Recommendations on the U.S. International Development Finance Corporation for the Biden-Harris Administration

Fully Realizing the DFC Development Mandate and NGO Partnerships

Since January 2020, COVID-19 has negatively impacted worldwide economic growth at levels unseen in a century. Current estimates predict a **3-6% contraction in global GDP**. Over the long-term, the deep recessions triggered by this pandemic are expected to decrease investment, erode human capital through lost work and interrupted schooling, and fragment global trade and supply chains. Development finance institutions (DFIs) and, notably, the U.S. International Development Finance Corporation (DFC), will play a critical role in mitigating the current economic impacts of COVID-19 and supporting the recovery of key sectors.

The passage of the Better Utilization of Investments Leading to Development Act of 2018 (BUILD Act) in October 2018 and the DFC launch in January 2020 created a much-needed opportunity to advance sustainable development through market-based approaches. **Efforts to prioritize development at the DFC thus far have met resistance.**

InterAction's DFC Working Group developed the following recommendations for the Biden-Harris Transition Team to maximize the DFC's potential to be a leader in sustainable development, far surpassing the Overseas Private Investment Corporation's (OPIC) positive impact and course-correcting from changes made or neglected by the current Administration. In parallel, the InterAction community is advocating for full resourcing by the U.S. Congress for the DFC to do this work.

Recommendations are organized according to the following sections:

- Ensure the new development mandate is fully realized in practice.
- Champion climate adaptation and mitigation through DFC investments.
- Bring the DFC into alignment with U.S. policy on environmental and social protection.
- Fully integrate gender into DFC work as a lynchpin of sustainable development.
- Set the gold standard on transparency, stakeholder engagement, and accountability.
- Champion diversity, equity, and inclusion in organizational culture and leadership.

It is a prime time for engagement. The elevated legislative mandate around development has opened the door for more partnerships with U.S.-based global development and humanitarian NGOs as first-loss investors, technical advisors, and conduits for local communities on the frontlines of the most significant development challenges of our time. InterAction Members bring a range of lessons learned, having partnered with the DFC's predecessor and other DFIs to implement billions of dollars in U.S. development finance in numerous countries over the past 15 years.

Recommendations

Ensure the new development mandate is fully realized in practice.

The new legislative mandate and removal of the U.S. nexus requirement at the DFC created an opportunity to focus on investments in low-income countries (LIC) and lower-middle-income countries (LMIC), as well as sub-national areas. Taking full advantage of this opening requires revisiting the DFC's risk profile, stronger connections with the interagency, changes to the deal sourcing process, internal incentive structures to balance return on investment with development gain, measuring development impact across the portfolio in addition to the project level, and instating the requisite quantities and competencies of staff for success.

- **Create an agency-level strategy that centers development—improving aspects of the new development strategy—and engage in joint planning with USAID to identify shared priorities.** The DFC launched a development strategy in October 2020 after ad hoc meetings with a small subset of stakeholders and very little time to comment. This strategy needs improvement, which can be partly achieved through more standardized consultation, and should be applied agency-wide, not just to one segment of the institution.

- **Cultivate stronger structural linkages between the DFC and USAID—such as through the Development Coordination Unit, Development Finance Coordinator Group, and USAID Missions—by assessing the status of the USAID-DFC Coordination Report and finalizing the creation of a staff secondment program.** The July 2019 coordination report identified several potential vectors for increased coordination of development finance activities across the inter-agency; this report needs to be reviewed and acted upon. The DFC can finalize a proposed agency secondment program to place DFC investment officers at USAID and USAID technical staff at DFC to build better cross-agency understanding. If successful, the Administration can broaden this to include other development agencies, such as the Millennium Challenge Corporation (MCC).

- **Institutionalize metrics that track the agency-wide pursuit of investments in LIC, LMIC, and fragile states.** Measure and publish the total dollar amount of the DFC portfolio invested in LIC, LMIC, and fragile states, not just the percentage of deals, which does not capture their size. The InterAction DFC Working Group has compiled a more comprehensive **list of metrics to track additional aspects of the entire DFC portfolio**. InterAction also has **recommendations on financing in fragile states**, particularly how working with first-loss actors, such as NGOs, can facilitate such investments.

- **Hire sufficient staff with competencies in sustainable development and incentivize all staff to work toward positive development outcomes.** DFC staff should have expertise in labor rights; climate change; risk management; gender; conflict issues and governance; accountability; and monitoring and evaluation. Develop an internal incentive structure for rewarding staff for positive development outcomes while avoiding negative environmental and social impacts.

- **Create a joint USAID-DFC fund.** This fund would draw on funds appropriated directly to the DFC to provide first-loss or subsidy to better enable riskier yet more developmentally impactful DFC deals. To start, such a fund could draw upon $25 million and would target projects in an established set of USAID priority countries and sectors. The DFC's Chief Development Officer (CDO) could manage this fund. To further strengthen collaboration, USAID should designate an appropriate individual to serve on the investment committee for these deals.

- **Work with the sustainable development community to prioritize investments that will have the highest development impact after COVID-19 and align it with the World Bank's 'Sustainable Checklist for Assessing Economic Recovery Investments.'** DFC capital can support sectors that remove long-term constraints to growth, including human capital development, health systems, food insecurity, climate change, water, and sanitation, among others. The DFC is a member of the **DFI Alliance,** which announced a joint commitment to work collaboratively to bring liquidity to the market, support companies impacted by the virus, and promote new investment in global health, safety, and economic sustainability.

- **Ensure the Chief Development Officer (CDO), Chief Risk Officer (CRO), Office of Development Policy (ODP), and DFC executives regularly meet with a diverse set of NGOs focused on sustainable development.** All other development agencies, including their USAID partners, have built relationships with the broad development community, including InterAction Members. Recent engagement—after multiple unmet requests from the NGO community— has been ad hoc. Effectiveness and credibility are undermined when the DFC does not demonstrate a genuine interest in working with this community.

Champion climate adaptation and mitigation through DFC investments.

The DFC could drive U.S. global action to address the climate crisis. To achieve this, a sea change is needed. When looking at the DFC's 2019 investments, fossil fuel projects represent increasingly large portions of the DFC's energy portfolio.[1] If this trend continues, fossil fuel projects could far outstrip any continued renewable energy investment. Fossil fuel projects are higher risk and **exacerbate extreme poverty** and the global climate crisis, impacting low-resource contexts the most. OPIC was a major implementer of clean, renewable energy projects in developing countries. The DFC can continue these efforts and much more aggressively use its finance vehicles to lead the global transition to a green economy.

- **Adopt a net-zero by 2050 (at the latest) target for the DFC's investment portfolio.** Similar to the U.K.'s CDC Group, DFI, and country governments such as South Korea and China, the DFC can demonstrate its climate leadership by ensuring its nearly $30 billion portfolio is working toward a net-zero world. Investment decisions today affect emissions tomorrow—a forward-thinking lens is imperative to ensure long term progress.

- **Restore provisions of the 2017 Environmental and Social Policy Standards (ESPS) removed in the 2020 Environmental and Social Policy and Procedures (ESPP).** The ESPP are the main standard for project-level due diligence and were changed in 2020 without consultation or proper protocols. Key changes lifted a prohibition on nuclear energy projects in high-risk environments. A side-by-side of these two policies and what has changed is available as needed.

- **Use the Impact Quotient (I.Q.), Environmental and Social Policy and Procedures (ESPP), and risk assessments to accurately assess all energy projects' feasibility—especially fossil fuel and nuclear projects—with respect to viable, sustainable renewable alternatives.** The DFC should review all fossil fuel projects approved during the transition period to understand what about the current I.Q., ESPP, and risk assessment allowed them to be approved and adjust policies accordingly.

- **Align with existing international frameworks relating to sustainable investments,** including the E.U. Taxonomy on Sustainable Finance and the Task Force on Climate-Related Financial Disclosures. Such alignment will allow for the DFC to join actors such as the OECD, IDB Invest, and the U.N. SDG framework to ensure U.S. impacts are counted toward global commitments.

- **Devote targeted efforts for adaptation and resilience.** At least 50% of the DFC's annual commitments should finance projects with climate adaptation and resilience co-benefits. This will ensure alignment with the 2015 Paris Agreement commitments on climate finance. These co-benefits should be clearly identified and monitored using frameworks such as the E.U. taxonomy that governs The European Green Deal.

1 Specific examples include: $450 million toward the Vaca Muerte ("Dead Cow") fracking projects in Argentina next to the biodiverse Patagonia region; $430 million to restore a 90km pipeline in Egypt to transport natural gas from North Africa to Europe, which was previously a target of armed groups, approved in November 2019; intent to support $632 million natural gas pipeline in Mexico; and the liquid natural gas plant in the Rovuma region of Mozambique.

Bring the DFC into alignment with U.S. policy on environmental and social protection.

The U.S. government has long been one of the most vocal supporters of strong safeguards at multilateral development banks (MDBs). However, the DFC's own ESPP are based on the Performance Standards of the International Finance Corporation (IFC), a set of safeguards that currently fall short of what the U.S. government regularly demands from IFC projects.

This creates inconsistency in U.S. government policies and messaging on human rights, social protections, and the environment. It also creates barriers for co-financing and undermines the DFC's overall message of being a vehicle of U.S. foreign policy.

- **Align the ESPP with U.S. policy toward the MDBs.** For example, an important, longstanding policy that the U.S. continues to promote at the MDBs is the requirement that environmental impact assessments for projects with significant risks be made available to the public for at least 120 days prior to a project's approval. The U.S. government is required to vote against projects that do not meet this minimum time period, and every year votes against several projects—including IFC projects—based on this mandate. It is a critical requirement that allows for input from communities, civil society, and experts at a point in the project cycle where the financing institution has maximum leverage to affect change on the ground. As longstanding U.S. policy, this should be reflected in the DFC's policy and practice. Other policy inconsistencies include differences in how to apply safeguards to financial intermediary subprojects, allowing investments in for-profit healthcare and education, the application of trafficking in persons (TIP) sanctions, and the threshold for delegating project approvals to management, among others.

- **Encourage greater cooperation between DFC staff and Treasury's Office of Development Results and Accountability (ODRA).** ODRA works closely with U.S. representatives at the MDBs to determine U.S. voting positions on individual projects, as well as on environmental and social governance issues more broadly. Through ODRA, Treasury also leads an interagency process to review every loan proposal that comes through the Boards of Directors at the MDBs to ensure their consistency with U.S. policy, and regularly engages with civil society organizations that monitor MDB projects and policy through monthly interagency meetings. Greater cooperation and engagement between the DFC and ODRA would highlight policy inconsistencies and provide a platform to resolve them.

Fully integrate gender into the DFC's work as a lynchpin of sustainable development.

Equal rights and treatment of all genders in society is one of the strongest determinants of successful development. Gender must be a central aspect of the DFC's investing, akin to how it has been successfully mainstreamed at other U.S. development agencies.[2] The 2x Initiative is a start, ensuring women have greater access to financing, though it constitutes just 5% to 15% of the total dollar value of the DFC portfolio, is staffed by two people, and was moved to an office that is farther from DFC leadership.[3]

The DFC has a legislative mandate to "prioritize the reductions of gender gaps and maximize development impact by working to improve women's economic opportunities."[4] To fully integrate gender into the DFC, policies and practices must recognize and address the multitude of social, economic, political, and regulatory barriers to entry that women uniquely face.

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2 See Feed the Future.

3 It is challenging to know the exact figure due to a lack of transparency around how the 2x portfolio compares to the total. The original $1 billion goal of the 2X Initiative is 5% of the $20 billion portfolio; however, an additional $2 billion in 2x financing has been catalyzed since. These amounts were spent over multiple years, so it is unclear what percentage of the portfolio 2x constitutes.

4 See BUILD Act Sections 1451 and 1443.

- **Apply Section 3 of the Women's Economic Empowerment and Entrepreneurship (WEEE) Act to the DFC.**[5] This section makes it U.S. government policy to reduce gender disparities, eliminate gender-based violence, and secure land and property rights for women. It also provides actions for USAID to take that should be mirrored at the DFC.

- **Develop a DFC Gender and Women's Empowerment Strategy, building on WEEE Act requirements.** Such a strategy or policy could outline the structures, staffing, leadership, processes, and resources to advance gender equality and women's empowerment throughout its entire portfolio. Such a strategy can include the pursuit of the EDGE Certification—a global DFI certification standard for gender equality.

- **Consider both positive and negative impacts on gender equality within the entire DFC investment lifecycle.** During the deal selection process, the DFC should conduct gender analyses with standard indicators informed by best practice that feed into the environmental and social risk assessments and risk mitigation plans. Such analyses identify how women and other marginalized groups benefit from and may be negatively impacted by DFC investments, such as increasing gender gaps and instances of gender-based violence. Equipped with this information, the DFC can work with potential investees and host countries to improve their practices and reduce gender inequalities. In addition, gender should be integrated into the I.Q. beyond the "Inclusion" pillar to capture potential positive gains to women's economic empowerment, narrowed gender gaps, and negative impacts. Disaggregating all DFC data on people by sex and age is a starting point. On the backend of a deal, the DFC should measure the outcomes of the risks that the DFC identifies. Actions that undermine gender equality should trigger a rescoring of the project and feed into lessons learned.

Set the gold standard on transparency, stakeholder engagement, and accountability.

Transparency, stakeholder engagement, and accountability are crucial for an effective DFI and U.S. government agency. To meet these standards, the DFC should incorporate **best practices** for transparency across all operations and at the project level and regularly engage with a broad set of stakeholders on its projects, policies, and approaches.

Even with the best risk management, negative impacts such as environmental damage, labor violations, or displacement can occur from DFI projects. Providing a comprehensive, timely, and regularly updated view of the DFC's operations would give the DFC public confidence and enable productive engagement with its work.

- **Create the Board Public Engagement Policy and Access to Information Policy through requisite consultation.**[6] In November 2020, the DFC held a very short, two-week consultation period on the draft Board Public Engagement and Transparency policies required by the BUILD Act. This consultation was not widely publicized, delegitimizing the product and resulting in weak policy. The period of consultation should be extended to give more robust opportunities for stakeholder engagement and to **strengthen** the Board Public Engagement policy. The draft transparency policy should be replaced by an **Access to Information** policy based on international best practices.

- **Strengthen the DFC's future work by fulfilling obligations under the Foreign Aid Transparency and Accountability Act of 2015 (FATAA) to externally evaluate 50% of the DFC's portfolio.** The BUILD Act includes an expansion of the legislative mandate around monitoring, evaluation, and reporting due to the conforming amendment that applies the FATAA to the DFC. As a result, 50% of the DFC's portfolio must now be evaluated. Recent reports from USAID's Office of Inspector General (2019 and 2015), OPIC's Office of Accountability (2018), and the Government Accountability Office (2015) identified specific weaknesses in OPIC's monitoring practices.

5 See BUILD Act on (b) International Development Cooperation Policy.
6 See BUILD Act Section 1413(b)(1)(C) and Section 1411(6).

This likely stems from both a lack of awareness about the importance of external evaluation and a lack of resources to pursue them.

- **Ensure that the new Independent Accountability Mechanism (IAM) has strong terms of reference, practices, and leadership.** The DFC Board approved the **resolution** for the IAM in September 2020 without the requisite public consultation. To ensure that the principles underpinning the IAM in the resolution—including impartiality, accessibility, and transparency—are effectively implemented, the IAM must have strong Terms of Reference (TOR) or procedures. The resolution commits to a public consultation on the TOR two years after the Board approves them. However, the initial TOR should be subject to a **public consultation** process before the Board approves them to ensure that they reflect international best practices and are shaped by the stakeholders that could potentially use the mechanism. The IAM should also have strong leadership. Following best practice at other DFIs, external stakeholders, especially civil society organizations, should be involved in the IAM director's selection process. This could be a role for the Development Advisory Council. When harm occurs as a result of the DFC's activities, the IAM should facilitate the provision of remedy so that communities can restore their livelihoods. The DFC's clients should be required to obtain project finance bonds, insurance, or trust funds in escrow to ensure that reserve funds are available to address adverse environmental and social harm.

- **Ensure the new Inspector General (I.G.) works in a timely, effective way.** The I.G. was recently appointed. OPIC's I.G. was housed within USAID and published important findings about OPIC's functioning over time. This is a critical role that should be held to a high standard of timeliness of responses to complaints. Importantly, the I.G. should be separate from the IAM such that none of its activity prevents an individual or community from filing a complaint with the accountability mechanism. However, coordination between the two is possible.

- **Abide by the Sunshine Act's requirements for transparency and public engagement.**

Champion diversity, equity, and inclusion in organizational culture and leadership.

Reforms are needed across the U.S. government to improve diversity across its workforce and leadership and to ensure it is an equitable and inclusive place to work. In the case of the DFC, this starts with the Board. The DFC Board of Directors currently has nine seats. Seven of those seats have been filled by Caucasian men and two remain vacant. The lack of gender and racial diversity on the DFC Board significantly undermines the institution's credibility and effectiveness. The DFC Board is currently comprised of enough political appointees to overrule any Board-level dissent on projects undergoing scrutiny that require a majority vote. This lack of oversight may enable more exceptions to be made.

- **Review the recommendations in the GAO Report 20-477, "USAID: Mixed Progress in Increasing Diversity, and Actions Needed to Consistently Meet EEO Requirements," and conduct an internal review of the DFC's current approach to diversity, equity, and inclusion.** This report is a useful jumping-off point for U.S. development institutions seeking to make improvements.

- **Fill the board's remaining seats with women and People of Color and represent views of organized labor.** There is one remaining vacant position on the DFC Board that is reserved for non-governmental roles that has not yet been filled. Nominees for the Board come from POTUS and require Senate confirmation. The people in these positions should be highly qualified in the global development field and development finance—especially labor rights—and environmental and social policy. These vacancies present an opportunity to not only rebalance the gender and racial inequality currently present on the DFC Board, but also to increase the level of oversight.

About InterAction's DFC Working Group

Established in July 2019, InterAction's DFC Working Group convenes international relief and development NGOs to advance the sustainable development mandate of the DFC to improve development finance outcomes for the world's poorest and most vulnerable people. This working group engages with the DFC, U.S. Congress, and USAID on development finance issues, alongside partner coalitions and working groups.

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About InterAction

InterAction is a convener, thought leader, and voice for NGOs working to eliminate extreme poverty, strengthen human rights and citizen participation, safeguard a sustainable planet, promote peace, and ensure dignity for all people.