Open Letter to World Bank Group Executive Board Members
Legal issues concerning the IFC/MIGA draft Approach to Remedy

The International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) are poised to enter an environment of heightened, diverse, and uncertain risks. The World Bank's Evolution Roadmap expects the IFC and MIGA to be more active and increase their financial and non-financial risk appetites in an increasingly demanding range of operational settings. To ensure that the proposed reforms put the institution on the path of enhancing rather than undermining development impact, IFC and MIGA must adopt a robust remedy framework to ensure that communities are not left as sole bearers of any negative externalities and harms of the projects. The recently published draft IFC/MIGA "Approach to Remedy" falls well short in this regard, as many commentators have already noted.

In 2020, the External Review of the International Finance Corporation (IFC)/Multilateral Investment Guarantee Agency (MIGA) Environmental and Social Accountability framework (the "External Review") recommended that the IFC/MIGA adopt a new remedy framework pursuant to which IFC/MIGA clients would be required to set aside resources to remedy instances of noncompliance with IFC/MIGA's environmental and social standards. The External Review also recommended that the IFC/MIGA should itself contribute to the remedy, where there was a finding by the Compliance Advisor Ombudsman (CAO) or by IFC/MIGA management of IFC/MIGA non-compliance that contributed to harm. Unfortunately, however, the IFC/MIGA's recently published Approach to Remedial Action has effectively rejected this suggestion. Apart from a passing reference to possible 'exceptional circumstances' in which remedies might be contemplated, the IFC/MIGA's proposed approach relies on a static delineation between a lender's and client's roles and asserts, without satisfactory explanation or substantiation, that there are concerns about litigation risks, moral hazard, and cost.

This rejection by the IFC/MIGA of virtually any meaningful remedial responsibility is deeply problematic, particularly where IFC/MIGA are considering investing in or guaranteeing higher-risk ventures. Like many public international organizations, the IFC/MIGA enjoys privileges and immunities which generally shield them from lawsuits in domestic courts. This means that in most of the IFC/MIGA's financing arrangements, the non-financial risk – including the risks of environmental, social, or other harms - is borne by its clients and any others who may be harmed by an investment. And while the IFC/MIGA in the recently published *Approach to Remedy* made vague reference to "theories of liability" as a basis for rejecting virtually all responsibility for or contribution to remedy, it is unclear what theories it has in mind. It is possible that the IFC/MIGA are implying that their relationship vis-à-vis clients is similar to the commercial relationships between Investment Funds and their portfolio companies. Courts and regulators have occasionally (and often under specific statutes) held investors liable for the actions of portfolio companies where the investors' conduct was so closely intertwined with the portfolio company as to justify this allocation of responsibility. However, the suggested comparison between the IFC/MIGA-client relationship and a purely commercial relationship is quite inapt for the following reasons.

- First and foremost, unlike market actors, IFC/MIGA are *primarily* development organizations and, as such, cannot be motivated solely by the pursuit of commercial profit. This development focus is not only key to how IFC presents itself externally—as "the largest global

development institution focused on the private sector in developing countries"—it is also clear in its Articles of Agreement which center development as the organization's key purpose.

- Second, even in the wholly commercial context, the risk of harm is not outsourced as the IFC/MIGA seeks to do. In the context of commercial asset management, where statute or equity concerns require, non-financial risks such as the risk of harm to third parties is potentially allocable between the investors (who are analogous to the IFC) and portfolio companies (analogous to IFC clients), depending on the level of respective contribution to the resulting harm. Thinking along these lines, the European Commission has proposed EU legislation on Corporate Sustainability Due Diligence, which would impose civil liability for failure to prevent and mitigate potential adverse human rights impacts and adverse environmental impacts, where the adverse impact has occurred as a result of such failure and has led to damage. Responsibility for harm is thus not externalized entirely onto the consumers, workers or other affected constituencies or communities outside of investors and the companies. In contrast, the IFC/MIGA's proposed approach to remedy would transfer the risk of harm entirely onto such affected third parties who often have no input or say in relation to the investment.

- Third, because of the IFC/MIGA's development mandate, they often guarantee investments or invest in areas where relevant regulatory frameworks for safeguarding against harms to people may be weak or under-developed (see e.g. the recent complaint to the CAO regarding the practices of six banks or microfinance institutions in Cambodia that are linked to 18 active IFC projects). In those instances, the risk of harm is even higher and the portfolio companies or IFC borrowers operating in such jurisdictions are unlikely to assume the risk of non-financial harm or to provide remedies to those harmed.

IFC/MIGA speculate in the *Approach to Remedy* that more actively contributing to remedies would fuel moral hazard concerns by removing incentives from clients and borrowers to undertake mitigation and remediation efforts themselves. This concern seems to be overstated as there are different ways to structure transactions that can ensure client performance, including through contractual leverage. Furthermore, the far greater moral hazard problem is the fact – and not mere speculation – that harms are routinely being externalized onto communities and individuals with no control over, and often no say in the project in question. By refusing to accept almost any responsibility for remedies, the IFC/MIGA would effectively leave people who are adversely affected by a problematic investment to bear the cost of the harm, particularly where the client has not taken adequate remedial action. This would not only violate the "do no harm" principle but risks undermining the development impact of IFC/MIGA's projects.

The argument is not that IFC/MIGA should in all circumstances bear the cost of all losses, but rather that they should be willing to contribute to the establishment and creation of appropriate remedies for harm caused by their investments. Even when IFC/MIGA conduct has been exemplary, a strong argument can be made that IFC/MIGA should contribute to remedial action where the intended development impact would otherwise be substantially compromised. As the UN Office of the High Commissioner for Human Rights has pointed out in its Remedy Report, discretionary contributions going beyond the harm for which the development bank itself is directly responsible could take account of other relevant circumstances including the setting of Fragile and Conflict-affected States, or the complexity of the financing structure of the investment in question. Such an approach would

incentivize the achievement of sustainability objectives, prevent repeat of past mistakes in subsequent projects, enhance the institutional credibility and legitimacy of IFC/MIGA, and further their development aims.

To the extent the IFC/MIGA is concerned about litigation risks, it is true that the immunity from domestic lawsuits is not absolute (see *JAM v. IFC*). However, the IFC/MIGA's outright refusal in most circumstances to accept any responsibility for remedying project harm, especially where the IFC has contributed to that harm either by action or by failure to prevent it, is more likely to lead to increased challenges to the IFC/MIGA's immunities, and possibly to an increasing likelihood that some courts will lift or limit those immunities. By contrast, if the IFC/MIGA were willing to provide or contribute to a meaningful remedy for harms flowing from its investments, this would be more likely to decrease its litigation risk, especially in those jurisdictions in which organizational immunity is balanced against the right to remedy (see, e.g., the European Commission's Proposal for a Directive on Corporate Sustainability Due Diligence, Article 22 on civil liability). While the future applicability of this kind of EU legislation to financing remains under debate, the direction of regulation in Europe is clear, and the link between institutional efforts to take appropriate remedial action and a relaxation of potential liability is evident. Meaningful remedy is not the same thing as legal liability – quite the contrary. If IFC/MIGA were willing to contribute significantly to the creation of appropriate remedial action, it would be more likely to ward off and hence reduce the risk of its own legal liability. In fact, when banks have contributed to remedies in the past (for example, the World Bank-supported Uganda Transport Sector Development Project, and in the case of a commercial bank, ANZ Cambodia), their actions were positively received by the affected communities and there had been no accompanying increase in litigation claims or claims to the institutional accountability mechanisms.

Informed observers, including the External Review, the UN Human Rights Office, and civil society organizations have suggested a number of options for mobilizing and apportioning resources to be earmarked for remedies, including a requirement for clients to set aside their own resources and a provision for contractual indemnification. Where the IFC lends through a syndicate, co-lenders could also be expected to contribute to a remedy fund since they enjoy both preferential creditor status and the benefits of the IFC's immunity. The IFC could also consider using an Equity Commitment Letter delineating conditions under which the client can call on the IFC to contribute capital to be used towards remedying harm. In this way, the IFC can condition contribution, among other things, on the client undertaking all efforts to prevent and mitigate harm *ex ante*. Other innovative mechanisms could also be considered if the IFC/MIGA were open to a genuine public discussion, rather than closing off any suggestion that it should be responsible for remedying harm caused by its investments.

The world is at cross-roads. The aftermath of Covid-19, the ongoing war in Ukraine, climate change, and rapidly evolving technologies are complicating the already sluggish pace towards the fulfilment of the Sustainable Development Goals. Geopolitical tensions and growing unhappiness with the current practices of MDBs in developing economies call for serious and even existential reflection about the role of these institutions. At the same time, this is also a moment of opportunity to rethink the frameworks that would shore up and enhance IFC/MIGA's contribution to positive development outcomes.

We use this occasion to remind the leadership and officials of the IFC/MIGA and their peer institutions that they are not just commercial entities, but public institutions created to serve not only their shareholders but also the peoples whose economic and social wellbeing they were established to improve, and whose development freedoms they are meant to enhance. Indeed, one of the expected

and value added contributions of the IFC/MIGA is their contribution to mitigating noncommercial risk (see, e.g., according to recently issued report by the Independent Evaluation Group on the International Finance Corporation Additionality in Middle-Income Countries, noncommercial risk mitigation represented 30% of IFC's nonfinancial additionalities). Any reform of the MDBs must include reforms to their institutional frameworks with the aim of maximizing development outcomes while minimizing and mitigating risks, and remedying harm to communities whose economic and social development underpins the mandate of MDBs.

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Given lack of publicly available information from the IFC/MIGA on the legal issues outlined above, we invite the Executive Board Members of the World Bank Group to ask the IFC/MIGA the following questions about its refusal to accept the External Review's recommendation that it adopt a robust remedy framework and contribute to remedy, as appropriate:

1. **Theories and potential costs associated with litigation risk.**
    a. What are the bases and legal theories that underpin IFC/MIGA's position that contributing to remedies would increase litigation risk?
    b. Has the IFC/MIGA already encountered legal challenges in similar contexts?
    c. Is it aware of legal risks materializing for other MDBs?
    d. If so, what is the cost associated with legal exposure as compared to the overall value of the portfolio?
    e. How do these legal risks associated with provision of remedies compare (in value and otherwise) to other litigation risks, for example in the context of corruption or money laundering?

2. **Existing litigation costs**. The IFC/MIGA's draft remedy paper states that "[c]urrently IFC allocates the amount of $15 million annually to cover legal costs associated with litigation cases." What percentage of this cost is used to address potential claims or concerns related to environmental and social harms (or otherwise harms resulting from breaches of IFC/MIGA's Performance Standards), on an annual basis? Historically (e.g., ten-year trend)?

Signed on June 5, 2023 by:

Victoria Adelmant, Adjunct Professor of Clinical Law, New York University
José Alvarez, Herbert and Rose Rubin Professor of International Law, New York University
Kristen Boon, Professor of Law, Ottawa University
Christine Chinkin, Emerita Professor of International Law, LSE Law School
Philipp Dann, Professor of Public and Comparative Law, Humboldt University Berlin
Gráinne de Búrca, Florence Ellinwood Allen Professor of Law, New York University
Angelina Fisher, Adjunct Professor of Law, New York University
David Kinley, Professor of Human Rights Law, University of Sydney Law School
Jan Klabbers, Professor of International Law, Helsinki University
Katerina Linos, Professor of Law at the University of California, Berkeley