

Implications for social and

Project financing from banks can be one means of funding a mine development, but as more financial institutions sign up to the Equator Principles, companies need to be aware of the environmental standards they will be required to meet

BY FIONA CESSFORD

IN THE current economic climate, funds are not always available to enable exploration or develop projects into going concerns without obtaining project finance. Although the need for external financing may not be welcome to many proponents, it has the potential to positively influence the likelihood of success. Depending on the lender, the successful integration of project finance requirements will facilitate schemes being developed, operated and closed in a socially responsible manner.

By reflecting sound environmental-management practices, a project is likely to enjoy significant cost savings in the long run. This integration will improve the chance of obtaining approval from the first three key decision makers: the board, on behalf of its shareholders; relevant host country governments, and any lenders. Adherence to project-finance requirements can also increase the chance of the project proponent obtaining its critical, fourth approval in the form of a social licence to operate.

TYPES OF PROJECT FINANCE

There are three main ways in which a company can get finance for a new project: self-funding; debt financing or raising equity. All of these can influence the scope of the environmental and social process, although the method and extent of influence will vary. In all cases, the mining company will have to comply with the legislation of the host country in which it wants to operate. International laws and norms may also apply, depending on which treaties or conventions the country has signed up to.

In cases where the company puts up the money itself, it will only have to adhere to its own corporate standards and any international standards it has signed up to. However, if debt financing against either the project or the company is required, the implications for the project will be a consequence of the choice of lender. This is particularly relevant if the lenders are signatories to the Equator Principles, which are a set of environmental and social standards that projects must adhere to in order to receive financing from the lender.

In a case where public equity is raised by listing on a stock exchange or seeking equity from individual investors, any additional, environmental or social requirements will vary, depending on which exchange is used or what the private investor is interested in. Private investors may expect companies to show compliance with the investor's own standards or various international standards before agreeing to invest. From an environmental and social perspective, however, debt financing potentially has the biggest implications for the environmental and social assessment process.

THE DECISION MAKERS

The decision-making processes may run in parallel, and one party's point of decision making may influence the decision points of the other parties. For example, some developers will only approve a scheme for implementation once the licence or permit has been obtained from the relevant regulator(s).

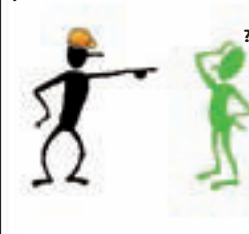
The 'deliverables' required for each decision will vary, depending on the decision maker, potentially forcing the company to generate a multitude of deliverables with different aims and objectives. In the case of financial institutions, the deliverables required will be a function of their risk profile and investing strategy. The risk is managed through the different stages of the lending process; for example, agreement on the loan, drawdowns and completion. These do not necessarily tie in with the generally accepted project-development stages (concept, pre-feasibility, feasibility, detailed design, construction). If not carefully managed, the deliverables can end up with inconsistent or confusing information.

February 2009 there were 65 signatories and the number is increasing, indicating the significance that lenders are assigning to the appropriate identification and assessment of environmental and social risks.

The Equator Principles require projects (with capital costs of greater than US\$10 million) that are likely to have significant environmental or social impacts to undertake a comprehensive assessment. This must be accompanied by thorough stakeholder consultation and disclosure. To support the EPFI's due diligence process, this assessment must be reviewed independently and there must be independent monitoring, review and reporting during project implementation. The proponent must also make covenants to comply with host country laws, implement and comply with specific action plans indicated by the assessment process and, of particular importance to mining projects, decommission facilities in accordance with an agreed plan.

With many mining projects being developed in emerging markets, it is important to note that for

1990s: project engineers said to environmental specialists "here's the project, get it permitted ASAP!"



2000: it changed to "just give us the environmental and social criteria, and we'll design the project to conform"



2010: aim to have "please join us to design a project that will work technically, economically, environmentally and socially"



To minimise the risk of inconsistency, it is incumbent on the company to understand all of the decision-making processes, and how these may influence the environmental and social work it needs to undertake to enable decisions to be made. Generally, the company will be well versed in the requirements for a feasibility study and is likely to be familiar with the environmental and social impact assessment processes needed to obtain regulatory approval. The company may be less familiar, however, with how its choice of lender could influence these studies.

LENDER REQUIREMENTS

Probably the most significant changes associated with the environmental and social requirements of project finance have arisen with the introduction of the Equator Principles in June 2003. Updated in July 2006, these state that Equator Principle Finance Institutions (EPFIs) will ensure they only provide finance to projects that are developed "in a manner that is socially responsible and reflect sound environmental-management practices".

The implication is that an appropriate assessment of the environmental and social risks and opportunities needs to be undertaken to ensure the project's value takes full cognisance of any associated costs. In

non-high income OECD countries the Equator Principles require the assessment to refer to the 2006 Performance Standards of International Finance Corp (IFC) and the General and Sectoral Environmental, Health and Safety Guidelines of the World Bank (the latest versions were published in 2007-08). These standards and guidelines go on to make further reference to various international standards and guidelines from other organisations, such as the World Health Organization, International Labour Organization, International Panel on Climate Change, International Union for Conservation of Nature, International Organization for Standardization, and the International Council on Mining and Metals. In most cases the requirements of these various standards and guidelines will be more onerous than the relevant host country legislation.

Although the assessment process described in the IFC's Performance Standards still follows the basic concept of screening, scoping, baseline studies, impact assessment and management planning, it has placed increased emphasis on areas such as consultation and disclosure, community issues like resettlement and land acquisition, indigenous people and the community, health and safety, and human rights and security.

environmental assessment

These aspects need to be fully integrated with more traditional environmental issues such as pollution prevention, and control and biodiversity. Emphasis is also placed on ensuring all stages of project development, from construction to post-closure, are fully considered in the assessment. The required performance standards go beyond the traditional assessment process by requiring the project proponent to show how the management of identified impacts will be implemented in practice. This means the financial and human resources needed for implementation must be clearly described in the project documentation and allowed for in costings.

PROJECT IMPLICATIONS

So, what does this mean for new projects? Basically, environmental and social studies will need extra planning, resources and time. SRK's experience, in both undertaking environmental and social assessments and reviewing them on behalf of EPFIs, shows the involvement of the relevant specialists early in the project development process can result in significant cost savings. Clear changes in the attitude of project developers have been apparent over the last decade, but there is still room for improvement. Some of the benefits of early involvement of specialists are listed below.

Certain environmental baseline studies will require at least one full year of data collection to cover all seasonal changes, and in some climates even more data may be required. Therefore, these studies may need to start as early as the exploration stage to ensure sufficient data is collected as input to the impact assessment without affecting the project development schedule.

Early start of baseline studies and stakeholder consultation can ensure the environmental and social criteria are taken into account during project

FOUR KEY DECISIONS

Where debt financing is needed, these decisions are required before the project can go ahead:

- **Go/No Go decision** – project developers, including the design team, future operations management team and shareholders, need to determine if the project is economically and technically feasible. This decision will be influenced by the risks and opportunities posed by the environmental and social consequences of the project.
- **Permitting approval** – the responsible government authority will decide whether to approve the project and what conditions of approval to impose on the project developer.
- **Loan agreements** – financiers need to understand the risks associated with their possible investments.
- **Social licence to operate** – other stakeholders, including local communities, will seek to understand the development proposal, and the impacts on the community/environment.

development, so there are no nasty surprises after engineering designs are completed. This could potentially result in the most significant cost-savings since the lining of tailings dams or the addition of abatement technologies could have material implications on project feasibility.

Assessment studies will need certain project information to enable accurate evaluation of impact significance. If this can be provided on an ongoing basis during development, rather than waiting for the feasibility study to be completed, the assessment process can, at least partially, be run in parallel with other work. This will reduce the risk of discrepancies between the feasibility-study project description and that described in the environmental impact

assessment report. In the long run, this may prevent the need for addendums to the environmental reports, saving money and reducing schedule overruns.

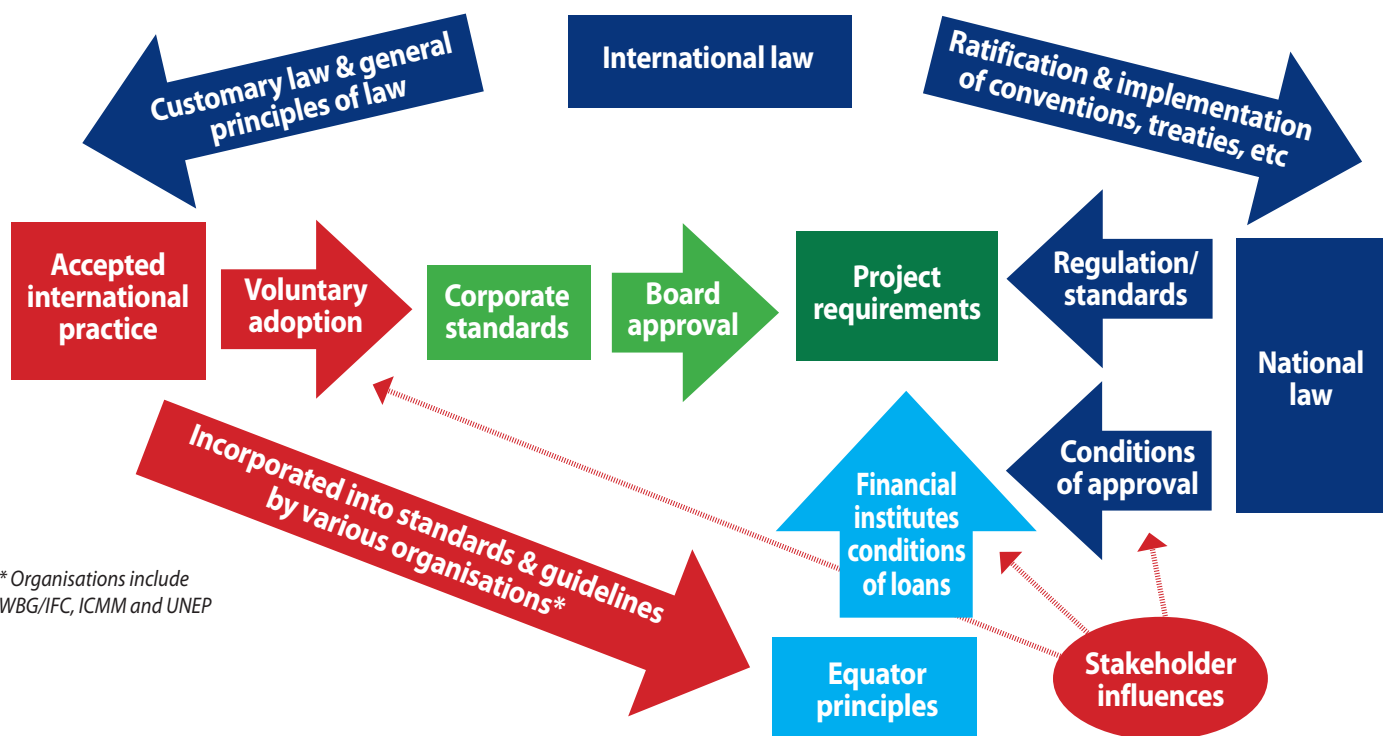
Careful planning during project development may reduce the time between approval decisions being made and the ability to implement the project. For example, if resettlement is needed to enable project construction then early planning, consultation and disclosure of the resettlement action plan is likely to facilitate the relocation process if the project proceeds.

To satisfy an independent reviewer working on behalf of the EPFIs, the firm will need to show that the environmental and social management requirements identified by the assessment process have been incorporated into the financial model. These can be as capital, operational or closure costs.

For risk situations where there may be uncertainty about whether or not the risk will occur, the company can undertake a sensitivity analysis using best case, worst case and expected case costs to determine if the risk could materially affect the project's overall value. If the costs and sensitivities are clearly spelled out in the feasibility study, there is less risk that lenders will demand additional deliverables to cover these aspects.

Although the need for project financing may not be welcome to many project proponents, it has the potential to positively influence the likelihood of success by ensuring environmental/social risks and opportunities are fully understood and integrated into the overall plan. The influence of project finance, particularly from EPFIs, is seen as a 'good thing', enabling generally accepted international practice to be applied wherever mines are developed.

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* Organisations include WBG/IFC, ICMM and UNEP