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Asian Infrastructure Investment Bank's (AIIB) Paper on the Accountability Framework:
Reflections from Civil Society

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The Asian Infrastructure Investment Bank's Accountability Framework should be analyzed and monitored simultaneously alongside the provisions set forth on the Paper, Regulation and the Decision on the said Framework. The Paper was adopted on 11 April 2018 and the Regulation shall be effective by 1 January 2019.

We re-echo our 6 April 2018 input sent to the AIIB that, "This decision goes to the heart of the question of governance at the Bank. Board members are accountable to their constituent governments, shareholders of the AIIB, for their decisions. Shareholder governments in turn are responsible to their citizens for ensuring that the Bank upholds its environmental and social standards in its lending operations. In essence, the project approval process by the Board provides an opportunity for civil society and potentially affected communities to raise their concerns with their representatives, to ensure decisions are well-informed and take account of potential harms."

Introduction

1. Accordingly, the Accountability Framework (AF) states that its purpose is to "clearly demarcate the role of the Board of Directors (BoD) and the President with respect to the financing operations of the Bank (para. 1)." The Paper also indicates measures by which the BoD will use to hold the President accountable.
2. However deeper reflections suggest that significant powers will be transferred from the Board to the President on project approval authority. The underlying rationale behind the document is to further fast track the AIIB loan approval process, which is already much ahead of other international financial institutions (IFIs). Nonetheless, there should not be a trade-off between the speed of approval of financing a project and the corresponding due diligence requirements of ensuring that any likely adverse harm will be mitigated, if not avoided.
3. The introduction alarmingly implies that further transfer of powers will be vested by the Board to the President, i.e. "...proportion of projects to be considered for approval by the President will increase very gradually over time... (para. 4)". While

this can be interpreted as a phased approach, the ambiguity and lack of guidelines pose risks on how the Bank will implement this new scheme of approving projects. For instance, if 2016 – 2017 will be the baseline for the Bank, does it have targets on how many projects will be approved by the President within the 18 – 36 months? Accordingly, efficiency is one of the objectives of this “new model of governance”. How then will this be assessed vis-à-vis the quality-at-entry, project readiness as well as ensuring a robust implementation of the Bank’s Environmental and Social Framework among others? While the Bank may argue that this can be covered in the review itself, discussions around this should start early on.

4. On the details of implementation, the AF loosely frames that “Board of Governors, the BoD and the President have or will shortly put in place the key documents necessary to ensure the Bank operates with high standards, the time is right to move to the next stage of developing the AIIB’s governance model (para. 7) (Note: emphasis supplied)”.
5. If the “key documents” being pertained to are the Environmental and Social Policy, Public Information Interim Policy (PIIP), other sectoral strategies, etc. to ensure the “Bank operates with high standards”, these still fall short with respect to the genuine consultation processes that should go through in developing these documents, e.g. translation of policy documents at least in key local languages; lack of AIIB’s consistent feedback mechanism in integrating CSO comments; providing response on instances where comments cannot be considered, etc. Despite these legitimate concerns, CSOs question how the timing can be appropriate in moving to the purportedly “next stage of developing AIIB’s governance model”.
6. Furthermore, looking at the AIIB’s operations since 2016, there is a significant lack of transparency on its information disclosure on all phases of the project cycle from the selection to project implementation. With the authority shifting to the AIIB Headquarters in Beijing, China where the President holds office, this further distances the Bank from public scrutiny.
7. In addition, the Bank at present has yet to approve its Policy on Public Information (PPI) and its Project-Affected People’s Mechanism (PPM). Furthermore, there is also the absence of Environmental Social Framework Guidelines for Implementation. Notwithstanding these critical policies to enable the Bank to “improve social and economic outcomes in Asia”, it has already approved 24 projects without any of these basic binding requirements.

On the Role of BoD – Policy and Strategy

8. According to the AF, the BoD is “responsible for the direction of the general operations of AIIB, including setting the Bank’s policies and strategy and for overseeing their implementation (para. 5)”. Furthermore, the BoD “drives strategy through sector strategies and the Business Plan and Budget (BPB). These strategies include objectives, approaches and a monitoring framework to track strategy implementation (paras. 10 - 11)”.
9. The Bank has approved the Energy Sector Strategy and the Transport Strategy both of which are very lean documents. There is no detailed monitoring framework nor implementation guidelines for these strategies in the public domain as of now. The Operational Policy on International Relations recently approved by the BoD also gives AIIB the license to finance “de facto” governments and finance through

international waterways. As opposed to this provision, there are no objectives, approaches and monitoring frameworks out to evaluate the implementation of these policies.

10. The following are identified as tools for the BoD to oversee Policy and Strategy Implementation:

- “Directives concerned with implementing a Policy and Strategy will be shared one week to the BoD prior to being issued by the President... (para. 13)”;
- “The main instrument through which the BoD directs the President in the operationalization of strategies and policies is the annual Business Plan and Budget (para. 14)”;
- “The BPB also includes quantitative and qualitative milestones to allow the BoD to monitor progress and hold the President accountable. This framework will allow Board members to assess, on a quarterly basis, AIIB’s performance. The indicators approved in each sector strategy are the building blocks of the Bank’s results framework, which will be fully developed by the time AIIB’s first Corporate Strategy is approved (para. 15)”.

11. This is the first mention of a broader AIIB Strategy since its inception in 2016. The AF further elaborates on the Corporate Strategy, i.e. “By 2021 AIIB will be operating under its first Corporate Strategy. This Strategy will outline a medium-term framework that integrates existing and future sectoral strategies, thematic priorities and core institutional principles, values and goals, and will also lay a Bank-wide foundation for the next phase of growth and for evaluating the results that AIIB aims to achieve (para. 17)”.

12. “AIIB’s strategy will be implemented within a set of risk thresholds agreed by the BoD. The BoD approved the Risk Appetite Statement (RAS) in January 2018 and will be asked annually to approve the specific levels of top-down risk allocation (para. 18)”.

13. While the BOD is opting to relinquish portion of its approval authority of projects to the President, the question of investment, social and environmental risk requires more in depth attention. Is the RAS open for public scrutiny? How will it be updated? What are its parameters for risk assessment? These questions will become more important as the AF will be implemented.

Critical Issues with regards to Delegation Principles and Project Approval Process

14. In realizing the potential risk of losing powers to management, the AF introduces a very critical clause into it for the BoD to retain its full powers - “The Articles of Agreement (AoA) confer the power to delegate authority for project approvals to the President. The BoD retains authority in these matters and may decide in future to amend or withdraw the authority that is delegated by these provisions (para. 19)”. Through this provision the BoD may invoke the AF to be withdrawn in cases where they feel that the President may have over extended his powers beyond what the AF permits.

15. The subsequent categories under para. 19 are deemed exceptions to the AF which need to be closely monitored by the civil society:

Category I – Precedent Setting:

- a) The first sovereign-backed project in a Member.
- b) The first non-sovereign-backed project in a Member.
- c) The first project in a sector in each Member.
- d) The first projects using a previously unused financing instrument, e.g. if AIIB for the first time lends to a bank for on-lending or provides subordinated debt.
- e) The first project involving a particular co-financier in which AIIB proposes to apply one or several policies of such co-financier.

Category II – Significant Strategic and Policy Issues:

- a) A project in a non-regional Member.
 - b) A project where a corresponding Sector Strategy has not yet been approved by the BoD.
 - c) A Project requiring a policy derogation, e.g., in terms of risk limits or procurement policy requirements.
 - d) A project which directly implicates the Operational Policy on International Relations.
- The Bank proposes to finance projects to “de facto” governments and across international waterways. This will directly lead to severe impacts on conflicted areas, and coastal zone with complex social dynamics.

Category III – Risk Tolerances - a project that falls into one of the following categories:

- a) The amount of AIIB’s economic capital (ECap) utilized by the Bank’s financing in a project is in excess of \$25 million.
 - The Category III on Risk Tolerance also limits the Bank’s perception to financial risks alone. The Accountability Framework is void of any indication that the potential environmental and social risks and harm would also be a factor in deciding if the project will be approved by the BoD or the President.
 - **According to investment managers, Economic capital is the amount of risk capital held by a financial services company (in this case AIIB) to enable it to survive any difficulties such as market or credit risks. The amount is determined internally by shareholders (AIIB BoD), often using a measure of portfolio risk such as Var, i.e., value at risk.
- b) The amount of AIIB’s financing for a project is in excess of any one of the following amounts:
 - i. \$200 million in case of sovereign-backed financing or guarantees.
 - ii. \$100 million in case of non-sovereign-backed financing or guarantees.
 - iii. \$35 million in case of equity investments.

16. Para. 20 elaborates that “the objective of setting financing thresholds is to assure that: 1) the riskier transactions are to be considered by the BoD...”. The specific limits proposed under (j) of paragraph 19 are derived from Management’s analysis of the ECap relative to target credit ratings. An ECap limit of \$25 million translates to a notional limit of about \$300 million for a BB rated borrower (the average portfolio target rating) for sovereign-backed projects and about \$150 million for a BB-rated borrower (the average portfolio target rating) for non-sovereign backed projects.

17. According to regulatory and credit rating standards, AIIB has a AAA rating which suggests that as an obligor it has extremely strong capacity to meet its financial commitments. It is important to note that AF now allows AIIB President to approve loans to BB and BB-rated borrowers, who are perceived in the near term and long term to be more financially risky to meet their financial obligations.
18. In other words, BB and BB rating may be more vulnerable to significant uncertainties and exposure to adverse business, financial or economic conditions which could lead to the obligor's inadequate capacity to meet its financial commitments. Through this framework, the BoD is relinquishing significant oversight on BB and BB-rated borrowers and this should be an area of long term concern for AIIB's risk considerations.
19. Para. 23 states, "A Director may ask that a project be considered and decided upon by the BoD at any time from the first time a project is included in the pipeline until a date which is fourteen (14) calendar days after Management provides the BoD with a final Project Summary Document (PSD)".
20. On this note since 2016 the AIIB has been grossly inadequate in providing project-related information upstream in the project cycle, especially during the pipeline/proposed project phase. Without adequate information regarding each project in the pipeline, the BoD may not have adequate information in order to dutifully exercise its right to implement key exceptions or pull up a project for board review. At present the current Policy on Public Information has also not been approved.
21. Para. 27 reemphasizes the need for reviewing the AF within 3 years (and mid-term review within 18 months) and states "... The review will include, but not be limited to, the delegation principles (including call-in rights), modalities of delegation and information sharing processes. It will also include an in-depth review, undertaken by the Compliance, Effectiveness and Integrity Unit (CEIU), of a sample of projects subjected to delegated approval to ensure that the decisions were robust and aligned with the BoD-approved policies and strategies".
22. In the AF, this is the first time CEIU is mentioned and given a key role in the review process of the AF. It needs to be noted that the independence of the CEIU will be absolutely critical to the performance and review of the AF.

BoD's tools for holding the President accountable

23. Para. 37 describes in detail the role and responsibility of the CEIU in the accountability of the President in implementing the AF and its functions:

"The President has established the CEIU that reports directly to the BoD. CEIU combines three functions traditionally carried out at other MDBs by different units. CEIU consolidates the integrity (fraud and corruption related to projects), project complaints and project evaluation functions under one roof. This allows for greater synergy between these functions, especially in deriving lessons learned, and supports the BoD in its supervisory role.

To reinforce this synergy, the President has invited the Managing Director of CEIU to attend the Management Meeting and Executive Committee as an observer. This aims to ensure that CEIU is well informed of important decision-making, and also positions the Unit to play a constructive role in expeditiously raising concerns with Management for

resolution. When issues cannot be resolved by Management, and without compromising the confidentiality of discussions and decisions within the Management and Executive Committees, CEIU has the ability to report them to the BoD. CEIU will also play a key role in the rigorous and independent evaluation of the performance of projects, thereby providing the BoD with an essential metric for supervising the project approval authority delegated to the President”.

24. There are no structural checks and balances between the CEIU’s role in the Management Meeting and the Executive Committee meeting. One cannot rule out the potential of compromise that the working environment, office culture and other unofficial exchanges between Management and CEIU may have on the AF evaluation. This is an alarming concern considering the scale of the finances and the impacts the projects may have on the ground.

On Holding the President Accountable

25. The AF in the remaining sections alludes to, “The primary tool for BoD to ensure that the President is operationalizing BoD approved policies and strategies is the BPB (emphasis supplied).” In addition, “... The President also reports to the BoD on how the financing program is supporting the thematic and sector priorities. The President and the BoD continue to discuss further sharpening of the strategic priorities and how best to report on these to the BoD”.

26. The AF points towards three lines of defense on the AF implementation. All three are headed by management positions including the VP for Strategy and Policy/ Chief Compliance Officer, the Chief Risk Officer and the Chief Auditor. Outside these three positions the CEIU is entrusted with independent evaluation of the AF and President and reporting to the BoD. Will these three management-led lines of defense be objective to the evaluation of the AF? Will CEIU conduct itself independently and fulfill all material obligations as articulated in para. 37? These are questions which can only be answered once the AF is set into operation.

27. In conclusion, civil society must continually monitor the AF and engage the BoD continually on AIIB operational realities. CSOs will remain steadfast in demanding the public release of all monitoring and evaluation frameworks, guidance notes and project related information to ensure that the Accountability Framework does not allow the AIIB HQ to operate away from Board of Directors’ oversight and full transparency.

Signed:

NGO Forum on ADB
Accountability Counsel (USA)
Asian Peoples' Movement on Debt and Development (APMDD)
Bangladesh NGOs Network for Radio and Communication (BNNRC)
Banktrack
BIC Europe
Cayan Bdr. Adhikakau, Nepal
Center of Bird Lovers
CLEAN (Coastal Livelihoods and Environmental Action Network)
Coal/Nuclear Free Bataan Movement Philippines
Envionics Trust
Environmental public alliance, Armenia

Equitable Cambodia
GreenID, Vietnam
Inclusive Development International
Indian Social Action Forum (INSAF)
Indigenous Perspectives, India
Jamaa Resource Initiatives, Kenya
Lumière Synergie pour le Développement
Mladi Za Zemiato, Bulgaria
Nash Vek Public Foundation, Kyrgyzstan
Oil Workers' Rights Protection Organization Public Union, Azerbaijan
Oyu Tolgoi Watch, Mongolia
Pakistani Fisher Folks (PFF)
Public Association for Assistance to Free Economy (Azerbaijan)
Rivers without Boundaries Coalition
SANLAKAS
Solutions for Our Climate, South Korea
ULU Foundation, USA
Umeedenoo Organization, Pakistan
Urgewald, Germany
VSEA, Vietnam
WomanHealth, Philippines

Source: <https://www.aiib.org/en/about-aiib/governance/accountability-framework/index.html>

Note: In the case of the ADB, its current Transitional Results Framework 2017 – 2020 does not have an indicator measuring the processing time from concept clearance to Board approval. However, according to the 2017 Development Effectiveness Review, sovereign operations processing time (from start of loan fact-finding to Board approval), it takes 7.7 months in 2017 which is slower than the baseline value of 5.7 months in 2016. Whereas for non-sovereign operations processing time (from start of due diligence to Board approval), it takes 7.4 months in 2017 with a 9.0 months baseline value in 2016. Period by which AIIB set that a mid-term and comprehensive review for the Framework will take place respectively.