The Global Environment Facility and the Search for Financial Strategies to Foster Sustainable Development

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During the decade of the 1990s, the financial context for global environmental issues has undergone a dramatic transformation. National foreign aid programs have declined markedly, while private investment in developing countries has increased sharply. At the same time, financial assistance to developing countries has been included as an important feature of treaties to protect the ozone layer, conserve biological diversity, and mitigate climate change, with ongoing negotiations to address persistent organic pollutants (POPs) and biosafety.

One important development in the evolution of targeted environmental aid has been the creation of the Global Environment Facility (GEF). The GEF is the financial mechanism for the Conventions on Biodiversity and Climate Change and has programs addressing land degradation, ozone depletion, and POPs. From 1991 to June 1999, the GEF committed $2.5 billion in grants to more than 100 countries. The growth of the GEF and other environment-related financial assistance programs raises both opportunities and challenges. This article consists of three parts. Part I presents an overview of investment trends in developing countries over the past decade, particularly with respect to the relative increase in the importance of private sources of financing. Part II presents the background, governing structure, and operational strategies of the GEF. Part III discusses some emerging issues with respect to dedicated environmental financing and the potential to effectively influence private investment to advance environmental objectives.

I. FINANCIAL FLOWS AND DEVELOPMENT: A NEW CONTEXT

"*Show me the money.*" Jerry Maguire[1]

During the 1970s and 1980s total foreign aid from industrialized to developing countries increased steadily, peaking at $69 billion in 1991.[2] However, total aid has since declined about one third in real (inflation adjusted) terms.[3] All major donors experienced the same trend. In 1997, U.S.

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1. JERRY MAGUIRE (Sony Tri-Star 1996)

2. *See* WORLD BANK, ASSESSING AID: WHAT WORKS, WHAT DOESN'T, AND WHY 7 (1998) [hereinafter ASSESSING AID]. The 1991 amount is in 1995 dollars.

3. *See* UNITED NATIONS DEVELOPMENT PROGRAMME, HUMAN DEVELOPMENT REPORT 30-31

bilateral aid was only 0.08 percent of the Gross National Product (GNP), amounting to about $7 billion compared with $14 billion given by the largest donor, Japan.[4]

According to a World Bank analysis, there are three primary reasons for this trend: fiscal problems in the industrialized countries; "the end of the Cold War; and the dramatic growth in private capital flows to developing countries."[5] While the effects of the first two factors were one-time events, the third is an ongoing, dramatic development. Prior to 1990, private investment in developing countries was only about one-half of financial flows from north to south.[6] By 1998, private capital flows exceeded $220 billion and constituted almost 90 percent of funds entering developing countries.[7]

The environmental implications of this trend are controversial and yet to be fully understood.[8] Two closely related phenomena, the rise of international trade and the increasing role of transnational corporations, have generated the most intense criticism.[9] The sheer magnitude of investment reflects a scale effect with positive and negative potential. Used wisely, this level of expenditure could be of enormous benefit. In 1992, the United Nations Conference on Environment and Development estimated that sustainable development financial needs in developing countries were on the order of $125 billion per year, substantially less than average annual Foreign

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(1999).

4. *See* ASSESSING AID, *supra* note 2, at 7; DAVID HUNTER ET AL., INTERNATIONAL ENVIRONMENTAL LAW AND POLICY 1459 (1998) [hereinafter HUNTER].

5. *See* ASSESSING AID, *supra* note 2, at 7.

6. *See* ASSESSING AID, *supra* note 2, at 7-8.

7. *See* HILARY FRENCH, VANISHING BORDERS: PROTECTING THE PLANET IN AN AGE OF GLOBALIZATION 6 (2000). While foreign investment in developing countries is often discussed in aggregate terms, the term encompasses several different types of investments. The most important categories include the purchase of previously public assets like utilities; purchase of privately held companies or assets; new business ventures; loans to domestic enterprises; and the purchase of securities issued by local firms. *See* WORLD BANK, ENTERING THE 21ST CENTURY, WORLD DEVELOPMENT REPORT 1999/2000 6-7 (1999) [hereinafter 1999/2000 REPORT]; Stephan Schmidheiny & Bradford Gentry, *Privately Financed Sustainable Development*, THINKING ECOLOGICALLY 118-20 (Marian R. Chertow & Daniel C. Esty, eds., 1997). About 40 percent of global foreign direct investment is going to developing countries or countries with economies in transition. Some of these investments are associated with long-lived durable investments like factories that cannot be withdrawn quickly, while others, like investments in securities, can be withdrawn quickly and without warning as perceptions of risk change.

8. *See generally* FRENCH, *supra* note 7; 1999/2000 REPORT, *supra* note 7.

9. From 1950 to 1998 world exports increased 17 times to $5.4 trillion compared with a six-fold increase in global GNP. From 1970 to 1998 the number of transnational corporations rose from 7,000 to over 53,000. Sales of such companies outside their home base are growing substantially faster than their exports, and sales by foreign subsidiaries substantially exceed world exports. International mutual fund assets, another measure of investment trends, grew from $16 billion in 1986 to $321 billion in 1996. *See* FRENCH, *supra* note 7, at 6. *See generally* WILLIAM GREIDER, ONE WORLD, READY OR NOT: THE MANIC LOGIC OF GLOBAL CAPITALISM (1997).

Development Investment (FDI) over the past decade.[10] There is also little doubt that much foreign investment has been associated with the installation of technologies that are cleaner and more efficient than those used locally.[11] A minority but growing number of transnational companies have policies that require all their factories to achieve environmental performance comparable to their American and European plants.[12] While some companies have eliminated pollution-intensive activities by selling off subsidiaries, others actively manage their procurement to promote good environmental practice through every stage of the products they make.[13]

On the other hand, the risks of adverse consequences from growing FDI are also supported by experience. In some countries, investment has been concentrated in resource-extractive industries with relatively greater environmental costs. Developing countries are the main exporters of natural resources, and the environmental and social costs of mineral extraction and related activities can be high even when relatively strict controls are applied.[14] At least some governments of developing countries have also decided that lax environmental regulation is a helpful strategy for attracting foreign investment in manufacturing.[15] Governments also sometimes adopt distortive policies as conditions or inducements to foreign investment (e.g., requirements that producers use domestic goods and services or trade barriers against competitive imports) that may outweigh the societal gains.[16]

Finally, the rise in FDI may be socially and environmentally beneficial, but the flow of investment dollars tends to be limited to a handful of countries.[17] More than 80 percent is going to about twenty countries, and

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10. *See* HUNTER, *supra* note 4, at 1459; Schmidheiny & Gentry, *supra* note 7, at 118-119

11. *See* Fredrik Sjoholm, *Technology Gap, Competition and Spillovers from Direct Foreign Investment: Evidence from Establishment Data*, 36 J. DEVELOPMENT STUD. 53 (1999); Muthukumara Mani & David Wheeler, *In Search of Pollution Havens? Dirty Industry in the World Economy 1960-1995, in* TRADE, GLOBAL POLICY, AND THE ENVIRONMENT 115, 127 (Per G. Fredriksson, ed., 1999); Alan S. Miller, *Externalities, Technology, and Sustainable Development*, 3-FALL WIDENER L. SYM. J. 287, 293 (1998). This effect is most likely to be evident when FDI is linked to the manufacture of internationally traded goods, which must be able to meet the highest standards in any likely market. In this case, the most stringent standards followed in major markets can drive standards all over the world. *See id.* at 296-97; TONY BRENTON, THE GREENING OF MACHIAVELLI: THE EVOLUTION OF INTERNATIONAL ENVIRONMENTAL POLITICS 246 (1994). Thus, for example, computer companies buying components made in Taiwan, Thailand, and Singapore pushed these countries to phase out their use of ozone depleting chemicals so that the final products would not have to be labeled or restricted for sale in the industrialized countries.

12. *See* HUNTER, *supra* note 4, at 1385-1409.

13. *See* LIVIO D. DESIMONE & FRANK POPOFF, ECO-EFFICIENCY: THE BUSINESS LINK TO SUSTAINABLE DEVELOPMENT 131-33 (1997).

14. *See* FRENCH, *supra* note 7, at 15-28.

15. *See id.* at 84-85; HUNTER, *supra* note 4, at 1222-24, 1270-74.

16. *See* 1999/2000 REPORT, *supra* note 7, at 82.

17. *See* UNITED NATIONS DEVELOPMENT PROGRAMME, HUMAN DEVELOPMENT REPORT 30-31(1999); WORLD BANK, GLOBAL DEVELOPMENT FINANCE 1999 47-80 (1999).

within those countries, a relatively small percentage of the population often receives the vast majority of available financial benefits.[18] More than 100 countries receive less than $100 million per year. Success in exports is, moreover, no guarantee of economic growth or improved quality of life. For example sub-Saharan African countries maintain a high export-to-Gross Domestic Product (GDP) ratio due to an emphasis on export of primary commodities. Nevertheless, they have low growth economies.

Analysis of the environmental implications of these trends is likely to be an ongoing debate for some time. However, there can be little doubt about their importance. To be successful, environmental financing strategies will have to find ways to influence the flow of private dollars to a wider range of countries and in a more environmentally beneficial direction. In addition, given the relatively greater magnitude and growth in FDI, it is apparent that successful public sector strategies will require a high degree of leverage from limited aid dollars. These criteria will increasingly be the measures of success for government sponsored environmental financing.

II. THE GLOBAL ENVIRONMENT FACILITY

"The United States is still highly resistant to initiatives that would involve significant new funding although there seems to be a growing acknowledgment of the principle that additional funding will have to be made available to developing countries to obtain their cooperation in dealing with global environmental concerns."[19]

A. A Brief Historical Review of the Creation of the GEF

International discussion of financial assistance to developing countries for global environmental protection can be traced back to at least the 1972 United Nations Conference on the Human Environment.[20] However, it was arguably the 1987 report of the World Commission on Environment and Development, *Our Common Future,* the so-called Brundtland Report, that first gave the issue prominence.[21] While the report is most often cited for its

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18. The inequity is less when investment is measured as a percentage of economic activity, and in the last few years the distribution of investment dollars has increased with a greater tolerance of risk among investors. Miller, *supra* note 11, at 292.

19. Memorandum from Maurice Strong to Mr. William Draper, Administrator, U.N. Development Programme (Sept. 11, 1989), *in* HELEN SJÖBERG, FROM IDEA TO REALITY: THE CREATION OF THE GLOBAL ENVIRONMENT FACILITY 14-15 (Global Env't Facility Working Paper No. 10, 1994) [hereinafter SJÖBERG I].

20. *See* SJÖBERG I, *supra* note 19, at 3; HUNTER, *supra* note 4, at 1458-60.

21. *See generally* WORLD COMMISSION ON ENVIRONMENT AND DEVELOPMENT, OUR COMMON

focus on defining sustainable development, the authors also cite the need for a "significant increase in financial support from international sources."[22] While avoiding quantified estimates of financial need and identification of specific institutions as sources of aid, the report initiated serious discussion of how revenue might be generated and channeled.[23] As one authority observed, "[t]here can be no doubt that the Bruntland Report inspired and legitimized the proposals for environmental financing mechanisms that followed. Over the next two years, many proposals were put forward, varying widely in quality, purpose, and political realism."[24]

The period immediately following the Bruntland Report was marked by intense political debate on the scope, magnitude, and institutional approach to dedicated international environmental funding.[25] One of the most important questions was where such a fund might be placed. The World Bank was one logical candidate based on its lead role in development lending and its creation of a central Environment Department for the first time in 1987. However, the concept faced resistance within the Bank from those who viewed it as contrary to a policy against dedicated funds, as well as from others who thought the Bank should not be viewed as advocating new missions. Cite? At the same time, two U.N. agencies with mandates related to the environment, the U.N. Development Programme and UN Environment Programme, felt they should be involved in any environmental fund.

The political support for an environmental fund coalesced in 1989, mainly from Europe, and framed around transboundary and global issues.[26] The issue of stratospheric ozone depletion mobilized public attention and became the subject of a 1987 agreement, the Montreal Protocol on Substances that Deplete the Ozone Layer. Country proposals were shaped by differing political concerns; the French government, for example, had a particular need to enhance its environmental reputation.[27] A common donor concern was that any aid be channeled through existing institutions, although there was no consensus on the identity or number of such organizations to be involved.

FUTURE (1987) (the Report's informal names comes from the Commission's chairperson).

22. *Id* at 336.

23. *See id.* at 336-41.

24. SJÖBERG I, *supra* note 19, at 4.

25. This discussion is based on Sjoberg's *From Idea to Reality*, which provides a remarkably candid and detailed account of the players and negotiations during this period. *See generally* SJÖBERG I, *supra* note 19.

26. "The buildup of political interest manifested itself in a host of conferences, declarations, and proposals by both governments and international organizations. The process culminated in a flood of initiatives in the spring of 1989." SJÖBERG I, *supra* note 19, at 11.

27. France was the first government to offer funds, about $100 million over three years. This overture played a critical role in giving the idea credibility and resulted in pressure on other governments to do the same. *See* SJÖBERG I, *supra* note 19, at 15-17.

The scope and purposes of the fund were also contentious. Some thought the resources should be linked with regular development work, while others wanted to focus on transboundary issues. This issue was influenced by parallel negotiations within the Montreal Protocol on new sources of funding to compensate developing countries for the added costs of substitutes for ozone-depleting chemicals. The creation of a new fund was one way to assure developing countries that funds were "new and additional"[28] and also responded to the growing public awareness of international environmental concerns. Three other issues made inclusion in such a fund logical: climate change, biodiversity, and international water resources.[29] The first two issues were on the agenda for the U.N. Conference on Environment and Development (UNCED) planned for 1992, which also provided some motivation for reaching an operational agreement in time to present some meaningful results. While finally agreeing to support such a fund, the U.S. insisted that it be a pilot facility for a three-year period, limited to paying the incremental costs of global environmental benefits, and open only to countries that "commit to appropriate environmental policies."[30]

The basic elements of an agreement were thus in place for a three-year pilot program to test the concept of a Global Environment Facility. Funding would be available for the incremental costs of developing country efforts directed toward climate change, biodiversity, international water resources, and ozone depletion. Administration would be housed in the World Bank, but the United Nations Development Programme (UNDP) would have a key role with respect to technical assistance and institution building, and the United Nations Environment Programme (UNEP) would have a role in ensuring that the policies were consistent with those of the evolving conventions. Voluntary pledges, including co-financing provided by the U.S. through the

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28. Andrew Jordan, *Financing the UNCED Agenda: the Controversy Over Additionality*, 36 ENV'T, April 1994, at 16.

29. *See* SJOBERG I, *supra* note 19, at 20-21. The Montreal Protocol was initially approved without explicit funding for developing countries, and as a consequence was not ratified by the two largest countries, China and India. An amendment to the Protocol approved in 1990 created a fund to pay for the "agreed incremental costs" of compliance with required changes in chemicals. *See* FRENCH, *supra* note 7, at 101-2; HUNTER, *supra* note 4, at 587-91. Subsequently it was agreed that the Ozone Fund would provide funding to developing countries, while the additional needs of economies in transition would be left to the GEF. Intergovernmental meetings on climate change began in 1990, and despite U.S. opposition there was already momentum for some form of international agreement. Marine pollution was an obvious choice, despite the absence of a focused environmental agreement, because of a program of action within UNEP and a history of international negotiations. Loss of biodiversity had yet to receive the same status and recognition but was becoming the subject of increasing attention and documentation.

30. Statement of Pat Coady for the United States (Nov. 27, 1990), *in* SJOBERG I, *supra* note 19, at 28.

Agency for International Development (AID), amounted to approximately $1 billion for three years.

B. The Restructured GEF

The commitment to a three-year pilot phase meant from the very start that either the GEF would end or be reshaped into something more permanent. Moreover, the political context for international financing evolved considerably during the pilot phase due to the 1992 UNCED conference and the negotiation of international agreements on climate change and biodiversity. The initial impetus for the GEF had come from donors and the international organizations themselves.[31] Rather than spend time developing procedures and priorities there was considerable pressure to get going as quickly as possible, in order to show progress before the UNCED.[32]

The role of the World Bank in the pilot phase was one source of controversy. The Bank had come under criticism from non-governmental organizations (NGOs) who argued that its investments had been a source of significant environmental harm. While the NGOs were afraid that Bank administration might hinder the GEF from achieving its goals, they also saw the potential benefits of reforming the Bank from within through experience, a kind of Trojan Horse effect.[33] As in other international forums, NGOs also sought opportunities for participation in the decision-making processes of the GEF. The initial response was to allow for a day of consultations with NGOs prior to meetings of the parties.

In the negotiations leading up to the UNCED, numerous proposals were advanced for Green Funds and other alternatives to the GEF. Much of the pressure for change came from developing countries who wanted more funds, wider scope,[34] and, most of all, greater political control than they had in the World Bank.[35] However, some international organizations, particularly the UNEP, also lobbied for structures that would have given the organizations greater prominence. Some countries also promoted an emphasis on greater

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31. Final negotiations on the pilot phase GEF were attended by 27 countries, all but nine of which were industrialized. *See* HELEN SJÖBERG, RESTRUCTURING THE GLOBAL ENVIRONMENT FACILITY 5 (1999). [hereinafter SJÖBERG II].

32. *See id.* at 11.

33. *See id.* at 12-13.

34. The African countries, for example, wanted to give the GEF a mandate to address land degradation. *See id.* at 19.

35. Voting in the World Bank is essentially a one dollar for one vote system. The result is that larger donors dominate.

development assistance. The future of the GEF thus became linked to the much larger politics of the UN conference.[36]

During the negotiations at the climate and biodiversity conventions, the GEF was recognized as the "interim" financial mechanism for both conventions. This reflected the reality that the GEF had already emerged as the only accepted source of finance for global environmental issues. During UNCED numerous promises were given for other sources of aid, but it quickly became clear that the GEF was the only real source of new money. The restructuring of the GEF, and its financial replenishment, thus assumed new significance as a measure of international environmental politics, post-Rio.[37]

The negotiation of the restructured GEF formally began in December 1992 and concluded in March 1994. The agreement that resulted was a compromise that included numerous significant points of departure from the pilot phase. The role of the three implementing agencies was preserved, but governance was formally placed in a new Council of thirty-two countries; all but the largest donors and China were grouped together into constituencies. Contested votes require a double majority, 60 percent of countries and 60 percent of contributions, effectively conferring veto authority on both developing countries and the largest donors. Periodically, all countries would be invited to meet in a Participants Assembly. Day-to-day administrative functions would be overseen by a CEO and a small independent Secretariat housed in the World Bank. While this would avoid the need for a new institution, it would be responsible to the Council, not the World Bank. It was further clarified that all projects would have to be endorsed by the recipient countries, which would therefore have both an operational and a political focal point. While the mandate was limited to the same four focal areas, it was noted that land degradation projects could be done insofar as they qualified within one or more of the four focal areas.

The contentious issue of NGO participation was finally resolved in favor of allowing NGOs to participate in Council meetings as observers, consistent with the trend in the Conventions but beyond normal practice in financial

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36. The GEF negotiations had been largely within the province of finance ministries, while the UNCED conference was a major international event that eventually attracted the participation of more than 100 heads of state.

37. For perspectives on the GEF in the context of negotiating the Climate Convention, *see generally* NEGOTIATING CLIMATE CHANGE: THE INSIDE STORY OF THE RIO CONVENTION (Irving Mintzer & J. Amber Leonard eds., 1994). *See* Bo Kjellen, *A Personal Assessment*, *in* NEGOTIATING CLIMATE CHANGE 149-74 (noting the role of new resources in Agenda 21, the limited response represented by the GEF, and its importance for the Climate Convention); Tariq Hyder, *Looking Back to See Forward*, *in* Negotiating Climate Change 201-26 (emphasizing the importance of the ongoing restructuring of the GEF to advancing the climate agenda); Atiq Rahman and Annie Roncerel, *A View from the Ground Up*, *in* Negotiating Climate Change 239-73 (contesting the role of the World Bank in the GEF and the concept of incremental costs as the basis for GEF funding).

institutions. Another round of difficult financial negotiations finally settled on $2 billion in total contributions for the next three-year period.

As part of the negotiation process, a commitment was also made to commission an independent evaluation of GEF operations. Despite the fact that few projects had actually been implemented on the ground, the report served as a check on some of the more important issues associated with project selection and implementation. They were particularly critical of the decision to move ahead quickly without the benefits of an overarching plan or priorities.[38] They recommended that strategies and program guidelines be developed before the expenditure of new funds - an approach that was subsequently adopted - while also recognizing that the Conventions would review the respective eligibility criteria for relevant projects.

An operational strategy and ten initial operational programs were agreed to in 1995. These respond to Convention guidance and define the basic parameters of eligible activities under the restructured GEF. Thus, for example, climate projects are defined by one of three strategies: short-term projects, with a cost-effectiveness of under $10 per ton of carbon; barrier removal projects, in which the underlying investment is expected to be cost-effective once certain "market barriers" are removed; and projects to help commercialize new technologies.

C. GEF and the Private Sector

The emergence of FDI as a key factor in development occurred together with the negotiation of the restructured GEF. While it was therefore not explicitly recognized in the initial strategy, the need to mobilize private sector activities was taken into account in important ways. Even without reference to the rise in FDI, the limited amount of GEF funds relative to the magnitude of the problems it was to address was immediately obvious.[39] To have any meaningful impact on global environmental problems, it was apparent that it would be necessary to leverage additional resources and create conditions for markets to work without continued subsidy.

This philosophy is explicit in the programs for promoting cost-effective energy efficiency and renewable energy technologies. These programs were a response to evidence that many cost-saving clean energy services were not

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38. *See* GLOBAL ENVIRONMENT FACILITY, INDEPENDENT EVALUATION OF THE PILOT PHASE 13 (1993); SJÖBERG II, *supra* note 31, at 38-39.

39. The UNCED Secretariat had estimated that the additional financial needs associated with the recommendations of Agenda 21 were on the order of $125 billion a year, more than twice the level of all international development aid. NGOs also believed that increased funding was necessary, as indicated by their emphasis on reforming the World Bank and its annual loan portfolio of about $25 billion.

being commercialized as rapidly as the economics would justify due to absence of financing, distorting policies, lack of local knowledge, or other factors. If GEF resources could remove these barriers, the effect could be lasting and replicable. A successful outcome is therefore not simply one in which the technologies are used successfully, but "one where particular least-cost, win-win renewable technologies have become financially sustainable in a recipient country market."[40] An indicator of success might be increased market share for the technology in the target area and replication in other markets.[41]

Some GEF projects also specifically targeted financial practices as the barrier to improving the environment. These projects are most often administered by the International Finance Corporation (IFC), the body within the World Bank family that lends directly to private companies. The assumption in these projects is that there is some perceived but exaggerated risk impeding investment in otherwise reasonably profitable ventures. If GEF-supported projects demonstrate that a profit can be made, the expectation is that private investors will become less risk-averse and will follow.[42]

III. ISSUES AND PROSPECTS

In 1997, prior to the second replenishment, an independent review was commissioned to evaluate GEF's progress and overall performance. The report included a frank assessment of efforts to leverage private sector investment and otherwise engage business contributions in global environmental projects.[43] Their major conclusions were :

- that private investment in GEF projects was relatively modest, particularly when adjusted to remove one very large geothermal project and investments by quasi-state enterprises in China, India, and Russia;
- that the role of private financial institutions such as banks and insurance companies was even more limited, and tended to be a factor only when projects became successful;
- that country case studies found that some governments did not know how to involve the private sector, while others deliberately did not

40. GLOBAL ENVIRONMENT FACILITY, OPERATIONAL PROGRAMS 6-4 (1997).

41. *See id.*

42. *See* ERIC MARTINOT & OMAR MCDOOM, PROMOTING ENERGY EFFICIENCY AND RENEWABLE ENERGY: GEF CLIMATE PROJECTS AND IMPACTS 23 (1999).

43. *See* G. PORTER ET AL., STUDY OF GEF'S OVERALL PERFORMANCE 14-17 (1998).

involve the private sector out of concern that the GEF support would subsidize individual companies;

- that the main barrier to commercial investment in GEF projects may be perceived higher risk, in which case guarantees or other risk-reduction measures might be less expensive and more effective than grants; and
- that the GEF implementing agency with most experience lending to the private sector is the International Finance Corporation (IFC), the agency within the World Bank that lends directly to private companies.

In sum, they found that "major barriers to increasing support from the private sector exist, particularly GEF's long and complex approval procedure and the comparatively greater risk of global environmental projects compared with normal commercial projects."[44]

Subsequent to the Overall Performance Study(OPS), in May 1999, the GEF Council approved a paper proposing further steps to engage the private sector.[45] The paper builds on the findings of the OPS but suggests, more specifically, that the primary challenges are building awareness of the GEF within the business community; simplifing and accelerating the project cycle; and providing support in forms that directly correspond to business needs.

Environmentally-oriented business organizations have long been aware of the GEF and its potential contributions. For example, in a 1994 book about the negotiation of the Climate Convention, the executive director of the Business Council for Sustainable Development (BCSD) stated support for the designation of the GEF as the financial mechanism of the convention.[46] Recognizing the incremental cost basis of GEF financing, the executive director argues for concentrating catalytic skills and experience in one institution:

> "...the GEF will be leveraging other sources of funds, most notably from the private sector. Our view is that the role and capacity of the private sector has been underestimated as a source of investment

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44. *Id.*

45. *See* GLOBAL ENVIRONMENT FACILITY, ENGAGING THE PRIVATE SECTOR IN GEF ACTIVITIES, GEF/C.13/Inf.5 (April 22,1999) < www.gefweb.org>. The paper was prepared in response to a Council request for a review including "modalities to facilitate private sector involvement in GEF-financed activities, including partnerships with the private sector to promote the transfer of technology." *Id.* at n. 1.

46. The BCSD is described as a coalition of major corporations interested in finding ways to link business goals more effectively with development needs. Their first publication, produced for the 1992 UNCED conference in Rio, was titled CHANGING COURSE.

> capacity and as a facilitator of technology cooperation. The GEF will address this question jointly with BCSD in the near future."[47]

A group like the BCSD is likely to be responsive to specialized environmental financing. However, from the standpoint of most companies, the scale of GEF financing may be too modest, and its role within the climate convention and national development strategies too complicated, to justify a high level of interest. On the other hand, more should be done to support the private sector within developing countries, since they may represent an untapped source of project ideas. These locally based firms are also often a major target group for GEF projects, because in order for the results of projects to be sustained and replicated much of the investment and leadership will need to come from within recipient countries.

The need to improve both awareness of the GEF and obtain more input on country needs is the objective of a program of country dialogue workshops approved by the GEF Council in October 1998.[48] These week long workshops are intended to expand understanding of the GEF in a wide range of interests, including the private sector.

There is also a link between the use of financial intermediaries, outreach to local businesses, and faster project processing. Five projects administered by the International Finance Corporation have collectively received $125 million in GEF financing designed to leverage $540 million in private sector contributions.[49] The structure of these projects is based on using GEF funds in a risk-sharing arrangement, through partial guarantees or concessionary loans. This allows transactions on terms as close as possible to standard commercial practice.[50] As noted above, the assumption in these projects is that, if successful, commercial lenders will recognize the potential profitability of these investments without the need for further subsidies.

A further benefit of these funds is the potential for faster processing of assistance, within the framework of the overall project. Concern about the length and complexity of the GEF project cycle has been a recurring theme in many countries. These views of the GEF are recognized in the Overall Performance Study.[51] The period of time between project inception to work

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47. Hugh Faulkner, *Some Comments on the INC PROCESS*, *in* NEGOTIATING CLIMATE CHANGE, *supra* note 37, at 229, 235.

48. The approved GEF project brief for the workshop program can be reviewed on the World Wide Web at: <http://www.gefweb.org/wprogram/Oct98/WP_Sum.html>.

49. *See* MARTINOT & MCDOOM, *supra* note 42, at 24.

50. Financial assistance can be provided in diverse ways. Alternative financing mechanisms are listed and defined in the GEF private sector paper. *See id.* at 10-11.

51. *See id.* at 65-69. The initial phases of the pilot phase were criticized for processing projects too quickly, without adequate oversight, strategy or technical input. *See* SJOBERG II, *supra* note 31, at 39.

program inclusion (formal approval by the GEF Council) can be on the order of eighteen months, with several additional months required for approval by the relevant implementing agency. Numerous steps have been taken to expedite this process. These include making available project preparation funds; creating a "medium-size" project window (projects up to $750,000) with simplified approval procedures, aligning GEF procedures more closely with those of the agencies, allowing for upstream consultations to approve project concepts, and eliminating steps wherever possible.[52]

A fund structure has the potential to be faster, insofar as authority for project approval is delegated to a single centralized agent and the range of issues to be considered is relatively narrow. The catch, however, is that funds have to be raised from private sources before investments can be made. Even with GEF funding lowering the overall risk, the expected return may still be marginal from a commercial standpoint. The first dedicated GEF-supported renewable energy and energy efficiency fund received final Council endorsement in October 1997, but did not achieve the necessary funding to become operational until December 1999.

The exclusive role maintained by the three implementing agencies has also been linked to the need to create more competition and flexibility in project development.[53] Within the framework of the three agencies, only the IFC, within the World Bank, has a focus and extensive experience with respect to private sector lending. In 1999, the GEF Council agreed to allow a modest expansion of authority for the four major regional development banks within the GEF system.[54]

The GEF Council is exploring a more programmatic approach, providing larger support on more flexible terms over a longer time period. In return, the country becomes more of a partner, accepting goals defined in terms of performance indicators. The concept was approved in principle by

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The subsequent emphasis on developing an operational strategy and programs and providing for Council review procedures and NGO input were therefore a necessary evolution but one that inevitably resulted in further processing time.

52. A specific procedural change in the interest of faster processing was Council agreement to eliminate a second review of final project documents. The purpose of this second review was to allow Council members to verify that any comments made on project briefs at the time of work program inclusion were in fact addressed in the revised documents. *See* G. PORTER ET AL., *supra* note 43, at 71. This step required up to six weeks. The Council has now agreed that this second review be waived, unless a request is made to the contrary at the time of work program inclusion.

53. *See id.* at 57-60.

54. The decision allows the regional banks to bring projects to the GEF Secretariat for concept approval, thus avoiding questions from the agencies about project eligibility. An approved regional bank concept must still be funded through one of the three implementing agencies. If none agrees to serve as implementing agency for the project, an explanation must be provided to the Council. *See* GEF Council Decision (May 1999) <www.gefweb.org>.

the GEF Council in May 1999 in the form of a renewable energy partnership with the World Bank.[55] The World Bank agreed to raise at least three times the funds contributed by the GEF, as a condition of the partnership. The details of the first such partnership (e.g., the nature of the performance indicators to be used and the schedule and conditions for disbursements) are expected to be reviewed and resolved at the May 2000 Council meeting. For example, the project might entail financial support over a decade, with the recipient government promising to make essential policy reforms during some initial period after the first tranche of funding. Subsequent funding could be approved without going back to the Council, assuming the country fulfills its promises.

The programmatic approach is consistent with research by the World Bank and others, showing that a favorable policy environment is essential for effective use of foreign aid.[56] According to a review conducted by the World Bank, "with sound country management, 1 percent of GDP in assistance translates into a 1 percent decline in poverty and a similar decline in infant mortality."[57] The effect is much less in a country without appropriate policies,[58] as the same amount of assistance would have only one- third as much impact on poverty reduction.[59] A similar synergy is found between a good policy environment, foreign aid, and private investment. "In countries committed to reform, aid increases the confidence of the private sector and supports important public services."[60] Every single dollar in aid can bring twice as much in private funds.[61] Insofar as a programmatic approach allows for engaging countries in more dialogue regarding the policy environment needed for attracting private investment, it is more likely to be successful.

A private sector variant on the partnership concept proposes engaging private firms in "progressive partnerships", defined as "direct collaboration . . .to achieve an identified global environmental benefit, with sharing of risks and project costs."[62] An example is an international waters project in the Malacca Straits region between Indonesia, Malaysia, and Singapore. The project will support a marine navigation system to minimize accidents and protect environmentally sensitive areas, and is being developed in cooperation with a Canadian entrepreneur. The private investment will be compensated

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55. *See id.*

56. *See* ASSESSING AID, *supra* note 2 at 2.

57. *Id.*

58. The range of relevant policies are defined broadly to include basic macroeconomic policies that support open markets and competition, the rule of law, and political stability.

59. *See* ASSESSING AID, *supra* note 2, at 2-3.

60. *Id.* at 3.

61. *See id.*

62. ENGAGING THE PRIVATE SECTOR, *supra* note 45, at 9.

in part by user fees included in the project design. The potential for this kind of arrangement represents a challenge to those companies willing to engage directly in developing innovative solutions to address global environmental problems while sharing the risks.

CONCLUSION

Since its inception in 1991 as a pilot program in the World Bank in 1991, the Global Environment Facility has proven to be an innovative and adaptable agent for developing and testing solutions to global environmental problems. From the very beginning, it has always been expected that the GEF would be a facilitator and catalyst, and not the sole solution, since the scale of the effort needed greatly exceeds its resources. With the rise in private finance over the same period, the challenge has somewhat evolved. Resources for investment in developing countries are increasingly available, but they are not always, or even often, being injected into activities consistent with environmental goals. In diverse ways, the GEF is seeking to meet this challenge by demonstrating that profits can be made in investments with global environmental benefits. Over the long run this must occur as the result of decisions by private actors without international subsidies.

While the GEF has been able to do a great deal while committing only about $500 million per year, much greater resources may be necessary as the extent of the problems become more apparent and as new issues such as the accumulation of persistent organic pollutants continue to be identified. Despite the continued decline in foreign aid, there are several promising ideas for greatly increasing environment-related investment in developing countries. Most likely to come to fruition may be the Clean Development Mechanism (CDM) in the Kyoto Protocol.[63] The CDM offers the possibility of a form of international emission trading, in which industrialized countries could achieve at least some of their target emission reductions by investing in less expensive projects in developing countries. The implementation of the Kyoto Protocol and the role of the CDM are far from certain. Nevertheless, some studies suggest that when fully operational the CDM could result in annual financial flows in excess of $5 billion.[64] If such funds are applied strategically to pay for the incremental cost of clean energy projects, the impact could be considerable.

Another proposal, first introduced by James Tobin of Yale University, is based on taxing the enormous amount of currency being traded

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63. *See generally* M. GRUBB, THE KYOTO PROTOCOL: A GUIDE AND ASESSMENT (1999).

64. *See* Duncan Austin et al., *How Much Sustainable Development Can We Expect from the Clean Development Mechanism*, (Nov. 1999) <www.wri.org>.

internationally. Because the volume is so large, even a very small tax could raise billions of dollars. While more funding is necessary, the solutions to global environmental problems ultimately require finding ways to make development compatible with overall local and global environmental constraints. The GEF and other sources of aid can help, but the political will and creativity necessary can only be found when all major stakeholders—public and private—are fully engaged.