdf>

3. BNDES – an introduction to a giant

The Brazilian Social and Economic Development Bank (*Banco Nacional de Desenvolvimento Econômico e Social*, or BNDES) is a federal public company associated with the Ministry of Development, Industry, and Foreign Trade. It was founded in 1953, has 2500 employees, and is 100% state-owned. Its stated goal is to provide long-term financing for endeavours that contribute to the country's development. The 'S' (for Social) was not added to the bank's acronym until the 1980s, and a popular criticism from Brazilian civil society organisations is that BNDES still has difficulties in integrating this socio-environmental perspective into its lending. BNDES has grown to become the largest development bank in Latin America and the second largest development bank in the world. The largest is the China Development Bank and the World Bank comes in as a distant third. In 2010, BNDES had a loan portfolio three times larger than the World Bank's.¹⁴

Figure 2: BNDES gross new lending (1997-2010)



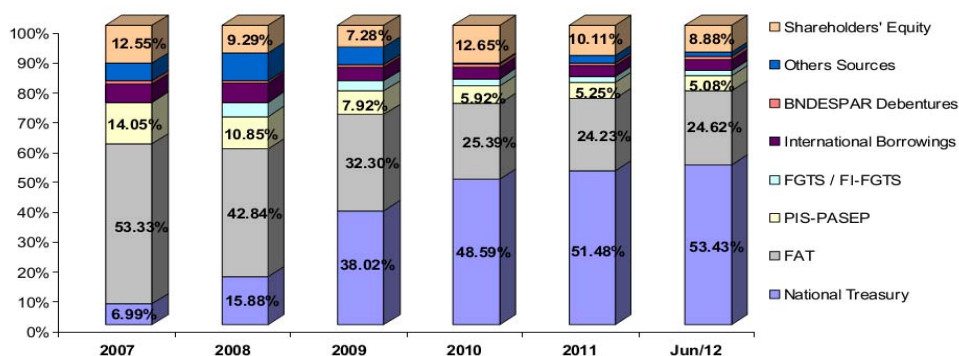
Source:
<http://forum.infomoney.com.br/viewtopic.php?p=1297981&sid=5ab585bf885aec1fea1e2fa4bfc1bacd>

BNDES is financed mostly through national funds and partly through international funds, including foreign government agencies and multilateral institutions, as well as market funding (see Figure 3 below). With regards to national funding, the Workers Assistance Fund (FAT) was the major financial contributor to BNDES until 2008, but a huge increase in funding from the National Treasury after the financial crisis has completely overturned the capital structure over the past five years. This has led to a very central position for BNDES in providing funding for Brazil's economic growth. The bank's participation in the financing of investments in the country reached 25% in 2010.¹⁵

¹⁴ <http://www.timizzer.com/business/economy/brazilian-development-banks-loan-bigger-than-the-world-banks/>

¹⁵ <http://www.bicusa.org/en/Article.12317.aspx>

Figure 3: BNDES' capital structure (2007-2012)



Source: http://www.bndes.gov.br/SiteBNDES/export/sites/default/bndes_en/Galerias/Download/AF_DEPCO_english.pdf

Since 2003, when former president Luiz Inacio Lula da Silva came to power, BNDES's loan portfolio has quadrupled, growing to a peak of €66.7 billion in 2010 and benefiting mainly manufacturing industries, farming projects, and infrastructure works in segments in which Brazil's federal government seeks to invest. Last year, infrastructure and industry received the biggest shares of BNDES's disbursements, at 39% and 34%, respectively.

BNDES has three wholly owned subsidiaries: FINAME, BNDESPAR (BNDES Participações S/A), and BNDES Limited. From a climate change and sustainable development perspective, it is interesting to look at its participations through BNDESPAR. One-third, or 33.2%, of BNDESPAR's investment portfolio goes to oil and gas companies (including Petrobras) and 20% to mining companies, such as Vale, the national mining giant. Another 16% goes to the electric power sector, where Eletrobras and CPFL Energia are the main beneficiaries. These companies are mostly established multinationals that could easily raise loans from Brazilian commercial banks and international institutions.¹⁶ Instead, BNDES' support structure has created fewer opportunities for private banks to develop and has entrenched a huge subsidy that is channelled towards large corporations through tax contributions. BNDES' business model is portrayed by critics as benefiting mainly large economic groups and enabling a concentration of wealth and power in the hands of few: around 60% of BNDES' portfolio is invested in large companies.¹⁷ It could be argued that, as a national development bank, a more important element to feature in BNDES' strategy would be to invest in small- and medium-sized enterprises, including small-scale farmers and informal sector enterprises, which are known to contribute most to local employment.

At the same time, and following the same logic, BNDES is paving the way for a green economy, dominated by business interests that treat nature mainly as an economic asset. BNDES's recent portfolio includes multibillion R\$ loans to controversial mega dams like Belo Monte and Jirau, the controversial nuclear power

¹⁶ <http://www.bdlive.co.za/articles/2012/08/02/armando-castelar-pinheiro-brazilian-financial-model-highlights-potential-shortcomings>

¹⁷ <http://www.ft.com/cms/s/0/983f1bca-0234-11e2-b41f-00144feabdc0.html#axzz2AOS60484>

plant Angra 3, meatpacking companies that exacerbate unsustainable cattle practices in the Amazon forest, sugarcane plantations in indigenous areas, and paper and pulp factories that lead to land conflicts. Civil society organisations in Brazil denounce the unsustainability of proceeding with the growth model promoted by BNDES, which capitalizes on Brazil's natural resources and fails to create high value jobs in the processing industries. Moreover, in examining the types of operations that BNDES finances, it is immediately clear that transparency, strong and sound safeguards, and accountability mechanisms need to be in place to avoid significant harmful social and environmental consequences.

4. BNDES' dubious climate change face

While in its function as a development bank BNDES has the opportunity to provide sound support to Brazil's industrial policy, and its essential questions of what energy technologies to support, the bank also rightly argues that it is not responsible for national energy planning. The bank is usually not in the position to choose the technologies or project options, but instead needs to judge single projects that are submitted for its appraisal, at least in theory. Some of these projects, as in the case of the Rio Madeira and Belo Monte dams, enjoy the explicit and specific support of the federal government, which appears to limit BNDES' sovereignty in deciding whether or not to finance them.¹⁸ For example, the Brazilian government's Programme to Accelerate Growth (PAC) envisages implementing mega infrastructure projects in the Amazon basin. Large dams, combined with industrial waterways, linked to highways, railroads, and the expansion of ports, all form components of transport corridors geared towards export-oriented agricultural and extractive industries.

Figure 4: Disbursements - green economy and climate change (in R\$ billion)

	2008	2009	2010	2011
Renewable energy and energy efficiency	5.7	5.7	6.0	7.1
Hydroelectric plants (over 30 MW)	3.7	8.4	6.2	5.2
Public transport	0.6	1.4	0.7	0.9
Cargo transport	1.5	2.0	1.4	1.6
Water and sewage management	0.8	1.6	1.9	1.5
Solid waste management	0.2	0.2	0.5	0.5
Forests	0.2	0.3	0.6	0.6
Agricultural improvements	0.1	0.4	0.5	0.3
Adaptation to climate change and disaster risk management	-	-	0.1	0.6
Other	0.1	0.1	0.1	0.2
Total	12.9	19.9	18.0	18.5

Source: Annual report 2011¹⁹

¹⁸ http://www.internationalrivers.org/files/attached-files/case_study_hydropower_development_in_brazil.pdf

¹⁹ http://www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Hotsites/Annual_Report_2011/Capitulos/the_bndes_in_numbers/disbursement_operational_indicators/socio_environmental_performance.html

Nevertheless, to measure disbursements directly linked to socio-environmental sustainability projects, BNDES has developed a specific statistical model for 'green economy' industries. The 'green economy' category involves operations in renewable energy, energy efficiency, water resources and environmental sanitation, solid waste management, hybrid and electric buses and trucks, as well as climate change projects.²⁰ Contributions to the sector reached R\$18.5 billion (€6.8 billion) in 2011. At the same time, according to BNDES' estimates, disbursements to the oil and gas industry will reach approximately R\$8 billion (€3 billion) in 2012, of which R\$3.8 billion (€1.4 billion) are directed towards the production industry. These numbers represent a significant increase compared to 2011, when a total of R\$3.3 billion (€1.2 billion) was released to the same sector, with R\$2.2 billion (€800 million) to production.

One of the key elements of this lending was the R\$9.4 billion (€3.5 billion) credit limit²¹ enacted in June 2012 to finance Petrobras' investment plan for 2011-2015. Several investor groups have criticised Petrobras' falling profitability, but the company, backed in large measure by BNDES, is likely to continue its steady efforts to invest in upstream production, with large hydrocarbon reserves coming into commercial production in the coming years. BNDES' increased investments in the sector and in Petrobras signal the Brazilian government's continued commitment to oil and gas production in the long term.²²

5. BNDES' risks of non-compliance to EIB standards

When looking at the facts, it is difficult to sustain the assumption that by supporting BNDES, the EIB is serving both its climate change and its development mandate. It also remains to be seen whether BNDES, as a major lender and development bank in Brazil, has a comparative advantage in finding clean energy projects that reach the poorest or can really be a game changer. At the very least, the delay in requesting the EIB disbursement shows that scenarios for which projects to finance were apparently not readily available or thoroughly pre-discussed between BNDES and the EIB.

The €500 million CCFL represents less than 1% of BNDES total project commitments of €55.4 billion²³ (in 2011). The EIB can therefore hardly claim to influence BNDES's energy portfolio. One positive effect of this CCFL, however, could be the stimulation of investments in genuine new renewable projects complying with EIB's standards. But serious efforts from the EIB's side are needed to ensure that this actually happens, because it would represent an explicit departure from BNDES's standard practices.

²⁰ http://www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/The_BNDES_in_Numbers/

²¹ A credit limit is the maximum amount of credit that a financial institution or other lender will extend to a debtor for a particular line of credit.

²² <http://www.brazil-works.com/bndes-delivers-up-more-financing-for-hydrocarbons/>

²³ BNDES total commitments in 2011 amounted to R\$139.7 billion (€51.5 billion). The 8 August 2012 exchange rate on www.oanda.com is of US\$1 to €0.3966

5.1 BNDES' safeguards – improving, but not there yet

Since 2008, BNDES has taken a number of steps to improve its safeguards system. For instance, in 2008, BNDES signed a 'Green Protocol' with the Ministry of Environment, in which it agreed to adopt social and environmental criteria, although no clear objectives and deadlines were set.²⁴ At the end of 2009, BNDES restructured its environmental department, which previously had been under the social department, thereby raising the profile of environmental issues within the bank.²⁵

Under a World Bank Development Policy Loan, signed in 2010, BNDES reviewed and extended its safeguards framework. Consequently, in November 2011, the BNDES board approved the Social and Environmental Policy, reaffirming the bank's commitment to sustainable development in the country. This document establishes principles and guidelines for the development and implementation of sustainable policies and practices. The following principles guide the operations of BNDES:²⁶

- Promotion of development of an integrated conception that includes economic, social and environmental aspects
- Respect for human rights as well as combating and opposing all practices that involve any kind of discrimination or violation of rights
- Ethics and transparency as the pillars of relations with all stakeholders, ensuring dialogue and accounting for its decisions and efforts
- Proactive operations aligned with Brazilian standards and public policies, while respecting international norms of behaviour

Sector guidelines have been developed regarding the cattle industry, sugar and *alcohol* (i.e. ethanol) production, and energy generation, but not on hydropower. One major problem with these sector guidelines is that they are only "indicative" and are not included in contractual clauses, nor monitored or controlled.

Although these measures can be considered as steps forward, BNDES' lending in practice shows little regard for its environmental and social impacts. This is illustrated by the bank's financial support for the controversial Belo Monte Dam. Like the Madeira River dams (also funded by BNDES), Belo Monte is expected to have devastating consequences for the ecosystem and its inhabitants, displacing entire communities, threatening food security and biodiversity, and straining already weak social services (see Text Box 1).



Photo: M. Cowan/Survival
<http://www.survivalinternational.org/news/7053>

²⁴ http://www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Hotsites/Annual_Report_2011/Capitulos/institutional_operations/the_bndes_and_the_green_protocol.html

²⁵ Tautz, C., et al. (2010), p.272

²⁶ http://www.bndes.gov.br/SiteBNDES/bndes/bndes_en/Institucional/Social_and_Environmental_Responsibility/

Text Box 1: Belo Monte Dam and Rio Madeira Dam

Belo Monte on the Xingu River (a tributary of the Amazon River) will be the third-largest dam in the world. It is also known as a highly controversial project. Indigenous peoples and social movements in the region have fought its construction for more than 20 years. To build Belo Monte, an area of more than 1,500 square kilometres will be devastated, resulting in the forced displacement of more than 20,000 people and grave repercussions to the land and livelihoods of 800 indigenous peoples and thousands of riverine and urban families. It is clear that the dam developer and BNDES have not complied with the obligation to obtain free, prior, and informed consent by indigenous peoples who will be affected by the project.

On 1 June 2011, Brazil's environmental agency IBAMA approved the installation license for Belo Monte, even though project developer Norte Energia (75% government owned) had not fulfilled the 40 social-environmental project prerequisites that were mandated in 2010. Among other things, 100,000 people are expected to move into the region over the next three years, with potentially grave associated social impacts.

BNDES has pledged to fund at least 80% of the project costs (current estimate R\$26 billion, the equivalent of €9.5 billion) and the remaining 20% is likely to be financed by the Norte Energia consortium. Nevertheless, the financial viability of the project is questionable. While the project will have an installed capacity of 11,233 MW, the dam will be highly inefficient, generating as little as 1,000 MW during the three- to four-month low water season.¹

As the main financier, BNDES plays a significant role in ensuring that the project goes forward. It has already made two initial bridge loans for Belo Monte. Yet clearly, BNDES's safeguards framework did not prevent the aforementioned problems from occurring.

In the implementation phase of the Rio Madeira dams, BNDES applied no process or system to prevent or appropriately mitigate environmental damage and social harm provoked by the projects. When questioned on this issue, BNDES representatives acknowledged the legitimacy of diverse 'viewpoints and perceptions that arise over certain issues', but pointed to the courts as the appropriate theatre in which to deal with claims, adding that BNDES would follow pertinent court rulings. When questioned, the BNDES department responsible for energy projects communicated that while they consider the environment as one of the various dimensions needing particular caution, it carries no more or less weight than others.

This attitude suggests a lack of appreciation for the irreversible nature of many of the issues at stake, and proves insufficient to effectively uphold the safeguard commitments professed by BNDES or even the most rudimentary and fundamental general safeguard principles applying to all financiers, especially the precautionary principle.

Source: Widmer (2012)

In combination with its investments in cattle ranching, soybean plantations and mining, BNDES' funding of the dam positions the bank as an important driver of deforestation in Brazil.²⁷

²⁷ <http://amazonwatch.org/work/bndes>

To summarise, BNDES fails to respect and uphold applicable safeguards in a systematic way. In the cases reviewed in Widmer's 2012 study on BNDES' safeguards system, passive interpretation of safeguards provisions have led to breaches of its own safeguards and failures to uphold relevant legislation. There is no indication that effective internal mechanisms exist to control and correct breaches of safeguards.

One of the underlying problems is the lack of an established tradition of conducting due diligence in Brazil. This must be improved in order to avoid potentially negative consequences of projects. There is also often a problem with the lack of independence of Environmental Impact Assessments (EIAs), which are mostly conducted by the advisory branches of the same engineering companies that are involved in the project's construction. Conditionalities set in the EIA process need to be respected: as long as the identified problems remain unsolved, no license should be given. The reality on the ground in Brazil, however, is currently very different. Brazilian rules for environmental impact assessments (EIAs) are not followed, and BNDES has to take responsibility in this regard.

In addition, as the second biggest development bank in the world, it is remarkable that BNDES refuses to follow even the Equator Principles²⁸. Private and development banks signatory to the Equator Principles commit to carry out socio-environmental assessments in line with the IFC Performance Standards of projects with a size of US\$10 million or more. Major Brazilian banks such as Banco do Brasil, Itaú, and Bradesco have signed the Principles, but BNDES chose not to. It is a discomfiting sign that BNDES, as a public bank, is not even willing to subscribe to principles that would meet the bare minimum under its due diligence obligations. BNDES should actually be willing to go further and follow not only the IFC model on Performance Standards on all projects that it finances, but also the IFC's provisions on transparency and accountability.

5.2 BNDES and transparency

Transparency is an essential building block in enhancing good governance, accountability, and developmental effectiveness. Openness promotes engagement with stakeholders, which, in turn, improves the design and implementation of projects and policies and strengthens development outcomes. It facilitates public information of public banks' operations during their preparation and implementation. This can be beneficial not only by exposing potential wrongdoing and corruption, but also by enhancing the possibility that problems will be identified and addressed in the earliest stages of a project.²⁹

In 2007, BNDES initiated efforts to increase the transparency of its operations. Through its portal *BNDES Transparente*, the bank now discloses a full list, updated at the end of every trimester, of approved projects by sector, although the information it reveals remains very limited: the list³⁰ contains the name of the

²⁸ www.equator-principles.com

²⁹ http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2010/06/03/000112742_20100603084843/Rendered/PDF/548730Access011y0Statement01Final1.pdf

³⁰ http://www.bndes.gov.br/SiteBNDES/bndes/bndes_pt/Institucional/BNDES_Transparente/Consulta_as_operacoes_do_BNDES/setorprivado.html, Consulted on 23 October 2012

client, a very short project description, the state, the date when the contract was signed, and the total amount of the contract. In comparison, the EIB³¹ and other Multilateral Development Banks (MDBs) have adopted more advanced policies, where the projects appear at least three weeks prior to board discussion. At the World Bank's private sector arm, the IFC, disclosure occurs 60 days prior to board discussion for all Category A investments.³² For all other investments, disclosure occurs 30 days prior to Board discussion.³³ Moreover, the World Bank Group and MDBs provide much more information than BNDES in order to give stakeholders a detailed and comprehensive picture of the project. The World Bank's Access to Information policy (2010) is based on the progressive principle of allowing access to any information in its possession that is not on a list of exceptions.³⁴

Thanks to the 2011 Brazilian Freedom of Information Act, it is possible to obtain more detailed information from BNDES upon request. Experiences of Plataforma BNDES³⁵ members, a network of Brazilian civil society organisations created in 2004 to monitor the bank, show that it requires the right skills to ask questions in a highly precise way to get meaningful answers from BNDES. They assert that, like other international development banks, BNDES needs to develop strong safeguards for environmentally and socially sensitive transactions, be much more transparent in how it conducts its operations, and include local communities and other stakeholders in decision making on investments that affect their legitimate interests.

Until now, the willingness of BNDES to provide information in relation to the CCFL has been limited. Although the funds have not yet been disbursed, it can reasonably be assumed that the EIB has approved the CCFL on the basis of a climate change or clean energy strategy. Regrettably, a lack of access to information about what the underlying strategy entails suppresses the opportunity for a public discussion about the best way to use these funds.

5.3 Accountability, including stakeholder engagement, at BNDES

Even though it is a public bank, there is limited accountability with regards to which projects BNDES funds and which sectoral strategies it follows. In Brazil, there is no public discussion on the Treasury allocations to BNDES and, apart from reviews of procurement procedures, there are no external assessments of the bank. The board members, directly appointed by BNDES' president, make all decisions about who should receive which credit lines. The bank refers to secrecy laws to explain the lack of openness and accountability, but it is questionable whether these should be

³¹ http://www.eib.org/attachments/strategies/transparency_policy_en.pdf

³² An environmental and social category is assigned to an investment project after appraisal and before public disclosure during the IFC project/investment cycle: CATEGORY A projects are expected to have significant adverse social and/or environmental impacts that are diverse, irreversible, or unprecedented; CATEGORY B projects are expected to have limited adverse social and/or environmental impacts that can be readily addressed through mitigation measures; CATEGORY C projects are expected to have minimal or no adverse impacts, including certain financial intermediary projects.

³³ http://www1.ifc.org/wps/wcm/connect/corp_ext_content/tobedeleted/what+ifc+discloses

³⁴ <http://documents.worldbank.org/curated/en/2010/07/12368161/world-bank-policy-access-information>

³⁵ www.plataformabnds.org.br/site/

applicable to subsidised finance.³⁶ BNDES lacks well-functioning, open relationships with the people and groups it is designed to serve, a troubled situation leading to frequent conflict around project decisions or during the implementation phase. Whereas consultations with stakeholders can improve policies and projects, BNDES is guarded against any “interference” from civil society.

The proposed mechanism for stakeholders to enter into contact with the bank is through its Ombudsman. While it is commendable that BNDES dedicated a person to deal with questions and complaints, the function does not bring any added value in cases where the bank does not want to disclose information. Consequently, the Ombudsman function, as set up by BNDES, cannot realistically replace an independent complaint mechanism. Given that this mechanism is not yet in place, the only way to oppose BNDES-funded projects is through court cases. But the Brazilian judicial system works very slowly, and is often subject to fraud. Court procedures are therefore unlikely to stop harmful projects. The importance and added value of an accessible and independent complaint mechanism, complementary to existing national redress mechanisms, is illustrated by the systems set up by the World Bank and IFC, where it is relatively easy to lodge a complaint, even for members of affected communities.

6. BNDES’ insufficient compliance to EIB rules

Positive developments, like the elaboration of guidelines for engagement in the cattle industry as well as the inclusive set-up of the Amazon Fund³⁷ can be noted. These changes came about under external pressure and remain very timid first steps in relation to the institution as a whole. Incentives related to the EIB CCFL could, like precedents already mentioned, give BNDES a gentle but necessary push in the direction of more progressive policies on safeguards, transparency, accountability, and stakeholder engagement. For the EIB to engage with BNDES as a financial intermediary, it is absolutely necessary that the EIB can be confident that the principles it commits to are upheld, and the EIB should offer full transparency of the compliance of its intermediaries with its own standards.

On a positive note, the EIB has established a clear commitment to encouraging many of these issues, most notably in its Transparency policy and related guidance notes³⁸ and its Environmental and Social Safeguards.³⁹

³⁶ <http://www.bdlive.co.za/articles/2012/08/02/armando-castelar-pinheiro-brazilian-financial-model-highlights-potential-shortcomings>

³⁷ http://www.amazonfund.gov.br/FundoAmazonia/fam/site_en

³⁸ <http://www.eib.org/infocentre/publications/all/eib-transparency-policy.htm>

³⁹ <http://www.eib.europa.eu/about/news/environmental-and-social-safeguards.htm>

Text Box 2: Main EIB commitments on safeguards, transparency, and public participation

EIB commitment to respect the Aarhus Convention:

As an EU body, the Bank has to comply with specific EU regulations, such as Regulation (EC) No 1367/2006 on the application of the provisions of the Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters to Community institutions and bodies.

http://www.eib.org/attachments/strategies/transparenc_policy_guidance_note_en.pdf

EIB commitments related to transparency:

In its financing operations, the Bank recognises the rights, interests and responsibilities of stakeholders to achieve sustainable outcomes. In this context, the EIB actively promotes transparency with its counterparts including with the development and operations of financed projects. [1.7.1]

Weak governance, corruption and lack of transparency are a major issue in some of the regions in which EIB operates and represent a serious brake on economic and social development. The EIB actively promotes transparency and good governance in the projects it finances, in the companies it participates and generally with its counterparts. [9.2]

http://www.eib.org/attachments/strategies/transparency_policy_en.pdf

EIB commitments related to stakeholder engagement:

The responsibility for information and consultation of local stakeholders on a project basis lies with the project promoter. However, the EIB has issued guidelines to its staff on how to assess stakeholders' concerns during the appraisal of the project. If deemed necessary meetings should be organised, through or in cooperation with the project promoter, with concerned parties to better understand their issues regarding the specific project. [5.5]

http://www.eib.org/attachments/strategies/transparency_policy_en.pdf

EIB Environmental and Social Safeguards:

The EIB's environmental and social safeguard policies are based on the EU approach to environmental sustainability. One of the principles reads as follows: "The Bank is also guided by recognised good international practices, such as those laid down by the World Commission on Dams (WCD) and the Extractive Industry Review (EIR)"

<http://www.eib.europa.eu/about/news/environmental-and-social-safeguards.htm>

Source: www.eib.org; emphasis added by author of this policy note

Moreover, the EU Agenda for change,⁴⁰ a 2011 communication of the European Commission (EC) seeking to increase the impact of EU development policy, also contains a clear commitment to human rights, democracy, and good governance. The following paragraphs are particularly relevant in relation to the CCFL to BNDES:

'Good governance, in its political, economic, social and environmental terms, is vital for inclusive and sustainable development. EU support to governance should feature more prominently in all partnerships, notably through incentives for results-oriented reform and a focus on partners' commitments to human rights, democracy and the rule of law and to meeting their peoples' demands and needs.

As long-term progress can only be driven by internal forces, an approach centred on political and policy dialogue with all stakeholders will be pursued. The mix and level of aid will depend on the country's situation, including its ability to conduct reforms.'⁴¹

The aforementioned EC and EIB commitments should trigger a thorough policy dialogue with BNDES. Serious doubts can be cast as to whether BNDES complies with these EIB commitments, and it is not clear how the EIB will work to ensure that these good practices are 'promoted' by its counterpart. As a minimum first step, the BNDES should be asked to publicly commit to transparency, accountability, and stakeholder involvement with regards to the CCFL.

⁴⁰ http://ec.europa.eu/europeaid/what/development-policies/documents/agenda_for_change_en.pdf

⁴¹ Idem, p.5, emphasis added by author of this policy note

7. Conclusion and recommendations

7.1 Conclusion

Is BNDES a wise and logical choice as an intermediary for the EIB to make a climate change loan in Brazil? This policy brief seeks to answer the following four questions:

- Are EIB climate change investments deployed where they are most needed?
- Is BNDES's development model climate friendly?
- Does BNDES comply with basic EIB rules on stakeholder involvement, accountability, and transparency?
- How can the EIB's CCFL to BNDES contribute to promoting a sustainable energy path?

The EIB's Climate Change Framework Loans are flowing mainly to middle income countries, such as the €500 million CCFL granted to BNDES in Brazil. At the same time there is a huge finance gap, especially for funding adaptation projects. It is unclear whether and how the European Commission ensures that the EIB mandate to finance climate change programmes is coupled with equal commitments to finance adaptation projects through other (non-lending) funding mechanisms. This is important for the Commission to hold up to the UNFCCC commitment to a balanced allocation between adaptation and mitigation. Moreover, BNDES is an institution that in its total portfolio contributes more to climate change than it can help reduce with this loan. This raises the question of whether the real transformational investments needed to counter climate change are being supported by the EIB.

Civil society organisations in Brazil, united in Plataforma BNDES, are concerned about the development model BNDES promotes and the lack of civil society dialogue sought by the bank. BNDES's model relies heavily on the unsustainable use of Brazil's natural resource base, the concentration of land and power in the hands of the few, and exporting raw materials without supporting processing industries in Brazil.

This situation is a clear challenge to the EIB's choice to support BNDES' alternative energy sector. As long as it is not clear how the EIB loan fits into a broader BNDES strategy, the suspicion remains that the EIB's money merely fills a gap and thereby creates more room for BNDES to proceed on a controversial energy path that has been designed by the Brazilian government. It is a discomfoting sign that BNDES is not willing to discuss this important question in an open dialogue with civil society and the EIB.

What is striking about BNDES's energy strategy for Brazil, designed in close cooperation with the Brazilian government, is that it relies heavily on hydropower development in the Amazon. This region symbolises Brazil's struggle to break away from unsustainable patterns of economic growth. The investments in large dams in this region run the risk of actually further contributing to climate change through deforestation and methane emissions, as well as having negative social, environmental, and human rights impacts. For that reason, it is crucial to ensure

that due diligence and accountability mechanisms are in place, which is not guaranteed in the case of BNDES.

In sum, this CCFL to BNDES is not in line with the EIB's commitments to transparency, accountability, and stakeholder participation, nor is BNDES a transformational actor in Brazil which can show that it contributes to changing the country's course in supporting a sustainable growth path.

Both ENDS and its partner organisations in Brazil therefore contend that the EIB should set stringent conditions on the Climate Change Framework Loan to BNDES in order to ensure that this loan does not simply allow BNDES to show a greener face while continuing business as usual. The only positive role the EIB can play at this stage, besides ending the loan, is to contribute in a positive way to a dialogue on changing the course of BNDES's larger portfolio.

7.2 Policy recommendations

In view of the challenges described in this policy note, we make the following recommendations to the EIB and the European Commission:

To the EIB

On EIB loans in general:

- Improve the selection of financial intermediaries, ensuring that their sector policies are in line with the purpose of the EIB loan.
- Commit to imposing basic EIB standards in relation to safeguards, transparency, accountability, and stakeholder engagement on financial intermediaries with which the EIB works.
- Sharpen its definition of clean energy in compliance to the EU's Energy for all ambitions – clearly formulate the target group and make very careful assessments in the case of dams and biomass/ethanol.
- Apply more care in ensuring civil society participation in Europe and the receiving country in the stage prior to signing a loan agreement with a financial intermediary.

On the CCFL to BNDES:

- First and foremost, stimulate national debate about BNDES's lending in relation to climate change, the way the CCFL is used, and how it fits into the broader BNDES strategy on climate change and sustainable development.
- Make disbursement of the loan dependent on the clear publication by BNDES of the social, environmental, and legal safeguards it demands to be in place before funding projects.
- Ask BNDES to publish all the projects that are funded under the CCFL, providing information about the EIAs and stakeholder participation in decision-making.
- Ensure that the EIB CCFL is not used for projects that have harmful social and environmental effects or even contribute to climate change.

- On the model of its role in the creation of national champions in various industrial sectors, suggest that BNDES could play a similar role in the sector of sound clean energy.
- Ensure that BNDES's guidelines to the electricity sector, including hydropower projects (which will most likely receive funds from the EIB Framework Loan), are operational and public.

To the European Commission

- Make it clear how EIB climate change programmes (loans) are complemented by equal commitments to adaptation projects based on grants and how European commitments under UNFCCC to a balanced allocation between adaptation and mitigation are upheld.

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