In the early 1980s, the World Bank came under fire for having financed multiple projects that led to spectacular environmental disasters in Brazil and Indonesia. As a result, an international coalition of environmentalists organized protests and lobbied the Bank’s staff for a change in lending practices. But Bank policy did not waver.

When direct appeals to the Bank failed, these critics turned to the Bank’s member governments in the developed world, where environmental issues had become politically salient. They focused most of their attention on the U.S. government, which appropriates the largest share of Bank funds, appoints the Bank president, and controls the largest bloc of votes on the Bank’s executive board. During the mid-1980s, the U.S. Congress threatened to withhold future funds from the Bank unless the organization changed its practices. The Bank complied, but only in part. In 1994, Congress followed through on the previous threat, withholding $1 billion from the Bank. Of equal importance, U.S., European, and Japanese representatives on the board sought to ensure that the Bank’s promised behavioral changes would actually be implemented. Shortly thereafter, the World Bank adopted sweeping institutional reforms and significantly altered its lending portfolio by increasing environmental lending and decreasing projects that caused environmental harm.

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This case presents a puzzle for international relations theory. The World Bank exhibited significant independence from its member governments for nearly a decade, then suddenly and repeatedly changed its behavior in response to increasingly coordinated demands by member governments. Neither neorealism nor neoliberalism, as currently conceived, can accommodate such autonomous action by international organizations (IOs) within their state-centric ontologies. This case, like many others in the study of IOs, requires a theory that can explain organizational autonomy as well as responsiveness to the demands of member governments. Extending neoliberal institutionalism, we propose a theoretical alternative that may fill this gap in the literature and have broad application for the study of IOs. We advance a principal-agent (P-A) model of international organization in which groups of member governments sometimes empower their IO agents with real decision-making authority.

However, three understudied factors complicate agency problems in the case of IOs, delimiting the conditions under which the insights of conventional P-A theory hold. First, member countries must solve collective-action problems multilaterally before motivating their agents. Such multilateral decision making highlights the problems faced by any "collective principal." Second, IOs often receive marching orders from organizationally distinct principals—particularly in the case where legislatures and executives in member countries act independently and have separate contracts with the same agent, creating the problem of "multiple principals." Third, IO agents act at the end of a long "chain of delegation," complicating the transmission of demands from the ultimate principals to the IOs.

If problems related to collective action, multiple principals, and agent proximity can be overcome—hardly a foregone conclusion—principals can then employ various tools to rein in errant behavior by IO agents. They can "screen and select" IO personnel more carefully, so that the new staff members more closely reflect their principals' interests. Principals can engage in "oversight" of the IO, not only through direct monitoring of agent behavior (police-patrol oversight), but also by enlisting the aid of third parties (fire-alarm oversight). Principals can generate "procedural checks and balances" within the IO, so that one set of agents has the authority to monitor other agents and report back independently to the principal, or even veto decisions made by other agents. Finally, principals can draft new "contracts" with the IO personnel, requiring modified behavior to achieve anticipated reward, or insuring punishment if behavior is not consistent with the interests of the principal.1

To evaluate our model, we examine multiple instances of institutional reform and behavioral change at the World Bank from 1980 to 2000.2 We trace the pro-

2. While we discuss numerous kinds of "Bank behavior" in the case study, we focus our attention on lending behavior—what type of loans does the Bank make, and does this change over time? After all, loans are the primary means by which the Bank shapes economic, political, and environmental outcomes in international relations.
cesses that brought about modest changes after 1986, and then the major institutional reforms of 1993–94. We then highlight the political process linking those institutional reforms to the punctuated and significant changes in the Bank’s lending portfolio.

**IR Theory and International Organizations**

Although neorealism and neoliberalism have dominated international relations (IR) theory debates for twenty years, a number of scholars have convincingly argued that neither paradigm can account for many important features, behaviors, and effects of IOs. These are serious criticisms because most multilateral cooperation now takes place within the context of IOs, the number of IOs is growing rapidly, and IOs seem to be exercising more authority than they ever have in the past.

Realists have largely not perceived IOs as worthy of explanation. On the rare occasions when realists have attempted to explain the behavior, the persistence, or the reform of IOs, they typically fail, sometimes flamboyantly. The thinness of realism’s state-centric ontology may explain these failures. Realists leave no place for IOs in their models; hence, international outcomes are determined by state power and interests alone. Substantive IO rules are created and maintained by the most powerful state(s) in the system. As the distribution of power changes, so too will IOs. Hence, IOs are not important arenas within which states interact, and IOs are certainly not autonomous actors in their own right. It follows from realist theory that outcomes in international politics would be the same with or without IOs.

Neoliberals have successfully exploited the empirical and analytical failures of realism, and they have done so with a virtually identical ontology. Unitary states are still the only significant actors in international politics, and states are still fundamentally concerned with survival in an anarchic system. A key difference between the two paradigms follows from an assumption about the role of information in international politics. For realists, information is always scarce and unreliable, thus risk-averse states assume the worst about their neighbors, and security dilem-

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mas result. For neoliberals, the quality of information in the international system varies significantly. As the quantity and quality of information increase, so do the prospects for cooperation. Crucially, IOs enable states to gather and share important information.\textsuperscript{11} Thus for neoliberals, IOs do matter, but they matter only as structural constraints on state behavior, not as autonomous actors. Therefore, because neoliberals largely share the realist ontology, they have not fully considered how IOs might be treated as agents of state principals and thus actors—albeit subordinate ones—in their own right.

This shortcoming of neoliberalism is both ironic and unfortunate. Pursuing the question of IOs as agents of their member states would have been the logical next step in applying the theory of the firm to international relations. Recall that Keohane began this application in 1984, noting persuasively how IOs might solve Coase’s classic problems of information asymmetries, transaction costs, and the absence of property rights.\textsuperscript{12} Once economists had developed the functional theory of the firm, they moved on to problems of its organization, including how shareholders attempt to control managers. However, international relations scholars have only recently begun to take the corresponding step for IOs.\textsuperscript{13} An explicit application of the theory of the firm to international relations would complement the extant neoliberal theories of IO creation and persistence with a more general theory of IO governance, behavior, and change.\textsuperscript{14}

This amendment may prove indispensable because, in its present form, neoliberalism simply has no theoretical apparatus to deal with IO agency. If IOs are important for cooperation in international relations because they reduce transaction costs, mitigate information asymmetries, and provide quasi-legal frameworks, then whether and how well IOs perform these tasks should greatly influence prospects for cooperation. If IOs have autonomy from their creators, they may actually undermine the purposes for which they were created. Given enough autonomy, one can even imagine pathological IOs actively sabotaging the interests of the states that created them.\textsuperscript{15} In fact, this vision of IOs running amok is pre-
cisely the world that some scholars (and politicians) envision today. Without a theory of IO behavior and reform, neoliberalism has no ability to address such empirical patterns.

Thus neoliberalism finds itself in much the same condition that Coase, Williamson, and other transaction cost economists did during the early 1960s. It is time to apply the insights of the theory of the firm to multilateral cooperation within IOs. Below, we propose a parallel and progressive shift within the neoliberal paradigm that would elaborate the microfoundations of international organization. Our model illuminates the conditions under which IOs will be given autonomy to pursue their preferences, and the conditions under which they will be reined in by member governments.

A Principal-Agent Model of International Organization

We thus develop a model of institutional and behavioral change in IOs, based on logic derived from agency theory in microeconomics. Member governments (making up the principal) hire an IO (agent) to perform some function that will benefit the members. In this framework, member governments establish the goals that IOs will pursue and then allow the IO to pursue those goals with little interference most of the time. Generally, IOs should be observed to act "on their own." As long as agents are producing policies that are broadly consistent with the preferences of principals, P-A theory suggests that member governments will not pay the significant costs associated with micromanaging the organization. But during periods when member governments and IOs differ with regard to preferred outcomes, we can assess the mechanisms that drive IO institutions and behavior. In our P-A framework, we should observe significant institutional reforms and intervention by the member governments if and only if the IO strays from its principals' mandated objectives or the preferences of member governments change in concert.

dysfunctional, even pathological, behavior." Barnett and Finnemore 1999, 699. Barnett and Finnemore offer a theoretically coherent explanation for such dysfunctional IO behavior. For discussions about how organizational theory (or constructivism more generally) can be tested empirically and whether it should be conceived as a complement or an alternative to P-A theory, see Nielson and Tierney 2001; and Weaver and Leiteritz 2002.

16. When distinguishing between neorealist and neoliberal predictions regarding the fate of NATO after the Cold War, Keohane 1993, 287, claims, "Institutionalists would expect NATO to use its organizational resources to persist, by changing its tasks." While little within Keohane's original theory can support this assertion, neoliberal institutionalism can be usefully adapted to encompass IO independence. In fact, neoliberals are shifting this way in recent research. See Keohane and Martin 1999; Wallander and Keohane 1997; and Martin 2002.

17. For a more detailed introduction of the P-A approach in IR, see Pollack 1997. For classic works in agency theory, see Coase 1937; Alchian and Demsetz 1972; Williamson 1975; and Fama 1980.

18. If the preferences of only a subset of members change, IO institutional change will depend on the decision rules within the IO and the relative power of various members.
Previous Arguments

For early agency theorists, the creation of a firm provided its founders with a way to internalize transaction costs and delegate decision-making authority to realize efficiency gains that follow from specialization. However, the structure of a firm presents a problem for its founders: How does one delegate authority without losing control? According to Kiewiet and McCubbins, a principal faces three specific difficulties when delegating. First, the agent can “hide information” from the principal whose revelation would hurt the agent and help the principal. Second, the agent can do things behind the principal’s back, “concealing actions” that the principal would sanction if known. Third, the principal faces “Madison’s dilemma”—in which the need to delegate authority may give powers to the agent that can be used against the principal. Because the interests of principal and agent are never completely coincident, there will always be agency slippage between what the principal wants and what the agent does.

However, the principal is far from powerless. Principals write initial employment contracts, and they can renegotiate—or threaten to renegotiate—those contracts. Although threats and institutional reform may have costs to principals, they can employ these tactics strategically to modify agent behavior. In an efficiently designed P-A relationship, the contract is self-enforcing. That is, institutional constraints induce the self-interested agent to abide by the wishes of the principal.

Principals possess at least four tools to help them design self-enforcing contracts and thus mitigate agency slippage. First, the principal can carefully screen the potential agent when hiring. Such “screening and selection” mechanisms may enable the principal to employ someone whose interests are similar to the principal’s, or someone who has demonstrated obedience and diligence in the past. Second, the principal can “monitor” the agent’s actions, either directly through “police patrol oversight” mechanisms or indirectly, by inducing third parties to perform the oversight functions and thus mitigate the cost of monitoring through “fire alarm oversight.” Third, the principal may employ contracting arrangements that include credible commitments to punish or reward the agent for specified behavior. Fourth, the principal can construct checks and balances that require coordination or competition between two or more agents. If designed properly, checks and balances can reveal information to the principal about agent behavior and can also inhibit agent behavior that is detrimental to the principal.

P-A models have been fruitfully applied in American and comparative political contexts. The most influential findings from this literature demonstrate that the previously widespread view among scholars—that all-powerful bureaucrats often run amok in the policy process—is dramatically overstated, if not false. Because bureaucrats were observed to have a distinctive culture, to be lobbying politicians,

to be expanding their range of tasks—in short, to be doing more; and because bureaucracies were growing in size and number, many scholars incorrectly concluded that these organizations were gaining power at the expense of elected officials. This "abdication hypothesis" in American and comparative politics parallels recent claims about IOs in the international relations literature.

P-A Complications and Theoretical Solutions

The perception of "abdication" to agents may persist in the IO literature because IOs introduce a set of complicating factors that the extant P-A literature has not adequately addressed. Initially, models of P-A relationships were kept simple—one principal, one agent—as suggested by our discussion of the literature summarized above. However, this stylized model of delegation imperfectly mirrors the great complexity involved in governing IOs. In particular, such simplifications overlook the problems of common agency and long delegation chains.

Common agency: Collective principal or multiple principals. A recent literature in political economy addresses the issue of common agency, where principals must solve problems of collective action and incompatible incentives before, and while, they resolve issues of agency slippage. Contributors to this literature continue to conflate two analytically distinct situations that may result in important empirical differences. Specifically, as Lyne and Tierney note, a delegation relationship can have one or more principals, and a principal can either be an individual or a corporate entity. Hence, when an agent has more than one employment contract with organizationally distinct principals, we say this is a delegation relationship with "multiple principals." When an agent has a single contract with a principal, but the principal happens to be composed of more than one actor, we call this a delegation relationship with a "collective principal."

The most familiar delegation relationships in politics and government involve a collective principal. Voters delegate to politicians, legislators delegate to party leaders, and nation-states delegate to IOs. In all these situations, a group of actors reaches agreement among themselves and then negotiates a contract with an agent to do something. If the group cannot come to an agreement a priori (whether because of restrictive decision rules, cycling, or preference heterogeneity), then they cannot change the status quo. This is true for initial hiring decisions, for proposals to renegotiate the agent's employment contract, or for giving the agent novel authoritative instructions. In all these scenarios, there is a single contract between an agent and the collective principal.

22. See Niskanen 1971; Lowi 1979; and Dodd and Schott 1979.
25. See Lyne and Tierney 2002; and Lyne forthcoming.
Ironically, while delegations from a collective principal are quite common in the world of politics, political scientists have written more extensively on the question of multiple principals. For example, in American politics there is a vigorous debate about the independent influence of Congress and the president on bureaucratic behavior. Neither the Congress nor the president requires the consent of the other to reward, sanction, or monitor the same agent. Hence, the interbranch politics of agency control entails delegation from multiple principals that can unilaterally renegotiate the agent’s contract without the consent of other principals.

However, the individual principals in these models of American politics do not seem to suffer from any internal coordination problems, even though both the House of Representatives and the Senate are themselves collective principals. While this assumption may be reasonable in the case of a domestic legislature organized along party lines, it is less plausible for independent governments attempting coordination within an IO. Within a collective principal, if one actor or some combination of actors within the collective principal has a veto, then any decision to remove the agent or reform the agent’s incentives must be preferred to the status quo by the veto player. This makes the status quo stickier than many extant common agency models imply. In the strategic situation discussed below, an agent at the status quo may be insulated from meddling principals, especially if coordination within the collective principal is costly or if any member or group of members with the power to veto a change is inclined to do so.

Ceteris paribus, agency slippage has a tendency to increase with the number of actors doing the delegating. As the number of actors grows, coordination within the collective principal gets more complicated. Fortunately, many collective prin-

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27. See Calvert et al. 1989; and Hammond and Knott 1996.
28. For example, the president can promote, demote, or fire bureaucrats, and Congress can increase organizational budgets, decrease them, or even eliminate them entirely—each without the cooperation of the other. Among IOs, the European Commission is now responsible to both the Council of Ministers and the European Parliament—a clear case of multiple principals.
29. See Olson 1965; and Hardin 1982.
cipals employ decision rules and institutional devices that induce a clear preference aggregation function for the group. Hence, if electoral rules are carefully designed, then millions of voters can coordinate as a collective principal and hold an elected official accountable.

Preference homogeneity within the collective principal may have similar effects.30 However, if actors within the collective principal do not agree on proposed policy changes or institutional reforms, and the agent is cognizant of this disagreement, then the agent may be able to play members of the collective principal against each other. Such a situation makes it difficult for the collective principal to alter, or credibly threaten to alter, the agent's contract.31 Hence, agents can more easily ignore threats and refuse to modify their behavior.

Depending on decision rules, the equilibrium outcome will be somewhere within the combined preference sets of the members of the collective principal, but where exactly is indeterminate without prior knowledge of the status quo and the institutional rules that govern the decisions of principals. The good news is that most IOs have formal decision rules. To the extent that these rules are efficacious, one should be able to deduce behavioral outcomes if one can specify the preferences of principals and the power of the principals defined in terms of voting share.

The Delegation Chain: Proximate Principals and Leapfrogging

The nested P-A relationships that are common to IOs further complicate our use of agency theory. This complication has received even less attention in the extant literature.32 Figure 2 illustrates the numerous P-A relationships that are typical for IOs, with agency slack increasing as the delegation chain grows longer. If there is some slippage at each link in the delegation chain, then the ultimate principals within member countries (citizens) face the possibility that they will pay the costs of membership without receiving the policy payoff promised by the initial delegation.33

One solution to the problem of nested P-A relationships emerges through institutional design. Institutions can be designed so that pressure on agents to alter their behavior is only effective if it operates through the “proximate principal”—that is, the principal with the formal authority to hire, fire, or otherwise alter the agent’s employment contract. This is so even if portions of the “ultimate principal”—say, voters within member countries—are the ones demanding change. The proximate principal may be designed to receive the petitions of its immediate principals in the chain of delegation, aggregate those demands, sort them, and re-

32. For an exception, see Bergman, Muller, and Strom 2000. Unfortunately, this work neglects the impact of actions at one link in the chain on outcomes at subsequent links.
33. On problems of IO accountability to the “ultimate principals” within member countries, see Keohane and Nye 2001.
Domestic preference change and pressure

Representative mechanisms

(Elections and constitutions)

Member governments

IO constitution

International organization

Organizational structure

Policy outcome

Agency Slack

FIGURE 2. Nested principal-agent relationships

spond to them. Proximate principals filter messages coming down the chain, so that erroneous or exaggerated information is not conveyed to the agent. Proximate principals have decision rules expressly designed for these purposes, whereas an agent once or twice removed by a link in the chain is suited to receive demands only from its proximate principal and no other. Thus pressure on IO agents is unlikely to succeed until it is filtered through authoritative institutional channels.34

Because staff members at IOs are not rewarded, and may even be punished if they respond too vigorously to stimuli other than the demands of their proximate principal, they should tend to ignore or discount demands made by interest groups in given member countries. Hence, as we show in the case study below, attempts to "leapfrog" intermediate links in the chain of delegation will likely fail.35

34. Alternatively, principals may design procedures to ensure that agents are receptive to demands from specific constituents. See McCubbins, Noll, and Weingast 1987 and 1989.

35. This remains consistent with principals’ use of fire-alarm oversight mechanisms. For example, while nongovernmental organizations (NGOs) and private actors are encouraged to provide the World Bank’s executive board with information about the behavior of Bank staff, the authority to sanction IO agents has been—by design—strictly guarded by member governments. Shihata 1994. Recent criticisms of the Bank’s inspection panel by NGOs make it clear that the inspection panel has not allowed NGOs to capture or block projects preferred by the board.
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(IO management and staff) that are more than one link removed from the ultimate principal (member-country electorates) in the P-A chain will not be equipped with mechanisms to discern whether activists' demands are representative of the distant principal as a whole. Such institutionalized insulation actually ensures that IO agents will not change standard operating procedures without a clear indication from member governments that such changes are desired. The proximate principal will thus prove most important when agents are sifting through conflicting demands for behavioral change.

Thus at both domestic and international levels we adopt a strictly formal notion of power, which flows through authoritative rule structures specified in constitutions, articles of agreement, or charters. This approach may seem blasphemous to those familiar with the literature on IOs, in which readers are constantly reminded that formal rules and codified treaties often obscure the actual distribution of power and rules of the game within a given IO. However, the formal approach adopted here allows us to deduce a clear set of behavioral expectations and aggregate outcomes—something that is missing from much empirical work on IOs. If formal rules are not efficacious within IOs, then our hypotheses are likely to be falsified.

Hypotheses and Methods

A number of hypotheses that relate to collective principals, multiple principals, preference heterogeneity among principals, and the amount and type of agency slippage can be deduced from our P-A argument, but many of these hypotheses are better tested by employing statistical methods on cross-sectional quantitative data from different IOs. In this article we are interested in demonstrating the plausibility of the P-A model by closely tracing the process of reform efforts and illuminating the causal links between our independent and dependent variables. To these ends we deduce the following hypotheses:

**H1.** When agent behavior diverges from principal preferences, credible threats by the principal to recontract with the agent will reduce the gap between the principal's demands and the agent's subsequent behavior. However, behav-

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36. As Canadian Prime Minister Jean Chretien explained in response to calls for greater "democratization" by anti-globalization demonstrators in Quebec City, "This meeting is the result of a democratic process. Each of the thirty-four governments represented here is responsible for the well-being of its own people and each government at this meeting has been democratically elected. Who elected these protesters?" MSNBC news broadcast, 21 April 2001.

37. In a typical review of this literature we are told that "informal power" and weakly institutionalized authority structures at the international level "make it difficult for these theories to offer accurate explanations." Middlemas 1995. He may be right. But we note that Middlemas never actually tests hypotheses derived from any theory that assumes the efficacy of formal rules. We believe it is more prudent to empirically test such theories before discarding them out of hand.

To evaluate the strength of these hypotheses we carefully trace the processes and reveal the causal mechanisms of institutional reform and behavioral change at the World Bank. This task requires a method that can reveal multiple steps within a causal chain, from principals’ preference changes/convergence to recontracting threats to IO organizational reform to IO behavioral change. Hence, we employ a qualitative case-study research method.

For three reasons, the World Bank presents a difficult case for our P-A model. First, the opportunities for hidden action and hidden information are extensive. The Bank’s staff of more than 10,000 full-time employees and its worldwide operations make it difficult for principals to monitor. Second, unlike most IOs, the Bank generates enough revenue to cover its entire operating budget independently. Also, roughly 80 percent of the money it lends is raised in private capital markets where the Bank enjoys a AAA bond rating. Such figures suggest that the Bank, unlike IOs relying on dues, enjoys significant financial autonomy from member countries. Third, for most of the Bank’s history, professional economists and engineers on staff have framed reports and proposals in highly technical language, often obscuring the actions taken or the anticipated outcomes. Also, until quite recently it was very difficult for Bank board members (or the government officials who appointed them) to obtain detailed project documents more than a few weeks before the board vote on a loan, making oversight periods very brief. Bank reports were kept secret in the name of preserving the sovereignty of borrowers.

But no matter how carefully “difficult” cases are selected, readers should be skeptical of attempts to generalize from a single case. We attempt to mitigate the small-n problem in several ways. First, while we do not increase the number of observations by looking across space at other multilateral development banks,
we do expand the \( n \) by looking across time. By examining institutional and behavioral outcomes at the Bank over a twenty-year period, we increase the number of observable implications for our theory. Of course, we do not claim that each year is independent from all previous years. However, if we encounter variance over time in our core explanatory variables—principals’ preference change and convergence, credible threats to recontract, and institutional reform—then each instance of variation expands the \( n \).

To increase robustness, we employ multiple measures to gauge variation in our dependent variables. We assess lending behavior by measuring the portions of money lent in various categories from year to year, by measuring the percentage of loans that fall into each category, and by employing three-year moving averages for both measures. We examine each aspect of institutional reform over time. Moreover, our model entails a causal chain. Principals’ threats engender institutional reform, which results in behavioral change. Our model is strengthened if we find evidence suggesting that more significant behavioral changes in lending follow from more significant institutional reform.

**Case Study: Environmental Reform at the World Bank**

Until the early 1980s, the World Bank’s task managers and project officers did just about as they pleased. Most politicians and other elites within donor countries believed the Bank was the organization best suited to meet the lending needs of world development, and therefore left it alone. As importantly, the Bank was not engaged in activities that fundamentally conflicted with the interests of the electoral coalitions holding power in the West.

Ironically, during the 1970s the World Bank was often seen as a leader among IOs on questions of environmental protection. It was one of the only IOs to explicitly discuss environmental issues and (at least rhetorically) incorporate them into policy decisions. But with only three environmental specialists on staff until 1983, the Bank’s Office of Environmental Affairs typically rubber-stamped projects late in the approval process, only occasionally making recommendations to reduce environmental “externalities.” Despite the public perception that the Bank was more sensitive to environmental issues than other IOs, the environmental staff,
without budget or authority within the organization, could neither monitor nor enforce compliance with the organization’s environmental guidelines.47

However, even the previous perception of the Bank as relatively environmentally friendly changed dramatically in the early 1980s. Then, as discussed below, a series of World Bank lending blunders helped to mobilize environmental nongovernmental organizations (NGOs), who succeeded in altering Bank behavior only after their demands were channeled through donor governments and the Bank’s executive board.

*Common Agency Problems at the World Bank*

It is important to revisit here the discussion of common agency, involving a collective principal and multiple principals. Both types of agency relationships are exemplified by the case of the World Bank.48 The Bank’s board of governors meets at least once per year and is composed primarily of member-country finance ministers. It has the authority to alter Bank policies, approve the annual budget, and amend the Articles of Agreement. In practice, and for all decisions over operations and policy, the member governments delegate decision-making authority to the Bank’s board of executive directors. This executive board is the Bank’s collective principal. A simple majority vote by the board is necessary for most Bank actions except amendments to the Articles of Agreement, which currently require an 85 percent supermajority of the board of governors. While all members of the Bank have voting shares, the Group of 7 (G-7) countries currently control nearly 50 percent of all shares.49 To force alterations in Bank practice, a coalition on the board must be built. (The collective nature of the Bank’s principal is represented in Figure 3 below, where the Bank’s three largest shareholders are listed). And coalition building on the board proves difficult without participation of the largest shareholder, the United States.

The U.S. president appoints (and the Senate confirms) the U.S. executive director to the Bank, who controlled 16.5 percent of the voting shares in 2000. That same year, Japan had 7.9 percent of the voting share and Germany had 4.5 percent. The large U.S. share provides an effective veto over major institutional changes at the Bank and facilitates blocking or building coalitions on the executive board. The United States is the only country with a unilateral veto over major institu-

47. Ibid., 635.
48. While the collective principal case is clearly illustrated by the World Bank, our choice to model the Bank as an agent of multiple principals is not as analytically clear. However, while the authority relationships are complex, we do gain leverage by conceiving of the Bank as an agent of multiple principals.
49. The size of a government’s voting share is determined by its financial contribution to the Bank, which is roughly proportional to the size of its economy.
The U.S. executive director reports to the U.S. Secretary of the Treasury, and the other G-7 directors report either to finance or foreign affairs ministers of their states. Only eight directors represent single countries. The other seventeen directorships are shared by groups of countries (usually clustered regionally), where individual directors are elected from the group by countries’ voting share.

The U.S. president may dismiss the U.S. executive director at any time. As an ultimate tool, the president can end U.S. membership in the Bank unilaterally. However, it is the U.S. Congress that authorizes and appropriates money to the Bank, both through the regular replenishments of the International Development Association (IDA), and when members of the Bank agree to increase their subscriptions. Because subscriptions directly affect voting share, the U.S. Congress can thus unilaterally alter the U.S. contract with the Bank. Thus Congress is an additional proximate principal. Further, the U.S. Senate, through advice and consent, can reject the president’s nominee for executive director. Also, Congress can dictate the votes of the director by statute (subject to veto and overrides, of

50. The United States has always controlled enough votes to unilaterally veto amendments to the Articles of Agreement. In the 1970s, when the Articles required only an 80 percent supermajority to pass amendments, the United States controlled more than 20 percent of the shares. As the U.S. vote share dropped below 20 percent, the board of governors voted to change the threshold to 85 percent.

51. The United States, Japan, Germany, France, the United Kingdom, the Russian Federation, China, and Saudi Arabia.

52. In fact, we would argue that a U.S. withdrawal from the World Bank—initiated either by the president or Congress—would fundamentally alter the Bank itself. Given the probable shift in priorities, personnel, and headquarters that a withdrawal of the hegemon would entail, the organization that emerged would be a fundamentally different one. The implications of a U.S. withdrawal anchor our claim that both the U.S. president and Congress are independent principals of the Bank.

53. This would hold for any other member country-legislature that exists independently of the executive and can unilaterally recontract with the Bank. This caveat applies to France during periods of cohabitation, and to most Latin American countries. France’s voting share is slightly more than 25 percent of the U.S. share. All Latin American countries, even Brazil and Argentina, are much lower. Hence, this multiple principals concept applies most strongly in the case of the United States.
course).\textsuperscript{54} Finally, the Congress can end U.S. membership in the Bank by statute (with the same veto caveat applying). Interestingly, the Congress has no direct budgetary authority over the U.S. executive director or the executive director’s office, both of which are funded by the Bank. Hence, the U.S. Congress (as represented in Figure 3) has numerous formal sources of authority that allow it to unilaterally recontract with the World Bank, directly through appropriations and membership decisions, and indirectly through its authority over the U.S. executive director.

The Bank thus faces both a collective principal and multiple principals. When preferences diverge on its board, reform of the Bank proves difficult. Also, disagreement between the U.S. Congress and president can give the Bank additional room to maneuver. However, when the preferences of the board members and the two U.S. government branches come together, our model predicts that this convergence will constrain Bank behavior much more tightly.

\textit{Rumblings over Rondônia}

Beginning in the early 1980s, principals’ preferences regarding Bank policy changed and converged markedly in response to Bank actions, both for the U.S. Congress and president and among Bank executive directors. In 1980, the World Bank was invited by the Brazilian government to participate in a transmigration and highway construction project, dubbed \textit{Polonoroeste}, in the heart of the Amazon rainforest. The project was intended to help accommodate the huge resettlement population influx to the state of Rondonia, while also meeting rural infrastructure and agricultural needs. Some members of Bank missions to the Amazon returned dubious about the prospects of the project to meet its stated economic and relocation aims and warned that environmental damage would almost certainly result.\textsuperscript{55}

Their warnings went unheeded. Bank staff claimed that the Brazilian government would proceed with or without them. The executive board approved a number of loans for the massive project in the hope that Bank participation could limit some of the project’s most destructive consequences. But the Bank failed to prevent the worst of these problems. The road was built; settlers poured into the jungle; indigenous natives died in waves from imported diseases; malaria infected many of the new settlements; and the rainforest burned—impressively and notoriously.\textsuperscript{56}

\textsuperscript{54} The Pelosi Amendment is a case in point. The Pelosi Amendment requires the U.S. executive director to vote against all World Bank projects that are not accompanied by an environmental assessment at least 120 days before a vote is taken on the project by the executive board. Upton 2000.

\textsuperscript{55} See World Bank 1992; and Wade 1997, 640–42.

\textsuperscript{56} See Keck 1998; and Rich 1994.
In the rash of finger pointing that followed this debacle, the Bank proved an easy target.\textsuperscript{57} Environmental NGOs and a growing number of scientists began to pressure the Bank through direct lobbying of staff and management, by encouraging press coverage, through protests in both Brazil and Washington, D.C., and through testimony in U.S. congressional hearings.\textsuperscript{58} Yet, despite a loud and sustained lobbying effort, these groups were unable to stop the project or convince the Bank to halt disbursements on the loans. Similar fiascos following other Bank projects, particularly a comparable Bank-funded transmigration project in Indonesia, amplified the criticisms from the environmental community but did not trigger any change in Bank policies or projects. In fact, Bank officials grew creative in the ways they deflected criticism and ignored critics.\textsuperscript{59} After almost three years of well-reasoned critiques, a mountain of scientific evidence and a complete lack of progress, frustrated environmentalists convinced the U.S. Congress to take action.\textsuperscript{60}

\textit{U.S. Congress Threatens, Treasury Adds Pressure}

An odd coalition of environmentalists and fiscal conservatives in Congress joined forces to pressure the Bank. Robert Kasten (R-Wis.), chair of the Subcommittee on Foreign Operations of the Senate Appropriations Committee, fit within both camps. He desired a reduction in Bank-funded projects that caused environmental problems, but he also believed the U.S. Congress should closely scrutinize all money allocated to IOs. Kasten had held multiple hearings on MDB lending and the environment from 1983–85.\textsuperscript{61} But more public airing of project foibles had little or no impact on the status of the Rondônia project, others like it, or Bank policy in general. In order to change Bank policy, the management at the Bank needed to believe that those making all the noise could give them something they wanted or take away something that they needed. Senator Kasten understood this; and he was in a position to withhold billions of dollars.

The jugular at the World Bank was the IDA, which makes no-interest loans on a fifty-year repayment schedule to the world’s poorest countries. Unlike the larger International Bank for Reconstruction and Development (IBRD), which actually turns a profit, the IDA relies on donor contributions for its allocations. At the behest of environmental groups, Kasten and his congressional allies targeted that Bank vulnerability. The U.S. Congress explicitly threatened to withhold further

\textsuperscript{57} Wade characterizes Polonoroeste as only the most visible of many such projects that allowed environmentalists to go after the Bank. Wade 1997, 658–60.
\textsuperscript{58} Wade 1997.
\textsuperscript{59} Ibid., 660–67.
\textsuperscript{60} See Udall 1998; and LePrestre 1989.
\textsuperscript{61} Kasten was not alone. Both the House and the Senate held numerous oversight hearings on Bank operations. See LePrestre 1989; and Wade 1997.
IDA replenishments until the Bank addressed environmental problems caused by the projects it financed. In 1985, the Bank responded to Kasten's threat by suspending disbursements to the Polonoroeste project. After a five-month suspension, disbursements resumed, but with minor modifications intended to mollify Congress.

Even when facing threats of funding cuts, Bank responses were sluggish. Subsequently, the U.S. Treasury, the second of the U.S. multiple principals, grew serious about environmental reform at the Bank. The second Reagan administration had become more friendly than the first Reagan administration both to environmental interests and to multilateral development banks. Treasury Secretary James Baker also needed the Bank to manage the Latin American debt crisis. Congressional approval of an IBRD capital increase was vital to the success of the Baker plan for resolving the debt crisis. Now, there were two funding vulnerabilities for the Bank: the IDA replenishment and the IBRD capital increase. Baker thus took Kasten's concerns seriously and added the Treasury's voice to those in Congress calling for environmental reforms at the Bank. The interests of the multiple principals had converged.

The subsequent U.S. pressure was more than rhetorical. On 19 June 1986, the United States became the first country ever to vote against a Bank project on environmental grounds. As Alternate Director Hugh Foster asked the Bank's board before casting his negative vote on the massive Brazil Power Sector loan, "How much confidence can we have that it will be carried out conscientiously when the same [Brazilian government] institutions will be implementing a series of environmental disasters at the very same time?" Despite U.S. opposition, the loan was approved by the board.

Although passage of the loan certainly indicates that the members of the collective principal were divided on the need for serious environmental reform, the loss actually strengthened the resolve of Kasten and his allies in the U.S. Congress to cut IDA financing. Further coordinated efforts of the U.S. legislative and executive branches enhanced the credibility of the threat to IDA funding. Moreover, at this time, interests of other members of the collective principal—notably the Nordic countries, Canada, the Netherlands, and the United Kingdom—were also converging around environmental reforms at the Bank. However, these other directors

62. In late 1984, the House Subcommittee on International Development held hearings and made a number of "recommendations" to the Bank. Highlights included the establishment of an Environment Department, hiring more environmental staff, reducing destructiveness of traditional projects, consulting with environmental ministers and NGOs in borrowing countries, and financing more projects that would enhance environmental protection. See U.S. House of Representatives 1984.


66. Foster, quoted in Rich 1994, 137.

applied pressure more subtly, and were more willing to accept Bank explanations for environmental problems at face value.68

Waves of Reform at the Bank

With the near certainty of substantial funding reductions, the new president of the Bank, Barber Conable, an environmental sympathizer and former U.S. Congressman, attempted to insure that the IDA would not be gutted.69 In May 1987, he announced a series of environmental reforms that addressed some of the concerns of the Bank’s environmental critics. Most notably, the Bank reorganized its Office of Environmental and Scientific Affairs into a separate Environment Department, boosting staff from a half-dozen people to more than eighty members charged with performing more stringent environmental assessments of projects. In addition, Conable promised to create a new category of free-standing environmental loans. There was no commitment to reducing the dirty “traditional” loans in energy and transportation that were at the heart of the environmental disasters of the 1980s, but Conable did initiate a process that made the Bank’s environmental policies more stringent (at least on paper). Over the next several years, the Bank did delay loan disbursements on some of the most controversial projects. However, these actions did little to alter the environmentalists’ perceptions of the Bank.70

After the 1987 reforms, the Bank increased the number of environmental loans. But many NGOs questioned whether these new loans were in fact “environmental,” rather than traditional sector loans with new labels.71 The incentives of task managers had not been altered by the financial threats of donors, so the Bank continued to favor large (and dirty) traditional loans. For many Bank critics, the behavioral changes that followed 1987 were a step in the right direction, but a very small one.72

One reason that the 1987 reforms may have failed to alter core Bank practice was that the threats had been contingent on short-term behavioral changes rather than institutional changes. The loan approval process was largely un-

68. Wade 1997, 671.
69. Conable was appointed precisely to avert congressional funding cuts and to fix the Bank’s environment image. See Wade 1997, 672.
71. In every year from 1987 through 1993, total lending on “brown” projects for water reclamation and pollution abatement was greater than lending for “green” projects aimed at natural resource preservation. The average ratio of brown to green was 3.6:1 for this seven-year period.
72. Our interpretation is at odds with Wade 1997, who emphasized the 1987 reforms as pivotal for environmental improvements at the Bank. However, the facts that NGO criticisms not only persisted but increased, meaningful change occurred sluggishly in traditional sectors, environmental assessment was piecemeal, and Bank approval and board oversight practices remained unaltered, all argue in favor of our interpretation that the 1987 reforms were less important than the 1993–94 reforms. For an interpretation consistent with our position, see Fox and Brown 1998.
changed, with the Bank’s board still dependent on project officers for information and the Bank still lacking qualified personnel to conduct all the environmental assessments required by its new policies. While the in-house Environment Department now had a higher profile and more personnel, it was not effectively integrated into the operational side of the Bank and had few levers of power compared to task managers. Hence, over the next few years, environmentalists inside and outside the Bank observed plenty of “bureaucratic drift,” but had no institutionalized role in the process through which to restrain such behavior.

Unsurprisingly, the 1987 reforms satisfied neither external critics nor the Bank’s executive directors. Evidence of Bank-funded fiascos continued to mount, and a series of documents catalogued Bank shortcomings. Notably, a 1992 report—commissioned by the World Bank but researched and written independently by the Morse Commission—on the Sardar Sarovar dam project in India sharply criticized the Bank for failing to meet its own environmental standards. On the heels of this pointed criticism, an internal Bank document, later known as the Wappenhans Report, echoed the Sardar Sarovar criticisms, and noted that 37 percent of Bank projects had proved “unsatisfactory.” Wappenhans and his colleagues attributed this massive failure to the “approval culture” inside the Bank, where task managers used project documents—especially the all-important Staff Appraisal Reports (SARs)—as “marketing devices” to ensure loan approval. This criticism stung the Bank’s management and further tarnished its public image. Still, Bank officials stonewalled and deflected criticism. It took coordinated actions by both branches of the U.S. government and the Bank’s executive board to change this pattern.

**Organizational Changes and Reform That Sticks**

As the chair of the House Subcommittee on International Development, Trade, Finance and Monetary Policy, Barney Frank (D-Mass.) was acutely aware of the

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73. While regional vice presidents became more directly involved with loan planning and development, the board still saw project documents for the first time only ten to fourteen days before voting on the loan. See Wade 1997, fn 142; and Upton 2000.


77. By late 1991, a growing number of executive directors simply did not trust the information provided by the Bank’s India operations staff. At the behest of the executive board, Bank President Conable appointed an independent review team to investigate the Sardar Sarovar project. The team was chaired by the former director of the UN Development Program, Bradford Morse. See Morse and Berger 1992; Udall 1998.

78. See Wappenhans 1992, 14; and Udall 1998, 401.
Bank’s failure to change. With the next round of IDA replenishment looming in 1994, Frank took a page out of Kasten’s book and in 1992 threatened to withhold a nearly $4 billion replenishment unless the Bank undertook serious and specific reforms. This time Bank officials fought back with lobbying efforts, venturing repeatedly to the U.S. Treasury Department and to Capitol Hill directly to argue for a reversal of Frank’s threat. For the most part they failed. The new Clinton administration was politically committed to environmentalism, and legislators from both parties ignored the issue at their electoral peril. The multiple principals within the U.S. government had converged. Congress did eventually authorize the IDA replenishment, but for two years rather than the customary three. The legislature thus reduced the authorized amount by more than $1 billion. The final increment of $1.25 billion was made contingent on the actual implementation of information disclosure and inspection-panel reforms over the next two years.

Bank officials got the message when U.S. threats were complemented by a resurgent board, which had become more unified on the environment during the early 1990s following the 1992 Earth Summit in Rio de Janeiro. Japan established the Policy and Human Resources Development Fund in 1990, which the Bank would manage. This included grants for technical assistance for a broad range of projects, including issues of health, water and sanitation, but especially environmental and resettlement issues. Additionally, Japan withdrew bilateral aid to India for turbines and generators necessary for the Narmada project.

Meanwhile, the West German Bundestag had been mobilized by the Green Party to support serious environmental reforms at the Bank. European environmental preferences had been converging for another reason as well. As the Single European Act and Maastricht Treaties were signed, Germany, the Netherlands, and Denmark were using their economic strength within the European Union (EU) to both raise, and make uniform, European environmental standards. Even less environmentally sensitive countries, such as Spain and Italy, had implemented more than 80 percent of the EU’s environmental rules by 1990. Britain and France had implemented nearly 90 percent. Employing an environmental policy index that we have constructed, this convergence on policy—and, by inference, environmental

80. Wade persuasively argues that the U.S. Treasury Department “above all” pressed the Bank to adopt reforms being championed by environmental NGOs. Wade 2002, 27.
81. But even then, the full amount was to be reduced by $200 million. Several years later the United States did eventually provide the final third of the replenishment. Interview with John Donaldson, Senior World Bank External Affairs Counselor, Washington, D.C., 31 January 2001; and Udall 1998, 403.
83. See Gyohten 1997; and World Bank 2002.
84. Wade 1997, 662.
preferences—among G-7 countries is shown graphically in Figure 4. The standard deviation on the index among G-7 countries shifts from a standard deviation of 15.6 in 1980 to 6.1 in 1991, and from an average of 60.3 to 84.3.

As the environmental preferences among the Bank's most powerful members increased and converged over time, the board was able to mandate multiple significant reforms. Notably, in 1994 the board empowered an independent inspection panel to hear complaints from groups that Bank projects would directly affect.

86. Using the revealed-preferences approach, we have compiled an Environmental Policy Index, patterned on the Environmental Sustainability Index of Esty 2001. In constructing the index we gathered data for 122 countries on twenty-two distinct measures of environmental policy outcomes for the years 1980–2000. The measures ranged from atmospheric sulfur dioxide concentration, to dissolved oxygen levels in freshwater, to number of reporting commitments kept as part of the Convention on International Trade in Endangered Species. We standardized the measures so that each country’s index score on any given measure is relative to all other countries on the same measure. Scores were also standardized relative to the base year of 1996, allowing country scores to vary over time as well as cross-sectionally. The overall index score is an average percentile ranking over the twenty-two measures. For details on the construction of the index, see Esty 2001 and Nielson and Tierney 2002.

87. The standard deviation and average for 2000 were 5.4 and 88.1, respectively.

88. This was one of the specific demands of the U.S. Congress. Frank’s committee recommended both an independent inspection panel and greater access to project documents for board members, NGOs, and legislators in member governments. On 20 June 1994, the day before Frank’s committee was to vote on reauthorization, the Bank released procedural guidelines for the panel that Frank demanded. See Udall 1998, 107–109; and Shihata 1994.
This move conforms closely to the fire-alarm mechanisms noted above. It gave numerous private and public groups an opportunity to bring outside information to the inspection panel and thus the executive board. Now board members found it much easier to get information about the likely impacts of Bank projects before the projects were implemented, as well as information about the conduct of their agents during the implementation phase.

Despite opposition from Bank staff and some borrowing countries, the board enacted sunshine practices and other reporting requirements at the Bank, substantially opening records and documents to the public that had previously been sealed. Since 1994, all project managers have been required to file, and periodically update, a public information document (PID). To ensure that interested societal groups could get relevant information about Bank projects, the board mandated that each PID would contain a section devoted to "environmental aspects" of the project. SARs—now including environmental assessments—were also made public after 1994. These and other sunshine practices were purposely designed as fire-alarm mechanisms that would allow the board to closely monitor its agents: the Bank staff and management.

For good measure, the board increased its police-patrol oversight activities as well. Before 1994, the board received project documents mere weeks before a vote would be taken. This dramatically reduced the probability of any negative decisions by the board, since halting or substantially altering a loan at that late stage of the project cycle would be quite costly and could even shake the credibility of the Bank. After the 1993–94 changes to the loan approval process, board members would be involved early in the planning stages of projects, and they began to exercise their option to question or suggest changes to projects long before they reached the decision phase. As Kapur, Lewis, and Webb, note,

Issues of accountability and discipline were also complicated by the actions of the Board. Although management held the initiative for bringing projects to the board and the board never turned down any management proposal, it now had influence before projects arrived and in collective discussion of future projects.

90. Of course, not all representatives on the board are enthusiastic about the inspection panel. Board members from borrowing countries see the panel as an intrusion into their domestic affairs. This observation simply highlights the fact that the World Bank responds to a collective principal with a majority-vote decision rule. The coalition led by the G-7 has more than enough votes to sustain the panel even in the face of intense opposition by member states in the minority. Preference convergence within the majority coalition does not imply unanimity on the board. See Umana 1998.
91. This policy only covered SARs written after October 1993.
This is precisely what our P-A model suggests we should observe in equilibrium. Bank staff ought to anticipate possible objections by directors and make adjustments so that those projects do not get rejected in later stages of the project cycle.

Finally, in part because of the bureaucratic drift observed after the 1987 reforms, the board now insisted on substantial changes in the type of staff hired by the Bank. The number of environmental economists, biologists, and environmental engineers employed by the Bank dramatically increased between 1993 and 2000. The number of personnel employed as environmental staff had increased from five in 1986 to more than three hundred by March 2000. By hiring agents with training in the environmental sciences, the board could be more certain that Bank staff now had the ability to analyze the environmental impact of projects, but also the interest in seeing that its new goals were realized. This is a classic example of screening and selection to avoid agency slippage.

More important than the fact that the board was hiring scientists, rather than exclusively economists and engineers, was that these scientists were no longer concentrated in the “ghetto” of the World Bank that was the D.C.-based Environment Department or the Regional Environment Divisions. Since 1994, each project with potential environmental impact has been assigned an environmental project manager (typically a non-economist) who is required to assess the environmental impact of each project and include a written evaluation to be sent to the board with other project documents. Having environmental scientists involved in project planning, approval, and implementation is likely to ensure that members of the board get more than mere environmental rhetoric from task managers. Since 1994 board members have received better and more timely information about the environmental impact of Bank projects because the administrative procedures that they passed in 1993 placed numerous checks on the authority of task managers.

Disbursement for any project categorized as environmentally sensitive A or B types now requires two distinct environmental assessments. First, during the project planning phase an environmental impact assessment (EIA) must be submitted and a pilot program must be designed to test for environmental degradation. After data is collected during the pilot phase, a second EIA must be submitted for the project as a whole. This larger EIA reveals practices that negatively affect the environment and recommends alternatives. In the absence of alternatives, the EIA evaluates the cost and feasibility of mitigation options. Loan disbursements cannot commence until these administrative procedures are completed and the documents submitted to the board by authorized environmental staff. This is a direct applica-

95. In 1993, less than 2 percent of Bank staff (roughly 200 people) had advanced degrees in the hard sciences, but by 2000 that percentage had more than doubled to 4 percent (more than 400 professionals). E-mail correspondence with Kristyn Ebro, World Bank External Affairs, June 2001.
tion of the Madisonian tactic of checks and balances. The principal has hired an additional agent with interests that diverge from those of the original agent, and has also created administrative procedures that check the ability of the original agent to act unilaterally.

These personnel and administrative changes at the Bank were not the direct result of a growing global norm of environmental protection or sustainable development. Such norms preexisted these personnel changes by many years.98 These administrative and policy changes came as a direct result of a change in the preferences of the Bank’s proximate principals and the principals’ subsequent employment of mechanisms explicitly designed to reduce agency slippage.

Conspicuous Absences

While reforms at the World Bank are impressive and, as we demonstrate below, have a measurable effect on Bank lending behavior, some notable absences persist. None of the reforms have addressed the basic employment incentives faced by task managers. That is, the collective principal of the Bank has not used the contracting method in an attempt to lock-in preferred agent behavior. Staff incentives to move large amounts of money through big projects persist.99 Bank critics have repeatedly called for reform of employment incentives,100 but little in this area has occurred.101 Bank critics have become intensely frustrated. Because these NGOs have achieved so many of their aims,102 failure on this front demands some explanation.

First, loans are negotiated settlements. There are at least two parties to all agreements. Despite conventional wisdom that portrays borrowing countries as helpless in the face of a unified “Northern Bloc,” developing countries often—if not always—have significant leverage over the architecture of the final loan document.103 They often find powerful allies within lending institutions that share the developing countries’ preferences for traditional, large loans.

Second, our model highlights the fact that NGOs, despite their energy, their activism, and the legitimacy given to their policy positions by a growing number of scientists, are not the ultimate principals of the World Bank. Instead, these groups compete with other social groups to gain the attention of their agents—elected

98. See Keck and Sikkink 1998; and Peritore 1999, 32–36.
99. See Treakle 1998; and Winters 1997. This conclusion was reconfirmed through interviews with members of Bank’s upper management on 17 December 2001 and with staff members under the vice president for operations policy and country services on 26 April 2002.
101. However, the Bank claims that employment incentives are changing. Interview with John Donaldson, Senior World Bank External Affairs Counselor, Washington, D.C., 31 January 2001.
102. In a recent analysis of global social movements O’Brien et al. argue persuasively that environmental NGOs have been more successful than any other issue-oriented NGOs at shaping the policies of multilateral economic institutions. O’Brien et al. 2000.
103. See Fox and Brown 1998, 14–16; and Nielson and Tierney 1999.
TABLE 1. Summary of institutional reforms

<table>
<thead>
<tr>
<th>Category</th>
<th>Pressure</th>
<th>Institutional reform</th>
</tr>
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<tbody>
<tr>
<td>Screening and selection</td>
<td>Kasten hearings (1985–86)</td>
<td>• Created Environment Dept. (1987)</td>
</tr>
<tr>
<td></td>
<td>Frank hearings (1991–93)</td>
<td>• New types of professionals hired as environmental staff (1994–)</td>
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<tr>
<td></td>
<td>IDA withholding (1994)</td>
<td>• Mainstreaming personnel (1994–)</td>
</tr>
<tr>
<td>Oversight and monitoring</td>
<td>Frank hearings (1991–92)</td>
<td>• Inspection panel (1994)</td>
</tr>
<tr>
<td></td>
<td>IDA withholding (1994)</td>
<td>• Sunshine policies (1994)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Reporting requirements (1993)</td>
</tr>
<tr>
<td></td>
<td>IDA withholding (1994)</td>
<td>• Mainstreaming (1994–)</td>
</tr>
<tr>
<td>New contracts</td>
<td>No agreement among proximate principals</td>
<td>• None</td>
</tr>
</tbody>
</table>

officials in developed countries. Because democratically elected governments are agents for a broad range of voters in a winning coalition, we should not be surprised by policy compromises that dilute the initial demands of particular constituent groups, environmentalists included. In fact, institutional channeling of societal demands may be essential to IO accountability.104 Further, at each successive level of delegation, we observe some agency slippage. This pattern follows from our model and appears to reinforce the conclusions of leading experts on Bank behavior.105

Summary of Qualitative Findings

We have argued that institutional reform resulted from pressure by principals for change, particularly when that pressure was emphasized by threats to recontract with the agent by withdrawing financial support. We argued that this pressure should result in specific outcomes such as new institutions designed for screening and selection, oversight, procedural checks, and new contracts. The findings are summarized in Table 1.

Even the Bank’s harshest critics recognize that substantial change has occurred in the organization.106 And some qualitative analysis has noted that the Bank’s

105. See Upton 2000, 63; and Wade 1997, 728–34.
loan portfolio is altered from the past. However, no researchers have undertaken statistical analysis of Bank lending practices that could offer systematic tests of our P-A model.

**Descriptive Statistics**

Accordingly, we compiled a large data set that includes every project approved by the Bank’s executive board from 1980 to 2000, representing more than 5,300 projects. We aggregated the projects by year and category to reveal overall World Bank lending over time (see Figures 5 and 6). In these figures, we averaged
Bank financing in specific categories for three-year periods, both to accommodate the two- to three-year project cycle and to smooth out year-to-year fluctuations. To ease interpretation of the data (with their large fluctuations in total number of projects and dollars lent from year to year), and to control for the general increase in number and size of World Bank projects over time, the figures represent percentages of projects and project dollars in the three-year periods.

There are two basic approaches to the question: How has the World Bank’s portfolio toward the environment changed as a result of principal demands? The first examines projects that actively attempt to preserve and improve the environment. The second considers projects that can harm the environment, particularly “traditional” lending in the areas of energy/electricity, industry, oil/gas exploration, transportation, and urban development. Critics of the Bank have pressed for both increases in environmental lending and decreases in traditional lending.

Alterations in the Bank’s environmental portfolio can be seen in Figures 5 and 6 as the lines punctuated by squares. The white squares represent stand-alone environmental projects, or projects aimed primarily at alleviating air and water pollution, protecting parks and wilderness, and improving environmental protection

**FIGURE 6. Percent of World Bank projects approved by category (three-year rolling average)**
infrastructure in governments. The solid black squares represent total environmental financing, once “mainstreamed” environmental components of traditional loans and Bank-managed Global Environment Facility (GEF) projects are included.

We expected environmental lending behavior to change beginning in 1987 and then again in 1994. Both of these trends occur roughly when predicted and thus support our model. Contradicting our expectations, we found that, beginning in the 1995–97 period (a peak of 9.4 percent of Bank-managed project dollars), environmental projects actually declined as a percentage of project dollars until 1998–2000 (see Figure 5). However, in none of the periods after 1994–96 did stand-alone environmental lending dip below the 1980–86 average level of 3.6 percent.

The fact that the post-1996 decline in stand-alone environmental dollars is flattened when GEF dollars are included suggests that a division of resources has developed at the Bank. Even though the same Bank staffers are initiating, organizing, and managing GEF and IBRD/IDA projects, GEF funds are increasingly being used to finance environmental projects as opposed to IBRD and IDA funds. The member countries that established the GEF in the early 1990s-dominated by the same countries that control the Bank’s executive board—likely anticipated this outcome.

Also, the Bank has touted its mainstreaming of environmental dollars into traditional project loans as a way of preventing or solving environmental problems earlier in the project cycle. These mainstreamed environment dollars have diminished in recent years, in part because of the decline in the traditional sectors as a percentage of the Bank’s portfolio, also seen in Figures 5 and 6. The post-1993 increase in the environment percentage of total Bank finance is statistically significant.

110. Before 1986, the Bank did not label environmental loans as such. But Bank environmental lending, particularly in the area of water reclamation, occurred long before the environmental reforms of the 1980s. Thus, we coded each loan as either primarily environmental or not, independent of the Bank’s categorization scheme. Two different researchers coded all of the data from 1970 to 2000. On the few occasions where disagreement arose, the research team coded the loans against the model—ambiguous loans were coded as environmental from 1970–86, and not environmental from 1987–2000. Given controversy over the categorization of forestry projects, we excluded them. See Rich 1994.

111. As we explained in the case study, mainstreamed funds are intended to ameliorate any environmental damage that may result from a given project. These environmental line-items have been included in project appraisal documents and SARs of traditional project loans since 1994.

112. The GEF was created as a small pilot program in 1991 and was funded entirely by contributions from developed-country governments. Replenished in 1995, the GEF provides grants to developing countries for projects that address various environmental problems (biodiversity loss, ozone depletion, climate change, and international waters). The World Bank administers roughly 60 percent of all GEF funds. Only Bank-managed GEF projects are included in the data reported here.

113. These dates are marking from the years that pressure for reform mounted in the U.S. Congress, 1985 and 1992, respectively.

114. Treating each year’s total as an independent observation and employing dummy variables for the periods before 1980, after 1986, and after 1993, the 1994–2000 trend is significant at the .01 level. The 1987–93 trend is positive but not statistically significant. The adjusted $R^2$ is .33 and the $F$ statistic for the regression is 6.07, which is significant at the .01 level. This simple regression is mathematically equivalent to a difference of means test and an analysis of variance (ANOVA) test. The results
When we consider total number of projects as an alternative measure of the dependent variable, rather than dollars lent, the trends toward the environment are more pronounced (see Figure 6). IBRD and IDA environmental projects are smaller on average ($60 million) than projects in traditional sectors ($90 million), and Bank-managed GEF projects are much smaller still ($7.8 million on average). The percentage of stand-alone Bank environmental projects has risen from an average of 4.6 percent of the total number of Bank projects from 1980 to 1986 to 6.0 percent for 1987–93, and to 7.3 percent for 1994–2000. However, when the much smaller Bank-managed GEF projects are included, environment projects as a percent of Bank projects jump from the 1980–86 average of 4.6 to 7.3 for 1987–93 and to 14.9 for 1994–2000. Because managerial effort is much greater per dollar for smaller loans, this shift in overall number of projects represents a large dedication of Bank administrative energy toward the environment. From 1996–2000, more than one sixth of all Bank-managed projects were in the environment category, making it the second largest category (in number of loans) behind the exploding social sector, which includes education, health, and social safety nets.

The sectoral patterns in Bank lending suggest additional support for our argument (see Figures 5 and 6). The sector trends reflect the “do no harm” approach to environmental protection. As we noted in the case study, while unsatisfied principals did pressure the Bank to support environmental protection in borrowing countries, the pressure to halt funding for environmentally damaging projects (such as Polonoroeste and Sardar Sarovar) was arguably even greater. In the 1987–93 period, we witness a sharp decline in Bank lending for traditional categories (energy, industry, transportation, etc.) in both dollars lent and percent of projects. The trend continues in the 1994–2000 period. The same largely holds for the agricultural sector, where most projects also have potential environmental impact. Further, there is little need for environmental amelioration for projects in economics/finance/public sector and the social sectors, where Bank lending is sharply and significantly increasing over time.

are qualitatively similar when total dollars lent in the environment category is used as a dependent variable. Of course, such basic analysis does not control for the numerous additional factors that may drive Bank environment finance. We employ such controls in other work, which treats individual loans as independent observations. Nielson and Tierney 2002.

115. The 1987–93 trend is positive, but not statistically significant. The 1994–2000 trend is significant at the .05 level. The adjusted $R^2$ is .20.
116. The 1994–2000 trend is significant at the .01 level; the 1987–93 trend is significant only at the most modest 0.1 level. The adjusted $R^2$ is .66.
117. The 1987–93 trend is significant for percent of projects at the .05 level, though it is not significant for project dollars; the 1994–2000 trend is significant at the .01 level for both percent of projects and project dollars. The adjusted $R^2$ for both regressions is .64.
118. In agriculture, the 1987–93 trend is significant at the .01 level for percent of projects and project dollars. The 1994–2000 trend is significant at the .01 level for percent of projects, though it is not significant for project dollars. The adjusted $R^2$ for the regressions is .81 and .64, respectively.
119. The trends in finance and social categories are also statistically significant at (at least) the .05 level in regressions for percent of projects and project dollars.
In nearly all cases, the statistical trends are stronger and more significant for the 1994–2000 period than for the 1987–93 period, suggesting that sectoral finance patterns at the Bank changed more profoundly after the 1993 reforms than they did after the much-heralded 1987 reforms. These statistical results reinforce the inferences we make following our case study and offer additional support for our model. Significant behavioral changes that stick follow institutional reforms.

Conclusion

We attempt to accomplish four important tasks in this article. First, we address an interesting empirical puzzle in international relations: How and why did the World Bank initially resist reform, and how did it ultimately come to change its organizational structure and its lending behavior? We offer an agency theory explanation for the observed empirical pattern. Further, we conduct qualitative and statistical analysis of the model.

Second, we provide the first overall (descriptive) statistical analysis of environmental lending at the World Bank and supplement it with an assessment of the entire portfolio. We find it remarkable that no one has done such work during the past ten years, especially considering the mountain of qualitative work done by both academics and activists on these subjects. Not only does this policy debate suffer from a lack of quantitative analysis, but also from an almost complete lack of quantitative data. We help to remedy the latter problem by compiling a large database that bears on various aspects of this debate.

Third, we explain why the next logical step in the neoliberal institutionalist research agenda should parallel a shift that took place in the economic theory of the firm decades ago. Because neoliberal regime theorists based many of their insights on the early work of Coase, it makes sense to pursue a parallel shift toward agency theory in IR in the hope that it will be as productive.

Fourth, in this spirit we outline a P-A model of international organization and discuss some of the special difficulties that we expect agency theory to encounter

120. Our findings strongly suggest that Bank critics are wrong when they conclude that the Bank is conducting business as usual when it comes to the environment. Environmental lending has increased significantly since 1987, the Bank has institutionalized checks on the dysfunctional behavior of its staff, the Bank has dramatically decreased lending for traditional “dirty” loans, and member governments have significantly increased their ability to monitor and sanction behavior that is not consistent with official Bank lending practices.

121. Further data collection efforts have produced: A database on voting shares in the eight largest international financial institutions from date of origin through 2000; a database of all MDB loans by type, year and organization over the past twenty years; and an environmental policy index for 122 countries from 1980–2000. We are currently extending our database on “mainstreamed” environmental lending by recoding line items in project documents before 1994. Without such data it is difficult to interpret changes in environmental lending following the 1994 reforms. Finally, we are gathering data on personnel assignments within the Bank and administrative spending by department. These data will help us to conduct much more precise tests of the P-A model at each step in the chain of delegation.
when it is applied to IOs. In fact, our insights about the role of a collective principal, multiple principals, and proximate principals may be germane to researchers in American and comparative politics, whose subjects are either connected by multiple links in a delegation chain or who fit the definition of common agency. Hence, we have not merely employed an existing model to address an empirical puzzle in IR, but have also suggested insights applicable to the broader literature on agency theory.

References


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